AIN BUSINESS JET TRAVELER

Fractional Jet Ownership

Are fractional shares worth the money?

By Jeff Burger - September 2009

Suze Orman didn't pause before answering when I asked whether she'd ever considered replacing her charter flights with a fractional jet share. "I think they're rip-offs," said the personal-finance guru, in an interview that appeared in our April/May 2009 issue. "First of all, you tie up a quarter-million dollars or whatever for the luxury of having the plane whenever you need it, at supposedly a reduced per-hour cost. Oh, give me a break: They charge you round-trips even if you're going one way."

Then, in case anyone might miss her point, she added, "I wouldn't own a fractional share if my life depended on it."

Well, Orman didn't become famous by soft-pedaling her opinions. But "rip-off" is a strong term, suggesting at the least overpricing and at the most outright fraud. And obviously not everyone agrees with Orman–including, presumably, most of the thousands of people who now own fractional shares in the U.S.

Up-front Expense

So who's right–Orman or the frax fans? She's clearly correct that buying a fractional jet share ties up lots of money–not as much as you'd spend to buy the whole aircraft, but her quarter-million-dollar figure is actually on the low end. At fractional provider NetJets, for example, prices start at around $425,000. That's for a one-sixteenth share–the equivalent of 50 hours a year of flying time–in a Hawker 400XP, which happens to be the model Orman likes to charter. The figure doesn't include monthly management or hourly operational fees, not to mention fuel surcharges, catering, onboard phone bills or a variety of other add-ons.

However, Orman is wrong in saying that fractional providers bill you for round-trips even if you're going one way–in fact, that's what charter operators do. Granted, fractional pricing does take into account the costs of so-called deadhead flights needed to position aircraft for their next revenue-producing trip, but those costs tend to be relatively low. That's because they're spread among all shareowners and because operators of large fleets typically achieve efficiencies that minimize the need for positioning flights.

Still, I haven't heard anybody call fractional flying less expensive than charter; when Orman mentioned a "supposedly reduced per hour cost," she was probably referring to the fact that the hourly operational fee for using a fractional share tends to be less than the hourly charge to charter the same model aircraft. Nevertheless, when you add up all the costs–including those mentioned in the previous paragraph and the substantial portion of the purchase price that you don't recoup when you sell out–you have to conclude that fractional shares represent one of the most expensive ways to fly privately. (For some buyers, tax write-offs can help ease the pain.)

But does that make them overpriced, as Orman suggests? In a word, no. If they were, the providers might well be making a fortune when in fact they've been struggling. Even industry leader NetJets appears to be having a tough time. Owner Berkshire Hathaway has stated that the fractional provider "experienced a significant reduction in revenue" in the last quarter of 2008, the most recent period on which the company has reported. The economy hasn't helped, of course, but one reason it's hard to make money in this business is that while the fractional operators charge hefty fees, they also deliver services that cost a bundle to provide.

Easy Access

To appreciate why, it might help to think in terms of cars. Understandably, you'll pay more per mile (or day or whatever) to rent a car–the rough equivalent of chartering an aircraft–than to buy one. You're paying extra in exchange for not having to commit lots of money, not having to pay for maintenance and other benefits. But what if you were to tell Hertz or Avis that you not only wanted those rental advantages but also wanted a particular make and model to always be available to you on four to six hours' notice, along with a driver; and you wanted the right to upgrade or downgrade to different models as necessary? That's the sort of access that fractional shares offer, plus a promise that you can recoup some of your investment at a fair-market-value price when the deal ends, usually in five years.

Providing aircraft at locations all over the U.S. on short notice is no small trick, nor is it inexpensive. I recall Ed Iacobucci, founder of the now-defunct air-taxi service DayJet, telling me that his biggest startup cost wasn't airplanes, pilot salaries, marketing or any of the other likely suspects. His largest initial expense–which totaled many millions of dollars–was for proprietary software designed to maximize efficiency of aircraft scheduling by making sure that the right ones were in the right cities at the right times.

Fractional operators face similar challenges. I vividly remember my visit to the technology-packed master control room at Flight Options' headquarters in Cleveland, where dozens of flight planners stared intently at their computer monitors and at a movie-theater-screen-sized moving-map display that reported the status of all of the operator's aircraft. Such technology allows fractional providers to comply when you call up and say, "I want 'my' Hawker 800XP in Milwaukee at 10 a.m. tomorrow for a one-way flight to Colorado Springs."

It's also part of what makes fractional shares so expensive. Are they the best choice for all business jet travelers? Of course not. And given Orman's flying needs, she may well be right to avoid them. But that doesn't necessarily mean you'd be smart to do likewise. It all depends on your situation.