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# PHILIPPE RENZ,

CO-FOUNDER CLEAN AERO.

By launching Clean Aero, the aviation lawyers Michelle Wade and Philippe Renz hope to improve integrity, transparency, and ethics in the deregulated market of aircraft sales and acquisition.

BY SYLVIE PERON

The market for the sale and acquisition of business aircraft continued to grow in 2018. The performance increase of this lucrative business has attracted more and more brokers in recent years. Some see this business as a way to make a substantial commission with very little investment and little work experience.

The business aviation industry has begun to take note of this problem, especially in the United States. The National Business Aviation Association (NBAA) and the National Air Transportation Association (NATA) have recently reaffirmed the ethics and integrity elements that should apply to business aviation stakeholders, especially in the sales and acquisition of aircraft. The International Aircraft Dealers Association (IADA), formerly NARA, has launched a campaign with the ultimate goal of standardizing contractual practices and improving the training of brokers. The subject of transparency and ethics also features prominently at our industry's conferences. And the issues are always the same: how to train, regulate, and monitor brokers in an international context? Who should or can do that? How to avoid illicit transactions that damage the sector's image?

In this climate of suspicion and momentum for compliance, American aviation lawyer Michelle Wade and her Swiss colleague Philippe Renz have just launched Clean Aero, a consulting service designed to secure transactions involving aircraft. The goal is to ensure that these proceed with the integrity, transparency, and ethics necessary to protect the interests of the key players.

Philippe Renz, speaks about the issues and compliance challenges that the transaction market is facing today which led him to found Clean Aero.

## How do you see the current market for aircraft transactions?

The aircraft transactions market is often a cross-border market, and aircraft owners are keen to preserve the confidentiality that is necessary when you hold an asset as exposed as a business jet. It's a very closed world, and one that isn't specifically regulated. The flip side is that this environment almost completely escapes any oversight by public authorities, which makes it an ideal breeding ground for abuses that seem to be constantly increasing. Several market players have confirmed this in recent months: more and more aircraft brokers are taking advantage of the situation to collect illicit commissions from their customers through so-called "back-to-back" structures. Many of them do not uphold the standards of integrity, transparency, and ethics that are essential for protecting their customers' interests. Many brokers haven't been trained for this demanding job. Basically, it's the law of the jungle. And it is becoming increasingly harder to navigate.

## You mentioned "back-to-back." Not many people will be familiar with this term.

Everyone who specializes in aviation transactions knows about back-to-back, or B2B, and some have even become experts on the matter. But most other people – and especially the victims of B2B, the sellers and buyers of aircraft – are in the dark. It's not their fault: B2B is a secretive underworld, as a standard Google search will show. A few mentions in 2018, eight years after the publication of an NBAA booklet on the subject. Nothing about B2B's in those 8 years and for good reason: B2B is the dark side of the ▶



FLIGHT DECK







► industry. Most B2B structures are intended either to scam the seller or the buyer of an aircraft, or to do something illegal. Those who profit from such behaviour obviously have no interest in unveiling it. Everyone else either doesn't know about it or doesn't know how to get rid of it.

#### **So what exactly is a B2B structure?**

A B2B is a transaction for the sale and purchase of an aircraft, where, usually a broker uses an intermediary company to “buy” the aircraft from its owner and “resell” it almost instantly to its actual buyer. As a result, the ordinary and direct contractual relationship between the actual seller and the actual buyer of the aircraft doesn't exist in a B2B transaction, as it is replaced by a dual contractual relationship. First, an initial sales contract between the actual seller of the aircraft and the intermediary company, acting as a “straw-man buyer.” Then a second identical sales contract between the intermediary company acting as “straw-

man seller” and the aircraft's actual buyer. The use of such a structure may be justified in some very specific cases, but the problem is that, instead of being exceptions, these supposedly beneficial structures have now become generalized in various places around the world – in more than 50% of cases according to some sources – and often, for the wrong reasons. These B2Bs expose the seller and buyer to risks that are unacceptable to them and our industry.

#### **How do you distinguish between good and bad B2Bs?**

A B2B can be justified alongside trade-ins or in the acquisition of a position on an aircraft. But even in such cases, the use of a dual simultaneous sale system isn't the expected sales structure, even for an aircraft. When you buy a car, I'm not sure that the dealer often signs deeds of sale with mailbox companies. It shouldn't be that different when it comes to planes. To be clear, the use of a B2B structure isn't reprehensible in itself. What's required is that the seller, the buyer, and if necessary, the financing party are transparently informed of the

chain of all parties involved in the transaction: their roles, and their links with the parties. They need to have been informed in detail of the reasons for setting up a B2B and have understood, approved, or neutralized the risks. They should be convinced that the B2B isn't being used to hide an illicit commission or to violate any legal or contractual obligations between the parties or arising from public law. Then yes, in such circumstances, the use of B2Bs can be justified. But you can imagine that in practice, things aren't so transparent.

#### **Does this mean many B2Bs aren't up to standard?**

To be perfectly frank, they're often totally illegal. Let's take a typical example. I'm the owner of a business jet and want to sell it. I don't know anything about the aircraft market, so I hire a broker. We sign a brokerage contract under which I promise to pay him 1% of the sale price of the aircraft if the transaction is successful. Under this

contract – in Swiss law, a mandate agreement – the broker has a duty of loyalty and proper execution of his duties toward me. This implies that he is obliged to safeguard my interests first and foremost. His interests should take second place. So I trust him to manage the sale of my plane. Now, say the broker advises me to put my plane on the market for a price of USD 10 million when he knows full well that he will be able to sell it for USD 10.5 million two days later to a buyer he is about to find or has already found. Say he discretely sets up a B2B to collect the extra USD 500,000 representing the difference between the selling price that I'll receive and the amount he actually received from the buyer. And after all that, imagine he willingly accepts the USD 100,000 brokerage commission I give him in good faith for defending my interests. Wouldn't that be an obvious scam?

**So how can this type of behaviour be dealt with?**

In civil law, this represents a gross violation of the duties of an agent. The represented party is entitled to sue for damages. In Swiss criminal law, it's called fraud or management impropriety, which are crimes. I've just described a "traditional" illicit B2B, but there are other situations. For example, such a structure can be used to circumvent laws or to undermine the economic interests of third parties, which is obviously unacceptable as well.

**Are these offenses prosecuted by the authorities or by the victims themselves?**

The victims are often not even aware that they were deceived. Or they notice it too late, and the money stolen by the intermediary company has already

disappeared, often abroad. Good luck trying to get it back. Meanwhile, public authorities are far too distant from the sector's realities to intervene post facto, once the offense has already been committed. As a result, the thriving B2B business is gaining momentum, and brokers are free to continue their illicit practices in peace. Sellers and buyers believe they are protected by the serious business aviation community, but they are victims of these practices that cause them to lose a lot of money and also expose them to risks they aren't aware of and therefore cannot control.

**What type of risks?**

There are several kinds, and they are found in both illicit B2Bs and legal, but poorly designed, B2Bs. First of all, the seller may not have rights to the deposit if the broker defaults or the deal falls through due to error, as he isn't directly bound by contract to the actual buyer. In the same way, 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. Also, 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. Furthermore, the seller may be breaking embargo laws if the broker did not take the necessary precautions. And last but not least, an increasingly common situation: the buyer and the seller may end up having to pay taxes, such as state sales taxes or VAT, on the transfer of ownership; or having to import the aircraft into a specific country, including payment of customs duties. All because the broker did not or could not, due to the hidden

B2B structure, take the necessary steps to eliminate any fiscal and customs risk. These are concrete risks that should not be taken lightly, and all parties to a transaction should be fully aware of them in order to avoid or neutralize them. That is rarely the case at the moment.

**In your opinion, what sort of regulations would counter these practices?**

Regulation by public authorities isn't feasible and would serve no purpose. Which country or state would be interested in adopting a ▶

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► specific regulatory framework for the brokerage of aircraft? Surely none. Because firstly, there is already a general national legal framework for brokering, and if a country starts to regulate the specific brokerage of aircraft, it would have to regulate all the other specific forms of brokerage as well. And secondly, what's the point of regulating the brokerage of movable property that can so easily fly to other countries that don't have any such laws? Clearly, global regulation is impossible, so control and compliance enforcement likewise is impossible by public authorities, anywhere.

#### **Are business aviation associations powerless?**

Without binding legislative power or power to sanction, they're even worse off. Establishing a code of ethics is a good start, because it gives everyone involved in the sector a guideline to follow. But ethical standards are quickly forgotten, and many brokers are free agents who wouldn't miss out on the opportunity to earn easy money. In view of this, the only solution to counteract illicit B2Bs is to nip them in the bud. This result can be achieved through contractual mechanisms and oversight.

#### **So that's what Clean Aero offers?**

Absolutely. Based on the mechanism for securing the simultaneous transfer of the title from the seller to the buyer and the payment from the buyer to the seller. This system was set up to prevent the title being transferred but not the money, or vice versa, and avoid complicated and endless lawsuits. However, in view of the illegal practices we've discussed, it would be justified to extend this protection mechanism to all the sums paid by the actual buyer with regards to the aircraft's

purchase price, in order to ensure none of them are diverted along the way. Clean Aero offers both the seller and the buyer a two-tier protection system that precludes the existence of a hidden B2B and thus avoids exposing the parties to risks without their knowledge. Clean Aero also offers this service to remove both parties' exposure to risks in the context of completely legal B2Bs. In view of the constantly increasing number of cases of abuse, it's time for our industry to strengthen the protection of all stakeholders and adopt the necessary standards to that end. That is what Clean Aero intends to work toward.

#### **Who would take on the role of adopting such standards?**

It would have to be the broker associations, because it's members of that profession who are causing the problem, and it's their duty to self-regulate it. But today, only the IADA seems to really exist and be active – for example, by launching a campaign for ethical aircraft transactions in the spring of 2018. Its goal is to standardize the contractual transactions in the medium term and improve its training and accreditation system for the brokers and dealers who are its members. With respect to contractual documents – including the LOI, sales and brokerage contracts, etc. – a good step would be to create basic models with sufficient detail to enable the recipients, who aren't specialists, to be aware of all the elements they need to consider when it comes to a transaction. However, standardization can't go further, because each transaction has its own specificities and problems to solve, often involving several jurisdictions at once, so standardized documents can only be of limited

use to the parties involved. In order to protect their interests, the parties will need to depend on specialists to adapt these documents to the reality and requirements of their case. Standardizing up to a certain point is useful and important. But claiming that standardized documents can be used as is, would be deceptive.

#### **What about training and the accreditation system?**

Training is always a good thing. And even if IADA is only planning it

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for its members, nothing prevents other brokers or associations from doing the same. Regarding the accreditation of brokers, a well-considered audit system is also always welcome, but it must be outsourced to be credible and follow the standards in our industry. That said, let's not fool ourselves: even the best auditing system won't prevent or uncover all the illicit B2Bs that are so easily concealable to auditors who have no police investigation powers. On a related topic, it doesn't seem necessary to specifically regulate dealers, who buy a plane in their own name and with their own money in order to sell it later at a better price to a third party. Firstly, a dealer's business model doesn't represent a particular risk for the owner of an aircraft. And secondly, there are no companies active in the business aviation transaction market that are only dealers, as the financial risk related to the acquisition and uncertain resale of an aircraft is far too high. At most, companies are both dealers and brokers who offer primarily brokerage services and advice on sales and acquisition. These are the services that need to be better policed.

#### **Should there be a difference between dealers and dealer-brokers?**

Yes, absolutely. A dealer can offer an aircraft owner a purchase price to take or leave, subject of course to the results of the technical inspection of the aircraft. In this sales contract, the buyer has offered and paid a certain price to the seller and is then free to resell the item at whatever price he wants, without prejudice to the seller who is not at all involved in the transaction. It's a different story if the dealer-broker, who intends to buy the aircraft with his own funds for subsequent resale, also offers the owner additional services. Like price determination, contracts, technical support, etc. As noted above, this relationship of trust from principal to agent forces the dealer-broker to protect the owner's interests. This implies that the dealer-broker cannot take advantage of the owner's lack of knowledge about the specificities and practices of the market to advise them in bad faith to sell the plane for a price which is too low that then ensures an oversized resale profit. In such a relationship, the dealer-broker must put their cards on the table;

otherwise he's violating his contractual obligations to the seller.

#### **Everything revolves around the "fair" price of an aircraft...**

And what constitutes a "fair" brokerage commission, which is where the problem lies today. Prices in the second-hand aircraft market are polluted by B2Bs, which result in uncertainty regarding the "fair price" and facilitate further abuses. As for the rate of brokerage commissions, nothing is settled or even recommended. It's the law of the jungle, and the fact that owners of business jets are generally wealthy doesn't justify taking advantage of their financial situation and not improving the situation. Eliminating looting through illicit B2Bs should be a priority, and that can only be achieved through the adoption of contractual protection mechanisms. The broker community should also take a hard look at its compensation model and propose solutions, especially when brokers are exposed to the risk of not being paid by their clients.

Brokers should receive fair compensation for the added value that they bring, not necessarily according to the value of the aircraft. Pay ranges should be determined. Almost everything remains to be done, and it is essential to begin these projects quickly to restore the market's trust in brokers, which is currently tarnished. 🌐

