Aircraft Finance

The stock market has bounded to new record highs, but...

Traditional measures point to a recovery in the economy in general, but the business aviation sector has yet to enjoy it. On the up side, credit has loosened somewhat for newer aircraft, as lenders find niche markets for themselves. For many buyers, however, cash remains king.

by Curt Epstein

It has been five long years since the start of the Great Recession, which shook economies the world over and chilled the business aviation industry. Since that fateful fall of 2008, traditional indicators have hinted at a gradual economic recovery. In May this year, the Dow Jones Industrial Average closed above 15,000 for the first time in its history, while last month the Dow and the Standard & Poors 500 each reached new high-water marks. Those Wall Street milestones may sound impressive, but once adjusted for inflation they have yet to exceed the highs set before the economic meltdown, meaning the U.S. economy is still creeping along the road back to where it was in 2007.

"The stock market has bounded to new record highs, reflecting the strength of large multinational corporations whose stock is traded, and also reflecting the Federal Reserve Board's [Fed] quantitative easing policy, which is supportive of stocks and bonds," said Mark Zandi, chief economist for financial research firm Moody's. "The Fed has been working hard to keep long-term rates down and that helps to support equity prices, so the stock market represents what's been going on among the strongest part of the economy."

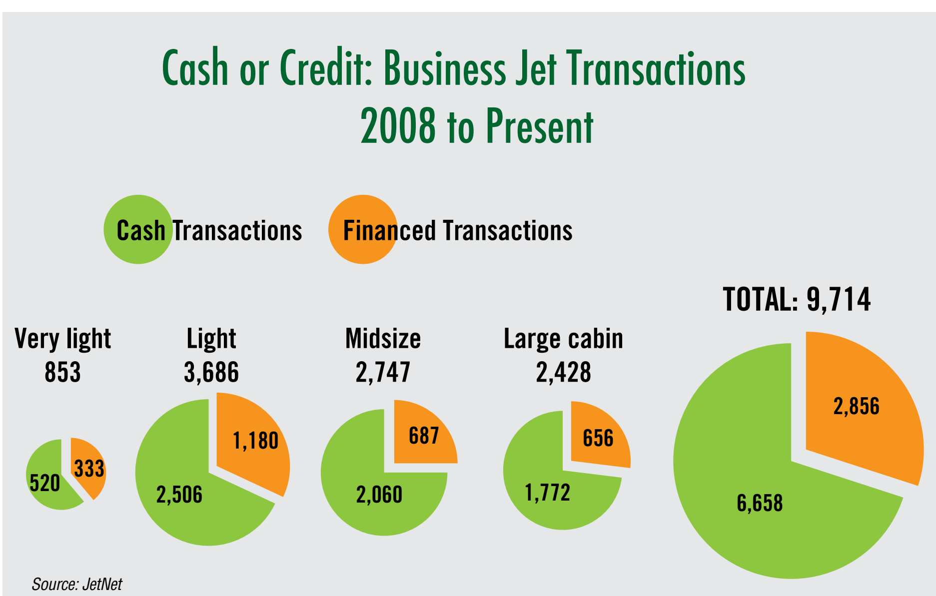
While these indicators show that major corporations are doing well, they don't in this case explain the entire picture or provide many answers to an unsettled business aviation community. "I am beginning to wonder if the traditional economic measures and metrics we have used in the past to gauge business aviation are relevant today," said Ford von Weise, director and head of aircraft finance with Citi Private Bank. "We have used corporate profits, the Dow Jones Index, GDP and so on in the past as proxy for the health of the business aviation industry; however, all of these indices have been up substantially over the past two years and yet business aviation has still not recovered."

"Clearly rising stock prices are helpful," Zandi told **AIN**. "They increase wealth and spending by high-income households that own the stocks. It's also a signal to American companies to go out and invest and hire and be more aggressive, but it's not been enough and it doesn't reflect the sort of lackluster conditions upon the rest of the economy, particularly among small and midsized companies." At NBAA's annual convention in October, opening session speaker Rep. Sam Graves (R-Mo.), chairman of the House small business committee, noted those particular business segments combined to account for 85 percent of the companies that use business aviation, a statistic that explains the continued softness in some areas of the business jet market.

Factors such as a national unemployment rate of more than 7 percent, stagnating wages and the recent budget stalemate in Washington have only served to fuel that lack of confidence in the slow-paced recovery. "I think some of the businesses and consumers are still shell-shocked from the recession," Zandi said. "It's hard to get by the nightmare of that period. It's fading with each passing month, but it's still quite indelible in people's thinking."

Under that assessment, it is easy for economists such as Zandi to account for the historically high levels of cash transactions for aircraft purchases, which reached highs of 77 percent this year. "I think it's because cash is everywhere," he noted, adding that the profit margins for large companies are currently wide with strong earnings. Such companies have also raised debt over the past several years, taking advantage of the low interest rates stimulated by the Federal Reserve. "I think that goes a long way toward why they are using that cash hoard to make their investments," said Zandi. "The other thing is it's not quite clear where else to put their money. They are a little hesitant to take big risks, so the cash they do have they are using for things that have a more concrete return or payoff."

"Cash has always been a formidable competitor for us," said Michael Kahmann, managing director and group head at CIT Business Aircraft Finance. "The question that any prospective [jet] purchaser needs to ask is what uses do I have for my cash? In the U.S. and elsewhere we see businesses sitting on their cash because of a dearth of investment opportunities." According to industry data provider JetNet, since the beginning of 2008, of the 9,714 U.S. retail jet transactions (new and used), 2,856 of them were financed, for a total of 29.4 percent. Of the 853 very light jet sales, 39 percent were financed, followed by light jets, which saw financing obtained on 32 percent of the 3,686 sales. Of the 2,428 large-cabin jet purchases, 27 percent were financed, while midsize jets had the lowest lending percentage at only 25 percent of the 2,747 deals. From the beginning of this year through the end of October, of the 1,426 U.S. business jet transactions, only one out of four involved financing, with overall decreases in each segment.



Source: JetNet

Know Your Borrower

For those aircraft buyers who seek financing for their purchases, the market is vastly different from what it was in the days before the recession. "We've gone through five years of a difficult market where borrowers have come in line with the expectations of the banks as well," said David Vandenberg, senior director of structured finance with Bombardier Aerospace. "After September 2008, there were banks rethinking how they would participate in this business, and customers were accustomed to the types of finance they got in 2006 and 2007, so you had this disconnect of expectations. The adjustment to this new reality has taken place over the last couple of years and it's just not as much of an issue now."

Those adjustments have included heightened diligence on the lender's part as more transparency is expected from the borrower. Most lenders now operate on a strict "know thy borrower," credo and existing relationships are in many cases more favorably considered. That scrutiny has tended to slow the pace of completing finance deals from the rapid-fire approvals prevalent before the recession. While once fairly common, asset-based financing has become highly specialized, with PNC Aviation remaining one of the main proponents with its no-disclosure, non-discourse financing program.

Part of the "new normal" is a down payment of between 10- and 40 percent of the purchase price. "Down payments or other forms of up-front equity have become more expected as lenders [shy away from over advancing] in aircraft financing, given what they experienced with the recent asset devaluation," said Michael Amalfitano, managing director and executive head of corporate aircraft finance with Bank of America Merrill Lynch, adding that loan terms tend to be shorter now. "Amortizations are beginning to move back toward the 20-year mark, while the current norm is still 15 to 18 years," said Wayne Starling, senior vice president for sales and marketing with PNC Aviation Finance. In general, the terms offered are a function of the credit strength of the borrower. Some lenders might still offer 100-percent financing, but they generally reserve such largesse for exceptionally favored customers.

While lender portfolios infested with undervalued repossessed aircraft have largely vanished, along with many fair-weather lenders, those financiers who rode out the storm learned some valuable lessons. "Commonly held beliefs that most business jets would maintain 50 percent or more of their original value throughout a recession proved to be wrong," said Allen Qualey, president of the specialty finance group at Indiana-based 1st Source Bank. "A lot of financing was closed on the premise that aircraft depreciation was less than what has been experienced in the past five years," echoed CIT's Kahmann. "Financing structures today better take into account the long but limited useful life of business aircraft, and I think that the long-term result of these structures will be a more resilient business aircraft industry as well as better access to financing."

Competition Among Lenders

New Jersey-based Valley National Bank recently decided to exit the arena, dissolving its private aircraft lending business because of losses sustained since the recession. Court documents show the company has filed several lawsuits attempting to recover on unpaid asset-based aircraft loans. Yet despite some lenders' withdrawal from the market, customers seeking funding are currently finding more choices than there were in the years immediately following the downturn, pointing to increasing appetite among lenders.

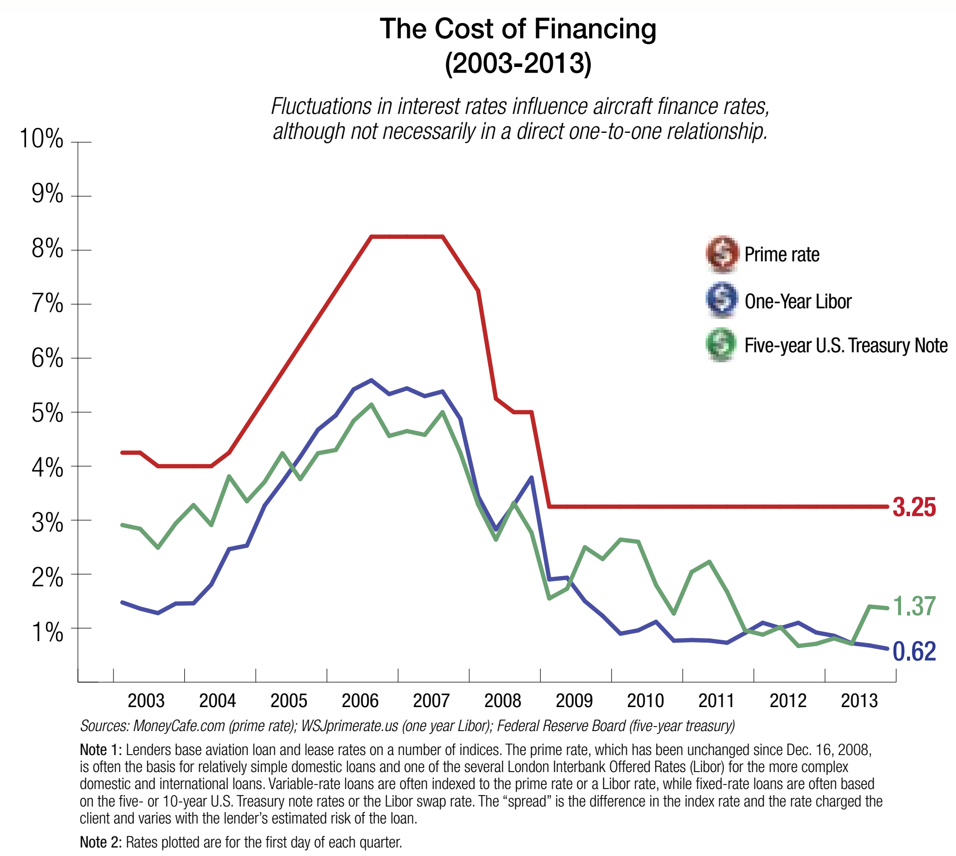
"An excellent indicator is the re-emergence of lenders that had abandoned the aviation finance sector years ago, and the programs they are beginning to offer again," said PNC's Starling. "After the fluctuations of the past several years, some lenders who left the arena with scorched fingers now find themselves cautiously returning, along with a new crop of financiers. "They are starting to appear more frequently and fighting for a share of the 23 percent of the market that is non-cash," said Qualey, whose own company considers aviation finance one of its core businesses. "The non-core are the fair-weather lenders, and they predictably come and go with generally limited success. Their greatest constraint is hiring seasoned sales officers to originate the business. Those people know they will be unemployed the minute storm clouds appear in the economy."

The growing array of financing options is good news for prospective aircraft purchasers, according to Robert Kent, president of Scope Equipment Finance. "Competition among lenders for aircraft finance has increased since the low point during the recession," he said. "Margins have tightened and should continue to do so." In the Fed's mid-year Senior Loan Officer Opinion Survey on Bank Lending Practices, while the vast majority of respondents indicated that their company's credit standards for approving commercial and industrial loans to companies have remained basically unchanged, approximately 14 percent indicated they have eased their standards, while only one bank reported it had tightened its standards somewhat. Nearly 65 percent of the banks in the survey said their spread of C&I loan rates for large and middle-market companies (annual sales of more than $50 million) had eased somewhat over the previous quarter, while more than 57 percent noted they had eased rates to small companies. "Lenders in the past have demonstrated short memories, relaxing their standards within a few years of a recession," Kent noted. "This applies not only to aircraft, but also to commercial real estate, housing and so on. The process has already started as lenders are hungry for earning assets."

These days, that competition among aircraft financiers is not limited solely to the traditional lending houses. "It's not just banks calling us saying, 'I'm in this business, can you send me some leads,'" Bombardier's Vandenberg told **AIN**. "We're now getting calls from specialized funds, we're getting calls from people who represent insurance companies. This is all new money coming into the market."

One change that has been noted in

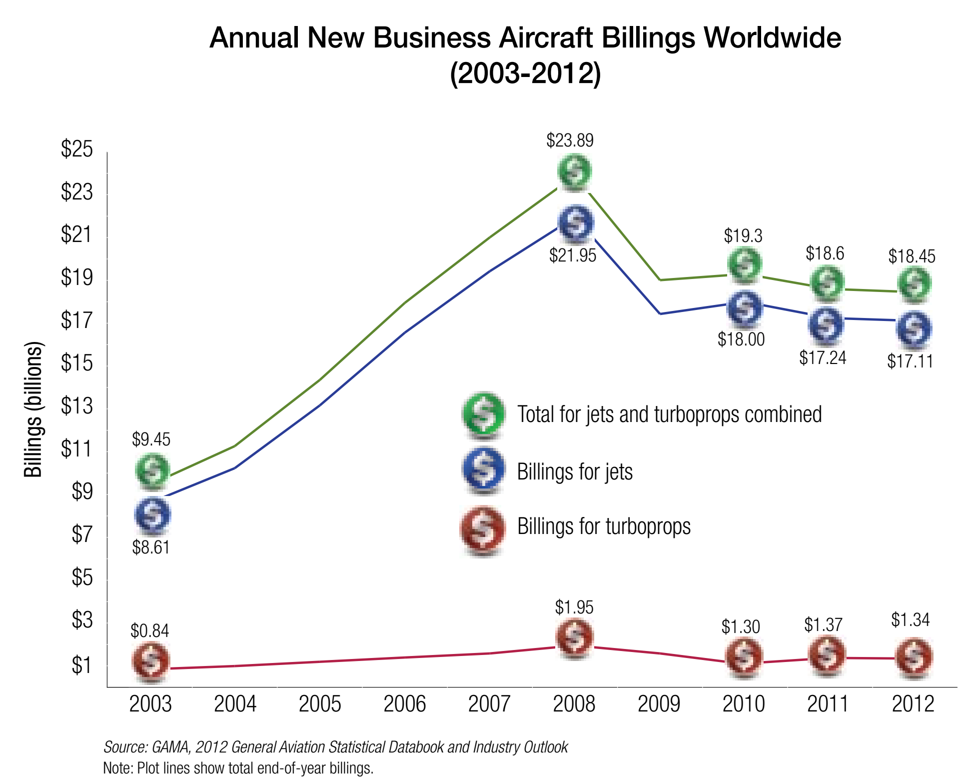
Continues on next page ▶



Sources: MoneyCafe.com (prime rate); WSJprimerate.us (one year Libor); Federal Reserve Board (five-year treasury)

Note 1: Lenders base aviation loan and lease rates on a number of indices. The prime rate, which has been unchanged since Dec. 16, 2008, is often the basis for relatively simple domestic loans and one of the several London Interbank Offered Rates (Libor) for the more complex domestic and international loans. Variable-rate loans are often indexed to the prime rate or a Libor rate, while fixed-rate loans are often based on the five- or 10-year U.S. Treasury note rates or the Libor swap rate. The "spread" is the difference in the index rate and the rate charged the client and varies with the lender's estimated risk of the loan.

Note 2: Rates plotted are for the first day of each quarter.



Source: GAMA, 2012 General Aviation Statistical Databook and Industry Outlook
Note: Plot lines show total end-of-year billings.

© 2013 AIN Publications. All Rights Reserved. For Reprints go to www.ainonline.com

Continued from preceding page

the aviation finance industry of late is the rise of specialized niches, with many financiers narrowing their focus zones in terms of deals. "They all know exactly what their sweet spot is in the market, and that's what they will do deals in," said Alasdair Whyte, founder and analyst with UK-based Corporate Jet Investor. "There's not really anyone who will try to do everything, and that's probably the biggest thing. Pre-2007, I think people were just trying to do deals, now they are much more self-selecting. They now know that lots of banks have been in lots of trouble, and the aircraft finance guys know which deals to take to the credit committee and which deals not to."

Signs of Stabilization

While the small and midsize jets experienced the worst value deterioration during the downturn, those segments appear to be gaining some traction at last. "The biggest growing client base that we have right now is U.S. small and midsize businesses and the types of aircraft that they are buying: turboprops and light jets primarily," said René Banglesdorf, CEO of Texas-based aircraft brokerage Charlie Bravo Aviation. She has noted an uptick in calls on those aircraft types over the past six months, calls she described as no longer the "bottom-feeder phone calls" from people seeking to exploit the depressed market. "We're seeing a huge increase. I'm optimistic that we are going to see some stabilization with the bread and butter of business aviation, which is those small and midsize U.S. businesses."

"We're seeing demand for new airplanes," noted Steve Smestad, president of aircraft finance broker AirFleet Capital. "When the [recession happened], that was probably the first area that was hit. But we're seeing pretty good sales now, at least in our market: high-performance pistons to light corporate jets." Smestad added that his company is seeing much more financially sound customers seeking aircraft financing than in previous years. Though many lenders have trodden cautiously when it comes to financing these aircraft over the past few years, there are numerous options at the lower end of the business jet spectrum. "The big lenders have been staying away from those aircraft," Banglesdorf told **AIN**. "There are lots of other lenders, lots of local banks that want to get into aviation and take good care of their existing business clients. There is financing for those deals, absolutely."

Another segment that suffered of late has been older aircraft. During the downturn, as the use of corporate jets plummeted in parallel with their values, operators looked to unload those airplanes which were idled. Many borrowers suddenly found themselves

Continues on page 24

U.S. economy looking better, despite lingering uncertainty

by R. Randall Padfield

Dr. James West is chairman of the Department of Economics and Business at Moravian College in Bethlehem, Pa. He has provided his unique viewpoint on the U.S. and global economies for **AIN***'s special report on aviation finance since 2007.*

How does the U.S. economy today compare with the economy at this time last year?

It continues to show signs of stabilization and growth, as evidenced by positive signs in the real estate market and consumer spending. Companies have largely worked their way out of issues created by the financial downturn of 2008. They've streamlined operations, cut costs and saved a lot of money. GDP [gross domestic product] growth rates are forecast at a moderate 1.8 to 2.8 percent–slow but steady.

However, there are continued uncertainties about the costs of government inaction and the shifting regulatory framework. Also, slowdowns in the global economy, especially the key emerging markets such as India, China and Brazil, are looming issues. Each country faces its own internal problems. We are seeing growth in some markets around the world, but overall the IMF [International Monetary Fund] has reduced its expectation of global growth rates. A number of U.S. forecasters have done the same.

Another issue affecting growth is the anticipated tapering of the Federal Reserve's massive bond-buying stimulus program, labeled QE [Quantitative Easing] 1, 2 and 3. The government shutdown and other setbacks in the economy caused the Fed to postpone this tapering program for the foreseeable future. Interest rates continue to be low, but fears of inflation could force an end to these easy money policies.

Our government's current "techniques," such as sequestration, for dealing with budget deficits and the uncharted waters of the Affordable Health Care Act may add to deficit worries, too.

Nevertheless, while there is a strengthening of the fundamentals of the U.S. economy, the level of demand is not such that we can expect a quick increase in GDP. But almost in spite of all the uncertainty, the U.S. economy is slowly and surely moving forward.

Standard & Poor's famously reported that the government shutdown took $24 billion out of the U.S. economy, but others argue that losses in one part of the economy are offset by gains elsewhere. Which viewpoint is correct?

First of all, we have a $3.5 trillion government budget, so any losses in government expenditures are relatively small. Confrontation seems to be the way the government does business these days, and shutdowns are one of the costs of doing business this way.

Much of reported cost was lost wages of furloughed employees, which will be repaid. The FAA closure limited the financing of some aircraft, because buyers were waiting for the FAA to clear papers, and other industries had similar regulatory slowdowns. But with the government working again, these things will be taken care of.

Dr. James West

Last year at this time, everyone was worried about sequestration, which did happen. In many ways it did not turn out to be as drastic as many had expected. No doubt, it is better to cut expenditures rationally, and sequestration forced the issue. But it also showed that there were many items that could be removed from the system.

Funding of the U.S. government is guaranteed through January 15 next year. Do we need to prepare for another government shutdown?

I think this next deadline will likely precipitate another near crisis. Unfortunately, the way we talk to each other now is through confrontation instead of consultation. There is such a great divide on the role of government in the economy that the debate has sunk to a level where shutdowns have become a technique to draw attention to the different sides of the issue.

Obamacare is still a ripe political issue, and now that the launch of the program has been so bad, people are really looking at the ramifications of it. Healthcare costs are going to increase for private firms; this also is an issue for government budgets. I think the Republicans are going to come at this with more steam. With intransigence on both sides, I think the possibility of a default threat will be there again.

You can cause a shutdown or use the threat of one only a limited number of times before instilling a lack of confidence in the country. Even before the shutdown, we were getting threats of downgrades in federal securities. But if we do this over and over again, it will cause a loss of confidence in securities, possibly a rating decline and increasing calls from outside the U.S. for new global currency arrangements to replace the dollar.

It is often reported that large corporations are "hoarding" large amounts of cash because they can't find good places to invest this money. Is this true and if so, when do you think they'll start investing again?

Hoarding is probably too strong a word, but there certainly is a lot of money on balance sheets, both here and abroad, looking for opportunities. This is mainly due to the many uncertainties already mentioned. The high tax rate on repatriated funds is another factor. Fiscal, monetary and regulatory clarity will be the key for generating investor confidence in better rates of return for their investments.

Assuming Joe the Investor still has some savings to invest, what should he do with his money now?

Last year, I was overly pessimistic about the impact of sequestration and the fiscal cliff and warned that the stock market could decline by 20 percent or more. Obviously, I was wrong. The stock markets, largely supported by consolidated demand in the U.S. economy as well as the Federal Reserve's accommodating bond-buying policy, resulted in pretty good investment returns for equities.

Going forward, these same conditions still exist: we have a commitment to growth, especially on the monetary side; American households and companies have been increasing their savings and now are showing signs of wanting to spend and invest; and foreign investors are still interested in the dollar.

So equities are a good investment choice, especially some of the smaller stocks in the U.S. I would advise against an over-reliance on emerging markets. Look for growth closer to home, because the U.S. economy seems to be the strong point moving forward. Despite our monetary and fiscal realignments that are creating uncertainty, the best conservative estimate for growth lies with the U.S. for now. ■

▶ *Continued from page 22*

with aircraft whose values were suddenly "underwater," meaning they owed more on the aircraft loans than the aircraft were worth. In some cases values were slashed by more than half. Faced with that unpalatable equation, many simply parked the aircraft and walked away, leaving lenders as the unwilling owners of scores of used older aircraft. "It shouldn't be surprising to the industry that since the global economic crisis hit, experienced corporate jet financiers have pulled back on financing 20- to 25-year-old jets," said Joseph DiLallo, director of corporate aircraft finance with BMO Harris Equipment Finance. "Since 2008, the inventory of 15-year-old-plus aircraft available for sale has skyrocketed and hasn't improved much over time. Nearly every aircraft broker, dealer and appraiser expresses little or no hope that demand for and values of these jets will pick up in the future."

"Lenders have been hurt by old aircraft, and their credit, risk and asset departments are seeking younger aircraft for their portfolios," confirmed Amalfitano. "An old aircraft is any aircraft that is older than 10 years at the inception of financing, and/or older than 15 years at the end of financing. We also try to limit the financing of aircraft that are two models out of production from today's current production." With the continuing development of derivative models from the OEMs, lenders are now paying closer attention than ever on loans on aircraft that have been superseded by newer, more capable replacements. "Aircraft finance underwriting will have to become more model specific, with particular attention paid to the anticipated life cycle of each product," said CIT's Kahmann. "Gone are the days of blanket 10-year loan terms based on 20- or 25-year loan amortizations."

Yet for those interested in seeking financing for an older jet, there are still options available. Some companies such as GE Corporate Aircraft Finance will, case-by-case, consider the financial characteristics of the buyer and the intended use of the aircraft as more significant than the age of the aircraft, while PNC Aviation Finance is among those that will generally finance aircraft up to 20 years old, with appropriate adjustments to the loan structure based on the aircraft's usage. Others will go even further. "We believe in the adage 'airplanes don't write checks, people do,'" said 1st Source's Qualey. "We are generally comfortable with jets up to 25 years old and turboprops and turbine helicopters up to 30 years old, provided we can get comfortable with their pedigree. Clearly the older the aircraft, the more skill required to underwrite it properly."

Lender Differentiation

Some see a divergence among lenders now taking place in the aftermath of the recession. "I see two levels of lender emerging out of the downturn in aircraft values," said Richard Ramsden, vice president and territory manager with Wells Fargo Equipment Finance. "Traditional lenders led by the major banks doing newer, larger aircraft, and a second group of lenders, often thinly capitalized, funded by private equity doing older, smaller aircraft that the major banks will no longer finance." Among its network of lenders around the world, Bombardier maintains a list of lenders that specialize in older aircraft deals mainly due to the lack of competition, said Vandenberg. "If you are talking to one of the bigger players who can pick and choose the types of deal they participate in, it would be unattractive to them to look at a smaller deal for pre-owned aircraft, but if you are looking for a niche player, they will seek out that kind of a deal. It's in the eye of the beholder."

A separate niche exists for wealthy individuals, with institutions such as Citi Private Bank, Credit Suisse or UBS. While those firms generally will not seek transactions on the open market, they are ready to handle aircraft financing for their existing clients, or for potential customers whose business they are courting. "Aircraft finance is simply a natural extension of our…suite of global investment finance products throughout the world," explained Citibank's von Weise. "Given our size and global reach and the type of client who requires this, we have no choice but to offer highly tailored debt and investment finance products."

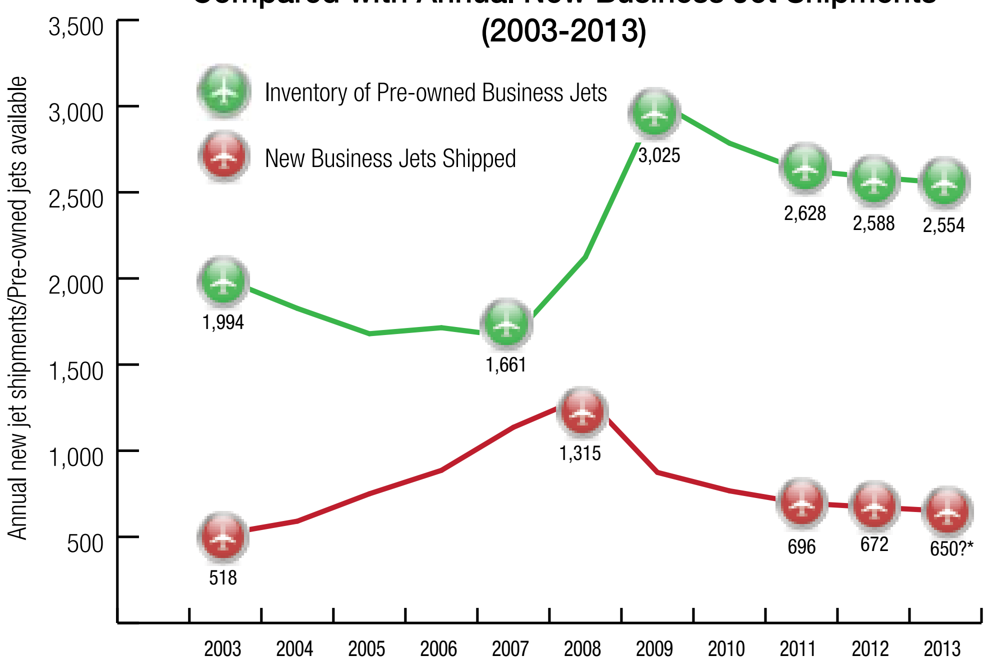
While the U.S. unquestionably is home to the world's most established business aviation finance market, the globalization of the industry has caused some lenders to cast their nets wider, seeking more international deals. "We do provide corporate aircraft financing globally and are seeing activity in Latin America, Asia-Pacific and Oceania, and we are actively doing business in more than 18 countries," Bank of America's Amalfitano told **AIN**. "There are banks that have identified key markets that they can participate in," said Bombardier's Vandenberg. "There was a push for a number of banks to get into China and take advantage of that market, there was a push for banks to look at Indian jurisdiction, and I'd say now there are probably more banks heading down to South America."

The role of the OEM has lessened somewhat in international transactions, he explained. "For example, on our first Chinese deals, we spent a lot of time. Now I think there have been reforms in China to make it easier for people to access funding and to get their money out of the country. That has made our job a lot easier and I think some of the banks are also just more practiced at it." Vandenberg also noted the emergence of Chinese leasing companies, which are taking a greater role not only within that country but outside its borders as well. "Last year we had ICBC. It was funding VistaJet, and we hope to see that as a trend for other banks to do deals external to China. Talking about emerging trends, I would think the Chinese leasing companies will become stronger players; they are certainly building their teams and they are certainly interested in participating in this market."

According to Corporate Jet Investor's Whyte, China is one of the easiest places to find funding. "If you want to buy an aircraft there are five or six large Chinese companies especially keen to talk to you and 15 to 20 that would talk to you. Even in the recent history of private aircraft financing in China, Whyte notes several firms (Minsheng for one) that have already funded a significant number of transactions. "I would say it's growing rapidly. It does take time to get the people, but there are some good people in China," he told **AIN**. "The interesting thing about the Chinese business jet finance [market] is that it hasn't been through a downturn…yet." ❏

Report continues on page 26 ▶

Annual Average Inventories of Pre-owned Jets Compared with Annual New Business Jet Shipments (2003-2013)



Sources: JetNet (Inventory of Preowned Business Jets); GAMA (New Business Jets Shipped); Honeywell (2013 forecast)
Notes: Inventory numbers for pre-owned business jets are averages for the year. New jet shipments are end-of-year totals.
*The total number of jets shipped by the end of 3Q/13 was 421. In 2012, it was 430.

A Look into the Crystal Ball

For this year's aircraft finance report, we asked these experts to predict the near future of the aircraft market.

Michael Amalfitano, managing director and executive head of corporate aircraft finance, Bank of America Merrill Lynch

"The market for both new and used business jets will be strong in the year ahead, with continued strength in North America, businesses becoming more interconnected globally, and OEMs expanding their global presence."

David Labrozzi, president, GE Capital, Corporate Aircraft Finance

"We believe the market will continue to strengthen slowly over time as the global economy heals and business activity increases."

Allen Qualey, president, Specialty Finance Group, 1st Source Bank

"We see minimal improvement with the exception of the new heavy jets."

Wayne Starling, senior vice president for sales and marketing, PNC Aviation Finance

"We have seen a steady pace develop in aviation financing, but this pace and any future growth will be affected by the economic and political environments and the tax implications they bring."

Michael Kahmann, managing director and group head, CIT Aviation Finance

"The evidence of a rebound has been long anticipated but remains hard to find. There are positive leading indicators, such as U.S. flight activity pointing to a future recovery, and we believe that an asset refreshment cycle will eventually fuel such a recovery; nevertheless, pegging the date of the recovery has proved to be difficult."

Joseph DiLallo, director of corporate aircraft finance, BMO Harris Equipment Finance

"I believe the buyer's market will continue, especially in the small and mid-cabin segments. I'm afraid that supply will continue to outpace demand, and this dynamic will continue to apply considerable downward pressure on new-jet pricing and used-jet values. I believe the most popular, highest pedigree, best-in-class aircraft will trade at fair prices, and others will move only at deeply discounted prices." –*C.E.*

Offshore registration offers more than tax incentives

by Curt Epstein

For many aircraft purchasers, the decision about where to register the new acquisition is an easy one. Most will simply brand the airplane with the ICAO letter code corresponding to their home country, but for others the choice is not so clear-cut. The recent expansion of foreign and offshore registries offers aircraft owners more options than ever based upon their specific needs.

"Questions that I get asked regularly are 'What's the Holy Grail of registration and can you tell me the big secrets that nobody else is telling me,'" said Aoife O'Sullivan, head of aircraft finance at London-based law firm Kennedys Aviation. She noted that the very word "offshore" tends to conjure an image of shady business dealings. "There's a tinge about the whole offshore thing that I actually think is unwarranted, and by tinge I mean you must be doing something dodgy, that you have this on a foreign registry," O'Sullivan said.

In fact, there are legitimate reasons an owner might choose to place an aircraft on a foreign registry in locales such as Aruba, the Bahamas, the Cayman Islands, the Isle of Man, Malta or even San Marino. While offshore registries might offer clear tax benefits, the long-held belief that they provide a tax dodge doesn't hold water, according to O'Sullivan. "You can't dodge taxes just by putting an aircraft on an offshore registry," she told **AIN**. "All you really get from the offshore guys that you won't get elsewhere is perhaps a bit more flexibility and more relaxed regulatory oversight."

"All of the offshore registries such as Aruba, Bermuda and the Cayman Islands are Organization for Economic Cooperation and Development compliant," noted Lincoln Gomez, a partner in the Aruba-based law firm Gomez and Bikker. "They have issued guidelines and regulations on taxation to make sure it's a level playing field. I can tell you Aruba has a tax information and exchange agreement with the U.S., so at any given point the governments can exchange information on any U.S. citizen who is lying here on the beach." Yet, in certain situations such as avoiding European VAT–a tax that could add several million dollars on a business jet purchase–for example, a carefully structured business plan involving an offshore registry could be effective.

Owners based in nations that lack a well developed private aviation industry might also opt for a foreign registry. "Certain civil aviation authorities are not up to par when it comes to registering business jets," Gomez said. "They simply lack the experience and the knowledge, and might even not be category-one status in terms of ICAO ranking." Such considerations could come back later to haunt the owner.

While many operators register their aircraft in their nation of origin, others look farther afield to take advantage of the benefits offered by the growing number of offshore registries. In some cases tax benefits are the big draw, but there are other significant incentives, such as privacy, increased flexibility and more regulatory oversight.

"If you are registered [in an undesirable territory] and you want to resell your aircraft later, [potential buyers] will see where it has been registered and that will adversely affect the resale value of the aircraft," he said.

Mission-specific Considerations

O'Sullivan advises her clients they will have to make several important decisions about their aircraft operation. "There isn't a Holy Grail," she said, "and [a client's] answer to any one of those questions that I'll ask will have me flicking from one registry to another." Gomez concurred. "Not all registries are alike," he added. "It's not one size fits all, and if you don't get the right match, you could end up not being happy with the experience."

He noted that nearly all of these registries courting business offer certain benefits. "They have the expertise in house to provide proper regulatory oversight of the aircraft, so that's where the residual resale value kicks back in. People have confidence in those registries, so bringing an aircraft back from one of these registries into the U.S., for instance, is not a problem and people will have confidence that it has been serviced properly."

In this politically turbulent world, there are owners who may prefer a more discreet registry, based on their sphere of operations. Some clients, depending on where they fly, won't choose FAA registration because it's America and they don't want their aircraft flying a big N on the tail, said O'Sullivan. "I've had clients for whom the perfect register is the FAA and they've refused to go on it purely for that reason."

"Some people think there is a benefit in having more of a neutral registry," said Gomez. He pointed out that Aruba, Bermuda, the Cayman Islands and the Isle of Man "are not jurisdictions that are at war with anyone, or that other countries have issues with, so it's a nice neutral registry" that allows an owner to fly anywhere without the tail number offending anyone.

If financing is required for the airplane, the lender will have a large say in where it is ultimately registered. "The minute you put an aircraft on a registry, you are by default involving a new legal jurisdiction, because when it goes to enforcement for the lender, they'll have to talk to the Isle of Man [for example] if there's a problem," said O'Sullivan. Lenders will push to select a registry in a jurisdiction that adheres to the Cape Town Convention, which will respect the rights of the lender as the true owner of the aircraft in cases of loan default. In such areas, the aircraft will be registered by the lender, who will require the borrower to sign an irrevocable de-registration and export request authorization (IDERA).

According to O'Sullivan, the document essentially gives power of attorney to the lender. "It says to the registry, 'I have the authority on behalf of the registered owner or operator to remove this aircraft from the registry and you must listen to me.'" The document will prevent the borrower from immediately de-registering the aircraft without the lender's permission and registering it on a less legal-friendly register. "The bank, in case of default, can go directly to the department of civil aviation and say, 'I want you to de-register my collateral,'" said Gomez. Some registries (Poland's and India's among them) have shown difficulties in this area, leading lenders to avoid them. Lenders on foreign-registered aircraft are also much more likely to require their enrollment in a maintenance program such as JSSI or Camp, to ensure that the asset is maintained properly.

Finding the Right Fit

The ownership structures that are available in a specific registry can also weigh heavily on the selection. O'Sullivan points out that having the provisions for a standard limited liability corporation are crucial to reduce the amount of exposure on the owner in the event of an accident. "What you are trying to do with the whole ownership structure is play a game of tennis with the risk side, and what you are trying to do is deflect all of the risk away from the owner and onto the operator or whoever else you can find," she said, adding that the legal system behind the registry is important.

Other decisions factor in as well when selecting a registry. If the aircraft is to be used for charter, that will eliminate certain registries (such as the Isle of Man's) that are strictly for private aircraft, making any paid transport of customers illegal. Some registries (China's is one example) won't take an aircraft older than 10 years, while others will not accommodate single-engine airplanes. Some are particular about who they will admit to their register, viewing it as a lure to attract business to their country. "The business side of an aircraft registry is thinking, 'I'm not just going to register any old aircraft for Mr. Random from Malaysia,'" explained O'Sullivan. "It's saying, 'You can put your aircraft on my registry, but I would like you to consider setting up your company and hiring local directors, opening a local bank account and please give us some business in return.'"

Discretion and the ability to keep aircraft ownership confidential are two longstanding hallmarks of offshore registration. "That can be important, particularly to a corporate [executive] who hasn't told his shareholders," quipped O'Sullivan.

There are some pitfalls to avoid when selecting a registry. Operators who place an FAA-certified aircraft onto a registry that operates under EASA rules could be facing a bill of hundreds of thousands of dollars to bring it into compliance. That goes for pilot licensing as well. Registries may recognize the FAA or EASA, but not necessarily both, which could either force pilots to requalify or the owner to search for new crew.

While some registries (Aruba's, for one) have existed for more than two decades, Gomez said potential clients should not underestimate others due to their youth. "A lot of them have highly experienced civil aviation authority guys from all over the world," he noted. "Their relative young age doesn't mean that [the registries] are inexperienced."