Timesharing and Realty Interests Under the Martin Act: Consumer or Investor Protection?

Yvette C. Mendez

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TIMESHARING AND REALTY INTERESTS
UNDER THE MARTIN ACT: CONSUMER OR INVESTOR PROTECTION?

I. Introduction

The popularity of condominiums and cooperatives and other innovative types of real property ownership has resulted in the birth of the timeshare. A purchaser of a timeshare—a member—purchases any week or series of weeks in a condominium or cooperative for a term of years. The owner then conveys a right to use, either as a timeshare estate or a timeshare license. A timeshare estate conveys a right to occupy, coupled with a freehold estate or an estate for years. A timeshare license, while conveying a right to use, does not convey a freehold estate. The timeshare license, in particular, is based almost


The New York Condominium Act, codified at N.Y. REAL PROP. LAW, ART. 9-B, § 339-d et seq., was enacted in 1964, almost 6 years after Puerto Rico became the first United States jurisdiction to adopt a condominium statute. See N.Y. REAL PROP. LAW § 339-d (Practice Commentary) (McKinney 1989). The Act provides, inter alia, that each unit is real property. See id. § 339-g (McKinney 1989).

2. A cooperative apartment arrangement involves a hybrid proprietary interest of the owner consisting of shares of stock in a cooperative corporation and a proprietary lease. See Anton Sattler, Inc. v. Cummings, 103 Misc. 2d 4, 425 N.Y.S.2d 476 (1980).

Cooperative apartments are governed by N.Y. COOP. CORP. LAW § 1-134 (McKinney 1951 & Supp. 1990).

Cooperatives are regulated as securities since they are “cooperative interests in reality.” See infra notes 112-116 and accompanying text.

3. “Timesharing is a generic term used to describe the interval ownership of an interest in real property . . . . To date, most real estate time-sharing has involved recreational or resort property.” See CLURMAN, ET AL., CONDOMINIUMS AND COOPERATIVES 156 (2d ed. 1984); see also infra notes 4-8 and accompanying text.

4. See MODEL UNIFORM REAL ESTATE TIME-SHARE ACT § 1-102(14) (1985 & Supp. 1990) [hereinafter MURETSA]; see infra notes 33-38 and accompanying text. Since an estate-type timeshare involves fee ownership and is, consequently, a cooperative interest in realty, this Note will focus upon timeshare licenses, particularly vacation licenses and campground interests. For more information regarding timeshare estates see M. HENZE, THE LAW AND BUSINESS OF TIME SHARE RESORTS § 3.03 (1989) [hereinafter TIME SHARE BINDER]; Langer, “Fee time sharing,” and Penwell “Structuring Fee Timesharing Projects” in The Legal Aspects of Real Estate Timesharing, Practising Law Institute at 25-210 (1982).


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completely on the terms of the timeshare agreement. A purchaser's ability to convey or transfer his right, or even to choose the particular unit for use or occupancy, may be restricted by the contract. Moreover, since a "license" is established, the owner conveys no interest in the property.

Many states, concerned about marketing practices and the impact

6. See infra notes 41-46 and accompanying text.
7. See infra notes 47-69 and accompanying text.
8. However, if exclusive possession is conveyed, a lease rather than a license may be established by the contract. For a discussion of exclusive possession see infra notes 47-69 and accompanying text.
9. A major complaint in several states (and the cause of several lawsuits) involves the techniques used in the initial sales of the timeshares. State lawsuits against timeshare developers and marketers have included such allegations as: misrepresentation of gifts and prizes offered, misrepresentation of the purpose of the solicitation; failure to disclose material facts about the offering; 'high-pressure' sales; and even 'verbal abuse' of consumers.

Bloch, Regulation of Timesharing, reprinted in The Legal Aspects of Timesharing, supra note 4, at 298 [hereinafter Bloch].

The method by which a developer acquires prospective purchasers and the techniques surrounding the sale play an important role in determining whether community officials will accept or reject the industry as a whole. [For example] Hawaii recorded numerous public complaints arising from the manner and intensity of sales activities of persons associated with the industry. Visitors in the Waikiki district reportedly were being accosted by high-pressure salespersons on beaches, sidewalks, and other public areas. Consequently, the Hawaii timesharing statute was amended requiring [disclosure of] the principal office address, telephone number, and the responsible managing employee to the Director of Regulatory Agencies.

Bilbray, Local Regulation of the Resort Timesharing Industry, reprinted in The Legal Aspects of Timesharing, supra note 4, at 463 [hereinafter Bilbray].

[T]he National Timesharing Council (NTC) of the American Land Development Association has recently adopted a tough new code of ethics by which all members must abide. In an effort to demonstrate the industry's concern over the use of unethical practices by a handful of operators, NTC has assumed the role of the industry's toughest critic. As a result, continuing membership in NTC has become one meaningful way to judge a developer's commitment to fair and ethical practices.


The New York Attorney General is also concerned about marketing practices:

Timeshare sales are often characterized by high-pressure sales tactics and misleading advertising. Direct mail solicitations promising valuable premiums and prizes are often used to lure prospective purchasers to the timeshare project where they are subject to lengthy, deceptive presentations. Many people quickly come to regret their purchase but have no way out.

ATTORNEY GENERAL LEGISLATIVE MEMO, No 298-89, at 2.

The New York State Attorney General's jurisdiction under General Business Law § 352-e extends to out-of-state developers entering the state to advertise or offer property sales in other states. N.Y. GEN. BUS. LAW § 352-e(1)(a) provides: "It shall be illegal . . . for any . . . corporation . . . to make or take part in a public offering or sale in or from the state of New York . . ."; see also Ledgebrook Corp. v. Lefkowitz, 77 Misc. 2d 867, 354
of timeshare units on the neighborhood, have enacted enabling and regulatory provisions. These statutory controls vary according to each state and take the form of timeshare laws, subdivided land sales acts, real estate commission acts, securities laws, "little FTC" acts and consumer protection acts.

New York State has chosen to regulate timesharing through its securities laws. New York’s Blue Sky Law, otherwise known as the

N.Y.S.2d 318, 320 (1974); In re Cenvill Communities, 82 Misc. 2d 418, 419, 372 N.Y.S.2d 281, 284 (1975) ("Martin Act provisions apply equally to property located within and without the State provided it is offered for sale in New York").

The Attorney General, under the authority granted it under General Business Law § 352-3(6), has also promulgated extensive regulations regarding condominium offerings within the state. See N.Y. COMP. CODES R. & REGS. tit. 13, §§ 19.1 et seq.

10. Local governments have exhibited concern to many aspects of community life, such as the impact on local housing, employment, public services, schools, police and fire protection, transportation, parks and recreational facilities, noise and air quality, etc. See Bilbray, supra note 9, at 461-62.

11. For an in depth state-by-state discussion of varying enabling and regulatory provisions, see TIMESHARE BINDER, supra note 4, at § 9.03[2]; see also Bloch, supra note 9, at 291.

12. For a classification of various state laws, see Ingersoll, State Regulation of Timesharing, reprinted in The Legal Aspects of Timesharing, supra note 4, at 321 [hereinafter Ingersoll].

13. See Bloch, supra note 9, at 292; see also Ingersoll, supra note 12, at 321; Bilbray, supra note 9, at 461.


It is unclear, however, whether ILSFDA applies to timeshare units, especially right-to-use licenses. "Lot" is defined as "any portion, piece, division, unit, or undivided interest in land located in any state or foreign country if the interest includes the right to the exclusive use of a specific portion of the land." See 24 C.F.R. § 1710.1 (1987). Regarding campground interests, the issue of exclusive possession is controlling. See infra notes 55-100 and accompanying text.

14. New York’s position of securities regulation of timeshares is the minority position; most states consider timeshares as an interest in real estate. For a discussion of New York’s minority view, see MADISON & DWYER, supra note 9, at §§ 10-16.

Nevertheless, "The staff of... [New York State’s] Department of Law has long indicated that any form of timesharing may be considered such a 'cooperative interest' [in reality]." See Bloch, supra note 9, at 298. Moreover, "[Martin Act] language is broad enough to include offerings of many types, including... various types of time sharing arrangements...." See N.Y.GEN. BUS. LAW § 352-e (Practice Commentary) (McKinney 1988).

15. "Since 1911, most states have enacted some form of legislation, generally known
Martin Act,\(^\text{16}\) requires the filing of an offering plan with the Attorney General for any “participation interests or investments in . . . real estate ventures . . . including cooperative interest in realty . . .”\(^\text{17}\)

“Cooperative interests in realty” include any individual ownership in cooperatives, condominiums and homeowner associations.\(^\text{18}\) Timeshare licenses, however, do not convey fee or individual ownership in property.\(^\text{19}\) Consequently, such licenses do not constitute cooperative interests in realty, despite indications from the Department of Law that timeshares may be considered such.\(^\text{20}\)

Timeshare licenses, however, may qualify as “participation interests in realty” under the Martin Act. Since the statute does not clearly define the term, great emphasis is placed upon the court’s interpretation of what constitutes a participation interest in realty. Specifically, it is unclear what role the potential for profit plays in determining participation interests.

The New York Court of Appeals has attempted to define participation interests in realty by engaging in an “investment contract” analysis, with an emphasis on profit potential.\(^\text{21}\) In *All Seasons Resorts v. Abrams (ASR III)*,\(^\text{22}\) the court held that the potential for profit was an essential element in determining participation interests.\(^\text{23}\) At issue, then, is whether a timeshare license that provides no potential for profit constitutes a participation interest in realty, and thus is subject to regulation under the Martin Act.

This Note will explore the property interests created by timeshare

\(\text{as Blue Sky Laws, regulating the issuance and sale of securities.) See I Loss, Securities Regulation 30 (2d ed. 1961); See also 47 A.L.R.3d 1378, § 2.}\)

\(\text{16. The statute was named after Assemblyman Martin, who introduced the bill in 1921. It passed by unanimous vote in the same year. N.Y. Gen. Bus. Law § 352-e (Practice Commentary (McKinney 1988)).}\)

\(\text{17. See infra note 105 and accompanying text.}\)

\(\text{18. From its use elsewhere in our statutory law, the phrase 'cooperative interest in realty' has acquired a meaning which includes cooperatives, as the term is usually understood, condominiums and interests in real estate owned through home-owner associations . . . The common element in . . . [cooperatives, condominiums and homeowner associations is] that the individual holds some ownership interests in the property.}\)


\(\text{19. See infra notes 39-40 and accompanying text; see also supra notes 5-8 and accompanying text.}\)

\(\text{20. See supra note 14 and accompanying text.}\)


\(\text{22. In ASR III, the Court of Appeals reversed the Third Department which had held that the potential for profit was a non-essential element. See All Season Resorts v. Abrams (ASR II), 491 N.Y.S.2d 516 (3d Dep't 1985), rev'd, 506 N.Y.S.2d 10 (1988).}\)

\(\text{23. Id.}\)
licenses in New York, advocating that a participation interest in realty is created and that the Martin Act is applicable to these licenses. Part II discusses the interests created by timeshare licenses as they relate to the real property concepts of license and lease. Part III examines the provisions and purpose of the Martin Act and the application of the profit potential theory to define the realty interests requiring the Act's protection. Part IV advocates legislative and case law alternatives to the New York "profit potential" approach. As a case law alternative, the risk-capital theory, which focuses on "valuable benefit" rather than "profit potential" will be discussed. As a legislative alternative, proposed legislation General Business Law § 352-eeeee, classifying timeshares as participation interest in realty, will also be addressed and advocated. This Note concludes in Part V that timeshare licenses are participation interests in realty, creating a property interest, regardless of profit potential, which requires consumer protection under the Martin Act.

II. Interests Created In Timeshare Licenses

A. History and Construction of Timeshare Interests

Timeshare arrangements originated in Europe in the late 1960s as a method of structuring vacation housing. The idea quickly spread to the United States in the 1970s, with the first large scale project appearing in Hawaii in 1971. By 1982, growth records estimated that 600 timeshare projects existed, with 20,000 operational units and sales

25. "Vacation timesharing began in Europe in the early 1960s. Marketed under the name 'Eurotel,' individuals could purchase the right to the exclusive use of a vacation facility for a specified period each year over a number of years." Madison, supra note 9, at § 10-2; see also Real Estate Law Newsletter, 11 Colo. Law. 1543 (1982) [hereinafter Real Estate Law Newsletter].
26. "Timesharing was a way for developers to market their previously unsaleable condominium projects. Since a prospective purchaser could not afford to buy a whole condominium, why not sell him a right to use that unit once or two weeks per year for a period of years?" See P. Rohan, Condominium Law and Practice, § 17C.01 (1972); cf. Madison & Dwyer, supra note 9, at S10-2.

One commentator attributes timeshare development to the recession of 1976, when "developers . . . needed a highly leveraged 'bail out' of their failing projects . . ." Real Estate Law Newsletter, supra note 25, at 1543. Cf., Annotation, Regulation of Timeshare Interval Ownership Interests in Real Estate, 6 A.L.R. 4TH 1288, 1289 n.2. [hereinafter Ownership Interests].

27. The Hawaiian project contained about 150 units. Timeshare Binder, supra note 4, at 1-3.
volumes approaching 1.5 billion dollars. In 1988, commentators estimated that timeshare owners in the United States numbered 400,000. Created by contract, these timeshare arrangements confer certain rights of possession upon the purchaser, usually based upon an underlying condominium or cooperative arrangement.

Many states have enacted legislation to protect the interests of the community in the structure of timeshare arrangements. These laws vary from state to state, but most, at least in structuring timeshare arrangements, abide by a uniform act: either the Model Uniform Real Estate Time-Share Act (MURETSA), or the ALDA/NARELLO Act. MURETSA offers a comprehensive definition of timeshare interests, establishing two types of timeshare arrangements. Timeshare estates involve a right to occupy, coupled with a freehold estate or an estate for years. Since fee ownership is conveyed, the buyer holds a deed to the property and assumes all the rights that accompany fee ownership, such as the ability to deduct interest and real estate tax payments, to build up equity and to convey, devise, or transfer his interest.

28. "Since 1975 timesharing in the United States has grown into a billion-dollar industry." MADISON, supra note 9, at S10-2, n.69.

29. MADISON & DWYER, supra note 9, at S10-2.


31. See supra notes 9-13 and accompanying text.

32. See supra notes 11-13 and accompanying text.

33. MURETSA, developed by the National Conference of Commissioners on Uniform State Laws and approved by the American Bar Association, offers a detailed and lengthy approach to the timesharing concept. See TIMESHARE BINDER § 10.02[1], supra note 4, at 10-5; see also Bloch, supra note 9, at 291.

34. The ALDA/NARELLO ACT was the first uniform time share act, developed during the late 1970s by the National Time Sharing Council of the American Land Development Association (ALDA) together with the National Association of Real Estate License Law Officials (NARELLO). The Act was adopted in its entirety by Nebraska, and used as a basis in the formulation of laws in several other states, including Florida, Hawaii, Tennessee and Virginia. The Narello Act treats timesharing as separate from real property or contract law and is criticized as insufficient because the Act offers "nothing indicating how the plans are to be construed . . . and the courts are forced to resort to the application of common law principles." See TIMESHARE BINDER § 10.02[1], supra note 4, at 10-5.

35. See supra note 4 and accompanying text.


38. Id at 18-19; MADISON & DWYER, supra note 9, at S10-4.
Unlike a timeshare estate, a timeshare license is not coupled with a freehold estate or an estate for years. The purchaser’s rights are determined almost exclusively through the written contract. Therefore, the purchaser’s ability to convey his interest may be limited through the contract provisions. For example, the contract may prohibit conveyances without management approval, as well as restrict or prohibit profits on a conveyance. Some contracts allow a buyer to select a particular unit to be occupied, while others place in the manager the power to select the particular unit upon notification by the buyer of an intent to occupy some unit. In short, the interest in property in a timeshare license varies widely according to the terms of the agreement.

B. Preserving Concepts of Real Property Licenses

Timeshare licenses are usually consistent with the real property concept of a license or a lease. A license is “a privilege to do one or more acts on the land, without having an interest therein. As a general proposition, it is personal to the licensee, is not assignable by him and is revocable by the licensor.”

39. See supra note 5 and accompanying text.
41. See Rohan & Furlong, supra note 30, at 17. MURETSA also provides for the rescission of a contract due to unconscionability. See MURETSA § 1-105, Unconscionable Agreement or Term of Contract.
44. “[T]he inclusion of a clause in a sales contract . . . prohibiting resales of timeshares at a profit will protect the developer from any misunderstanding [regarding] the investment sales pitch.” See Bloch, supra note 9, at 307; see also ASR III, 68 N.Y.2d 81, 86, 497 N.E.2d 33, 35, 506 N.Y.S.2d 10, 12 (1988), where “[t]he price paid on a transfer [could] not exceed the original purchase price plus the reasonable cost of the transfer.”
45. Some licenses do not allow members to specify the dates of occupancy in advance but require reservations. See Nevada v. Carriage House, 94 Nev. 707, 709, 585 P.2d 1337, 1338 (1978); see also Cal-Am, 104 Cal. App. 3d at 456, 163 Cal. Rptr. at 731; ASR III, 68 N.Y.2d at 86, 497 N.E.2d at 35, 506 N.Y.S.2d at 11-12.
46. See supra note 41 and accompanying text.
47. See infra notes 49-54 and accompanying text.
48. See infra notes 72-74 and accompanying text.
Because a license does not convey or imply an interest in the land, a license is the lowest order of privilege touching or affecting real property. Timeshare contracts are treated as timeshare licenses when they contain rights that are limited regarding alienability and exclusive possession. In fact, many owners and developers will limit the interests conveyed to the purchaser, insuring the creation of a license and avoiding federal and state regulations. By limiting the interests conveyed, regulation of the license is also limited. In some cases "[t]he various types of [right to use] timesharing were developed to escape federal and state regulations governing the marketing of securities or interests in real property." Some contracts, however, provide additional rights which ultimately destroy the license-nature of the arrangement. For example, where the contract allows purchasers to choose the particular unit of use or occupancy, such an allowance creates a right of exclusive possession. Any conveyance of exclusive possession of the premises as against the whole world, including the owner, creates not a license, but an irrevocable estate or interest in land.

Whether or not exclusive possession or control of any specific area is granted is of great importance in determining whether a license or lease is constituted. If a contract confers exclusive possession as against the whole world, it is a lease; but if it merely confers a privilege to use or occupy under the owner, it is a license.

50. Id.
52. See supra note 49 and accompanying text.
53. "[A]voidance of both federal and state securities is difficult. If a membership time-shared offering can be structured... then it is possible for the offeror to avoid costly and time-consuming securities regulation... [o]bviously, every offeror should seek qualified advice at an early stage of project evolution to determine whether securities problems exist, and if so, whether it is possible to structure the offering so as to avoid such problems." Ellsworth & Prendergast, Securities Maze Awaits Resort Time-Share Offerings, reprinted in The Legal Aspects of Real Estate Timesharing, supra note 4, at 403, [hereinafter Ellsworth & Prendergast]; see also TIMESHARE BINDER § 3.02[a][a], supra note 4, at 3-6.
54. Rohan & Furlong, supra note 30, at 17; see supra notes 41, 53 and accompanying text.
55. See infra notes 56-69 and accompanying text. Where exclusive possession is created, the Interstate Land Sales Full Disclosure Act may apply, requiring filing of statement of record and property report. See supra note 13 and accompanying text for a discussion of ILSFDA applicability to condominium sales.
Consequently, many owners and managers structure the contract to eliminate any signs of granting a right of exclusive possession.\(^{58}\)

At least one court has held that the right of exclusive possession is created with the specification of weeks for use or occupancy together with a defined and specific right to occupy.\(^{59}\) In *Cal-Am v. Department of Real Estate*,\(^{60}\) members purchased up to four one-week time share interests, but were not entitled to reserve particular units.\(^{61}\) The developers, RHAC, assigned the particular units, although members specified dates, making reservations at least sixty days in advance.\(^{62}\) Members could transfer their interest with the consent of RHAC and bequeath their interest without consent.\(^{63}\) The California Court of Appeals found that an interest in real property was created by the club memberships: \(^{64}\) "[d]espite [RHAC's] contentions, the fact that RHAC retains the right to specify which unit will be occupied . . . does not derogate the exclusive possessory interests of the members during their annual periods of one to four weeks."\(^{65}\)

The court considered any type of exclusive occupancy "even for only a portion of each year . . . [as placing the occupant in] a special position with relation to a portion of the condominium premises . . . it is an estate or interest or possessory interest in the property itself."\(^{66}\) Retention by the seller of the right to specify units and provide maintenance did not alter the nature of the exclusive possession.\(^{67}\) The buyer's specification of dates of occupancy, together with the contractual right to occupy a unit, gave a right of exclusive possession suffi-
cient to constitute an interest in real property. The memberships were, therefore, more like leases than licenses.

Arguably, according to the court's reasoning, a hotel room reservation could also be considered as conveying a right to exclusive possession because the reserving party has the right to occupy a unit on dates specified by that party. A hotel room reservation, however, does not rise to the level of the property interest involved in *Cal-Am* because the buyers in *Cal-Am* had a right to exclusive possession of the unit, whereas a hotel occupant's rights of possession are limited by those of the hotel owner. Furthermore, a person who sues for breach of a timeshare contract can recover expectancy damages, whereas a consumer who sues for breach of a hotel room reservation can only recover any downpayment or out-of-pocket expenses he actually made. Thus, unlike the contract in *Cal-Am*, a hotel room reservation confers only a license, i.e., a right to use or occupy a unit of real estate.

C. Creation of Leases and Hybrids

A lease creates a present interest and estate in land by conveying a right of exclusive possession in the lessee as against the world (including the lessor) for purposes not prohibited by terms of the lease. A contract, therefore, which allows for exclusive possession, either through choice of units, specification of dates or the ability to convey the interest to another, may be considered a lease, rather than a license, creating an interest in property.

The *Cal-Am* court, however, was unwilling to classify the memberships as leases, saying, "[i]t is unnecessary to assign a name to the interest thus created." The element of exclusive possession, however, established an interest in the property itself, similar to a lease-

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68. *Id.* at 458, 163 Cal. Rptr. at 732.
69. "While it is unnecessary for the purposes of this appeal to classify the interest in real property thus created, the nature of the interest is that of a lease." *Id.* at 457, 163 Cal. Rptr. at 732.
70. See supra note 66 and accompanying text. For a discussion of innkeeper/guest liability regarding reservations, see Dickerson, *Travel Consumer Fraud: Rip-Offs and Remedies*, 28 Syracuse L. Rev. 847 (1977) [hereinafter *Travel Consumer Fraud*]; see also Kellogg v. Commodore Hotel, 187 Misc. 319, 64 N.Y.S.2d 131 (1946).
71. See *Travel Consumer Fraud*, supra note 70, at 860-62.
72. See supra notes 56-57 and accompanying text.
74. See also 49 N.Y. Jur. 2d, § 199.
75. See supra notes 55-69 and accompanying text.
76. *Cal-Am* Corp. v. Dep't of Real Estate, 104 Cal. App. 3d 453, 457, 163 Cal. Rptr.
hold. "Regardless of the term used to describe the purchaser's rights of exclusive occupancy, it is an estate or interest or possessory interest in the property itself."\(^7\)

In *State of Nevada v. Carriage House*,\(^7\) however, the court held that neither a license nor a lease was created in a timeshare arrangement. In *Carriage House*,\(^7\) members purchased a contractual right to reserve a suite for occupancy seven days each year, but were not entitled to make reservations for particular dates or units.\(^8\) The memberships were irrevocable, transferrable by gift, devise or consent of the management,\(^8\) and subleases and rentals were prohibited.\(^8\) The interests lasted for the useful life of the building, estimated at forty to sixty years.\(^8\) The court held that the memberships "fail[ed] to achieve the status of an interest in real property"\(^8\) because the interests created by the agreements defied the real property concepts of license and lease. "Indeed, it is not a license as defined by the law of real property, because it is irrevocable and transferrable. Nor is it a lease because it is not definite as to its duration or description of the property involved."\(^8\) The court did not specify what type of interest was created by the agreements, although it concluded that the legislature should amend the statutes to adequately regulate timeshare interests.\(^8\)

The *Cal-Am* court distinguished the result in *Carriage House* on the facts of both cases.\(^8\) The *Cal-Am* arrangements resembled leases not just because members held a right to occupy together with power to specify dates, but also because the dates of duration were so specific, much like leases which are specific as to duration.\(^8\) RHAC members held their memberships until exactly December 31, 2041. This date

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729, 732 (quoting Estate of Pitts, 218 Cal. 184, 191, 22 P.2d 694, 697 (1933)) (citations omitted).
77. *Id.* at 457, 163 Cal. Rptr. at 732.
79. *Id.* at 707, 585 P.2d at 1337.
80. *Id.* at 709, 585 P.2d at 1338.
81. Carriage House Associates was the management body. *Id.* at 709, 585 P.2d at 1338.
82. *Id.*
83. *Id.*
84. *Id.* at 709-10, 585 P.2d at 1339.
85. *Id.* (citations omitted).
86. The court construed NRS ch. 119 and 645 which delineate licensing requirements for interests in real property. *Id.* at 708, 585 P.2d at 1338.
88. *Id.*
was so specific as to resemble a lease. In *Carriage House*, however, the court pointed out, the members held their interests for the useful life of the building, which is an estimated period rather than a specific duration. Leases cannot be ambiguous regarding duration. According to both *Cal-Am* and *Carriage House*, leases specify dates and duration and convey a contractual right to occupy. When a timeshare agreement possesses these elements, it will be held to constitute a lease, thereby conveying an interest in the property.

Ability to convey one's right to occupy may also evidence exclusive possession. The contract provisions control the type of timeshare created by delineating a freehold estate or a license. Conveyance provisions usually accompany only the estate-type timeshares, since an estate in fee is created. Indeed, with estate-type timeshares, the contract need not provide for conveyances, since a deed is transferred to the purchaser. Some license-type timeshare contracts allow limited conveyances. For example, in *Carriage House*, members could transfer their interests by gift or devise or with the written approval of the management. The court found no property interest existed. In *All Seasons Resorts v. Abrams (ASR III)*, members were not allowed to transfer or convey their interests within two years of acquisition, except to family members; thereafter, only two transfers were allowed and resale could occur only once. The Court of Appeals held that a property interest did not exist. The court looked to the conveyance provisions in the contract for some intent to give exclusive possession. The restrictions on conveying or transferring one's membership in *ASR III* defeated a property interest by eliminating an investment opportunity: "To prevent the acquisition or sale of memberships for investment purposes, the agreement imposes restrictions upon the alienation of memberships."

89. *Id.*
90. *Id.*
91. See supra notes 59-85 and accompanying text.
92. See supra notes 59-69 and accompanying text.
93. See supra notes 42-46 and accompanying text.
94. See supra notes 35-38 and accompanying text.
95. See supra notes 35-38 and accompanying text.
96. *Id.* at 709, 585 P.2d at 1338.
97. *Id.* In *Cal-Am*, however, members could only transfer their interests by bequest or with consent of RHAC. There the court found no property interest existed. See supra notes 76-77 and accompanying text.
99. *Id.* at 85-86, 497 N.E.2d at 35, 506 N.Y.S.2d at 12.
100. *Id.* at 86, 497 N.E.2d at 35, 508 N.Y.S.2d at 12.
101. *Id.* For discussion of exclusive possession as an interest in real property, see supra notes 55-77 and accompanying text.
III. Martin Act Protection And Realty Interests

The type of interest created in realty determines whether it must conform with New York's Blue Sky Law, also known as the Martin Act. Created to protect the public from fraudulent exploitation in the offer and sale of securities, the Martin Act, by its provisions, also governs the real estate market. Section 352-e of the General Business Law provides:

It shall be illegal and prohibited for any person, partnership, corporation, company, trust or association, or any agent or employee thereof, to make or take part in a public offering or sale in or from the state of New York of securities constituted of participation interests in real estate, mortgages or leases, including stocks, bonds, debentures, evidences of interest or indebtedness, limited partnership interests or other security or securities as defined in section [352] of this article, when such securities consist primarily of participation interests or investments in one or more real estate ventures, including cooperative interests in realty, unless and until there shall have been filed with the department of law, prior to such offering, a written statement or statements, to be known as an "offering statement" or "prospectus" concerning the contemplated offering.

The statute confers jurisdiction upon the Attorney General over any realty or securities offerings within and outside of New York State made through advertisements, mailings, etc. The Attorney General has the duty to prevent fraudulent practices by launching investigations, invoking injunctive relief, and pursuing criminal prosecu-
Because the Act does not define the terms "securities," "participation interests in realty," or "cooperative interests in realty," the Attorney General's jurisdiction over license-type timeshare agreements is questionable. For example, if a timeshare agreement conveys some right to exclusive possession, it may convey a "participation interest in realty," requiring the developers to file a prospectus and comply fully with the disclosure requirements under General Business Law section 352-e. Conversely, timeshare agreements that possess license characteristics and do not convey any elements of exclusive possession retain their license status, convey no "participation interest in realty" and need not comply with these disclosure requirements. Thus, in order to determine whether the Martin Act applies, the courts examine the terms of the timeshare agreement to discern a participation interest or cooperative interest in realty.

A. Cooperative Interests in Realty and Individual Ownership

New York Courts have provided little assistance in defining the realty interests within the Martin Act. The All Seasons court, however, did directly address the issue of cooperative interests in realty. There, the court held that cooperative interests in realty require a conveyance of individual ownership or an individual interest in the property as evidenced by ownership of units, stock or shares. Co-operatives, condominiums and homeowner associations each convey ownership interests which qualify them as cooperative interests in realty. The Court held, however, that the All Seasons memberships did not so qualify because none of the ownership elements were present.

B. Investment Contract Theory of Profit Potential and Participation Interests

The "investment contract theory," espoused by the Supreme Court of New York, 111 for Martin Act violations.112

111. See id. §§ 352-d, 358.
112. "[T]he Martin Act confers upon the Attorney General some of the broadest and most potent investigative powers." See N.Y. GEN. BUS. LAW § 352-e (Practice Commentary) (McKinney 1988).
114. See supra notes 18-20 and accompanying text.
115. Id.; see also ASR III, 68 N.Y.2d at 90-91, 497 N.E.2d at 38, 506 N.Y.S.2d at 15.
116. Id. 68 N.Y.2d at 91, 497 N.E.2d at 38, 508 N.Y.S.2d at 15. See infra notes 136-48 and accompanying text.
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in \textit{SEC v. Howey}, \textsuperscript{118} is inexorably linked to the securities field. There, the Court held that the major consideration in determining whether or not a security exists is the role that profit or investment plays in the venture, i.e., whether the arrangement is an "investment contract" \textsuperscript{119} negotiated by the buyer for profit rather than merely for housing. Profit potential, therefore, is presently the \textit{basis} for defining a security interest within the securities field. \textsuperscript{120}

The Martin Act, however, applies not only to traditional securities interests such as those contemplated by the Court in \textit{Howey}, but also to interests in realty. \textsuperscript{121} Where the federal securities laws might not regulate certain securities because they have no potential for profit, such securities might fall within the scope of the Martin Act because they constitute "cooperative interests in realty" or "participation interests in realty." Such was the case in \textit{United Housing Foundation v. Forman}, \textsuperscript{122} where the Court, construing the federal securities laws, applied the investment contract analysis. \textsuperscript{123} The Court held that cooperative interests in realty did not constitute securities because the purchasers were more interested in housing than making a profit from their investment. \textsuperscript{124} In \textit{Forman}, the tenants of Co-op City in New York alleged federal securities and civil rights violations in the sale of common stock to the United Housing Foundation. \textsuperscript{125} The tenants, in order to occupy an apartment, were required to purchase eighteen shares of stock per room. \textsuperscript{126} The shares, explicitly tied to the apartment, could not be transferred to a non-tenant, nor pledged or encumbered. \textsuperscript{127} No voting rights attached to the shares, and the shares descended only to surviving spouses. \textsuperscript{128} Tenants wishing to move had to offer their shares to the developer at the initial price, and in any event, could not resell shares at a profit. \textsuperscript{129}

The Court, reversing the Second Circuit, \textsuperscript{130} engaged primarily in the investment contract analysis, based upon Congressional intent in

\begin{itemize}
\item \textsuperscript{118} 328 U.S. 293, \textit{reh'g denied}, 329 U.S. 819 (1946).
\item \textsuperscript{119} The \textit{Howey} Court defines an investment contract as: "a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party." \textit{Id}. at 298-99.
\item \textsuperscript{120} \textit{See supra} notes 117-18 and accompanying text.
\item \textsuperscript{121} \textit{See supra} note 105 and accompanying text.
\item \textsuperscript{122} 421 U.S. 837, \textit{reh'g denied}, 423 U.S. 884 (1975).
\item \textsuperscript{123} \textit{Id}. at 851-54.
\item \textsuperscript{124} \textit{Id}. at 854.
\item \textsuperscript{125} \textit{Id}. at 840.
\item \textsuperscript{126} \textit{Id}. at 842.
\item \textsuperscript{127} \textit{Id}.
\item \textsuperscript{128} \textit{Id}.
\item \textsuperscript{129} \textit{Id}. at 842-43.
\item \textsuperscript{130} \textit{Id}. at 847.
\end{itemize}
enacting the Securities Acts. The primary purpose of the Acts of 1933 and 1934 was to eliminate serious abuses in a largely unregulated securities market. The focus of the Acts is on the capital market of the enterprise system: the sale of securities to raise capital for profit-making purposes . . . . The Court found, therefore, that "the inducement to purchase was solely to acquire subsidized low-cost living space; it was not to invest for profit."  

The subsidized realty interests in Forman, however, qualify as cooperative interests in realty under the Martin Act and, therefore, would require filing with the Attorney General. Unlike the federal securities acts at issue in Forman, the Martin Act explicitly applies to cooperatives, condominiums and homeowner associations, regardless of profit potential. License-type timeshare agreements, however, introduce a different concept: whether an ownership interest, similar to that present in cooperative or condominium arrangements is created by the timeshare agreement, requiring the application of the Martin Act. Under the federal securities laws, such timeshares would not constitute securities unless a potential for profit is present. Since New York State expressly included these realty interests in the Act, profit potential could not have been the only criteria for determining the existence of a security. Thus, one can infer a legislative intent to protect purchasers of real estate regardless of profit potential.

Recently, however, the New York Court of Appeals, applying the investment contract theory, held that timeshare licenses which do not involve a profit margin, but involve mere use or occupancy do not involve the Securities Acts. The primary purpose of the Acts of 1933 and 1934 was to eliminate serious abuses in a largely unregulated securities market. The focus of the Acts is on the capital market of the enterprise system; the sale of securities to raise capital for profit-making purposes . . . . The Court found, therefore, that "the inducement to purchase was solely to acquire subsidized low-cost living space; it was not to invest for profit."  

The Martin Act, however, is designed to protect consumers from fraudulent practices and explicitly enumerates "cooperative interests in realty" as within the purview of the Act. See supra notes 105-07 and accompanying text.  

See supra notes 117-18 and accompanying text.
require Martin Act protection.137 In ASR III,138 buyers were offered membership in campgrounds outside of New York State. No right or interest in the property was conveyed, nor any share of income or gains or voting rights in the campground.139 Members could only transfer their memberships to family members within the first two years, and thereafter were restricted to two transfers and only one sale.140 The court, applying an investment contract analysis, construed “participation interests in realty” to require some type of investment contract.141 “It is significant that ‘participation interests’ are treated in the statute not as a separate category but as being equivalent to and virtually synonymous with ‘investments.’ Wherever the words ‘participation interests’ appear in the statute they are paired with the word ‘investments’ in the phrase ‘participation interests or investments.’”142 The court held that where an interest in realty is created which does not include an interest in profit-making or investments, protection from the Martin Act is not required.143

The Third Department, however, considering the same case, found no necessary correlation between participation interests and profit potential or investments.144 In All Seasons Resorts v. Abrams (ASR II),145 the court found that a very narrow reading of the Martin Act’s protection resulted from the undue emphasis placed on profit potential and investment.146 “The fact that the [l]egislature included participation interests along with the phrase ‘cooperative interests in realty’ indicates that it intended that the statute cover non profit or ‘consumer-type’ securities as well as investment securities.”147 Continuing its analysis, the court construed the Act broadly, advocating that the Act’s purpose was to protect the public, regardless of profit potential.148 The court noted that a participation interest was created

138. Id.
139. 68 N.Y.2d at 85, 497 N.E.2d at 35, 506 N.Y.S.2d at 12.
140. Id. at 85-86, 497 N.E.2d at 35, 506 N.Y.S.2d at 12.
141. Id. at 89, 506 N.Y.S.2d at 14, 497 N.E.2d at 37.
142. Id.
143. Id.
145. Id.
146. Id.
147. Id. at 191, 491 N.Y.S.2d at 518, rev’d, 68 N.Y.2d 81, 497 N.E.2d at 33, 506 N.Y.S.2d 10.
148. “[The Martin Act] should be flexibly interpreted to effectuate its purpose to afford potential investors, purchasers and participants an adequate basis upon which to found their judgments.” Id. at 192, 491 N.Y.S.2d at 519, rev’d, 68 N.Y.2d 81, 506 N.Y.S.2d 10, 497 N.E.2d 33.
because the buyers had an interest in the financial well-being of the property and the All Seasons organization itself.  

Application of an investment contract analysis, which the Howey Court extracted from the federal securities laws, is inappropriate in New York, where the Martin Act, unlike the federal securities laws, includes realty interests in its definition of "security." The Third Department accurately assessed the consumer protection nature of the Act, broadly construing its provisions to render protection to those consumers who invest money without intention of receiving a profit. The federal securities laws were created, according to Forman and Howey, to offer protection against fraudulent practices for "investment contracts." The Martin Act, by including realty interests, applies its protections beyond "investment contract" situations to the context of realty interests.

IV. Case Law and Legislative Alternatives

A. Risk-Capital Analysis As A Case Law Alternative

Rather than apply the investment contract analysis, many state courts engage in a risk capital analysis of the realty interest. In applying the risk capital analysis, the court considers the "valuable benefit" inuring to the purchaser by placing his capital at risk in the enterprise. Generally, if a state adopts the risk capital analysis, "it may view the use of a resort condominium, campground or hotel suite as the benefit which will accrue to the purchaser of a timeshare." The theory was clearly espoused by the Supreme Court of Hawaii in State v. Hawaii Market Center, Inc. In Hawaii Market, realty interests were not at stake, but memberships in an enterprise involving sales and commissions were. Founder members purchased a sewing machine or cookware and were then eligible to earn money through many activities, including referrals. The court engaged in a risk

149. Id.

150. See supra notes 117-35 and accompanying text.


152. "[T]he initial [investment] is induced by the offeror's promises or representations which give rise to a reasonable understanding that a valuable benefit of some kind, over and above the initial value, will accrue to the offeree as a result of the operation of the enterprise. . . ." Hawaii, 52 Haw. at 649, 485 P.2d at 109; see also Bloch, supra note 9, at 300.

153. See Bloch, supra note 9, at 300.


155. Id. at 644, 485 P.2d at 107.
capital analysis, finding that the investment contract theory espoused by Howey was too restrictive, "[leading] courts to analyse (sic) investment projects mechanically, based on a narrow concept of investor participation." The members were unequivocally exposed to risks and should, therefore, be protected.5

Similarly, in Silver Hills Country Club v. Superior Court,158 purchasers were entitled to protection under California's securities act regardless of profit potential.159 There, the members paid to use the services of the club and had no rights in the income or assets of the club.160 Memberships were transferrable, but only to persons approved by the board of directors.161 Construing the California Blue Sky Law, the Silver Hills court found that the memberships conveyed a "beneficial interest in title to property,"162 and applied a risk-capital analysis, rather than the investment contract/profit potential analysis:

[Developers] are soliciting the risk capital with which to develop a business for profit. The purchaser's risk is not lessened merely because the interest he purchases is labelled a membership. Only because he risks his capital along with other purchasers can there be any chance that the benefits of club membership will materialize.163

The court found that the legislature designed the definition of "security" broadly so "to protect the public against spurious schemes, however ingeniously devised, to attract risk capital."164 As in California, application of the risk capital analysis generally results in protection of a purchaser's interests under that state's securities acts by requiring compliance with disclosure provisions.165 Even without a

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156. Id. at 647, 485 P.2d at 108.
158. 55 Cal. 2d 811, 361 P.2d 906, 13 Cal. Rptr. 186.
159. "[W]hether or not they expect[ed] a return on their capital..." Id. at 812, 361 P.2d at 909, 13 Cal. Rptr. at 189.
160. Id. at 811, 361 P.2d at 907, 13 Cal. Rptr. at 187.
161. Id.
162. California Corporations Code § 25008(b) defines "security" as;"[a]ny stock, including treasury stock; any certificate of interest or participation; any certificate of interest in a profit sharing agreement; any certificate of interest in an oil, gas or mining title or lease; any transferrable share, investment contract, or beneficial interest in title to property, profits, or earnings." CAL. CORP. CODE § 25008(b) (West 1988); see also Silver Hills, 55 Cal. 2d at 812, 361 P.2d at 907, 13 Cal. Rptr. at 187.
163. 55 Cal. 2d at 813, 361 P.2d at 908, 13 Cal. Rptr. at 188.
164. 55 Cal. 2d at 812, 361 P.2d at 907, 13 Cal. Rptr. at 187.
165. "If there is evidence... that a state follows the risk capital theory, the developer should realize that he may be subject to securities regulation." Bloch, supra note 9, at 301.
profit motive, investors are protected from the risk of losing invested capital.  

The Martin Act was also drafted to broadly extend protection from fraudulent exploitation. New York courts, however, have applied the investment contract analysis, rather than the risk-capital analysis to determine whether license-type timeshare interests are covered by the Martin Act. The Court of Appeals in ASR II refused to even consider a risk-capital analysis: "[T]he memberships could not constitute securities even under a 'risk capital' analysis, [and] we need not decide whether, under other circumstances, the Silver Hills ... rule or some variant of it could prove to be a helpful addition to the 'Howey test'. ... 

Application of the investment contract analysis to a statute, such as the Martin Act, designed to broadly encompass realty interests, would thwart the consumer purpose of the Act. The risk-capital theory allows the court to consider the capital at risk without intent to reap a profit. Ignorance of these interests neutralizes the purpose of the Martin Act. Developers would not be required to disclose information to purchasers, nor would the Attorney General have jurisdiction over any possible fraudulent activities, eliminating any criminal sanctions. Remaining civil liability would depend solely upon the provisions of the contract, resulting only in compensation to plaintiffs, rather than protection of purchasers from fraudulent activities. The risk-capital analysis, then, rather than an investment contract analysis, more accurately considers the interests at stake in determining whether the Martin Act applies to license-type timeshares.

B. Timeshare Provisions as a Legislative Alternative

The New York State Department of Law agrees with the Third Department, and has requested legislation classifying timeshares as "participation interests in realty." Proposed section 352-eeeee of the General Business Law provides:

166. "The significant difference between the two theories for timesharing ... is that the risk capital theory interprets "profits" as a "valuable benefit." Bloch, supra' note 9, at 300.
167. See supra notes 101-11 and accompanying text.
168. See ASR III, 68 N.Y.2d at 94, 506 N.Y.S.2d at 18, 497 N.E.2d at 40, where the court refused to consider the risk capital test, dismissing it as not a helpful addition to the Howey test for determining the existence of a security under New York law; see also N.Y. GEN. BUS. LAW § 352-e (Practice Commentary) (McKinney 1988).
169. ASR III, 68 N.Y.2d at 94, 506 N.Y.S.2d at 18, 497 N.E.2d at 40.
170. The Department of Law supports the proposed legislation. See ATTORNEY GENERAL LEGISLATIVE MEMORANDUM No. 298-89; see also Proposed Legislation S.3430 and A.5378, proposing new ARTICLE 31, MEMBERSHIP CAMPGROUNDS.
All the provisions of this article, including the requirements for filing an offering plan with the department of law pursuant to (§ 352-e) of this article, shall be fully applicable to any public offering or sale in or from the state of any timeshares. Timeshares are hereby deemed to be participation interests in real estate covered by (§ 352-e) of this article.

Any ambiguity involving the application of "participation interests in realty" to timeshares is thus eliminated. The Department of Law declares the legislation necessary, in light of ASR III, "to clarify the Attorney General's jurisdiction to regulate all timeshare sales. Otherwise, sponsors may begin to structure their contracts conveying right to use timeshares in order to try to come under the All Seasons exception to the Department of Law's jurisdiction." For example, a sponsor may construct a right to use contract as a club membership, similar to the All Season memberships, specifically to avoid Martin Act regulations and Attorney General jurisdiction.

The proposed legislation not only requires filing with the Department of Law for all timeshares, but also allows a seven day cooling off period during which purchasers may rescind the purchase contract. Unfair marketing practices which might coerce a purchase are neutralized by the purchaser's ability to cancel. The right to rescind the contract is not waivable by either party. Most states require this right of rescission—an "effective remedy for 'overzealous' salesmen." Because the proposed legislation clearly classifies timeshares as participation interests in realty, and further provides purchasers with the right to rescind the contract, consumers would have adequate protection from "unscrupulous promotion."

171. Proposed General Business Law § 352-eeeee was first introduced in 1987 and passed the Assembly in 1988 as A.7259. A similar bill had been introduced in 1983.

172. Attorney General Legislative Memorandum No. 298-89.

173. Proposed General Business Law § 352-eeeee(3)(a)(i) provides:

(a) Purchaser's right to cancel contract.

(i) The purchaser may cancel a contract to purchase a timeshare with or without cause within seven business days after the execution of the contract or within seven business days after the purchaser has received the prospectus filed with the department of law under (§ 352-e) of this article, whichever is later;

174. Proposed General Business Law § 352-eeeee(3)(a)(ii) provides:

(ii) The right to cancel provided in this paragraph may not be waived by a purchaser under any circumstances. Any instrument executed by a purchaser which purports to waive such right shall be deemed void and of no effect;

175. Madison & Dwyer, supra note 9, at S10-5.

176. See Ledgebrook, 77 Misc. 2d at 871, 354 N.Y.S.2d at 323.
IV. Conclusion

The Martin Act, unlike the Federal Securities Laws, was clearly established to protect consumers from fraud within both the securities and real estate markets. New York courts, then, should emphasize, not the role of profits and investments, but whether an investor’s capital is at risk, in determining whether the protections of the Martin Act apply. By considering risk rather than “profit potential,” more consumer activities and investments would be protected, regardless of expectations of profit.

The legislature should also confer jurisdiction upon the Attorney General in timeshare offerings by adopting proposed General Business Law 352-eeeee, allowing a non-waivable seven day cancellation period. By so doing, the Martin Act would expressly apply to all timeshare arrangements, eliminating any ambiguities regarding developers’ compliance with disclosure requirements and the Attorney General’s ability to prosecute violators.

Yvette C. Mendez