



Chris Younger is a partner at GKG Law, P.C. practicing in the firm's Business Aircraft Group. He focuses his legal practice on business aircraft transactions as well as issues relating to federal and state taxation and regulation of business aircraft ownership and operations. Mr. Younger can be contacted at cyounger@gkglaw.com

Business Aircraft Ownership & Ops: *Common Mistakes, and How to Avoid Them (Part 2).*

Following last month's article, Attorney Chris Younger describes two additional mistakes that Boards make in connection with the acquisition and operation of business aircraft.

"The Board must ensure that myriad restrictions on the availability of deductions relating to aircraft ownership and operations are analyzed and thoroughly considered..."

Issues related to federal tax liabilities and the need for adequate documentation are addressed in the following paragraphs.

TAX PLANNING AND FINANCIAL REGULATORY COMPLIANCE

A corporation's Board must consider the federal income tax and excise tax ramifications of an aircraft acquisition and the requirements of any financial regulations that the company must follow in connection with ownership and operation of the aircraft. In many instances, a Board fails to adequately address these issues.

Business aircraft are depreciable business assets that can provide a company with substantial deductions from taxable income provided that they are owned and operated in a manner that allows a company to take those deductions. The Board must ensure that myriad restrictions on the availability of deductions relating to aircraft ownership and operations are analyzed and thoroughly considered to ensure that a company gets the income tax benefits to which it is entitled, and on which an aircraft acquisition may be predicated.

These include basic issues such as whether the deductions are ordinary, necessary and reasonable, and whether the correct depreciation schedule is utilized. However, there are far more complex and esoteric issues that a Board must analyze, including limitations on deductibility of hobby losses and passive activity losses, listed property rules, at-risk loss limitations, and compliance with like-kind exchange requirements.

There are also a host of income tax and financial regulation requirements that pertain specifically to non-business employee use of company-provided aircraft. Knowledge of, and careful compliance with, these regulatory requirements is an essential element



What the Boardroom needs to know about Business Aviation

of any aircraft owner's acquisition plan.

Another common mistake is the failure to consider potential federal air transportation excise tax liability. This issue often arises when a company enters into a poorly structured aircraft management agreement, which can unknowingly subject the aircraft owner to federal excise taxes.

Companies that own business aircraft often utilize the services of a third party aircraft manager in lieu of establishing their own internal flight department. The manager provides aircraft support services to the owner including items that are essential to the operation of the aircraft such as crew, insurance and hangar. However, if the agreement between the company and the manager is not properly structured, the company could be held liable for federal excise tax of 7.5% of all amounts it pays to the manager.

The Board's failure to adequately consider and address any of these issues can lead to severe financial consequences to a company and to substantial tax liabilities and civil and criminal penalties imposed on the company and/or its owners and officers. Examination of these issues ahead of time is therefore imperative.

INCOMPLETE OR INSUFFICIENT DOCUMENTATION

Designing and implementing a legally-compliant and tax-efficient business aircraft ownership and operating structure is just the tip of the iceberg. Much of the real work in this area comes after a company acquires an aircraft. The Board must ensure that the company creates and maintains adequate documentation to support its tax planning objectives and to meet its ongoing legal obligations.

In many instances, the Board hires a Business Aviation consultant who works with it to create a dazzling aircraft ownership and operating structure that is designed to minimize sales tax liability, maximize income tax benefits and ensure full compliance with all regulatory requirements. However, follow-through is often lacking.

Specifically, the Board may not fully understand its recordkeeping and reporting obligations, which include creating internal systems and hiring external advisors and consultants to provide and maintain the records that provide the foundation to support the plan that was so carefully designed.

It is essential for the Board to understand that a company needs adequate and thorough documentation to support its position in the event of a sales or income tax audit.

In many instances, because of the complexity inherent in the ownership and operating structure that is utilized, the creation and continued maintenance of these records can be time consuming and expensive. However, the failure to create and maintain appropriate records will ultimately lead to higher costs and a more time consuming problem.

It is also essential that the Board gain a complete understanding of the company's regulatory reporting obligations, and that the company file all reports that are required of it with respect to its business aircraft ownership and operations.



"Specifically, the Board may not fully understand its recordkeeping and reporting obligations..."

Note: This article should not be construed as legal advice or legal opinion on any specific facts or circumstances. The reader is urged to consult legal counsel or other advisors concerning his/her own situation and specific legal questions.

Do you have any questions or opinions on the above topic? Get them answered/published in World Aircraft Sales Magazine. Email feedback to: Jack@avbuyer.com
Business Aviation and the Boardroom continues on Page 58