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GOVERNANCE STRUCTURES OF THE AGRICULTURAL CO-OPERATIVES IN BULGARIA – CONCEPTS AND PRACTICES

Summary: This paper examines the governance structures of Bulgarian agricultural co-operatives and the effective informal changes in the governance model. In this context, the focus is to study the innovations in the internal governance that either improve or deteriorate the governance structure. The agricultural co-operatives, as specific forms of doing business in agriculture, are part of the world economy. In the global world in which they are currently operating, market dynamics and growing competition have a significant impact on them: their visions, strategies, governance and governance structure are changing.

The empirical data are the result of case studies and in-depth interviews conducted by 32 agricultural cooperatives in Bulgaria during the period 2013-2016. Qualitative research techniques are used. As a result of the reported deviations from the legal framework, the in-depth study highlighted the need for new informal assisting bodies of the governance structure in Bulgarian agricultural cooperatives – Members Council, informal interest groups, attracting external experts. The loss of trust from members to management leads to their leaving the cooperative and directing them to corporate structures.

Key words: governance, governance structure, co-operatives and corporate governance, agricultural co-operatives, Bulgaria.

1. INTRODUCTION

The agricultural co-operatives, as specific forms of doing business in agriculture, are part of the world economy. In the global world in which it operate at the moment, market dynamics and increasing competition have a significant impact on them: their visions, strategies, governance, and governance structure are changing.

Over the past decades, these changes have focused the attention of a considerable number of researchers, practitioners and policy makers in Europe and North America. Their research focus are cooperatives operating on the basis

of non-traditional cooperative model. Part of the research advocates the thesis of radical deviations from traditional (classic) governance structure, in which property rights [Nilsson 1999] belong not only to members of the co-operative. Researchers have developed typologies with a different ownership structure (investing members and accrual of votes) focusing on capital investors and the control rights, property rights [Chaddad, Cook 2003], decision-making processes, formal and real (informal) governing bodies [Chaddad, Iliopoulos 2012]. Other scientists, consider decision-making process [BOEVSKY, LAURINKARI 2017], delivery rights – NGC, [Fulton 2000], changes of the formal rights of governing bodies (General Assembly, Board of Directors, Supervisory Committee, Chairmen), and the introduction of innovations in the governance structure (inclusion of non-members and external experts in management bodies, appointment of a professional manager, introduction of proportional voting, depending on the amount of capital invested, etc.), [Bijman, Hanisch, Sangen 2012], internal governance of agricultural production cooperatives [Boevsky, Hanisch, Sagebiel 2012]. These concepts respond to the understanding of the adaptation of agricultural cooperatives to the external environment. They explain deviations between the principles of traditional cooperatives and the requirements of modern governance.

Bulgarian experience shows that sometimes the newly created institutions and forms of organization in agriculture are not successful projects. In the last decade we witnessed globalization, changing market environment, growing competition and reduction of the number of agricultural co-operatives in Bulgaria. According to data from the “Agricultural statistics” Department at the Ministry of Agriculture and Food (MAF), agricultural co-operatives decreased in number. In 2003 they were 1941, in 2010 years – 940 agricultural co-operatives, and in 2013 they were 811. These data show a negative trend in the development and future of the cooperatives. Reasons for this we are looking for in the governance and particular in the governance structure of agricultural co-operatives.

Over the last decade, as a result of increased competition from corporate structures, the agricultural co-operatives are forced to focus on its survival and adequate behavior. We are witnessing the introduction of innovative approaches to the governance of the co-operatives borrowed from corporate business units.

Regarding the governance and particular governance structure of the co-operatives in Bulgaria, there is not a large quantity of literature. Previously explored are strategic management in agriculture, internal and external and organizational strategy [Kopeva 2003], strategic orientation and *innovation potential* [Stoyanova 2010, 2011], where it has close characteristics whit the governance. The focus of research is toward papers regarding diversification of Bulgarian agricultural cooperatives, property rights [Popova 2009], euro integration and economic indicators [Koteva 2009], impact of CAP policy [Kaneva 2015; Bachev 2013], governance of agrarian sustainability [Bachev 2010]. Recent paper on issue is analyzed in the context of sustainable development of farms in the broadest sense [Bachev 2016]. Lately (from 2013), we examine co-operative governance structure, as part of common corporate governance. The focus of their research

is on internal governance of agricultural cooperatives [Sarov 2014], challenges and perspectives to the governance of agricultural co-operatives [Sarov, Boevsky 2016, 2017] innovations in the governance structure of agricultural co-operatives (Sarov 2016, 2017) and other with an emphasis on developmental possibilities, in keeping with the trends in developed countries. The theme is new in Bulgaria, and there is an evident lack of papers exploring governance structure in the agricultural co-operative.

2. OBJECTIVES, RESEARCH QUESTIONS AND HYPOTHESIS

The goal of this paper is the researching of the governance structure of Bulgarian agricultural co-operatives. Based on the underlying theories and concepts, researchers present concepts of cooperative change and modern governance structures.

The co-operative organizations units have to balance interests between owners (members) and managers. However, in practice this often deviates. In other words, we will analyze how different perceptions of both parties for the purposes of the agricultural organization generate conflicts. The analysis gives more explanations on the differences of the objectives of the co-operatives, such as governance structures.

In this context, the focus is to study the innovations in the internal governance that either improve or deteriorate the governance structure. The key issues covered in these case studies are as following:

The study is seeking answers to the following research questions:

- What is the main concept of the essence of co-operatives as governance structure?
- Why managerial bodies change the organization's goals and why they conflict with co-operative members?
- How does the governance structure change?

Therefore, we will test the following working hypothesis in Bulgaria:

H 1: The Increased competition and rapidly changing market environment lead to convergence of the governance structure in the agricultural cooperative with that of the corporation one.

3. METHODOLOGY

The empirical data are the result of case studies and conducted in-depth interviews during the period 2013-2016, and the implemented 32 agricultural co-operatives in Bulgaria. Qualitative research techniques are used. They include Case study, Interview, Analytical Narratives, Observation, Establish of Trust, which are suitable for gaining an understanding of decision-making process. An emphasis was placed on internal governance, institutional environment,

market mechanisms, including management structure, rights of ownership and control, collective action, the importance of governance relationships between the stakeholders, the co-operative values and principles, social role, partnerships, networking. The governance structure of the traditional co-operative is described, then the focus is put on the innovative governance models and embedding new elements in the governance bodies.

According to Theesfeld (2005) the empirical field research is intertwined with the analytical stages in the process. According to Stake (1995) quantitative studies explain and control relationships, while qualitative research wants to understand the complexity of the relationships. The present study aims to analyze the relationships of the different bodies in the governance structures of the agricultural co-operatives. The research strategy involves planning, collection and analysis of data, and reporting the results. These techniques are used simultaneously and when the results are synthesized rich qualitative data can be assembled.

Criticism to the present study may be directed to the point that the presented case studies are not typical cases. In response, the first argument is that in Bulgaria at this stage there is no single methodology for studying governance structures in agricultural co-operatives. The research focused on co-operatives has focused on other criteria. So, every case study is a representation of a new methodological approach to study governance structure in cooperatives. Second, each case study was selected to represent the typical for the region, summarizing the characteristics, traditions and attitudes.

In order to detect the invisible at first sight, unimportant details in connections and relationships of management bodies of co-operatives, the researcher becomes a member of a co-operative. This approach provides comprehensive information on the informal groups in the agricultural cooperative

The focus will be on behavioral processes and logical perceptions. Using of behavioral theory in the study, in some aspects will emerge from the abstract concept of co-operative nature. It will be offered a point of view on the processes and goals of collective action.

4. GOVERNANCE STRUCTURE

The governance structure, as an economic and behavioral category in the governance of the firm, is a concept of evolutionary and wide-ranging character. The institutional economy prevails in the concept that choosing an organizational form is not just a production function, it is also a governance structure. Governance structures can be referred to two groups – traditional and innovative [Georgieva 2013].

According to Williamson (1996), the firm is understood to mean „a model of governance that has an internal governance structure” which „must arise for some reason”. The company is not perceived as an independent business unit, but is always compared to alternative governance models. Other authors [Yin, Zajac 2004] associate the governance structure with organizational design, focus-

ing primarily on decision-making processes. The concept includes the processes of corporate control and incentive allocation. The authors develop the theory of modern understanding of the governance structure of the organization by looking for the answers to the questions: who performs the control; whose interests are represented and who is the beneficiary of the goods.

The researcher team accepted the definition for governance structure of the agricultural co-operative as a peculiar institutional framework between owners and contractors, controlling the activities and governance, including internal and external relations, monitoring and other issues associated with them. The governance structure reflects the own governance mechanisms, as the main goal is to maximize the benefits, strengthen good governance and effective competitiveness [Weiqian 2015].

The internal governance structure is defined as a way of arranging governing bodies; the ongoing relations between them on the one hand and between them and the employees; functions and delegated responsibilities to meet the objectives set. They synchronize the elements of the management system in the organization. The external governance structure includes the interaction and influence of the external environment (institutions, market, and competition). Also, some informal elements such as behavioral characteristics, economic rationality, historical dependence, logical actions, flexibility, adaptability, etc. are also included in the governance structure.

5. ANALYSIS OF THE GOVERNANCE STRUCTURE IN THE AGRICULTURAL CO-OPERATIVES

When dealing to the co-operative organizations as a phenomenon, most researchers, practitioners and policymakers unite over the theoretical formulation that they contribute to economic and social sustainability in the rural areas. Worldwide, dominates the belief of their undeniable contribution to increasing the welfare of their members. Co-operative society has been accepted as a unique business model of functioning democratic mechanism for governance, equality and solidarity. Furthermore, emphasis is placed on the cooperative identity established values and principles.

More than two decades in Bulgaria „agricultural co-operative” is accepted by some and denied by others. The first ones manifest sentiments in the recent past by memories of „the common good of the people” and „equality” among the workers. Those who deny co-operatives highlighted the perception that they have adopted elements of the old, shabby, powerful and unnatural organization form the recent past (TKZS). Currently there is an attempt to be adopted a new and modern style of Bulgarian agricultural co-operative. At the same time, the agricultural corporations are making their appearance and widen their reach to society. They apply modern concepts in marketing management and attract more and more of farmland owners. In addition, goals are clear – maximum profit.

The co-operative and the corporation regarded as business units in agriculture have similar characteristics, but (and) different goals. The governance structure of the agricultural co-operative and the content and determinant corporation are similar: voting rights, income rights, property rights, decision-making hierarchy, governing bodies, established formal relationships between governing bodies as well as between governing bodies and stakeholders (members, officers), influence of the external environment (market, competition), social responsibility. The main differences are related to the objectives, separation of ownership from management and implementation control. In the cooperative, the goal is primarily to support members (users) and meet certain needs. The corporate structure aims to maximize profits for owners (investors). In the co-operative governance structure is a complex set of interdependent elements. Also, farmers have a commitment in terms of transactions and ownership. The attitude to the ongoing transactions is most important because the co-operative was created to provide services to members. Ownership is subject to the relationship to transactions; it is designed to preserve the effectiveness of transactions between the members' holding and the services provided by the cooperative.

The research team outlines the following determinants in the governance structure of agricultural co-operative that will be explored in more detail:

5.1. PROPERTY RIGHTS

The main distinction in property rights between the two organizational forms in agriculture is characterized by the fact that the co-operative ownership rights are collective (all members together), but in the corporation – individual. The collective property in a co-operative implies a non-tradable property right while in the corporation the property right can easily be traded. In the agricultural cooperative there is no differentiation between ownership and management that belongs to the members. The vote is based on “one member – one vote”, i.e. the right to vote is not based on the size of the investment, as in corporations. That is why it is assumed that the co-operative is a union of people, but the corporation – of capital. This element formally determines democracy in the governance of the co-operative. It allocates the right to income, the right to take part in management, the right to decide, the right to control and to implement (Grossman and Hart, 1986). In co-operatives ownership is collective and the ownership of each member is assigned individually. A disadvantage of collective ownership in a cooperative is that it reduces incentives for members to provide additional capital, especially when needed and at risk investment. However, another way of capitalizing investment capital is the possibility of subsidizing the various CAP measures.

5.2. DECISION-MAKING PROCESS

Formally, in the agricultural co-operative, decision-making process is a democratic that is greatly facilitated by the homogeneous nature of membership. This means that members as suppliers and users of agricultural products have equal shares

in the services provided by the co-operative. At the co-operative level, operational decisions are made by bodies, in the person of the Chairman, jointly with the Board of Directors (BD), and then supervised by the Supervisory Committee (SC), who are elected by the members of the co-operative. In cases where important strategic decisions have to be made, the General Assembly is called to vote directly on the strategy. Generally, in the case of collective decision-making, transaction costs are generated: on the one hand, costs related to the process of organizing member conventions themselves, lobbying, membership fees, travel expenses, etc. The columns of “ineffective” solutions include those who serve a certain range of members (coalitions and informal interest groups) and do not contribute to the good of the cooperative as a whole. Member’s cooperative can try to influence decision-making to secure their own interests. The effectiveness of democratic decision-making increases when the members’ homogeneous interests increase. When interests are not homogeneous, the decision-making process is difficult. Decision-making process can be defined as democratic (bottom-up) and autocratic (top-down).

In the corporate structures, therefore, there are usually more different groups and the decision-making process is autocratic. It is delegated to the members of the Board of Directors and the Director (CEO). According to the law, the executive bodies are obliged to work in the interest of the contracting authorities. Shareholders and/or owners exercise control over these decisions. In addition, it is the responsibility of the SC to require at any time information on operational decisions, actions and performances. Thus, heterogeneous investor interests and autocratic decision-making seem stable in the corporate structure.

5.3. CONTROL RIGHTS

In the traditional co-operative, communication channels between members and management are short. Also, according to the law, the meetings of the BD and the chairman must be at least once a month. This means that the necessary discussion and control is formally carried out when discussing strategic and all operational issues. For individual members, there is no difficulty in attending these meetings, even if they are involved in the discussions. Also, the legal framework allows the election of assisting bodies and committees to assist management (in particular, control). Consequently, the influence of members on the policy and activity of the co-operative is significant. In the case of formal separation of ownership (members) from management (as in corporate structures), greater freedom is given to create innovative co-operative organizations. They may also include external experts (non-members) to attend the meetings, which enhances the performance of independent monitoring.

5.4. FORMAL INTERNAL GOVERNANCE STRUCTURE OF CO-OPERATIVE

The agricultural co-operatives in Bulgaria operate on the basis of the governing bodies regulated by the Law on the cooperatives: General Assembly of the

members, Board of Directors, Supervisory Committee, Chairman, other assisting bodies.

The members of the co-operative are participants in the governance structure. They draw the main strands, strategies and choose the governing bodies. This is one of their most important responsibilities – to choose responsible and capable leaders to represent and guide them. In addition, they have the right to receive constant information on the state of the cooperative and the future actions of the governing bodies.

The General Assembly (GA) includes all members of the co-operative. The Chairman shall ensure that the decisions taken reflect the will of the majority of the members. The GA allows members' requests to resolve certain issues to be put to discussion. Often, however, informal interest groups are formed by members who naturally dominate over others. A major advantage of these groups is the high activity at GA meetings and that the set is stronger than the unit. Typically, interest groups have a leader who plays a key role in defining common interests, which in most cases fully reflect the leader's interests. Any member can challenge decisions of the GA by raising a «procedural» issue. The Chairman of the GA should be impartial. As Chairman, he is not entitled to reject or accept proposals alone without proposing them for a vote. When a proposal is received, it must be discussed and voted. The GA decides on the proposal only when a vote is taken by the members.

The main responsibility of the Board of Directors (BD) is to provide the overall management of the co-operative. The role of the BD members is a legal responsibility and trust. The trust means that they have to act in the interest of the member's cooperative, not for themselves. The legal responsibilities mean that they have to lead the organization with care and skill. There is no legal requirement for members of the BD to be experts, but they are required to reasonably apply knowledge and skills so that the cooperative works and is appropriately managed.

The role of the Chairman is to implement the cooperative policy, determined by the members, under the direction of the BD. At the General Meetings, the Chairman is obliged to inform the members about the cooperative's vision for the next year. This is a way of building trust between stakeholders and creating a pleasant atmosphere for working together.

The Chairman must be a professional, possess the necessary knowledge and apply modern innovative methods of work. Basically, his work is based on satisfying the interests of members. This means, for example, the supply of goods and the provision of services at better prices than competitors. The modern and flexible Chairman is the one who succeeds in creating markets, but not only that. It is not only necessary to adapt to changes in the market, and also to change themselves.

The Supervisory Committee is elected by the General Assembly of the member's co-operative. A primary responsibility is to protect the interests of members, as well as to monitoring and controlling all those involved in the organization's activities.

The members of the agricultural co-operative have an additional opportunity to be an active part in the governance structure. Through legally regulated mechanisms, additional governing bodies and committees may be elected. They can carry out preventive activities, such as assisting the SC to protect the co-operative from abuse, to elect committees on social activities. In addition, these committees, to having an assisting, controlling, and social role, also have some informal functions relating to morality and sentiment among the society.

5.5. INFLUENCE OF THE EXTERNAL ENVIRONMENT

The influence of the external environment on the governance structure of the agricultural cooperative is related to the increasing competition and the change in the market dynamics. This means that the main interests of the management are no longer in line with the member's interests. To survive and adapt to the changed, the co-operative is forced to implement approaches and tools borrowed from corporate structures (change in goals, strategy, and vision). Consequently, the new market conditions impose more of management freedom in decisions making process.

As a result of the increasing heterogeneity of the interests and customer orientation of the co-operative, members are forced to strengthen their specific interests in terms of their dealings with the organization. The relationship between of the co-operative members and the exercised control decreases. As a result, new associations have been created, representing their interests with regard to transactions of the co-operative.

6. RESULTS AND DISCUSSION

The case studies present the vision, the state and the main changes of the governance structure in the Bulgarian agricultural co-operatives. The emphasis is on changes in the decision-making process, blurring property rights, the right to control, the distribution of benefits, and the change in goals. Basic information is gathered through the "implemented" case study that is a successful strategy for the researcher to get into the depth of the problems.

Although has been created a well-balanced institutional order, coordination and established democratic systems for monitoring and control. In particular, legal regulations have been created in agricultural co-operatives, which relate to the right of members to participate in the governance, safeguarding property rights, the right to income, the right to use of scrutiny. These indicators are encouraging entrepreneurs to unite in collective action to serve their interests. The study looks for the causes that shape the change in the co-operative governance structure.

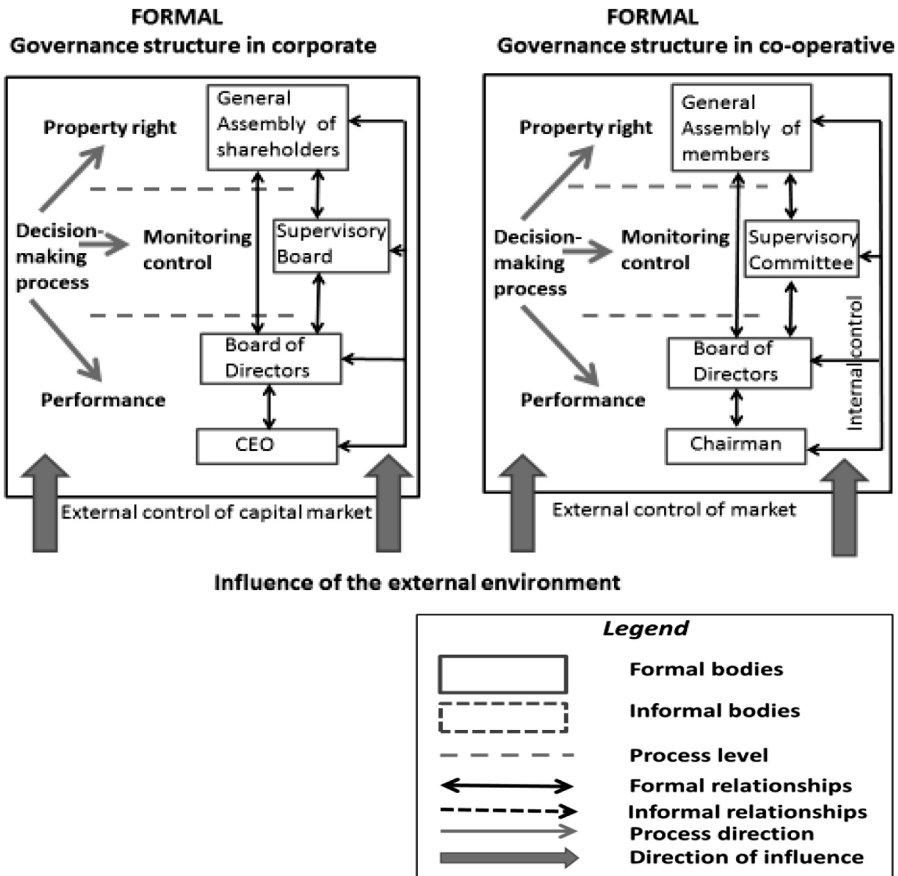
However, in practice results are inconsistent with the theory. The heterogeneity of the entrepreneurial group usually causes trouble finding enough members with sufficient skills and knowledge to be elected to the governing bodies of the co-operative. They fail to balance the interests of owners and cooperation's goals.

In the current conditions of market dynamics, managerial bodies have to learn to “play according to the market rules” and to be more flexible to the dynamic external environment: to produce and sell products and services at competitive prices; to use various management tools and strategies to satisfy the consumers’ needs; a risk management; to trust their partners and avoid the destructive of competition force.

The co-operation as a business units are under strong impact competitive, which requires informal change targets. From supporting businesses of members, managers are focusing on the market, or they are other words, “goals are economized”. Therefore perceptions of the governing bodies to the co-operation doesn’t fully coincide with the goals of the owners.

The co-operative’s members ranked on first place the historical traditions, community, values, communication, and sense of belonging, mutual satisfaction. In practice the two groups (managers and members) operate as an organization, but with different motivations and goals. The difference is in understanding the objectives of the co-operative and the cooperation process.

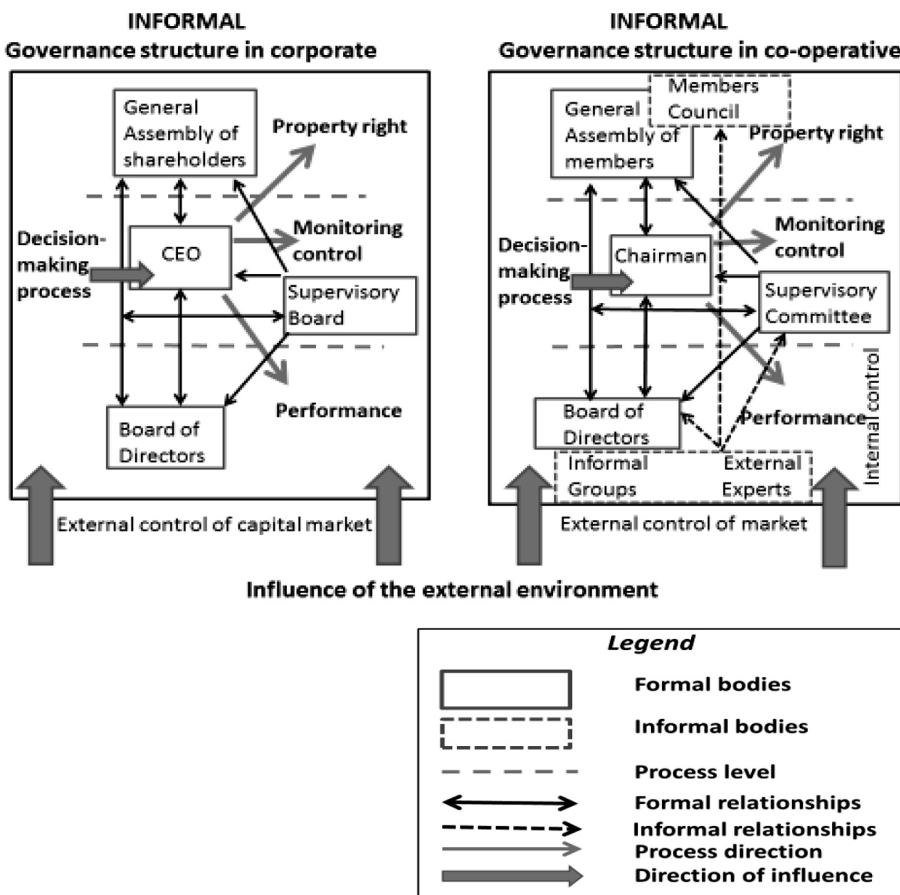
Figure 1. Formal governance structure in corporate and co-operative



Source: own figure.

Figure 1. presents the traditional governance structure in an agricultural co-operative and corporate in Bulgaria. It presents the governance authorities and the relationships between them. The Bulgarian Law on co-operatives regulates the framework and opportunities for change in the governance structure. The survey reported that the greater part of the agricultural co-operatives operate traditionally and have not introduced innovations in their internal and external governance. In them, as we know, the following authorities perform: General Assembly, Board of Directors, Supervisory Committee and Chairman. The internal governance in agricultural co-operatives gives effective control of the users, members, and owners over the decision-making in the cooperative.

Figure 2. Informal governance structure in corporate and co-operative



Source: own figure.

Figure 2. presents the informal model in the governance structure of agricultural cooperatives and corporations. An example of such a body is the Member Council to whom the General Assembly delegates some of its rights. This provides an opportunity to strengthen the control over the co-operative management. Members’

commitment to their cooperatives is strongly influenced by their participation in the governance. The reason for the creation of the Council is the need for taking urgent solutions. Their number is usually up to 10 members who have representation over the other members. We know that the major problem in agricultural co-operatives is the low involvement of members in decisions-making.

The Chairman imposes an authoritarian (“top-down”) decision-making and changes the formal governance structure. The explanation for this action is in his strong desire and desire to centralize the distribution of information channels and to exercise sole power resources seized by the BD and the SC. The members increasingly lose confidence in the democratic governance. A testimony to this is that it is the President who impose his own opinion on the other members in the decision-making process

The agricultural co-operatives in Bulgaria involve new formal and informal bodies which support innovation of governance structure. The study identified supporting informal groups that have come together in support of the Board of Directors and Supervisory Committee. Usually these members have homogeneous interests. Often these informal interest groups put pressure and influence other members over decisions-making process. The existence of more such groups makes more difficult to combine the common interests of the co-operative. The in-depth interviews revealed that members accept these positive innovations in the governance structure, since as they contribute to increasing competitiveness.

Also, co-operatives invite experts for assisting and improving the management. This is a step towards professionalization of the governance and stronger customer focus. The study identifies the involvement of professional managers largely took over the functions of the Chairman of the cooperative. In this way the Chairman has more representative functions, and operational functions are implemented by the professional managers. They use modern management techniques and tools, motivation, to achieve the defined financial goals. The results indicate that in the agricultural co-operatives in Bulgaria the economic goals dominate over the social ones. As we said in the beginning, the competition is one of the reasons for the introduction of innovations in governance structures in co-operatives. This confirms the hypothesis that the governance structure in the agriculture cooperative is getting increasingly closer to the structure in the corporate one.

The innovations in the governance structures of agricultural co-operatives in Bulgaria are in line with the legal framework and in compliance with the co-operative values and principles. Co-operatives need their members to engage more in efficient operations and to participate in the governance. It should be stressed that these principles of the co-operatives would change depending on changes in the market environment, which means that they are not constant. We can expect in the future regulated change of co-operatives values and principles.

7. CONCLUSIONS

Over the last decade, Bulgarian agricultural cooperatives have faced the challenges of the external environment (political, institutional, social, market), which forces them to increasingly focus on external consumers and to change their goals.

The competition has a significant impact on the development of agricultural co-operatives. Many politicians, economists, scientists and practitioners fear that cooperatives lose their typical characteristics – values and principles. Statistic dates indicate that co-operatives are no longer the main players in market activity. At the same time, co-operatives are under the influence of market conditions. Evidence of this is their hybrid form – co-operatives are growing horizontally. Examples are some agricultural consumer and credit co-operatives, which are becoming corporate companies. Consequently, the distinction between co-operatives and corporations will be increasingly difficult.

As a result of the reported deviations from the legal framework, the in-depth study highlighted the need for new informal assisting bodies of the governance structure in the Bulgarian agricultural cooperatives – Members Council, informal interest groups, attracting external experts. Loss of trust from members to management leads to their leaving the cooperative and directing them to corporate structures.

Therefore, the conducted analysis has confirmed the working hypothesis: *The Increased competition and rapidly changing market environment lead to convergence of the governance structure in the agricultural cooperative with that of the corporation one.*

Enhanced competition alters the orientation and objectives of the cooperative, which are already connected with the realization of higher profits and transactions with non-members (as in the corporation). Governance is “professionalized”; a process of “economizing” takes place.

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