The significance of cooperation between the developer and the real estate manager in light of agency theory

Katarzyna Kania¹, Katarzyna Najbar²

¹ Cracow University of Economics, Poland, ORCID: https://orcid.org/0000-0003-4116-5971, kaniak@uek.krakow.pl
² Cracow University of Economics, Poland, ORCID: https://orcid.org/0000-0002-7088-7044, najbark@uek.krakow.pl

ABSTRACT
Purpose - The paper discusses the problem of the significance of cooperation between both entities in respect of the implementation of projects which will make it possible to appropriately arrange their cooperation, thus enabling them to achieve the assumed objectives of their activity.

Design/methodology/approach - The research was conducted among selected real estate development companies.

Findings - Taking into consideration different objectives of developers' and real estate management firms' activity, we should provide for different relationships of those entities with the final recipient of developer products, namely the real estate user.

Research implications - From a theoretical perspective, the relations between participants of ventures are explained by agency theory, which treats an enterprise as a network of contracts concluded between individual participants of a given venture. It concerns attitudes of the stakeholders of a given project, which depend, among others, on benefits they want to gain.

Keywords: developer; real estate manager; agency theory; investment process

JEL codes: L14, L21, L85

Article type: review article

DOI: 10.14659/WOREJ.2021.115.05
In the course of the investment process, the developer and the real estate manager cooperate for a relatively short period, if we consider the whole life cycle of real estate. The cooperation is most often limited to the stage of the facility handover to use to the management entity. The facility commences the stage of use in the shape in which it was designed and executed as commissioned by the developer. Such a design can be subject to the real estate manager's standard service and then it will be such an asset in the developer's portfolio which he will be able to call a success. In practice, there are also real estate development ventures which, due to reasons related to design or execution, as well as unexpected events in the period of their use, limit satisfaction from the use of the real estate and do not accomplish objectives assumed by the developer and the real estate manager.

Considering different objectives of the activity conducted by developers and real estate management firms, we should also assign for different relationships of those entities with the final recipient of developer products, namely the user. Looking from their perspective, we should look for common objectives between the developer and the manager, the effect of which would be meeting users' needs. In the context of the above relationships, it will be a positive side effect. To understand the relationships between the participants of contracts/ventures from the theoretical perspective, we can apply agency theory, which treats an enterprise as a network of contracts concluded between individual participants of a given venture. It concerns attitudes of the stakeholders of a given project which depends, among others, on benefits they want to gain.

The authors of the paper discuss the problem of the significance of cooperation between both entities regarding the implementation of the projects, which will make it possible to appropriately arrange their cooperation, thus enabling them to achieve the assumed objectives of each party's activity. They assess the importance of this cooperation by studying selected entities of the property development market. They ask about the time, the scope and the area of possible cooperation. The research goal of the presented paper is to identify possibilities for cooperation between the developer and the real estate manager at the stages of the investment preparation, execution and use. The authors pose a hypothesis that understanding mutual benefits of the cooperation, the awareness of threats to mutual relationship and their neutralization are possible on the grounds of this cooperation. The research was of a pilot nature by surveying the chosen real estate development companies. Their goal was to assess, based on the
results obtained, whether this problem occurs. The article is conceptual and the outlined research problem will be the subject of further research.

**LITERATURE REVIEW**

In the existing research, one can find positions of the literature which refer to defining activities of a developer and a real estate manager adequately to their areas of specialization (Peiser, 2012; Peca, 2008; Belniak & Kania, 2018, p. 80). The views expressed in specialist literature regarding the precise definition of the term ‘real estate development’ (also referred to as ‘property development’) are varied and, in part, differ from each other. Most definitions refer to a sense of creativity and focus and coordination to realize real estate assets (Neary, 2009). The presented study combines the problems of creating a new real estate resource and the requirements related to the use of real estate in the period of its use. The authors notice a necessity for cooperation between the developer and the real estate manager at the early stage of creating the idea of real estate. The growth of the real estate development market in Poland forces developers to monitor completed facilities at the stage of their use in respect of end users' satisfaction. Understanding mutual benefits from the cooperation, considering authentic value-added for the developer, is the basis for building their permanent partnership relationship.

Developers do not notice that in addition to information concerning the assessment of functional and technical solutions applied in facilities, the real estate manager can be an intermediary in building the developer's positive image upon the completion of the investment.

In literature, we can find references to the significance of the developer's and real estate manager's cooperation during the preparation of the investment project, where the manager is one of the developer's partners (Miles, Berens et al., 2007, p. 39-64). Unfortunately, in Polish papers the subject of mutual influences of the developer and the real estate manager is marginal (Najbar & Nalepka, 2007).

It should be also emphasized that legal regulations in force since the end of 2014 have bound the developer with users of residential real estate for longer, extending the warranty against physical defects from 3 to 5 years (Consumer Rights Act of 30 May 2014).

Based on the analysis of an investment project comprising the whole life cycle of real estate, we can define the role which should be played in this process by individual specialists, with special attention paid to the role of the developer and the real estate manager. Their role is particularly important
during the construction, use and development of real estate (Najbar & Nalepka, 2008, p. 98).

An attempt to refer the developer's and the real estate's objectives of activity to agency theory seems one of the ways of understanding relations and mutual benefits which may shape a valuable business relationship, the effects of which will be felt by a real estate user. As S. P. Shapiro writes: “(...) harmonious cooperation and mutual benefits depend mainly on agreeing on goals enabling the integration of efforts of the partners, who at the same time will strive for ensuring equal access to information (Shapiro, 2005, p. 263-284).” Under conditions of incomplete and asymmetric information among developers, real estate managers and users, agency theory finds new applications (Liu & Ma, 2020). In recent years, the core of agency theory puts more concern on how to design effective incentives and restraint mechanisms to control agent’s behaviour to minimize the cost and maximize their benefits at the same time of resolving the conflict interests and asymmetric information (Xu, 2016, p. 45), incentive strategies for a construction project manager (Sha, 2019, p. 461) or risk allocation in construction contracts (Chang, 2014).

E. Kanak discusses the problem of the shaping of relationships by the developer and entities of the environment. Maintaining and developing relationships is important for the firm's development and developers should engage in those activities. Efficient relationship management with the environment results in the growth of their competitiveness on the market, reduction of marketing costs, an increase in the loyalty of entities of the environment towards the firm. Caring about the satisfaction of clients - buyers of flats, but at the same time partnership relations with suppliers, cooperating companies, intermediaries, banks, institutions regulating the market, media and their personnel must be at the required level so that the development firm could develop in the dynamically changing competitive environment (Kanak, 2014).

**RESEARCH METHODOLOGY**

**The objectives of the developer's and the real estate manager's activities**

Real estate development activity means a comprehensive type of business comprising actions aiming at the development of real estate via building new or using existing buildings, as well as the purchase of land to adapt it for development. Therefore, development activity will be planned, harmonious implementation of individual development investments in the way providing developers with maximum profits with the optimum use of available
resources (Crosby, Devaney & Wyatt, 2020). The developer aims to achieve profits through the creation of value-added for the specific area. The effect of a developer's activities can be provided areas which will be the object of use, that is, the developer is a producer of usable floor area or gross leasable area. In consequence of undertaken investment activities, the developer ensures the execution of a given type of area. On the other hand, the real estate manager is the recipient of the developer's products it is going to manage during the real estate use, representing the owner of the real estate and meeting the needs of the users of the area or the premises. Project development in the real estate industry is a complex process and has a long lifecycle from initiation to completion (Fayadh, 2020). German papers on developer activities propose the division of investments into four stages: investment initiation, investment concept, execution, investment market exposition (Dąbrowski & Kirejczyk, 2002, p. 16), which is illustrated below in Figure 1.

![Figure 1. Stages of real estate development investment](source)

When referring to the specificity of the developer's activity, we should remember that they can implement various models of activity, which include:

1. construction – lease – sales,
2. construction – lease – use,
3. construction – sales.

Some developers also manage facilities built by themselves. Developers can perform the tasks in two models:

1. by providing management services independently, thus continuing cooperation with clients who have purchased the space from them or lease it from them,
2. commissioning management services to entities that provide real estate management services (the commissioning model).
On the housing estate market, most often developers sell completed premises and choose a real estate manager who takes over problems connected with the organisation of the newly-created community and the real estate use during the Defect Liability Period and later on. Thus, the developer’s responsibility as to the quality of the completed facility obliges them statutorily to 5 years, but it often depends on the manager’s competencies and efficiency to what extent buyers of the premises will pursue their claims.

On the other hand, entities providing management services conduct activity oriented to addressing their clients’ (real estate owners) needs. The activity of entities managing real estate will focus on five areas:

1. real estate management in the technical aspect, including its technical maintenance, control and raising the value of the invested capital,
2. human resources management, including personnel team management, which maintains, supports activities in the real estate,
3. finance management, including preparation of budgets, keeping books, making financial analyses,
4. lease management, including the preparation of the area for lease, marketing and presentation of the real estate, negotiating the lease terms and conditions,
5. knowledge-based management and risk management, including real estate insurance, the development of emergency procedures, knowledge of regulations (Get Real, 2008, p.2).

The objective of real estate management firms will be to maintain or increase the resources in their portfolio and strengthening their position on the market of those services.

To sum up, the activities conducted by developers and managers, we can show their main objectives and specificity (Tab. 1).

Table 1. The objectives of developers’ and real estate managers’ activities

<table>
<thead>
<tr>
<th>Main objectives of activity of:</th>
<th>the developer</th>
<th>the real estate manager</th>
</tr>
</thead>
<tbody>
<tr>
<td>Execution of an investment project in accordance with investment efficiency calculus</td>
<td>Company development via maintaining or increasing the managed resource</td>
<td></td>
</tr>
<tr>
<td>Identification of potential buyers’ needs</td>
<td>Identification of threats and risk in the manager’s activity</td>
<td></td>
</tr>
<tr>
<td>Efficient commercialisation of the project</td>
<td>Performing tasks according to regulations and the real estate management contract</td>
<td></td>
</tr>
</tbody>
</table>
The significance of cooperation between the developer ...

Shaping the developer’s image/brand utilizing good quality of facilities | Recognition of know-how brand

Source: own study.

What clearly results from the above comparison is that in the developer-real estate manager relationship it is the developer who is a strategic partner and the real estate manager is a service provider. The real estate manager operates on the facility built by the developer, the real estate manager’s activity would not be possible without the developer’s product, which is real estate. The capital needed for the fulfilment of the objectives of both activities is very varied. The developer must have much higher funds to launch and conduct his activity. For the real estate manager the most important thing is to win the first facilities to be managed and managing them does not require the engagement of much capital.

When looking closer at the indicated objectives set by the developer and the real estate manager to themselves in conducting their activities, the following question arises: is there any space for cooperation and is it necessary so that we could talk about benefits for both parties of the business relationship?

When analysing the costs of the execution of a real estate development investment, we should look at their progression over the whole investment project. When deciding on some project solutions, an investor is guided by his premises, an adopted strategy of conducting the activity, including an adequate cost of the investment implementation, complex time of its implementation (often stemming from obligations towards end-users), easiness of the application of some solutions and a possibility of switching responsibility for the completed investment to contractors, especially in the case of new technical solutions. Every project - its execution and then maintenance – is strongly individualised, which means that it has specific and unique physical, functional and location-related parameters (Najbar, 2014). What is more, a given facility is executed and then maintained in the changing legal regulations defining the conditions of construction and use.

Figure 2 is illustrative, however, it shows an important relationship between the progression of costs and possibilities to influence them. With the subsequent stages of the investment project, the costs of the investment increase and the influence of the investor and the user on their amount decreases. What results from it is that proper decision and works undertaken in the initial stages of the investment project influence greatly not only the cost of the investment execution but also the costs of using the real estate
produced in this process (Śliwiński & Śliwiński, 2006, p. 16). Similar conclusions have been formulated in consequence of research carried out abroad (Redlein, 2004, p. 35-37). The first decisions in the investment planning stage, concerning the directions of investing, the size of the real estate and its technical equipment, shape operating costs of management by about 70 %, which cannot be influenced in the use stage.

The research findings should have a chastening effect on those developers who out of the models of activity presented in the first part of the article implement the one in which the real estate created as a result of the investment process remains to be their property and they incur costs of maintaining it. Even if it becomes leased, high costs of the use may discourage tenants, and they certainly reduce income on the leased area.

Figure 2. The developer's influence on the costs of investment in time
Source: own study based on (Geltner & Miller, 2007).
Agency theory and the cooperation between the developer and the real estate manager

To the relations which take place between the developer and the real estate manager and, in consequence, the real estate user, agency theory can apply. Following the assumptions of this theory, attitudes of the parties to the contract are characterised by (Shapiro, 2005):

- preferring one’s benefits,
- reluctance to risk,
- asymmetry in the access to information.

The relations are often defined as „principal-agent“ relations and they are characteristic especially for the activity within an enterprise, but they also occur between individuals cooperating on the market. According to the assumptions of the presented concept, the agent performs tasks entrusted to him by the principal, and owing to information advantage over the principal, he can manipulate this information for his benefit.

Among many relations which the developer establishes to implement the venture, one of the key ones from the point of view of long-term success of the executed investment is a real estate manager to whom the developer commissions to administer the facility at the stage of its use. Depending on the adopted model of operation, the developer may also become a manager himself, when he completes the execution of the construction investment.

Therefore, a developer can be defined as a principal who engages a real estate manager (agent) to manage facilities during their use. It is the simplest approach. At the same time, the manager becomes an agent on the part of the owners of premises, who, in light of agency theory, with time (along with the transfer of the rights of the ownership of the real estate) become principals in this relationship. For some time the manager is the linker and at the same time the negotiator between the developer and the owners of the premises. The relationship is often the cause of the conflict of interests.

 Conscious determination of the objectives of every type of conducted activity (see: Fig. 3) and an attempt to establish the field of cooperation may contribute to its proper arrangement to avoid unnecessary ambiguities in seeking claims in the user-developer relationship.
In the opinion of experts in the real estate management industry, developers often do not attach importance to the completed facilities and proper relations with the existing clients anymore. Due to shortages of the workforce in construction, buyers of premises struggle first of all with a higher and higher risk of the occurrence of defects, but most of all with difficulties in enforcing their removal (Kowalska, 2018). Moreover, in order to meet the quality standard as expected by the property owners and to survive in the market, efficient and effective strategic management are developed as the main focus of facility management companies (Wang et al., 2020).

On the other hand, managers chosen by the developer as the first ones to manage the facility are treated with reserve by users (new owners of facilities), claiming that they do not fulfil their goals, but the goals of the first principal, namely the developer. It often happens that the developer imposes a low-cost manner of managing the facility, primarily in the situations when the developer did not commercialise the majority of the area (premises), and then there is a practice of transferring the burden of charges on underestimated costs of management to new owners of the premises (based on authors’ experience).
The survey was carried out among representatives of development companies investing in Krakow. The survey in the form of a prepared questionnaire was sent to 13 entities out of 154 operating in 2018 in Krakow (NBP, 2020) - experts who were selected by the authors based on their previous experience. Those were entities investing only in a residential real estate in Krakow. The questionnaires filled in by respondents were supplemented with interviews.

Respondents represented a few areas of activities making up the whole investment process, namely the sales department (7 people), investment preparation and execution department (3 people) and project management department (3 people). Therefore, they represented different time during the investment process, some of them had contact with the investment at the stage of commercialisation, which often finished (in the year 2017 and 2018) before handing over the facility to use, and some respondents were involved throughout the whole investment process.

Most of the development companies taking part in the survey represented the legal form of a limited joint-stock partnership (very popular in the implementation of real estate development projects), the other numerous part of respondents operated in the form of a limited liability company.

Experience in developer activities of the companies participating in the study varied (in years: from 7 to 28 years). Respondents operating in the form of special-purpose entities provided data related to parent companies, their founders’ details. More than a half of respondents (61%) have implemented over 20 projects so far, 31% of them executed 6-20 investments. Three employed up to 9 workers, the remaining ones were companies with 10-49 employees. No relationship between the number of workforces and the legal organisation of entity was observed.

Among the surveyed companies the area of activities was distributed as follows:
- locally (the city of Krakow) – 38%
- plus regionally (Krakow Poviat) – another 31%
- plus domestic – 23%
- plus abroad – 8%

Among respondents with the longest experience, the local or maximally regional range of activity prevailed, whereas younger firms, with a several-year tradition could pride themselves in domestic and international projects.
Over the last 5 years, the subject of development firms’ activities were mainly investments in the housing estate market, which on average constituted 92% of the activities undertaken by them. More than a half of them also conducted investment activity on the market of office and commercial properties, however, this area constituted on average 14% of the activities undertaken by them. All of them handed over one facility to use over the last two years on average. Those were large buildings of the area of 6500 m² and 115 premises on average.

**Management model**

12 of 13 respondents chose the management method in the commission mode (Nalepka, 2006, p.59), entrusting management functions of a newly-completed facility to a professional real estate management entity. Figure 4 shows arguments that contributed to the choice of this form of management.

![Figure 4. Factors determining the choice of the commission-based management model by the developer](image)

The experience of development companies so far in the case of as many as 77% of respondents reassured them to choose this form of cooperation with the manager. Several additional factors occurred in the responses, namely:

a) no need to extend the firm,

b) better reception by clients (end users),

c) the adopted strategy of the firm in terms of not combining the developer and the real estate manager in one legal entity,

d) Bad experience of direct management by the developer (to keep a good image of the firm after the handover of the building to use, more works were done than it was necessary),
e) Due to a 5-year warranty period, an external real estate manager guarantees his customers (in principle) reliable enforcement of rights arising from the warranty.

Over 90% of developers commission the management of the completed investment to professional, external entities. Their main argument for that choice is the relevant experience so far. Only one developer tried to deal with it on his own, but in the long run, it proved to be inconsistent with the company's strategy or highly ineffective. The second group of developers are companies that have been outsourcing management from the very beginning of their development activity, which is a positive experience for them. This applies to 10% of the respondents.

Almost 40% of entities do not see any other possibilities of cooperation with a real estate manager except for commissioning management to them upon the handover of the building to use. The remaining part of respondents indicates possible areas of the manager’s engagement. Respondents gave examples of such areas:

- including the real estate manager in the organisational structure of the firm,
- advisory function, among others during multi-stage investments (coordination of activities concerning the joint elements of the investment),
- passing feedback about the technical maintenance, applied solutions of materials in the investments executed so far.

Moreover, developers want real estate managers to influence or require proper use of the facility, take care of its proper management, also via an increase in the quality of guarantee service.

The above findings confirm answers to the next question, namely at what stage the cooperation with the real estate manager should be commenced. By far the majority of respondents engage a real estate manager at the stage of the building use, only 4 of 13 respondents see their role during the execution of the investment, and nobody engages a manager at the stage of designing the facility.

In practice, the above state boils down to the situation when a real estate manager shows up in the facility on the completion of the building and takes it over with the benefit of inventory. He should find himself in this role, manage the facility efficiently, conduct proper guarantee service and advise the developer when in the case of the completed facility he does not influence many things anymore. Of developers commissioning the management service, 58% diversify their contractors, and 42% always
cooperate with one entity. Respondents indicated two main reasons for the diversification: better perception by clients, adjusting managers to various types of investments/clients. Respondents assessed their real estate managers in 5 aspects:

• professional experience,
• dedication,
• choice of subcontractors (managing the facility),
• ability to solve conflicts,
• effective communication.

They assessed dedication and professional experience highest. Skills and choice of subcontractors for the completed investment were assessed as the poorest. None of the respondents was fully satisfied with the management of the completed investment, some even expressed negative opinions on that. The aspects of effective communication and the ability to solve problems were assessed as very good by one-fifth of respondents. 53% of representatives of development companies assessed those areas as good.

The approach to the assessment of the same areas by representatives of various departments of real estate development firms varied. The sales department, which had the most numerous representation, assessed real estate managers from the point of view of clients to whom it sold the premises. Some of them came to a given firm to buy other premises and owe to that they indicated advantages and disadvantages of work of a given real estate manager.

The investment execution department (often performing the function of the guarantee department, too) evaluated real estate managers from the point of view of the assessment of investment and the number of reported defects during the guarantee and warranty period. On that basis, it was established whether the real estate manager was effective in terms of communication and whether it can solve conflicts.

To sum up, the survey conducted with the participation of developers’ representatives, we can indicate in individual stages of development investment activities in which a real estate manager should engage to fulfil, together with the developer, their objectives related to the activities conducted by them. Proposals of activities and the time of their implementation are presented below.
The significance of cooperation between the developer ...

In the earliest stage of the process, the real estate manager should perform the advisory function. It can take place in the case of planning complex investments, that is multi-stage investments or those having common elements on a few real properties. We should remember that due to the decreasing supply of land, there are more and more such projects. A real estate manager having experience in the management of such investments can indicate disadvantages of the applied functional, system and material solutions, and at the stage of designing can suggest proven solutions within that scope.

At the stage of construction, the real estate manager can get involved in negotiating contracts with the contractors of individual systems and equipment producers as for terms and conditions of the guarantee, guarantee service and maintenance. He should also see to the investment during the construction to check the execution of major stages of the project from the point of view of further use.

During the commercialisation of the facility, the real estate manager can prepare provisions of acceptance protocols with end-users, prepare or

Figure 5. Areas of cooperation between the real estate manager and the developer during the investment process
Source: own study.
verify the provisions of instruction manuals for the premises/facility, establish the material scope of the property management and in the case of housing estates prepare the “commissioning” documentation for newly-created tenants’ association (the content of the resolutions, including, among others, rules and regulations of facilities, budget project).

During the maintenance of the facility, the real estate manager should conclude contracts on maintenance of buildings, use the facility properly, report defects and help in efficient guarantee service. For many developers also feedback on the completed investment, its functionality and satisfaction of end-users will be extremely important.

Attention should be paid to the fact that the moment of handing over the facility to use is for the developer the final stage of his very active operations during the process. Often after a very intensive period of execution, the developer wants to conclude the transaction as soon as possible, which will help him recover the funds invested so far from funds accumulated on escrow accounts. It happens that final decisions related to the facility are taken fast and in a chaotic way, and the real estate manager invited to cooperate has little time to familiarise with the facility and prepare it to use. Those entities could certainly reduce this nervous time if the cooperation had started at an earlier stage.

Allowing the real estate manager to the project at an early stage of preparing the investment project gives several benefits which could bring positive results to both parties at the stage of real estate management, including reduced maintenance costs (which is important for the developer in the case of low commercialisation of the area), guarantee service and satisfaction of end-users.

Therefore, we can assume that the participation of experienced real estate managers is important already at the stage of designing or the execution of the investment. The principal or developer, wanting to avoid risk, the problem of asymmetry of information, pays the manager for information, experience, which will help adjust the planned project in the best possible way to end users' needs. The presence of an experienced real estate manager who supports the developer, starting from the preparation of necessary documents, appropriate contracts, resolutions and regulations, and ending with the facility handover allows the developer to hand over the facility smoothly.

According to the assumptions of the agency theory, the above cooperation enables risk reduction by bringing the interests of the principal (developer) and the agent (property manager) closer together. This
cooperation should also lead to keeping the project costs as low as possible for the principal.

**CONCLUSION**

The conducted pilot study enabled to indicate unused areas of cooperation between the real estate manager and the developer on each stage of the investment process. In future research, attention should be paid to examples of such activities where the cooperation of those entities takes place throughout the whole investment process. It would be very important to verify the developer’s approach to management (and the cooperation with the real estate manager) in the case of different models of his activity and decision to sell the investment (model 1 and 3 described above), or the decision to leave the real estate in his portfolio (model 2).

In theory, we could assume that in the other case the real estate maintenance costs could be lower, more optimal and flexible, if they were taken into consideration at an earlier stage of the investment process, calculating the real estate maintenance costs which will be to be incurred by the developer.

**ACKNOWLEDGEMENTS AND FINANCIAL DISCLOSURE**

The article came into being within the project no. 058/WEKEN/01/2019/S/9058 entitled ‘Rozwój instytucjonalny i funkcjonalny sektora nieruchomości w Polsce – II etap’ financed by Cracow University of economics conducted by prof. dr hab. Adam Nalepka.

**REFERENCES**


