



## BACK-TO-BACK AIRCRAFT TRANSACTIONS THE RISKS FOR SELLERS AND BUYERS

The sale or acquisition of a business jet is a complex process that involves commercial, technical, contractual, regulatory, fiscal, and/or customs aspects and involves the intervention and coordination of a number of stakeholders with different interests – among which: the seller, the buyer, the escrow agent, the broker, the operator, and the financing institute.

As a result, the seller and/or the buyer who don't have the necessary experience to successfully complete the sale or purchase of a business jet would benefit greatly by enlisting the help of trusted professionals who can assist them and take all necessary precautions to safeguard their interests. Thus, the seller and the buyer may have to call on the services of a professional broker with a good network, who is able to find the ideal buyer for the seller, or help the buyer find an aircraft that exactly suits his needs.

While brokers play an essential role, they do not necessarily enjoy a good image, due to the abusive practices of a minority. Generally, the international market for business jets suffers from a lack of integrity, transparency, and ethics, and is largely beyond state control. In recent years, one of the most flourishing such practices has been for the broker to receive an illicit commission by setting up a hidden so-called "back-to-back" (B2B) transaction.

While certain B2B transactions may be justified in specific cases, any B2B transaction made without the knowledge of the seller and/or the buyer involved exposes them to financial, contractual, regulatory, fiscal, and customs risks – not to mention, risks related to the aircraft's ownership – without the seller and the buyer being able to control them. This memo introduces the concept of a back-to-back transaction – particularly when it is illicit – as well as the risks both parties are unwittingly exposed to in such transactions.



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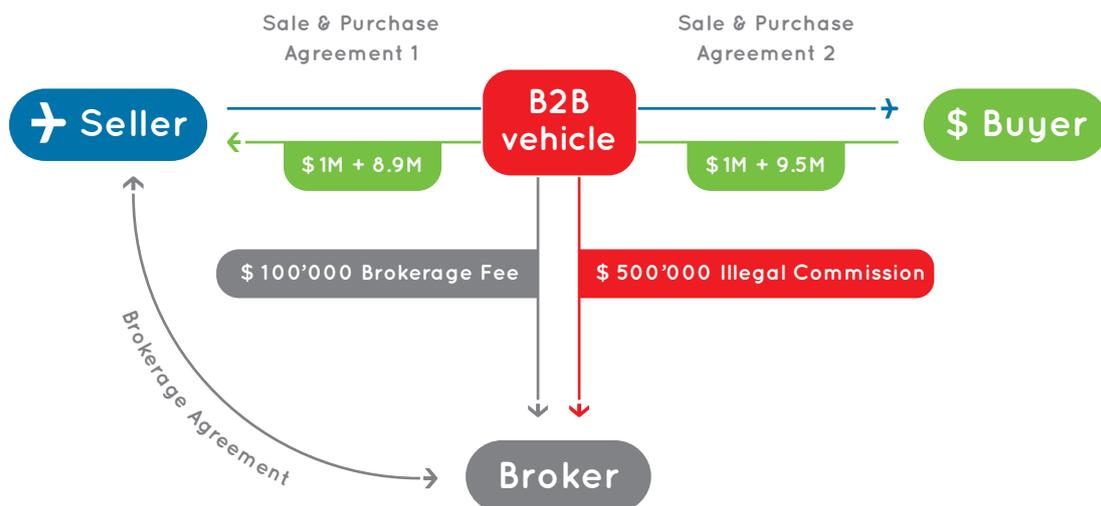
## THE “BACK-TO-BACK” TRANSACTION

In the context of a “back-to-back” transaction, ownership of the aircraft does not pass directly from the seller to the buyer but rather passes through an intermediary company that buys the aircraft and resells it almost instantly to the buyer. As a result, the ordinary and direct contractual relationship between the real seller and the real buyer of the aircraft does not exist in a B2B transaction, as it is replaced by a dual contractual relationship: an initial sales contract between the real seller of the aircraft and the intermediary company, acting as “buyer,” then a second sales contract between the intermediary company acting as “seller” and the real buyer.

The use of a B2B transaction may be justified in certain specific cases, for example in the context of a corporate mandate, trade-in, or aircraft positions. However, many brokers are setting up illicit B2B structures for the sole purpose of illegitimate personal enrichment, at the expense of their clients.

## AN ILLICIT BACK-TO-BACK

Here is an example of the simplest and most common type of illicit B2B transaction:



In practice:

- A broker has an exclusivity agreement with an owner who wants to sell his business jet. He is promised a brokerage fee of 1% of the aircraft's sale value.
- The broker advises the seller to put the aircraft on the market for \$10 million. However, the broker knows that he can probably find a buyer who is willing to pay \$10.5 million, and that is what happens. The non-refundable deposit to be paid by the buyer to the seller is set at \$1 million.
- The broker creates or uses an intermediary company ("B2B vehicle"). The seller believes that the intermediary company is the acquiring company, and the buyer believes that it is the selling company. The broker finalizes two identical sale and purchase contracts, one between the B2B vehicle and the seller, the other between the B2B vehicle and the buyer.
- The broker uses an escrow agent and the intermediary company to transfer the non-refundable USD 1 million deposit advanced by the buyer to the seller and, upon closing of the transaction, the balance of the sale price paid by the buyer. The broker does not invest any personal funds in the transaction, as only the buyer's money is used.
- During the closing, the broker retains an illicit commission of \$500,000 via the intermediary company – that is the difference between the \$10 million his client receives and the \$10.5 million actually paid by the buyer. In addition, the broker also pockets the official \$100,000 brokerage fee. The intermediary company is then liquidated, and the illicitly acquired funds are transferred to his account.
- In doing so, the broker is violating his contractual obligations toward his client: he is improperly enriching himself without his client's knowledge, and furthermore, is exposing him to significant uncontrollable risks. Moreover, this deception is often a criminal offense, such as improper management or fraud.



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## THE RISKS OF THE SELLER AND OF THE BUYER

The use of a hidden and illicit B2B transaction, or of a transparent and lawful but poorly designed B2B transaction, exposes both the seller and the buyer to financial, contractual, regulatory, fiscal, and customs risks – not to mention, risks related to the aircraft's ownership. Both parties have a vital interest in understanding and avoiding, anticipating, or controlling these risks. The main risks are the following:

- If the broker defaults or there is an error in the transaction, the seller may be left without any right to the deposit, as he does not have a contract with the buyer who paid it.
- If the broker did not take the necessary precautions in designing the B2B structure, the seller may find himself in an awkward legal position with regards to legislation prohibiting sales to countries subject to an embargo.
- The buyer may not be able to assert the seller's liability for certain events that take place after the sale, such as if a third party claims a lien was placed on the aircraft prior to the sale.
- The buyer and the seller may not be able to assert any failings relating to the promises, representations, warranties, indemnifications and disclaimer arising from the sales contract, since they do not have a contract directly between them.
- The buyer and the seller may end up having to pay taxes (State sales taxes, VAT, etc.) on the transfer of ownership and/or having to import the aircraft into a specific country, including payment of customs duties, because in the course of concealing the B2B structure, the broker did not or could not take the necessary steps to ensure that the parties would not run into any fiscal and customs risk.



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## SECURE YOUR TRANSACTION WITH CLEAN AERO

Clean Aero assists the sellers and buyers of aircraft to eliminate their exposure to risk, by offering following services:

- Analysis of the structure of a transaction to detect the potential presence of a hidden and illicit intermediary company (B2B).
- Advice on how to structure a transaction from a contractual perspective to eliminate the risk that a hidden and illicit intermediary company is used.
- Analysis and follow-up of sales, purchase, brokerage, escrow agreements, etc., according to the principles of transparency and ethics recognized in the business aviation market (NBAA - IADA - NATA).
- Analysis of the risks of using a transparent and legitimate intermediary company in a transaction. Advice on how to remove these risks.

## YOUR CLEAN AERO TEAM



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