

BUSINESS AIRCRAFT: OWNERSHIP, SOURCING AND SOLUTIONS— HOW TO MOVE FROM CONCEPT TO REALITY



The digitally designed Dassault Falcon 7X business jet, which first flew in May, is expected to enter service in 2006. The new, three-engine, long-range aircraft is unique among corporate airplanes in that it features fly-by-wire flight controls, which will enable it to fly more efficiently and handle even better than its predecessors.

Examining aircraft selection and ownership options is a key element within the overall process of acquiring private air transportation.

It's about time. You have heard Warren Buffet, Jack Welch and other business leaders talk about the benefits of business aviation, especially the advantages of setting your own travel schedule and being able to work undisturbed on the company aircraft.

You know travelers who have chosen business aircraft because too many hours have been consumed waiting for airline connections. Too many trips that should have been made were postponed because of scheduling conflicts. Too many of their competitors had gained an advantage because they used a business aircraft to reach their customers faster,

thereby having the right person in the right place at the right time.

Perhaps you know people who have sufficient means to have their own jet or turboprop and who spend less of their leisure time traveling and more of life's precious resource with their family, and you want that mobility for yourself and those close to you.

You have done enough research to determine that your company can afford an aircraft and use it efficiently to increase the productivity of your key personnel. Or perhaps you have reached that stage in life where you can afford private air transportation. You

are impressed with the excellent safety record of professionally flown business jets,

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A THREE-PHASE APPROACH

Leading Edge Aviation Solutions, LLC, the Dallas-based aviation consulting firm, has developed a methodology to help guide clients through the myriad steps needed to make sound, unbiased and informed decisions regarding aircraft acquisition.

According to Leading Edge CEO Barry Justice, this method works for all types of clients—from private individuals who participate in jet card or fractional ownership programs to multinational public corporations that operate a fleet of aircraft.

The three phases of aircraft acquisition are **strategic planning, tactical implementation** (execution of the strategic plan) **and operations** (operational start-up and transitional issues). Perhaps the most important phase is strategic planning, which begins by performing a “current-state assessment” and ends with a comprehensive plan that addresses all pertinent issues related to the acquisition of an aircraft.

- What are you doing now to satisfy air travel requirements—airline, charter, jet card, fractional aircraft, whole aircraft or a combination of the above? What in your present arrangement works and what doesn’t? If you have a flight department, does it employ industry best practices and protocols?

- What are your annual travel requirements? What percentage of those trips are short, medium and long range? How many passengers are on each of those kinds of trips?

- Establish a baseline current-state financial model to compute sensitivities to key issues, including market values and appraisals of all assets, lease documents (cost to terminate), ownership entity structures and purpose, current costs and spend rate, forecast capital and operating budgets to continue with current assets based on miles flown.

- Perform a needs and wants assessment. First, understand the difference between a want and a need. Often, high-net-worth individuals don’t have to justify cost or needs, while corporate governance generally requires documentation of business purpose and need justification.

- Establish a planning team to help define all elements of the needs and wants assessment. Involve the following people, as applicable: owner(s) and/or senior management, flight department management, aviation consultants, legal (internal and external), financial planners (CFO, internal and external analysts), capital appropriation planners, accountants, administrative services, banker, security, risk management, human resources, procurement and facilities management.

- Define needs around strategic plans, organizational and legal entities and governance and compliance requirements (i.e., what’s going on in the business—organizationally, geographically and demographically). Travel to new destinations and frequencies of travel should be articulated. If organic growth, mergers, acquisitions or divestitures affect the business, define travel impact by destinations, frequencies and passenger demographics.

- In short, what do the owner(s) or senior management need to efficiently manage the business? Is there personal use? Is it documented and reported in compliance with regulatory requirements?

- Will the existing entity continue to own the assets (if aircraft are owned), or is a change contemplated?

- What type of operational constraints must be met regarding aircraft range and cabin size, capital outlay, operating budgets, headcount, facilities and locations? Are there specific types of aircraft that are, or are not, to be considered? Is there a preference for a new or a previously owned aircraft?

- Financially and operationally model (qualitative and quantitative) alternative solutions. Outline the process and define default assumptions of factors. Define a broad scope of aircraft that will meet requirements. Narrow the candidate aircraft based on constraints, needs, wants, and pros and cons of assets and original equipment manufacturers.

- Model the costs based on the following factors: Type of operation (FAR 91 private or FAR 135 commercial). Will there be income generated, and how will it affect depreciation schedules? Miles flown. Type and age of aircraft and projected maintenance (new in-warranty vs. previously owned and out-of-warranty). Aircraft-specific historical residuals and market trends. Consider all financial assumptions—cost of capital, default tax rate, appetite for depreciation and alternative minimum tax situations.

- Model output should provide initial capital to purchase, operating budget for asset period defined, pre-tax cash flow, after-tax cash flow, net present value under three assumptions—(1) keep the asset operational after the tax depreciation schedule is amortized, (2) trade the asset utilizing an IRS-qualified 1031 like-kind exchange, (3) sell the asset and pay the recapture on the gain at ordinary tax rates.

- Finally, review the financial and operational output of the analysis with management. Agree on a strategy and the next steps. Define roles and responsibilities of team members for implementation. ♦

which is on a par with that of the largest scheduled airlines. You seek the security that comes from knowing who is on your aircraft.

Deciding that you or your company would benefit from business aviation is the first step. What to do next may seem complex because many options exist and business aviation probably is not your area of expertise. The purpose of this special section is to help you decide how to proceed.

A PROCESS APPROACH

Acquiring all or part of a business aircraft should be examined as a key element in a multi-step process of providing efficient air transportation. Procedures exist for arriving at each decision, and they should be understood and applied in keeping with best prac-

Make sure that the airplane is mechanically sound. Don’t simply fall in love with the aesthetics (e.g., a beautiful interior).

tices of the aviation industry. For the process to produce an optimal result, metrics for measuring the outcome need to be established and examined. Each step along the path must be identified with sufficient specificity so that the entire process of providing safe and efficient transportation can be repeated to achieve consistency, audited to ensure quality and monitored to facilitate continuous improvement.

The need for a rigorous process approach is more important now than ever before. Business aircraft fly higher and faster than their look-alike predecessors. They are equipped with advanced navigation and safety systems that provide a new dimension of safety, making them among the best-equipped aircraft in operation today.

Government regulations also have changed recently, most notably the rules gov-



Fractional aircraft provider Flexjet, a division of Bombardier, offers a variety of business jets built by its parent company, including the new Challenger 300.

erning fractional ownership and the operating requirements for flying in high-altitude airspace. In addition, two new federal laws—the Sarbanes-Oxley Act of 2002 and the American Jobs Creation Act of 2004—have changed reporting requirements and tax treatment of corporate-owned aircraft when flown for personal use or entertainment.

In addition to equipment and regulations, new ways for delivering business aviation travel have emerged and evolved, from fractional ownership and innovative aircraft management plans to prepaid charter cards that allow the purchase of a few flight hours on business aircraft for a flat fee.

EXPERT ADVICE

Yes, it's a sophisticated world in which business aircraft operate, but those who are knowledgeable and experienced can navigate it. The transportation process begins by acknowledging that whatever you or your company knows about business aviation could be enhanced by tapping additional resources.

Barry Justice, CEO of Leading Edge Aviation Solutions LLC, a Dallas-based consulting company that has worked for more than a decade with hundreds of individuals and many S&P 100 corporations, as well as the top private banks and wealth-management firms, to provide business aviation solutions, said, "When you buy an airplane, you really ought to solve a travel problem in a system-

Hire a qualified company (an FAA-designated repair station for the type of aircraft you are considering) to perform a pre-purchase inspection of a previously owned aircraft.

atic way and source a solution that meets your needs. One of the keys to doing it right," said Justice, "is to assemble a team of aviation, financial, legal, risk management and other experts—from both inside and outside your company. This is important because many people not involved in business aviation on a daily basis 'don't know what they don't know.' An informed aircraft-acquisition decision based on quality information is not that expensive to attain, but a decision based on poor or incomplete information can cost millions."

IDENTIFYING NEEDS

The first step in the process is to identify what your travel needs are, and the industry-leading suppliers are adept at helping with such studies.

Bryan Moss, president of Gulfstream Aerospace Corporation, which makes a line of business jets, said, "We begin our dialogue with customers with a series of discussions, the purpose being to determine what is most important to them. We probe to clearly identify what role an aircraft will play in their company or their personal life. What will be the mission of the aircraft? Are travel needs simply domestic, or does the client intend to fly internationally? How many people are likely to be traveling at any one time? Where will the aircraft be based, and what facilities are available there? How much does



Helicopters such as the Sikorsky S-76 offer fast, point-to-point transportation for corporate travelers, especially in congested regions such as the Northeast.



Cessna's Citation Mustang is one of the new generation of very light jets that promises to make private jet travel even more affordable. The six-seat aircraft, which first flew in April, is expected to enter service in about a year.

the client expect to use an aircraft each year? We seek to fully understand the client's travel expectations, as well as additional objectives—such as sources and uses of funds, depreciation and other tax considerations—before proposing a Gulfstream to meet their needs.”

Because business aviation is a specialized form of transportation involving many sophisticated decisions and technologies, those who decide to buy their own aircraft often turn to aircraft management companies such as TAG USA for expertise.

“Our job is to find out what a company or individual needs and provide it,” commented Gil Wolin, VP of corporate communications for TAG Aviation USA, Inc., which manages a fleet of 130 aircraft at 55 locations. “TAG provides services, such as crews and scheduling, as well as expert advice for the company or individual at each step within the process of providing private air transportation. We also are able to use our clients' aircraft within our charter fleet if the owner wishes to make the aircraft available for such revenue-producing activity.”

In recent years, many people have been introduced to business aviation through frac-

tional ownership programs, which allow companies and individuals to own a share of a business aircraft without the associated obligations, and at a fraction of the cost, of running their own flight department.

Flight Options focuses first on customer needs before offering solutions. Cameron Gowans, chief marketing officer for the Cleveland-based provider of fractional ownership, charter cards and all-inclusive leases of business aircraft, said, “We begin discussions with potential customers by asking three questions: What is their mission need? Are they financially capable of using private air travel? And finally, does the client truly desire this form of travel? Business aviation provides great value, but on the surface it is not the cheapest way to travel. The buyer must accept the premise that the overall value of time saved and time used productively more than balances the cost of this form of travel.”

Because travelers' needs are diverse, another major fractional aircraft provider, Flexjet, a division of Bombardier Aerospace, offers customers a variety of lift options, from chartering, to purchasing flight time in 25-hour blocks, to buying a share of one of the business jets built by the parent company.

Michael McQuay, president of Bombardier Aircraft Services, said, “Flexjet is distinctive for its focus on service excellence and continuous program innovations that provide unique benefits to owners, such as our waiver of ferry fees to the Caribbean and other island destinations.”

KEY DECISION POINTS

With the start and end points of the transportation process defined, the next step is to identify the decisions that lead to achieving safe and efficient travel. Prominent among them is deciding which aircraft, business aviation option or blended solution of aircraft, fractional share and/or charter card best supports the desired results.

Get your insurance company or risk manager involved in the aircraft acquisition process early. Otherwise, you could find yourself operating with inadequate coverage or an unacceptable level of risk exposure.

“I agree that looking at the acquisition of an aircraft as an element within the process of providing transportation is a reasonable approach,” observed Jeff Habib, Dassault Falcon Jet Vice President for Western U.S. Sales. “But I caution that every deal is different, and not all clients follow a structured approach to business aviation, even if they should.”

“At Dassault Falcon Jet, we start the dialogue with prospects by identifying several



Advanced cockpit technologies incorporated into Dassault's EASy flight deck (left) are designed to make piloting new business jets more intuitive. The 13-passenger Embraer Legacy (right) is the largest and newest aircraft offered by fractional provider Flight Options.

Examine the tax consequences of your aircraft purchase. Failing to plan properly could cost you dearly in the long run.

issues, including what are their budget considerations," continued Habib. "Then we move into a full discussion of the client's transportation requirements, such as typical missions, range and runway performance, cabin volume, passenger load, baggage space, tax considerations and anticipated years of service for the aircraft. It is important that clients consider the residual value of an aircraft when defining what they want from their business aviation experience.

"We [also] introduce independent third-party information on hourly and life-cycle costs from respected sources," added Habib. "Our sales engineers use established financial tools and computer programs to do comparisons, as do our competitors. It is not unusual to have clients hire the services of independent experts to assist in their evaluation of business aviation options. Business aviation

involves significant capital expenditures and ongoing costs of implementation. There is a risk that the buyer may move too quickly. It is essential that those considering the purchase of an aircraft be mission-focused."

HOW TO PAY

The process of achieving satisfactory transportation solutions involves more than just deciding which aircraft to purchase or which fractional ownership program or charter card is best. Using business aviation involves a significant commitment of capital, so the financial tools used to acquire an aircraft or fractional share require careful consideration. Should assets be purchased outright or financed? What about leasing? What is the best way to depreciate these assets? And when is it best to replace a business aircraft that has been depreciated rapidly?

"Financial considerations are woven into many elements of the transportation process," said Jim Dickerson, head of Bank of America's Aircraft Financing Division. "They start with selection of an aircraft, the structure of ownership and the method of operation," he continued. "Will the client select the right asset, and if it is a pre-owned aircraft, was there a good pre-buy inspection to ensure it was fairly valued? Will a C corporation own the aircraft, or will the owner elect an S corporate structure? Does the owner plan to make the aircraft available to an air

taxi company that will offer it for charter, thereby generating income for the owner when not being flown for company or personal use?

"How a company or individual plans to use an aircraft is fundamental, particularly in light of the tax implications of the American Jobs Creation Act of 2004. What about the aircraft's residual value and the tax consequences of a fully depreciated asset? What about the cost of money, which is always a consideration? It is vital to address financial and tax issues early in the process."

PROCESS OVERVIEW

Establishing the operating parameters for achieving safe and efficient transportation also involves hiring personnel to manage the

Spend the money to hire the best available aviation staff. They are there to protect you and your assets by providing the highest possible level of safety and professionalism.



Gulfstream Aerospace, renowned for long-range jets such as this G550, now offers mid-size models as well. New features include advanced equipment such as enhanced vision systems.

transportation process, establishing reporting procedures that align the transportation function with overall company objectives, finding pilots, selecting suitable sources of maintenance, constructing a system for scheduling flights, determining how the aircraft will be allocated between users, setting safety-oversight and risk-management functions, developing and implementing security procedures, and selecting a training organization to satisfy safety requirements.

Each step within the transportation process should be documented to ensure that personnel responsible for specific functions know what they are

expected to accomplish and how to achieve it. Measures of success—such as travel hours saved by using business aviation, rather than airlines, improved client relations, new customers reached, cost per passenger mile or other metrics—should be established and systematically reviewed to determine the degree of success you are achieving in satisfying your travel objectives. The entire process of providing transportation via business aircraft should be audited to ensure compliance and to identify areas for improvement.

You know you can benefit from using private aircraft.

Now you just need to examine carefully all the options to determine which solution is best for you. ♦

Understand that your business acumen will not necessarily make you an expert in aircraft procurement. Seek the counsel of others who are intimately familiar with the technical details and current market conditions.

TWO VITAL RESOURCES

The National Business Aviation Association (NBAA), located in Washington, D.C., provides excellent guidance material and expert assistance for operators of business aircraft, including advice on how to start and run a flight department. NBAA's *Management Guide* is considered the industry standard for best operating practices for flight departments, and the association's TravelSense software program offers an objective format for quantifying the time saved by using business aviation. NBAA also is a leading source of tax-related information.

Another primary source for business aviation information is *Business and Commercial Aviation* magazine, the leading monthly publication in the industry. It provides a wealth of information on how to acquire and operate business aircraft.

Subsequent special advertising sections will drill down on each of the process steps and decisions that will enable you and your company to optimize business aviation.

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