SPECIAL SECTION: **CHARTER, JET CARDS, FLYING CLUBS, AND FRACTIONAL SHARES**

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Robert Herjavec

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We talked with two longtime consultants about how they help clients get the most for their bizav dollar.

by James Wynbrandt

ON YOUR SIDE

FractionalLaw's Daniel Herr


COURTESY OF DANIEL HERR

Asked in 2002 to review NetJets invoices for a friend's parents, Daniel Herr discovered numerous overcharges and questionable fees. "I wound up saving them a significant chunk of money," he recalled.

Sensing an opportunity, the former NetJets pilot launched a consultancy for fractional shareowners. However, "It became clear that if I really wanted to help my clients, I needed to be there when the contracts were written. So I signed up for law school." In 2005, juris doctorate in hand, Herr "morphed the consulting business into FractionalLaw," which he has operated as a sole practitioner since.

Friendly, soft spoken, and precise with his words, Herr met with us at Lehigh Valley International Airport in Allentown, Pennsylvania, where he bases his King Air 350.

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Fractional Law's Daniel Herr

What do you do for clients?

I spend only about a third of my time on the legal aspects—contracts, the liability associated with fractional ownership, insurance, the structure of ownership, tax issues, depreciation, and personal use.

The rest is the same consulting I did when I started—residual-value projections, finding the best plane for the budget. For clients with vacation homes in Colorado, the single-engine climb gradient of the airplane is an issue, and you have to dig relatively deep into the weeds of the performance manuals. Some clients charter for supplemental lift when they're short on fractional hours, so I help with that.

Who owns a fractional share today?

People who find value in the consistency, convenience, and safety of the fractional industry. There seems to be a misconception that fractional owners are idiots who don't know they can save a lot of money by buying a plane or jet card, but that's largely false. They know shares are a premium product and they're willing to pay for it. Despite what the industry says about fractional being a stepping stone to whole-aircraft ownership, I've had only one or two clients go from fractional to whole ownership.

What percentage of fractional owners seek professional representation?

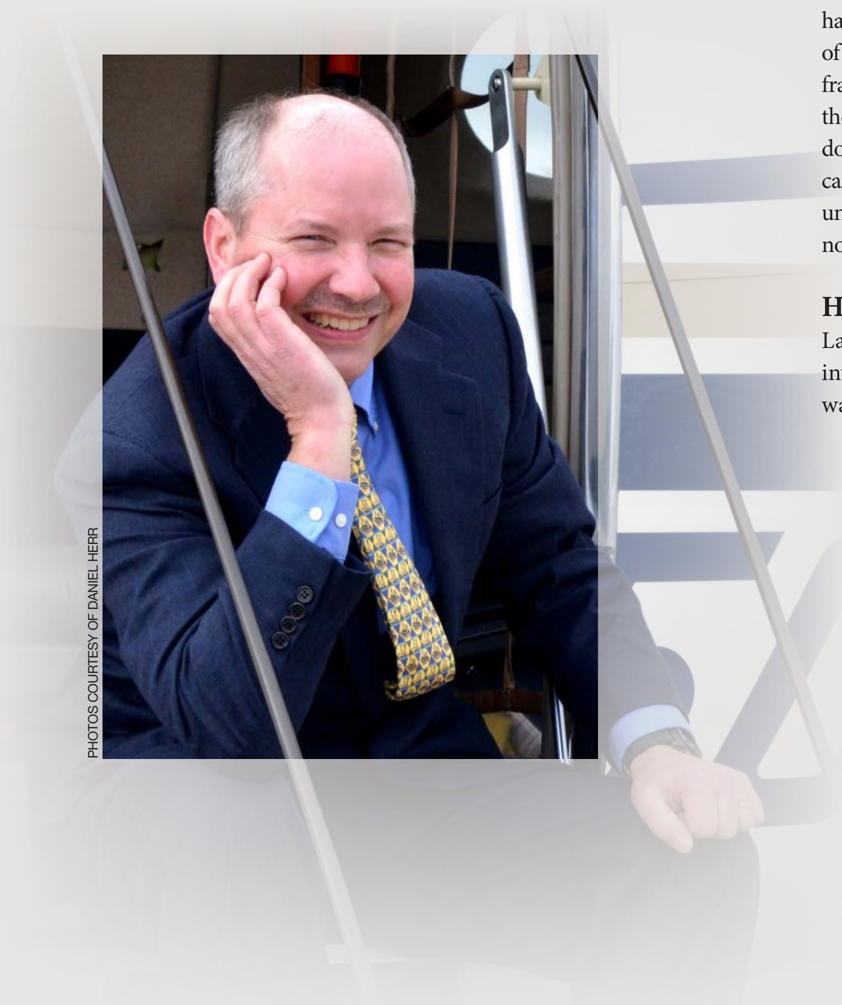
Most don't. My clients tend to be more cautious, more detail oriented, more involved, and maybe more business savvy. Most owners don't realize their name is on the FAA registry as the aircraft operator under Part 91 Subpart K, and they have just as much liability as a whole owner—maybe more.

What benefits could fractional owners be missing without representation?

They may not be getting the right airplane or the right program for their mission; and they may not realize the impact their own operational needs or quirks have on the program costs. A particular short leg they do, or a particular series of flights they make on a regular basis may be treated very unfavorably in the fractional boilerplate contract, but you might be able to get an exemption. And there are always variables, such as length of the contract term, special upgrade or downgrade ratios, short-leg waivers, and flexibility on the number of hours that can be used each year. Without help from someone who knows the industry and understands the contract and what's possible to be tweaked, people probably are not taking full advantage of their fractional program.

How do you charge for your services?

Largely on an hourly basis, at $400 per hour. When I started, I billed invoice auditing on a one-third [of recovered charges] contingency. That was very profitable in the early years and is very unprofitable now. The



PHOTOS COURTESY OF DANIEL HERR

"They may not be getting the right airplane or the right program for their mission; and they may not realize the impact their own operational needs or quirks have on the program costs."

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computer systems have more controls in place; there are not the systemic errors I used to see.

The time needed to review and negotiate a fractional contract is widely variable. A boilerplate contract can go quickly. In other scenarios, the cost of the aviation or business analysis is two or three times the legal fee. I'll talk to new clients and find out which category they're in and give them a ballpark. Even a 50-hour fractional share for a light jet, if you bake in all the expenses, costs at least $7,000 an hour, so it doesn't take much on that budget to find some tweak that pays for my legal bill several times over.

Do you foresee additional players joining the fractional space?

The ferry costs and operating costs are through the roof until you achieve economies of scale, and that takes a lot of investment. I don't see any rational business case for investing the capital to scale up a fractional program when the profitability of the fractional industry has historically been pretty lousy.

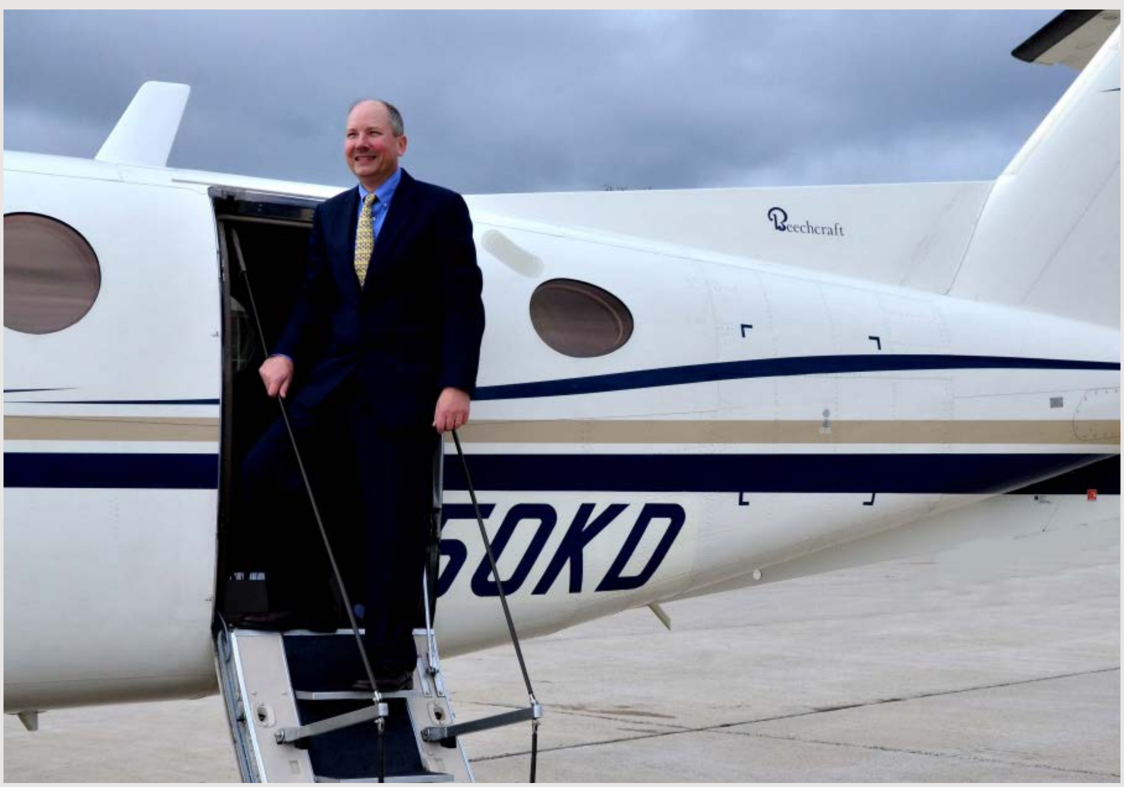
What has changed in the fractional arena since the 2008 financial collapse shook the industry?

In 2009 and 2010, I would get phone calls from clients saying, "Free catering isn't what it used to be," or, "The standard champagne isn't what it used to be." While my role is to promote my clients' interests, my advice was, "The industry has lost a lot of money. You will not be treated well on much bigger issues if the industry continues to lose money, so this is your new reality."

Today I see fractional owners accorded less and less respect, and getting closer to being treated like glorified cardholders. The industry was always leery of giving too much pride of ownership. I think they didn't want to tie owners to a particular tail number. I can see the rationale for that. The owner says, "Oh, my airplane has a new interior, and I haven't flown it." But it's gotten to where the purchase of the asset is looked at as the entrance fee to join the club, and the owners aren't treated the way a management company would treat an owner. That sense of appreciation for what the owners have put up seems to be fading.

Where does the fractional model go from here?

If the industry continues to believe its customers owe it a certain level of profitability, and the programs focus on setting their rates or selecting aircraft to achieve a certain profitability target rather on operational efficiencies or giving customers products they want, it runs the risk of killing the golden goose. If a certain chunk of the clientele say, "We've been pushed as hard as we can," and goes to less-expensive alternatives, and it gets to the point where the fractionals lose their scale, then it unravels. The customer base is pretty tolerant of paying a hefty premium, but I'd say there's a limit to that, and we don't know where that is. BJT



Daniel Herr

Born: June 13, 1966 (age 52) in Flemington, New Jersey

Position: Founder/principal, FractionalLaw

Education: B.A., economics, Princeton University, 1988; J.D., Rutgers Newark Law School, 2005

Personal: Lives in Murray Hill, New Jersey. Married, two children. Enjoys fixing antique tractors and making ice cream with an antique churn. Owns and flies a Beech King Air 350; has type ratings for Cessna Citation 500 and Fairchild Metro/Merlin.

The interviews with James Butler and Daniel Herr have been edited and condensed.