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## FAA ISSUES AIRCRAFT LEASING GUIDANCE

In February 2016, the FAA, for the first time in nearly forty years, replaced its Advisory Circular on aircraft leasing. (AC91-37B (February 10, 2016), superseding and replacing AC91-37A (January 16, 1978).) The new guidance expresses the FAA's continuing concern over arrangements where operational control is retained by the aircraft lessor, and that thus constitute de facto uncertificated air charter. Also included are some noteworthy additions, such as (a) a statement that the operational control concerns apply to aircraft of all sizes (even though the specific subject of the Advisory Circular relates only to large aircraft, exceeding 12,500 pounds gross take-off weight), and (b) the introduction of seven factors that the FAA encourages lessors and lessees to examine in clarifying which party truly operates the aircraft.

### BACKGROUND

Among the FAA's most abiding and profound concerns is that of unlawful commercial carriage. The right to carry passengers or property in exchange for compensation is allowed (apart from certain narrow exceptions) only to those few operators that hold air carrier operating certificates. The regulatory air-carrier authorization process is intended, among other things, to ensure as to each carrier: the skill and proficiency of their pilots and crew; the quality and maintenance of their aircraft; the suitability of their resources to their missions; their adherence to strict operational limitations; and the integrity of their business practices. In AC91-37B, the FAA expresses the need for potential passengers/lessees to be attuned to whether the arrangements they enter into provide for them to (a) receive air transportation, or (b) become the custodian of the aircraft, which they then use to transport themselves. The FAA cautions against aircraft owners who may imply an arrangement in the first category, while actually offering only the second:

[T]here are aviation companies certificated to offer charter air service; however, there are also dozens of other companies or individuals who have no air carrier or operating certificate but who are willing to violate the law by evading safety requirements. Some evade air carrier certification by using devious leasing schemes intended to appear legitimate. Before you sign for a charter air service, ask to see their air carrier operating certificate issued by the FAA. Additionally, before entering into an aircraft lease, ensure you understand and are willing to accept your responsibilities for compliance with air safety regulations.

Leases that convey to lessees the right to use an aircraft as a piece of equipment (and, thus, include a transfer of the rights and responsibilities to operate the aircraft) are not only acceptable to the FAA, but widespread throughout the industry. In 2011, the FAA Office of Chief Counsel wrote that:

In general, the FAA recognizes two general types of leases—wet leases and dry leases. A dry lease of an aircraft is one in which the owner provides the aircraft and the lessee supplies his or her own flight crew and retains operational control of the flight. Under a dry lease, operational control resides with the lessee, and the lessee is permitted to operate the aircraft in furtherance of its business under



part 91. In contrast, under a wet lease, the lessor provides both the aircraft and the crew and retains operational control of the flight. Generally speaking, under a wet-lease arrangement, the lessor of the aircraft is considered to be the operator of the aircraft and may be required to hold an operating certificate because it is providing air transportation. (August 11, 2011 ruling to Eric L. Johnson (internal citations omitted).)

Lessees in a dry (i.e., uncrewed) leasing arrangement must be aware of “their responsibilities for compliance with regulations.” In cases where they are not, their “unknowing assumption of responsibility creates a serious problem in air safety and may involve legal liabilities.” AC91-37B.

The FAA's concern over unauthorized commercial carriage relates to aircraft leasing insofar as it is possible for a “devious leasing scheme” to purport to simply rent the aircraft to the lessee while, in fact, the lessor retains operational control and is involved in unlawful air carriage.

The Department of Transportation enacted the Truth in Leasing (“TIL”) Regulation (FAR 91.23) to address its concern over arrangements that either (a) transfer operational responsibilities to lessees who are unaware of, unprepared for, and unable to satisfy those obligations, or (b) retain operational control with lessors engaged in unlawful air carriage. The TIL regulation, which imposes requirements on leases of large aircraft (over 12,500 GTOW), is AC91-37B's nominal subject. However, the Advisory Circular's recent revision adds a statement that “Operational control is not dependent on the size or the number of aircraft operated; it is instead a matter of legal responsibility.” This new statement emphasizes that the same analysis of whether unlawful charter is being provided applies regardless of aircraft size, and is not restricted to aircraft governed by Truth in Leasing under FAR 91.23.

Briefly summarized, the TIL rule requires for large aircraft that: (a) leases be in writing and signed by both parties; (b) leases include a mandated statement of responsibilities directly above the signature block; (c) lease copies be kept onboard; (d) lease copies be sent to the FAA within 24 hours of execution; and (e) the FSDO nearest to the aircraft's first flight under the lease be notified of that first flight at least 48 hours prior to departure.

## **DETERMINING OPERATIONAL CONTROL**

The determination whether a lessor is providing air transportation (as opposed to simply leasing equipment) is based on all of the facts and circumstances. One useful addition in the new Advisory Circular, however, is a list of seven factors that aid the determination:

1. Who makes the decision to assign crewmembers and aircraft; accept flight requests; and initiate, conduct, and terminate flights?
2. For whom do the pilots work as direct employees or agents?
3. Who is maintaining the aircraft and where is it maintained?
4. Prior to departure, who ensures the flight, aircraft, and crew comply with regulations?
5. Who decides when/where maintenance is accomplished, and who directly pays for maintenance?
6. Who determines weather/fuel requirements, and who directly pays for the fuel?
7. Who directly pays for the airport fees, parking/hangar costs, food service, and/or rental cars?

The new Advisory Circular indicates how these factors will be applied, stating that “If [the lessee is] not responsible for any or all of the[se] criteria [], then [it does] not have operational control and the aircraft is a wet lease requiring full compliance with the provisions of part 135 for air charter operations to carry passengers for hire.” Conversely, “If [the lessee is] responsible for any of the[se] criteria [], then [it has] some operational control and should clarify [its] leasing arrangements accordingly or [it] will be held accountable for violations of 14 CFR for operations of the aircraft.”

In evaluating the operational control question, the new Advisory Circular makes clear that “how the lease is named” is not controlling, and encourages lessees to be wary of “evasively worded” arrangements. The FAA's inquiry can extend to the actual practice and routine of the parties:

You should note that operational control may remain with the lessor even though the lease is characterized as a dry lease and expressly states that items such as flight following, dispatch, communications, weather and fueling are to be performed by the lessee. Therefore, in some instances it may be necessary to look at the actual manner in which the operations are conducted to determine which party on the lease has operational control. AC91-37B.

Further, the FAA reasserts its position that “if a person leases an aircraft to another and also provides flight crew, fuel, and maintenance, the lessor of the aircraft is the operator. If the lessor makes a charge for the aircraft and services,” beyond certain narrow exceptions, the flight becomes commercial carriage, and is subject to regulation as such. AC91-37B. Of the indicia of operational control, the most important is the flight crew. As stated by FAA Chief Counsel in 2009, “if an aircraft and pilot are provided to another as a package, the operations would be considered transportation of people or property for compensation or hire, and a part 119 operating certificate would be required.” (July 31, 2009 letter to George C. Douglas, Jr.)

The FAA defines illicit compensation that an aircraft operator might receive to include “anything of value,” not requiring “a profit, profit motive, or the actual payment of funds.” (Feb. 25, 2010 Chief Counsel letter to James Wagner.) Examples found to constitute compensation include: (a) reimbursement of expenses; (b) the ability of the pilot to acquire flight hours at another's expense; (c) capital contributions by a company owner; (d) payment in terms of barter (e.g., payment for dinner); (e) receipt of publicity; and, of course, (f) any actual cash or in-kind payment.

Thus, under the applicable regulatory scheme, parties intending to engage in aircraft dry leasing must ensure that the lessee takes on genuine responsibility for the aircraft, as reflected not only in the text of the negotiated agreement, but also by the conduct of the parties. Failure to delineate this may render the operations unlawful.

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This article provides an introduction to a complex, and often ambiguous, area of law. Knowledgeable people may disagree as to outcomes in particular cases. Always consult with your advisor.

