



NEIL ABERCROMBIE
GOVERNOR

SHAN S. TSUTSUI
LT. GOVERNOR

STATE OF HAWAII
OFFICE OF THE DIRECTOR
DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS
335 MERCHANT STREET, ROOM 310
P.O. Box 541
HONOLULU, HAWAII 96809
Phone Number: 586-2850
Fax Number: 586-2856
www.hawaii.gov/dcca

KEALI'I S. LOPEZ
DIRECTOR

JO ANN M. UCHIDA TAKEUCHI
DEPUTY DIRECTOR

**PRESENTATION OF THE
PROFESSIONAL AND VOCATIONAL LICENSING DIVISION**

TO THE HOUSE COMMITTEE ON
CONSUMER PROTECTION AND COMMERCE

TWENTY-SEVENTH LEGISLATURE
Regular Session of 2014

Wednesday, January 29, 2014
2:10 p.m.

TESTIMONY ON HOUSE BILL NO. 2021, RELATING TO TIME SHARE.

TO THE HONORABLE ANGUS L.K. MCKELVEY, CHAIR,
AND MEMBERS OF THE COMMITTEE:

My name is Lori Beth Van Cantfort, Time Share Administrator of the Professional and Vocational Licensing Division ("PVL"), testifying on behalf of the Department of Commerce and Consumer Affairs ("Department").

House Bill No. 2021 seeks to allow time share developers to take purchasers' funds out of escrow prior to construction of the time share project being completed as long as the developer posts a surety bond, escrow bond, or irrevocable letter of credit. The Department opposes this bill because there are still questions as to the level of consumer protection provided by this provision. The Department has been in discussions with the proponent of the bill but the parties need more time to resolve

Testimony on House Bill No. 2021
Wednesday, January 29, 2014
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various issues. Therefore, the Department requests that the bill be held to give the parties time to work on the proposal during the interim.

Thank you for this opportunity to provide testimony on H.B. No. 2021.



January 24, 2014

TO: HOUSE COMMITTEE ON CONSUMER PROTECTION AND COMMERCE
Representative Angus McKelvey, Chair
Representative Derek S.K. Kawakami, Vice Chair

FROM: Henry Perez, Chair
ARDA-Hawaii

RE: HB 2021, Relating to Time Shares
Position: Support

Dear Chair McKelvey, Vice Chair Kawakami and members of the Committee:

The American Resort Development Association (ARDA) Hawaii, the local chapter of the national timeshare trade association, supports HB 2021, Relating to Time Share. This bill would allow disbursement of purchasers' funds to a developer provided that an assurance is provided.

Under current law, buyers' funds may be placed in escrow and disbursed prior to the closing and deeding of the property to the buyer. When funds are placed in escrow for a project under construction, they can be disbursed to the developer for use in construction. If the developer defaults, because of the use of subordination clauses in the purchase contract, the buyers' rights are subordinated to the rights of the construction lender. The lender may foreclose and acquire title to the project free of any claims of the buyers.

To overcome this disadvantage to purchasers of incomplete projects, other states have adopted laws permitting a timeshare developer to use buyers' deposits upon posting a bond or other financial assurance. This provides buyers with a remedy in the event the developer fails to complete construction or defaults on the construction loan.

We believe similar protections in Hawaii will serve the consumers well. This bill is a starting point for discussion and remains a work in progress. We look forward to working with this committee, the DCCA, and other stakeholders to revise and refine this bill as it moves through the process. Thank you the opportunity to submit testimony in support of HB 2021.

**Testimony of
Jason Gamel
on behalf of
Wyndham Vacation Ownership**

DATE: January 28, 2014

TO: Representative Angus McKelvey
Chair, Committee on Consumer Protection and Commerce
Submitted Via CPCtestimony@capitol.hawaii.gov

RE: **H.B. 2021 - Relating to Time Share**
Hearing Date: Wednesday, January 29, 2014 at 2:10 p.m.
Conference Room 325

Dear Chair McKelvey and Members of the Committee on Consumer Protection and Commerce,

I am Jason Gamel, SVP-Legal, testifying on behalf of Wyndham Vacation Ownership. Wyndham offers individual consumers and business-to-business customers a broad suite of hospitality products and services through its portfolio of world-renowned brands. Wyndham Vacation Ownership has substantial presence in Hawaii through its Wyndham Vacation Resorts and WorldMark by Wyndham brands.

Wyndham **strongly supports** H.B. 2021, which allows disbursement of purchasers' funds from escrow to a developer, provided that the developer first posts a bond, letter of credit or other financial assurance to an unaffiliated third party.

Under current Hawaii law, a developer that constructs a time share project must hold a time share buyer's funds in escrow after both the 7 day rescission period has passed, the project is completed, and closing has occurred. In only one limited circumstance can the developer remove funds from escrow, and that process is labor and time intensive for both the developer and the DCCA. This means that a significant amount of money (sometimes tens of millions of dollars) may remain in escrow for months at a time. H.B. 2021 would allow those funds to be used by the developer and it would protect the funds with a third party assurance, giving the consumer ample protection if the project

Gary M. Slovin
Mihoko E. Ito
Tiffany N. Yajima
Jennifer C. Taylor

1099 Alakea Street, Suite 1400
Honolulu, HI 96813
(808) 539-0840

was never completed and allow the developer to access funds to apply to construction costs.

This approach, which has been implemented in Florida and many other jurisdictions around the United States, benefits both developers and buyers by providing a remedy if the developer fails to complete a construction project or the consumer is otherwise entitled to a refund of funds where the developer is no longer able to provide one.

For the above reasons we support H.B. 2021 and ask for the Committee's favorable consideration of the bill.

Thank you for the opportunity to submit testimony.



9002 San Marco Court
Orlando, Florida 32819
(407) 418-7271

January 29, 2014

To: Honorable Angus McKelvey, Chair
House Committee on Consumer Protection and Commerce

RE: **HB 2021 - Relating to Time Share – In Support**
Conference Room 325, 2:10 p.m.

Chair McKelvey, Vice Chair Kawakami and members of the committee:

Starwood Vacation Ownership (“Starwood”) appreciates the opportunity to offer testimony in support of HB 2021, which allows escrow to disburse purchasers’ funds to a developer, provided that the developer first posts a bond, letter of credit or other financial assurance to assure payment of any refunds purchasers are entitled to receive.

Starwood supports this bill because it is beneficial to both consumers and the industry. In addition, this update will continue the modernization of the Hawaii Timeshare law, as escrow bonds, letters of credit or other approved financial assurances are permitted by other states which regulate timeshare, including states with highly restrictive timeshare laws such as California, Florida and New York.

Permitting funds to be withdrawn from escrow upon the posting of a letter of credit, bond or other financial assurance is beneficial to developers by assisting with cash flow in large resort construction projects, which often take two to three years to complete. It is beneficial to consumers because it guarantees them a refund of all purchase funds if the project is not timely completed. Currently, purchaser funds may be released to reimburse a developer for construction expenditures. This procedure could result in an incomplete project and insufficient funds remaining to complete the project.

Based on current industry data, the main carriers who provide escrow bonding and other assurances are generally rated as more stable and financially secure than traditional banking institutions. Finally, as you will no doubt hear from the American Resort Developer Association (“ARDA”), the timeshare industry is pleased to report a history in which all posted escrow bonds and other financial assurances have been fully satisfied without a single incident of default.

For the aforementioned reasons, we respectfully request that you pass HB 2021. Thank you.

Robin Suarez
Vice President/General Counsel
Starwood Vacation Ownership

MARRIOTT
VACATIONS
WORLDWIDESM

January 28, 2014

Rep. Angus L. K. McKelvey, Chair
Rep. Derek S. K. Kawakami, Vice Chair
Members of the Committee on Consumer
Protection and Commerce
Twenty-Seventh Legislature
Regular Session, 2014

Re: H.B. 2021
Hearing on January 29, 2014, 2:10 p.m.
Conference Room 325

Dear Chair, Vice-Chair and Members of the Committee:

My name is John McGowan, Vice President & Assistant General Counsel for Marriott Vacations Worldwide (“Marriott”). Marriott is the developer and operator of multiple vacation ownership properties in Hawaii including Marriott’s Ko Olina Beach Club and Marriott’s Maui Ocean Club. Marriott supports H.B. 2021.

H.B. 2021 allows a timeshare developer to receive disbursement of a purchaser’s funds from escrow if the developer first posts a bond, letter of credit or other financial assurance to assure payment of any refunds that purchasers may become entitled to receive.

Under current law, a timeshare purchaser’s funds may be used to pay the costs of construction and various other development expenses. To do so, the developer must first file with the DCCA a budget of construction costs, evidence of the financing sources, the construction contract, and performance and payment bonds. These measures are intended to ensure that construction of the project will be completed. Once these measures are in place, the developer is entitled to the release of all the purchasers’ funds in escrow to pay for construction and development costs of the project.

However, none of these measures protect the purchasers’ right to a refund in other circumstances. For example:

- If the developer defaults under its construction loan, the lender can foreclose on the project and acquire title free of the rights of the purchasers – even though the purchasers’ funds may have been used to help pay the cost of constructing the project.
- If the developer fails to complete construction *on time*, purchasers may have a right to cancel but there is no money for escrow to refund.
- If there are material differences between the project as represented and the project as actually constructed, purchasers have a right to a refund but there is no money available to be refunded.

6649 Westwood Boulevard, Orlando, Florida 32821 t 407-206-6000 marriottvacationsworldwide.com

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With an escrow bond, purchasers can get a refund of their deposits under any of these circumstances.

In addition to providing more comprehensive consumer protections than the current law, H.B. 2021 removes the DCCA from the process of evaluating and approving the construction budget, source of funds, construction contract and performance and payment bonds for a project, an administrative burden that commercial construction lenders frequently are unable to accomplish successfully.

H.B. 2021 relies on the credit of a bonding company. If the developer fails to make a required refund, the risk of failure is transferred to the bonding company instead of remaining with the purchasers.

Of course, a bond is only as good as the company that issues it. But bonding companies often have higher credit ratings than the banks in which purchasers' funds are deposited in escrow. In addition, bonding programs provide a prequalification process that, in the case of an escrow bond, benefits purchasers. Before issuing a bond, the bonding company performs a thorough underwriting of the financial wherewithal of the developer and expects the developer to perform its obligations. By contrast, a bank merely accepts and holds the deposits.

Escrow bonds can be drawn so that both the escrow agent and the State can enforce the bonds. However, the escrow agent is in the middle between the purchaser and the developer, so the primary burden of enforcing the bond resides with the escrow agent. But if the escrow agent fails, or if it wrongfully disburses funds, the State can call the bond, assuring that purchasers will receive their refunds. The current law affords no similar protection for purchasers.

In short, under the current system of releasing funds for construction, consumers could potentially get a half-complete project with a litigating developer and lender. The project could never be built and consumers could even lose their funds entirely in the case of an eventual liquidation of the project. An escrow bond can help to avoid this. A construction bond will not.

Thank you for your consideration of this legislation and thank you for the opportunity to submit this written testimony.

Sincerely,



John McGowan
Vice President & Assistant General Counsel, Marriott Vacations Worldwide

McCORRISTON MILLER MUKAI MACKINNON LLP

ATTORNEYS AT LAW

CHARLES E. PEAR, JR.

DIRECT #S:
PHONE - (808) 223-1212
FAX - (808) 535-8029
E-MAIL - PEAR@M4LAW.COM

January 29, 2014

LATE

Rep. Angus L. K. McKelvey, Chair
Rep. Derek S. K. Kawakami, Vice Chair
Members of the Committee on Consumer
Protection and Commerce
Twenty-Seventh Legislature
Regular Session, 2014

Re: H.B. 2021
Hearing on January 29, 2014, 2:10 p.m.
Conference Room 325

Dear Chair, Vice-Chair and Members of the Committee:

My name is Charles Pear. I am appearing as legislative counsel for ARDA Hawaii.

ARDA Hawaii supports the bill.

In 1982, at the request of the Chairperson of the House Consumer Protection Committee, I drafted comprehensive legislation regulating the financial structure of time share plans and establishing escrow requirements governing the sale of time share interests.

The 1982 amendment requires that the developer establish an escrow account in Hawaii¹ pursuant to a separate written escrow agreement between the developer and an escrow agent.² All funds received from the buyers must be deposited in the escrow account until closing.³

Funds may be released from escrow prior to closing if the buyer cancels his or her purchase during the 7-day rescission period or if the contract is otherwise terminated in accordance with its terms.

Buyers' funds may also be used to pay the costs of constructing and developing a time share project if certain conditions are met.⁴ Those conditions include a requirement that the

¹ §514E-16(b), H.R.S.

² §514E-16(c), H.R.S.

³ §514E-16(a), H.R.S.; Rule 16-106-34(c)(1), H.A.R.

⁴ §514E-17(a)(4), H.R.S.

developer deposit the following with the Director of the Department of Commerce and Consumer Affairs:

- a copy of the executed construction contract;
- a statement showing the costs to complete the project, including the costs to furnish the time share units;
- evidence satisfactory to the Director that there are sufficient funds to pay the costs of constructing, furnishing and completing the project (whether from buyers' funds, the developer's funds, or loan proceeds);
- a copy of executed performance and labor and material payment bonds.

If the foregoing requirements are met, then the buyer's funds may be disbursed to pay the costs of construction (to the extent completed) and the cost of purchasing furnishings and fixtures for the time share units. The Act also permits disbursement of buyers' funds to pay architectural, engineering, interior design, finance, and legal fees. And buyers' funds may be disbursed to pay "other incidental expenses of constructing the time share units or developing the time share plan", although the nature of such expenses is not defined by the Act.

The legislative history is instructive insofar as it indicates the intended purpose of this section:

* * * Subsection (4) parallels section 514A-67 of the Horizontal Property Act which permits the disbursement of buyers funds to pay the costs of construction. A developer will not be permitted to use buyers funds for construction until he files a copy of the executed construction contract and a copy of the executed performance and labor and material payment bonds insuring that all amounts due under the construction contract, including change orders up to 10%, and all other costs of construction will be paid.⁵

Under §514A-67 of the Hawaii condominium law (now Section 514B-92, H.R.S.), buyers' funds may be disbursed to pay the costs of construction (to the extent completed) and also to pay architectural, engineering, finance, and legal fees. (The condominium law does not permit disbursements for furnishings or for interior design fees.) The statute also permits disbursement of purchasers' funds to pay "other incidental expenses of the condominium".

These measures are intended to ensure that the project will be constructed. However, none of these measures protect the buyers' right to a refund in other circumstances. For example:

⁵ Conf. Com. Rep. No. 52-82 on H.B. No. 3078-82, 1982 Senate Journal, page 901.

- If the developer defaults under its construction loan, the lender can foreclose on the project and acquire title free of the rights of the buyers – even though the buyers’ funds may have been used to help pay the cost of constructing the project.
- If the developer fails to complete construction *on time*, buyers may have a right to cancel but there is no money for escrow to refund.
- If there are material differences between the project as represented and the project as actually constructed, buyers have a right to a refund but there is no money available to be refunded.

In the market downturn of 2007 – 2008, many condominium unit purchasers sought to cancel their sales contracts and obtain a refund of their deposits. I personally was involved in buyer remorse lawsuits covering more than 50 units.

In those cases, construction of the condominium had been completed. Buyers asserted, however, that they were entitled to rescind their purchases for various other reasons. We advise the buyers and their counsel that, while they may have claims to rescind their purchases, all of the buyers’ deposits had been used to pay construction costs, so there was no money in escrow to refund.

This bill proposes to authorize developers to withdraw funds from escrow upon posting an escrow bond. An escrow bond assures that buyers will receive any refund to which they become entitled. With an escrow bond, buyers can get a refund of their deposits if the lender forecloses, if the developer fails to complete construction, if the developer does not finish construction on time, or if the project is materially different than promised.

This concept is currently used in Florida. ARDA Florida’s legislative counsel reports that the Florida regulators have never had to call an escrow bond.

Of course, a bond is only as good as the company that issues it. But buyers funds held in escrow are deposited in a bank. But bonding companies sometimes have higher credit ratings than the banks used to hold funds in escrow. For example, consider these ratings of prominent bonding companies by Moody’s:

Federal Insurance Company (Chubb)	Aa2/Stable
Zurich Insurance Company	Aa3/Stable
Traveler’s Casualty and Surety Company	Aa2/Stable
Westchester Fire Insurance Company (ACE)	A1/Stable

as compared to the ratings by Moody's of prominent local and national banks:

J.P. Morgan Chase & Co.	A3/ Stable
Bank of America	Baa2/Stable
CitiGroup	Baa2/Stable
Wells Fargo	Aa3/Stable
Bank of Hawaii	Aa3/Stable
First Hawaiian Bank	A2

In addition, bonding programs provide a prequalification process that, in the case of an escrow bond, benefits the buyers. Issuance of a bond means that the bonding company has completed a thorough underwrite on the financial wherewithal of the developer and expects the developer to perform its obligations. By contrast, a bank merely accepts and holds the deposits.

Escrow bonds can be drawn so that both the escrow agent and the State can enforce the bonds. However, the escrow agent is in the middle between the buyer and the developer, so the primary burden of enforcing the bond resides with the escrow agent. But if the escrow agent fails, or if it wrongfully disburses funds, the State can call the bond, assuring that buyers will receive their refunds. The current law affords no similar protection for purchasers.

In short, under the current system of releasing funds for construction, consumers could potentially get a half-complete project with a litigating developer and lender. The project could never be built and consumers could even lose their funds entirely in the case of an eventual liquidation of the project. An escrow bond can help to avoid this. A construction bond will not.

Thank you for your kind consideration of this legislation. I would be happy to take any questions if you think that I may be of some small assistance.

Very truly yours,

MCCORRISTON MILLER MUKAI MACKINNON LLP



Charles E. Pear, Jr.