

# DE-RISKING YOUR BUSINESS AIRCRAFT TRANSACTIONS

Why owning an aircraft doesn't have to give you a headache

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Mark Byrne



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# Foreword

Nearly all decisions involve taking risk. Sometimes taking a risk can lead to reward - such as deciding to invest in a start-up business – and the decision making process will involve weighing up the potential reward against the potential loss. If the reward significantly outweighs the risk, it is likely the decision will be taken to proceed.

In circumstances where taking a risk presents a very limited (or very short term) reward, and the probability of negative consequences is high – the decision to proceed is unlikely. Low upside, high downside risks should be avoided, and if they cannot be avoided, it is important to understand how these risks occur and what can be done to manage them.

It is unlikely that a business would deliberately choose to expose themselves to a low upside, high downside risk. However, many businesses unknowingly increase their risk exposure by participating in transactions outside of their sphere of experience and knowledge, and without proper assistance. This is particularly true where a specialist asset is involved, there are tight timeframes, and the team has little understanding or knowhow of the asset - there is an increased chance that something will go wrong.

Business aviation is just like any other specialist industry; it has its own language, nuances and ‘way of doing things’ which would not be obvious to an outside observer. It is also a ‘hands on’ industry with no formal route to education – education is by way of experience. As a result, if a business makes the decision to buy a business aircraft but neglects to engage specialist assistance for the purchase, it has just exposed itself to the first low upside, high downside decision.

This e-book will provide a simple, high-level overview of risk and risk management in business aircraft transactions from hands on and practical experience. The e-book will identify key areas in transactions where risk is amplified, how to reduce risk exposure and when it is possible to plan for risks that are unknown in advance.



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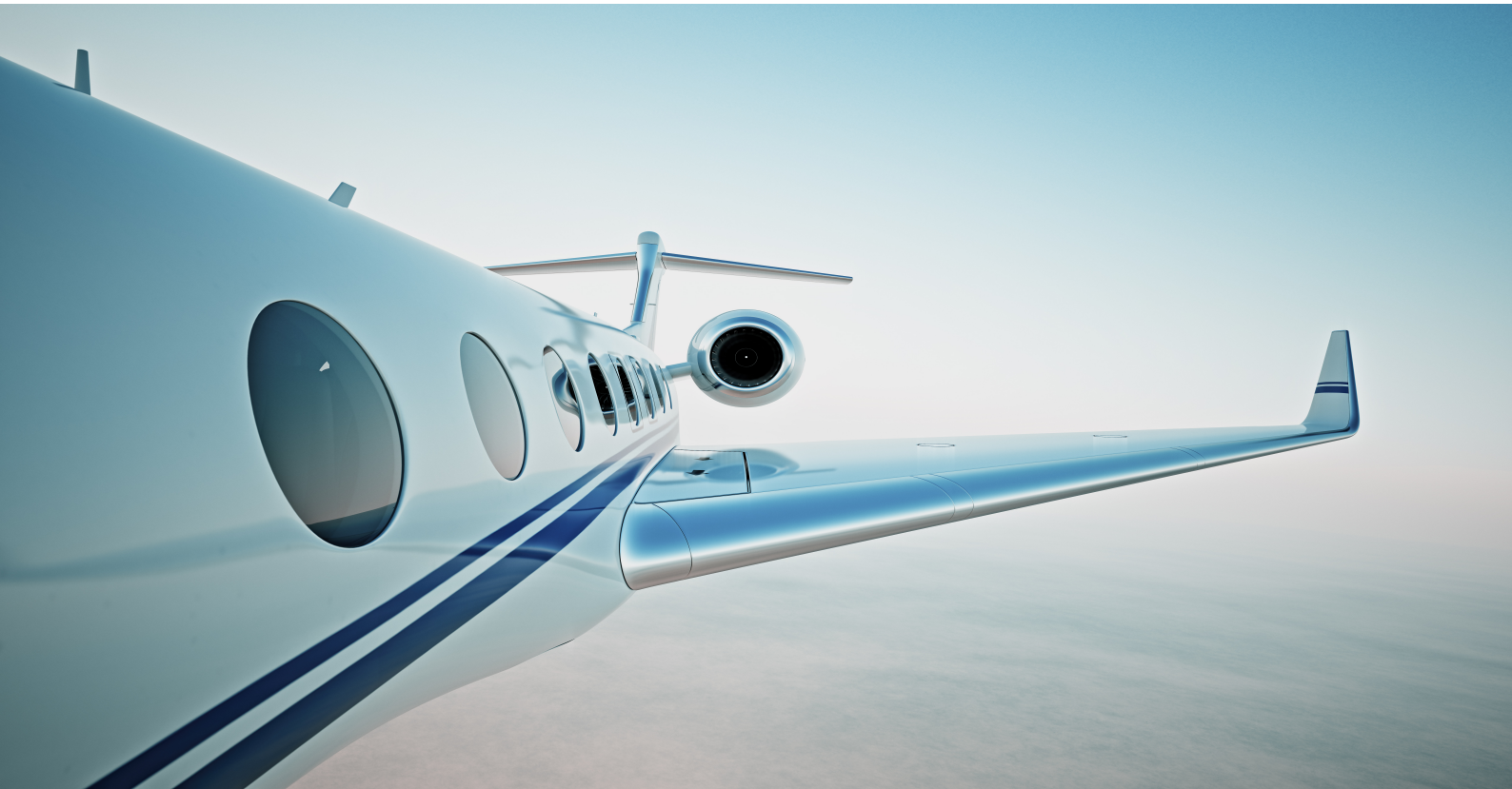


# How to reduce risk from the outset?

An aircraft owner will always be concerned with ensuring their aircraft is properly maintained and their crew are experienced, qualified professionals with continuous training on safety and flight matters. Similar concerns should be applied to the purchase and sale of a business aircraft (a significantly complex and expensive asset) but when something gets overlooked it usually results in delays, additional cost, and a bad client experience.

At its worst, failure to properly manage risks in aircraft transaction will increase the chance of creating legal, tax and/or insurance issues and could result in significant financial penalties for the client.

There is no such thing as a transaction without risk, however, it is possible to reduce risk likelihood with proper management and planning. Moreover, increased risk in aircraft transactions can be generalised in 7 core areas which are helpful when managing and mitigating risk exposure.



## 1. Know the mission

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## 2. Manage expectations

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## 3. Choose the right team and encourage effective communication

A good leader can make or break a transaction, but the leader also needs a team of experts for the different aspects of the transactional journey. Buying a business aircraft is a complex process with unique attributes; it requires the expert advice of specialists who understand the context of a business aircraft transaction and have experience in dealing with them.

An experienced and appropriate leader (usually, but not always, an aircraft transaction lawyer) will manage the transaction from start to finish and, while it may not be apparent, will save the client time and money. They will draw out from the client the mission, the timeframe, and any unique matters – for example, a client may have already chosen a registration mark, or the aircraft may need to visit an airport with reduced runway length – and then create a transactional map of what needs to be attended to by who and by when.

The transaction leader will build a team of specialists, including relevant jurisdictional legal counsel, tax advisor, financier (if applicable), insurer, and perhaps a corporate service provider (if a corporate structure is required) to give advice at the appropriate times throughout the transaction. A good leader will carefully select a team who will complement each other and ensure the advice provided by each advisor fits together in the transaction map. It is therefore essential that they have an overall view of the transaction and will be able to keep the right people updated and in the know about what is happening at any given moment. The transaction team leader should be directly communicating with the clients representative (or the client directly) throughout the transaction.

#### 4. Seek and set up professional advice early

Aircraft will nearly always cross borders and regulatory and tax rules differ between regions and jurisdictions. Therefore, it is crucial to seek experts in the key jurisdictions involved in the transaction. It is a good idea to source jurisdictional advisors at the start of a transaction to navigate any restrictions or tax liabilities early. Remember that when considering the different rules of one jurisdiction to the next, it is not just the aircraft ownership that needs to be considered, the client's existing corporate structure may need to be considered too.



#### 5. Plan with change in mind

Heraclitus said, “The only constant is change”. While this is true, most transaction managers would prefer the predictable.

Mission, team, time, and expectations can, for the most part, be controlled and managed internally by the client and their team of specialists. The environment however, whether it be political, social, or economic, carries heavy circumstantial risk which is unfortunately impossible to control in advance.

Transactions can be impacted (or completely derailed) by changes in the environment; by keeping an eye on external events it may be possible to anticipate these to some extent. Surprises cannot be handled in advance when buying an aircraft, but the team should be looking to minimise environmental risks by assessing the current global situation and predicting possible obstacles further down the line. For example, in 2018 it was known that the UK would leave the European Union and the possible impact that political change could have aircraft operations, tax and customs in either the UK or EU. As a result, many transaction leaders sought advice on the possible challenges aircraft owners would face on the lead up to and after Brexit.

## Good transaction leaders will consider the future environment by asking:

- Will this aircraft and its proposed operation still be appropriate and meet the mission expectations in a year's time?
- If changes are made to rules and regulations, does the transaction structure have sufficient flexibility to adapt?
- If something changes dramatically, what is the exit plan for the client and what will their exposure be?



## 6. Allow enough time

Tempus fugit!

While there are circumstances in which adding people and money to a transaction can reduce timescales, this is not always true. Processes such as aircraft licence applications, registration and other governmental involvement have timescales out of the control of commercial influence.

For this reason, it is important to understand and recognise points during the transaction which require set periods of time (or jobs to be completed in the right order). For example, while an aircraft delivery date coming forward may present an opportunity to a client to get their aircraft sooner, if there is insufficient time to have the ownership and registration correctly arranged then problems will arise. Without understanding this the client and team could get caught out and face financial and other consequences. Being caught out adds time and expense in the middle of the transaction that wasn't planned. It is crucial to know what elements of the transaction are time-bound in order to minimise risk (and knowing that these change with the environment of the transaction).

Planning an appropriate transaction timeline (and understanding how long each element will take) will allow for a smoother transaction; then, if the unexpected happens, time will be available to positively react to the event.

## 7. Compliance: Have the CDD ready to go

Just as the pre-purchase inspection (PPI) and title/lien checks on the aircraft are incredibly important, knowing who you are dealing with on the other side of the transaction is also vital. This is underlined by recent US investigations which demonstrate the need for client due diligence (CDD) across the industry. The regulatory environment means that nearly everyone needs to provide CDD, so be sure to have it ready in advance to speed up the transaction. With regards to CDD documents, generally at a minimum the client should expect to be asked to provide a certified copy of their passport and utility bill, but more will be required dependent on the client and their corporate structure.

With regulatory and legal requirements being what they are, it is important to establish the legitimacy of funds used to buy such expensive assets, therefore please don't be surprised or offended when questions are asked about Source of Wealth and Source of Funds. It is important for all parties to comply with international legislation in this area and increasingly proof of any payments made may need to be provided.

To summarise, compliance is mandatory for nearly all transactions, so be prepared and save time by having the relevant documentation ready.



## Prepare yourself for the unexpected

There is a difference between risk and uncertainty. Risk can be mitigated or planned for; possible issues and the probability of their occurrences are known (or should be known) by decision makers. Uncertainty on the other hand is a situation where no information is available to a decision maker in advance.

In business aviation transactions, manageable risks occur regularly and can therefore be anticipated in the transaction plan. Risk evolves to uncertainty when an event occurs which was unknown and unavoidable. The safe navigation of uncertainty requires the experienced team working together to deal with the unexpected in a timely and efficient manner.



Over the last five years we have all been hit by the unexpected; the pandemic, Brexit, financial crises. You will also have been affected by events closer to home, whether that be unforeseen aircraft technical issues, sudden absence of team members, or even IT and email crashes.

Most businesses have a business continuity plan which serves as a generic checklist of how to handle a crisis. Similarly, this can be applied to aviation transactions and can be the difference between a positive or negative outcome.

## Your checklist for the unexpected

### a. Identify the issue

When the unexpected happens care must be taken to identify the key issue arising as this will inform the other actions and decisions to be taken in managing the event.

In practice there will often be a ripple effect – a key issue to resolve but several others that will arise as a result. For example, if an aircraft is suddenly unable to fly, there may be knock on issues with future flights, routine maintenance, or crew hours.

It is vital to consider very early on whether a potential reputational issue may arise as a result of an unexpected event (for example an aircraft incident or publicity scandal). If in doubt you should appoint a dedicated person responsible for managing media and public relations. This is an incredibly important and dedicated role that you want in place at the outset.



### b. Forming the team and lines of communication

It is highly likely that a small core team will already be involved if a transaction is underway when the unexpected event occurs. If not, this should be formed quickly and consist of persons that control, operate and manage the business of the aircraft; people that are able to take decisions and have lines of communication with the owner. This core team will then need to identify whether any specialist and/or local advisors are required. This will depend on the nature and location of the event.

Lines of communication must be established as unexpected events often unravel quickly. As mentioned above, identifying persons who are permitted to take decisions is important – often in business transactions board level approval will be required for certain actions. Depending on the event external bodies, such as the relevant aircraft registry, may also need to be informed and have input.



### c. Information gathering

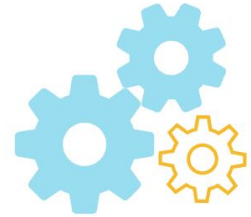
Assessing what information is available and any additional information required will be essential for the team to take actions and decisions. In particular is there any critical information that is required to resolve the issue.

It is likely that different members of the team will have different information priorities, however, it is unlikely that you will get all information immediately; realising that you are dealing with an unexpected scenario and that you might not be able to obtain all the information you'd hoped for is important, as you may need to make decisions made on 'good enough' information..



#### d. Identify the options

The team need to identify the options available to resolve the situation in order of priority and viability. This will include any immediate short-term options (such as safeguarding the aircraft and crew or providing copy documents if originals will be delayed) and, if applicable, any other options or considerations that will need to be resolved as a result of the event.



The next step will be to communicate the chosen option(s) to all relevant parties to see if there are any unintended consequences which result. Establishing timescales for plan review and activation should not be underestimated.

#### e. Timescales

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#### f. Implement the plan and maintain communications

Putting the plan of action in place is only the start of the resolution; it is important to provide regular review and updates. Even if there is no update to give, it is still crucial to keep everyone involved up to date until the event has been handled, so that no party is left wondering.



# 5 Common risks to look out for

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## 1. Closing formalities found wanting

Frequently last-minute problems arise because something has been overlooked. In our field of work this tends to be the formal customs export of the aircraft not having been put in place: whether this has been overlooked or it has been assumed to be managed by the buyer or the seller. This obviously impacts the timeline. In such scenarios contacting your specialist trusted advisors to assist and advise on the options available to resolving the issue is key. Communication is also required to explain if there is going to be a delay to all parties and keep everyone well informed.

## 2. EU Customs

Unexpected issues quite often crop up from aircraft ramp checks. If a ramp check leads to customs problems, you need to ensure the crew understand what allegations are being made and what their rights are.

The easiest way to help prevent such issues occurring or to stop allegations escalating is to ensure you always carry the correct documentation on board in anticipation of such situations. However, this is a very technical area and if you come into difficulty you should contact your trusted advisors to get the support you need.

## 3. Aircraft grounded and taxes imposed

It is not just in the European area that customs issues arise. An aircraft may frequently fly into another customs territory without complication and then suddenly, the next time, the aircraft is boarded, and the crew are told that there is going to be a certain taxation levied.

If you are brought into a scenario at this point, it is important to remember where your limits lie and to call upon the relevant contacts in the industry to assist you. Once you have local experts assisting you can then start conversations to understand the perceived issue and what is needed to secure the aircraft.

In these situations, time is of the essence, the longer the situation is left, the more the allegations start to solidify. Therefore, it is important to get local advisors onboard ASAP who can not only translate but understand the terminology and also benefit from having a cultural understanding of how the situation should be dealt with.

## 4. Politics and legal

Some unexpected events arise from global politics and sanctions are a prime example. These can cause serious problems; for example contractual payments may be suspended and assets frozen.

This will nearly always require additional, specialist advisors who really understand the sanction rules put in place, the politics behind it and the information that is required as well as any possible solutions. Timescales will likely be out of the hands of the aircraft owner – it will rest with any court or government involved.

While it is possible that the situation could resolve itself, this is unlikely to be under the control of the parties involved. It will therefore be important for the team to consider whether a transaction needs to be suspended temporarily or indefinitely. For example, if sanctions prevent a party from continuing a contract or making repayments, an event of default is highly likely to occur. The parties will need to consider ending the contracts and remedies available to them.

Lines of communications will need to be established to make all relevant parties aware of the situation and discuss options for resolution if this is possible. Addressing issues early on is more likely to lead to a better outcome and will give all parties time to get legal and other advice needed.

## 5. The out of the blue scenarios

Sometimes an event out of the control of all parties happens ‘out of the blue’ often causing an unexpected time delay. For example, a power outage in Oklahoma City or adverse weather conditions in the location of original documents.

Usually, these sorts of unexpected issues will only cause a short delay but in each of these cases the core team will need to identify how the immediate time delay will impact the closing mechanics and any knock-on effects. Understanding the movement in timescales and informing the parties that a short but unstoppable delay is occurring completely out of the hands of those involved is again essential.

There are likely to be multiple elements to consider. For example, if original documents are delayed from being sent due to weather, can copies be used until you can send the originals? Alternatively, if the aircraft lien checks and opinions cannot be issued in the original time frame, what other options are available to the parties?



# Summary

It is important to understand your avoidable risks on aircraft transactions. Similar risk areas occur on every transaction – by knowing what these are you have made the first step towards de-risking. Some risks are more manageable and there are some easy things you can do to reduce risk. Experience shows that the unexpected happens all too regularly and while we cannot plan for such events, we can prepare ourselves to manage them in the best way possible.

To coordinate a positive outcome, we have highlighted a simple checklist involving identifying the issues, looking at the timescales, getting your team together and identifying various options that flow from the primary crisis event and any ancillary issues that may arise.

Where the risk is high and the reward is low, why take the risk?!

- Identify what the client's mission is
- Get a team together that have experience and complement each other
- Understand what the time scales are, and which one are flexible
- Set reasonable client expectations
- Spend time early on in a transaction to spot risk areas
- Know the present environment and try to pre-empt what will likely come later down the line