

Timeshare in Mixed Use Projects: Success and Risk Factors

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Mixed use projects with both a timeshare and hotel component are increasingly popular as the resort development project of choice. Given the many advantages of mixed use, the purpose of this paper is to present five keys to success as well as five risks associated with mixed use. An evaluation of these success and risk factors leads to the conclusion that the synergies and advantages of mixed use far outweigh the risks, which although must be addressed, can be properly accounted for and mitigated. Research pertaining to these keys to success and risk factors are a combination of analysis, insights, and findings obtained from timeshare and hotel industry executives.

Key for Success 1: Marketing Synergies

Timeshare development differs from traditional development in that timeshare development must bring the market to its product versus a traditional development bringing its product to the market. From a cost standpoint, this causes the cost of marketing a timeshare development to be significantly higher than a traditional development. It is common for marketing costs to approach 45-50% of revenues. Considering that a high percentage of the revenue is being consumed by marketing, uncovering areas that can lower the marketing costs by even a few percentage points translates into a tremendous savings and increased profit.

Mixed use developments that combine a hotel and timeshare component can create synergies for both components. From the viewpoint of the timeshare developer, the main synergy will be the linkage to the hotel guests. Fred Hawkins, managing director of South Seas Resort on Captiva Island, a MeriStar Resort, states, "*A developer has a built-in marketing magnet when [opening] a destination resort, they've come here, like what they've seen and make a vacation investment.*"¹ If a timeshare developers can get a hotel guest to tour their product, they can effectively save the money that would have been spent marketing to the contact. The money saved would come in the form of acquiring the contact information, marketing to the contact and a majority of the cost it takes to normally subsidize the contact during their visit. Considering the percentage of revenue associ-

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¹M.A. Baumann, "Hotel & Motel Management.", September 20, 1999, Dow Jones Interactive Volume 214; Issue 16

ated with marketing, this savings could substantially add to the development's bottom-line. Another way of lowering the marketing costs associated with timeshare development is access to the database maintained by the hotel. This access will provide the developer with lists of people who are familiar with the area and either like or are inclined to use the hotel brand associated with the development. This access will allow the developer to target these individuals and optimistically enjoy a higher capture rate than other contact lists would provide. The use of cross promotions that encourage visitors to the development are a potential win-win situation for both parties. *"Mixed-use developments also can optimize marketing efficiencies and cross promotions through lead-generation programs. The partnering can boost sagging hotel occupancy while housing potential timeshare purchasers."*² The ability for timeshare developers to house their prospective owners at a discounted rate can be a boon for their bottom line. When you consider that every dollar saved on marketing flows to income before taxes, it is in the developer's best interests to examine every opportunity to lower costs.

Key for Success 2: Management Company

An issue that has to be dealt with in a mixed-use development is the interaction between the different users. On one side, you will have a hotel user who expects a certain level of service. On the other, you have the timeshare owners who generally expect a different and altogether higher level of service. Stuart Woolley, Senior Vice President of Eagle Crest Communities and General Manager of Running Y Ranch Resort, states, *"There are higher expectations on the part of timeshare owners. Their purchase is driven by a comparison against renting hotel rooms, on a financial basis, but also a service basis. Timeshare owners expect a higher level of service commensurate with their investment, which can range from under \$10,000 to well over \$30,000 per one week equivalent. At the same time, their desire is not always for the same type of service typical of a hotel guest. For example, daily housekeeping service may conflict with the family-use schedule of the accommodations. Our company has successfully run a mixed use hotel for many years, but we have created a separate check-in facility for timeshare owners to help meet the need for a different service experience."*³ Besides different check-in facilities, there are other ways to ensure that the varied needs of the guest are met. Fred Hawkins of South Seas Resort, states, *"The property owner wants to be dealt with as a property owner. They have the same mentality as club members. This requires good communication among the developer, the homeowner's association and the owner to be effective. To address this issue, South Seas established an owner services department to act as ombudsman for owners. The team is dedicated to providing personalized service to its 5,000 owners."*⁴ To be successful in the mixed-use arena, it is imperative that the management company addresses the differing needs of each user.

²M.A Baumann, "Hotel & Motel Management.", September 18, 2000, Dow Jones Interactive Volume 215; Issue 16

³Stuart Wolley, Senior Vice President of Eagle Crest Communities, Interview December 3, 2002

⁴M.A Baumann, "Hotel & Motel Management.", September 20, 1999, Dow Jones Interactive Volume 214; Issue 16

The management company and the associated brand can also lend credibility to the timeshare component of the development. *“There is a historical perception of unscrupulous operators and sellers of vacation ownership intervals who, for example, have utilized high-pressure sales techniques and oversold floating intervals.”*⁵ The reputation of the management company can help to fix the tarnished image associated with timeshare operations. *“Vacation ownership projects are now being conducted by developers who are entering into relationships with hospitality companies and/or affiliation companies and the major hospitality players, including Embassy, Hilton, Marriott, Hyatt and Disney. These participants should result in a perception that the industry has been legitimized.”*⁶ The legitimized perception that the affiliation with these companies affords is invaluable. The affiliation can help in the financing of the development. The affiliation and the improved reputation could also make the difference between a pass and a sale.

Key for Success 3: Amenities

A major synergy and success factor to leverage off a timeshare/hotel mixed use project involves the shared amenities used by both the hotel guests and timeshare owners. A shared amenities complex truly offers mixed use developers/owners the opportunity to gain significant economies of scale from existing infrastructure. As Gustavo Ripol, Senior Vice President of product development for Raintree Resorts International points out, *“A symbiotic relationship lets timeshare owners share existing hotel amenities including restaurants, swimming pools, golf courses, retail outlets and 24-hour room service, enhancing the guest-service level.”*⁷ Importantly, guest services are very much enhanced thru more amenities that would otherwise not exist except for the fact that guest traffic has increased so much due to multiple customers in a popular mixed use destination that to not include these enhanced amenities would dilute the synergies and profitability/guest satisfaction level of the mixed use destination. As Fred Hawkins states, *“Cross-utilization of amenities and exposing traditional hotel guests to timeshare are advantages of mixed-use resorts.”*⁸ Interestingly, the positive synergies and enhanced services associated with the amenities on a mixed use project are a major draw in boosting timeshare sales and filling rooms as well as making guests and owners happy. Kristin Amarante reinforces this by saying, *“The question always is what can we do to make the guest experience more pleasurable? And the different alternatives for eating and entertainment add great value.”*⁹

⁵Vacation Ownership, Jeffer, Mangerls, Butler & Marmaro, March 1997, Ideas & Trends Hotel Online

⁶Vacation Ownership, Jeffer, Mangerls, Butler & Marmaro, March 1997, Ideas & Trends Hotel Online

⁷M.A Baumann, “Hotel & Motel Management.”, September 18, 2000, Dow Jones Interactive Volume 215; Issue 16

⁸M.A Baumann, “Hotel & Motel Management.”, September 20, 1999, Dow Jones Interactive Volume 214; Issue 16

⁹Kristin Amarante, More Money in Mixed Use, August 20, 2002.

Key for Success 4: Spreading Risks

How do mixed use projects spread out or reduce project risk? Simply put, timeshare units can be rolled out at different times and sold quickly, thus alleviating as much financing needs and importantly, build project value in the short-term and long-term. As Jim Butler of Jeffer, Mangerls, Butler, & Marmaro states, "...vacation ownership resorts can be built and financed in stages, allowing both developers and lenders to ease back into the resort development business a few units at a time; developers can develop a resort with a timeshare component that could not be developed as a hotel alone; and borrowers can sometimes refinance a bullet loan that otherwise may not be refinable in today's economic environment."¹⁰ In line with spreading out the risks is making better use of the amenities to ensure that they are used to their utmost potential, Mr. Butler said, "High-quality amenities cost a lot of money. The ability to spread out the use and the cost of the amenities — it's simple economics — makes it cheaper for everyone as long as the load isn't too great."¹¹

Furthermore, the idea of a mixed use project is that since the property is diversified between hotel and timeshare and hence, purchasers, the project is better able to weather any downturn, and revenue streams can be smoothed, thus removing some of the seasonality, which leads us to our next point.

Key for Success 5: Multiple Revenue Streams

Multiple revenue streams from profitable sources at a mixed use project are a key success factor. As previously indicated, mixed use projects benefit from numerous amenities and services, and therefore open up the door to grow cash flow from these businesses given the diverse and attractive traffic that visit or stay at the mixed use project. Additionally, a good portion of seasonality can be removed from operations given the multiple and diverse business components that cater to both hotel and timeshare users. As Gustavo Ripol said, "The scenario (of mixed use) also drives a constant flow of business from timeshare owners to hotel restaurants and retail outlets. The year-round occupancy can smooth out seasonal employment issues. There's no layoffs, rehires or retraining. The peaks and valleys in the staffing cycle are very small."¹² Additionally, this success factor gels well with also leading to success for the spreading of risks success factor. Allen Broek, President and CEO of the Mariner Group, Inc. said, "The advantage of a mixed use project is that it provides a variety of income streams during the course of development. That way, it is easier to assemble the complex deals and make the most of synergy to boost each of the included business components."¹³ The idea of leveraging multiple revenue streams is quite the "strategic formula" these days as Kristin Amarante elaborates on, "When the first properties to use this strategic formula opened to success because investors created multiple revenue streams, that attracted and dramatically increased foot traffic while also enhancing the guest experience..."¹⁴

¹⁰Vacation Ownership, Jeffer, Mangerls, Butler & Marmaro, March 1997, Ideas & Trends Hotel Online

¹¹Vacation Ownership, Jeffer, Mangerls, Butler & Marmaro, March 1997, Ideas & Trends Hotel Online

¹²M.A. Baumann, "Hotel & Motel Management.", September 18, 2000, Dow Jones Interactive Volume 215; Issue 16

¹³Allen Broek, President and CEO of the Mariner Group, Inc.

¹⁴Kristin Amarante, More Money in Mixed Use, August 20, 2002

Five Risks of Timeshare Mixed-Use Projects

In addition to the many keys to success, timeshare mixed-use facilities also have numerous amounts of embedded risk associated with each other that need to be addressed. The majority of these risks deal with coordination and interests among the developers, management companies, service contracts, and the different market segments to each facility. From development, operations, to exit, there exists a wide array of possible risk factors that any potential mixed-use developer needs to be aware of.

Risk 1: A Problem with One is a Problem with the Other

The timeshare project and the hotel act as one entity. When there is an issue which arises in hotel it will directly relates to the Timeshare project. Usually this is discussed as a benefit since mixed-use is touted as providing synergies and strengths between the projects, but this can also backfire as negatives. Success in one does lead to success in the other; failure in one also leads to failure in the other. For instance, if the hotel is a success then chances are the timeshare will benefit and be a success as well, but if the hotel should be a failure then the timeshare is sure to be one as well. Furthermore, any problems associated with one will be mirrored in the other. This can range from services such as housekeeping to hard issues such as utilities. Patrick McCudden, Vice President of Development at Marriott Vacation Club International states that *"The availability of amenities in the neighboring hotel are typically protected through a form of easement, however, services provided by the hotel to the timeshare project would be significantly affected in the event of a termination."*¹⁵ This statement reflects the idea that any issue, such as hotel management termination, would directly affect the timeshare's amenities and ability to sell future units. With a reduction in amenities, the timeshare portion would lose value. This would lead to a dramatic drop in sales as well as a rise in defaults from the timeshare owners.

In addition, the physical quality of one resort will severely affect the other. If the capital expenditures for the hotel decrease, then the hotel will start to deteriorate and drop in value. Also if the timeshare association does not maintain the property well, it will become an eyesore on the property and affect the hotel's ability to fill rooms. Both properties act as one and both must have a commitment to quality in order to benefit each other. Furthermore, the reputation of either the hotel or timeshare will definitely have an influence on the reputation of the other. If the hotel's reputation is a young singles scene then the timeshare will obtain the same reputation because of its association. Both parties must agree to a strategy and marketing campaign which has similar

¹⁵Patrick McCudden, Vice President of Development at Marriott Vacation Club Ownership, interview on November 27, 2002

target markets and yearns for the same reputation. A mixed-use facility is a single facility and the introduction of a hotel or a timeshare is not an automatic solution. Jim Butler states that *"Vacation ownership is not the cure for all problems—a failed hotel project will be a failed timeshare."*¹⁶

Risk 2: Two Different Teams

Two different teams in a mixed-use project create another level of coordination, add another player to the process, and add another level of complexity. The challenge facing mixed-use developers is to ensure that both groups communicate well and have shared interests. The two teams must operate as a united front with a common shared goal to minimize conflict. From the inception of the idea, both teams should meet to find a shared goal and work together during the development process to ensure the idea mutually benefits both parties. For instance, during the initial planning phase, the two teams will need to agree on what the basic product mix is between the hotel and the timeshare, or if there is room for both. When Marriott was planning on entering the Boston market, they needed to decide on an appropriate site mix and opted for just timeshare. *"Real-estate limitations can dictate the product form as well. Kinney said Marriott's recent purchase of a landmark Boston parcel could not facilitate a full-service lodging option because of its size. An urban timeshare concept was a viable business decision."*¹⁷ Based on the land constraints, Marriott as one owner was able to make a unilateral decision to not have a hotel component. On the other hand, the land may not be an issue and Marriott may need to produce a product mix through both teams. *"The way we try to approach it is to see what the best mix is,"* said Ed Kinney, director of advertising and communications for Marriott Vacation Club International. *"We have two development teams on both sides of lodging to determine what is going to be the best utilization of that land. We want to maximize yield of a particular property."*¹⁸ With these mixed-use properties both teams need to coordinate their goals in order to maximize the use of the property which may result in some compromises and conflict.

Risk 3: Timeshare Sales Depend on Hotel Performance

The success of the timeshare component of a mixed use development depends on the positive performance of the hotel in order to bring potential customers to the site, share amenities, and keep existing timeshare owners happy with their purchase. The largest risk is if the hotel management company is non-performing. This can result in not meeting construction schedules, maintaining amenities, or losing its contract as a result

¹⁶"Vacation Ownership", Jeffer, Mangerls, Butler & Marmaro, Ideas & Trends, Hotel Online March 1997

¹⁷M.A Baumann, "Hotel & Motel Management.", September 20, 1999, Dow Jones Interactive Volume 214; Issue 16

¹⁸M.A Baumann, "Hotel & Motel Management.", September 20, 1999, Dow Jones Interactive Volume 214; Issue 16

of poor occupancy. Patrick McCudden states that “*The failure of the hotel owner to complete the hotel project on time, or at all because of financial difficulties or cost overruns there (can affect timeshare). Typically there will be a different ownership group for each of the hotel and the timeshare projects. Timeshare owners, particularly Ritz-Carlton Club owners, would be greatly impacted as the amenities of the hotel (i.e.: spa, swimming pools, restaurants, etc) are a significant part of the amenity package expected by purchasers. Further, operations support for the timeshare portion are typically provided through the hotel. Lastly, there could be significant sharing of back-of-the-house space, utilities, i.e. condensers, hot water heaters, etc that could disrupt the operations.*”¹⁹ Mr. McCudden outlines a few practical concerns, such as amenities and services, in the operation of a mixed-use facility which can affect the sales performance of the timeshare as well as the happiness of the timeshare owners. Furthermore, a decrease in the quality of the amenities can cause an increase in the default rates of current timeshare owners, which can cause the timeshare developer to resell at a lower price and a loss. Failure of the hotel to perform can cause the timeshare development to have a loss in lead generation, lower sales, and higher default rates, and a loss of synergies in marketing. This can destroy the benefits of having a mixed-use facility in the first place.

Risk 4: Different Travelers’ Interests

Hotel guests typically are transient travelers and tend to be younger travelers in their 20’s and 30’s. Depending on the hotel location, an urban hotel would have more business travelers while a resort hotel caters more towards young adults and couples. Timeshare is about vacation ownership and is marketed to a group which takes vacations every year, which are families. A mixed use facility needs to have management staff which is capable of handling the needs of these different sets of travelers. As quoted before, Stuart Wolley, Senior Vice President of Eagle Crest Communities states that “*Timeshare owners expect a higher level of service commensurate with their investment which can range from under \$10,000 to well over \$30,000 per one week equivalent. At the same time, their desire is not always for the same type of service typical of a hotel guest. For example, daily housekeeping service may conflict with the family use schedule of the accommodations. Our company has successfully run a mixed use hotel for many years, but we have created a separate check-in facility for timeshare owners to help meet the need for a different service experience.*”²⁰ Eagle Crest Communities has successfully understood this difference and instead of one type of service for both, they are focusing their services specifically to the separate market segments.

Furthermore, the physical asset needs to coincide with the interests of these two different types of travelers. A mixed-use facility must understand what sort of facilities each group is interested in and decide if they can either share amenities or have separate ones. Nicholas M Weiner from Hotel Employees & Restaurant Employees states that “*Competition exists between the two travelers. They are a different type of customer and traveler and tensions can arise between travelers.*”²¹ This sort of competition can be caused by one group

¹⁹Patrick McCudden, Vice President of Development at Marriott Vacation Club Ownership, interview on November 27, 2002

²⁰Stuart Wolley, Senior Vice President of Eagle Crest Communities, Interview December 3, 2002

²¹Nicholas M Weiner from Hotel Employees & Restaurant Employees, Interview November 26, 2002

feeling alienated due to amenities which are not available to one or if a set of amenities are perceived as leaning towards one of the groups. If the mixed-use facility is not cognizant of these issues, this can be a risk which causes grief among the travelers and management.

Risk 5: Legal Issues

Legal issues in a mixed-use development stem from possible issues that may arise and complications created with a complex set of players and owners. One of the first risks has to do with possible conflicts over exit strategies for the hotel owner and the timeshare. What would happen if the hotel owner sells the property and what would the state of the current management company be? Are interests aligned with the exit strategies between the hotel owner and the timeshare management company? Hotels are typically short term hold periods while timeshare managers and developers continue to see revenue in the future besides the sale of the units. To combat this risk, the owner or owners need to have provisions in the contract which include legal stipulations to address these issues. In addition, there also needs to be provision which deal with possible change in the management company at the hotel that ensures a certain quality. Also, with a mixed use project there are many different service contracts, owners, management contracts, vendor contracts, associations, etc. which all have intertwined liability issues. *“Integration of a timeshare component with its mixed use setting often calls for attention to the legal relation among the various components including standards of maintenance/management of the various components, and assurances of continued access by the timeshare component to any other component deemed essential to the offering such as an adjacent golf course, hotel pool, or other outdoor or indoor amenities. Florida requires a combination of reasonable assurances and high standards of disclosure for consumer protection.”*²² This statement speaks to the complexity of legal issues between the hotel and timeshare that require coordination and standards. Furthermore this also extends the basic deal which is made between the hotel management company and the future timeshare association. *“The business deal negotiated between the developer and the franchise company may conflict with the provisions of the controlling timeshare (and possibly condominium) declaration, bylaws, rules and regulations, etc., as well as applicable federal and state laws (which will vary from state to state) relevant to the project. In addition, when franchise agreements are executed, the timeshare (and possibly condominium) associations may not yet be formed.”*²³ Both parties need to be cognizant of these legal coordination issues which result from new entities as a result of having a mixed use facility. Early agreements and up front negotiations can aid the different interests that are involved in a project to be aligned.

²²Robert M Chasnow, Trends in Florida Timeshare Regulations, September 1, 1999, Holland & Knight LLP

²³Vacation Ownership, Jeffer, Mangerls, Butler & Marmaro, March 1997, Ideas & Trends Hotel Online

Ultimately, these risk factors represent just that—risks, they must be taken into account and properly addressed. Marketing Synergies, management company, shared amenities, spreading risks, and multiple revenue streams are 5 synergies of mixed use resort development that make these projects viable and attractive. A problem with one is a problem with the other, two different teams, performance, different travelers, and legal complexities are issues which make mixed use resorts risky and complicated. Overall though, when the advantages, success factors, and benefits of mixed use (in the form of potential synergies realized, investor returns, hotel guest/timeshare owner satisfaction, etc.) are measured against these risk factors, properly planned and well-located mixed use projects are a superior destination format to single use resorts and hence offer a very compelling, and successful resort destination project for owners, hotel guests, and timeshare owners. Instead of just creating resorts, mixed use resort developments create places and memorable destinations for the hospitality industry.

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