

FRACTIONAL OWNERSHIP 101

By D. Andrew Sirkin

The common sense of fractional ownership is so elegant and obvious, it is puzzling that these arrangements are only now attracting the attention and popularity they deserve. Why incur all of the costs of owning something you will only use part of the time? Why not share the costs with other people who want to use the same thing? This simple logic is now being employed by buyers of many types of luxury items, from executive jets to fabulous yachts. But by far the most common use of fractional ownership today is the vacation home.

Statistics show that most people only use their vacation home 17-30 days each year. Fractionals are appealing because they allow people to own only the share of a vacation home that they will use, rather than the entire property. The main benefits of fractional ownership are:

- **Lower Acquisition Costs:** Buying a fraction of a property means the buyer pays only a fraction of the cost of the entire property. In addition, the costs of renovating, furnishing and outfitting the property are shared. Although the per-share cost of fractionals packaged by a property owner or developer include a “markup” (on average the total share price will be 150-250% of the cost of the home and contents), they are still a good deal for most buyers because they avoid the time, effort and difficulty of outfitting the property, creating the legal structure and assembling the owner group.
- **Lower Operating Costs:** Owning real estate involves ongoing operating costs such as property tax, insurance, utilities, and maintenance, including the cost of repairing and replacing the furniture and other household goods inside. Maintaining a vacation home can be particularly complex because of intermittent usage and the distance between the owner and the property, often requiring the assistance of a local manager or management company. Sharing the cost and efforts of operating dramatically lightens all these burdens.
- **Eliminate or Diminish Need for Rental Tenants:** Most vacation home owners face the unpleasant decision between leaving the property vacant when it is not being used by the owner, or renting it out. As anyone who has been involved in vacation rental knows, the rental option has significant downsides. Do it yourself, and you spend innumerable hours promoting the rentals, responding to inquiries, handling bookings, checking tenants in and out, and readying the property between tenants. Hire a manager or rental agency and you will generally give up 30-50% of the rent. Either way, the tenants extract a significant toll on the property, and the rental periods most demand are the same ones when you would prefer to use the home yourself. While some fractionals allow owners to rent out their home when they are unable to use it, the lower cost of buying and owning a fractional means that most owners do not need to use this option.

- **Diversification of Investment and Destination:** Fractional ownership allows the money that would have been needed to own and operate a single vacation home to be spread over two or three vacation homes. Spreading your dollars over several homes lowers investment risk and increases the likelihood of profit by exposing you to two or three different real estate markets. Moreover, owning vacation homes in several locations gives you more vacation options each year, while still allowing you to spend your time in your own homes where you are comfortable with the surroundings and know how everything works.

The benefits of fractional ownership are so compelling that many people who could easily afford their own place are opting for fraction ownership instead. Perhaps even more surprising, many people who already own a vacation home are choosing to sell some fractional interests in it in order to lighten their cost and management load and still use the property as often as they ever did.

Today's fractional ownership arrangements are often organized by the users themselves. More frequently, they are set up by a property owner or developer who outfits the property, creates the legal structure and documents, then offers the fractional interests for sale. Contrary to what you might think, groups of complete strangers who come together through these packaged offerings are generally more successful at managing the shared property than groups of friends or family members. The key is good advice, careful planning, and a comprehensive legal agreement.

In coming issues, we will explore many of the issues raised by these arrangements. Are they just timeshares with a new name? In the world of pre-developed "fractionals", "condo hotels", "condotels", "private residence clubs", and "destination clubs", how can you tell a good deal from a bad one? If you're organizing your own fractional, how do you develop an arrangement that is fair and will withstand the test of time? Most important, do the risks and headaches of sharing with others outweigh the economic benefits?

ABOUT THE AUTHOR

D. Andrew Sirkin is a recognized expert in fractional ownership and other co-ownership arrangements including shared vacation homes, TICs, equity sharing, co-housing, and legal subdivisions such as condominiums. His practice areas include transaction planning, offering materials, co-ownership agreements and CC&Rs, entity formations, regulatory approvals, fractional lending and mediation. From offices in San Francisco California, Evergreen Colorado, and Paris France, he has worked on projects all over the World, including most U.S. States, as well as Italy, France, Spain, Portugal, Ireland, Argentina, Nicaragua, Costa Rica, Panama, Dominican Republic, Nicaragua, Belize and Mexico. Since 1985, he has prepared fractional ownership documentation for over 6,000 clients. He is an accredited instructor with the California Department of Real Estate, and frequently conducts co-ownership workshops for attorneys, real estate agents, corporations, and prospective home buyers. Andy is the co-author of *The Condominium Bluebook*, published annually by Piedmont Press, and *The Equity Sharing Manual*, first published by John Wiley and Sons in November 1994 (order the book). He has written numerous articles on related topics, all of which are available at www.sirkinfractionallawyers.com. Mr. Sirkin can be contacted via email at DASirkin@earthlink.net. Mr. Sirkin can be reached by telephone at 415-738-8545.