



A Guide to Terminating Failed or Struggling Single-Site Projects

Older timeshare projects that were created prior to the entrance of the brands into the timeshare industry may struggle or fail for a number of reasons, including the project falling into disrepair or the original developer failing to properly market and sell interests in the project. Many times, an enterprising new developer may attempt to take over the project or a lender may foreclose on the project and become a successor developer. In these situations, the new/successor developer (referred to as the “Developer”) may decide that the best course of action is to terminate the project, buy out all of the existing timeshare owners, and start over.

Terminating a timeshare project, however, can be difficult, particularly when there is the issue of hundreds if not thousands of existing timeshare owners that the Developer must handle. Some of these owners the Developer may not be able to locate, others may not be responsive to the Developer, and still others may refuse to sell their timeshare interests back to the Developer—even though the project is struggling or has failed. When the Developer terminates a timeshare project, the Developer’s objective is to purchase all of the timeshare interests at the project and obtain insurable title to such interests. Here is a summary of the steps necessary to terminate a failed or struggling single site timeshare project.

Step 1: Obtaining Control of the Association—Reviewing State Law and Governing Documents to Determine Whether Termination is Feasible.

A Developer wishing to terminate a timeshare project must first look at state law and the governing documents of the timeshare regime to determine whether the Developer can purchase a sufficient number of timeshare interests that will enable the Developer to: (1) unilaterally amend the project documents, if necessary, to include the termination language

discussed in Step 3 below; and (2) control enough votes to unilaterally terminate the timeshare regime. The key provisions to review are the amendment and termination requirements in the timeshare declaration, as well as the state’s non-profit corporation act, timeshare act, and, if applicable, condominium or common interest ownership act⁵.

If the voting requirements (under state law and the project documents) for termination and/or amendment require 100% of the total votes of the owners association, then it will not be feasible for the Developer to obtain control of the owners association. If such voting requirements are only at 70% or 80%, then it is more likely that the Developer can gain control of the owners association and terminate the project.

Step 2: Obtaining Control of the Association: Buy-Back Program.

If a Developer determines that it is feasible to obtain enough votes to terminate a timeshare regime, then it must launch a buy-back program. This program may be as simple as offering to pay existing owners an amount that is higher than the current value of their timeshare interest, which often has a depressed value. However, some Developers have offered additional incentives, such as offering “trades” into ownership in a multi-site program that would offer more benefits at a lower annual cost. Under such an incentive program, owners are required to “quitclaim” their timeshare to the Developer and to release the Developer from all liability. The owners are then issued an ownership certificate in the new program. No additional costs are charged to the owners under this approach.

Step 3: Amending the Declaration to Clearly Address Termination.

Once the Developer has obtained the requisite number of votes to terminate the project and amend the project documents,

the Developer will most likely need to amend the termination provisions in the timeshare declaration because, in many instances, the timeshare declaration and state law do not thoroughly address how a project is terminated and what happens after termination.

This amendment should include the following provisions: (1) upon termination, title to the timeshare interests shall vest in the owners association as trustee for the benefit of its members; (2) the owners association shall have the authority to terminate the project documents and sell the entire property, usually to the Developer; (3) each remaining timeshare owner shall be paid an amount equal to the fair market value of the timeshare interests as of the date of termination of the timeshare program; and (4) a “Termination Agreement” shall be recorded terminating the timeshare regime and setting forth the minimum terms of the sale of the timeshare interests.

Step 4: Appraisal and Determination of Purchase Price.

The purchase price for the timeshare interests should equal the fair market value of the timeshare interests as of the date of termination of the timeshare program. Unless otherwise required by state law, the purchase price does not need to be based on the current market value of the property and building(s) in which the timeshare project is located. This is a critical distinction. The Developer should obtain an appraisal from someone who is experienced in appraising timeshares and fully understands this distinction. This appraisal may also be used in the quiet title action discussed in Step 7.

Step 5: Voting on Amendment to Timeshare Declaration and Termination Agreement.

Even though the Developer may have the votes necessary to unilaterally approve the amendment to the timeshare

declaration and unilaterally approve the recordation of the Termination Agreement, the project documents may require that the owners association give the owners an opportunity to formally vote on the termination. This process is helpful in informing all of the remaining timeshare owners how the project is going to be terminated and how the owners will be compensated for their timeshare interests. If the project documents and state law permit, the easiest way to hold the vote is to send ballots out to all of the owners and require that they return the ballots by a specific date.

Step 6: Recording Declaration Amendment and Termination Agreement; Executing Purchase Agreement.

Next, the amendment to the declaration and the Termination Agreement can be recorded. Concurrently with the recording of these documents, the Developer and the owners association should execute a purchase agreement, whereby the Developer agrees to purchase the remaining timeshare interests from the owners association. The Developer and the owners association may want to deposit the purchase money in escrow pending the completion of the quiet title action discussed in the next step.

Step 7: Quiet Title Action.

Most title companies will require that the Developer complete a quiet title action before they are willing to issue a title policy insuring that the Developer owns marketable title to the terminated timeshare interests, free of any timeshare owner claims. Title companies require the quiet title action because there are most likely timeshare owners who (1) have died, (2) are not responsive to the Developer, or (3) are not able to be located—such owners will not have deeded their interests to the Developer. Title companies are not comfortable with record title owners showing in the title records, even though the termination procedures have been strictly followed by the Developer.

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Through a successful quiet title action, the Developer will be able to obtain a judicial determination that the termination process was valid and that the timeshare owners who have not transferred title to their interests (even those that the Developer was not able to find or that voted against termination) no longer have any ownership in the project. In most instances, the Developer can obtain a default judgment making the quiet title action very streamlined.

Step 8: Judicial Reformation—An Alternative Approach.

In the event the Developer is taking over a project that is in disrepair and determines that it is not feasible under the project documents to terminate the project or achieve the necessary ownership interests to control the votes in the owners association, the Developer may need to have the project facilities updated, so it can successfully market and sell timeshare interests in the project.

Renovating projects to meet today's competitive market standards is costly, and many owners balk at paying the increased assessments necessary to cover such expenses. As a result, owners associations and/or Developers are often times unable to obtain the votes necessary to renovate projects. The only option the Developer may have is to file a complaint and petition in state court for judicial reformation of the project documents to reduce the percentage vote required for owner approval of the proposed capital repair and replacement budget. Upon the voting requirements being lowered, the Developer may then control enough votes to cause the owners association to levy a special assessment to cover the costs of renovating the project. Some state statutes explicitly provide for judicial reformation when the voting requirements in project documents are too restrictive. Some Developers have even been successful with judicial reformation in states where judicial reformation is not provided by statute.

Re-thinking Business

In summary, terminating a timeshare project can be long and complicated but may be profitable for an enterprising Developer willing to wade through a difficult process. This may also be a helpful option for owners who otherwise can not get the funds needed to refurbish their project. When structuring a termination plan, the Developer's primary goal must be to obtain insurable title to all of the timeshare interests, while complying with state law and the project documents and attempting to be as fair as reasonably possible to the existing timeshare owners. For projects that cannot be terminated, the Developer may want to look into judicial reformation as a possible alternative. **D**

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Endnote

¹ Some timeshare projects are in condominium projects and are subject to state condominium and/or common interest ownership laws. Other timeshare projects are not in condominium projects and buyers are sold undivided interests ("UDI") in the entire project. In most states, UDI timeshare projects are not subject to common interest ownership acts.

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