Making an early exit

Need to opt out of your fractional contract? Selling your share back to the provider probably isn't the most cost-effective way.

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Fractional owners opt out of their contracts early for many reasons. You may have sold an out-of-town business and so charter or a jet card may better serve your reduced needs. Maybe you're flying more than you expected and it makes sense for you to purchase a whole aircraft. Perhaps you want to share flights with business associates or friends, but they all belong to a different program.

If you have a standard contract, it most likely obligates the provider to buy back your share at a price calculated as the fair market value of your aircraft multiplied by the size of the share, less a "remarketing fee." However, you may have a large amount of unused flight hours for which you've already paid management fees–hours you'll lose if you sell to your provider. Besides, you most certainly paid a premium over the aircraft's fair market value for your share and your provider undoubtedly will offer less than you paid. No doubt, also, the remarketing fee will be large–probably 3 to 12 percent, depending on when you sell (some providers charge more early in the contract term) and whether you negotiated this fee before you signed.

There are, however, other roads you can take. Selling to a third party rather than to your provider holds many potential advantages. If you have much flight time remaining, below-market management fees or other favorable contract terms, these benefits would be lost in a sale to your provider but may be captured in the purchase price in a third-party sale. And, generally, no remarketing fee is payable to the provider on a third-party sale.

Many providers, however, are intent upon controlling the market for their shares. They don't want you competing with them for customers and they don't want to lose that fat remarketing fee. So they've changed their contracts to restrict third-party sales, either by adding outright prohibitions or by insisting upon onerous approval rights. Indeed, to date, a significant secondary market in fractional shares has not developed, although avenues do exist for reselling shares online *(see box)*.

If your contract effectively blocks you from selling to a third party, consider whether you may achieve the same result by selling membership interests in the limited liability company you probably set up to own the share. Indeed, if you're inclined to sell because your share is too large, consider selling a part of the membership interests to a partner, thereby relieving you of excess financial burden while leaving you with a share that's sized for your needs.

By structuring the transaction as a "stock sale" instead of an "asset sale," you may avoid running afoul of your contract restrictions because the entity that owns the share will not change. But, as with all these suggestions, you should consult legal counsel to make certain that the sale is structured correctly; that safeguards are in place; and that, after the sale, you're no longer liable for the obligations of the limited liability company (or the portion that you sold).

Avoiding Financial Haircuts

If a sale isn't in the cards, you may want to investigate yet another road–restructuring your investment with the provider, perhaps reducing it and thereby avoiding or at least postponing the financial haircut. You may consider moving to a smaller share or different aircraft to better manage costs. Transitioning to a jet card may be an attractive option as well. You'll recover much of your capital investment and perhaps avoid an even lower share resale value down the road.

Most providers will offer more hospitable exit terms if you're continuing as a customer. Reduced remarketing fees may be possible and you also may find more flexibility in negotiating the value of your share. Be aware, however, that a provider's jet card program may have more restrictions and fewer concessions than you enjoy in its fractional program. Review the contract documents thoroughly so that you fully understand your rights and obligations.

Finally, if you're exiting because of service problems, and so remaining a customer isn't an attractive option, consider whether these service failures amount to a default by your provider under your management agreement. If so, you may be entitled to exit the program without paying a remarketing fee on repurchase of your share. Be sure to document any service problems in writing with the provider at the time they occur so that you have a solid paper trail.

If you find that your fractional investment just isn't working, you can follow the costly exit ramp laid out by your provider, or you can travel a road less taken, a road that, to paraphrase the poet Robert Frost, "can make all the difference." ❑

Where To Sell Your Share

Although a significant secondary market in fractional jet shares has not yet developed, there are some resources on the Internet. On my firm's Web site, www.shaircraft.com, we recently launched Shaircraft Connections, a forum for private jet travelers, where you can post your share for sale. Also, the Web site JetRe.com advertises preowned shares for sale, although its listings generally are sparse and it charges sellers half the remarketing fee specified in the seller's contract. *–J.B.*

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