Buying your share from another owner

Here's what to watch out for–and why this approach might save you money

The vast majority of fractional aircraft share buyers who purchase "pre-owned shares" obtain them directly from the providers, not the shares' previous owners. The buyers enter into new contracts with the providers, rather than assuming former owners' agreements.

Somewhat surprisingly, a secondary market in owner-to-owner sales of fractional shares hasn't really developed. Indeed, some providers recently have changed their contracts to restrict the ability of owners to sell their shares, other than back to the company. This benefits the providers because they can charge hefty brokerage fees to sellers; they can buy shares back at a discount (since most owners choose not to contest the low valuations providers offer) and resell them at a premium; they can get out from under old contracts that probably are less advantageous to them than current ones; and, in general, they can monopolize the market for their shares.

However, under many existing fractional contracts, the owner is relatively free to sell his share to a third party with reasonable restrictions. (For example, the buyer must be creditworthy and must reside in the provider's prime service area.) Although such transactions occur infrequently, they can provide good opportunities for buyers.

The buyer may capture the value of certain concessions and other contract terms. For instance, the contract may include short-leg waivers, peak-travel and upgrade guarantees, ferry-fee waivers and simultaneous-use rights, some or all of which may no longer be available under the provider's program. Also, because escalations in management fees and hourly rates generally are capped at 3.75 percent annually, the buyer who assumes an existing contract may face lesser charges than the provider is assessing under its new contract. There may be new surcharges–such as those relating to pilot salary increases–that do not apply under older contracts. All these factors may combine to offer significantly more value than you will find in a share offered by the provider.

Although, in general, shareholder contracts have become less generous over time, providers have become more generous in some ways. (Prime service areas have been expanding, for example.) If you buy another owner's share, providers generally will honor such benefit upgrades because they apply to all shareholders across the board.

That's not to say there aren't complicating factors. If you're considering buying a fractional share from the owner, it's important that you confirm the contract's business and legal terms. Understand that, for good or ill, you'll be stuck with them; you won't be able to renegotiate with the provider. Determine how long you can use the share before the provider can force you to sell it back. Also, confirm the number of flight hours remaining under the contract. And determine whether you need the provider's approval to complete the purchase and, if so, the process for obtaining that approval.

You will be assuming the seller's obligations under the contracts, so confirm that he isn't in default and all payments are current. Also, determine whether the seller financed the share and, if so, make sure that any liens will be satisfied and released as part of the closing.

After you've done all this, you must determine the value of the aircraft and the other benefits of the contract in order to calculate a fair price for the share. This will be difficult because unlike in direct sales by the provider, there is no set purchase price. Nor is there a history of comparable sales to guide you. Each share is somewhat different and currently no clearinghouse of information exists on such sales.

Purchasing a fractional share directly from the owner may offer substantial savings and better terms than you will find buying direct from the provider. It's a bit more complicated, but if you're prepared to do the necessary due diligence, you may find that you don't need the provider sitting in the middle seat. ■

What's in it for the seller?

Why should owners get involved in complicated third-party sales when providers are ready, willing and able to buy their shares? Simple. Sellers may end up with more cash in their pockets.

Providers charge sellers a hefty brokerage fee, generally anywhere from 5 to 12 percent. There's no such charge in a third-party sale.

The concessions and below-market management fees and hourly rate charges that shares may hold are of no value to the provider, so their offers won't reflect them.

From a seller's perspective, the main thing to make sure of is that you're not on the hook if the buyer defaults on its obligations to the provider after the sale. Try to get full release from the provider and an indemnity from the new owner. Confirm that the new owner is substituted on all documents, including the title to the aircraft.

With the right protections in place, owner-to-owner sales may benefit sellers as well as buyers. *–J.B.*

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