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THE HAZARDS OF OPERATING FLIGHT DEPARTMENT COMPANIES

I. Scope of the Inquiry.

Flight department companies are routinely employed as subsidiaries of parent corporations or holding companies. These flight department companies, financed by the parent corporations or holding companies, own, operate and maintain aircraft, employ the flight crew, and provide air transportation to employees and guests of parent and subsidiary corporations. These operations are typically conducted under Part 91 of the Federal Aviation Regulations (FARs) without an air carrier certificate. Because flight department companies represent a major enterprise for profit and their income is not incidental to any other source of income, the Federal Aviation Administration (FAA) takes the view that operation of these companies violates the FARs. This article will examine the exposure to corporations employing flight department companies.

II. Subpart F of the Federal Aviation Regulations.

Subpart F of the FARs is found at 14 CFR §91.501 which deals with the operation of large and turbine powered multi engine airplanes. While many jet and turboprop aircraft may not be "large aircraft" (weighing more than 12,500 pounds), the operator of such aircraft may avail itself of an exemption to operate under Subpart F by joining the National Business Aircraft Association (NBAA).[2]

We begin our analysis with 14 CFR §1.1 which provides:

> Commercial operator means a person who, for compensation or hire, engages in the carriage by aircraft in air commerce of persons or property, other than as an air carrier or foreign air carrier under the authority of Part 375 of this title. Where it is doubtful that an operation is for "compensation or hire," the test applied is whether the carriage by air is merely incidental to the person's other business or is, in itself, a major enterprise for profit.

Parent corporations and holding companies that have created and funded flight department companies, have invested substantial sums of money in the acquisition of aircraft, funded the creation of the flight department company, acquired hangar space and committed to funding same, obtained aircraft insurance, financed the training of flight crews and incurred a host of expenses in bringing one or more aircraft on line to service the transportation needs of the company. Risk adverse lawyers and accountants understandably oppose having the assets of the flight department owned by the parent corporation or holding company. Because they do not want to place at risk the major economic engine that drives the business forward out of concern for potential exposure from an air

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[2] See FAA Exemption Number 7897 that permits aircraft weighing less than 12,500 pounds to be operated under Subpart F. See also FlightWatch Vol. 148, September 2004, *Exemption Number 7897 Granted to the NBAA* on author's website: www.alanarmstronglaw.com/FlightWatch.

disaster, they counsel clients to set up flight department companies in the belief that this is authorized by the Federal Aviation Regulations. Such advice is based upon a misreading of the regulations and a misunderstanding of Subpart F of the FARs.

The operation of large, turbine powered multi engine aircraft and aircraft operating under NBAA Exemption No. 7897 are specified in 14 CFR §91.501(b). Operations may be conducted without complying with Parts 121 and 135 in relation to: (1) ferry or training flights;[3] (2) aerial work operations such as aerial photography and pipeline patrol;[4] (3) demonstration flights;[5] (4) flights conducted for personal transportation;[6] (5) carriage of officials, employees, guests and property of a company or its parents or subsidiaries (other than transportation by air);[7] (6) flights operated under time sharing, interchange or joint ownership agreements;[8] (7) carriage of property in the furtherance of a business (other than transportation by air);[9] (8) carriage of athletic teams, sports groups and choral groups if no charge or assessment is made for the carriage;[10] and (9) carriage of persons aboard an aircraft for the purpose of selling them land, goods, or property, including franchises or distributorships (other than transportation by air).[11]

The regulation relied upon by corporations in setting up their flight department companies is typically 14 CFR §91.501(b)(5) which permits:

> Carriage of officials, employees, guests, and property of a company on an airplane operated by that company, or by the parent of a subsidiary of the company or a subsidiary of the parent, when the carriage is within the scope of, and incident to, the business of the company (other than transportation by air) and no charge, assessment or fee is made for the carriage in excess of the cost of owning, operating, and maintaining the airplane, except that no charge of any kind may be made for the carriage of a guest of a company, when the carriage is not within the scope of, and incidental to, the business of that company.

In creating flight department companies, the companies and their counsel frequently overlook the phrase "other than transportation by air" contained in §91.501(b)(5). Understanding that language is critical to our analysis; and it is essential to understanding why the FAA views flight department companies to generally violate the provisions of the Federal Aviation Regulations.

III. The Bell South Flight Department Illustration.

In a letter from W. H. Williams, Assistant Vice President, Corporate Aviation, Bell South Telecommunications, Inc. dated February 13, 1997, it was related to the FAA that Bell South Corporation ("Bell South") had established a wholly owned subsidiary known as Bell South Corporate Aviation and Travel Services, Inc. ("BCAT"). BCAT was employed to provide air transportation for officials, employees, guests and property of Bell South, and its affiliates in furtherance of Bell South's telecommunications business.[12] According to Mr. Williams' letter, Bell South and its other subsidiaries are assessed a fee by BCAT that is proportionately related to the amount of time used by the various Bell South entities. The amount of the fee is based upon and does not exceed the total cost of owning, operating and maintaining the aircraft."[13] On an annual basis, the

[3] 14 CFR §91.501(b)(1).
[4] 14 CFR §91.501(b)(2).
[5] 14 CFR §91.501(b)(3).
[6] 14 CFR §91.501(b)(4).
[7] 14 CFR §91.501(b)(5).
[8] 14 CFR §91.501(b)(6).
[9] 14 CFR §91.501(b)(7).
[10] 14 CFR §91.501(b)(8).
[11] 14 CFR §91.501(b)(9).
[12] See letter from W. H. Williams, Assistant Vice President, Corporate Aviation, Bell South Telecommunications, Inc., to Francis DeJoseph, Federal Aviation Administration, February 13, 1997 ("the Bell South Letter").
[13] Id.

the cost of the BCAT corporate aircraft operation was projected to be $11.4 million.[14] With regard to Bell South and its flight department company, BCAT, William G. Nelms, Esq., an attorney in the office of the Assistant Chief Counsel of the FAA, Southern Region, wrote Mr. Williams on April 18, 1997 noting: "...the provision of air transportation services to other corporate entities, including the provision of both aircraft and piloting services, is subject to FAA regulation as an air carrier. BCAT has 'operational control' of flights it conducts for the other corporate entities, in that BCAT is responsible for aircraft maintenance they had created was not acceptable to the FAA noting:

> As you know, 14 CFR Parts 119 and 135 (Parts 121 and 125 for large aircraft) contain provisions that are more demanding than Part 91 safety rules. Those air carrier certification and operational rules apply when someone engages in transporting people or property from one point to another for compensation or hire. Under the circumstances you describe in your letter, BCAT aircraft operations are subject to those air carrier regulations.

IV. The FAA Interpretation on Flight Department Companies Issued by Donald P. Byrne, Esq.

On August 8, 1989, Donald P. Byrne, Esq., Acting Assistant Chief Counsel for the FAA, dispatched a letter to John Craig Weller, Esq. responding to Weller's letter of April 10, 1989. In Weller's letter, he advised Byrne that many corporations had decided to place their flight departments into separate companies. Further, Weller maintained that the flight department companies cannot be construed to be commercial operators and the structure satisfied what was then codified as 14 CFR §91.181.[15]

Byrne concluded that the flight department companies Weller described violated the Federal Aviation Regulations because, "Section 91.181(b)(5)[16] allows the carriage of company officials, employees, and guests on a company aircraft provided the carriage is – 'incidental' – to the company's business. Clearly, when the redactors adopted the concept of 'incidental' they contemplated that the company's aviation activities would be secondary to the overall business of the company."

Byrne went on to drive the point home declaring as follows:

> The business structure you describe, viewed as a whole, does not fit the literal language of FAR 91.181(b)(5), which does not provide for "flight department companies." Additionally, it is clear that these "flight department companies" are organized solely for the purpose of owning and operating aircraft. If so, they do not fall within the coverage of §91.181 since that regulation requires that the transportation by air be "incidental" to the company's business. In or those "flight department companies" to conduct the operations you describe, they must obtain an appropriate operating certificate.[17]

[14] *Id.*
[15] 14 CFR §91.501 was previously codified as 14 CFR §91.181 before Part 91 was recodified.
[16] Presently codified as 14 CFR §91.501(b)(5).
[17] Byrne's letter to Weller of August 8, 1999 is available as FAA Interpretation 1989-22, *Federal Aviation Decisions* published by Thomson-West.

V. The Civil Penalty Exposure for Engaging in Air Transportation Without a Certificate of Authority

49 USC §46301(a)(1) authorizes the FAA to recover a civil penalty of $25,000.00 per violation or $1,100.00 per violation if the person is an individual or small business concern. According to 13 CFR §121.201, a business concern is considered to be small in Subsector 481, Air Transportation, if it involves non-scheduled chartered air transportation and has less than 1,500 employees. However, even if the business entity is viewed as a small business concern, the civil penalties can be substantial.

In the matter of *Air Solutions, LLC and Air Solutions Group, Inc.,* 2009 WL 8502643 (FAA), Acting Administrator Robert A. Sturgel reversed an Initial Decision by Judge Isaac D. Benkin and reinstated a civil penalty of $44,000.00 for two flights. The flights were ostensibly demonstration flights. But the FAA found that they were actually the provision of transportation by air for flights to Harrah's Casino in Atlantic City, New Jersey and that it was, therefore, a chartered flight. Demonstrating no lack of imagination, the FAA cited the respondent with 18 violations of the Federal Aviation Regulations.[18] While Judge Benkin found that the FAA had brought the action against the wrong entity, the Administrator in reversing the judge, disagreed and reinstated a civil penalty of $44,000.00 on the theory that there were two violations per flight, to wit: (1) operating without an air carrier certificate on two flights, and (2) operating with unqualified crew members on two fights.[19]

VI. Conclusion

While there is a simplistic attraction to establishing a flight department company, the sole purchase of which is to provide air transportation to parent and affiliated corporations, such a course may lead to substantial economic hazards to the operators of the flights. This article has been written to give pilots and aircraft operatives an appreciation for the hazards presented in employment flight department companies. There is no substitute for obtaining informed and competent judgment in properly structuring corporate flight departments.

A more expansive analysis of the underpinnings and legal considerations that apply in actions brought by the FAA for commercial air transportation provided without an air carrier certificate of authority may be found in an earlier article written by the author related to this topic.[20]

[18] 14 CFR §§119.33(a)(2) [operating as a direct air carrier without a certificate]; 119.33(a)(3) [operating without operation specifications]; 119.5(g) [operating as a direct air carrier without or in violation of a certificate and operation specifications]; 119.5(i) [operation without economic authority]; 135.21(a) [operating without a manual]; 135.244(a) [using a pilot in command who lacks experience]; 135.293(a) [using a pilot who has not passed a test]; 135.297(a) [using a pilot who has not passed an instrument proficiency check]; 135.299(a) [using a pilot who has not passed a flight check]; 135.3(a)(1) [not complying with 14 CFR Part 135]; 135.323(a)(1) [not having a training program]; 135.327(a) [not having training program curricula]; 135.341(a) [not having an approved pilot training program]; 135.343 [using a crew member who lacks recurrent training]; 135.351(a) not ensuring that crew members receive recurrent training]; 135.63(a) [not keeping required information]; 135.77 [not listing in the manual the identity of each person authorized to exercise operational control]; and 91.13(a) [operating an aircraft in a careless or reckless manner].

[19] Civil Penalty Decision 2009-1, *Federal Aviation Decisions*, Thomson Reuters/West, 4/2009 MAT No. 40715772. The Administrator's civil penalty decisions, along with indices of the decisions, the rules of practice and other information may be found at: www.faa.gov/about/office_org/headquarters_offices/age/pol_adjudication/AGC400/Civil_Penalty. The Decisions are available through LEXIS (TRANS Library) and WestLaw (FTRAN – FAA Database). See 2009 WL 8502643 (FAA Docket No. CP-05EA0012, DMS No. FAA-2005-2162-29 (January 12, 2009).

[20] Alan Armstrong, *Navigating in the Zone of Confusion – Reflections on Illegal Air Taxi Operations,"* 21 Transp. L.J. 329 (1993).

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