

# Submission

## Property & Environmental Law Section

To: The Secretary, Parliamentary Joint Committee on Corporations and Financial Services

### **Submission on inquiry into regulation of the time share industry**

A joint submission from: the Commercial Law Section and the Property and Environmental Law Section of the Law Institute of Victoria

Date: 16 February 2005

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### 1. Background

The Parliamentary Joint Committee on Corporations and Financial Services has agreed to inquire into the regulation of the time share industry in Australia.

By letter dated 15 December 2004, Ms Sarah Bachelard, Committee Secretary, invited the Law Institute of Victoria (**LIV**) to make submission on the inquiry's terms of reference. The LIV welcomes the opportunity to provide comments on the subject of regulation of the time share industry and provides the following comments.

We note that the inquiry is in the initial stages of developing the Government's approach to reviewing time share industry regulation. Consequently the comments provided in this submission are general in nature. Elaboration can be provided once the recommendations of the inquiry are released. The LIV would welcome continued involvement in the consultation process and the opportunity to comment on specific proposals.

### 2. Summary

The LIV believes that the current regulatory regime for the time share industry is not satisfactory in that it does not provide sufficient consumer protection for prospective purchasers, nor does it sufficiently address the behaviour of developers and salespeople of time share resorts.

The LIV suggests that a new dedicated piece of legislation, perhaps entitled The Time Share Resorts Act (**Act**), be drafted to deal with all aspects of the time share industry. A separate part could deal with clubs and resorts that are fully sold out and another part could deal with clubs and resorts with which a developer is involved. This would relieve the fully sold clubs of the burden of compliance with the Corporations Act and would ensure the developers are subject to specific controls dedicated to their industry. The new Act could remove the existing torrens title method of landholding and vest the land in a trustee or the responsible entity.

### 3. The effectiveness of the current regulatory arrangements for the time share industry under the *Corporations Act 2001*

#### 3.1 Current regulatory arrangements

Time share is the division of the use of holiday facilities into equal units of time (usually by week) or points so that different people can use these facilities on a regular organised basis. From the viewpoint of consumers of time share resort accommodation in Australia, there is currently little regulation of the activities of salespeople and developers. The current regime contained in the *Corporations Act 2001* (Cth) (**Corporations Act**) has been introduced to control the affairs of time share developers but the LIV believes that this is not an appropriate mechanism for the many resorts and clubs that have been fully sold for many years and have no connection with developers.

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As the law presently stands, unless a fully sold time share resort or club obtains an exemption from complying with the Corporations Act requirement for a responsible entity, it cannot operate. The LIV queries why such resorts and clubs should need to comply with these requirements if they are simply organising the use of the facility between their members and not selling time. It appears that the legislation was intended to address the problems that arise for consumers who fall for the traps of salespeople who are selling "new" time but does not address the specific needs of resales of time or those needs of fully sold resorts.

### 3.2 Developers and salespeople

In relation to developers of time share resorts, they are an essential aspect of ensuring top quality resort accommodation continues to be made available to the Australian and international consumer. However, LIV believes that the regulatory framework that should govern developers should be quite separate to the regime that addresses fully sold resorts. The LIV considers that developers should be regulated by their own dedicated legislation that is not mixed with the interests of the "mums and dads" who are only interested in having a holiday.

### 3.3 Consumers

Consumers of new time in time share resorts have little protection or redress available to them, compared with other consumer interests, such as consumer credit and residential tenancies. The tactics of some salespeople in the time share industry are unscrupulous. High-pressure sales techniques can be invoked to persuade members of the public to purchase without opportunity to carefully consider the consequences and high cost. However, it is important to balance any prospective consumer regime with the need to continue the development of new resorts and encourage sales.

## 4. Advantages and disadvantages of possible models for reform of the regulatory arrangements applying to the time share industry

### 4.1 Type of regulation

The LIV recommends that a specific legislative regime be introduced for time share. The time share industry is relatively easy to define and deserves its own legislative framework which caters for its particular needs.

It is also important that there be some access to legislative support for the many thousands of Australians who have chosen to organise their holidays in this way. Time share is a popular option for holiday-makers in Europe and the United States of America but is alien to many Australians who are suspicious of it and find the concept difficult to understand. Many potential time share owners may have been dissuaded by the unsavoury selling techniques adopted by some in the industry.

Considering the possible models for reform of the regulatory arrangements, self-regulation would seem to be a less satisfactory option than dedicated legislation. Whilst it would be possible for developers and salespeople in the industry to develop their own code of

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conduct, the LIV believes it would be a much more difficult process for fully sold resorts and the many time share owners to organise in this way as there are many fragmented players in the market. Dedicated legislation would result in a more systemised and comprehensive solution to the time share industry's needs.

The nature of time share and the ability of consumers living in one State of Australia to own time in a resort in another State lends itself to a Commonwealth legislative regime.

Therefore, the question is should the required regulation be included in the Corporations Act or should a new piece of legislation be dedicated to the time share industry? The LIV believes the latter would be the most suitable option.

The reason for inclusion of time share in the current Corporations Act is not clear to many people involved in time share. First, it was included in the Managed Investments amendments. This is based on the mistaken notion that time share is an investment. Whilst some salespeople may argue this is the case, the fact is a purchaser of time share can generally only expect to receive a small proportion of that investment back. In fact, there is no opportunity to redeem the investment and usually the resale market will dictate that the timeshare week that was purchased for \$25,000.00 a few years ago is now worth only \$3,000.00 on the open resale market.

The Corporations Act is not a suitable vehicle for time share on the basis that it concerns corporations. It may have been appropriate if the clubs or resorts were organised on a corporate basis, however this is usually not the case. Often, unit trusts control the entitlements to occupation of the resort units. As a means of controlling the activities of those corporations involved in the development of time share resorts and their sales and administration methods, the Corporations Act seems to have created a set of rules and a framework that is unworkable in the long run. It has not included any framework for clubs or resorts that are no longer conducted by a developer. In due course, all units will become fully sold and thereafter out of the control of the developers. Therefore control by way of the Corporations Act becomes redundant.

The LIV therefore recommends for the above reasons that the enactment of a dedicated piece of legislation is the most appropriate form of regulatory arrangement for the time share industry.

ASIC, by way of a policy statement, has indicated that all clubs will need to reorganise themselves in due course into a structure that is corporation based and therefore controllable by ASIC. The LIV questions why this is necessary in the time share context. The Australian Time share and Holiday Ownership Council (**ATHOC**) has been designated as the industry representative, however ATHOC is an organisation to which some clubs and resorts belong as a necessity to meet exemption conditions and have no meaningful voting power as the bigger participants can outweigh the smaller groups.

Fully sold resorts and clubs do not share the same interests as developers and should not be subject to the same controls. The LIV proposes that they should be each subject to separate parts of the same legislation. Part A could be for the developers and entrepreneurs

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and control their activities and also dictate the structure of the clubs. Part B could provide a framework similar to the Cooperatives Act that provides legislative structure.

This legislation should not be administered by ASIC but could be part of the portfolio of the Minister for Tourism. Time share is about holidays and facilitating the swapping of holiday destinations and this should be the key focus.

### 4.2 Title-based resorts

Many of the older clubs and resorts in Australia are title-based. This was the early model for timeshare and seems to follow models from the United States and Europe. In the case of title-based shares, every week of timeshare is represented by a torrens system title being issued for a 1/52nd share in the piece of land where the resort is built. The title is in turn encumbered by a 99 year lease to a company which is in turn the trustee of a unit trust. The trust issues a unit for each week owned and it is the unit that bears the right to occupy the timeshare resort for one week. This works well in theory until inevitably some owners decide they do not want to own the responsibility of timeshare any more and simply do not continue to pay their dues. The unit trust deeds usually contain a right to forfeit the right to use the timeshare resort facilities but unfortunately there is no similar right to take over the title. Therefore, many clubs have suffered from the growing problem of disappearing owners and no means of replacing them. It has been the practice in the past that the trustee of the unit trust would carry on and issue a unit in the unit trust to new members to take the place of the titleholder who had disappeared. This practice is still carried on today as people want to buy an entitlement to timeshare and do so by participating in the resale market.

The LIV therefore proposes that the new regulatory regime must address the problem of how to deal with disappearing title holders.

### 4.3 Resales

A resale is the reselling of a week's entitlement to time share from an existing owner to a new private owner, rather than through a developer. The average value of a resale week is \$3,000.00 whereas a developer can be charging anywhere up to \$25,000.00 for a "new" week. There is a very slow market for resales.

Older resorts have, over many years, depended on reselling the weeks of recalcitrant owners to remain afloat. Like a cooperative, all of the costs of maintaining the resorts must be paid by the owners through their annual maintenance fees. If there are fewer owners, the costs to remaining owners are higher, and significantly more than they had anticipated upon purchase of their units. Therefore, older resorts rely on resales to ensure a continual flow of income for maintenance costs.

The LIV contends that resales must be protected and encouraged in the new regulatory regime. This could be achieved by ensuring that developers are not able to sell "new" weeks whilst there are resale weeks available at the same resort.

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### 4.4 Older resorts and rebuilding

Time share resorts by their very nature as places of vacation, take heavy traffic and require regular refurbishment of both buildings and furniture. If the clubs are responsibly managed, they will make proper sinking fund provision for refurbishment. Because this is a continued impost on the owners, some clubs struggle with their refurbishment and eventual replacement. Issues also arise in relation to the resort being able to deal with the land due primarily to disappearing titleholders. It is possible to sue each one for their unpaid maintenance fees, obtain judgment and have the sheriff sell the title. However, identifying and locating owners and calculating the money they owe is a difficult, time-consuming task and usually an expensive exercise. If there were several hundred in this category how could the litigation be afforded and to whom could the units be resold in such a limited market?

The new regulatory regime must therefore deal with ongoing management issues for the time share resorts.