

# Unique Issues in Aircraft Purchase and Sale Transactions Involving a Non-U.S. Party & Tax-Free Aircraft Exchanges Under IRC 1031

GKG Law, P.C. Webinar Series

Presenter: Troy A. Rolf  
Partner  
GKG Law, P.C.  
Phone: (952) 449-8817  
trolf@gkglaw.com

Presenter: Christopher B. Younger  
Partner  
Phone: (202) 342-5295  
cyounger@gkglaw.com  
www.gkglaw.com



# Unique Issues in Aircraft Purchase and Sale Transactions Involving a Non-U.S. Party





# Import/Export Transactions: Managing Expectations

- Types of representations
  - Clear title
  - Aircraft condition/airworthiness
  - Aircraft specification
- Survival of representations



# Import/Export Transactions: Managing Expectations

- Timing of release of funds
  - Lenders' requirements
  - Escrow Agreements
- Delivery location
- Use of Trusts/U.S. Brokers





# Import/Export Transactions: Managing Expectations

- Deposit amount
- Exchange rate fluctuations
  - In what currency is the purchase price payable?
  - Increased risk of default may justify increased deposit/remedies



# Import/Export Transactions: Managing Expectations

- Carrying Seller as an additional insured
- Choice of law/forum
- Article 2(e) of the United Nations Convention on Contracts for the International Sale of Goods





# Import/Export Transactions: Exporter's Issues

## Deregistration request

- Make/model/serial number/N-number
- Reasons for deregistration (e.g., export)
- Destination country

→ No liens on file



# Import/Export Transactions: Exporter's Issues

- Notice of Deregistration/Non-Registration
- Export C-of-A / DAR Inspection





## Import/Export Transactions: Exporter's Issues (IDERA on File)

Secured Parties/Lenders acting pursuant to an Irrevocable Deregistration and Export Request Authorization (IDERA) must:

- certify “that all registered interests ranking higher in priority to that of the requestor have been discharged or that the holders of such interests have consented to the cancellation for export purposes”
- provide evidence of the discharge of interests or consent of higher ranking interest holders



# Import/Export Transactions: Importer's Issues

- ➔ Notice of Deregistration/Non-Registration
  - Should be in English to avoid a 1-3 day delay
  - Additional certification may be required if 90 days has elapsed
- ➔ Bill of Sale/Proof of Ownership
  - Original, ink signature (no fax/pdf/etc)
  - Establish full Chain of Title





# Import/Export Transactions: Importer's Issues

## → C-of-A

- DAR inspection
- 135 Conformity inspection
- Equipment requirements

## → DAR inspection letter



# Import/Export Transactions: Importer's Issues

- Title Opinion/Title Insurance
- Application for Registration (8050-1)
  - Pink copy is not an authorization for domestic ops
  - Fly-wire automatic; no need for DIO





# Tax-Free Exchanges Under IRC 1031



## Disclaimers

- This presentation is being provided for general information and should not be construed as legal advice or legal opinion on any specific facts or circumstances. You are urged to consult your attorney or other advisor concerning your own situation and for any specific legal question you may have.
- IRS CIRCULAR 230 DISCLOSURE - To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. tax advice contained in this communication is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.





## Your Tax Concerns

- Your aircraft has been fully (or nearly fully) depreciated for tax purposes
- Your aircraft has significant market value



## Your Tax Concerns Cont...

- ✈ You want to sell your aircraft and use the proceeds to buy another aircraft, but the sale of your “old” aircraft could result in millions of dollars of recapture, all of which could be taxable at ordinary tax rates





## Your Solution

→ If you "exchange" your old aircraft for your "new" aircraft in a transaction qualifying under Section 1031 of the Internal Revenue Code, you may be able to defer recognition of some or all of the gain from the sale of the old aircraft



## Issues?

- Qualifying a transaction under Section 1031 can be complicated
- Transaction form and timing are critical





## Issues Cont...

- An inadvertent or relatively minor timing or documentation error in an otherwise properly structured transaction can cause the whole transaction to fail to qualify under Section 1031



## Statutory Elements of a Tax-Free Exchange

- You must have held your old aircraft for productive use in a trade or business, or for investment
- You must hold your new aircraft for productive use in a trade or business, or for investment





## Statutory Elements of a Tax-Free Exchange Cont...

- Your new aircraft must be “like-kind” to your old aircraft
- You must NOT sell your old aircraft and purchase your new aircraft in separate transactions, but rather must exchange your old aircraft for your new aircraft



## Statutory Elements of a Tax-Free Exchange Cont...

- You must recognize gain to the extent of any cash or any other non-qualifying property received in the exchange
- Your basis in your new aircraft will be adjusted downward by the amount of gain deferred by the exchange





# Multi-Party Exchange and Deferred Exchange Safe Harbors

→ If you are not actually selling your old aircraft to the same party from whom you will purchase your new aircraft (e.g. an OEM), the transaction must be structured as a multi-party exchange



## Multi-Party Exchange and Deferred Exchange Safe Harbors Cont...

- In multi-party exchanges, the sale of the old aircraft and the purchase of the new aircraft may occur simultaneously, or up to 180 days apart





## Multi-Party Exchange and Deferred Exchange Safe Harbors Cont...

- If you will close the purchase of your new aircraft within 180 days subsequent to the closing of the sale of the old aircraft, you must structure the transactions as a “Forward Exchange”



## Multi-Party Exchange and Deferred Exchange Safe Harbors Cont...

- ➔ If you will close the purchase of your new aircraft within 180 days prior to the closing of the sale of the old aircraft, you must structure the transactions as a “Reverse Exchange”





## Forward Exchange Basics

- Authorized by Treasury Regulations § 1.1031(k)-1
- Qualified Intermediary (“QI”) acts as middleman in sale of the old aircraft and acquisition of new aircraft



## Forward Exchange Basics Cont...

- You and QI enter into an Exchange Agreement which restricts your rights to receive proceeds from the sale of the old aircraft
- Proceeds from the sale of the old aircraft are held in a qualified escrow account or a qualified trust account pending purchase of the new aircraft





## Forward Exchange Basics Cont...

- You **must** either acquire the new aircraft, **or** specifically identify the aircraft that will be acquired, **within 45 calendar days** after completion of the sale of the old aircraft.
- You may be allowed to identify multiple and/or alternate aircraft



## Forward Exchange Basics Cont...

- You **must** complete your acquisition of the new aircraft no later than the earlier of:
- (1) the **180th calendar day** after completion of the sale of the old aircraft; or . . .





## Forward Exchange Basics Cont...

(2) the due date (including extensions) of your Federal income tax return for the taxable year in which the sale of the old aircraft occurred



## Reverse Exchange Basics

- Authorized by IRS Revenue Procedure 2000-37, 2000-40 IRB 1 (September 15, 2000)





## Reverse Exchange Basics Cont...

- Procedures are similar to Forward Exchange, except that an Exchange Accommodation Titleholder ("EAT") holds title to either the old aircraft (a "Front-End Reverse Exchange"), or the new Aircraft (a "Back-End Reverse Exchange") until a closing of the sale of the old aircraft can be arranged. (The EAT usually also performs the QI function)



## Reverse Exchange Basics Cont...

→ You and EAT must enter into a Qualified Exchange Accommodation Agreement





## Reverse Exchange Basics Cont...

- You **must** either complete a sale of the old aircraft to a third-party buyer, or specifically identify the aircraft that will be sold, within **45 calendar days** after the acquisition of the new aircraft by you in a Front-End Reverse Exchange, or by the EAT in a Back-End Reverse Exchange



## Reverse Exchange Basics Cont...

- The sale of the old aircraft **must** be completed no later than: the **180th calendar day** after the acquisition of the new aircraft by you in a Front-End Reverse Exchange, or by the EAT in a Back-End Reverse Exchange; OR
- The due date of the taxpayer's federal tax return, including extensions, if prior to 180 days





## Common Questions

- 1) Who may and who may not serve as Qualified Intermediaries and/or Qualified Exchange Accommodation Titleholders? (e.g., Lawyers, Accountants, Aircraft Brokers)



## Common Questions Cont...

→ 2) Are OKC escrow accounts "Qualified" escrow accounts?





## Common Questions Cont...

→ 3) In a forward exchange, can I take title to a **green** aircraft in exchange for my old aircraft?



## Common Questions Cont...

→ 4) Can I make progress payments on a new aircraft?





## Common Questions Cont...

- 5) Can I exchange my aircraft for:
1. An interest in a partnership that owns a different aircraft?
  2. A 100% interest in a limited liability company that owns a different aircraft?
  3. A fractional interest in a new aircraft?



## Common Questions Cont...

→ 6) Can I trade two old aircraft for one new aircraft in a single 1031 transaction?





## Common Questions Cont...

→ 7) Can I exchange my old aircraft for a new aircraft of lesser value and receive the price difference in cash tax-free?



## Common Questions Cont...

→ 8) What happens if I do a Reverse Exchange and can't sell my old aircraft within 180 days of the purchase of my new aircraft?





## Common Questions Cont...

→ 9) Will my exchange qualify as a “trade-in” for state sales and use tax purposes?





## Closing Remarks

**Christopher B. Younger**  
**GKG Law, P.C.**  
**1054 31<sup>st</sup> St., Suite 200**  
**Washington, D.C. 20007**  
**Tel: (202) 342-5295**  
**Fax: (202) 965-5725**  
**[cyounger@gkglaw.com](mailto:cyounger@gkglaw.com)**

**Troy A. Rolf**  
**GKG Law, P.C.**  
**700 Twelve Oaks Center Dr., Ste 700**  
**Wayzata, MN55391**  
**Tel: (952)449-4817**  
**Fax: (952)449-0614**  
**[trolf@gkglaw.com](mailto:trolf@gkglaw.com)**

