

Chapter 4

Regulatory options

Introduction

4.1 In the previous chapter the Committee considered the current approach to the regulation of timeshare and found that there is widespread support for continuing to have a national regulatory scheme with a focus on consumer protection. In this chapter the Committee considers what the general approach to a national timeshare scheme should be. Chapter 5 will consider some aspects of the proposed regulatory scheme in detail.

4.2 In general, four broad regulatory approaches emerged from the evidence:

- continued regulation of timeshare under the *Corporations Act 2001*, with the Australian Securities and Investments Commission (ASIC) as the lead regulator;
- regulation of timeshare under specific provisions of the *Trade Practices Act 1974* (most likely via a mandatory industry code of conduct), with the Australian Competition and Consumer Commission (ACCC) as the lead regulator;
- regulation of timeshare via nationally consistent real estate legislation, regulated in each state by the appropriate regulator; and
- self-regulation by the industry.

4.3 The Committee took the view that the best scheme would be one which retained, and possibly extended, current protection for consumers while minimising the compliance burden for the timeshare industry.

4.4 The latter two proposals, consistent state legislation and self-regulation, attracted little support, and are considered briefly below.

Consistent state legislation

4.5 One option to regulate timeshare would be for all states and territories to introduce consistent legislation which would then be administered by the states. This would allow for nationally consistent legislation albeit via a series of identical regulatory schemes.

4.6 Possibly because of the amount of timeshare activity in Queensland, the Queensland Government is the leader in the development of state-based timeshare regulation. The Queensland Department of Tourism, Fair Trading and Wine Industry Development (TFTWID) informed the Committee that it is in the process of considering a proposal for dedicated timeshare provisions incorporated into the Queensland *Body Corporate and Community Management Act 1997*. The objective of

these provisions would be to address differences between timeshare schemes and other collective investment schemes in the state.¹ The TFTWID submission reported the findings of a public consultation on body corporate issues commenced in July 2004. Submissions to the consultation indicated a lack of knowledge about the interrelationship of state and federal laws in the area, in particular the effect of the Corporations Act. The TFTWID submission concluded that the case for education to clarify the current arrangements for consumers was 'overwhelming'.²

4.7 There was no evidence before the Committee which suggested that consistent state-based legislation is the best way to regulate timeshare. The Committee would observe that such a scheme may seem to be cost-shifting by the Commonwealth, because the states would become responsible for the regulation of timeshare within their state borders. Additionally, it is reasonable to consider whether states and territories such as the Northern Territory and South Australia, with relatively little timeshare activity, would be inclined to adopt new regulatory structures for an industry which has not attracted great attention within their jurisdictions.

4.8 The Committee concluded that any regulatory scheme should be a Commonwealth scheme.

Self-regulation

4.9 In its terms of reference the Committee canvassed the possibility of self-regulation as one regulatory option. This option received virtually no support in evidence, and attracted criticism from both within and outside the industry. For instance, Ms Catherine Wolthuizen, Senior Policy Officer of the Australian Consumers Association (ACA), stated:

In our view, self-regulation of this industry would be ineffective in ensuring consumer protection. There is little evidence that the industry is capable of self-regulating to an adequate degree. Voluntary codes would simply mean that better operators would comply and the rogues would opt out, and consumers would generally be unaware of the difference. We also believe that as time share is often sold as an investment it should be regulated as such. The risks that exist are similar to those of other forms of investment and they require transparency, accountability and access to independent redress to overcome. In our view, without requirements to disclose commissions, refrain from inappropriate hawking activity and provide access to satisfactory dispute resolution, there is little evidence the industry would do it voluntarily.³

1 Queensland Department of Tourism, Fair Trading and Wine Industry Development, *Submission 2*.

2 Queensland Department of Tourism Fair Trading and Wine Industry Development, *Submission 2*, p. 4.

3 Ms Catherine Wolthuizen, *Transcript of evidence*, 15 April 2005, p. 2.

4.10 Mr Martin Kandel, Chief Executive Officer of Accor Premiere Vacation Club (APVC), stated:

Finally, we are not in favour of self-regulation or separate state and territory legislation, as we believe that time share should be regulated by the Commonwealth within the overall framework of the Corporations Act but without labelling it as a managed investment scheme or a financial product.⁴

4.11 Australian Timeshare and Holiday Ownership (ATHOC) which did not directly call for self-regulation, saw a greater role for industry as a co-regulator, particularly through its code of ethics and dispute resolution scheme:

...approximately 5 years ago, ATHOC made an application to ASIC for approval of it or an independent body incorporated by it as an external complaints scheme ('EDR') so that ATHOC members could have complaints dealt with by a scheme familiar with timeshare regulation rather than having to be a member of a scheme (such as the financial industry complaints scheme) which has little or no familiarity with timeshare regulation. The application by ATHOC was not approved by ASIC. The matter is currently before the administrative appeals tribunal for determination.⁵

4.12 Obviously the Committee has no intention of interfering in a matter before the Administrative Appeals Tribunal (AAT). The Committee did, however, receive some evidence in relation to ATHOC's dispute resolution scheme from another witness, Mr Paul O' Shea of the University of Queensland, who stated:

ATHOC put up a comprehensive proposal which, in its documentary form—in its final form—was quite a good proposal in that the scheme it proposed, the Australian timeshare industry complaints scheme, did have an independent board of management and an independent complaints panel. But, on its face, it was not given sufficient funding to allow it to stand alone with respect to the use of resources. So these probably would have to have been shared with ATHOC, which would have been unsatisfactory. And there were doubts about its long-term viability with respect to things like advertising and the three-year regular reviews, which are a requirement of PS139 approval. So ASIC has refused it.⁶

4.13 It should be noted however that Mr O' Shea was also optimistic about the overall performance of the dispute resolution scheme:

On an operational basis, at least in the last two or three years of the scheme when I have been the consumer representative on the CRC, its outcomes for

4 Mr Martin Kandel, *Transcript of evidence*, 13 April 2005, p. 37.

5 ATHOC, *Submission 10*, p. 34.

6 Mr Paul O' Shea, Lecturer at the Beirne School of Law, University of Queensland, *Transcript of evidence*, 28 April 2005, pp. 4–5.

consumers have been favourably comparable with other better constituted schemes in the financial services sector.⁷

4.14 The Committee supports ATHOC in its attempts to increase continually the prevalence of professional conduct within the timeshare industry. The development and improvement of a dispute resolution system is an important component of that. However, the Committee makes no reflection on ASIC's decision regarding ATHOC's application to become an independent dispute resolution service provider, nor on any review of that decision by the AAT. On balance, the Committee prefers at this point to propose a government-based regulatory scheme.

Alternative statutory approaches

4.15 Having eliminated state-based regulation and self-regulation, two approaches remain: regulation under the *Trade Practices Act 1974*, and regulation under the *Corporations Act 2001*.

4.16 During its inquiries, the Committee arrived at the view that the nature of timeshare should be the factor deciding which of these Acts are appropriate. If timeshare is a consumer product in the nature of a consumer durable or a long term service contract, then regulation under the Trade Practices Act would appear to be more appropriate, as this is the source of Commonwealth protection for consumers of other like products and services. If, on the other hand, timeshare continues to be regarded as a financial instrument, then it should be regulated under the Corporations Act along with other financial instruments.

The legal nature of timeshare

4.17 One function of the Trade Practices Act (TPA) is to provide the Commonwealth framework for consumer protection. In particular:

- Part IVA of the TPA prohibits unconscionable conduct in trade and commerce by corporations (but does not apply to the supply of financial services);⁸
- Part IVB of the TPA allows for mandatory industry codes of conduct to be given the status of subordinate legislation; and
- Part V of the TPA contains a wide range of provisions essentially prohibiting misleading or deceptive conduct, and false or misleading representations (again, this Part does not apply to financial services).

4.18 Services, under section 4 of the TPA, are defined as follows:

7 Mr Paul O' Shea, *Transcript of evidence*, 28 April 2005, p. 3.

8 See s.51AAB.

services includes any rights (including rights in relation to, and interests in, real or personal property), benefits, privileges or facilities that are, or are to be, provided, granted or conferred in trade and commerce...⁹

4.19 Timeshare would certainly appear to fall within this definition. As noted above, however, most of the consumer protection provisions exclude financial products and services.

4.20 Currently, timeshare is specifically defined as a financial product and is excluded from the relevant provisions of the TPA by a somewhat complex series of cross-references:

- Section 4 of the TPA gives 'financial product' and 'financial service' the meanings given to them in Division 2 Part 2 of the *ASIC Act 2001*;
- Division 2 Part 2 (section 12BA) of the ASIC Act gives 'financial product' the meaning given to it in section 12BAA and 'financial service' the meaning given in section 12BAB;
- Subsection 12BAA(7)(b)(i) of the ASIC Act makes an interest in a managed investment scheme a 'financial product';
- The meaning of 'managed investment scheme' in turn is taken from s.9 of the *Corporations Act 2001* in which the definition of managed investment scheme includes paragraph (b) specifically describing 'a time-sharing scheme' as a managed investment scheme.

4.21 While this describes the current state of the law, the Committee need not necessarily be bound by this series of definitions. The more general definition of 'managed investment scheme' given in section 7 of the *Corporations Act 2001* is as follows:

managed investment scheme means:

- (a) a scheme that has the following features:
 - (i) people contribute money or money's worth as consideration to acquire rights to benefits produced by the scheme (whether the rights are actual, prospective or contingent and whether they are enforceable or not);
 - (ii) any of the contributions are to be pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the people who hold interests in the scheme (whether as contributors to the scheme or as people who have acquired interests from holders);

9 *Trade Practices Act 1974* s.4.

- (iii) the members do not have day-to-day control over the operation of the scheme (whether or not they have the right to be consulted or to give directions)...

Timeshare also appears to fit well within this definition. Consequently, on an initial reading, timeshare could adequately fall within either the TPA definition of 'services' or the Corporations Act definition of a managed investment scheme.

Evidence on the legal nature of timeshare

4.22 The Committee tested this question of the proper nature of timeshare with a number of witnesses. ATHOC agreed with the view that timeshare is more like a consumer durable product or service than like a managed investment:

Not only is timesharing a long-term consumer durable product, it is also unique amongst consumer products and therefore requires legislative recognition which addresses its unique nature. Though a motor vehicle and washing machine are consumer products and an admission ticket to a football match and an airline ticket are consumer services, they are different consumer products and different consumer services but are more similar than they are different in terms of their essential component parts. There is widespread public recognition as to the nature and purpose of each of these consumer products and services. Accordingly, there is no particular need for licensing or disclosure.¹⁰

4.23 Mr Paul O' Shea pointed out some differences between the nature of what is 'purchased' by a timeshare member, and a more customary purchase of goods or services:

the legal nature of the interest is that it is now more akin to a share. It is a floating point product: it does not actually relate to any specific piece of real estate. So, whatever pretensions the old product had to being a kind of title—and I am sure that you have been amused by some of the elaborate certificates that used to be given to people when they bought them in the old days—the modern product has no such relationship to a particular piece of real estate. In fact, the actual resort theoretically could cease to exist yet there would still be the right to use, say, resorts that were in the same group in the hands of the time share owner.¹¹

4.24 Associate Professor Mike Dempsey of Griffith University came to the centre of this difficulty by pointing out just how blurred is the line between 'investment' in timeshare and 'consumption' of a vacation:

But if you have what you referred to as an ongoing consumable that lasts for 20 years, it starts to have those characteristics of an investment. If you suddenly decide that it is not what you want after all—we all change our

10 ATHOC, *Submission 10C*, p. 1.

11 Mr Paul O' Shea, *Transcript of evidence*, 28 April 2005, p. 6.

minds two, three or five years later—then as much as you may have thought of it as a consumable at the time, when you come to part company with it for a very disappointing price, for all intents and purposes, at that point in time it is now an investment that in your own thinking went badly wrong. The distinction between a consumable and investment in the case of time share is not quite as distinct as it may be normally. A holiday in Bali is a consumable; putting extra money into my superannuation fund is an investment. But what we call a consumable over many years can have characteristics of an investment when you part company with it, especially if you did so prematurely—meaning that you do not wish to keep it for life after all.¹²

Conclusions

4.25 Regrettably, this definitional question is not one which will admit of an easy and self-evidently correct answer. As Professor Dempsey has pointed out, timeshare can be seen either as a long term service contract, or as an investment which is unlikely to create a capital return, but which provides benefits (in the form of vacations) for so long as the investment is held.

4.26 The Committee noted, however, the important fit between timeshare and subparagraphs (ii) and (iii) of the definition of a managed investments scheme.

4.27 Subparagraph (ii) notes that managed investments are pooled or used in a common enterprise. One of the key characteristics of timeshare—perhaps the definitive feature of timeshare—is that it is a *pooled* system, where timeshare members join with one another to acquire, through a trust or a company, ownership over a resort or a series of resorts. In the case of the larger players, the pool may have many thousands of members, and may have a portfolio of property worth many millions of dollars. The very reason why timeshare members are able to holiday in countries around the world is because they have pooled their contribution with the contribution of many others. The definition of managed investment schemes captures the pooled nature of timeshare far better than does the TPA definition of a service.

4.28 Subparagraph (iii) notes that in managed investments, the investor gives up day-to-day control of the investment—this gives the investment its 'managed' character. This is also the case for timeshare, as ASIC pointed out:

It is not a consumer durable in a narrow sense, because, while the consumer has use access to the underlying asset, the asset in many cases continues to be managed by another person. Your ability to enjoy that asset going forward depends on the way it is managed by another person. That distinguishes it from many consumer durables.¹³

12 Assoc. Prof. Mike Dempsey, Head of Finance Discipline, Department of Accounting, Economics and Finance, Griffith University, *Transcript of evidence*, 13 April 2005, p. 6.

13 Mr Malcolm Rodgers, Executive Director, Regulation, *Transcript of evidence*, 28 April 2005, p. 13.

4.29 On the basis of these observations, the Committee concludes that the *Corporations Act 2001* will continue to be the best legislative 'vehicle' for the regulation of timeshare.

Recommendation 1

4.30 The Committee recommends that timeshare should continue to be regulated under the *Corporations Act 2001*.

Regulation under the Corporations Act

4.31 While the Committee has recommended that timeshare should continue to be regulated under the Corporations Act, the Committee is not simply supporting the status quo. In Chapter 3, the Committee canvassed some of the difficulties associated with the current regulation of timeshare under the Corporations Act. The current process has led to substantial costs of compliance for timeshare operators, and has not necessarily delivered successful protection for consumers as a result.

4.32 In particular, the paradox of regarding timeshare as a managed investment and yet forbidding timeshare operators from selling it as an investment, is exasperating both for the industry and the Committee. Mr Ramy Filo, ATHOC President, neatly outlined the paradox in terms of the 'investment' training the current regulations require for staff:

I have just finished doing a training session for a couple of people. At the end of it I said, 'You've got to learn all of this to pass but once you've passed I want you to forget everything you've learnt here—just understand what time share is about and make sure you never say that it is an investment.' It is an investment in lifestyle, but you should not use the word 'investment'.¹⁴

4.33 Evidence before the Committee from within the industry called for continued treatment under the Corporations Act, but called for separate provisions within the Corporations Act. Mr Kandel from APVC, for instance, stated:

[Timeshare] should have a separate chapter within the Corporations Act with relevant consumer protection provisions but dispense with the irrelevant financial product related requirements.¹⁵

4.34 ATHOC in its submission made a similar argument based on securing appropriate exemptions from the current Corporations Act provisions.¹⁶ The Committee notes that providing a separate chapter for timeshare would have the same effect as selectively providing exemptions from current arrangements, but would be far neater from a regulatory perspective. In evidence, Mr Filo from ATHOC stated:

14 Mr Ramy Filo, *Transcript of evidence*, 13 April 2005, p. 25.

15 Mr Martin Kandel, *Transcript of evidence*, 13 April 2005, p. 37.

16 ATHOC, *Submission 10*, p. 21.

The timeshare industry is regulated within legislation that fits our industry like a square peg in a round hole. Although the corporations legislation is the best overall framework for our industry, there are key aspects that need modification and/or review for their appropriateness. We have detailed these aspects in our submission. Our industry is the most regulated consumer product in Australia. Even as a financial product, time share is subject to more regulatory requirements than many other financial products.¹⁷

4.35 The Committee accepts these views. While timeshare is more like a managed investment than a service, there remain some important distinctions between managed investments and timeshare. An investor in a managed investment is attempting to gain a return on the capital invested. The expected return will almost certainly be financial in nature. A timeshare purchaser, on the other hand, will almost certainly not realise a financial return on their investment. Indeed, price signals from the timeshare resale market¹⁸ suggest that the initial timeshare entry price should be regarded as virtually a sunk cost, which cannot be recovered.

4.36 It is clear to the Committee that continuing to regulate timeshare as a managed investment is inappropriate. However, any separate chapter on timeshare in the Corporations Act must ensure that consumers receive the same levels of protection as are currently provided. The regulatory regime may be tailored differently, to suit the special nature of timeshare and to minimise compliance burdens, but it must be no less rigorous than the scheme which currently applies.

4.37 In the next chapter, the Committee will outline some of the issues which should be addressed in a Corporations Act chapter on timeshare.

Recommendation 2

4.38 The Committee recommends that:

- **timeshare should be removed as a definitional element of managed investment funds under s.7 of the *Corporations Act 2001*; and**
- **a separate chapter should be inserted into the *Corporations Act 2001* to deal specifically with timeshare.**

17 Mr Ramy Filo, *Transcript of evidence*, 13 April 2005, p. 13.

18 See discussion in the next chapter.

