

MANAGERIAL DISCRETION IN NON-PROFIT ORGANIZATIONS: AN APPLICATION TO SPANISH WORK ACCIDENT MUTUALS

*Eugenia Suárez Serrano**

Abstract

This paper explores the problems of managerial discretion in the non-profit sector, with special consideration to Spanish Work Accident Mutuals (MATEPs). Firstly, from Transaction Costs, Property Rights and Agency perspectives, the economic rationale of mutuals is analyzed, paying particular attention to MATEP's peculiarities and incentives in terms of competition, regulation and ownership. Subsequently, the effectiveness of governance mechanisms is discussed, showing that the status quo leaves excess power in the hands of the managers of these organizations.

Keywords: Work Accident Mutuals, non-profit sector, managerial discretion, corporate governance, Agency Theory, Property Right, Transaction Costs, Spain

* *Universidad de Oviedo, Escuela Universitaria Jovellanos, C/ Francisco Tomás y Valiente 1
33201 – Gijón (Spain), Teléfono: + 34 985 182 177, Fax: + 34 985 182 161
E-mail: meugenia@uniovi.es*

1. Introduction

The problems of managerial discretion that are usually studied in the field of corporate governance can also arise in other types of organizations in which a delegation of the capacity of decision occurs. This article analyses the possible existence of managerial discretion in Work Accident and Occupational Disease Mutual Insurance Companies (MATEPs), entities of a great economic and social significance in Spain.

MATEPs are voluntary associations of employers, which act as collaborating entities of the Social Security in the carrying out of occupational risk insurance¹. They are financed by compulsory employer's contributions and, as a counterweight, offer to the associated companies a comprehensive service that includes: (i) preventive measures; (ii) health care for workers affected by occupational accidents and diseases; and (iii) monetary compensations in case of incapacity, disability or death. Because they manage public funds, the functioning of the MATEPs is, moreover, subject to strict and exhaustive controls

This sector, originally highly diffused and of a marked regional and sectoral nature, has experienced an intense process of realignment and concentration in the last decade, propitiated mainly by the tightening up of constitution requirements. In a short period, two out of three MATEPs disappear, allowing nearly

thirty better prepared entities and of a greater geographic implantation to assume the new competences conferred on by the Social Security (Suárez and Ventura, 1999). Likewise, the government introduced, some years ago, a new Regulation of Collaboration² aiming to rationalize the MATEPs governance.

The paper first approaches, from the Economy of the Organizations perspective -Transaction Costs, Property Rights and Agency- the economic rationale of non-profit organizations and of the MATEPs, in particular. Next, we study and discuss in detail the MATEPs and their external and internal governance mechanisms to, finally, draw a series of conclusions regarding the degree of managerial discretion in these entities.

2. Economic Analysis of Non-Profit Sector

2.1 Economic Rationale of Non-Profit Sector

The non-profit organizations (NPOs) coexist with for-profit and the public sector. However, fixing the limits that separate such organizations from the rest is not an easy task; although private, they actively collaborate in the aiming of public objectives. Thus, the NPOs are set in the so-called Third Sector³ con-

¹ The insurance of labour contingencies is compulsory; however, employers are free to choose between the Social Security and MATEPs. Now, the whole market is practically controlled by the latest.

² RD 1993/1995 December 7, in substitution of RD 1509/1976, May 21.

³ The Third sector delimitation is in many cases confusing, as this term, of Anglo-Saxon origin, tends to be used as a synonym of the

text, as a residual group of neither capitalist nor state organizations (Mertens, 1999). However, what makes an organization be non-profit? According to Hansmann (1980), the NPOs differ in the following characteristics: a) they are not allowed to pay their surplus and b) their functions are limited to certain activities.

The importance of this sector to the economy is not questionable, since, from the eighties, its contribution to the Welfare State is increasing. However, which have been the causes that lead to this expansion? In other words, which is the economic rationale underlying this mixed form of transactions governance? The three theories taking part in the so-called Economy of the Organizations -Transaction Costs, Property Rights and Agency- will help us to explain the emergence of the NPOs⁴.

According to the Transaction Costs Theory, only those organizational forms, which reduce the transaction costs derived from the asymmetries of information, will survive (Williamson, 1975). In this way, Hansmann (1980) suggests that the origin of the NPOs is based on the 'contract failure' associated to certain transactions. In his opinion, these organizations arise when a separation between the purchaser and the beneficiary takes place, when strong investments in specific assets -which generate conflicts in the appropriation of quasi rents- are required and/or when the characteristics of the product -complexity, intangibility, multidimensionality - make its evaluation difficult. Under these circumstances, the donor or the client, facing possible opportunistic behaviour from the suppliers of such services, may choose a NPO to compensate the problem of asymmetric information (Weisbrod, 1988). Although, corporations own mechanisms to protect buyers -as warranties- (Williamson, 1985), some transactions are subject to uncertainty and to which a failure in the service can be so costly that the ex-post compensation would not be enough for the client (Holtmann and Ullmann, 1991).

Another theory related to the 'contractual failure' is that of the Property Rights. The property of an asset means the right to the appropriation of the residual rent (Alchian and Demtsetz, 1972) and to the residual control (Grossman and Hart, 1986). Both concepts are linked to the absence of full contracts; otherwise, everything would be contractually specified and assigned and the residual rights would have no significance. The efficiency of the non-profit governance mechanism can be explained by the specific distribution of property rights in these organizations, as it mitigates 'contract failure' -that together with government and philanthropic failures

are regrouped around the concept of 'coordination failure'- (Enjolras, 2000).

Gui (1991) and Mertens (1999) distinguish the NPOs from the rest of organizations according to two categories⁵: the 'beneficiary category', which acts as a claimant, that is, it is entitled to receive the residual rent; and the 'dominant category' on which the residual control rights lay. Whereas the investors assume both roles in corporations, in the NPOs the beneficiaries are different from the investors. In other words, facing market failures -asymmetric information, market power, public goods-, the NPOs come out as organizations where residual rent does not rely on the owners but on the consumers. Nevertheless, as Mertens (1999) explains, this definition should not confuse the NPOs with the Public Sector, since in the former the residual control is not in the State hands.

From an Agency perspective, the survival of an organizational form will depend on its comparative advantage to control agency costs resulting from the conflict of interest between the parts (Jensen and Meckling, 1976). In this way, the peculiarities of the residual claimants will help to distinguish one organization to the others and to explain their survival (Fama and Jensen, 1983b). These authors suggest that NPOs appear to be the solution to solve the agency problems derived from donations: making inalienable the right to demand residual claims and agreeing with donors that in the future, all surplus will be applied to services. Furthermore, these authors affirm that the larger the quantity of donations and the easier to separate the executive and control decisions, the more successful the organization will be.

Although all the analysed theories point to the asymmetric information problem as the factor to justify the creation and survival of the NPO, they also agree to emphasize that these organizations show limits in their functioning, motivated by the ineffectiveness of the imposed restrictions on the profit-making (Figure 1)⁶. Despite the fact that surplus cannot be distributed as dividends, in practice they are distributed in other ways. From the Transaction Costs approach, the donors and clients who choose a NPO, to protect them from the suppliers' opportunistic behaviour, have some difficulty to control the managers' opportunism (Hansmann, 1980). According to the Property Rights Theory, the residual rent was placed in the client, but the reassignment of the residual control right could turn managers into the 'dominant category' (Hansmann, 1988; Gui, 1991). In that case, how can it be guaranteed that clients

French term Social Economy, which includes not only NPOs but also cooperatives and certain types of profit making mutuals.

⁴ Nevertheless, many other theories are used to justify the survival of NPOs, for instance, those based in tax incentives, institutional inertia or altruism.

⁵ Gui (1991) makes a distinction between NPOs and corporations; and Mertens between NPOs and public organizations.

⁶ Which would explain that non profit, for-profit and public institutions survive in the same industry (Handy, 1997). For instance, the following sentence by Rose-Ackermann (1996:717) is very controversial "NPOs emerge due to, not despite of, their inefficiencies.

have more control over the managers than the shareholders do? Finally, based in the Agency Theory, Fama and Jensen (1983b) suggest that the surplus generated by NPOs is assigned, although nobody has property rights over it, and they state that donors (and/or clients) face problems of managerial discretion similar to those in other organizations subject to the separation between ownership and control. In addition, Rose-Ackerman (1966) points out that this is a particularly serious problem in the non-profit sector, since the absence of a market for corporate control does not allow disciplining the managers in a proper manner.

Figure 1

As it is not clear that the limit imposed on the profit-making leads the organizations to focus exclusively on the attention to the clients, it will be precise to find a mechanism of control to prevent managers from appropriating parts of the surplus in form of salary increase, excessive expenditure, over-investments and risky growth strategies. Easley and O'Hara (1983) affirm that it is necessary to introduce an additional restriction on managers' compensations. Fama and Jensen (1983b) suggest that, to control the managerial discretion in the NPOs, there must be an effective separation between execution and control decisions. According to Knapp and Kendall (1991), the main point is to make NPOs more transparent and able to provide disintegrated information about their activities and results, highlighting the significance of self-regulation through Codes of Good Practice. Other authors give perhaps more influence to the external mechanisms. Thus, Hansmann (1980) maintains that the competition in markets against other organizations leads the NPOs to maximize the output to satisfy their clients. In other cases, the protection of the users' rights by the government intervention is defended (Krashinsky, 1986; Gui, 1991). Nevertheless, Rose-Ackermann (1996) proposes that, even if the supervision makes sense to avoid the managers' opportunism, there is a risk that an excessive intervention could lead to a loss of the advantages that NPOs offer in terms of quality and differentiation.

Mutuals in The Non-Profit Sector

So far the criteria used to classify the organization have been the profit restriction, distinguishing between the profit-making and non-profit organizations. Nevertheless, The NPOs might have different legal forms and seek diverse goals (Salamon, 1991). For a better understanding of the non-profit sector, we opt to divide the organization according to their objectives⁷. Thus, as we can observe in Figure 2, there are

two different types of NPOs: a) the mutual interests organizations, focused in the rendering of goods and services to its members –mutuals, unions, clubs, professional associations-; and b) the public interest organizations, which contribute to the general welfare, offering services to social groups with great sanitary, cultural and educative needs.

Figure 2

According to the classification stated above, mutuals are included into the 'member oriented' NPOs; in other words, they are organizations with an 'internal projection' and with performance aim to improve their associates' welfare (Montserrat, 1991). Not all the authors include mutuals in the profit-making sector. For instance, Gui (1991) states that the lack of profit making of these organizations cannot be asserted, since they seek their associates' interests. Hansmann (1980) goes further and declares that mutuals are even closer to the cooperatives than to the non-profit sector. On the other hand, Mertens (1999), with a more European vision, defends the explicit inclusion of mutuals into the Third Sector because although the 'dominant' and 'beneficiary' categories fall on the same person -the service's target group- this category does not have the condition of investor. In his opinion, despite the fact that the members of a mutual play a double role, they are not interested in increasing the profitability of their contributions -as associates- but in obtaining the greatest benefits -as users.

Once mutual organizations have been placed in the non-profit sector, we return to the three theories analysed in the previous epigraph. As stated by the Transaction Costs perspective, mutuals would allow solving information problems present in certain transactions. Therefore, the pursuers of a difficult evaluation product will overcome their lack of information by taking part in the donor organization (Ben-Ner, 1986). Consequently, mutuals would be a hybrid governance mechanism that, through relational contracts, would ease the control of an activity without requiring its integration. Figure 3 shows the relation of substitution between the incentives and the control proposed by Rumelt (1995), to whom relational contracts⁸ are explicitly added as an intermediate solution able to generate mayor incentives than those of the hierarchy, but reaching a superior coordination to that of the market. Precisely, Kay (1991) asserts that the main advantage of mutual forms is based in the easy development of relational contracts, as it can be observed in the underlying culture of the most successful mutuals.

⁷ It is commonly said that profit-making companies have private objectives, but, as showed in Figure 2, there are also certain public companies which, despite their legal form that allow them to share the surplus, their objectives are public -employment promotion, exploitation of local resources or strategic sectors protection.

What usually happens in these organizations is that, in many cases, the benefits are not distributed since they are loss-making.

⁸ Relational contracts appear when the recurrence of the exchange justifies an ad-hoc instrument to rule long-term and continuous relationship between the parts. Their terms are usually explicit and based on a mutual necessity of continuing the relations in the future (Williamson, 1985).

Figure 3

The Property Rights approach highlights the double role given to the clients of mutuals, as a way to solve the 'contractual failure'. Since the organization control is held by the 'beneficiary category', the clients will be in a position to ensure them that in case the surplus occurs, it will be in their benefit. This peculiarity allows mutuals to have an implicit distribution, to the detriment of explicit causes of distribution (Gui, 1991). Moreover, Kay (1991) suggests that the relative ambiguity in the distribution of the residual rent could be one of the factors that explain the success of some mutual organizations, since they are capable of accumulating substantial reserves to finance their development. Finally, the Agency Theory emphasises once more that clients have the right to demand residual claims in mutuals, which means a restraint on managerial discretion in comparison with the NPOs of general interest. Nevertheless, as maintained by Fama and Jensen (1983b), the mutuals survive due to a singular characteristic by which, each client can exercise the above mentioned right at any moment, for a value calculated according to an established regulation. This form of partial liquidation minimizes the agency costs, since it reduces the managers' control over the entity's assets⁹. Moreover, mutuals either usually limit the acceptable risk because their activities are restricted by regulatory imposition or voluntarily established in their articles of association (Kay, 1991). Therefore, the agent's margin of action is restricted so as not to deviate from the principal's objective. From the above argument, it can be stated that, mutual organizations main advantage is their capacity to facilitate the observance of the performance and, thus, to mitigate informative problems¹⁰. However, this type of organization is not exempt from inconvenient. Firstly, clients usually subsidize other clients; because the condition of associate guarantees their contribution is to be used as services for the members, but not entirely in their own benefit (Hansmann, 1980). Secondly, as the title of mutualist is not transferable through a market, an improvement in the management is not immediately capitalized as the associates' wealth, which propitiates the managers' negligence (Alchian and Demtsetz, 1972); what is more, this does not allow the existence of a market for corporate control as strong as at the public limited companies. Finally, the lack of clarity in the residual rent distribution is reflected in a less effective way of managers' accountability (Kay, 1991). In any case, if mutual forms are to survive in an increasingly global and competitive environment, they

⁹ The facility associates have to abandon the entity makes necessary a compulsory secondary market, where its assets can be exchanged and valued to a low cost. This allows explaining the reason why mutuals are typical organizations of the financial sector.

¹⁰ Some authors have found evidence that changing form a stock to a mutual-ownership structure is on average efficiency enhancing (Mayers y Smith, 1986).

will need to adopt effective corporate governance rules to safeguard members' control (Chaddad and Cook, 2004).

3. Description of MATEPs

The uncertainty and the limitations of civil law with respect to responsibility have justified the development of labour contingencies insurances. Therefore, although the financial burden derived from the worker's accident or damage fall on the employer, the difficulties to determine the fault on the part of the company have led to substitute possible litigations for an insurance coverage. In Spain, once the Law of Work Accidents, which held companies responsible for such accidents, came into force in 1900, voluntary mutuals of employers started to be set up to share occupational risks. The asymmetries of information induced these organizations to have a rapid expansion as a more efficient formula than capitalist companies. Later, the insurance became compulsory and profit-making insurance companies disappeared from the section of occupational risks. In 1974, MATEPs were incorporated into the Social Security as collaborating entities and they have been progressively subject to an exhaustive regulation, which, not only establish tariffs but also covers from their functioning delimitation to the surplus application. This wide regulation in the sector has created a complex agency relations network, in which MATEPs act as double agents in front of the companies and the Social Security. As it can be observed in Figure 4, when an employer -responsible for the working health of his employees- chooses a MATEP, he delegates on it the necessary services caused by occupational risks, in exchange for the compulsory tariffs to be paid to the Social Security. At the same time, this institution -competent organ in the field of occupational contingencies insurance- transfers the coverage to the MATEP and, therefore, the management of such risks. Nevertheless, in case surplus occurs, mutualists will not share it by way of bonus, but -according to the regulator- by applying it to social funds.

Figure 4

To sum up, MATEPs appeared as NPOs of 'mutual interest' with the aim of safeguarding the rendering of certain services -preventive, sanitary and economic- to their members. Nevertheless, contrary to the conventional mutuals, residual claim and control rights do not exactly fall on the same people: on the one hand, employers are, along with workers, the target group of the MATEPs services and, on the other, the residual control is shared by mutualists and the Social Security. The complexity of the system generates, therefore, problems of decisors behaviour observance, closer to the ones existing in the 'general interest' than in the 'mutual interest' NPOs. The most part of the MATEPs compensations are assigned to protected workers, so employers will have difficulties to control services. Likewise, being

MATEPs financed by social contributions paid by companies to the Social Security, a separation between the donor of the cause -public funds- and the beneficiaries may occur. In conclusion, the carried out analysis points out that the problems of asymmetric information regarding managers will be more noticeable in MATEPs than in conventional mutual organizations, generating a greater margin of managerial discretion. However, the appearing of opportunistic behaviour will depend, in the last place, on the effectiveness of governance mechanisms, which will be discussed in the following epigraph.

4. Evaluation of The Managerial Discretion in MATEPs

There is a wide range of instruments that can condition and limit the managerial discretion¹¹. On the one hand, the external mechanisms, related to the different markets capacity to discipline decisors. On the other hand, the internal mechanisms emerged from the assignment of residual control rights in the core of an organization. However, we should take into consideration that empirical research on non-profit boards suggests governance being a complex, inherently difficult and problematic activity; so only multiple theoretical perspectives allows to explain the ambiguities that these boards face (Jegers, 2002; Cornforth, 2004).

4.1 External Governance Mechanisms

Product Market Competition

If a company acts in a competitive product market, the managerial discretion will be limited, since an inadequate administration would be reflected in the entity's result. However, while the company holds certain market power, managers will have a margin to meet the principal's objectives and dedicate part of the surplus to satisfy their own utility functions (Holmstrom and Tirole 1990)

The market where MATEPs perform is very peculiar. MATEPs cannot compete through the price mechanisms, since the State, according to the occupational risk in each working post, fixes prices to the entire system. Nevertheless, as Lewis and Sappington (1988) suggest, it is necessary to establish prices that are sufficiently high enough to ensure quality services. However, if they are excessive, inefficiency and waste may occur (Pope, 1990). In the case under discussion, it is commonly agreed the existence of a gap between risks and prices (Suárez and Loredó, 2001). During the last twenty years, the pricing framework has just suffered light modifications and a 10% reduction. Despite this situation, the permanent and almost generalized generation of surplus indicates that prices, once the mutualist expectation was covered, allows a wide actuation margin to the

managers. Additionally, the existence of over-investments and excessive administration costs would corroborate this affirmation (Loredó, Suárez and Ventura, 2001). The quality-price ratio will also depend on the existence of competitors. In this sense, Joskow and Rose (1989) affirm that when prices are regulated, companies tend to compete in other variables, so if these tariffs were fixed above market prices, the competition between entities would encourage a quality improvement. It seems that the MATEPs regulator has consciously opted for fixing high prices and letting competition to promote the quality of services. Thus, associates could change entity voluntarily, providing that contracts are renewed on an annual basis and applications requested a month ahead. Moreover, any mutual chosen by an employer must admit him as an associate, since MATEPs cannot openly select their risks. This situation causes a low cost change, giving the employer an advantageous negotiating position against his present mutual.

Nonetheless, this result can be achieved by giving users real freedom to choose and exercising this right properly. Several factors prevent an intense competition among MATEPs. Firstly, the strong asymmetric information employers suffer; since, in most cases, they are not aware of the advantages they have been conferred by their associate position -premiums are considered as taxes-. Similarly, mutuals have restricted actions in the commercial field, so problems of information cannot be solved. Secondly, the MATEP election, especially in the case of smaller firms, is delegated on an external labour advisor who simultaneously acts as a MATEP implicit commercial agent¹². Thirdly, the company's geographic location can be another restriction as MATEPs are not distributed homogeneously throughout Spain and, depending on the region, some entities have certain market power¹³.

To sum up, the combination of high tariffs and imperfect competition confers managers a comfortable situation, allowing them a broader degree of discretionality. The product market capacity -tariffs- to discipline managers gets complicated by the amplification of the given competences to the MATEPs, whether inside the Social Security system -temporary disability for common contingencies -or outside -preventive measures¹⁴.

¹¹ The enumeration done in this sector is not meant to be exhaustive, since other governance mechanisms as the competition in the market for executives (Fama, 1980) or systems of incentives (Murphy, (1997) take place.

¹² In the segmentation done by Suárez and Ventura (1999), it is confirmed that inside the group of 'unsatisfied clients' is where a major number of employers delegated the election of entity on an external advisor.

¹³ This situation could have been accentuated by the concentration experienced in the last years, although it is also possible that the territorial expansion process undertaken by small mutuals could have intensified the competition in certain areas.

¹⁴ De las Heras (1997) and Sempere (1999) suggest that MATEPs could create an unfair competition with profit-making companies specialised in prevention management. Not for nothing, when a regulating entity is allowed to diversify towards a competitive market, it will tend to produce a quantity superior to the optimum (Averch and Johnson, 1962).

Market for Corporate Control

The market for corporate control allows substituting, through an acquisition offer, those managing teams that do not generate value (Manne, 1965). Given that this governance mechanism is usually costly, it is only activated once the rest have failed. A real control market does not exist in MATEPs, because the residual property rights are inalienable. If the management is inadequate, associates can either change the mutual or wait for the merging or taking over of the entity. Likewise, the concentration process this sector has come through during the last decade could be understood as a corrective action against inefficiency situations. Nevertheless, most merging and taking over actions among MATEPs seem to have been friendly, so this mechanism does not mean a clear limit for managers -it could be said that merging and taking over show the managers' interest in expansion strategies.

Debt

Debt introduces incentives that prevent managerial discretion (Jensen, 1989). The firm is contractually bound to pay the interest and redeem the principal. Consequently, denotes a strong commitment in comparison with equity; as it reduces the amount of free cash flow available to managers, forcing them to disgorge cash rather than waste it. However, the financial debt in MATEPs is insignificant, because, the development of their projects is commonly self-financed. Therefore, the absence of debt will not restrain the managers' opportunism.

4.2 Internal Governance Mechanisms

Exit as a Governance Instrument

As we have just indicated, Fama and Jensen (1983b) see the members' exit as a peculiar internal governance mechanism that comes to replace, in mutuals, the equity market. Although in MATEPs exit, as well as in all the Spanish mutuals, the associate is regarded as a client, not as a member. The employer leaving the entity has no right to receive compensations due to accumulate assets through surplus. Accordingly, this instrument -as Fama and Jensen state- is not present in MATEPs, despite of the exit as a client will impose an external limit to the managerial discretion through the product market.

Regulator Control

The systematic supervision practised by the regulator is usually considered as an external governance mechanism (Demsetz and Lehn, 1985). Nonetheless, in the case of MATEPs, the Social Security and mutualists jointly assume the role of principal. Therefore, the regulator control should be included within the internal governance devices.

On the one hand, the State applies a group of preventive measures to avoid misgovernment situa-

tions: submission to the public budget, audit reports, permissions to undertake investments, inspections and controls by the competent institutions. On the other hand, the regulator can also correct irregularities through penalties, restructure plans, cease of governing organs, or even the entity's liquidation. Both types of control -preventive and corrective- mean a fundamental makeweight to limit the moral risk in managers' decisions inside the MATEPs.

Associates' Control

The control exercised by associates through legal established means should be the most patent device. They take transcendental social decisions by the Annual Meeting. The existence of jointly held responsibilities would encourage the participation of this organ and a greater concern about the entity good functioning. Although these incentives are undeniably present, it is also true that, as it happens in large diffused corporations, the 'free riding problem' may appear (Grossman and Hart, 1980). The supervision accomplished by an associate rewards equally the rest, including those employers who never take part in the Annual Meeting. This asymmetry between the effort and the reward obtained discourages the surveillance works. It must be taken into account that, the diffused property is maximum in MATEPs, since decision taking is based on one vote per member, regardless the contribution provided¹⁵. In corporations, on the contrary, the presence of large shareholders reduces managerial discretion (Shleifer and Vishny, 1986).

In conclusion, given the concentration process in this sector, as the entities size increases, the intensity of incentives to participate decreases and so the 'free riding behaviour' will become stronger.

Boards Composition and Functioning

The argument supported by San Sebastián (1996) in relation to corporations can be extrapolated to MATEPs: the centre of decision has been progressively shifting from Annual Meeting to the Board of Directors. The former holds just certain fundamental decision and delegates the real control of the organization to the managers. To avoid an excessive power accumulation by the directors, diverse modifications have been introduced in the MATEPs control boards' configuration, being all of them summarised and develop by the Regulation of Collaboration of 1995. These changes in the regulator framework have been permeable to the proposals of different Codes of Good Practice that have come out in the last decade (Cadbury, 1992; Vienot, 1995; Olivencia, 1998; Hampel, 1998; OCDE, 1999; OCDE, 2003):

¹⁵ According to the extension of collaboration in 1996 to temporary disability for common contingencies of self-employed workers, these will not acquire the condition of associates, so they will not bear the jointly responsibility but neither could they take part in governance control organs. In fact, they act as clients of an insurance company (Panizo, 1999).

A) Firstly, a drastic separation of functions has been chosen. The Board of Directors is constituted by non-executive members and, as it will be later seen, the executive tasks fall on a single Executive Director. The Regulation of Collaboration code establishes that the components of the Board of Directors will not work for the MATEP, have a rendering service contract, or be remunerated by the entity. This measure is just taking to the extreme the recommendations from the above-mentioned Codes of Good Practise, which defend the existence of non-executive members who can balance the power relation and avoid boards being dominated by executives¹⁶. The former regulation allowed, instead, executive and remunerated posts, which could have originated opportunistic behaviours. On the other hand, in contrast to the previous regulation that provided the possibility of naming a manager with an associate condition in the MATEPs, the current rules governing MATEPs force these entities to name a professional Executive Director through the Board of Directors. The Executive Director independence also introduces a second separation of power, since this person cannot be the same as the Chairman. The fact that the Executive Director can attend the Board of Directors meetings without the right to vote reinforces institutional subordination of the chief executive. The last link in this segregation of functions is jointed round two organs of participative control, in which the protected workers as well as the associated companies are represented. From 1995, each MATEP should constitute a Monitoring and Control Committee¹⁷, whose functions are to request all the necessary information regarding the mutual management and propose whatever measures aimed to best fulfil the entity's objectives. There is also a Special Social Benefit Committee, which distributes, among protected workers, the Social Assistance Fund -endowed with the 10% of generated surplus-. These organs are similar to those supervision committees in large German companies, in which workers are present. However, in the MATEPs case, the particularity lies in that the represented workers are not from the mutual, but indirectly -and through unions- from associated companies.

Overall, regarding the division of responsibilities at the head of MATEPs (Figure 5), the regulation has gone further up than in the private sector. Not even The Olivencia Report (1998) contemplates the dualism, and simply recommends non-executive members in the composition of Boards in corporations. However, in the case of MATEPs, a model combining dualist features with an almost preponderance of non-executive members has been chosen.

¹⁶ Nevertheless, some authors disagree with this type of design and defend that, when in the Board's composition there is an only member with executive responsibilities, a strong informative asymmetry occurs regarding the entity's real situation (Johnson, Daily and Ellstrand, 1996).

¹⁷ This control mechanism appears with the Law 42/1994, although it is later gathered in the Regulation of Collaboration.

Figure 5

B) The size of the Board of Directors has also been limited to a maximum of twenty members. Large boards have been proved ineffective and slow. In addition, they lack the necessary cohesion and encourage passive attitudes (Yermack, 1996). Two arguments would lead us to state that MATEPs will tend to increase the Boards of Directors dimension above an optimum. On the one hand, MATEPs, to fulfil their growth targets, will offer -through a mechanism similar to the usual cooptation in Boards of Directors- posts in the Board to large employers that agree to become members¹⁸. On the other, the concentration through friendly or agreed merging taken place in this sector during the last years could have derived in an increase of the number of Board members, since all the components would like to be represented in the new entity. Taking this into account, if limits had not been imposed, the meetings would have been more complicated and the decision making slower. Nevertheless, we should bear in mind that the restrictions of twenty members surpasses even the Olivencia Report Recommendations for the private sector, which establishes the adequate size between five and fifteen members.

C) Finally, incompatibility, responsibility and retributions are reformed in depth to obtain a major transparency. It seems logical that the legislator, preoccupied by the public funds use, has made an effort to prevent any conflict of interests, thoroughly establishing the incompatibilities¹⁹ and responsibilities²⁰ of Board members. To clarify the managers' compensations, it is forbidden, according to the 1995 Law of General Budget, to give compensations charged to public funds and the existing blinded contracts became illegal²¹. In addition, the Regulation governing MATEP Collaboration limits the administration costs according to income. This represents a strong restriction, as executive personal objectives (retributions, excessive expenditure...) are charged to this entry.

5. Conclusions

In this theoretical discussion has been showed that the restriction upon the profit-making present in mutuals does not eliminate the problems of managerial discretion. In the MATEPs case, this problem is

¹⁸ According to the Theory of Resources Dependency postulates (Pfeffer, 1972)

¹⁹ Any person who maintains a labour service, rendering or commissioner relationship with a mutual will not be legible to become a member of the Board.

²⁰ The rule regarding board members responsibility is perhaps the newest. Firstly, the MATEPs constitution articles are to establish such responsibilities, although in any case could be exonerated because the Annual Meeting authorise the detrimental act. On the other hand, according to the nature of the damage, the responsibility emerges -as an individual or jointly liability form- facing employers, the Social Security or the MATEP itself.

²¹ As a result, the Labour Department removed hundred compensations that MATEPs have agreed with their general and middle line managers.

particularly marked, since public intervention has been shaping a complex model in which managers act as agents regarding two principals -the Social Security and associates.

Some governance instruments that play an important role in corporations to mitigate agency costs are not plenary present: the financial debt is inexistent and the market for corporate control weak. This deficit has been compensated through a strict supervision by the regulator and facilitating the change of entity. However, the laxity of the established tariffs and the lack of effective competition have generated a comfortable environment for managers. The existence of excess in those inputs in which managerial discretion is clearly observed -assets over-investments and administration overstaffing- would confirm this argument. The associate control -underlying in the MATEPs spirit- should also contribute to restrict the manager opportunism. Originally, employers felt as a part of their MATEP and, therefore, they were interested in exercising their control rights. Nonetheless, the concentration process and the extension of competences to new activities have adversely affected the sense of identity among associates and led them to behave as clients.

Consequently, the control has been displaced towards the Boards, as in large corporations. The legislator reaction to rationalise the MATEPs governance -imposing separate functions, restricting the size of Boards and limiting responsibilities, incompatibilities and remunerations- runs in the same direction as the different proposals to reform Boards of large public limited companies.

References

- ALCHIAN, A. and H. DEMSETZ (1972): "Production, information and economic organization", *American Economic Review*, 62, 777-795.
- AVERCH, H. and L. JOHNSON (1962): "Behaviour of the firm under regulatory constraint", *American Economic Review*, 52.
- BEN.NER, A. (1986): "Non-Profit Organizations: Why do they exist in market economies", in Rose-Ackerman (ed.), *The Economics of Nonprofit Institutions*, Oxford University Press.
- CADBURY, A. (1992): *The financial aspects of corporate governance*. London: Gee.
- CHADDAD, F.R. and M.L. COOK (2004): "The economics of organization structure changes: a US perspective on demutualization", *Annals of Public and Cooperative Economics*, 75(4).
- CORNFORTH, C. (2004): "The governance of cooperatives and mutual associations: a paradox perspective", *Annals of Public and Cooperative Economics*, 75(1).
- DEMSETZ, H. and K. LEHN, (1985): "The structure of corporate ownership: causes and consequences", *Journal of Political Economy*, 93 (6), 1155-1177.
- EASLEY, D. and M. O'Hara (1983): "The economic role of the non-profit firm", *Bell Journal of Economics*, 14, 531-538.
- ENJOLRAS, B. (2000): "Coordination failure, property rights and non-profit organizations", *Annals of Public and Cooperative Economics*, 71(3), 347-374.
- FAMA, E. (1980): "Agency problems and the theory of the firm", *Journal of Political Economy*, 88.
- FAMA, E. and M.C. JENSEN (1983a): "Separation of ownership and control", *Journal of Law and Economics*, XXVI (2), 301- 326.
- FAMA, E. and M.C. JENSEN (1983b): "Agency problems and residual claims", *Journal of Law and Economics*, XXVI (2), 327- 349.
- GROSSMAN, S.J. and O.D. HART (1980): "Take-over bids, the free-rider problem, and the theory of the corporation", *Bell Journal of Economics*, 11 (1).
- GUI, B. (1991): "The economic rationale for the 'third sector'. Nonprofit and other noncapitalist organizations", *Annals of Public and Cooperative Economics*, 62 (4), 551-572.
- HAMPEL, R. (1998): *Report of the Committee on corporate governance*. London: Gee.
- HANDY, F. (1997): "Coexistence of nonprofit, for-profit and public sector institutions", *Annals of Public and Cooperative Economics*, 68 (2).
- HANSMANN, H.B. (1980): "The role of nonprofit enterprise", *The Yale Law Journal*, 89 (5), 835-901.
- HANSMANN, H.B. (1988): "Ownership of the firm", *Journal of Law, Economics and Organization*, 4.
- HERAS, A. de las (1997): "Problemática de la actuación de las Mutuas de Accidentes de Trabajo y Enfermedades Profesionales de la Seguridad Social como servicios de prevención ajenos", *Revista Estudios Financieros, de Trabajo, Seguridad Social y Recursos Humanos*, 171, 47-58.
- HOLMSTROM, B.R and J. TIROLE (1990): "The theory of the firm", in R. Schmalensee y R.D. Willig (eds.), *Handbook of Industrial Organization*, North-Holland, Amsterdam.
- HOLTMANN, A.G. and S.G. ULLMANN (1991): "Transaction Cost, uncertainty and non-for-profit organizations", *Annals of Public and Cooperative Economics*, 62 (4), 641-654.
- JEGERS, M. (2002): "The economics of non profit accounting and auditing: suggestions for a research agenda", *Annals of Public and Cooperative Economics*, 73(3), 429-451.
- JENSEN, M.C. (1989): "Eclipse of the public corporation", *Harvard Business Review*, 5.
- JENSEN, M.C. and W.H. MECKLING (1976): "Theory of the firm: managerial behavior, agency costs and ownership structure", *Journal of Financial Economics*, 3 (4), 305-360.
- JOHNSON, J.L.; C.M. DAILY and A.E. ELLSTRAND (1996): "Boards of directors: a review and research agenda", *Journal of Management*, 22 (3).
- JOSKOW, P.L. and N.L. ROSE (1989): "The effects of economic regulation", in R. Schmalensee y R. Willig (eds.), *Handbook of Industrial Organization*. Amsterdam: North Holland.
- KAY, J. (1991): "The economics of mutuality" *Annals of Public and Cooperative Economics*, 62 (3), 309-318.
- KNAPP, M. and J. KENDALL (1991): "Problemas de política pública en el sector voluntario del Reino Unido en los años 90", *Economistas*, 51, 12-27.
- KRASHINSKI, M. (1986): "Transaction Costs and a Theory of Non-Profit Organizations", in Rose-Ackerman (ed.), *The Economics of Nonprofit Institutions*, Oxford University Press, Oxford.
- LEWIS, T. and D. SAPPINGTON (1988): "Regulating a monopolist with unknown demand", *American Economic Review*, 78.

31. LOREDO FERNÁNDEZ, E.; E. SUÁREZ SERRANO and J. VENTURA VITORIA (2001): "Discrecionalidad directiva en las Mutuas de Accidentes de Trabajo", Cuadernos de Economía y Dirección de la Empresa, 10, 465-483.
32. MANNE, H.G. (1965): "Mergers and the market for corporate control", Journal of Political Economy, 73.
33. MAYERS, D. and C.W. SMITH (1986): "Ownership and control. The mutualization of stock life insurance companies", Journal of Financial Economics, 16.
34. MERTENS, S. (1999): "Nonprofit organisations and social economy: two ways of understanding the third sector", Annals of Public and Cooperative Economics, 70 (3), 501-520.
35. MONTSERRAT, J. (1991): "Hacia una teoría económica del tercer sector: una primera aproximación", Economistas, 51, 48-55.
36. MURPHY, K.J. (1997): "Executive compensation and the modern industrial revolution", International Journal of Industrial Organization, 15 (4), 417-425.
37. NEWHOUSE, J.P. (1994): "Frontier estimation: how useful a tool for health economics?", Journal of Health Economics, 13, 317-322.
38. OCDE (1999): Principles of corporate governance. París: OCDE.
39. OCDE (2003): Recommendation on guidelines for managing conflict of interest in the public service. París: OCDE.
40. OLIVENCIA, M. (1998): El gobierno de las sociedades cotizadas, Madrid: Comisión Especial para el estudio de un Código Ético de los consejos de administración de las sociedades.
41. PANIZO ROBLES, J.A. (1999): "Los órganos de gobierno y participación de las Mutuas de Accidentes de Trabajo y Enfermedades Profesionales de la Seguridad Social", Tribunal Social, Revista de Seguridad Social y Laboral, 100, 47-61.
42. PICAZO, A.J. (1995): "La eficiencia en los seguros", Revista de Economía Aplicada, 3 (8).
43. PFEFFER, J. (1972): "Co-optation and the composition of electric utility boards of directors", Pacific Sociological Review, 3.
44. POPE, G.C. (1990): "Using hospital-specific costs to improve the fairness of prospective reimbursement", Journal of Health Economics, 9 (4), 327-251.
45. ROSE-ACKERMAN, S. (1996): "Altruism, nonprofits and Economic Theory", Journal of Economic Literature, 34 (2), 701-728.
46. RUMELT, R.P. (1995): "Inertia and transformation", in Montgomery C. (ed.), Resource based and evolutionary theories of the firm: towards a synthesis, Kluwer Academic Publishers, Boston.
47. SALAMON, L.M. (1991): "El sector no lucrativo en los Estados Unidos de América: una introducción", Economistas, 51, 6-11.
48. SAN SEBASTIÁN, F. (1996): El gobierno de las sociedades cotizadas y su control, Madrid: Centro de Documentación Bancaria y Bursátil.
49. SEMPERE NAVARRO, A.V. (1999): "La incesante metamorfosis de las mutuas patronales: ideas para el estudio", Revista de Seguridad Social y Laboral, 100.
50. SHLEIFER, A. and R.W. VISHNY (1986): "Large shareholders and corporate control", Journal of Political Economy, 94 (3), 461-488.
51. SUÁREZ SERRANO, E. and E. LOREDO FERNÁNDEZ (2001): "Organizational alternatives for companies' management of occupational risks: The examples of Spain and Argentina", International Social Security Review, 54 (1), 41-57.
52. SUÁREZ SERRANO, E. and J. VENTURA VICTORIA (1999): "Las Mutuas de Accidentes de Trabajo dentro de la Seguridad Social: ¿colaboración o competencia", Hacienda Pública Española, 151 (4), 71-83.
53. SUÁREZ SERRANO, E. and J. VENTURA VICTORIA (2001): "Managed competition and user satisfaction: the case of Spanish Work Accident Mutuals", International Journal of Public Sector Management, 14 (2), 149-164.
54. VIENOT, M. (1995): Le conseil d'administration des sociétés cotées. París: CNPF y AFEP.
55. WEISBROD, B. (1988): The non-profit economy, Harvard University Press, Harvard.
56. WILLIAMSON, O.E. (1975): Markets and hierarchies: analysis and antitrust implications. New York: Free Press.
57. WILLIAMSON, O.E. (1985): The economic institutions of capitalism: firms, markets, relational contracting. New York: Free Press.
58. YERMACK, D. (1996): "Higher market valuation of companies with a small board of directors", Journal of Financial Economics, 40 (2), 185-211.

Appendices

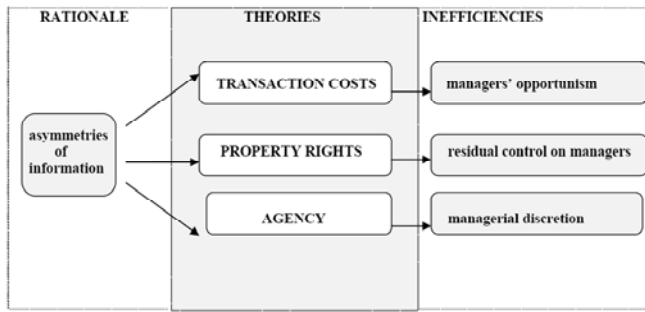


Figure 1. Economic rationale and limits of the NPOs

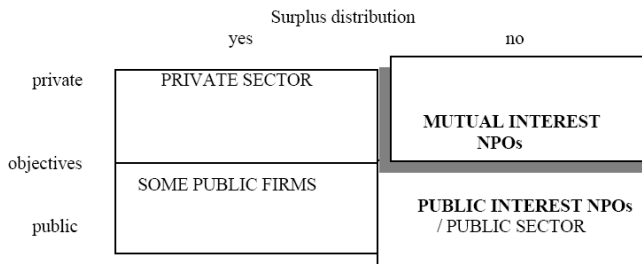
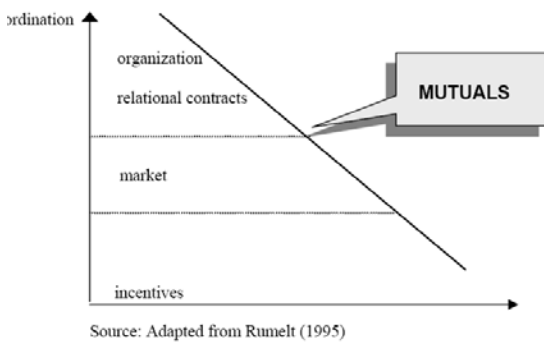


Figure 2. Classification of organizations



Source: Adapted from Rumelt (1995)

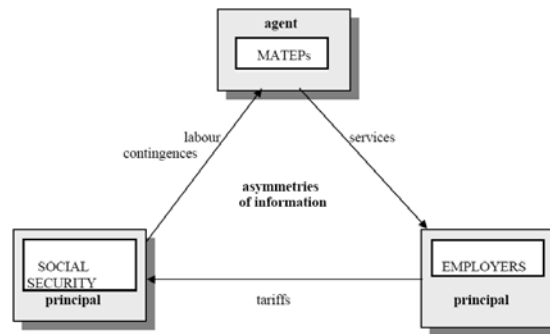


Figure 3. Relation between coordination and incentives

Figure 4. Agency relations in MATEPs market

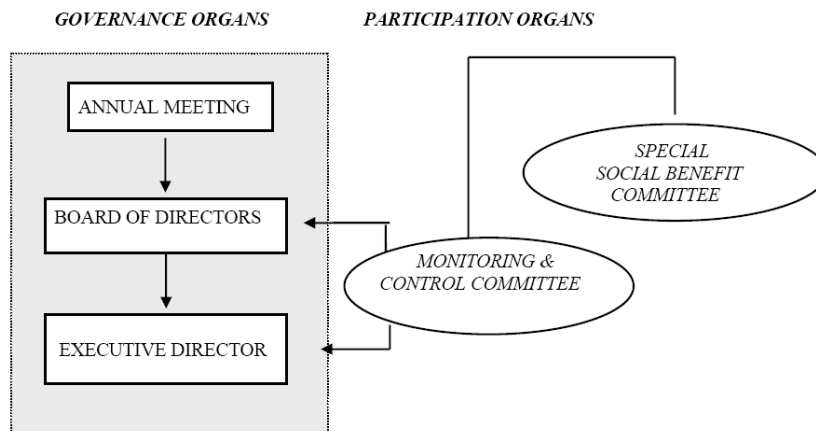


Figure 5. The MATEPs Governance