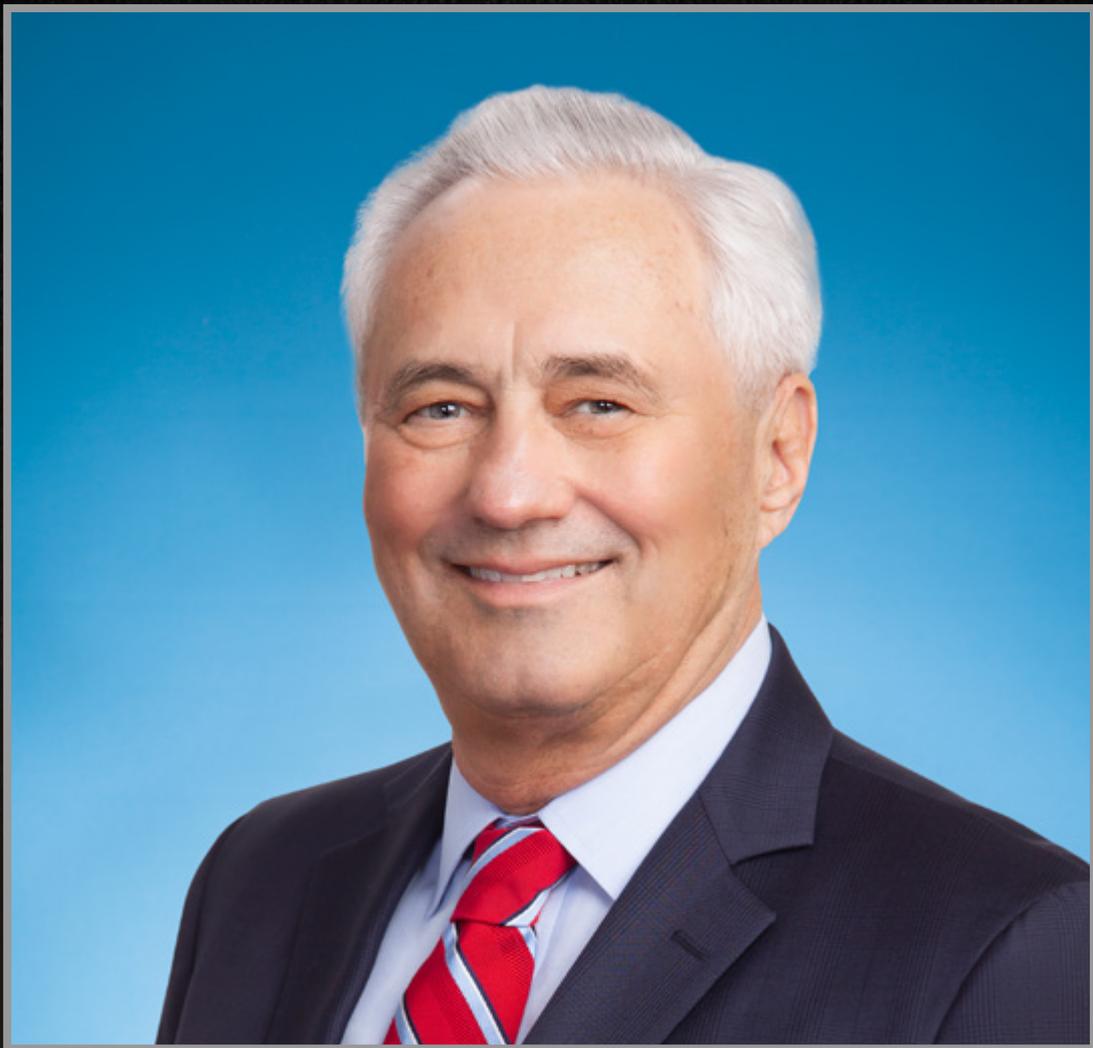


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PLANE TRUTH

The economic substance behind aircraft ownership



By Grant Atchison, Client Services Director at IQ-EQ

Buying an aircraft doesn't have to be complicated. However, with more jurisdictions waking up to the need for economic substance, it needs a thorough, measured approach that considers every layer of complexity. What appears to be the quickest, least expensive and easiest option – as attractive as it may initially look – is unlikely to be the best way to secure the asset and owner interests and it may be a costly path to tread in the long run.

As a private wealth specialist, I've witnessed the aftermath of owners rushing to create an asset-holding company in particular jurisdictions off their own bat and without due consideration as to how it might affect them from a personal tax point of view – not to mention a raft of other costly legal complications.

Authorities are increasingly making sure problematic structures are hard to unravel and re-do at a later date. Remaining within the law and planning properly when buying an aircraft is therefore more pertinent than ever.

Ownership considerations

Whether you're a high-net-worth individual wanting to invest directly from day one, or a JetCard traveller clocking up 200+ flying hours a year and taking the decision to own outright, the initial steps involved in buying an aircraft are the same. Firstly, the type of aircraft needs to be considered, alongside how much to spend and where it will be based. Other considerations, such as whether the aircraft will be utilised commercially to create an income, will also need to be taken on board. The next pivotal decision is about who is going to manage it operationally. Will an in-house team be used or will management be outsourced to a third party? Once these key decisions are made, it's time to build the ownership structure – and these foundations need to be solid from the start.

Trusted network

This is where the role of trusted advisers takes centre stage; acting as a figurative legal and corporate Praetorian Guard, they can ensure your interests are

protected from the outset. They can assess your personal circumstances and create a structure specifically suited to you – one that has economic substance and is fully compliant. These experts can also help you to decide how to fund the purchase and the best way to structure the investment. For example, if a trust is set up the monies will be placed into a shareholding company that will in turn fund the aircraft owning entity. The importance of getting professional guidance on the right structure – from a tax, corporate governance and/or accounting point of view – should not be underestimated.

Costly mistakes

This is especially true when it comes to tax compliance. Personal taxes, of course, depend on an individual's worth, income and where they are resident or domiciled. Many countries have their highest income tax rates at almost 50%. Then there's VAT, which in Europe ranges from 17% to 27%. These are big numbers when placed against the value of your asset. If you have, for example, a \$50 million aircraft and your VAT or income tax is calculated incorrectly you could be looking at multi-million dollar penalties. So it's worth getting it right.

Lessons from the past

As history has shown, if a solution looks too good to be true, then it probably is. For example, in 2010, Denmark took the decision that business aircraft could no longer be imported at a zero rate of VAT. Similarly, post 31 December 2010, UK authorities no longer permitted business jets with a maximum take-off weight in excess of 8,000 kg to be imported as 'qualifying' aircraft and, as such, be zero rated for VAT purposes.

The reasons for those decisions? The EU Commission successfully argued that the Danish and UK interpretations of Article 148 of the EU VAT Directive were not in line with the legislation and must be discontinued. The possibility of similar infringement proceedings and related reputational damage should be considered when it comes to planning the aircraft structure to be put in place.

Tax efficiency

Tax should never be the main driver behind any aircraft-owning structure. If the primary focus seems to be tax mitigation, it invites further scrutiny. As the saying goes: 'don't let the tax tail wag the dog'. Rather, the

goal is to ring-fence and protect the asset against any form of claim or liability. Having said that, there should be a tax efficiency element to operating and creating the structure. Whether an aircraft is funded privately or through a trust, the establishment and management of the structure should incorporate best practice with respect to regulatory compliance, risk mitigation and asset protection.

Good governance

Aircraft owners also need to take corporate governance seriously; to show that there are real people making real decisions in real time. One of the best ways to achieve this is to create a 'Chinese wall' between directors and trustees and ensure independence between the decisions taken by entities within the structure as appropriate. This will involve greater costs but ultimately increased peace of mind as not only will your structure be under constant review, but your dedicated team will be ready to adapt proactively to changes in your personal circumstances or in the regulatory, political or aviation landscape.

Brexit impact

On that note, it would be remiss not to mention Brexit. In the UK and Europe, Britain's departure from the EU may have implications for any current or prospective aircraft owner. For example, if a no-deal Brexit goes ahead, this could have an immediate impact on structures and aircraft operating in Britain and the rest of the current EU27. Having an expert team on hand would facilitate a full assessment of the different scenarios that will impact what happens, when and where and if any restructuring is necessary. Without that trusted network taking protective steps, the owner would be left with conjecture and uncertainty.

Historically, potential aircraft owners may have sought the quickest, most cost-effective way to buy an aircraft. Now, special purpose vehicles (SPVs) and entities for high-value assets need to be robust and compliant as more and more jurisdictions seek structures with economic substance. Once more, if the proposed solution seems too good to be true, then the chances are it is just that. Approached in the right way, the journey towards buying an aircraft should be smooth, efficient – and, above all, exciting.

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