

# An agency theory perspective on the owner/manager relationship in tourism-based condominiums

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## Abstract

This paper draws on field study data to provide an examination of the condominium owner/manager relationship in the Australian tourism context. Although there has been considerable growth in tourism accommodation owned through strata-title, no research examining the somewhat idiosyncratic relationship between unit owners and resident managers has been found in the literature. The peculiar nature of the relationship underlines its significance as a context in which to apply the agency theoretical model. As Australian condominium resident unit managers provide letting and caretaker services for condominium unit owners, it appears that the relationship can be justifiably viewed as a principal-agent exchange (Mills, P.K., *J. Business Res.* 20 (1990) 31).

The study specifically focuses on strata title condominiums located in major tourism regions. This sub-sector of the condominium management industry was chosen for study because it exhibits several key attributes distinguishing it from the non-tourist-based condominium sector. For example, two different parties represent the principal (resident owners and investor owners), also a significant proportion of a resident manager's work relates to the management of short-term holiday unit letting. In light of the particular agency relationship dynamics arising in large tourist-based condominium governance, several suggestions concerning the legal environment of the industry are provided.

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## 1. Introduction

This study is concerned with the governance of condominium complexes (sometimes referred to as “strata-titled” complexes). In Australia and New Zealand, the typical condominium complex comprises multiple dwelling units in a shared community title scheme whereby there are as many private owners of units as there are lots within a scheme. These complexes can assume a variety of physical forms. They can be designed as detached villas, duplexes or townhouses; as low rise (typically 2–3 storeys) apartment complexes comprising usually around 6–12 units;<sup>1</sup> or as high-rise

apartment complexes generally comprising eight or more storeys and comprising many units (can be up to 500 or more units).

In Australia, there are 35,000 holiday apartments in condominium complexes with more than 15 apartments in the holiday letting pool (Australian Bureau of Statistics, 2002). If we impute an average value of AUS \$250,000 per unit, this represents an overall investment of AUS \$8.75 billion in the tourism accommodation sector. Due to Australian income tax provisions that provide a tax deduction for expenditure related to investment properties, most units are owned by individuals. In the 2001/2002 financial year, this investment generated AUS \$932 million in rental income (i.e., about one-fifth of total accommodation sector earnings).

The majority of financial institutions that finance condominium complex developments require 25–50% of the apartments to be sold off the plan (i.e. prior to building commencement), before releasing the capital

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<sup>1</sup> Some of these low-storey complexes can comprise as many as 100 units, however.

required to complete the major building works. Without investor owners who plan to use their apartments for holiday lettings, the number of potential buyers would be substantially lower and initial 'off the plan' sales would take much longer to reach the required quota. Furthermore, holiday apartments are often purchased as a means to diversify investment portfolios for retirement funds. Appropriate governance of condominium complexes is therefore not only a tourism management issue, it also carries more general socio-economic implications.

The last quarter of a century has seen major growth in the provision of tourist accommodation in condominium complexes. While one tends to think first of hotels when conceiving of tourist accommodation, this is becoming an out-dated notion as condominiums now represent the primary form of accommodation in many tourist resorts such as Australia's Gold Coast (Warnken, 2002; Warnken, Russell, & Faulkner, 2003). In light of this condominium tourist accommodation growth, relative to the volume of research conducted into hotel management, there is a startling paucity of research concerned with condominium management. The study reported herein was conducted in light of this apparent gap in the literature.

The study draws on the agency theory framework to provide insights into the idiosyncratic nature of condominium governance and also the conflicts that can arise between a condominium complex's unit owners and its resident manager. This appraisal is conducted in the context of condominiums located in tourist regions. In tourist region condominiums there are two main types of unit owner: resident owners and investor owners that sub-let their units to short-term stay holiday-makers. Tourist region condominiums also carry the additional dynamic of a broadened resident manager responsibility due to the provision of a short-term letting management service.

The validity of drawing on the agency theory framework in connection with condominium operations becomes evident when comparing the nature of a hotel's operational and logistical operations with those of a tourist-based condominium. Data for this study has been collected from parties involved with large condominiums located, in the main, close to Australia's Gold Coast. This area represents an archetypal tourist centre with a high density of high-rise buildings located adjacent to a commercially developed beach-front. For some time it has been widely acknowledged to represent Australia's premier tourist destination (Russell & Faulkner, 1999). Condominiums in tourist regions can be compared to hotels due to the provision of a reservation management and room cleaning service. From an operational perspective, the primary difference between a tourist-based condominium and a hotel is the fact that condominiums generally provide no or minimal food and beverage services other than self-catering

facilities.<sup>2</sup> A hotel represents a commercial setting where the conventional owner/manager relationship that has been the primary subject of agency research can be readily applied. Similarly, the conventional workings of a condominium complex signifies an agency relationship where the wealth-seeking objectives of unit owners have to be reconciled with the wealth-seeking objectives of a resident manager. As will be noted below, however, the governance arrangement typically implemented in Australian condominiums departs radically from the generally applied owner/manager governance structure evident in most Western commercial organisations.

The remainder of the paper is organised as follows. The next section overviews the agency theory model and the nature of research conducted within the agency theory tradition. Following this, the particular nature of agency relationships apparent in the context of condominium management are outlined. The qualitative data collection research methods applied and also findings made in connection with the specific issues arising in this relationship are then presented. The paper concludes with a summary of the main findings, a discussion of the practical implications arising from the study and an outline of some research initiatives that can build on the study reported herein.

## 2. Agency theory

Agency theory concerns exchanges where one party, the principal (typically represented by the owner(s) of a business), delegates work to a second party, the agent (typically represented by a manager or some other employee of the business owned by the principal). It attempts to draw out contractual problems that can arise as a result of agents acting opportunistically when their interests depart from those of the principal (Berle & Means, 1967; Jensen & Meckling, 1976). These problems are exacerbated where information asymmetry favouring the agent exists.<sup>3</sup>

Agency theory has been a popular conceptual framework for researchers interested in conflicts of interest, incentive problems and also mechanisms for managing incentive problems (Eisenhardt, 1989; Mills, 1990;

<sup>2</sup> A particular aspect of the provision of a short-term stay condominium unit may in fact give rise to more complex labour management implications than is the case for hotel guest management. As condominiums provide self-catering facilities, it is to be expected that in many cases the time taken to clean a unit following a guest's departure will be greater than the time taken to clean a hotel room following a hotel guests departure. The provision of self-catering facilities also carries implications for maintenance and control of self-catering infrastructure.

<sup>3</sup> Information asymmetry arises when one party has access to information that the second party cannot access.

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