

DIFFERENCES BETWEEN FRACTIONALS AND TIMESHARES

By D. Andrew Sirkin

The common wisdom is that timeshares are a scam perpetrated on the naïve. Relaxed during their vacation in a storybook location, hapless couples are lured into high-pressure presentations by offers of free meals, lodging and recreational activities, then sold on the idea of an annual “prepaid vacation” for the rest of their lives. Soon afterward, they discover that their “prepaid vacation” is difficult to use, in undesirable facilities, more expensive than a regular hotel, or all three. When they try to sell, they find their investment worthless. Sometimes they can’t even walk away without credit agencies hounding them for ownership dues.

Whether or not this picture is accurate, developers of today’s fractional resorts struggle mightily to distance themselves from this perception. Central to this effort has been renaming and repositioning the product. Regardless of how similar or different they are from the timeshares of the past, today’s arrangements are called fractionals, condo hotels, condotels, private residence clubs, destination clubs, or something else, but rarely timeshares.

Are today’s fractionals really different from yesterday’s timeshares? In general, the answer is yes, but this generalization can be misleading, especially if one puts too much stock in the name of the arrangement, and not enough in the arrangement itself. The idea behind traditional timeshares was every bit as logical and compelling as the idea driving today’s fractional explosion. The problem was not the concept; it was the execution.

In virtually every state, any arrangement involving time-based sharing of an asset falls within the legal definition of a timeshare, and is regulated under timeshare laws. This means that, from a legal standpoint, all fractionals are timeshares. But it does not mean that all fractionals share the same problems that have given timeshares a bad name.

The most important distinguishing factor between modern fractionals and traditional timeshares is the number of owners per home or apartment. Most timeshares involve as many as 52 owners per unit, and many of the rest involve 26. The main consequence of having so many owners is short and/or infrequent owner stays. Most timeshare owners visit their property only once a year, often for only one week. This means there is little emotional connection between the owners and the property, often called “pride of ownership”, and this lack of connection translates into lack of care and apathy. Higher traffic also means more wear and tear.

By contrast, most fractionals involve 2-12 owners per unit, meaning owners visit the property more frequently and stay longer. Larger ownership shares and more time spent at the property gives fractional owners a greater stake in how the property looks and feels, and in how it appreciates over time. Fractional owners care about their property and their investment, and it shows in how the property is maintained and operated.

Higher quality and cost also distinguish fractionals from timeshares. In general, fractionals involve larger apartments or homes, more amenities and better finishes. Fractional buyers pay more to purchase and expect to pay more in maintenance and management fees. Higher quality construction and finishes, coupled with more resources for maintenance and management, and fewer users, tends to keep the property looking good and operating smoothly. By comparison, timeshare properties often degrade over time, causing them to become less desirable for original purchasers and lose most or all resale value.

This degradation results from lower initial quality, inadequate maintenance and management, and higher user traffic.

Another common distinguishing factor between modern fractionals and traditional timeshares is the degree of owner control. Properly structured fractional associations operate much like homeowners associations, and retain ultimate authority and control over their property. Day to day operational responsibility is delegated to a manager or management company, but owners retain the right to replace management if it is not performing. In contrast, most timeshares are permanently controlled by a developer or hotel operator, and timeshare buyers are viewed more as repeat hotel guests than as property owners. This arrangement provides little incentive for the operator to maintain high standards after the last timeshare interest is sold.

But the fact that most fractionals do not share the characteristics that have made most timeshares bad deals does not mean that all fractional are good deals, or even that fractionals are always better than timeshares. Rather, it means that fractional buyers need to assess the details of the arrangement before buying, and not be distracted by the label attached by the seller. How many owners per unit will there be? What is the quality of the construction and furnishings? Is there a realistic budget that will provide money to operate the property as well as to replace the furnishings and equipment regularly? To what extent can owners exercise control over the property and the management?

In coming issues, we will explore the various types of fractional arrangements in more detail, and provide the tools needed to analyze the options and decide which arrangement works best.

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.