

Total Quality Management and Residential Real Estate Agency

View metadata, citation and similar papers at core.ac.uk

Authors Hans R. Isakson and Michael Spencer

Abstract This study explores the implications of applying Total Quality Management (TQM) principles to residential real estate brokerage, specifically the need for customer focus. Deming's (1986) TQM system of fourteen points is reduced to four distinct subsystems. The most critical of these is the need for customer focus. Several approaches to agency in residential real estate brokerage are presented, with an examination of the ease with which customer focus can be obtained within each approach. The main finding is that customer focus can be achieved easier with the agency specialization approach.

Introduction

One of the fastest growing trends in business today, Total Quality Management or TQM, originated in the 1950s. The term continuous quality improvement (CQI) is more common in some service sectors, however this study uses the term TQM as the managerial roots of CQI to better lay the foundation for the discussion of Deming's ideas and their applicability to residential real estate brokerage. TQM principles were developed by Deming (1986) as a means of delivering error-free war munitions and equipment to allied forces during World War II. Following the war, Deming went to Japan to help with their census, and ended up assisting in the rebuilding of their industrial base. His ideas were discarded by industries in the United States as being unprofitable, especially in the short-run dominated, post-war U.S. economy. Thus, Deming went to work assisting the Japanese to rebuild their war torn industries. (Deming's work was so successful in Japan that their highest quality award is called the Deming Prize.) Since the 1970s, the Japanese successes with Deming's ideas have caught the attention of U.S. businesses. Today, practically all major U.S. industries, such as Xerox, Procter & Gamble, Texas Instruments, IBM, Microsoft and Boeing, are adopting some form of TQM. The purpose of this article is to explore TQM and the implications of its application in the residential real estate industry by examining the critical role of delineating the customer in residential real estate brokerage.

An Overview of TQM

Several researchers have examined TQM and developed alternative configurations for critical TQM components (Saraph, Benson and Schroeder, 1989; Flynn, Schroeder and Sakakibara, 1994; Powell, 1995; and Ahire, Golhar and Waller, 1996). The most recent in-depth analysis of the fourteen points in Deming's original system of quality control was conducted by Anderson, Rungtusanatham and Schroeder (1994) who used it to propose a theory of quality management. While there is disagreement among researchers about the specific TQM components and their appropriate definitions, an analysis indicates that TQM can be synthesized into four distinct subsystems: (1) a customer focus; (2) top management support; (3) employee fulfillment; and (4) continuous improvement. These components are the most commonly cited.

Customer focus means that every division, department, system, procedure, policy and person in the organization focuses on what is of value to the customer. In TQM, all organizational systems and people are geared to satisfy the needs of the customer. The customer's needs always come first!

Continuous improvement means that all systems in the organization are constantly evaluated and improved. Processes, products and services that produce flaws (*e.g.*, customer complaints, duplication of efforts, costly rework, etc.) are subjected to never-ending evaluation and improvement. The emphasis is on the systems and processes, not the employees who implement them. In TQM terms, if an employee or worker is not contributing his or her share to the product or service being produced, it is more likely due to faulty systems or procedures, not a faulty employee. Employees improve when the systems and procedures they follow are improved.¹

The purpose of employee involvement is to involve all employees in quality-related activities using a variety of management techniques (*e.g.*, team or task force approaches, collaborative decision making, etc.). Everyone in the organization works toward the common goal of customer satisfaction. Furthermore, everyone in the organization must be empowered to make the decisions necessary to achieve the organization's goal of customer satisfaction, especially those employees who actually deliver the service or produce the product. The area of empowerment is one of the most difficult to implement in large organizations, with a pyramid type organizational structure. A TQM organization has an organizational chart that is flat and often consists of overlapping circles rather than distinct boxes connected by lines of authority.

Top management support, or visionary leadership, is the ability of management to establish a long-term view of the goal and direction of the organization. This long-term vision allows the preeminent position of the customer to dominate over short-term internal concerns. Often a non-autocratic, supportive and nurturing

leadership style is observed. Sufficient self-confidence exists within the top managers to allow for the fulfillment of employees, through empowerment. Additionally, top management support channels the empowered employees to use TQM methods to seek out current and prevent potential problems without fear, and in doing so the empowered employees continually improve the process.

TQM principles are not easy to implement as indicated by various industry surveys (American Quality Foundation and Ernst and Young, 1991; and Arthur D. Little Corp., 1992). Indeed, TQM is like utopia or heaven to many in management. Everyone wants it, but no one wants to do what it takes to get there. Nowhere is this quip truer than in the residential real estate business.

The focus of this study is the critical issue of customer focus within the residential real estate brokerage industry. Neither TQM nor CQI can be achieved without properly identifying the customer. If this article sparks just one ember of interest within the residential real estate business in TQM and TQM's emphasis on the customer, it will have met its objective.

TQM in Residential Real Estate

The application of TQM in service industries is more difficult than in manufacturing industries because of the intangible nature and immediate consumption of the product (Heskett, Sasser and Hart, 1990; Heskett, Sasser and Schlesinger, 1997; and Fitzsimmons and Fitzsimmons, 1998). The emphasis in service industries tends to be on the processes of the organization that deliver the services the organization sells. For the most part, the application of TQM in the residential real estate business means addressing the quality of agent services delivered to the customers and clientele of the residential real estate firm. In TQM terms, the quality of agent services is driven by the process through which these services are delivered. This process is largely determined by the type of agency relationship, if any, established with the customers and clients of the firm. It is the agency area that will naturally receive the greatest scrutiny as TQM principles find their way into this industry.

Who is the Customer?

First, a residential real estate brokerage firm interested in TQM must decide, who are its customers/clients? Is it the seller, the buyer or both? Or, is it the transaction? Largely, the identity of the customer/client is determined by the type of agency used by the residential real estate firm. Second, the residential real estate firm must make sure that the customer/client understands the meaning of the relationship they have established with the firm. The first step in applying TQM principles to residential real estate is to decide exactly what the relationship is

between the firm and its customers/clients, and then to make sure that the customers/clients fully understand the relationship.

Agency Approaches in Residential Real Estate Brokerage

Agency is unquestionably one of the hottest issue in the residential real estate brokerage industry today. With the abandonment of mandatory seller sub-agency in multiple listing services, it seems that everyone is reexamining their relationships with buyers and sellers. Several approaches can be found in use today. In the traditional approach, the firm acts as the agent of the seller and treats buyers as customers. Newer approaches include agency specialization, in which the firm specializes in representing only the seller or only the buyer; and the facilitator or transaction broker approach, in which the firm represents neither the buyer nor the seller. Another approach is called consensual dual agency, in which the firm attempts to act as a buyer's agent for buyers and as a seller's agent for sellers, and as an agent for both in certain cases (in states where dual agencies are permitted by law). Before applying TQM to residential real estate brokerage, a look at the approaches to agency is appropriate.

The Traditional Approach

Traditionally, residential real estate brokers establish an agency relationship with sellers, while treating buyers as customers. Within this approach, agency law governs a broker's relationship with the seller/client, while tort law governs the broker's relationship with the buyer/customer.

The traditional approach has created problems for the industry. In 1983, the Federal Trade Commission reported that home buyers are often confused about their relationship with residential real estate agents. A full 72% of the buyers believed that the selling agent was representing the buyer and not the seller in the transaction. Moreover, almost 67% of the buyers relied heavily on the selling agent's advice when making decisions about purchasing their houses. Agency disclosure laws enacted in various states should help to alleviate this problem somewhat. However, too many of these laws permit buyer disclosure to take place as late as at the signing of any offer to purchase, rather than on the initial contact with the buyer. Nonetheless, effective agency disclosure practices, especially to buyers, will make implementation of TQM in residential real estate brokerage much easier.

In addition to the problems reported by the FTC in 1983, the 1992 report of the National Association of Realtors (NAR) Presidential Advisory Group on Agency cites several additional problems: (1) some buyers want client representation, just like the sellers; (2) buyer agents often encounter the multiple listing services barrier of seller sub-agency in accessing properties to show their clients; (3) some sellers do not want to assume the legal liability for the unauthorized actions and representations of sub-agents who are not under the control of their agent.

To alleviate these problems, the NAR recommends that sellers should be given choices regarding their legal relationships with agents. Namely, the choice of the listing broker using subagents, buyer agents or both to market the seller's property. Let us now examine these newer approaches suggested by NAR as well as one approach that NAR does not like.

Specialization in Buyer or Seller Agency

One way to respond to NAR's recommendations is for the firm to specialize in representing only buyers or only sellers. This so-called agency specialization approach can be found in some larger urban areas but it is not very popular with most residential real estate brokerage firms. The major roadblock to shifting from the traditional approach to agency specialization is the prospects of the firm's giving up either its buyers or sellers in order to specialize in one or the other. Yet, agency specialization complies exceptionally well with the basic TQM principle that the entire focus of the business must be on its customer/client. With only buyers or only sellers as agents, the firms that practice agency specialization will be well positioned to benefit from the implementation of TQM principles.

Agency specialization has another potential benefit for residential real estate brokerage firms. The agency confusion found in the 1983 FTC study can and has lead to costly litigation for some firms that make use of the traditional approach. Several sellers have successfully sued to recover their commissions (and punitive damages in some cases) from firms who leaned too heavily toward representing a buyer's interests in order to get the sale. Some of the offending brokers have had their licenses suspended or revoked in addition to paying compensatory and punitive awards to their dissatisfied clients. (See March and Zumpano (1988) for a discussion of the legal problems created by traditional residential brokerage practices.)

Another issue of importance in agency specialization is the structure of the commissions paid to the buyer's agent. If the commission of the buyer's agent is a percentage of the selling price of the property (as is the custom in the traditional agency approach), the agent has a potential conflict of interest. The buyer would like his or her agent to assist them in paying the lowest possible price for any given property. However, this will result in the agent receiving a smaller commission. Fortunately, Colwell and Trafzger (1993) and Colwell, Trafzger and Trevleven 1993) have devised a means of structuring the commission that eliminates this potential conflict of interest. As a result, the structuring of both seller and buyer commissions does not have to be a barrier to the success of agency specialization.

Consensual Dual Agency

Another alternative is consensual dual agency approach. In this approach, the broker takes listings as before, but shares these listings with other brokers only

on a cooperative basis. No automatic sub-agency relationship is created with each listing. This arrangement allows the firm to offer a seller only agency to sellers. Buyers are treated in a similar fashion. On initial contact, if the buyer is completely unknown to the broker and others in the firm, the buyer is initially treated as a customer and is shown the firm's own listings. If the buyer does not find what he or she wants among the firm's own listings, or if the buyer is known to the broker or others in the firm prior to the initial contact, a buyers agency is offered to the buyer in order to show other brokers' listings. If the buyer/client later decides to make an offer on one of the in-house listings, a consensual dual agency is necessary. Once the buyer passes over the line from customer to client, there is no going back. After crossing over this line, a consensual dual agency is the only alternative for offers from the buyer/client on in-house listings, assuming state laws do not automatically outlaw consensual dual agencies.

The consensual dual agency is fraught with problems. Moreover, given a choice, rational buyers and sellers should prefer specialist brokers to those who practice consensual dual agency. Agency specialization should always be preferable to consensual dual agency, wherever and whenever informed consumers have a choice. These problems also make implementation of TQM principles more difficult. Full agency disclosure would not be sufficient in the consensual dual agency approach, because the process of the buyer changing from a customer to a client is so complex. However, as long as the firm has very few such conversions, TQM principles would be no more difficult to implement than in the traditional approach.

The Facilitator Approach

One alternative is to give up agency all together and practice something that is known as the facilitator approach. In this approach, the broker serves neither buyer nor seller. Instead, the broker serves the transaction, and focuses on facilitating the transaction. This approach was developed by an attorney in Colorado, and it has been the focal point of a fair amount of discussion in the residential real estate industry. However, at the 1993 meetings in Miami, Florida, NAR announced that it did not support or encourage members to practice the facilitator approach.

The facilitator approach serves the interests of no one person over those of another. The broker who practices this approach treats both buyers and sellers as customers, establishing an expressed agency relationship with neither of them. Unfortunately, an implied agency, especially an implied dual agency, may emerge out of the behavior and practices of the broker who employs this approach. For example, if the broker wins the trust and confidence of either the buyer or seller or both, an implied agency could be the result. Furthermore, if the public generally expects residential real estate brokers to be agents, it may be impossible for the facilitator-broker to avoid the appearance of agency.

The facilitator approach, properly practiced, requires that the practitioner give up all appearances of being a residential real estate agent. The facilitator can provide

buyers and sellers certain services and products they need to buy and sell residential real estate, but they should not act as a middle person between buyers and sellers. For example, the facilitator can provide sellers advertising services, or buyers a market analysis of selling prices, but the facilitator should not communicate offers and counteroffers between buyers and sellers; doing so would give the appearance of being an agent of one or both of the parties involved.

The application of TQM principles in the facilitator approach would appear not to be particularly difficult, because the firm would be treating everyone as a customer and no one as a client. As long as the services being offered as well as the services not available to the customer are fully disclosed, firms that practice the facilitator approach should be able to make excellent use of TQM techniques. However, the public may or may not be able to fully differentiate between a facilitator and a traditional or specialist broker. In this case, facilitators might find it difficult to stay in business.

The Firewall Approach

One way brokers can represent buyers and sellers at the same time is to build a firewall between clients. As long as the buyer/client never buys from the seller/client, a broker will not be forced into a dual agency situation. The most natural way for a firm to achieve this sort of separation is to focus buyer agency on a completely different market segment than seller agency. For example, a broker might choose to represent only sellers of high-priced houses, and only buyers of low-priced houses, or vice versa. Other combinations of market segments might include residential versus commercial, one city versus another (especially in rural areas), buyers or sellers versus renters, etc. However, within each market segment, the broker must specialize as either a buyer or a seller agent.

Another technique, that tends to work better in a large firm, is to place the firewall between the in-house agents, by dividing them into buyer and seller specialists. This technique requires that the specialists never discuss their clients privileged information with the other specialists. In other words, the large firm is divided into two smaller divisions, in which there is little interaction between divisions. Whenever interaction occurs, it should be supervised by a managing broker to insure that privileged information is not revealed. This puts a great deal of strain on management to insure that not even the semblance of a dual agency exists. Indeed, the agents are best instructed by management to keep all proprietary information about their clients to themselves. The end result of a successful firewall operation is a side-by-side specialized agency, with dual operations under the same ownership. Subsequently, TQM principles would work in a manner similar those in the agency specialization approach.

Quality Issues and the TQM Residential Real Estate Firm

In order to apply TQM principles in residential real estate brokerage, the quality of services provided to the customer(s) of the firm is of paramount importance.

Therefore, a look at the overall quality of broker services is appropriate. In a study by McDaniel and Louargand (1994), significant buyer dissatisfaction with the services of brokers in the Boston area is reported. Their study also reports a significant difference between what brokers perceive as being important and what customers perceive as being important in determining the quality of broker services. The authors conclude that the goal of residential real estate agents should be a satisfied customer, and that the typical broker is unable to identify what customers think constitutes quality service.

McDaniel and Louargand also report that the order of importance of the quality dimensions of service to customers is as follows: reliability, assurance, empathy, responsiveness and tangibles. This sequence is similar to sequences reported in studies of other service industries. However, residential real estate agents in the McDaniel and Louargand study thought that the order of importance to their customers was: assurance, reliability, empathy, responsiveness and tangibles. The differences between the customer's actual order and what the agents believed to be their customer's order was statistically significant. Furthermore, free-form responses by customers frequently included comments that there is a conflict of interest for the agent who acts for the seller, yet purports to also act in the buyer's best interest.

Johnson, Dotson and Dunlap (1988) also study consumer satisfaction and quality in the residential real estate brokerage business. They report that service in this industry falls below customer expectations in the areas of: (1) service assurances and responsiveness; and (2) tangible characteristics of the firm. The authors call for a TQM type of effort in which performance feedback and evaluation of broker and salesperson service becomes a base for continuous improvement. The RESERV instrument developed by Nelson and Nelson (1995) could easily be used for measuring the quality residential real estate brokerage services as suggested by Johnson, Dotson and Dunlap.

The findings should be of concern to the residential brokerage industry. Fortunately, TQM techniques, such as those discussed, can be drawn on to improve the quality of agent services. The firms that do so will survive into the next millennium, while those that do not will perish. However, without first determining exactly who is the customer, residential real estate brokerage firms will never be able to implement any of the TQM principles. Indeed, to do so could make the firm worse off. Even Deming warned of partial adoption of his principles.

Conclusion

Total Quality Management is sweeping the country, first in manufacturing then in service industries, from automobile production to hospitals and from law firms to colleges, and it is about to hit the residential real estate brokerage business. The agency reforms recommended by the NAR and agency disclosure laws should

make TQM more attractive in residential real estate brokerage firms. As more firms explore the various alternatives to the traditional approach to agency in residential real estate brokerage, more firms will find TQM an attractive tool for improving the quality of the services they provide. The importance of customer satisfaction in the TQM approach will enable residential real estate brokerage firms to become more profitable and viable businesses.

Endnotes

¹ The term employee is used here in its generic form, not in its legal form. An employee in TQM may be an independent contractor.

References

- Ahire, S. L., D. Y. Golhar and M. A. Waller, Development and Validation of TQM Implementation Constructs, *Decision Sciences*, 1996, 27:1, 23–56.
- American Quality Foundation and Ernst and Young, *International Quality Survey: The Definitive Study of the Best International Quality Management Practices*, Cleveland, OH, 1991.
- Anderson, J. C., M. Rungtusanatham and R. G. Schroeder, A Theory of Quality Management Underlying the Deming Management Method, *Academy of Management Review*, 1994, 19:3, 472–509.
- Arthur D. Little Corporation, *Executive Caravan TQM Study Summary*, 1992.
- Colwell, P. and J. W. Trefzger, More on Compensating Buyer Brokers, *ORER Newsletter*, 1993, Summer/Fall, 14–16.
- Colwell, P. F., J. W. Trefzger and R. A. Trevleven, Compensating Buyer Brokers, *ORER Newsletter*, 1993, Winter/Spring, 12–16.
- Deming, W. E., *Out of Crisis*, MIT Center for Advanced Engineering Study, Cambridge, MA, 1990, originally published in 1986 for Deming's 14 points (Jan 1990 revision).
- Evens, J. R. and W. M. Lindsay, *The Management and Control of Quality*, Fourth edition, South Cincinnati, OH: Western College Publishing, 1999.
- Federal Trade Commission, *The Residential Real Estate Brokerage Industry*, Washington, DC: U.S. Government Printing Office, 1983.
- Fitzsimmons, J. A. and M. J. Fitzsimmons, *Service Management: Operations, Strategy, and Information Technology*, second edition, Boston, MA: Irwin/McGraw Hill, 1998.
- Flynn, B. B., R. G. Schroeder and S. Sakakibara, A Framework for Quality Management research and an Associated Measurement Instrument, *Journal of Operations Management*, 1994, 11, 339–66.
- Heskett, J. L., W. E. Sasser and C. W. L. Hart, *Service Breakthroughs: Changing the Rules of the Game*, New York, NY: Free Press 1990.
- Heskett, J. L., W. E. Sasser and L. A. Schlesinger, *The Service Profit Chain*, New York, NY: Free Press, 1997.
- Johnson, L. L., M. J. Dotson and B. J. Dunlap, Service Quality Determinants and Effectiveness in the Real Estate Brokerage Industry, *Journal of Real Estate Research*, 1988, 3:2, 21–36.

- Marsh, G. A. and L. V. Zumpano, Agency Theory and the Changing Role of the Real Estate Broker: Conflicts and Possible Solutions, *Journal of Real Estate Research*, 1988, 9: 2, 151–64.
- McDaniel, J. R. and M. A. Louargand, Real Estate Brokerage Service Quality: An Examination, *Journal of Real Estate Research*, 1994, 9:3, 339–51.
- Mitra, A., *Fundamentals of Quality Control and Improvement*, Second edition, Upper Saddle River, NJ: Prentice Hall, 1998.
- Nelson, S. L. and T. R. Nelson, RESERV: An Instrument for Measuring Real Estate Brokerage Service Quality, *Journal of Real Estate Research*, 1995, 10:1, 99–113.
- Powell, T. C., Total Quality Management as Competitive Advantage: A Review and Empirical Study, *Strategic Management Journal*, 1995, 16, 15–37.
- Saraph, J. V., P. G. Benson and R. G. Schroeder, An Instrument for Measuring the Critical Factors of Quality Management, *Decision Sciences*, 20, 810–29.

Hans R. Isakson, University of Northern Iowa, Cedar Falls, IA 50614-0124 or hans.isakson@uni.edu.

Michael Spencer, University of Northern Iowa, Cedar Falls, IA 50614-0125 or spencer@uni.edu.