What to do with legacy timeshare resorts
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COVER STORY • Many legacy timeshare resorts are struggling to survive: why? And: what can be done?

Vacation Ownership WORLD contacted some of vacation ownership’s leading figures, as well as experts on the subject, and asked them about a much discussed matter within the industry: why are so many legacy timeshare resorts having such a tough time and what can be done about it? Many of these resorts are failing due to an assortment of problems that include: a lack of professional management; a lack of adequate reserves; a resistance by the HOA board of directors to impose an adequate assessment for operating expenses; an underperforming or non-existent external exchange relationship; an aging owner base that no longer uses the resort or that wants to exit ownership but is generally unable to; and, diminishing resort maintenance standards. ARDA president and CEO Howard Nusbaum and senior partner in the Orlando office of Baker & Hostetler and ARDA treasurer and Board member Rob Webb offer their viewpoints on this issue. This is the first of a two-part story; the second article on the subject will appear in the next issue.

The year’s best quotes – 2013 as seen by the vacation ownership industry’s leading executives and experts

How do you describe a year? Vacation Ownership WORLD delved through its 2013 archives and collected the quotes from industry professionals that its editors believe best reflect the events, ideas, and innovations that characterized vacation ownership the past twelve months. The perspectives run the gamut: the significant financial challenges confronting timeshare HOAs, the continued consolidation of the industry, the 10% growth rate top developers attained in 2012, efforts to combat the fraudulent dealings of many Viking Ship LLCs, rapidly declining resale prices and the plusses and minuses re: the state of the vacation ownership industry, new products and vendors, the high performing hospitality brands, a still stagnant North American fractional market – and more.

Diamond Resorts International’s 2013 results all up through year’s first three quarters: show growing revenue, timeshare sales, tours, transactions and transaction prices

“We are very pleased to report a record third quarter, as our unique business model delivered strong operating performance, underscoring the advantages of our asset light, integrated hospitality platform,” stated Diamond Resorts International president and CEO David F. Palmer. “As we look to the remainder of the year and 2014, we remain confident that our hospitality-oriented approach to our business and our value proposition for consumers and HOAs position us to produce strong future results and shareholder value.” Vacation ownership sales through 9/30/2013 were $325.8 million vs. $202.8 million in 2012.

Industry Wrap • A briefing on recent news, developments, and emerging trends in the vacation ownership and related industries

COVER PHOTO • The snow draped The Ridge Resorts at Lake Tahoe in Stateline, NV.

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Timeshare legacy resorts: what is the true situation and what is to be done?

A Q & A with ARDA president and CEO Howard Nusbaum and senior partner in the Orlando office of Baker & Hostetler and ARDA treasurer and Board member Rob Webb.

Q: Define timeshare legacy resort. What is it? What are some of the primary characteristics of timeshare legacy resort?

Nusbaum: I don't believe there is a technical definition; however, to me legacy resorts are older resorts developed under the original "single site resort development model" rather than today's common multi-site club product." In today's model, resorts are working long term with a developer (even when governed by the HOA); and therefore, HOAs always have access to a sales line. In the original legacy model the development company planned, built and sold-out the resort then moved on to the next project; turning over the governance and management operation to the HOA. In the early days neither the developer nor the HOA anticipated the recycling need. Thus legacy resorts don't have a sales arm or function; and they often do not have a club relationship outside of their exchange affiliation.

Legacy timeshare resorts typically offer a “fixed week” - “fixed unit” product, meaning that owners acquire timeshare interests that give them the right to occupy a specific accommodation unit (“fixed unit”) during a specific week of the year (“fixed week”). Currently, the timeshare industry has moved from this “legacy” fixed week product into a “points” product which allows for more flexibility in terms of use. Legacy resorts are typically self-managed or managed by small local or regional management companies that may or may not have an expertise in the management of timeshare properties. The management firm or the resort itself typically sees itself in a local perspective. Consequently, they are not able to easily integrate into the larger international timeshare industry. These resorts are typically isolated and may not even be members of ARDA, ARDA-ROC or other timeshare specific organizations, although they usually offer owners the ability to exchange the use of their units through exchange companies like RCI or II.

Often times the Board members believe their only responsibility is...
to keep maintenance fees as low as possible, thus the resorts do not have the funds to make the necessary improvements to stay competitive with other types of vacation properties. To further complicate the problem, many of these resorts were not purpose built, rather they were converted properties built for some other type of business – i.e. apartment rentals, transient hotel or motel occupancy or wholly owned condominiums. As a result the construction of the property makes it much more difficult to retrofit for contemporary amenities and services which today’s timeshare consumer expects. The biggest problem of all is the legal documents for many legacy resorts as they were drafted when the timeshare industry was in its infancy, thus documents may require a very hard to reach threshold of a 100% vote by the owners to modify the resort structure, programs and services, thus putting these resorts at a disadvantage to make substantive changes that may be required for the long-term viability of the property.

Webb: I would characterize a “legacy resort” as a single site timeshare project of a certain age, say 20 years old or older; one that is not part of a vacation club, of a trust product, or of a branded resort system; one without an active sales program of any kind; and one that may or may not be managed by an employee(s) or a management company in addition to its HOA board of directors. I do not believe that being in financial trouble is a primary characteristic of legacy resorts, although I believe that many of them are in at least some form of financial distress.

Q: How many timeshare legacy resorts are there now? How many owners are we talking about in the U.S.?

Nusbaum: It is difficult to provide an exact count of the number of legacy resorts located in the U.S. In the 2013 State of the U.S. Timeshare Industry report released by the AIF, a total of 1,551 timeshare resorts were identified. Of this number approximately 620 are associated with a family of 10 or more resorts – either developer or management company involvement. Of the remaining 931 resorts, it is estimated that as many as fifty percent of them could be classified as a legacy resort. But keep in mind that the early resorts often had fewer actual units so the number of actual units doesn’t mirror this percentage. To be clear, being a legacy resort does not mean that the resort is in trouble or lacks viability. The questions we are trying to answer via AIF (ARDA’s Foundation) research is how many resorts in this category need help and what type of help do they need. Once we have answered these questions, ARDA and ARDA-ROC can discuss potential solutions to address problems associated with troubled legacy resorts and develop best practices and appropriate legislative support. We are presently employing both legal research as well as census research to answer these questions.

Webb: This is a question best answered by ARDA. My guess would be that 35-40% of the timeshare resorts in the country are legacy resorts. A critical related question is: How many legacy resorts are in financial trouble, and how do we measure “financial trouble?” This is an issue that ARDA is currently considering, and we are also discussing what additional legislative remedies we might support or suggest to help financially troubled legacy resorts either recover or terminate.

One idea we are talking about is proposing an amendment to the U.S. Bankruptcy Code that would allow a qualified financially troubled timeshare HOA to initiate a special liquidation proceeding. This proceeding would give the bankruptcy court jurisdiction over all of the timeshare interests managed by that HOA, for the purpose of ultimately ordering the sale of the entire timeshare property in the event good cause is shown to do so. If the court were to approve the sale of the timeshare property as part of the liquidation of the HOA, each timeshare owner’s rights would be preserved but would be transferred from her timeshare interest title to an equity account in the proportion of her share of the sale proceeds. If she has any outstanding debt secured by her timeshare interest, the lender’s lien would similarly transfer from her title to her equity account. As is typically the case in a bankruptcy sale, the property would be sold free and clear of the timeshare plan and of any related ownership or lien claims, and the sale itself would always be subject to higher and better offers right up until closing. ARDA is currently gathering more information about the size of the legacy resort community, and about the extent of the financial troubles of the segment, before determining whether to pursue this bankruptcy
concept or any other legislative or policy strategy to benefit legacy resorts.

Q: What are the core problems of timeshare legacy resorts? Can they be solved/saved? How? What are the options?

Nusbaum: Legacy Resorts are analogous to people. Some folks at the age of 75 or 80 are highly active, healthy, very engaged in the world and others at the same age are infirmed or have physical or mental issues that make everyday life problematic. Legacy Resorts mirror this same diversity. Some older resorts are well run with robust rental programs, well maintained facilities, an engaged competent board and effective management teams. Conversely, there are others facing high defaults, systemic facility issues and management teams that are not properly trained. Like most things in the world of solutions, one size doesn’t fit all. I know we always want to put bright lines on things, but the world of legacy resorts isn’t that simple.

Fortunately, there are a number of options for many legacy resorts facing challenges. Solutions range from hiring a management company or hiring a management company with expertise in working with legacy resorts, reengaging and educating the board members, developing strong rental programs, to finding ancillary revenue streams and partnering with a sales organization that can help resell inventory that HOA has obtained through either foreclosure or deed back programs.

All of the options begin with an honest appraisal of the present situation and a good consultant or a pro-active board that can guide the resort through the process. The capital light model that many developers have embraced makes for partnership opportunities for resorts with an owner base that is demographically strong, dues paying and/or located in a high demand market.

The ARDA International Foundation (AIF) conducted its first study of HOA controlled resorts in 2010 and updated in 2012. The research revealed that there are marked differences between independent legacy resorts and those where the developer is still present. Some of the known issues are: an aging product; lifecycle changes of long-term owners; challenges in the resale market; and a host of other factors that contribute to increased delinquencies in maintenance fees.

Webb: I would say that the core problems of legacy resorts include some or all of the following: (i) lack of professional management; (ii) lack of adequate reserves; (iii) a resistance by the HOA board of directors to impose an adequate assessment for operating expenses; (iv) an underperforming or non-existent external exchange relationship; (v) an aging owner base that no longer uses the resort or that wants to exit ownership but is generally unable to; and (vi) diminishing resort maintenance standards. These problems are all obviously interrelated and can be solved with some combination of an infusion of new capital; the employment of new management with the resources and expertise to cost-effectively provide necessary (and desired) services; improved communication with owners about the problems, the solutions and the cost /risk associated with the solutions; and an effective resale program that will bring new owners into the resort who will use and enjoy it and who will pay their assessments on time.

Q: What are the main challenges to solving the problems associated with timeshare legacy resorts? Are there certain resorts beyond saving? What characterizes these resorts?

Nusbaum: The challenges are as diverse as the resorts themselves. If we wanted to put them into buckets, I would begin with three major areas: 1) Maintenance fees – issues ranging from the level of defaults to the actual amount of the fee (and whether or not the fee is adequate). Is the annual fee more or less than a rental cost for a comparable week, etc.; 2) Physical condition of the resort, its location and the amenities it offers – how do they stack up in the marketplace? Is there a niche for this product? If it needs improvement is there an ROI on that re-investment?, and; 3) Governance and management. As in every business, success relies upon effective leadership at the top. It starts with examining the effectiveness of the board (if board members think their job is to keep maintenance fees low rather than nurture and sustain the resort, then you have a problem). Is management effective? Additionally, the governing documents matter in terms of percentages for votes to make changes as well as state laws.
and their impact on such proposed changes.

Webb: One challenge is getting the attention of the existing HOA board or management and securing their support for a project that will be expensive, will take time, and will almost certainly result in the diminution or elimination of their current roles or power at the resort. Another challenge is that not all resorts that have fallen into financial distress are good targets for the additional investment and effort that will be necessary to salvage them. What most of these resorts face is a real chicken-and-egg dilemma: it is difficult to attract new capital without owners that have a demonstrated commitment to timely paying their maintenance fees, and owners don’t generally want to pay increasingly higher maintenance fees for a resort that is becoming correspondingly less desirable to use. This dilemma is exacerbated by Generally Accepted Accounting Principles (GAAP) and by state regulations that require timeshare HOAs to assess their members for any prior year operating deficit, as well as for any accounts receivable that have been written off because the HOA's auditors no longer consider them collectible (also known as “bad debt”). Once things start going badly, these are aggravating factors that can make the financial situation grow worse.

Q: What types of timeshare legacy resorts are savable? Why are they savable? How might they be saved?

Nusbaum: As with all real estate – location, location, location! If you have a resort (even in poor condition) that sits on a very valuable piece of underlying real estate, then the opportunities are greater for recapitalization as a timeshare resort or selling the real estate and utilizing the proceeds of the sale to satisfy the present timeshare owners. The other key factor is the owner base. Would another developer or club be attracted to the project when part of the benefit to that developer is the ability to include participation of those owners in the club? Finally, the marketplace itself is important. Over the years, some resort communities for various reasons (availability of good sites, zoning, moratoriums on development, etc.) have had little new development opportunities. In closed markets like these, developers must look to existing resorts as the opportunity to grow their businesses.

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Q: What are the primary differences between savable and non-savable legacy timeshare resorts?

Nusbaum: Each case must be viewed on its own merits and situation; however’ features of a viable resort are more likely to include maintenance fees set at a level that can sustain the annual operations and long-term maintenance and refurbishment of
the physical property, alternative revenue streams including but not limited to rental and resale, good location, marketplace demand, and engaged dues-paying owners. Additionally, aligning itself with a developing entity through a fee for service agreement or through a contract with a solid timeshare management company are two ways for legacy resorts to find a path to continued success. An engaged relationship with a major exchange organization is another important factor. Finally, seeing the resort as a part of the larger timeshare industry with a Board that is knowledgeable and takes advantage of the education opportunities provided by ARDA, ARDA-ROC and other organizations can also make the difference between survival and failure. Rental opportunity, a good location, a strong marketplace, the strength of the existing owner base, and the condition of the property are key components to success.

Webb: Here’s my list: location; the resort’s condition and operations; the attitude of the HOA Board and resort management towards charge and its costs; the willingness of owners to pay more to get more, and; the level of support from an external exchange company.

Q: One solution that’s been proposed is to convert legacy timeshare resorts to full ownership condominiums. What is involved in that? How complicated is this process? How feasible is this process? Where might it work? Where will it just not work? Why will it work or not work? What about converting the legacy timeshare resort to a hotel?

Nusbaum: Individual state laws as well as local ordinances come into play. If the location and product are desirable, and the regime documents are flexible or easily amendable, then converting from timeshare to whole ownership, condo hotel or traditional hotel can be compelling. The seasonality of the destination matters as does attractiveness of any specific opportunity. One size does not fit all.

Webb: This solution can work if the timeshare plan can be terminated for all units, and it simply will not work if it cannot be terminated for all units. Unless the resort’s operation is already heavily rental-oriented, it can be difficult to market a whole unit within a timeshare condominium, particularly if that whole unit is encumbered by a legal obligation to share in timeshare plan (interior of unit) expenses in addition to regular condominium (exterior of unit) expenses. And if a timeshare project is 20+ years old, it can be very expensive to convert it to whole ownership even if it has been well maintained.

Q: What is the fall out for legacy timeshare owners in either the convert to condominium or convert to hotel scenario? What happens to the owners? What do they get out of it?

Nusbaum: Again, each situation comes with its own set of variables and I cannot make a blanket statement. Yet, the questions that owners need to ask themselves are rather simple – “Did I get value out of my original purchase?” If you had rented hotel rooms or condos over the years would your experience have been better or worse? Would your financial commitment have been less or more? If an owner is happy with what they received, then the residual value at the end should matter less. And, conversely what are the costs of doing nothing?

Webb: As noted above, some existing legacy resorts in higher-demanded locations are putting far more of their effort and resources into renting defaulted inventory than into recovering and reselling the delinquent timeshare interests. To the extent that this produces enough additional revenue for the HOA to cover its expenses, it may prove to be a good temporary alternative. However, in the longer run, there are potential legal, regulatory and tax consequences of this kind of unilateral project conversion that may trump the benefits of eschewing the creation.
of new, long-term owners in favor of cheaper—and more expedient—short-term renters.

Legacy timeshare owners get something substantially different than they originally bargained for in either scenario. Whether that is a good thing or a bad thing depends on such post-conversion factors as, (i) the extent to which the financial health of the HOA improves; and (ii) the extent to which timeshare use continues to be compatible with the new residential or hotel regime (which in turn will be affected by such factors as occupancies, rates, unit sale prices, and amenities access and absorption).

Q: What lessons can we learn from the problems of timeshare legacy resorts so history doesn’t repeat itself?

Nusbaum: It is easier to be a settler than a pioneer! Settlers get to homestead and reap the benefits of the lessons learned from the pioneers that came before them. Pioneers get arrows in the head. Like all emerging products, the next iteration improves upon the last. Today’s contemporary timeshare clubs have wonderful flexible offerings and the benefit of an ongoing sales line to recycle inventory as the life cycle and vacation needs of owners change. The original less flexible product offered great vacations through a new product called timeshare but didn’t build in tools to recycle product.

Finally, it is important to note that many legacy resorts are still flourishing – think Scottsdale Camelback Resort, The Trapp Family Lodge, and The Christie Lodge (just to name a few great legacy resorts with very diverse locations), which proves being a legacy resort in itself is not in any way negative. Again, it is about being well run by the board, well managed by the management entity and realistically viewed by.

Webb: (1) Developers can’t syphon off all of the ancillary revenue streams from HOA operations and expect maintenance fees to remain at manageable levels without substantial subsidies; (2) A long-term, deeded timeshare product requires a robust resale market in order to have any sustainable value. And; (3) A chain is only so strong as its weakest link.