STANFORD
GRADUATE SCHOOL OF BUSINESS

CASE: HR-29
DATE: 04/12/07

KELLER WILLIAMS REALTY

There is nothing that Coldwell Banker or any other company has that can compete with this model.

– Mark Willis, President and CEO, Keller Williams Realty

INTRODUCTION

Mark Willis had just finished meeting with Mo Anderson and Gary Keller. Willis, who was the president and CEO of Keller Williams Realty, was discussing with his vice chairman and the founder of the company plans to expand Keller Williams' presence on the East and West Coasts. The three executives knew the financials extremely well. They knew that the company's operating model made it among the most profitable (if not *the* most profitable) of the major real estate companies in the United States. In addition, the company was also on its way to becoming one of the largest real estate companies by number of agents, having grown from 8,000 in 2000 to over 70,000 in 2006 through the sale of new franchises and through agent recruitment.

Nevertheless, the plan to increase Keller Williams' presence on the two coasts was not without risk. Willis, Anderson, and Keller knew that preserving the culture of the company was critical to its future success. It would be easy to replicate the operating systems—everything from the economic model to the compensation plan, the profit share, and the organizational structure—most of which were unique to the industry. But if Keller Williams could not find new franchise owners or recruit agents who *lived* the company's culture, expansion would fail. As Anderson told Willis in the meeting, "The culture in this company is like the life blood flowing through a body. Culture supplies the oxygen for the body to live, and without it, this system falls flat on its face." Willis knew she was right. Competitors had woken up to Keller Williams' success, and several upstarts had tried to replicate their systems. None had adopted the culture and none to date had been financially successful. As Keller Williams expanded to a much larger size, competition would increase from both new and established players, and the company would have to be careful to find new franchise owners who would continue to implement the culture and systems that were responsible for its success.

Professor James N. Baron and Brian Tayan prepared this case as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

RESIDENTIAL REAL ESTATE INDUSTRY[1]

The housing market constitutes a significant portion of economic activity in the U.S., representing approximately 15 percent of gross domestic product (GDP). In 2005, 1.3 million new homes and 7.1 million existing homes were sold.[2] The median price for existing home sales was $208,300, up from $185,200 the previous year.[3] The housing sector provided millions of jobs directly in construction, mortgage finance, property management, and real estate brokerage, and indirectly in the form of home improvement and property management.

Home ownership represents a significant source of wealth for individuals and their families. In 2004, 69.0 percent of U.S. households owned the homes in which they lived, up from 64.7 percent in 1995 and 63.9 percent in 1985.[4] Home ownership accounted for 32.3 percent of U.S. household assets in 2004, compared to 35.7 percent for financial assets such as stocks, bonds, and other savings.[5] Low long-term interest rates allowed many families to refinance their mortgages and withdraw cash to provide for personal consumption.

Real Estate Brokers – Principles of Operation

Most home sale transactions are facilitated through real estate brokerage firms whose agents represent either the buyer or the seller. In 2004, there were 236,000 real estate office locations in the U.S. These offices included all ownership structures—from independently owned and managed to regional or national franchises. Major nationwide brokerage firms included Coldwell Banker, Century 21, and Prudential. Despite the nationwide presence of some real estate brokerage firms, the industry remained local and fragmented. The top ten regional brokerage firms had only a 9.1 percent market share in 2004.

In order to operate in a local market, a brokerage firm must be licensed by the state. The individual real estate agents also must be licensed. Brokerage firms earn revenue through commissions generated by the sale of a home. Standard commission rates are typically 5 to 6 percent of the transaction value, although in some cases the customer can negotiate a discount. Commissions are split when two brokerage firms are associated with a transaction, in order to compensate for the work performed by both the buying and the selling agent. The broker compensates the agent responsible for the transaction with either a fixed fee or, more typically, a

---

[1] Industry information from: National Association of REALTORS®, "Structure, Conduct, and Performance of the Real Estate Brokerage Industry," November 2005, http://www.realtor.org/Research.nsf/Pages/CompetitioninRealEstateResearch, (April 3, 2006), except where noted.

[2] U.S. Census Bureau and the Department of Housing and Urban Development, "New Residential Sales," 2005, http://www.census.gov/const/www/newressalesindex.html (April 3, 2006).

[3] National Association of REALTORS®, "Existing Home Sales, Monthly Data for the U.S. and Regions," 2005, http://www.realtor.org/Research.nsf/Pages/EHSdata (April 3, 2006).

[4] U.S. Census Bureau, "Homeownership Rates for the U.S. and Regions: 1965 to Present," 1985-2005, http://www.census.gov/hhes/www/housing/hvs/historic/histt14.html (April 3, 2006), average over four quarters.

[5] Bucks, Brian K. et al, "Recent Changes in U.S. Family Finances: Evidence from the 2001 and 2004 Survey of Consumer Finances," Federal Reserve Board, http://www.federalreserve.gov/pubs/bulletin/2006/financesurvey.pdf (April 3, 2006).

percentage of the commission. In 2004, a common split was 60 percent paid to the agent and 40 percent retained by the broker to cover operating expenses.

Brokerage firm expenses include rent and occupancy, advertising, listing service fees, local real estate board fees, insurance, recruiting, training, and miscellaneous office expenses. Some brokers seek to differentiate themselves in the market by entering into franchise agreements with a national firm. Under such an agreement, the regional brokerage office pays a franchise fee in exchange for the right to use the national firm's name. These franchised brokers remain independent, with local management; however, they have to agree to adhere to the basic operating principles of the national firm as outlined in the franchise agreement.

Home Sale Process

Home owners sell their property by listing it with a local brokerage firm. An agent for the brokerage firm enters the property information into a regional or local database, called the Multiple Listing Service (MLS). Access to the MLS is restricted to licensed real estate agents. Most MLSs make their listing available to all licensed participants in the area, thereby ensuring that most brokers in a region have access to the full inventory of properties on the market at a given time. As a result, home sellers can list their property with one brokerage firm and still be certain that it is available to the entire market of buyers. Likewise, home buyers need to contact only one brokerage firm to have access to the complete listing of properties for sale.

Customers typically choose a brokerage firm or agent based on referral or their experience in a previous transaction. The National Association of REALTORS® estimated that, in 2004, 60 percent of customers relied on a referral or past experience when selecting an agent. In addition, homeowners consider such factors as reputation in the market, expertise with a particular type of transaction, or brand name. In many cases, the customer chooses a particular agent with a reputation of knowledge and good service rather than the brokerage firm.

In some cases, homeowners choose to offer their property without listing through a broker. These transactions are called for-sale-by-owner (FSBO). In FSBO transactions, the homeowner seeks to execute the transaction without the help of a seller's agent and the property is not listed in MLS. However, the seller might be contacted by a licensed real estate agent representing the buyer, in which case the seller has to negotiate directly with the buyer's agent for appropriate compensation. In 2004, approximately 14 percent of home sales were FSBO.

Real Estate Agent

Most real estate agents are independent contractors representing a particular brokerage firm. Agents typically do not receive salary, health and retirement benefits, or paid time off. In most cases, the single source of compensation agents receive is the commission split negotiated with the broker.

Real estate agents are required to pass a qualifying exam and be licensed in order to do business in a particular state. New real estate agents often have to climb a steep learning curve in order to gain expert knowledge of the local market and build a reputation in the community. As a result, it often takes several years before a real estate agent gains financial success.

Agents select the broker they work for based on the commission split offered, the broker's franchise name and reputation, or other work arrangements directly negotiated. Successful agents often seek improved compensation terms from their existing broker. If they are unable to achieve improved compensation terms, they might choose to switch to a competing broker that offers a more favorable commission split, or start their own independent brokerage firm.

Because agents are the main source of contact with a customer, they have strong influence over that customer's satisfaction. As an agent becomes more successful in a given local market, his or her reputation often becomes more important than that of the brokerage firm when it comes to attracting business. Because the relationship between the agent and his or her customer base is transactional, there are low switching costs for the homeowner to continue working with the same agent if s/he changes firms. As a result, the agent, too, faces low switching costs when deciding whether to change brokerage affiliations.

National Association of REALTORS®

The National Association of REALTORS® is a trade organization that provides political lobbying, advertising, and economic analysis in support of the real estate industry. A National Association of REALTORS® membership serves as a professional designation for real estate agents and is a signal of professional quality to many prospective customers. In 2004, there were approximately 2.5 million licensed real estate agents in the U.S., not all of whom were active in the market. Of these 2.5 million, more than 1.2 million were members of the National Association of REALTORS®.

RE/MAX: THE 100 PERCENT COMMISSION COMPANY[6]

In 1973, a new competitive model was introduced to the real estate industry. David Liniger, a real estate agent in Denver, Colorado, perceived many deficiencies in the operations of traditional real estate brokerages. He believed that the real estate profession was widely characterized by junior-level, inexperienced agents whose lack of knowledge led to poor customer service. For the owner of the brokerage firm, these agents were expensive to maintain, because they required the same amount of overhead expense as top-producing agents but did not contribute the same level of commission revenue. In many cases, a junior-level agent might sell only one or two houses per year, barely generating enough commission to cover his or her costs to the firm. By and large, these agents ended up leaving the profession after only a few years, leading to expensive turnover for the brokerage.

The favorable economics of the industry were largely generated by top-producing agents. Liniger observed that the top 20 percent of agents generated approximately 80 percent of the commission revenue for the industry. In addition, these agents had reputations for providing the highest level of customer service and were most knowledgeable about their local markets. Nevertheless, these agents were employed under compensation agreements that obligated them to split their commissions evenly with their brokerages. The commission split was generally the

[6] RE/MAX information from: Harkins, Phil and Keith Hollihan, *Everybody Wins*, (Hoboken, New Jersey: John Wiley & Sons, 2005).

same for top-producing agents as for low-producing ones, even though top producers were significantly more profitable for the firm. In effect, top-producing agents were subsidizing low-producing agents. Unable to negotiate substantially better compensation terms, these agents often left to start their own brokerage firms.

Liniger's vision for RE/MAX was to create a company that employed only top-producing agents. To attract these agents, RE/MAX would offer 100 percent of the commission as compensation to the agent, and in turn would charge the agent a flat fee to cover operating expenses and use of the RE/MAX name. The flat fee would be set such that an agent would break even at approximately three sales transactions per year. Above that level, commission revenue would flow entirely to the agent; below that level, an agent would be better off under the standard industry split. This compensation structure would be attractive to top-producing agents who were confident in their future success and would deter entry-level of low-producing agents who could not afford the risk of such an arrangement. The result would be a self-selection process whereby the best real estate agents would flock to and remain with RE/MAX.

From Liniger's perspective, RE/MAX was not in the real estate business so much as it was in the real estate *agent* business. In order for RE/MAX to succeed, it needed to offer the best environment for its agents to succeed. As a result, in addition to its compensation system, RE/MAX focused on creating a training-based organization that would increase the success of its agents.

KELLER WILLIAMS HISTORY

In 1986, Gary Keller, real estate agent and president of a small real estate company in Austin, Texas named Keller Williams Realty, found that he was losing a significant percentage of his top-producing agents to a fast-expanding RE/MAX franchise in the area. They were leaving because a crash in the Austin real estate market made economic conditions difficult and RE/MAX was offering 100 percent commission, which was superior to the standard 50 percent split that Keller Williams offered at the time. To Keller, it was expensive to dedicate resources to the development of agents, only to lose them once they became productive.

Keller gathered his remaining agents and asked them to work with him to create a system that would encourage people to stay. Together, they designed a new model for managing the firm, which he implemented the following year. Keller believed that this new model would not only stem the tide of losses to 100 percent commission firms, but would reverse the trend in Keller Williams' favor. He was convinced that the system that he and his agents designed was superior from both an economic standpoint and from a management and cultural standpoint, and that it would ultimately provide a sustainable competitive advantage in the real estate brokerage industry.

Keller continued to manage the company throughout the 1980s and into the early 1990s, opening additional offices in Austin and other cities in Texas. Not all of these offices proved to be as successful as the original Austin office, although Keller had continued confidence that the Keller Williams model would work. In 1992, he began to consider taking the company national. At that time, he met Mo Anderson and discussed with her the idea of opening an office in Oklahoma. Anderson, who was in her mid-50s at the time, had grown up as the daughter of a tenant farmer and spent her early career as a public school music teacher. Later, she entered the real estate industry and successfully managed a Century 21 office in Edmond, Oklahoma, which she eventually sold to Merrill Lynch. At the time, it was the third most productive office by transaction volume in the Century 21 franchise system (7,500 offices) even though the average home price in Oklahoma was substantially below the national average.

Anderson recognized the promise of the Keller Williams model, having herself implemented similar policies and practices in her Century 21 office, and quickly went to work building the Oklahoma Keller Williams office. By 1995, Keller recognized that Anderson held many leadership skills that he himself lacked and asked her to take over as CEO of the company. Under Anderson's leadership over the next 11 years, Keller Williams corrected operational issues at offices established early on, standardized its operational model, and successfully grew to over 600 offices and 72,000 agents (see **Exhibit 1** for Keller Williams growth statistics). By 2006, at the age of 69, Anderson ceded much of the management of the company to Mark Willis, who assumed the role of president and CEO, and to Mary Tennant, COO. However, Anderson continued to play a very visible leadership role in the company as vice chairman.

The Keller Williams Model

The Keller Williams approach combined an economic model that delivered profits through economies of scale and a cultural model based on interdependent relationships and succeeding through the efforts of others. Keller Williams believed that its model was uniquely differentiated from that of its two primary competitors: traditional real estate brokerages and 100-percent commission organizations.

Traditional real estate brokerages that were either part of a national franchise or independently owned operated under what Keller Williams described as a "dependent-relationship model."[7] These companies spent millions of dollars on advertising to increase local awareness of their brand, which they believed gave them an advantage in attracting business in the marketplace. The agents who worked at these companies sought to gain business referrals and increase their own reputation in the marketplace through an association with this brand. Even though agents at these brokerages were independent contractors, the office manager made all major decisions in a top-down manner and the relationship was culturally one of employer-employee. For example, in recruiting a talented real estate agent to his office, the broker could cut special side deals that included a more attractive commission split or other financial terms without the other agents in the office knowing.

The 100-percent commission organizations, in particular RE/MAX, operated under an "independent-relationship model." In charging agents a fixed expense for the use of office space and the company's name brand, these firms effectively created a culture where agents operated largely as independents within the office. Very successful agents were attracted to the model because it provided generous commission splits; however, it did not create a culture of people working together to improve their own success and the success of the whole office.

---

[7] Interview with Mark Willis, president & CEO, Keller Williams Realty, November 8, 2006. The language of dependent, independent and interdependent relationships adopted from Stephen Covey.

Keller Williams described its own business model as an "interdependent relationship" between the owners of the local office and the agents, designed to achieve profits through economic scale. Both the brokerage and the agent were expected to profit as partners, sharing in both the net income and the decision making. Not liking the connotation implicit in such words as "broker," the company referred to its brokerages as "market centers," the owners of the market centers as "operating principals" (or OPs), and the individuals who led the market centers as "team leaders." The agents, the OPs, and the team leaders were expected to succeed through each other's efforts.

The Economic Model

The Keller Williams economic model was based on keeping fixed expenses low and generating high commission volume to achieve economies of scale and excess profitability at the market-center level. This economic leverage was driven primarily by having a significantly larger number of agents per market center than competitive real estate companies. Where the average brokerage in the U.S. had 49 agents per office in 2006, the average Keller Williams market center had 174 agents. As a result, the average Keller Williams market center generated significantly higher transaction volume and gross commission income than its competition. This higher aggregate transaction volume at the market-center level more than compensated for lower average sales productivity per agent (see **Exhibit 2** for information on Keller Williams market center productivity versus its competition).

Both traditional brokerages and 100-percent commission organizations failed to achieve similar economies of scale because their offices were located too close together. The international headquarters for those companies, seeking to maximize franchise fees by increasing the number of offices opened, allocated too small a territory to each brokerage. These brokerages might achieve a large market share of both agent count and transaction volume in a given territory but this market share was split among more than one office. As a result, these franchises operated with a larger fixed cost base that decreased their profitability.

In contrast, the Keller Williams model encouraged each market center to keep overhead low and to lead growth by building revenues before incurring the associated expenses. The main driver of profitability was agent count, with market centers designed to break even at approximately 40 agents. Keller Williams referred to the first 18-month period that a market center was in operation as the *launch period.* The most profitable Keller Williams market centers often had 40 agents recruited within the first month of operation and increased that count to 100 agents by the end of the launch period.

Finally, Keller Williams gave explicit instructions to OPs and team leaders about how to manage a market center to maximum profitability. The instructions covered such specific issues as budget and cash flow management, through which Keller Williams sought to instill a regimented business management perspective to the operation of the market center.

Compensation Model

The commission split that Keller Williams offered agents was a hybrid of that offered by traditional franchises and 100-percent commission organizations. The Keller Williams agent received a 70/30 commission split from the first dollar of gross commission income (GCI) generated. The agent was responsible for paying a franchise fee to the international office each year, which was capped at $3,000. The agent was also responsible for paying a fee to the market center, referred to as *company dollar*. The company dollar was also capped, at a level that varied by region, with areas with high average home prices having a higher cap to account for the general higher cost of doing business in such areas. The cap was determined by the OP at the time of launch and generally varied from $20,000 per year to upwards of $50,000 per year. The agent kept all GCI generated above these payments. The agent was charged for all variable expenses out of their retained portion of GCI (see **Exhibit 3** for a comparison of Keller Williams and competitor commission splits).

Agents who generated sufficient GCI to pay the maximum company dollar to the market center were referred to as cappers. From the perspective of the market center, it was profitable to increase the number of cappers because these individuals were making the maximum contribution to cover the market center's fixed costs; that is, they were the most efficient revenue producers. Agents who produced above the cap did not generate additional revenue to the market center and therefore made no additional contribution to profitability. Because the market center was largely a fixed-cost operation, a high number of cappers led to a high level of profitability.

Keller Williams was unique among real estate companies in that it offered a second source of income—profit share—to its agents. The formula for distributing profits was based on the agents each agent recruited to the company, the productivity of those agents, and the cash profits generated by each market center. This formula gave agents credit not only for the productivity of agents they directly recruited but also agents that those agents recruited in an elaborate step-function that extended seven levels. Importantly, agents were given credit and a piece of profit share regardless of which market center they recruited an agent to; an agent in Texas could received profit share for the productivity of an agent that s/he referred to a Florida market center.

Every month on the 21st day of the month, each market center was required to transmit a report of the profits it had made to the international office. These numbers were fed into a centralized system which computed the profit share owed to each agent in the company. All market centers used the same profit share calculation:

- 25 percent of the first $2,990 in market center profit was contributed to the profit share pool.
- 35 percent of the next $8,250 was then contributed to the pool.
- 50 percent of any profit above $11,240 was also contributed to the pool.
- The remaining profits belonged to the OP of each market center as a return on his or her capital.

The total profit pool was then allocated to all the agents in the company according to the profit sharing formula (see **Exhibit 4** for the profit sharing formula). Effectively, the profit share rewarded the recruitment of high productivity agents. Although the size of the profit share varied based on a number of factors, an agent with approximately 10 people in his or her "tree" (at all seven levels) would receive about $200 per person annually from the profit share formula; an agent with 200 people in the tree would receive about $90 to $95 per person; and an agent with 500 people would receive $75 per person. Importantly, a Keller Williams agent who retired from the company would continue to receive profit share so long as the agents they recruited remained with the company. Even if the agent died, his or her estate would continue to receive the profit share. This policy represented a rare form of residual income in an industry where agents typically saw their income stop entirely upon retirement.

In 2005, Keller Williams shared profits of $48.5 million with its agents. The company expected to have a total profit-share pool of $150 million by 2010 (see **Exhibit 5** for the historical growth in profit share). No other national franchise in the real estate industry had a common technology and accounting platform shared by all offices whereby it could easily replicate this calculation. Implementing such a system for established real estate companies would represent a significant investment.

The combination of the Keller Williams economic model with the two-part compensation system resulted in a system that offered high profitability both to agents and to the market center OPs (see **Exhibit 6** for a comparison of the profitability of Keller Williams to that of top real estate companies).

Cultural Model

Two essential factors that led to Keller Williams' rapid growth were the economic model of achieving outsized profits at the market-center level through economies of scale and the compensation model of offering a generous commission split and a share of the profits. Yet according to the leaders of Keller Williams, it was the cultural model of interdependence and success through the efforts of others that was the critical element leading to Keller Williams' overall success. Mary Tennant, COO, stated: "We know for a fact that our systems don't work without our culture. We need our culture to reach our full potential."[8] Mo Anderson called the culture "the glue that holds it all together."[9] According to Sharon Gibbons, former vice president of finance, "It's very difficult to separate the culture and the systems, because the systems are written for the culture and the culture exists for the systems."[10]

The Keller Williams culture was described in the company's mission, values, and belief statements and was reflected in all aspects of the company's systems, policies and practices.

Mission, Values, and Beliefs

The Keller Williams mission was: "To build careers worth having, businesses worth owning, and lives worth living." Building careers worth having meant that every individual—whether an agent, an OP, a team leader or other position—was expected to strive to reach the highest level of professional performance. It also meant that those individuals should help those around them to reach that highest level. Building a business worth owning meant a company that was highly profitable, with those profits shared by the OPs and agents alike through profit share. Creating lives worth living meant behaving at the highest ethical and moral level possible, with the fruits

[8] Interview with Mary Tennant, COO, Keller Williams Realty, November 8, 2006.

[9] Interview with Mo Anderson, vice chairman, Keller Williams Realty, November 8, 2006.

[10] Interview with Sharon Gibbons, VP of MCA Division, November 8, 2006.

of that effort clearly visible through a sound reputation and a practice of giving back to the local community.

The company's values were:

- God, family, then business.
- We believe real estate is a local service business driven by individual real estate agents, their local images, their centers of influence, and their client base.
- We believe our associates should be treated like stakeholders.
- We believe stakeholder companies always measure profit or loss, open the books, and tell the truth.
- We believe who you are in business with really does matter.
- We believe profit matters.
- We believe no transaction is worth our reputation.

Mo Anderson elaborated on the company's value system:

> The first one is the most important one to us and that is "God and family first, and then business." Well that's about as politically incorrect as you can get, but you know what, I don't care. I tell the people who come to see us – because we make everybody come to see us before they think seriously about buying a franchise – I tell them up front that you need to know that God and family are really important to this company. Now you may be Jewish or Buddhist or you may be Christian, but whatever your thing is, that and your family are supposed to be first. And this business is second. And if that doesn't feel right to you, then we're not a match. Because that's the most important value we have.[11]

Keller Williams' belief system was documented by Gary Keller in collaboration with a group of his top-performing agents from the original Keller Williams office in southwest Austin. They were written as a description of the aspects of the work environment and professional standards that these agents felt led to their success as a business. This belief system was later institutionalized by Anderson and the other leaders of Keller Williams as a set of standards that all team members were expected to use to guide their professional interactions. According to Gary Keller:

> Working together successfully with anyone else, one of the things that you begin to realize is there has to be a certain amount of commonality, and usually it's commonality of culture – of how you think, how you talk to each other, how you make decisions together, how you interact together.[12]

The common culture of Keller Williams was described in this belief system which Gary Keller encapsulated with the acronym WI4C2TS (pronounced "why four see two tees"):

- Win-Win Or no deal

[11] Interview with Mo Anderson, Keller Williams, July 17, 2006.

[12] "Gary Keller on the History of Keller Williams," Keller Williams Realty, Inc., 2006.

- Integrity — Do the right thing
- Customers — Always come first
- Commitment — In all things
- Communication — Seek first to understand
- Creativity — Ideas before results
- Teamwork — Together everyone achieves more
- Trust — Starts with honesty
- Success — Results through people

Of these, Gary Keller believed that the first and the last were the most important:

> Really it became the "win-win philosophy" because that was the first one… and it became known for the last S, which is "success through others, not around them." And I really believe that when you talk to people about WI4C2TS that even though there are some who can recant all of it, what almost everyone remembers is the first and the last… When you go to make decisions, and you go to succeed, that your literally include everyone that you can in the decision-making process and ensure that everyone gets a success through it… And so for me, "win-win" and "succeeding through others" were like book ends to a philosophy that has built this incredible culture.[13]

Mark Willis, president and CEO, agreed that the company's belief system was integral to the growth of Keller Williams and used the "independent-relationship model" of RE/MAX as a point of contrast. Specifically, he disagreed with RE/MAX President David Liniger's assertion that brokers were in the real estate agent business, with agents as the customer of the broker:

> The agent is not your customer. The agent is your partner. And you have got to treat them like your partner. If you want a doomed relationship, go into a customer relationship and overcharge them or give them less than what they can get some place else and you will be the problem. But the language of partners is that we are in this together, we're going to own problems together, we're going to solve them together, we're going to work in a win-win solution where you are going to get the most out of a relationship and I get the most out of a relationship, and it's a higher level relationship. Partners won't leave you. They won't hold a gun to your head, but customers will.[14]

In order for an agent to feel like a stakeholder and partner of the company, Willis believed that the company had to maintain four practices. First, the company had to share its profits. Second, the company had to involve agents in the decision making. Third, the company had to open its financial books. And fourth, the company had to train its agents to be better agents and business people. Together, these practices created a culture of interdependent relationships that allowed team members to reach a high and satisfying level of success.

---

[13] Ibid, op. cit.
[14] Interview with Mark Willis, president and CEO, Keller Williams Realty, November 8, 2006.

Organizational Structure and Policies as Manifestation of Culture

The leaders of Keller Williams believed that the structure of the company grew out of its culture and that the company's systems, policies and practices were a product of the WI4C2TS belief system. Also, they believed that the economies of scale and high profitability of their market centers were the direct result of the culture and organizational practices, and that market centers that failed to achieve high levels of profitability failed because they did not successfully implement the culture and practices.

Structure of the Market Center
The market center was owned by an operating principal (OP) who was then responsible for hiring a team leader to lead the market center. It was important that these two roles be separated and that the OP not also serve as the team leader. Gary Keller believed that in order for the team leader to improve the market center over time and help it achieve its full potential, an outside person should hold him or her accountable for results. In addition, a successful team leader required a unique personality set that was different from that of an OP, because of the responsibilities required by the position.

Before being hired as the team leader for a new market center, the candidates for the position had to take a personality test designed for Keller Williams by a third-party consulting company. The model evaluated individuals according to four personality attributes and each job function had its own optimum mix. The ideal profile of a team leader was:

- Drive: The team leader was expected to have high drive in that s/he was results-oriented, decisive, demanding, and direct. A person with low drive would be described as process-oriented, cautious and conservative.
- Sociability: The team leader was expected to be highly sociable. Sociability should be a natural quality and not something that required a lot of effort or psychological energy to maintain.
- Calmness: The team leader should not score high on this factor but instead should be impatient, constantly changing, and fast-paced.
- Conformity: The team leader should also not score high on this factor but instead should be self-reliant, free in his or her actions, opinionated, and individualistic. S/he should not be a perfectionist, overly precise, detail-oriented or require direction.

A unique personality profile was designed for all positions within Keller Williams, including the CEO, and all candidates hired into the company were expected to take the test in a process called Recruit Select. Candidates who did not have matching personality profiles were encouraged to apply to more appropriate positions.

The first responsibility of the team leader in launching a new market center was to recruit a core group of five top-performing agents from other companies in the local area. It was important that the team leader recruit a core group of agents who were influential in their market, because these agents would be responsible for recruiting additional agents during the launch period. Successful agents who were respected in the local market but did not have influence would not be effective recruiters. Because a market center did not begin to break even in profitability until it reached 40 agents, it was important that the size of the team scale quickly. Both the team leader and the core group had to be in place before the franchise agreement for a new market center was approved by the international office.

Because the role of team leader was filled by someone other than the owner, the team leader built his or her income primarily through profit share by recruiting agents, particularly cappers. A team leader who was able to recruit an influential core group that in turn recruited several more agents to the market center would quickly build his or her income through profit share. Because the profit share formula gave credit for individuals recruited up to seven degrees of separation away, the team leader received a share of the profits for all of the agents recruited to the market center. The economies of scale implicit in the fixed-cost market center meant that the team leader and core group had every incentive to build the agent count quickly (see **Exhibit 7** for information on the companies from which Keller Williams attracted its most successful agents).

Agent Leadership Council

The management of the market center was not the sole responsibility of the team leader, nor was it the joint responsibility of the OP and the team leader. The leaders of Keller Williams believed that agents had an equal stake in the success of the market center and therefore should share in the decision-making process. As a result, management of the market center was a shared responsibility of the OP, the team leader, and the top agents within the market center who all jointly served on what was called the Agent Leadership Council (ALC). Subcommittees of the ALC made recommendations on specialized issues such as financial planning, recruiting and retention, marketing and advertising, training, technology, social events, and philanthropic giving. The ALC structure ensured that each market center was run as a true partnership.

The leaders of Keller Williams believed that having an ALC management structure accomplished several goals. First, because the top 20 percent of agents in a market center (measured by gross commission income) were invited to sit on the ALC, the committee was comprised of the agents with the most knowledge of the local market. These individuals would be able to make better decisions affecting the success of the business. Second, and closely related, management decisions that were made by top agents instead of an owner would have better validity throughout the market center, particularly with agents. Decisions would be recognized as having gone through a negotiation and buy-in process and were less likely to be perceived as "cram downs." Third, by participating in management decisions, agents would learn a business mentality with special attention to cost control. When agents were asked to approve fixed costs and pay for them by effectively reducing their own profit share, they had more incentive to be cost-conscious. Finally, the ALC structure led to better retention of top-performing agents who felt they were truly managing their business.

Willis explained how the ALC structure and shared decision making led to a greater sense of partnership:

> What we do is we empower our people to make decisions that they literally own and are accountable for, because they have been given a voice. They've been treated like partners and they've been respected.... If I define your win for you, and I tell you how we are going to win on some level you are going to resent me. Whereas on the other hand, if you get to define your win, and I help you get that

> win, then you're going to feel good. You're going to feel like you're contributing and that somebody has given you what you want.[15]

In Keller Williams, there was an ALC not only at the local level, but also at the city, regional, and international office levels. Agents who served on these higher-level ALCs were greatly respected throughout the company.

Open Books

In order for the profit share and ALC decision-making systems to maintain their integrity, Keller Williams operated an open book policy in each market center. All agents had access to view the expenses and revenues of the market center. Because the profit share formula did not change, agents could run the calculations themselves to make sure they were receiving their proper share. Although books were not officially open across the company, an individual who recruited an agent to another market center could have access to that market center's books on a one-off basis, if requested. In addition, the minutes of ALC meetings were available for agents to review, which meant that there were no secrets between the leaders of the market center and the agents. For example, in the event that the team leader made a special arrangement in recruiting a top agent into the office, the details of that deal were decided by the ALC and became public information throughout the market center.

Training

The leaders of Keller Williams believed that if individuals were expected to play a significant role in the decision making and management of the company and their careers, then the company had an obligation to provide the training needed for them to achieve their full potential. Training was such a key element of the company culture that Dave Jenks, vice president of research and development, referred to Keller Williams as "a training and consulting company masquerading as a real estate company." He went on to describe Keller Williams as "the most training-oriented company in the industry."[16] The company used extensive training to turn real estate jobs and real estate office management into a business. Examples of training events and seminars included:

- Camp 4-4-3: Training for all agents to achieve 80th percentile industry productivity.
- Millionaire Real Estate Agent: Training for Keller Williams and non-Keller Williams agents based on techniques published in the book with the same title.[17] It was also an effective recruiting tool for the company.
- Mega Agent Camp: Training for top-producing agents (GCI greater than $180,000) designed to take their productivity to the next level.
- Mega Management Camp: Training for OPs and team leaders focused on leadership and management issues.

---

[15] Ibid, op. cit.

[16] Interview with Dave Jenks, vice president of research and development, Keller Williams, November 8, 2006.

[17] Keller, Gary, Dave Jenks and Jay Papasan, *The Millionaire Real Estate Agent*, (New York: Rellek Publishing Partners, McGraw Hill, 2004).

- Masterminds: Group seminars and break-out sessions for OPs, team leaders, and agents, led by Keller Williams leadership.
- Family Reunion: Combination of educational, inspirational, and fun activities for all Keller Williams team members.

The leaders of Keller Williams believed that education was an ongoing process within the company. In addition to real estate and management techniques, the company also taught life-improving perspectives that the company thought led to improved performance. According to David Osborn, vice president of CORE Services:

> Education in our company is massive, focused, and ongoing. People think you get out of college and education ends but in reality the education just begins. It's not so much education focused on how to sell another deal, and we do plenty of that, but it's life mastery. How do you think correctly to succeed? We teach that all the time. Now if only 5 percent of our people get that, they will permeate the entire organization. You need a few people in the office to get that and they will set the standard for everyone.[18]

(See **Exhibit 8** for an example of life perspectives taught by the company.)

BE THE BEST THAT YOU CAN BE

The leaders of Keller Williams believed that business should be infused with a higher purpose, and the company's culture encouraged team members to commit to a lifestyle of self-mastery that would improve both business and life skills. People within Keller Williams spoke of the company's "productivity warrior attitude" about increasing efficiency and profitability. They spoke of a desire to "absolutely develop wealth and then share it" through charitable activities. According to Mo Anderson, "The energy this culture creates feeds the bottom line."[19]

Although the company was very selective in terms of the individuals to whom it awarded franchises, almost any aspiring real estate agent could be hired. Over time, these agents were expected to prove themselves, and those that did not reach minimum levels of productivity and contribute to the bottom line were asked to leave. As a result, agent turnover could be high. Dave Osborn cautioned: "Judge us by who we keep, not who we hire." Part of that assessment was sales productivity, with the specific criteria decided by each market center. Just as importantly, however, agents were expected to buy in to the culture, policies, and processes of the company; those that did not often self-selected out of the company.

Also, agents were expected to adhere to a basic level of moral conduct, and part of the independent contractor agreement that each agent signed granted Keller Williams the right to fire the agent for "moral turpitude"—grossly inappropriate behavior that harmed other team members, external partners, or customers. In addition, agents were asked to leave if their conduct undermined the integrity of the company or its processes, such as using a position of influence to try to claim credit for recruiting agents who had actually been recruited by another

[18] Interview with David Osborn, vice president of CORE Services, Keller Williams Realty, November 8, 2006.
[19] Interview with Mo Anderson, November 8, 2006.

person (in order to redirect profit share to themselves). Keller Williams was unique in the industry, however, in that all terminated agents were given the rights to the homes they had listed in MLS; by law, listing rights were held by the brokerage, and other companies in the industry insisted on retaining the listings of a terminated employee.

Once an agent did achieve high levels of profitability, s/he was expected to be an engaged contributor to the community. The company did not mandate contributions, but implicit in the "win-win" belief system was the notion that the more an individual gave, the more s/he would receive, and the boundaries of this behavior extended beyond the company to the community. The leaders of the company were active philanthropists through a foundation they established out of their own income called KW Cares, a 501(c)3, which provided emergency financial assistance to any member of Keller Williams in need because of tragedy or illness. For example, after Hurricane Katrina, KW Cares raised \$5.3 million dollars from Keller Williams offices nationwide to support more than 700 Keller Williams team members who were displaced by the catastrophe. By comparison, the National Association of REALTORS® with more than 1.2 million members raised \$5.8 million.

Keller Williams agents were encouraged to give 10 percent of their income to the charity or community organization of their choice and to make giving a part of their lifestyle. According to Mo Anderson:

> I want people to experience the higher purpose of business. In my humble belief, the higher purpose of business is to absolutely develop wealth, become wealthy, and then share that wealth with the charities that you are passionate about, with the religious organization you are passionate about, the poor, or whatever it is that moves your heart. I encourage our people that if you have wealth, and you're not sharing it, you're going to miss out on one of life's great learnings .... There's no joy in life like being able to step up to the plate and help somebody in need.[20]

Looking Forward

The leaders of Keller Williams believed that they had a competitive model that was superior to that of every other major company in their industry. The successful application of this model led to exponential growth in market centers, agent count, and company profits. The company expected to end the year 2006 with over 75,000 agents. Looking forward, they expected to have over 150,000 agents by 2010 and 300,000 agents by 2015. "At that time," said Mark Willis, "any agent who is not with Keller Williams probably shouldn't be."

No single policy or practice accounted for the company's financial success. It was the unique way in which the company's economic model, compensation model, culture, and company practices worked together to achieve results. According to Mark Willis:

> Keller Williams is not different because we profit share. We aren't different as a company because we educate. We aren't different because we open the books. We aren't different because we have an ALC and give agents a voice in the

[20] Ibid, op. cit.

decision making. We are different because we succeed through others... We are all about succeeding and achieving results through other people.[21]

Expanding into New Territories

As Willis thought about the expansion plans he discussed with Anderson and Keller, he knew that it was critical that the company find OPs who would take both the systems and the culture with them into their territories. He and his regional managers would have to review very carefully the applications they received requesting franchise rights for new territories to ensure that the applicants understood both the economics and the vision of the company.

QUESTIONS

1. Explain the way in which the company's economic model, compensation model, culture and company practices work together.

    a. What role does the Agent Leadership Council play from both a management perspective and a cultural perspective? Is it necessary for Keller Williams to have an ALC?

2. In general, how important is the compensation system to Keller Williams?

    a. What is the potential payout curve for commission splits for a Keller Williams agent versus an agent at a traditional real estate company?
    b. What is the potential payout from profit sharing for a Keller Williams agent?
    c. What behaviors do you believe are encouraged by the Keller Williams compensation structure?
    d. How important is the company policy of maintaining open books?
    e. Does Keller Williams have a competitive advantage because of its culture? Could a competitor successfully compete against Keller Williams by adopting its economic models but without adopting its culture?

3. Assume Keller Williams were planning to add a new market center in the Laguna Niguel, CA area and you were applying for the franchise rights to that territory (see **Exhibit 9** for market data on Laguna Niguel).

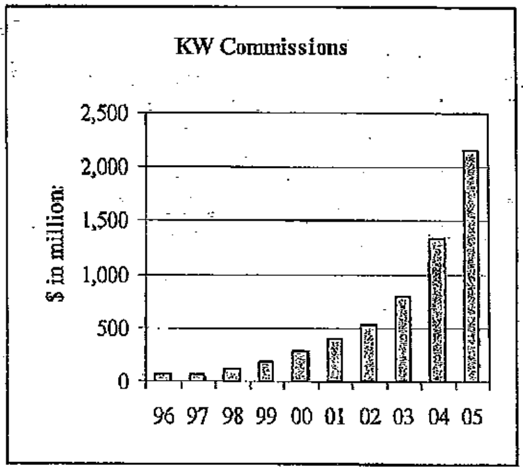
    a. How many agents would you plan to recruit before launch and how many would you expect to have by the end of 18 months?
    b. From which companies would you expect to successfully recruit these agents?
    c. How would the recruitment of a core group help you to achieve your 18-month recruitment goals?
    d. What sales productivity (gross commission income) would you expect your agents to have achieved by the 18th month?

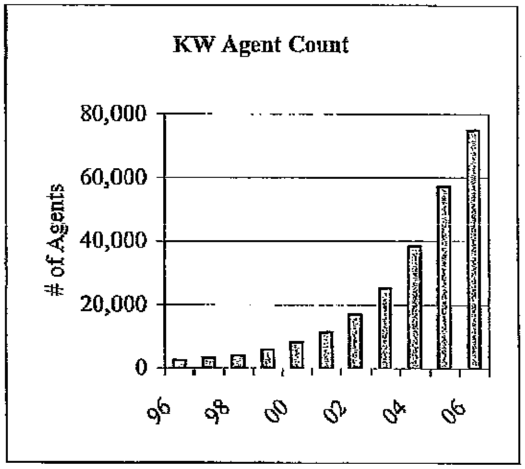
---

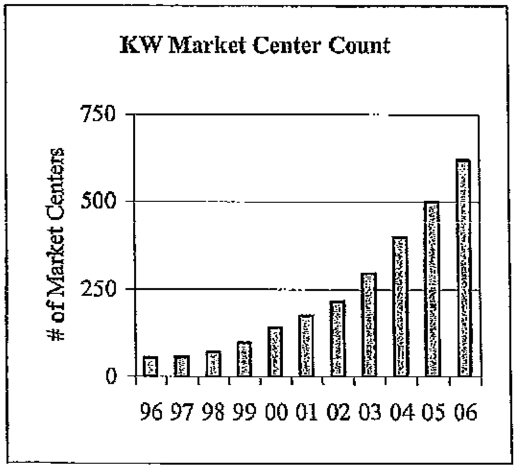
[21] Mark Willis, speech at Keller Williams Launch Boot Camp, November 9, 2006.

e. What is the expected profitability of your market center after 18 months and how is it dependent upon the number of agents? Their productivity?
f. How does the profitability of your market center after 18 months compare to that of your competitors?

Exhibit 1
Keller Williams: Growth Statistics (1996 – 2006)







Source: Keller Williams Realty.

Exhibit 2
Keller Williams vs. Industry Competitors: Productivity Statistics

	Agents per office				Volume per office ($ in millions)			
	2002	2003	2004	2005	2002	2003	2004	2005
National average	47.1	45.2	47.2	49.1	113.5	125.8	140.3	154.7
Century 21	37.8	37.9	37.2	36.1	74.6	78.7	88.7	93.6
Coldwell Banker	42.3	35.8	34.6	50.1	124.6	87.3	94.9	172.5
ERA	34.0	24.6	24.7	28.2	89.9	56.8	61.7	68.4
GMAC	33.8	35.7	37.6	45.6	89.9	92.3	105.2	129.7
Keller Williams	**116.0**	**163.1**	**138.1**	**174.1**	**155.6**	**214.9**	**194.5**	**367.1**
Prudential	38.2	41.6	43.5	44.4	89.2	100.8	117.0	120.9
Realty Executives	32.1	39.7	43.2	41.6	108.9	132.1	153.2	162.7
RE/MAX	44.1	42.5	42.3	45.3	172.7	182.1	190.0	212.6
Independents	39.6	45.0	45.3	46.8	107.5	118.4	126.6	133.0

	Sides per office*				Sides per agent*			
	2002	2003	2004	2005	2002	2003	2004	2005
National average	493	508	508	504	11.9	11.2	10.8	10.2
Century 21	424	424	414	377	11.2	11.2	11.1	10.3
Coldwell Banker	491	495	481	468	10.4	13.7	13.9	9.3
ERA	455	343	346	372	13.4	14.0	15.1	13.2
GMAC	347	337	335	338	10.3	9.5	8.9	7.4
Keller Williams	**885**	**1252**	**929**	**1653**	**7.6**	**7.7**	**6.7**	**9.5**
Prudential	383	397	392	364	10.0	9.5	8.9	8.2
Realty Executives	606	622	643	586	18.9	15.7	16.1	14.1
RE/MAX	861	776	761	745	19.6	18.3	18.0	16.1
Independents	462	486	465	475	11.7	10.8	10.3	10.1

* The term "sides" refers to transactions done by either the selling agent or the buying agent. Because there are usually two agents on each real estate transaction, the industry reports approximately twice as many sides as home transactions.

Source: Real Trends 500 Survey.

Exhibit 3
Keller Williams vs. Industry Competitors: Commission Splits

1. Century 21 – Starts at 50 / 50 split with 8 percent off the top (6 percent royalty, 2 percent advertising fee).

   At $25,000, GCI split 55 / 45
   At $50,000, GCI split 65 / 35
   At $75,000, GCI split 70 / 30
   At $100,000, GCI split 75 / 25

2. RE/MAX – Charges $2,000 per month desk fee.

3. Keller Williams – 70 / 30 split. 6 percent royalty, capped at $3,000. Company dollar capped at $30,000.

Volume	GCI	Century 21	RE/MAX	Keller Williams
		Agent Dollars		
$ 1 M	$ 30,000	$ 14,030	$ 6,000	$ 19,200
$ 2 M	$ 60,000	$ 30,130	$ 36,000	$ 39,000
$ 3 M	$ 90,000	$ 48,760	$ 66,000	$ 60,000
$ 5 M	$ 150,000	$ 89,700	$ 126,000	$ 117,000
$ 10 M	$ 300,000	$ 193,200	$ 276,000	$ 267,000
		Company Dollar		
$ 1 M	$ 30,000	$ 13,570	$ 24,000	$ 9,000
$ 2 M	$ 60,000	$ 25,070	$ 24,000	$ 18,000
$ 3 M	$ 90,000	$ 34,040	$ 24,000	$ 27,000
$ 5 M	$ 150,000	$ 48,300	$ 24,000	$ 30,000
$ 10 M	$ 300,000	$ 82,800	$ 24,000	$ 30,000
		Franchise Royalty		
$ 1 M	$ 30,000	$ 2,400	0	$ 1,800
$ 2 M	$ 60,000	$ 4,800	0	$ 3,000
$ 3 M	$ 90,000	$ 7,200	0	$ 3,000
$ 5 M	$ 150,000	$ 12,000	0	$ 3,000
$ 10 M	$ 300,000	$ 24,000	0	$ 3,000

Commission splits, caps, and royalty rates are indicative only and vary by office.

Source: Keller Williams Realty.

Exhibit 4
Keller Williams: Profit Share Formula, Sample

1. Calculation of Market Center Profit

Gross Commission Income (GCI)	$ 150,000
(-) 70% Agent Split	105,000
(=) Company Dollar	$ 45,000
(-) KW Approved Costs	22,500
(=) KW Market Center Profit (or Loss)	$ 22,500

2. Creation of Monthly Profit Share Pool

	Profit Share Pool		Owner Profit	
Level 1 (first $2,990)	25%	$ 747.50	75%	$ 2,242.50
Level 2 (next $8,250)	35%	$ 2,887.50	65%	$ 5,362.50
Level 3 (above $11,240)	50%	$ 5,630.00	50%	$ 5,630.00
		$ 9,265.00		$ 13,235.00

3. Contribution to Profit Share by Agent

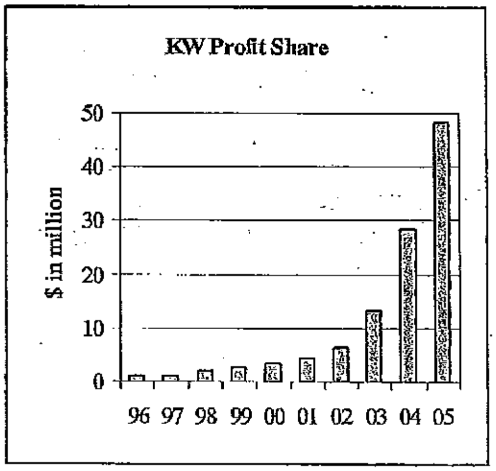
	Agent Company $		**Total Company $**		**% of Profit Share**
John contributed	$ 3,886	out of total	$ 45,000	equals	8.64 %
			Total Profit Share Pool		**Contribution to Profit Share**
That	8.64 %	times	$ 9,265	equals	$ 800

4. Distribution of Profit Share to Agent's Upline (KW Team Members Who Recruited the Agent)

1st Level Sponsor	Mary	gets	50 %	$ 400
2nd Level Sponsor	Tom	gets	10 %	$ 80
3rd Level Sponsor	Joe	gets	5 %	$ 40
4th Level Sponsor	Nancy	gets	5 %	$ 40
5th Level Sponsor	Jane	gets	7.5 %	$ 60
6th Level Sponsor	Mike	gets	10 %	$ 80
7th Level Sponsor	Carol	gets	12.5 %	$ 100
			100 %	$ 800

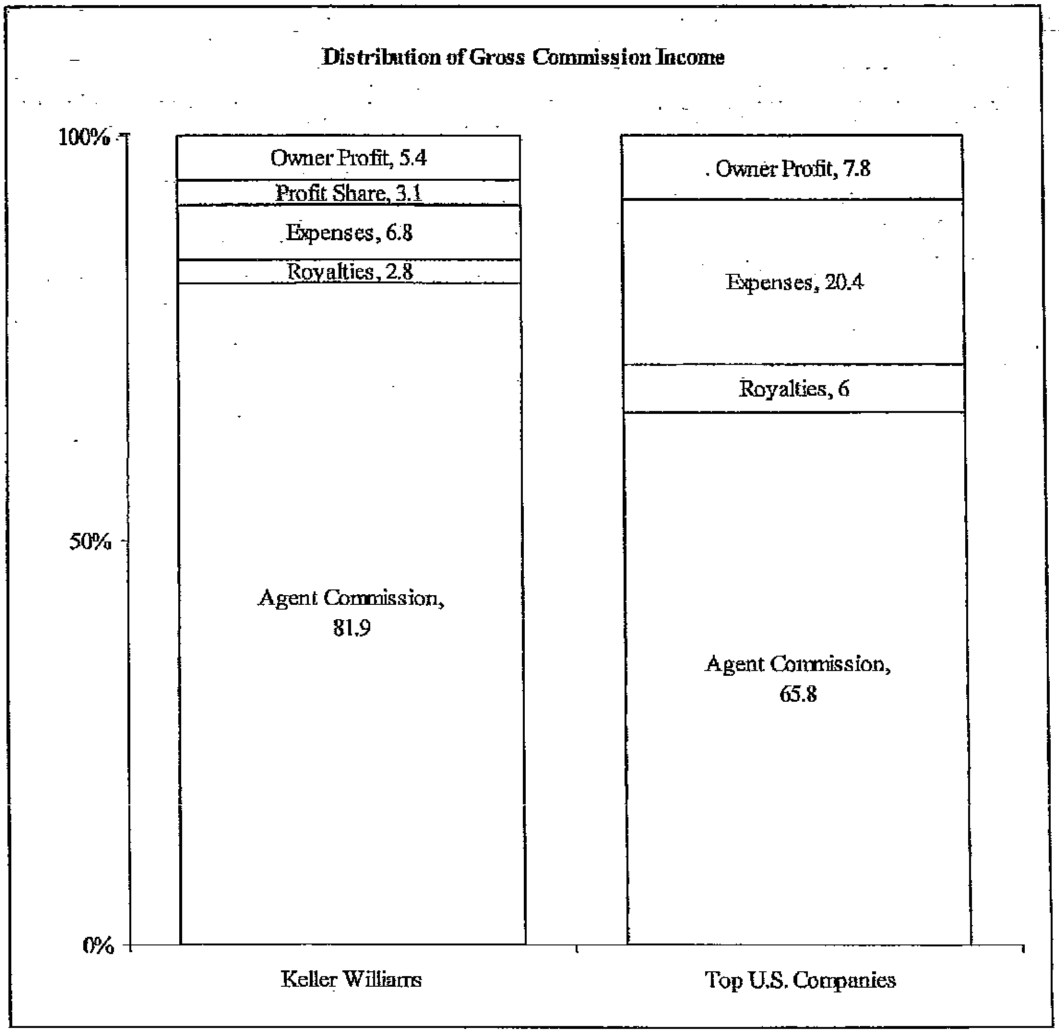
Source: Keller Williams Realty.

Exhibit 5
Keller Williams: Historical Growth in Profit Share



Source: Keller Williams Realty.

Exhibit 6
Keller Williams vs. Industry Competitors: Big Picture Economic Model



Source: Keller Williams Realty. Based on 2005 performance of top 25 percent Keller Williams market centers versus top 500 real estate companies as reported by Real Trends (October 2005). Estimate of royalties for top 500 real estate companies for those national companies that charge 6 percent on all GCI (may vary from office to office and company to company).

Exhibit 7
Keller Williams: Recruitment of Mega Agents

The Companies Mega Agents Were with Prior to Joining Keller Williams

Rank	Company	Keller Williams
1	RE/MAX	34%
2	Coldwell Banker	17%
3	Century 21	9%
4	Prudential	7%
5	Realty Executives	2%
6	Crye-Leike	1%
7	Ebby Haliday	1%
8	ERA	1%
9	GMAC	1%
10	Home Services of America	1%
11	Long & Foster	1%

Source: Keller Williams Realty, based on survey of top producing agents only (median volume $13.0 million and median gross commission income $329,000 at previous agency).

Exhibit 8
Keller Williams: Life Perspectives

Personal Perspective, Overview

Step 1:	Commit to "Self-Mastery" Possession of great techniques, skill and habits that makes one master of a subject	"I'm going to nail it!"
Step 2:	Commit to the 80 / 20 Rule 20 percent of the effort often leads to 80 percent of the results	"I want to change the predictable imbalance of my wealth"
Step 3:	Move from "E" to "P" "Entrepreneurial style" does what comes naturally "Purposeful style" uses models and systems	"I want to break through my ceiling and commit to models and systems"
Step 4:	Commit to Being "Learning Based" Effective learning as the foundation of the action plan to develop one's life; work smarter not harder	"I'm willing to be taught and to pursue learning"
Step 5:	Remove "Limiting Beliefs" Avoid limiting thinking and focus on unlimited thinking	"I will be positive"
Step 6:	Be Accountable Acknowledge reality, own it, find solutions and get on with it. Don't be a victim, seek blame, wait and hope.	"You can count on me"

Source: Keller Williams Realty.

Exhibit 8 (continued)
Keller Williams: Life Perspectives

Self-Mastery: How a learning-based individual becomes a black belt in life

The 10 Step Experiential Learning Process (Training)	**The 4 Steps to Personal Power**	**The 5 Steps to Unconscious Competence**
		1. Life of ignorance is Unconscious Incompetence
1. Read 2. Lecture 3. Discuss	1. Understanding "I get it" *Mentally*	2. Moves you into Conscious Incompetence
4. Participate 5. Analyze Case Studies 6. Analyze Role Models	2. Knowledge "I relate to it" *Emotionally*	3. Moves you into Conscious Competence
7. Role Play 8. Experience Structured Activities 9. Practice	3. Wisdom "I can & will do it" *Behaviorally*	4. Moves you into High-Level Conscious Competence
10. Move into **Self Mastery**	4. Personal Power "It's part of me" *Life Habits*	5. Moves you into Unconscious Competence
What You Do	**What You Experience**	**What You Become**

Source: Keller Williams Realty.

Exhibit 9
Competitive Market Data: Laguna Niguel, CA (Hypothetical)

1. Territory Profile

Estimated current population	61,891
Projected population in five years	61,813

2. MLS Information

	# of Transactions	Sales Volume
Five years ago	1,761	$ 507.5 M
Three years ago	1,841	$ 648.8 M
Last year	1,366	$ 569.5 M

3. Competitive Real Estate Brokerages

Company Name	Total Offices	Total Agents
Century 21	9	263
First Team	4	200
RE/MAX	4	228
Prudential	3	78
Coldwell Banker	3	147

4. Market Center / Real Estate Brokerage Budget

Operating Expense	Monthly
Rent	$ 3,000
Salaries (administrative)	12,000
Other	5,000
Base budget	$ 20,000
Costs associated with first $1M GCI	2,500
Base budget up to $1M GCI	$ 22,500
Incremental budget, each additional $ 1M GCI	$ 2,500