Managerial discretion, incentives and governance rules for non-profit organizations

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Abstract

This paper analyzes the effects of managerial discretion and some possible solutions in non-profit sector. It is shown how the traditional incentives' mechanisms are modified in a non-profit setting. In particular, market, reputational and ideological incentives are considered. The analysis highlights that new governance rules are necessary. In this context a new financial model is analyzed where the competition between for-profit and non-profit firms is extended from the products level to that of private financing.

Keywords: non-profit; managerial discretion; incentives, governance rules
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1. Introduction

In the modern welfare states, non-profit organizations have an increasing role. So, the economic, sociological and legal literature is interested to this topic in a very extensive way. From the economic point of view, two perspectives of analysis can be identified: normative and positive analysis. In the first perspective, the economic and social role of non-profit organizations is highlighted [WEISBROD 1975; HANSMANN 1980]. Non-profit sector is considered an effective and efficient alternative to State failure or to contract failure. The basic idea is that the non-distribution constraint assures an organizational behavior consistent with institutional objectives of the organization.

The second perspective of analysis points out that this constraint is consistent with a variety of behaviors on the part of non-profit organizations. In particular, the behavioral models of non-profit organizations [JAMES, 1983; SCHIFF-WEISBROD, 1991; BISES 2000] considers self-interested managers whose preferences and objectives are different from institutional objectives of organization. The negative effects of managerial opportunism and managerial discretion on efficiency and effectiveness of organizational activity are pointed out.

The negative effects of managerial discretion can not be considered exclusive to the non-profit sector [WILLIAMSON, 1964; FAMA AND JENSEN, 1983] Nevertheless, the possible solutions supplied by economic analyses for profit-oriented firms, such as contracts and incentives theories, are not applicable to non-profit organizations.

At the same time, the positive theories affect the robustness of normative theories. If non-profit activity fails either in efficiency or in effectiveness, its social role as solution to State failure or contract failure becomes feeble.

An important matter, not only from a theoretical point of view but also for policy intervention is, therefore, to investigate why positive theories does not confirm normative theories and what solutions are implementable in order to coordinate efficiency of non-profit organizations with their social role.

The aim of this paper is to give an answer to the following questions: what are the effects of managerial discretion on organizational efficiency of non-profit organizations? How different kinds of incentives work in non-profit organizations and what is their effectiveness? What are the possible governanance rules of non-profit organizations?

The paper is developed as follow. The economic literature on behavioral analysis of non-profit organizations is reviewed in a comparative analysis in section 2. Section 3 focuses on different types of organizational incentives: market incentives, reputational incentives and ideological incentives. In particular, their role and their effectiveness in non-profit context are highlighted. Possible governance rules of non-profit organizations are analyzed in section 4. In particular, a new financial model and a new control structure are analyzed. Finally, section 5 concludes the paper.

2. Managerial behavior and efficiency in non-profit organizations

As the for-profit firms, the non-profit organizations are characterized by asymmetric information and imperfect monitoring. In general, the main agency relations involves the individuals who fund the organization by different means (i.e. the *patrons*) and those who effectively run the organization (i.e. the *managers*). In the case of *donative* organizations, the *patrons* are donors. Differently, in *commercial* organizations, the agency problem is like the consumer-supplier relations in market transactions with imperfect monitoring.

The basic idea is that, as the monetary remuneration of a non profit manager is usually fixed because of non-distribution constraint, the manager will seek to raise his remuneration (or his utility level) through power, status, prestige, that is through non-monetary variables. To this purpose the informative advantage is strategically used.

Nevertheless, the effects on organizational efficiency can be different according to the stereotypical model of manager adopted.

Different kinds of managers are proposed from the economic literature. They can be summarized in the following types: the *power-seeker* manager, the *income-seeker* manager and the *products mix- oriented* manager.

The *power-seeker* manager is analysed by NISKANEN [1971] with reference to a commercial organization. Like public bureaucrats maximizing budget, this kind of manager maximizes sales subject to a balanced budget constraint because managerial power is correlated to the dimension of the business.

From a more general point of view, JAMES [1983] and SCHIFF and WEISBROD [1991] consider a multi-product non-profit organization where the production of different goods or services is subordinated to a cross-subsidization policy between the different activities carried out. In the first case [JAMES, 1983], the non-profit organization produces two unspecified goods. In the second case [SCHIFF and WEISBROD, 1991], the non-profit activity is oriented to a commercial activity and to an institutional activity with characteristic of public good (for example scientific research, health services).

Both cases show that managerial discretion has repercussions on the choice of levels and mix of activities carried out, because the «only way in which the manager can increase his benefits is by altering the mix of services to emphasize those that best reflect his preferences. This will lead him to produce more than a profit making company would of certain services, and less of others»[JAMES, 1983, p. 351][1].

The particular mix choosen depends on the manger's preferences. So, if he/she receives negative utility from the commercial activity and positive utility from the institutional activity, the manger's behavior will be oriented to expand the institutional activity and to reduce the commercial one [SCHIFF-WEISBROD, 1991].

Equally, the product mix will be oriented to the preferred good in the case of two unspecified products [JAMES, 1983].

Extending previous analyses, Bises [2000] refers to an *income-seeker* manager whose objective function is positively correlated to the institutional activity of the organization and to a variable representing the 'budget surplus', that is the excess of income over expenses, available for 'discretionary expenses' [2]. So, this manager's behavior is similar to the public bureaucrat's behavior of Migué and Bélanger [1974] and to the mangerial behavior analysed by Williamson [1964].

Different implications on the organizational equilibria and efficiency derive from the particular manager considered. This following section analyses this point.

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[1]For an extensive classification of models of entrepreneurs see YOUNG [1981].

[2] These expenses are aimed at raising the status, prestige, and power of the manager, as, for example

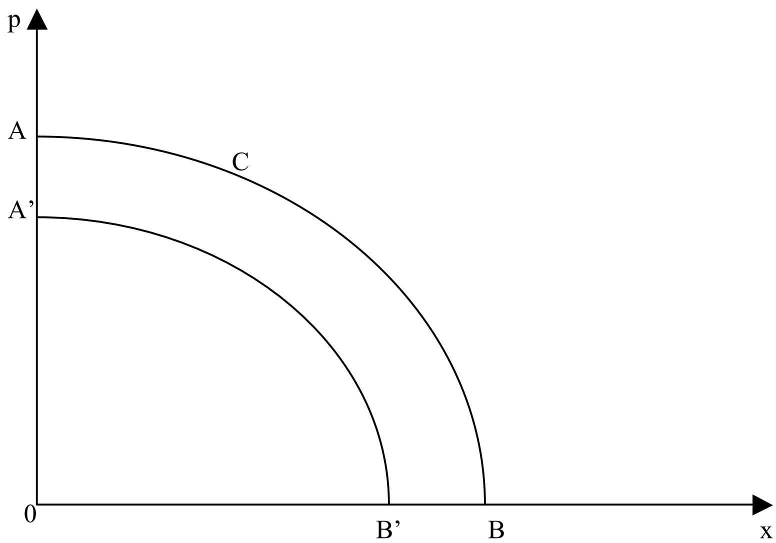
2.1 Equilibria and efficiency of the non-profit organization

We consider a non-profit activity with two characteristics: a “private” characteristic (x), i.e. commercial activity, and a “public” characteristic (p).

The last can be, for example, the “quality” of the good/service produced for a pure commercial non-profit organization or an “institutional” activity for a multiproduct non-profit organization.

With given resources, the possible efficient combinations of the two characteristics are represented by the frontier in the following figure 1:

Figure 1: the production frontier



Following Bises [2000], the institutional organizational objective function is $W=W(x,p)$ with $W_x \leq 0$ and $W_p > 0$.

Since x is a “*bad or neutral characteristic*”[3], organization’s equilibrium would be A. This is a pure theoretical result, because the public and the private characteristics are

expenses for personnel expansion or to improvements in the work-environment.

[3]In the first case, the indifference curves are increasing with positive slope, in the second case are horizontal lines.

connected each other. In order to assure some level of the public characteristic (the quality of the good/service produced or the institutional activity), some level of private characteristic (commercial activity) is necessary[4]. This minimum level of commercial activity can be considered as a constraint for the organization. In a more realistic way, the organization's equilibrium will be a point on the upper side of the frontier (for example C).

The managerial objective function is U=U(x,p,M) where M represents the "managerial discretionary expenditures". To simplify, we assume that this utility function is a Cobb Douglas function, i.e. $U=ax^{\alpha}p^{\beta}M^{\gamma}$ with a >0 and $\alpha+\beta+\gamma<1$[5].

Case 1: the power-seeker manager

As Niskanen [1971] points out, the power-seeker manager maximizes the sales. Then, for this manager $\gamma=0$ and $\beta=0$. His utlity function becomes $U=ax^{\alpha}$ (with a>0) and his behavior is like a for-profit manager maximizing sales. The managerial equilibrium will be B[6] where technical efficiency is assured (because B is on the frontier) but not organizational objective.

Case 2: the product-mix oriented manager

The *product-mix oriented* manager has a less extreme behavior respect to the *power-seeker* manager. His utility is not correlated to managerial expenditures ($\gamma=0$) but both activities (characteristics): commercial (private characteristic) and institutional (public characteristic). Two cases are possible: the manager likes both activities (case 2.1) or the manager dislikes commercial activity[7] (case 2.2) .

[4]In the case of institutional activity, some level of commercial activity is necessary for *cross-subsidization* policies because we are not considering pure donative organizations.
[5]Assuming the sum of exponents lesser than one, the Cobb-Douglas function is stricly concave.
[6]In this case, indifference curves are vertical lines.
[7]If the manager likes only commercial activity, we have the case 1: the *power-seeker manager*.

Case 2.1

γ=0, U_x>0, U_p>0. Given the manager's utility function $U=ax^{\alpha}p^{\beta}$ (with α, β>0 and $\alpha+\beta<1$), the indifference curves are *well-behaved* and the equilibrium is interior (for example D). It is on the frontier, then it is efficient from a technical point of view but it is characterized by an inefficient *product-mix*. In particular, there is an over production of commercial activity respect to the optimal level for the organization.

Case 2.2

γ=0, U_x<0, U_p>0 with $U_x \neq V_x$ and/or $U_p \neq V_p$ [8]. In this case, the manager's utility function is $U=ax^{\alpha}p^{\beta}$ (with $\alpha<0$, $\beta>0$ and $\alpha+\beta<1$). As in the organization's objective function, the commercial activity is distasteful. Then, the pure theoretical equilibrium is A. But since commercial and institutional activities are connected each other, the equilibrium carried out is such that some level of private characteristic (commercial activity) is performed[9]. Nevertheless, it is characterized by a different *product-mix* with respect to the *mix* maximizing the organization's objective even if technical efficiency is satisfied. The managerial equilibrium point is on the frontier, but it is not C.

Case 3: the income-seeker manager

The utlility of the *income-seeker manager* is positvely correlated to the managerial expenditures. So, γ>0 and his/she utility funcion is U=U(x,p,M) with $U_x \geq$ or <0, U_p>0, U_M>0[10]. In analytical form it is $U=ax^{\alpha}p^{\beta}M^{\gamma}$ (with with $\alpha \geq$ or <0, β, γ>0 and $\alpha+\beta+\gamma<1$).

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[8]If $U_x=V_x$ and $U_p=V_p$ the manager has the same objective function of the organization and his behavior is such that organization's objectives are realized.

[9] This is true also if U_x=0.

[10]Like the cases 2.1, 2.2 and the note 9, the commercial acivity can be utility improving, neutral or

Differently from the previous cases, the optimal manager's choice is such that M>0, but because of managerial expenditures, the frontier becomes A'B'. Managerial equilibrium is like the case 2.1 if $U_x \geq 0$ and the case 2.2 if $U_x<0$. In both cases, it is on the new interior frontier A'B'. AA' is the organization's inefficiency due to managerial expenditures. This is a technical and an allocative inefficiency. When the manager uses discretionnally some resources, he/she uses greater quantity of inputs respect to the minimum quantity and not minimizes costs. As M increases, the possibility frontier moves towards to the axis origin and the inefficiency increases.

3. Incentives for non-profit organizations

Previous section highlights a relevant problem of managerial accountability and commitment. The non distribution constraint does not seem an effective incentive to solve this problem. From a general pint of view, the non-profit organizations are similar to the public bureaucracies: in most cases, the organization's results can not be measured because their "social or public" content, organizational objectivs are, sometimes, multidimensional and there are many principals in the principal-agent relationship. Unlike most of public bureaucracy, most of the non-profit organizations work in a market setting with for profit firm. In this way they promises greater competition and responsiveness to market forces. Then, most of non-profit organizations are in an intermediate position between public and private sector. What are the effective incentives for this kind of organizations? How does the "traditional" economic incentives are modified in this context?

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distasteful.

Since contractual incentives, as profit share rules, can not be used in non-profit organizations because of the non distribution constraint, we consider the following three kind of incentives working in the organizations: market, reputational and ideological incentives. The aim is to show how their effectiveness can be modified in a non-profit setting.

3.1 Market incentives

Market incentives operating for the organizations can be divided in two groups: property rights incentives (or financial market incentives) and product market incentives.

3.1.1 *Property rights incentives*

Most of organizations, for-profit and non-profit, are characterized by the "separation of property from control" [FAMA-JENSEN, 1983; WILLIAMSON, 1964].

It is widely held that the greater efficiency of for-profit organizations is based on the effects that the ownership structure generates on the incentives received by agents operating in the organization. From an economic point of view the property rights are defined as 'residual control rights'. They consist in the authority that the holders of the right have to "choose, referring to specific goods, any whatsoever utilization within a set of non prohibited utilizations" [ALCHIAN, 1965, p. 90], and which confer the status of residual claimants.[11] Despite the ambiguities deriving from such definition[12], it is

[11] This is the power to acquire the income deriving from the use of the property resource object after having met all contractual obligations [MILGROM - ROBERTS, 1994]

[12] As Milgrom and Roberts [1994] point out, the concept of residual claimant is far from exhaustive. When, e.g., a company pays its staff a bonus, increases salaries in favourable periods, or uses various incentive techniques linking remuneration to profits, it could be said that some worker are sharing in the company's residual claims?

possible to state that the property incentives are realized when the decision-maker fully sustains the consequences of his/her choices.

In a non-profit organization there is no residual claimants. An immediate consequence is a larger management discretion, no longer exposed to control and sanctioning mechanisms exerted by the property rights market[13].

For-profit organizations with a low-performance, can be subject to the *take-over*, i.e. the acquisition of the control package by groups able to replace the organization's management. Then, the threat of substitution, can constitute a tool to enforce a managerial behavior more consistent with organizational objectives[14].

Moreover, the lack of property rights implies that it is not possible to reallocate the risk between agents and to reserve the role of "owners" to less risk adverse subjects. This might be a partial explanation as to why many non-profit organizations operate in sectors (charities, culture, health) with low risk levels, impeding, from a macroeconomics point of view, the development of more innovative and risk-taking activities.

At the same time, the lack of a property rights market implies that the ownership can not be reserved to subjects acquiring more specific information and knowledge in those sectors that they consider more useful and into which they decide to invest their wealth. The lack of "specialization" of ownership reduces the patrons' incentives to efficiently control the behavior of agents working in the organization, in particular of the management.

[13] i.e. the lack of a corporate control market.

[14] It is, however, necessary to clarify that the corporate control market is not always able to guarantee efficient form of manager control. Grossman and Hart [1980] maintain that, with multi-participant shareholding, the prevalence of free-riding behaviour neutralizes the efficacy of take-over. In general, the effectiveness of corporate control greatly depends on the working mechanisms of the shares market. The existence of speculative maneouvres, asymmetric information and transaction costs can alter the mechanism of the corporate control market.

3.1.2 *Product market incentives*

Many non-profit organizations carry out commercial activities in competition with for-profit firms. What are the effects of this different organizational objectives on market mechanism?

From a traditional economic point of view, the market is an institution with voluntary transactions. In this setting, the different agents' objectives are made compatible each others by the market's coordination function between the demand and supply side.

With perfect competition the equilibrium is *market clearing* and the market offers endogenous incentives to an efficient uses of resources. This situation changes with competition between firms with different objective, i.e. non-profit and for-profit firms.

When firms'objectives have a prevalent "social" content, the impossibility of their misuration (even if partial) can generate "barrier to exit" [HANSMANN, 1980].

In particular, this is true for the organizations whose funds are donations or public funds not correlated to the efficiency and effectiveness of the organization. In this case, the market selection is not oriented towards the more efficient firms and inefficient and not effective firms can survive. Their activity is, therefore, justified only for the social content.

Even for pure commercial non-profit in competition with for-profit firms, the market selection mechanism can work in a different way respect to the traditional way.

We consider two cases. In the first case, the non-profit organizations are not minimizing costs. They have higher costs with respect to the for-profit commercial firms. In the second case they have smaller costs.

With non-profit organizations not minimizing costs, inefficient organizations with higher costs can survive if their objective is to obtain some resources (even if smaller with respect to the others commercial firms) only to finance some level of insitutional activity with *cross-subsidization* policies. [MITTONE, 1996, p.143]. Then there is a weak incentive to search technologies *costs-saving*.

If non-profit organizations have smaller costs compared to for-profit firms (for example because they use voluntary job), their could be, in theory, more competitive. Then, from an economics point of view, their market share expands with respect to the lucrative firms. Nevertheless, the non-profit organizations not always are able to increase their supply as the demand increases, thus leaving market shares to less competitive firms. This process occurs because non-profit financial resources (such as private donations, revenues from commercial activity or public funds) not always are easily and immediately available. In others words, the non-profit organizations can have more difficulties to collect capital[15] when they need.

3.2 Reputational incentives

Firms with a "good reputation" on the market have a greater probability of success. In order to provide oneself with a good reputation, some firms have to enforce correctly the contracts with the consumers. Then, reputation is another source of potential incentives for the firms.

Nevertheless, the incentive to accumulate "reputation" is effective if the consumer is able to "punish" any possible opportunist behavior of the organization through the exit from the contractual relation.

[15]Unlike the for-profit firms, the non-profit organizations does not trade in capital assets market.

The heterogeneity of goods and services produced from the non-profit sector, their social content and the multidimensional objectives of the non-profit organizations make not easy for the consumer to acquire informations and to exert some control on organization's activity and/or on the characteristics of the good/service supplied[16].

These informative problems can make less plausible the threat of eventual sanctions from the consumer or from the beneficiaries, thereby also reducing the effectiveness of reputation mechanisms. The reputation of a non-profit organization (with respect to the quality of goods sold or the destination of donations) can be an incentive to organizational efficiency when the commercial activity either supplies experience goods (services), or is run in a competitive context that permits, at least ex post, some comparative evaluation.

In any case, the reputation mechanism is effective only when there is not any rationing of the goods/services on the supply side.

From the point of view of Weisbrod, for example, the non-profit organizations are a private solution to an unsatisfactory supply of public goods as regards both quality and quantity. Then, the possible difficulty of obtaining private donations due to the organization's "not very good" reputation can unlikely constitute a credible threat, since there are no alternative sources capable of fully satisfying the citizen's demand for same goods or public services. In other words, citizens unsatisfied for the goods/services offered by the non-profit sector should appeal to an alternative source, in this case the State which, however, is unable to entirely satisfy the demand. Thus for 'high-demand' citizens unsatisfied for public supply, the non-profit production can be a source of

[16]The same informative problems can characterize the relation between consumer and for-profit firm. Nevertheless, in non-profit sector they can be more relevant because of the particular nature of some activities (i.e. social activities) and the multidimensional objectives of non-profit firms. In this sense, non-profit organizations are more similar to the public bureaucracy.

increased utility, even if the amount or qualitative level of the goods is inferior to the quantitative or qualitative level which would maximize their utility.

3.3 Ideological incentives

A traditional line of reasoning argues that explicit incentives are not necessary in non-profit organizations because the agents involved in organization's activity have ideological incentives making their objectives identical to the organization's objectives.

This thesis can be acceptable for mutual benefits organizations of small dimension. On the contrary, it is not applicable to public benefits organization with a hierarchic organizational structure.

In such cases, the high number of principal-agent relations makes improbable the coincidence of the agent's objectives with the institutional ones of the organization. At the same time, where the management is not constituted by *patrons* but selected on the market on the bases of "economic"[17] criteria rather than on purely ideological criteria, it seems impossible to eliminate any agency problems.

A parallel thesis [YOUNG, 1983] is based on the idea that in non-profit sector, managerial remuneration is lower than in for-profit sector. A manager accepts a lower remuneration because he/she is satisfied by working in an organization whose objectives reflect his/her ideology. Then, the labour market self-selection is the more effective recruiting method for non-profit organizations. However, this thesis seems based on the assumption that the labour market works efficiently and its equilibrium is *market clearing*. On the contrary, if the labour market equilibrium is characterised by involuntary unemployement, the previous thesis does not hold. In this case, a worker

[17] For example on the base of the accumulated human capital. This situation occurs, with high probability, in very large organizations, run by "specialized" staff.

can be disposed to accept a lower remuneration if the alternative is the unemployement, even without any ideological motivation. So, the market labour does not implement any self-selection process and managerial opportunism is not eliminated.

4. The fiduciary duties of the administrators: implementation problems and possible governance rules of non-profit organizations

Previous sections highlight a relevant accountability problem in the non-profit sector.

The weakness of incentives implies that principal-agent relations are regulated almost exclusively by trust.

Two questions raise: what are the administrator's fiduciary duties? How can they be implemented?

Neither it is not possible to give a single definition of fiduciary duties, or to define effective implementation mechanisms which are not excessively expensive. It is however possible to define a number of important points on the basis of which to analyze the question.

We shall take, as starting point, the responsibility concept proposed by LEAT [1990, p. 144] who locates the responsibilities of the administrators in four diverse typologies dealing with:

a) the appropriate use of funds (accountancy responsibility);

b) the respect of rules dictated by organizational procedures as set out in the statute or internal regulations (procedural responsibility);

c) the quality of work carried out in the organization and administration of projects (program responsibility);

d) the destination of work to projects (see point c) or, in general, to activities considered ‘priorities’ for the organization (priority responsibilities).

The definition of precise responsibilities of the administrators of non-profit organizations inevitably raises a further question: who are the individuals legitimated to act in the event of the violation of same responsibilities?

An articulated classification of the various responsibilities necessarily involves different individuals who could, in different measure, oversee the implementation of those responsibilities. If the patrons are mostly interested in an appropriate use of the financial resources of the organization or, using Hansmann’s terminology, in evaluating the marginal impact of their donation on the organization’s activity (point a), the members seem to be the best candidates to evaluate internal organizational aspects (points b and c) and finally the beneficiaries probably represent the most suitable candidates to exert a control over the quantity and quality of the institutional activities of the organization through ex post evaluations (point d).

However, the selection of many subjects having power to implement precise responsibilities, is an expensive solution. The assignment of formal and effective legitimacy to different categories of individuals, can result in greater organizational rigidity. This means a reduced flexibility and speed of organizational action in offering of particular goods or services, which is among the principle motivations in favour of non-profit organizations in economic systems.

HANSMANN [1980] identifies two possible governance rules for the non-profit organizations divided in two groups: mutual and entrepreneurial.

In the first, “control” is carried out by the patrons through the exertion of the right to elect the administrators of the organization, who thus become susceptible to possible turnovers even if not dictated by market pressure. The situation reproduced is thus basically analogous to the separation of property from control regarding for-profit organizations. On the other hand, the governance model of entrepreneurial organizations is different because the board of director is "self perpetuating" and thus more similar to public bureaucratic models.

Even if the division proposed by Hansmann occurs in different non-profit organizations, it is not satisfactory for different reasons.

Firstly, the removal or the election of administrators is logically justified in cases of mismanagement or, in general, of non-satisfactory performances. Then, it is consequential to the collation and elaboration of the information necessary to evaluate managerial performance. But non-profit organizations occur in response to contractual failures whenever the informative disadvantage of the patrons is such as to make it impossible to monitor the contractually-established performances. Then, the patrons are not, by definition, able to carrying out efficient controls and evaluation performances. Even if these limitations were of minor importance, i.e. in small mutual organizations, the enforcement of the fiduciary duties through the possible actions of the patrons is, fundamentally, in contrast with the non-profit organization's economic role to protect the consumer and/or donor from self-interested behaviours. In other words, if the governance of the non-profit organization is entrusted to the general category of consumers or donors, who are then responsible for protecting themselves from any opportunistic behaviour, the boundary line between the non-profit and for-profit sector is greatly weakened. The latter can also assume a position of relative advantage due to its exposure to market pressures and to the mechanisms of corporate control.

A possible governance rule can be found by means of a public regulation of the sector. However, the centralized solution presents high administrative costs and has to operate in an extremely heterogeneous reality. Then, detailed and specific information on every organization are necessary.

Another possible governance rule is relative to the financial recruiting method of non-profit.

From a strictly financial point of view, the donor of a non-profit organization -the patrons-, provides the capital necessary for the organization's activity, but does not acquire any property right within organization. His role is, from this point of view, more similar to that of a bondholder who, however, has no direct economic interest in the activity of the organization and may therefore have fewer incentives to control the organization's activity.

Some proposals[18] suggest, for non-profit organizations, financial policies through the issue of bonds.

One aspect characterizes these bonds: the capitalized interest and bond's face value are paid after the liquidation of the organization. According this model, the investment in a non-profit organization does not give an immediate remuneration. This implies that investments are not directed only towards successful organizations but also towards new emerging organizations. At the same time, the bonds' market assures the mobility of investment.

An immediate consequence is therefore the projection of the non-profit organizations into a more competitive context, thus extending the competition with for-profit organizations on the financial level too.

[18]See for Italy the Parliamentary Act n. 6, doc. XXI, 2000.

A second effect concerns the possible modification of the control powers. In order to preserve the non-profit aim, control power could be structured on two levels. One level is mainly related to the administrative efficiency of the organization, and the other more geared to evaluating the effectiveness of the organization's activities. In this case, the role of member is separated from that of bondholder. The members would thus play an active role in fixing organizational policies, while the bondholders would supervise the economic and administrative aspects of the organization trough direct access to social information, and the exercising of any necessary sanction where the policies of the organization are inconsistent with investment security or, in general, in case of mismanagement.

Moreover, the selling of bonds can promote turnover of controlling group and this can prevent possible collusion agreements between backers and management.

5. Conclusions

This paper has analyzed the effects of managerial discretion on organizational efficiency of non-profit organizations in a comparative perspective and the effectiveness of different governance rules. Three different types of managers are considered: the *power-seeker* manager, the *product-mix oriented* manager and the *income-seeker* manager. The analysis shows that, according to the particular type of manager considered, different results can arise in term of efficiency.

Even if the managerial discretion problem is similar to the correspondig problem in for-profit firms, for non-profit organizations market, reputational and ideological incentives turn out to be weak. This is fundamentally due to the particular nature of goods/services produced. Their social content (even if in different measure among the organizations) poses non-profit organizations in a intermediate position between public and private economic sector.

Then, particular governance rules enforcing powers control are necessary besides “traditional” incentives.

A possible suggestion is to extend the competition between non-profit and for-profit organizations from the products level to that of private financing. Financing policies of non-profit organizations which offer them the tangible possibility to access debt capital could, on the one hand, reduce sub-capitalization problems and, on the other, to modify the backers’ interests as regards organization activity. Their investment has both an ethical and an economic content. In order to avoid a possible distancing from the non-profit philosophy, the role of backer is separated from that of member. Moreover, the bonds of non-profit could be such that their remuneration is not immediate. In this case a self-selection of investors could be implemented. Power control on economic and administrative aspects of the organization’s activity are given to the investors leaving to the members an active role in fixing organizational objectives.

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