



A GOVERNANCE-STRUCTURE APPROACH
TO VOLUNTARY ORGANIZATIONS

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ABSTRACT

This paper develops a governance-structure theoretical understanding of voluntary organizations. Voluntary organizations are seen as governance structures reinforcing the norm of (generalized or balanced) reciprocity, making possible the pooling of resources based on the reciprocity principle. Voluntary organizations' governance structure presents some specific features in terms of formal ends, ownership, residual claims, decision-making procedures, accountability, checks and balances, control procedures and embedded incentives facilitating collective action oriented towards public or mutual interest or towards advocacy. Because the voluntary governance structure is also compatible with several types of coordination mechanisms, voluntary organizations are able to operate in complex environments, mobilizing resources from market operations, governmental subsidies, or from reciprocity (volunteering, donations) while pursuing civic and democratic objectives. Their governance structure allows them to mitigate coordination failures and remain comparatively more efficient than other organizational forms. However, voluntary organizations may be subject to governance failures, the result of which could undermine trustworthiness and efficiency.

INTRODUCTION

The main economic theories of nonprofit organizations – based on government failure (Weisbrod 1977) and market failure (Hansmann 1980; Ben-Ner and Van Hoomissen 1991) – explain why they, rather than for-profit or public organizations, produce certain goods and services. Economic theory essentially defines the voluntary organization as a non-profit organization, based on the fact that it cannot distribute any profit. This characteristic of non-profit organizations is referred to as the non-distribution constraint. However, as noted by contributors to the field (Ben-Ner and Gui 2003; Ortmann and Schlesinger 2003; Steinberg 2006), the non-distribution constraint neither guarantees trustworthiness nor is it sufficient to characterize voluntary organizations. Ortmann and Schlesinger (2003) have identified three challenges – incentive compatibility, adulteration, and reputational ubiquity – to be met by proponents of the non-distribution constraint in order to demonstrate that this constraint is sufficient to guarantee voluntary organizations' trustworthiness. The incentive compatibility condition implies that various forms of opportunistic behavior and misappropriation are effectively constrained by the non-distribution constraint. The adulteration condition requires that the non-distribution constraint be sufficient to avoid goal-displacement, whereas the reputational ubiquity challenge requires proponents of the non-distribution constraint to explain why reputation works in the case of the non-distribution constraint but not for for-profit providers.

Attempts to go beyond the non-distribution constraint have been made for example by Hansmann (1987), who states the role of patron's control on organizational behavior, and by Ben-Ner (1986), who underscores the importance of consumer control as a means to mitigate informational asymmetries. However, we still lack a general framework explaining how voluntary organizations mitigate market and government failures. This article seeks to sketch such a theoretical understanding of voluntary organizations, envisaged as governance structures (Williamson 1996) adapted to the coordination of purposive action, and able to alleviate different forms of coordination failures, namely market failure, government failure and collective action failure.

1. COORDINATION MECHANISMS

Organizations are collective actors characterized by their ability to centralize decision-making (Elster 2007: 427). Voluntary organizations display this characteristic of being a centralized decision-making structure as well, but differ from for-profit and governmental organizations inasmuch as their governance structure (formal goals, ownership, distribution of property rights, and decision-making procedures) is adapted to the requirements of collective action allowing the pooling of resources and of providing trust goods. From this perspective, voluntary organizations have recourse to hierarchy as a means of coordinating their constituencies. Coase (1937) and Williamson (1975, 1985) have shown that in the presence of transaction costs, the hierarchy may be more efficient than the market as a coordination mechanism. Voluntary organizations may also be seen as mobilizing different *coordination mechanisms* – which are institutionalized patterns or regularities (Enjolras 2000) – in order to achieve their goals.

Voluntary organizations, like other types of organization, operate in complex environments characterized by several coordination mechanisms. They are involved in different types of transaction that provide access to resources and enable diversification. For example, Weisbrod (1998a, 1998b) views nonprofits as multi-product organizations potentially producing three types of goods: a preferred collective good (the organization's mission-related output); a preferred private good; and a non-preferred private good (potential sources of revenue for financing the mission-related output). In this approach the private goods are produced in order to cross-subsidize the collective good. From this viewpoint, voluntary organizations may realize three types of transaction (Polanyi 1957a; Polanyi 1957b; Zelizer 1998): commercial transactions, where money is used as compensation in exchange for a good or a service; entitlement, where money, goods or services are allocated according to a predefined right to a share; and reciprocal transactions, where money, goods or services are mutually exchanged as a result of the norm of reciprocity (Gouldner 1960; Fehr and Gächter 1998). Each type of transaction corresponds to a type of resource for voluntary organizations. Public funding involves entitlement-based transactions; donations and voluntary work involve reciprocal transactions; and finally, revenues from sales involve commercial transactions. A "pure" voluntary organization is therefore one whose resources derive exclusively from donations and voluntary work, i.e. involve exclusively reciprocal transactions. Besides the "pure" type, three other types of nonprofit may be distinguished (Enjolras 2002), depending on their dominant resource. The "commercial" type is characterized by the predominance of the market output in its resources. The "third-party-funded" type occurs when public funds form the dominant part of its resources. And thirdly, the "community-based-economy" type combines market, voluntary and public resources. These transactional principles may also be conceived in terms of coordination mechanisms.

The first coordination mechanism to be considered is that of *collective action*. Voluntary organizations may be envisaged in terms of "pooling mechanism" (Horch 1994). They are organizations where people with shared interests associate and pool resources to further these interests. From this viewpoint, voluntary organizations involve the coordination of actors on the basis of mutual interest. But the pooling of resources also involves some kind of *reciprocity*. In reciprocal transactions the values are exchanged as the result of a reciprocal obligation. Transactions occurring within the family or a personal network, and involving personal links, are not coordinated by price considerations but by social and moral obligations (norms). Other types of transaction such as gifts and volunteer work are not coordinated by prices either. These types of transaction involve the conformity to a "general norm of reciprocity" (Gouldner 1960; Kolm 2006) defined as "a mutually contingent exchange of gratifications between two or more units". The obligation to requite a benefit or show gratitude to the person bestowing it appears as a powerful coordination mechanism in personal transactions involving trust, as well as in non-personal transactions such as giving and volunteering. The existence of *Homo Reciprocans* (Fehr and Gächter 1998), as reported in several games experiments, suggests widespread readiness to reward kind acts and punish hostile ones. In primitive societies, the connection between material flow and social relation may imply a given movement of goods, but a specific transaction – "by the same token" – suggests a particular social relation (see also Mauss [1923] 1991). As stressed by Sahlins (1972: 187), the array of economic transactions may be resolved into two types (Polanyi 1957a, 1957b). First, there are those movements between two parties known as reciprocity. Second, there are the centralized movements that imply collection from members of a group, and redistribution or "pooling" within this group. However, on a more general view, the two types merge, since pooling is an *organization of reciprocities*, a system of reciprocities.

Pooling is socially a *within* relation, the collective action of a group, whereas reciprocity is a *between* relation, the interaction of two parties. For Sahlins (1972: 190–3) reciprocity qualifies a whole class of exchange, a continuum of forms. At the one end of the continuum stand the assistance freely given, everyday kinship, friendship, and neighborly relations - the "pure gift" of Malinowski. "Generalized reciprocity" constitutes the solidary extreme, referring to transactions that are altruistic, transactions of assistance given and, if possible and necessary, returned. At the other pole, "negative reciprocity", or the unsociable extreme, as Gouldner phrases it, is characterized by the attempt to get something for nothing with impunity. At the midpoint, "balanced reciprocity" refers to direct exchange.

The second coordination mechanism involved in voluntary organizations is the market. In market exchanges, values are exchanged at bargaining rates (Polanyi 1957b) or at prices determined by the interplay of supply and demand, i.e. the market mechanism. Economists think of the economic system as being coordinated by the price mechanism. Each actor will behave taking into account the signal given by the price. In the general equilibrium model, producers and consumers coordinate their respective plans by the interplay of the price mechanism. The market appears then as a self-regulating mechanism. Each economic actor adjusts his behavior according to the same signal (the price).

Following the same logic, the third coordination mechanism involved in the voluntary organization is state-centered coordination. This coordination mechanism is associated with "entitled transactions", which occur when the values exchanged are determined by laws and regulations, and involve potential coercion for their implementation.

Table 1 - Coordination mechanisms involved in voluntary organizations

| | | | |
|------------------------|---|---|---|
| Coordination mechanism | Market | Collective action | State-centered |
| Coordination principle | Price | Mutual interest / Norm of reciprocity | Law / Coercion |
| Allocation mechanism | Market | Pooling | Redistribution |
| Coordination failure | Market failure: Externalities Informational asymmetries Public goods | Collective action failure: Free-riding Negative reciprocity | Government failure: Dissatisfaction of preferences |

2. COORDINATION FAILURES

Each coordination mechanism corresponds to an allocation mechanism - i.e. the mechanism by which resources are directed and distributed in the economy - and displays some form of coordination failure. Three types of failure may be distinguished: market failure; government failure; and collective action failure.

Market failure. In the case of market failure, different phenomena such as moral hazard, adverse selection, or the impossibility of contingent claims contracts may be involved. All these phenomena are characterized by uncertainty over the behavior of one of the parties to the transaction or by uncertainty concerning the quality of the object exchanged. Usually this uncertainty is due to informational asymmetries between the parties. Adverse selection characterizes situations in which there is uncertainty over the quality of the exchanged object. Moral hazard refers to situations in which the object of the exchange is the action of one of the parties and this action is not directly observable by the other party; uncertainty thus characterizes the object of the exchange. When dealing with long-term transactions, "contingent claims contracts" (documents that specify all the obligations of each party to an exchange, contingent upon all future states of nature) cannot be written, given uncertainty and opportunism. The presence of specific knowledge or investments (irreversibility) is also a factor explaining market failure. In addition, when externalities occur, coordinated actors do not reach a socially optimal outcome, because of the presence of interdependencies not taken into account by the coordination mechanism (the prices). In the case of a public good, the nature of the object, characterized by indivisibility and non-excludability, does not permit the transaction. Given the nature of the object, actors have no incentive to coordinate themselves (hence potential problems of free riding) and governmental provision may be an alternative.

Government failure. Purely public goods possess two distinctive features: it is virtually impossible to exclude someone from using them or to ration their use, nor is it desirable to do so. Indeed, the nature of these goods is such that it is difficult or very costly to ration their use (for example, national defense). Neither is it desirable to employ rationing since the use of these goods by an additional consumer does not restrict the use by other users (the marginal cost of production is zero). Public goods raise the free-rider problem: users are not interested in paying for the good or revealing their degree of preference as they will benefit from using the good in any case. As a result, the market fails, since there is no incentive for the service to be offered on a voluntary basis. Many goods are not pure public goods (i.e. they do not possess the two characteristics of non-excludability and undesirability of exclusion), but they are merit goods, i.e. goods possessing one of the two characteristics to varying degrees: either exclusion is possible but costly, or exclusion is feasible but not desirable. Governmental provision of public or merit goods may be non-optimal since actors have no incentive to reveal to the state their true preferences, and it would be too costly - when not impossible - for the state to get this information; given this information problem, the allocation resulting from a state-centered coordination mechanism is likely to lead to a non-optimal outcome, and we will then talk of government failure.

Collective action failure. If voluntary associations are thought of as systems of privately organized collective action, coordinated by generalized or balanced reciprocity, it could be argued that they are subject to the collective action problem as stated by Olson (1965), and therefore to free-riding. In his simplest statement of the logic of collective action, Olson (1965) presents the equation of costs (C), gross benefits (V_i) to the individual (i) and net benefits (B_i) to the individual accruing from i 's own contribution to a group's collective good: $B_i = V_i - C$. In the absence of a selective incentive, individuals will contribute to the collective good if $B_i > 0$. In Olson's formulation, collective action will take place if the net benefit for each individual is positive. But the problem of collective action involves more than this. We can restate it as a

"prisoner's dilemma" (Hardin 1992), for even when individuals achieve a positive net benefit from collective action, no matter what other individuals do, a given individual is better off by not contributing. Not contributing (free-riding) is the best strategy, irrespective of whether others contribute or not.

So far, we have distinguished three types of coordination mechanisms which are mobilized to varying extents by voluntary organizations in order to operate. As we have underlined, each of these coordination mechanisms is subject to different types of coordination failure. The main question to be answered is how voluntary organizations are able to mitigate these coordination failures. As pointed out by Weisbrod (1977), collective action within voluntary organizations is a way to deal with government failure. When government provision of public goods leads to widespread dissatisfaction among consumers, some being over-satisfied, some under-satisfied, the production of public goods by voluntary organizations is likely to satisfy heterogeneous and/or minority demands. But how do voluntary organizations mitigate market failures when it comes to trust goods and how are they able to deal with the collective action problem? The argument advanced in this article is that the specific governance structure that characterizes voluntary organizations allows them, when governance failure does not occur, to mitigate market failures and collective action failures and therefore to constitute an alternative to government provision of collective goods. In order to develop this argument, we will proceed in two steps. First, we will see (in section 3) how taking into account the norm of reciprocity reduces the salience of the collective action problem. Secondly, we will show (in section 4) how the governance structure of voluntary organizations enhances reciprocity and trustworthiness.

3. COLLECTIVE ACTION AND THE NORM OF RECIPROCITY

Not contributing (free-riding) may appear as the best strategy, irrespective of whether others contribute or not to collective action; but when introducing a new parameter, namely compliance to a norm (for example the norm of reciprocity), the conclusion may be different. Indeed, the existence of a norm of reciprocity reduces the occurrence of the free-riding problem that is specific of collective action (Holländer 1990; Koford and Miller 1991; Kollock 1998; Lindbeck et al. 1996; Kübler 2001; Hechter and Opp 2001; Feld 2002).

When I do not conform to an internalized moral principle or norm (Sherif 1966; Scott 1971; Elster 1989, 1990), a process of dissonance generates feelings of shame and guilt. There is dissonance when a distance is created between what I should do (obey a given norm) given my social status (and my conception of myself), and what I actually do, i.e. what I am communicating about myself to others (not obeying this norm). The distance between my subjective perception of how I am perceived by others (social status or social identity) and my own claim about the person I am (self-esteem) creates dissonance. As put by Elster (1999: 304),

An individual who is subject to several motivations that point in different directions will feel an unpleasant feeling of tension. When on balance he favors one action, he will try to reduce the tension by looking for cognitions that support it; when he favors another, he will look for cognitions that stack the balance of argument in favor of that action. Thus the timing of the switch in behavior will be path-dependent. Dissonance theory is more realistic than the cost benefit model in that it views

individuals as making hard choices on the basis of reasons rather than on the basis of introspections about how they feel.

According to Leon Festinger (1957), the existence of dissonance, being psychologically uncomfortable, motivates the person to reduce the dissonance and achieve consonance. Dissonance is defined (Festinger 1957: 3) as

the existence of non-fitting relations among cognition (...) [By] cognition I mean any knowledge, opinion or belief about the environment, about oneself or about one's behavior. Cognitive dissonance can be seen as an antecedent condition which leads to activity oriented toward dissonance reduction just as hunger leads to activity oriented toward hunger reduction.

Dissonance with respect to a norm or a moral principle will occur when an agent's action, given his conception of himself (self-esteem), jars with the given social expectations (norms) that are attached to the agent's self-conception (social identity). In other words, normative dissonance will occur when the agent feels that what he is doing is out of step with what he is expected to do given the social context and the person he wants to be socially. Psychologists agree on the importance of internalization of rules or norms for behavior. Sociologists stress the role of group pressure in the process of norm conformity. When a person has internalized a principle or a norm and when the principle or norm is enacted by the group to which the person belongs, the prospect of an action running counter to the norm will create dissonance between what the person should do and what he or she is planning to do. This dissonance will produce feelings of anxiety, guilt and shame. The individual may reduce this dissonance by choosing the action which is most consonant with the norm.

Compared to the prisoner's dilemma game, where the dominant strategy of both players is to defect – not cooperate –, conformity with a common norm leads to a cooperative solution. The game is basically an assurance game, but unlike what is the case in assurance games (where defection can be a dominant strategy if one player believes the other player is likely to defect), there is only one equilibrium – that of cooperation, since both players are committed to cooperating.

What is the effect on social dilemmas of introducing a cooperation norm when information is incomplete (i.e. when none of the players knows what the others stand to gain) and when the possibility that the players may not be self-interested (i.e. are conforming to a norm) is considered? The game presented in the appendix shows that those self-interested individuals who take into account the fact that some individuals are normatively committed to contributing, instead of choosing to free-ride, may nevertheless end up contributing despite their initial commitment not to contribute. The prisoner's dilemma structure of the public good game is due to the fact that it is common knowledge that both players are self-interested. Considering the possibility that the players may be committed (i.e. have a norm-based behavior) and that the players ignore the type of the other player changes the structure of the game. The most important feature of this analysis is that strategic interactions in a "normative" social setting, i.e. where individuals take into account the fact that other individuals may be committed to a norm, do not necessarily lead to the same outcomes as interactions where individuals expect others to act according to their own self-interest. The collective action problem is solved and cooperation is

sustained by the norm of reciprocity as long as the anticipated benefit of contributing is high enough, even if some individuals do not conform to the norm.

4. GOVERNANCE STRUCTURE

If the norm reciprocity can solve or at least reduce the collective action problem, any solution to a coordination failure (Enjolras 2000; Bowles 2004) will presume an allocative outcome (the benefit each contributor receives). Reciprocity-based collective action is incompatible with for-profit governance structure, since individuals neither have an incentive to contribute to an organization (collective action) when such action effectively lines the pockets of the organization's owners (profits), nor will they comply with a norm of reciprocity when the allocative outcome of their contribution contradicts this norm in terms of distributive justice.

By contrast, voluntary organizations have a governance structure (formal goals, ownership, distribution of property rights, and decision-making procedures) that fosters and sustains collective action based on (generalized or balanced) reciprocity. Indeed, voluntary organizations operate as a "pooling mechanism" (Horch 1994). The principle or generalized norm involved in pooling resources is reciprocity and the governance structure of these organizations has to be compatible with this norm.

The governance structure of these organizations may reinforce the norm of reciprocity, alleviating by the same token the collective action problem. However, the ability of the organization to foster behaviors based on reciprocity is dependent on its trustworthiness. In the case of transactions involving trust (Coleman 1990), the decision of the trustor in a relation of trust is subsumable to the paradigm of decision under risk. The potential trustor must decide between not placing trust and placing trust. His decision will depend on his estimation of the probability that the trustee complies with the norm of reciprocity. If the uncertainty concerning the potential behavior of the trustee exceeds a certain threshold, the trustor will not place trust and the transaction will fail. As illustrated by Hansmann's model of the donor, asymmetric information may lead to the failure of a transaction based on reciprocity. Considering a person who wishes to increase the quantity or quality of an organization's product but cannot directly observe the impact of her gift (in time or money) the uncertainty about the way her donation will be used may lead her not to donate. From this viewpoint the problem of collective action based on reciprocity is common with that of market failure. Similarly, the ability of the voluntary organization to mobilize public funding through public grants and contracts with public authorities is heavily dependent on the organization being trustworthy when it comes to the use of public funds. Consequently, the main issue is to determine how the governance structure of voluntary organizations is able to enhance trustworthiness.

The perspective developed here is designed for use with all types of voluntary organization, though Europe, especially Scandinavia, has a preponderance of membership organizations, unlike the board-managed organizations that obtain more often in the U.S. and U.K. Membership organizations are governed democratically, ultimately by the annual general meetings (AGM) of members who elect a board to oversee the organization's management and to hire personnel, including a salaried manager resources permitting. The trustees of board-managed organizations, on the other hand, are usually appointed by external organizations or authorities or are indeed

self-recruited and self-perpetuating. As we will see, these two main types of voluntary organization display differences in terms of governance structure, especially accountability mechanisms.

Each institutional form – for-profit, governmental, voluntary – can be characterized by a specific governance structure. We can identify six dimensions of a governance structure (see table 2): the organizational purpose; the ownership; the distribution of property rights and particularly residual claims; the way decision-making power is vested; the control and accountability mechanisms implemented; and the incentives embedded in the governance structure.

Table 2 - Governance structures and organizational forms (ideal-types)

| | For-profit | Governmental | Voluntary |
|---|---|--|---|
| Organizational ends | Profit Economic action | Public interest/good Economically oriented action | Public benefit Mutual benefit Political action Economically oriented action |
| Ownership | Private | Public | Collective ownership/ Trust |
| Residual claims: -Residual control (<i>ius abutendi</i>) | Owners/Shareholders | State | Members/board/trustees (with limited alienation rights) |
| -Residual income (<i>ius fruendi</i>) | Owners/Shareholders | State | No residual claims on income (non-distribution constraint) |
| Decision making | Board/ general assembly of shareholders in proportion of the share of the capital | Members of the board appointed by public authorities | Members of the board co- opted or elected by the general assembly of members Trustees |
| Control and accountability mechanisms | Capitalistic | Democratic | Democratic and/or checks and balances |
| Embedded incentives | Extrinsic | Extrinsic and intrinsic | Extrinsic and intrinsic Reputational |

The first dimension is concerned with the organization's encompassing *formal ends* and *goals*. The main objective of for-profits is to make profit. Governmental organizations pursue the public interest or provide public goods, whereas voluntary organizations may pursue the realization of public or mutual benefit as well as political aims. In addition, voluntary organizations do not have economic goals as primary ends. Max Weber (1978: 64) distinguishes between the "economic action" and the "economically oriented action", which is "primarily oriented to other ends [but] takes account, in the pursuit of them, of economic considerations." Economic activities are those aiming at producing and consuming goods and services whereas economically oriented activities aim at other finalities but imply the production and consumption of goods and services in order to realize those finalities. A significant share of the activities carried on by the voluntary sector belongs to this category. Most of the work done within the

fields of education, health, social services, art and culture, philanthropy, sport and religion do not have the production and consumption of goods and services as their primary finality. The for-profit institutional form and its governance structure are efficient in the area of economic activity. The voluntary institutional form and its governance structure are useful for organizing economically oriented activities involving axiological objectives and for allocating resources on the basis of reciprocity. Axiological and instrumental objectives differ in as much as the former are not aimed at realizing a benefit or interest but the effectuation of non-monetary values. The market only values what can be quantified and expressed in monetary terms. However, social life cannot be reduced to monetary values. Human beings entertain and seek to uphold other values such as culture, solidarity, humanity, prestige, beauty, democracy, public interest, etc. that cannot be quantified and expressed in monetary terms. Many human activities are aimed at actualizing these values. Their implementation often necessitates the production and consumption of goods and services, conferring upon them an economic dimension. But they cannot be reduced to monetary value.

Organizational forms are also distinguished according to their *ownership*. In the case of for-profits, ownership is private. Governmental organizations are publicly owned, whereas the ownership of voluntary organizations may be collective or take the form of a trust (Salamon 1997). The property rights literature classifies institutional forms according to the type of contractual arrangement that governs the rights over the residual claims, i.e. residual incomes - the remaining incomes once all fixed contractual remunerations have been paid - and residual control - the power of management, including that of alienation (Eggertsson 1990). In for-profit firms (if one ignores the problems due to principal-agent relationships between shareholders and managers that are often overcome by giving stock options to managers), owners bear the wealth consequences of their actions. In governmental and voluntary organizations there are no owners who directly bear the wealth consequences of their decisions. This characteristic constitutes the basis for demonstrating that for-profit firms are more efficient than public and voluntary organizations since for-profit firms display incentives for cost minimization that the other institutional forms do not. It is worth emphasizing that this line of argument is based on the idea that actors are selfish and uniquely motivated by their material (extrinsic) interest and does not take into account other governance mechanisms implemented in order to enhance efficiency.

Institutions are usually classified in terms of the contractual arrangements that govern the *distribution of property rights* and especially of the ownership of their *residual income* (the sum that remains when those with fixed pay-off contracts have been paid). This classification seeks to highlight the extent to which chief decision-makers bear the wealth consequences of their action. It is indeed usual to distinguish three types of property rights (Eggertsson 1990; Furubotn and Richter 1998: 77):

- The right to make physical use of physical objects (*ius utendi*).
- The right to the income from the use of physical objects (*ius fruendi*).
- The power of management, including that of alienation (*ius abutendi*).

A voluntary organization is characterized by the following distribution of these rights:

- The right to make use of physical objects is open to members/trustees.
- There is no right to the income.
- The power of management is delegated by the general assembly to the executive (committee) or is vested in the trustees, whereas the power of alienation is limited.

Voluntary organizations have therefore a specific distribution of property rights (no residual claimant, limited alienation rights). In turn, this specific distribution defines in part the contours of their governance system, incorporating, in membership organizations, a membership-based control structure usually characterized by a general assembly of members which controls and elects a board which may or may not hire a paid executive manager. In membership organizations the Annual General Meeting (AGM), in which ultimate authority is vested, controls the activity of the board. In board-managed organizations, the control and accountability procedures are weaker, being based on the integrity of the trustees and on their accountability to the stakeholders (donors, beneficiaries, etc.) and the general public.

Governance structures characterizing the different institutional forms are also differentiated according to the principles by which *decision-making* power is devolved, i.e. the rules of choice and nomination of the executive committee and the way their power is weighted. In for-profit firms power is proportional to the share of capital owned; in governmental organizations members of the executive committee achieve power through delegation by the political authorities; whereas in voluntary organizations members of the executive committee are elected by the members of the association or co-opted. Following Salamon (1997), one may distinguish "membership organizations" from "board-managed organizations". In the case of membership organisations, ultimate authority rests with the membership, whereas in board-managed organisations authority is self-perpetuating. In governmental and voluntary organizations the members of the executive committee do not bear the wealth consequences of their actions. However they are "politically" responsible for their actions and are accountable to the authorities delegating their authority and to the general public.

Governance structures are also defined by the modalities by which managers are *accountable*. In for-profit firms managers are accountable to the owners and shareholders. In public organizations managers are delegated their power by the political authorities and are directly or indirectly politically accountable to the citizens. In membership organizations the managers are accountable to the general assembly through democratic procedures whereas in board-managed organizations the co-opted trustees are subject to a set of rules. The separation of power between the management of the organization and the board entails a system of checks and balances that strengthens accountability and entails the implementation of internal control procedures.

The last element characterizing the structures of governance is the type of *incentives* they embody and which motivate the managers. For-profit firms offer their managers monetary, instrumental, and extrinsic incentives taking the form of stock options, bonuses based on profit, etc. Managers in public and voluntary organizations are motivated by both monetary/instrumental and extrinsic incentives as well as by axiological and intrinsic incentives. Values such as public interest, public service, public spirit play an important but often underestimated role as motivating factors for public and voluntary managers. In addition, the members of the board have some incentives to maintain their reputation as good citizens and disinterested administrators.

5. GOVERNANCE STRUCTURE AND TRUSTWORTHINESS

Each of the dimensions of the governance structure has to be assessed in terms of its contribution to organizational trustworthiness. To this purpose, the challenges formulated by Ortmann and Schlesinger (2003) – especially incentive compatibility and adulteration – constitute a useful grid of analysis.

Incentive compatibility. According to the incentive compatibility criteria, it has to be demonstrated why opportunities and incentives for various forms of opportunistic behavior and for misappropriation are negligible in voluntary organizations. Relative to market failures, Hansmann (1980) has emphasized asymmetric information, voluntary organizations being more "trustworthy" than for-profits. Indeed, in Hansmann's model, the producer has more information concerning the product quality than the consumer. The producers have incentives to cheat on the quality as long as they have more information relative to the quality of the product than the consumer. But the non-distribution constraint (the absence of residual claimants) contributes to reducing the organization's incentives to downgrade quality in order to increase its profit and gives assurance to the consumer relatively to the quality level. The voluntary organization, being more trustworthy than the for-profit one, has a comparative advantage in the production of "trust goods" and therefore is more likely to be the dominant form of provision of such goods. But the non-distribution constraint does not guarantee that voluntary organizations are not profit-maximizers. The voluntary organization can maximize profit as well as the for-profit one in order to satisfy other goals than to remunerate shareholders. Why should these organizations be considered more trustworthy?

Another line of argumentation underscores the fact that voluntary organizations are characterized by the absence of residual claimant and by the exercise of a direct or indirect control by the members/trustees. As shown by Fama and Jensen (1983), the absence of a residual claimant may lead to inefficiencies while the division between ownership and control leads to a principal-agent problem. As property rights are attenuated for nonprofits, the members cannot appropriate the residual. Further, they cannot capitalize the firm's wealth by selling the rights to future income flows (Frech III 1976; Frech III and Ginsburg 1981). Attenuated property rights may lead to different behavior than private property rights: for instance, they reduce the price of managerial emoluments (pleasant office colleagues, short working hours, greater output) to the members and to the managers. According to this argument, if these non-pecuniary benefits include elements other than quantity and quality of output, the voluntary organization will exhibit higher production costs for the same output than the profit-seeking firm.

Adulteration. An organization may be said to display a governance structure (values, formal goals, with normative rules that define how the organization should be run) and a social structure (behavior of and interaction among participants). The governance and social structures are interdependent but not identical, as the governance structure imposes a set of constraints on the social structure. The main problem when considering the functioning of the voluntary organization's governance structure is to determine whether such a structure is enough to ensure that the organization will not deviate from its formal aim, what Panebianco (1982) calls "the dilemma of rational model versus natural system model". According to the rational model, organizations are instruments for the realization of specific goals whereas the natural model sees the organizations as "a structure which responds to, and adjusts itself to, a multitude of demands from various stakeholders, and which tries to maintain balance by reconciling these demands". According to the natural model, the official aim of a voluntary organization is a facade behind

which the real aim, the survival of the organization and perpetuation of the leaders, is concealed. However, official aims cannot be reduced to a mere facade in as far as they are part of an ideology necessary to maintain the identity of the organizations in the eyes of their supporters (members, funders, donators). But at the same time, organizations may develop tendencies towards self-preservation and diversification of aims under the pressure of their environment.

Summing up these lines of argumentation, inefficiencies, downgraded quality, misuse of resources and goal displacement may characterize voluntary organizations' economic activity; the non-distribution constraint not only does not guarantee trustworthiness, it is also the source of the voluntary organization's efficiency and governance problems. However, as we will see, the governance structure of voluntary organizations embeds compliance mechanisms and incentives that partly counteract these perverse effects. Three main compliance mechanisms – democracy, checks and balance, and control – and two types of incentives – intrinsic and reputational – may be distinguished.

Democracy. In membership-based organizations the board is elected by the general assembly of the members and acts on behalf of and is accountable to the members. In such a democratic representative system the main reason the members of the board may represent the interests of the members is that the members use their vote effectively to threaten those tempted to stray from the path of virtue with being thrown out of office. As far as the organization is controlled by members that represent directly or indirectly the interests of the clients, the fact that it is run by members and not by owners may constitute a more credible source of trust than the non-distribution constraint. This compliance mechanism relies, however, on active member participation, and the lack of participation may precipitate oligarchic governance, characterized by the lack of leadership turnover, minority control over organizational resources, professionalized leadership, and low level of participation in governance.

Checks and balances. The governance structure of voluntary organizations incorporates the principle of separation of power. In membership-based organizations the AGM elects the members of the board who are responsible for the strategic orientation of the organization and who control the manager of the organization. In such organizations, the board is accountable to the members and may have an incentive to be reelected. The same principle is valid in board-managed organizations, the difference being that the board is not accountable to the members but to the general public. The reason why the separation of power and the system of checks and balances which is embodied in the governance structure of voluntary organizations strengthens accountability so decisively is because the board is not a residual claimant, and does not benefit, as the manager may do, from managerial emoluments. However, when collusion between board and manager occurs, the system of checks and balances fails to guarantee accountability and efficient use of resources. It is worth noting that the principle of separation of powers entails the implementation of control procedures.

Control. The governance structure of voluntary organizations also embodies the principle of active control of the organization's operations by the board. If this control by the board/trustees is effective, i.e. if the voluntary organization has a democratic functioning and/or an effective and accountable board, inefficiency-related problems may be reduced (even if the principal-agent problem between the board and the manager is not completely eliminated, due to

informational asymmetries). However, control and active leadership by the board and the trustees are costly in terms of time and resources and governance failure may occur.

If governance failure – oligarchy in membership-based organizations, collusion between board and manager, and lack of effective control – is likely to occur, there are two sets of incentives that limit the occurrence of such governance failure and that operate in order to ensure the compliance of the stakeholders with the goals and missions of the voluntary organization.

Intrinsic incentives. Individuals have intrinsic and extrinsic motivations (Frey 1997). Extrinsic motivations are imposed on individuals from the outside. They take the form of either money or threats of punishment. Intrinsic motivations are reasons for action that come from within the person, such as pleasure and personal satisfaction. Extrinsic motivations may crowd out intrinsic motivations because they impair self-determination and self-esteem. Extrinsic motivations often overlap with instrumental ones, whereas intrinsic motivations are often axiological (value-oriented). Involvement in voluntary organizations as a member, volunteer, board member or paid worker is more likely to be motivated by intrinsic and axiological incentives than by extrinsic and instrumental incentives. Some dimensions of the governance structure, such as organizational goals and distribution of property rights and residual claims, function as a signal for individuals motivated by intrinsic and axiological incentives. In other words, the choice to be involved in voluntary organizations is likely not to be primarily motivated by extrinsic and instrumental rewards. Voluntary organizations, because they offer intrinsic and axiological incentives, may be less exposed to opportunistic behaviors and misuse of resources than their for-profit counterpart.

Reputation. Another incentive that may prevent governance failures is the stakeholders' desire to maintain their good reputation and that of the organization. In board-managed organizations, trustees are often chosen on the basis of their experience, notability and integrity. Their social and reputational capital represents an asset and they are not willing to waste it. They have therefore an incentive for doing a good job as part of the leadership of the organization. In membership-based organizations, in addition to the same type of reputational incentives, the trustees are accountable to the general assembly of members and submitted to re-elections. They have consequently the additional incentive of staying in office as a motivation to avoid opportunistic behavior and misuse of resources.

Summing up, it appears that the lack of instrumental and extrinsic incentives that characterizes the governance structure of voluntary organizations and that is often invoked as a source of inefficiency and misconduct of these organizations is compensated by different compliance mechanisms (democracy, checks and balances, control) and incentives (extrinsic incentives, reputational incentives) that are embedded in the governance structure and that, taken together, when effectively implemented, ensure an effective governance of these organizations and their trustworthiness. As all governance systems, though, the governance structure of voluntary organizations is not exempt from the risks of governance failure and residual governance problems (Ben-Ner and Van Hoomissen 1994). Compliance mechanisms and incentives have to be implemented into adequate social practices in order to produce their effects. Insufficient democratic participation, oligarchic tendencies, lack of adequate control, collusion, failure to comply with ethical and judicial standards, crowding out of intrinsic incentives by extrinsic ones,

stakeholders' opportunistic behaviors, may all affect the functioning of the governance structure and eventually undermine the organization's trustworthiness and efficiency.

6. A CASE STUDY

We can illustrate the differences between the governance structure of different organizational forms by comparing typified facets of the governance structures of public, nonprofit, and for-profit organizations (see table 3). The sample organizations each run a rehabilitation center for disabled children. The for-profit rehabilitation center is owned by private individuals who expect a return on their investment in the enterprise. This governance structure tends to preclude voluntary fundraising since no one is willing to give time or money that would increase the organization's profit. The managers of the organization, who are accountable to the board and shareholders, may not stray from the budget approved by the board (in terms of return on investment). The organization implements quality management procedures to ensure minimum standards for customer satisfaction, but quality is not its primary concern and is audited only to the extent that it contributes to profitability. Only individuals who can pay the organization's fees are admitted.

The public-owned rehabilitation center is owned and run by a local municipality. It is incorporated as a publicly-owned company whose board is appointed by the local council. It provides services for a specific segment of the population as defined by the councilors. It is funded by local government and applicants are screened (income, level of disability, etc.) to make sure they belong to the right target group. This organizational form precludes voluntary fundraising or donations by the general public as well. Administrative standards define how the services are run and managers are accountable to the board, which in turn is accountable to the councilors who appointed them. Minimum standards of care are adhered to, without necessarily meeting the diverse needs of all beneficiaries.

The voluntary-based rehabilitation center was set up by parents of disabled children who were unhappy with the alternatives. The organization has to maintain high standards of personalized care for its members. Parents have to be members of the association running the center before their children are admitted. They are also expected to volunteer to help raise funds among the wider membership and general public. Further revenue comes from parental fees and a grant from the local authority. The managers are accountable to the board, which is in turn accountable to the annual general meeting. As it is the case within most voluntary organizations, some members are more active than others. Care is personalized around the needs of the children, quality of care is a priority, and opinions of parents are taken into account in care planning.

Table 3 - Typified features of three organizational forms running a rehabilitation center

| | For-profit | Governmental | Voluntary |
|---------------------|---|---|------------------------------------|
| Organizational ends | To generate profits to the owners by delivering demanded services on the market | To deliver public services to target groups | To deliver services to the members |
| Ownership | Private ownership | Public ownership | Collective ownership |

| | | | |
|---|--|---|--|
| Residual claims: -Residual control (<i>ius abutendi</i>) | Owners | Public authority | Members |
| -Residual income (<i>ius fruendi</i>) | Owners | Public authority | No residual claims |
| Decision making | Board / shareholders | Public authority | Board / Annual General Assembly |
| Control and accountability mechanisms | Accountability of managers to the owners | Administrative internal control Indirect accountability of managers to elected politicians | Accountability of managers to the board and the AGM Check and balance Accountability of the board to the AGM |
| Embedded incentives | Extrinsic | Intrinsic and extrinsic | Intrinsic and extrinsic |

This illustrative example emphasizes the governance structure of a membership-based voluntary organization compared with that of a governmental and a for-profit organization. A board-managed organization, for example a charity created by a church, would not have democratic accountability mechanisms, but would display accountability mechanisms based on board members' reputation and on check and balances between board and managers. This example illustrates also that the governance structure determines the ability of the organization to mobilize reciprocal resources taking the form of volunteering or donations. Finally, this example underscores that the trustworthiness of the organization, a necessary condition for mobilizing voluntary resources and donations and for mitigating market and government failures, is dependent upon governance and accountability practices that are in accordance with the formal governance structure and principle that define a voluntary organization. An issue in board-managed organizations, especially in large hierarchical and impersonal nonprofits that purchase labor and sell products in the market, is the extent to which check and balance and reputation mechanisms work. Reputation mechanisms are relevant to large impersonal organizations since they do not require necessarily that board members know each other well and that peer pressure enhances accountability among them. Indeed, most trustees and boards' members are usually notabilities (within a professional field or a community) and are also preoccupied by their reputation, independently of peer pressure. However, reputation mechanisms are weaker than democratic accountability procedures (when they work accordingly to their principles) and on this ground one can expect that the likelihood of governance failure will be higher in large hierarchical and impersonal organizations than in smaller or membership organizations. When governance fails, adulteration of goals, misappropriation of resources and inefficiencies occur, jeopardizing the organization's trustworthiness and in the long run its comparative advantage. This may be a reason why we witness many attempts to develop codes of good governance for voluntary organizations, including ethical behavior guidelines for board members, as it is the case with the code of governance developed by the UK-based NCVO (2005). Codes of good governance may provide voluntary organizations with additional tools for guaranteeing organizational trustworthiness, in spite of their lack of compliance and enforcement mechanisms (Dawson and Dunn 2006).

7. SUMMARY AND CONCLUSIONS

This article has sketched a theoretical understanding of voluntary organizations by considering these organizations from the viewpoint of their particular governance structure. Voluntary organizations are seen as governance structures reinforcing the norm of (generalized or balanced) reciprocity, making possible the pooling of resources based on the reciprocity principle, and, because of these features, facilitating collective action oriented towards public or mutual interest or towards advocacy. Because the nonprofit governance structure is also compatible with other types of coordination mechanisms, voluntary organizations are able to operate in complex environments, mobilizing resources from market operations, governmental subsidies, or from reciprocity (volunteering, donations). They are equally able to pursue civic and democratic objectives such as advocacy and interest representation. This ability confers on them a comparative advantage when providing certain goods (trust goods, collective goods, club goods, cultural goods, etc.) in competition with for-profit and governmental organizations. From a governance-structure perspective, their ability to mitigate coordination failures explains why these organizations survive in competition with other institutional forms as a result of selection and reinforcement processes (Elster 2007: 271). However, voluntary organizations are exposed to governance failures that might jeopardize their trustworthiness and efficiency.

By focusing on the non-distribution constraint – an important, but partial, aspect of voluntary organizations – the main theoretical approaches toward the nonprofit and voluntary organization have neglected important features of this type of organization. The conceptualization offered here – stressing the governance structure as well as the role of reciprocal coordination – provides a corrective to these theories while synthesizing them in a unified framework by introducing a plurality of action rationales (instrumental, normative, axiological), of coordination mechanisms and of coordination failures.

Stressing the crucial roles played by the governance structure and the governance practices that are associated with this structure has not only theoretical implications, but also practical ones. The main practical implication of this theoretical approach consists in underscoring the interdependencies existing between the organization's capacity to generate resources and its governance. Well-functioning governance enhances at the same time the trustworthiness of the organization, its ability to mitigate coordination failures, and its capacity to attract market, reciprocal and public resources. In spite of the tensions that characterize nonprofit governance (Cornforth 2003), the practices of governance embodied into voluntary organizations' governance structure is the best guarantee for organizational efficiency and trustworthiness. Repeated "scandals" within the voluntary sector remind us that the voluntary organization's governance may fail and public trust in voluntary organizations may vanish. Increased awareness, especially among board members, of the centrality of voluntary organization's governance as the main determinant of their trustworthiness and efficiency may be gained from a better theoretical understanding of the specificities of voluntary governance and of the functional links between coordination failures and internal governance.

APPENDIX

Incomplete information in a public good game with normative commitment

Consider the following public good game:

| <i>Individuals:</i> | <i>j</i> | |
|---------------------|---|---|
| <i>i</i> | Contributes | Does not contribute |
| Contributes | $1 - t_i + a_i(\theta_i),$ $1 - t_j + a_j(\theta_j)$ | $1 - t_i + a_i(\theta_i),$ $1 - t_j - a_j(\theta_j)$ |
| Does not contribute | $1 - t_i - a_i(\theta_i),$ $1 - t_j + a_j(\theta_j)$ | 0,0 |

Where $a_i(\theta_i) = 1$, (i 's benefit = 1) if θ_i , i.e. i 's type is to conform to the cooperation norm, and $a_i(\theta_i) = 0$ (i 's benefit = 0) if θ_i , i.e. i 's type is to not conform to the cooperation norm. t_i and t_j , the costs of contributing, are supposed to be the same for individuals i and j : $t_i = t_j$ and are common knowledge.

If p_i is the equilibrium probability that player i contributes: $p_i = \Pr(s_i^*(a_i(\theta_i))) = 1$.

Player j 's optimal behavior is:

$$s_j^* = 1 \text{ if } 1 - t_j + a_j(\theta_j) > 1 - a_j(\theta_j)(1 - p_i)$$

$$s_j^* = 0 \text{ if } 1 - t_j + a_j(\theta_j) < 1 - a_j(\theta_j)(1 - p_i)$$

Player j will contribute if his pay-off is more than his benefit from the public good, times the probability that player i does not contribute.

Conversely, for player i

$$s_i^* = 1 \text{ if } 1 - t_i + a_i(\theta_i) > 1 - a_i(\theta_i)(1 - p_j)$$

$$s_i^* = 0 \text{ if } 1 - t_i + a_i(\theta_i) < 1 - a_i(\theta_i)(1 - p_j)$$

If $a_i(\theta_i) = 0$:

$$s_i^* = 1 \text{ if } 1 - t_i > 1 \cdot (1 - p_j)$$

$$s_i^* = 0 \text{ if } 1 - t_i < 1 \cdot (1 - p_j)$$

If $a_i(\theta_i) = 1$:

$$s_i^* = 1 \text{ if } 2 - t_i > 0$$

$$s_i^* = 0 \text{ if } 2 - t_i < 0$$

In other words, a player whose type is of conforming to the norm will contribute whatever the probability that the other player does not contribute, as long as there is a positive pay-off for contributing (i.e. the cost does not exceed the benefit). But the interesting feature of this game is that a player whose type is of not conforming to the norm *will* contribute if his subjective probability that the other player will not contribute (i.e. the other player's type is of not conforming to the norm) is high enough, and his cost is low enough.

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