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Lease Deal Helps Plane Expansion Take Off

By SIMONA COVEL

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William Herp needed several million dollars last year to expand his jet-taxi company. He wanted to buy a fleet of a new kind of small jet -- one that would transport businesspeople visiting clients, like a car service with wings.

With airports overflowing with weary travelers and interest in private planes on the rise, Mr. Herp believed the new jets' speed and access to smaller regional airports would lure small groups of business travelers and families who may have never chartered a plane. Instead of paying by the seat, groups could rent the planes by the hour.

But a new kind of jet for a new kind of business -- banks "would never touch it," says the president and chief executive of Concord, Mass.-based Linear Air, which was founded in 2004.

Lease With a Twist

So he began courting wealthy individuals to help finance his idea. His pitch: Buy the small planes -- classified as very light jets -- and lease them to Linear Air. The buyers would receive income from the lease and a sizable tax benefit from the plane's depreciation, plus the ego boost from saying they own a jet. Linear Air, in turn, would have access to the planes without taking on high-interest loans. And the planes' owners would likely become repeat paying customers.

While most small companies don't need to buy \$1.7 million jets, Linear Air's solution, a twist on a sale-leaseback arrangement, could work for entrepreneurs who need capital but don't want to sell equity or take on debt.

Leasing, says Murray Low, an associate professor at Columbia Business School and the director of Columbia's Eugene M. Lang Center for Entrepreneurship, is a form of financing "entrepreneurs probably don't use enough. It's relatively low-cost financing without tying up the rest of the balance sheet."

Mr. Herp, 44, a former chief financial officer of a public company and a recreational pilot, knew the risks associated with buying planes -- expensive products that depreciate quickly. And he knew individuals would be more likely to take this kind of risk than most bankers, because banks prefer to lend to firms with a track record of success. Recent widespread troubles among traditional airlines have rendered bankers even more hesitant to finance a new kind of plane and a new kind of operation.

Linear Air, with 40 employees and \$2.3 million in revenue last year, has six Cessna Caravans -- three leased and three that it owns. But Mr. Herp's dream was a fleet of very light jets. The four-passenger jet is about the same price as the Cessna but able to go farther and nearly twice as fast. Taking the plane, for example, from Boston to Elmira, N.Y., might cost \$3,000. That's within reach for a group of four business travelers and less costly than a traditional charter flight.

The plan wasn't easy. The jets' manufacturer, Albuquerque, N.M., start-up Eclipse Aviation Corp., has run as much as a year behind on delivery, Mr. Herp says. And, the "air taxi" model, where planes rent by the hour, is still unproven.

Eclipse spokesman Andrew Broom says the production delays are due to normal "teething pains" for a start-up manufacturer.

"We learned from the experience buying the Caravans what criteria equipment-finance companies or banks use to lend money," Mr. Herp says, "and we realized quickly Eclipse wasn't going to meet that criteria."

Mr. Herp says several finance companies offered to lend him money to begin the purchases -- but nowhere close to the amount he needed to put down deposits on several planes. Sixty percent of the price of each plane is due six months ahead of its scheduled delivery.

"The pricing was unworkable," he says. Even with the loans, "we'd still have to go out and raise cash" by selling part of the business.

So, Mr. Herp and his investment bankers constructed a leasing arrangement. Under the agreement, wealthy individuals buy a plane from Eclipse and agree to lease it to Linear Air for a period of time. During that time, the owner gets a discount if he or she wants to use the plane and also can usually earn an accelerated depreciation write-off on his or her taxes.

Leasing is common for owners of corporate jets and other transportation equipment, says Rick Schroeder, a partner in commercial finance at law firm Davis Wright Tremaine LLP in Seattle. Typically, the owner of a corporate jet will turn to an aviation-finance company, which will buy the aircraft and lease it back to that original owner. Linear Air's arrangement is a twist on that idea. In Linear's case, the company never owned the jets but persuaded investors to buy them instead. Those investors are then required to lease the jets to Linear.

While most industries don't deal with rapidly-depreciating assets like planes, lots of small companies can avoid taking on loans by leasing some of their equipment, says Prof. Low.

In the case of Linear Air's arrangement, the jet owners are also likely customers. Prof. Low notes that tapping into a potential customer base "is one of the most attractive

sources of financing." When customers help finance the business, "it makes them vested" in the company's success, he says.

A Slow Beginning

Linear Air's plan appears to be working -- slowly. While several hundred potential jet owners have requested more information about the leasing program through the firm's Web site, only two deals have been completed.

That's partly because of manufacturing delays. Eclipse planned to deliver the first jet to Linear Air in August 2006, but now the plane isn't expected to arrive until August or September of this year. Because so much money is due prior to delivery, a handful of potential buyers balked after hearing of the delays. "They take a step back. They say the timing has changed, so there's no reason to do the deal now," Mr. Herp says.

One investor who has completed a deal is Chris Covington, founder of Boston boutique investment-banking firm Covington Associates, which does work for Linear. Mr. Covington, who also is a pilot, says he was attracted by the potential investment income as well as getting priority on flights. As someone who charters planes somewhat regularly -- he's been shuttling his teenage son on college visits -- he expects to reserve the Eclipse jet as often as once a month, especially if he's traveling to a city that's hard to reach directly on a commercial flight.

Mr. Covington's plane was to be delivered in May, but is now expected in September. While the delay is "regrettable," he says, "I want them to get it right."

Write to Simona Covel at: simona.covel@wsj.com