

OVERVIEW

Sunrise Analysis: Destination Clubs

Report No. 08-01, January 2008

Summary

In Senate Concurrent Resolution No. 75, Senate Draft 1, the 2007 Legislature requested that the Auditor conduct a “sunrise” analysis of Senate Bill No. 697, which proposes to regulate destination clubs. The Hawai‘i Regulatory Licensing Reform Act (Chapter 26H, Hawai‘i Revised Statutes) requires that legislative bills proposing regulation of previously unregulated professions or vocations be referred to the Auditor for sunrise analysis prior to enactment. The Auditor is to assess whether the proposed regulation is necessary to protect the health, safety, or welfare of consumers and is consistent with the regulatory policies in Chapter 26H, HRS. In addition, the Auditor is to examine the probable effects of the proposed regulation and assess alternative forms of regulation.

Destination clubs are a relatively recent, fast growing segment of the vacation market. There are eight destination clubs with properties in Hawai‘i and an estimated 15 Hawai‘i residents are club members. About 20 clubs offer their members luxury accommodations in multi-million dollar properties around the world. They are the primary choice of affluent households, particularly those with families who prefer to vacation in luxurious homes instead of hotels. Destination club services may include travel, private jets and yachts, concierges, housekeeping, and private chefs. Members who wish to join must pay initial membership deposits that range from \$40,000 to \$3,000,000 as well as annual fees. The amount of the initial deposits and the annual fees vary according to the number of days of planned usage and the quality and size of the vacation homes owned and offered by the club. For the most part, destination clubs are not an investment. Members receive no equity in most clubs; instead, they have a membership contract that gives them the right of access to a portfolio of properties owned or leased by the club. Club memberships cannot be sold or traded. All clubs allow members to resign as they wish and receive a refund of their membership deposits that range from 80 percent to 100 percent.

In January 2004, an advertisement for the destination club Exclusive Resorts triggered an investigation by the Regulated Industries Complaints Office (RICO) of the Department of Commerce and Consumer Affairs to determine if Exclusive Resorts was operating as an unlicensed real estate broker under Chapter 514E, HRS. Later that year, a civil action was filed in the Hawai‘i Third Circuit Court to prohibit and enjoin Exclusive Resorts from any commercial or time share activities in the Pauoa Bay Subdivision on the Big Island. A similar complaint was filed in U.S. District Court.

In July 2005, the Third Circuit Court declared that Chapter 514E, HRS, did not apply to Exclusive Resorts’ plans to use its Pauoa property for club members. The judge ruled that the planned use was not a “time share ownership plan” because the



members have no ownership interest in the accommodations. In August 2005, the U.S. District Court concurred with the state court that Hawai'i's time share law did not apply.

These decisions notwithstanding, DCCA maintains that destination clubs may be regulated under the state's time share law. In November 2006, Exclusive Resorts signed an Agreement of Voluntary Compliance with the department. The agreement lapsed as of May 2007. During the interim, several destination clubs formed the Destination Club Association to promote responsible business practices. The department convened a working group composed of destination club and time share industry representatives to develop new regulations. Senate Bill No. 697 is the resulting bill. The department has taken no further action against Exclusive Resorts pending the outcome of the bill.

We believe that Senate Bill No. 697 should not be enacted because it does not meet sunrise criteria requiring evidence of abuse. The bill is an unnecessary regulatory measure that would add little consumer protection. We also conclude that destination clubs should not be regulated under the State's Time Sharing Plan law since the provisions in the law are inappropriate for regulating their operations. The time share law was enacted to prevent rampant abuses early in the industry. These abuses are not characteristic of the operations of destination clubs. If the department chooses to enforce Chapter 514E, HRS, it would have to do so piecemeal as major provisions would have to be waived or modified. Finally, no other states regulate destination clubs under their time share laws.

Recommendations and Response

We recommend that:

1. The Legislature not enact Senate Bill No. 697, 2007 Regular Session.
2. The Department of Commerce and Consumer Affairs close its investigation of Exclusive Resorts and issue a no action letter regarding its regulation under the Chapter 514E, HRS, the *Time Sharing Plan* law.

The Department of Commerce and Consumer Affairs agrees that Senate Bill No. 697 is imperfect but believes that some type of regulation is needed to protect consumers, other than Chapter 514E, HRS. Nevertheless, the department presents no new evidence of consumer harm in the destination club industry or abuse similar to those found in the time share industry.

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