

---

# Ownership structure and composition of boards of directors: evidence on Brazilian publicly-traded companies

---

Eduardo Schiehl  
Igor Oliveira dos Santos

## RESUMO

### Estrutura do controle acionário e composição do conselho de administração: evidência sobre empresas brasileiras de capital aberto

O objetivo neste estudo é fornecer evidências preliminares sobre a estrutura do controle acionário e a composição do Conselho de Administração das empresas listadas na Bolsa de Valores de São Paulo (Bovespa). Os atributos do Conselho de Administração investigados junto com a estrutura do controle acionário das empresas são o tamanho do Conselho de Administração, a proporção de *outsiders* e a dualidade do diretor-presidente. Constatou-se que o capital votante e o capital total das empresas listadas na Bovespa ainda são bastante concentrados, sugerindo que a separação do controle acionário e do controle de decisão não é a questão de agência mais relevante. Essa evidência também sugere que, em geral, o Conselho de Administração das empresas listadas na Bovespa é predominantemente composto por acionistas majoritários e por executivos dessas empresas. Isso suporta o argumento de que conflitos de interesse entre acionistas minoritários e majoritários podem existir, assim como oportunidades para a expropriação de acionistas minoritários pelos controladores e/ou executivos. Ainda nesse sentido, documentou-se que a proporção de *outsiders* no Conselho de Administração é menor entre empresas possuindo um acionista controlador na estrutura de capital social. Essa evidência suporta o argumento de que a independência do Conselho de Administração é inversamente relacionada com a concentração do controle acionário das empresas. Além disso, constatou-se número menor de membros do Conselho de Administração na amostra brasileira, se comparado a outras amostras de companhias abertas dos Estados Unidos e do Canadá. Por fim, documentou-se uma incidência significativamente menor de dualidade do diretor-presidente nessa amostra, se comparada a outras amostras semelhantes de companhias negociadas nos Estados Unidos e no Canadá.

**Palavras-chave:** governança corporativa, estrutura do controle acionário, conselho de administração.

Os autores agradecem ao suporte financeiro da *Chair in Governance and Forensic Accounting, HEC Montréal*, e do *Social Sciences and Humanities Research Council of Canada*.

Recebido em 14/abril/2004  
Aprovado em 04/novembro/2004

---

Eduardo Schiehl, MSc e PhD, é Professor Assistente de Contabilidade na *HEC Montréal*, escola afiliada à *Université de Montréal*, Montréal, Québec, Canada (Canada H3T 2A7).  
E-mail: eduardo.schiehl@hec.ca  
Endereço:  
HEC Montréal  
3000, chemin de la Côte-Sainte-Catherine  
Montréal (Québec)  
Canada H3T 2A7

Igor Oliveira dos Santos é Mestrando em Gestão Internacional na *HEC Montréal*, escola afiliada à *Université de Montréal*, Montréal, Québec, Canada (Canada H3T 2A7).  
E-mail: igor.oliveira-dos-santos@hec.ca

## 1. INTRODUCTION

Considerable attention has been devoted in both the academic literature and the business press to the impact of governance structure on firm valuation. Investors associate specific governance conditions such as ownership structure, composition of the board of directors and executive compensation plans with the optimal use of the firm's resources and lower agency costs, which lead to better performance and higher stock prices. Investors also perceive effective governance as a means of reducing investment risk, since they believe it decreases the likelihood of unfortunate events befalling the company (BUCHHOLTZ, YOUNG and POWELL, 1998; CONYON and PECK, 1998; COLES, McWILLIAMS and SEN, 2001).

Corporate governance differs significantly across countries due to variations in political and legal constraints on the ownership and control of public companies. Government regulations affect the ways companies are owned (stock exchange rules), the manner in which they are controlled (legal structures), and the processes by which changes in ownership and control take place (takeover codes) (WEIMER and PAPE, 1999; GIBSON, 2003). These regulations have a direct influence on two important factors affecting corporate governance and control: the structure of corporate ownership and the structure of corporate boards. In Brazil, for example, the 1976 Corporate Law enables groups or individuals holding relatively small amounts of a firm's capital to exercise control, mainly through a system of dual shares. Ordinary shares come with voting rights, while preferred shares do not. Only ordinary shareholders may vote on the appointment of directors to the firm's board. The method of electing the directors therefore reinforces the dominance of ordinary shareholders, although the minority (of voting shares) is entitled to one seat on the board through multiple voting.

Consistent with the governance literature, this study takes the perspective that the board of directors is the primary mechanism for achieving top-level separation of the decision management and control functions in public companies. The board delegates decision management functions and many decision control functions to internal agents (managers), while retaining ultimate control over these agents through the right to ratify and monitor key decisions and the right to appoint, dismiss and determine the compensation of managers. In short, the board of directors holds the ultimate responsibility for ensuring that the firm is run in the best interest of all stockholders. Following this line of reasoning, this study uses agency theory to examine ownership structure and the composition of the board of directors of Brazilian publicly-traded companies. In particular, this study examines whether the firm's ownership structure is associated with three dimensions of the board of directors, namely board size, percentage of outside directors on the board and CEO duality.

This study documents that voting privileges and the total capital of Brazilian publicly-traded companies remain strongly

concentrated, suggesting that the separation of ownership and decision control is not the most important agency issue. On the other hand, the data suggests that controlling shareholders in Brazilian public companies are very likely to be executives or directors of the corporation. This implies a greater potential for conflict and the expropriation of minority shareholders by these controlling shareholders. This findings also suggest that the proportion of outside directors on the board is lower among firms having a single controlling shareholder in the ownership structure. This is consistent with the argument that board independence is inversely related to the firm's ownership concentration. In addition, the data documents that the number of directors on the board in this sample is smaller than in comparable samples of publicly-traded companies from the United States and Canada. Surprisingly, the incidence of CEO duality in this sample is significantly smaller than in similar samples of public companies from the United States and Canada.

The organization of the remainder of this paper is as follows. Section two presents the theoretical governance framework used to examine the proposed associations between the firms' ownership structures and attributes of their boards of directors. Section three describes the sample and the variables used in the investigation. Sections four and five present the discussion and the findings on the ownership structure and board composition in this sample of Brazilian publicly-traded companies. Finally, conclusions and suggested avenues for further research are presented in section six.

## 2. CORPORATE GOVERNANCE

Evidence for the association between governance structure and firm performance is found throughout the agency literature in finance, accounting and management research. The agency relationship has been described as a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf that involves delegating some decision-making authority to the agent (JENSEN and MECKLING, 1976). Essentially, agency theorists predict that the separation of ownership and control increases the potential for opportunism on the part of a manager, and makes it critical that organizations design mechanisms to limit such possibilities. In short, the agency literature advocates that when the interests of principals and agents are not aligned, conflicts of interest arise, and control mechanisms become an important factor to explain firm performance. The agency research has therefore focused on designing corporate governance structures that motivate managers to make performance-enhancing choices that in turn maximize shareholder value (BARKEMA and GOMEZ-MEJIA, 1998; COLES, McWILLIAMS and SEN, 2001).

Differences in corporate governance across countries appear to be the result of variations in corporate organizational structure, particularly the ownership structure and composi-

tion of the board of directors. Corporate governance in Brazil, for example, follows an *insider* model rather than the Anglo-Saxon approach, where capital markets act to discipline management. Brazil is also distinct from other countries such as Germany, where the banking sector plays an important role in the governance of companies (LEAL and DE OLIVEIRA, 2002; WEIMER and PAPE, 1999). Given the concentrated ownership structure of Brazilian public companies, it follows that the separation of management from ownership is not the most important agency issue in Brazil. The most crucial issue would be how to offer protection to minority shareholders. In this respect, the study by *Instituto Brasileiro de Governança Corporativa* (IBGC, 1998) finds no evidence of any influence of minority shareholders over board composition or the decision-making process. According to the IBGC (1998), for example, 48.7% of companies have their directors appointed by shareholders, 17.9% by their CEO and only 2% by an independent minority group. In addition, the presence of large shareholders as well as family owners is greater in Brazil than in the United States (CORE, HOLTHAUSEN and LARCKER, 1999; LEAL and DE OLIVEIRA, 2002). In contrast to United State public firms, where all shares have similar voting privileges, Brazilian public firms are allowed to have dual class shares. Thus, the combination of dual class shares and pyramids allows the dominant shareholders of the business group, who are very often the founding family, to control the firm with only a small percentage of the total capital. This situation offers an interesting opportunity to examine the issue of ownership structure and its relation to board composition. There exists a high potential for conflict and expropriation of minority shareholders by controlling shareholders, which may prevent boards of directors from acting effectively in Brazilian public companies. Following this line of reasoning, the purpose of this study is to document descriptive and preliminary evidence on the association between ownership structure and the composition of board of directors in Brazilian public firms. The next section describes the data used in this study.

### 3. DATA

The database for this study was developed from a single main source: the São Paulo Stock Exchange (Bovespa). As such, the starting point was represented by a set of 405 Brazilian publicly-traded companies listed at the Bovespa in December 2002. Companies pertaining to the financial institutions and the natural resources exploitation sectors were excluded in the first round, leaving a list of 284 companies. Three companies were then eliminated since they were no longer listed on the São Paulo Stock Exchange (Bovespa) on February 2004, period when the governance data was collected. A further 41 companies were discarded because they had incomplete information on either the members of the board or their main shareholders. The final database therefore consists of 240 listed com-

panies from 71 different industrial segments<sup>(1)</sup>. Table 1 below presents the distribution of the sample along the industrial segments.

**Table 1**

***Distribution of Main Segments and Percentage of Total Sample***

Industry Category	Number of Firms	Percentage of Total Sample
Diversified holding companies	42	17.50
Telecommunications	21	8.75
Metallurgy	18	7.50
Textiles	18	7.50
Steel	12	4.00
Petrochemical, Plastics & Rubber	8	3.33
Auto parts	8	3.33
Pulp and Paper	6	2.50
Civil Construction	5	2.08
Food	8	3.33
Air Transportation	3	1.25
Ceramics, Glass & Crystal	3	1.25
Chemical Products — Miscellaneous	3	1.25
Construction & Engineering	6	2.50
Department Stores	3	1.25
Fertilizers, Manure & Agricultural Defensives	3	1.25
Household Appliances	3	1.25
Oil Prospecting and Refining	3	1.25
Real Estate	3	1.25
Other industries with less than three companies	64	
<b>Total Sample</b>	<b>240</b>	

From the Bovespa database ([www.bovespa.com.br](http://www.bovespa.com.br)) governance data was collected for each company in the sample. More specifically, the data collection focused on companies' boards of directors, capital structure and the identity of majority shareholders. The data collected from *Grupo 2 — Administração — Quadro 01-Composição Atual Conselho de Administração*, about a company's board of directors, were basically: the number of directors on the board, their names and respective positions in the company and its board. Based on this information the variables board size, proportion of outsiders on the board and CEO duality were measured. The equity data gathered from a spreadsheet available at the Bovespa's website were essentially related to the book value of each listed company's equity. The shareholder data collected from *Grupo 3 —*

*Distribuição do Capital — 02-Posição Acionária* were percentages of voting capital and total capital. All these data were used as the main elements for the analyses presented in this paper.

#### 4. OWNERSHIP STRUCTURE

According to the traditional agency literature, the more concentrated the firm's ownership structure, the more the agency costs and economic benefits of monitoring increase to shareholders (JENSEN and MECKLING, 1976; DEMSETZ and LEHN, 1985). The premise is that large shareholders tend to engage in closer monitoring activities, which reduces informational asymmetries between owners and managers as well as between the firm and external investors. However, the ability of large shareholders to impact firm governance and performance may depend on their identity. Inside control by shareholders, or owner management, may represent a higher degree of control at any given level of shareholding than the control provided by outsiders (LEHMANN and WEIGAND, 2000; SCHULZE *et al.*, 2001; GIBSON, 2003). From this perspective, one may suggest that family relations tend to make agency problems associated with private ownership and owner management more difficult to resolve, due to self-regulation and problems engendered by altruism. In other words, controlling shareholders combined with owner management may collude

to keep minority shareholders at bay, starting with the composition of the board of directors.

This study focuses on direct ownership and control, measured by the proportion of voting shares held directly by a single shareholder or a small group of shareholders. Following this line of reasoning, firms in this sample were classified into two groups. The **firms with a majority shareholder** have a single shareholder, person or institution directly owning more than 50% of the firm's voting equity shares. The second group, **firms without a majority shareholder**, includes firms in which no single shareholder directly owns more than 50% percent of the firm's voting shares<sup>(2)</sup>. Tables 2 and 3 present some descriptive statistics (means and medians) on the ownership structures of companies in the sample as of the end of fiscal year end 2002. Specifically, table 2 presents the percentage means and medians of outstanding shares directly owned by a single large shareholder, the three largest shareholders and the five largest shareholders. For comparison purposes, table 2 is presented in the same format as used in the study by Leal, Da Silva and Valadares (2002), which presents ownership data for a similar sample of Brazilian public firms as at of the end of fiscal year 1998. This comparison sheds light on whether changes have occurred in the capital structures of Brazilian public companies since 1998.

Table 2 shows that 70% (167) of the firms in the sample have a majority shareholder, while 30% (73) do not. These proportions are similar to those in the sample studied by Leal,

**Table 2**  
**Percentage of Directly Owned Shares**

	Companies With a Majority Shareholder (167)		Companies Without a Majority Shareholder (73)		Total (240)	
	Voting Capital	Total Capital	Voting Capital	Total Capital	Voting Capital	Total Capital
	(%)	(%)	(%)	(%)	(%)	(%)
Largest Shareholder	72.12	55.85	31.85	25.65	59.87	46.67
Median	72.71	53.00	30.87	22.85	59.14	44.30
Three Largest Shareholders	85.38	68.43	62.15	49.19	78.32	62.58
Median	93.66	70.05	63.31	48.04	87.42	61.51
Five Largest Shareholders	86.10	69.65	70.35	56.16	81.31	65.55
Median	94.01	74.22	73.13	55.86	88.93	66.71

**Table 3**  
**Number of Companies Without a Majority Shareholder (73) by Level of Ownership (Voting Capital)**

	0 – 5%	5% – 10%	10% – 20%	20% – 30%	30% – 40%	40% – 50%
Largest Shareholder	1	0	10	24	18	20
Three Largest Shareholders	1	0	1	2	5	64
Five Largest Shareholders	1	0	1	1	3	67

Da Silva and Valadares (2002). In the group of firms with a majority shareholder, the average percentage of the voting (total) capital owned by the largest shareholder is 72% (55%), while the voting (total) capital owned in the group of three and five largest shareholders is 85% (68%) and 86% (70%), respectively. Overall, these statistics document that the ownership structure of Brazilian public firms has not changed significantly since 1998 and remains highly concentrated.

In the group of firms without a single majority shareholder, the average ownership by the largest shareholder is 31% (25%) of the voting (total) capital. This is similar to the levels found by Leal, Da Silva and Valadares (2002). However, some significant changes can be observed here with regard to ownership level in the groups of three and five largest shareholders. In this respect, table 2 documents that the group with the three largest shareholders owns 62% (49%), on average, of the voting (total) capital, while the group with the five largest shareholders owns 70% (56%), on average, of the firm's voting (total) capital. Comparing ownership levels in the groups with three and five largest shareholders between 1998<sup>(3)</sup> and 2002, a slight reduction is observed in voting capital ownership and, at the same time, an increase in the ownership of total capital in both groups. These variations may provide evidence that privatization and the inflow of foreign investment have begun to change the equity structures of Brazilian publicly-traded companies. Although not reported in this paper, there is also evidence that foreign investors took control of some large Brazilian companies in the 1997 privatization process. In order to take advantage of the capitalization opportunities offered by privatization, private family-controlled companies appear to have begun adjusting their capital structures to a more competitive environment.

The objective of table 3 is to analyze the ownership concentration of the group of Brazilian publicly-traded companies without a single majority shareholder (N = 73). As such, table 3 classifies companies in this group per different levels of ownership of the voting capital. Such classification is done according to the voting capital owned by companies' largest shareholder, the group of three largest shareholders, and the group of five largest shareholders. The results in table 3 show that voting capital in the group of firms without a single majority shareholder tends to be concentrated in the hands of a few shareholders. For example, the first column of table 3 reports that only one company out of 73 does not have a single shareholder holding more than 5% of the voting capital. In fact, 42<sup>(4)</sup> out of 73 companies (85%) without a majority shareholder have at least one shareholder holding more than 20% of the voting capital. Moreover, 64 out of 73 companies (87%) without a single majority shareholder have a group of three shareholders holding more than 40% of the voting capital. Finally, looking at the ownership level of companies' five largest shareholders this number increases to 67 companies, which means that 91% of companies without a single majority share-

holder have more than 40% of their voting capital held by a group of five shareholders. Further analysis in the data also indicates that very often these five shareholders have family links<sup>(5)</sup>. In sum, the data reported in tables 2 and 3 provides significant evidence that the ownership structures of Brazilian publicly-traded companies are strongly concentrated, and corporate governance thereby follows the insider model, where the separation of ownership and decision control is not the most important agency issue. Although controlling shareholders ultimately appoint the management, this data also provide evidence that controlling shareholders in Brazilian public companies are likely to be executives or directors of the corporation. This implies that a controlling shareholder who is an executive or director (or both) may derive either pecuniary or non-pecuniary benefits from occupying the position of executive/director, and may wish to retain control in order to maintain the flow of these benefits, which are not shared by minority shareholders. These findings provide evidence of potential agency problems in closely-held firms, involving what financial economists<sup>(6)</sup> term entrenchment of dominant shareholders. The entrenchment perspective predicts that large shareholdings by management or founders often enable them to dominate shareholder meetings and control director appointments, and thus directly or indirectly control the firm's decision-making process. The result is a decrease in the firm's value due to potential conflicts of interest between minority outside shareholders and large inside shareholders looking to extract private benefits from the firm. In such a context, the most crucial issue is how to offer protection to minority shareholders. Assuming that the board of directors is the primary mechanism for achieving the effective monitoring of management decision-making, next section analyzes the corporate board attributes in the sample of Brazilian publicly-traded companies.

## 5. THE BOARD OF DIRECTORS

As mentioned above, the distribution of power among corporate managers, shareholders and directors is established when shareholders nominate a board of directors to represent and protect their interests and to ensure that executives duly assume their responsibilities. As such, the proposed relationship between the board of directors and the firm's ownership structure emerges from the issue of the separation of ownership and control. The literature suggests that the more concentrated the firm's ownership structure, the greater the degree to which agency costs and the economic benefits of monitoring increase to the same shareholder (JENSEN and MECKLING, 1976; FAMA, 1980). For example, when ownership is concentrated, the large shareholder can effectively monitor the management, sometimes by personally sitting on the board and/or influencing the appointment of members of the board of directors. This leads one to expect that ownership concentration and the control of voting privileges have an impact on the following board

attributes: board size, percentage of outside directors and CEO duality (table 4). Focusing on such board attributes, the following paragraphs analyze the governance data of this sample of Brazilian publicly-traded companies.

**5.1. Board size**

The debate on board size and its influence on the effectiveness of board monitoring suggests that large boards bring a diversity of competences and experiences, increase opportunities for broad geographic representation and provide extensive director resources to allow board committees to deal effectively with complex issues. Beyond a certain threshold of board size, however, information flow and decision-making could become more difficult and cumbersome, and the directors might lose their sense of responsibility and accountability. Prior research is not conclusive as to whether board size has a positive or negative effect on the effectiveness of governance in public firms. A small board serves to control managers, whereas a larger board may not function effectively as a controlling body, leaving management freer to act. However, a larger board may be more valuable for the breadth of its services (CORE, HOLTHAUSEN and LARCKER, 1999; COLES, McWILLIAMS and SEN, 2001; ANDRÉ and SCHIEHL, 2004).

Table 4, Panel A, shows no difference between the average number of directors of companies with a majority shareholder (6.06 directors) and companies without a majority shareholder (6.85 directors). The maximum number of directors in both groups is 16, and it applies to Net Serviços de Comunicação S.A. and Tele Norte Leste Participações S.A. (see table 7 for details). Surprisingly, table 5 documents that 106 (44%) companies in the sample have fewer than five directors on the board. Also, table 5 shows that board size tends to be positively associated with the firm’s equity size. At the same time, it also suggests that board size in this sample of Brazilian companies is relatively small, compared to publicly-traded companies in the United States and Canada, where the average number of directors on the board is 9.25 and 9.87, respectively (KORN/FERRY INTERNATIONAL, 2004). These findings are consistent with the argument that ownership and voting concentration negatively impacts board size (COLES, McWILLIAMS and SEN, 2001). Nevertheless, the empirical issue remains whether ownership concentration affects board size because it reduces the complexity of monitoring management decisions or because ownership concentration is a sign of the potential entrenchment of inside controlling shareholders.

Along the same line, table 6 shows the average number of directors on the board for the ten largest industry groups in the

**Table 4**  
**Cross Classification of Companies by Ownership Structure and Board Composition (Board Size, Proportion of Outsiders and CEO as Chairman)**

		Companies With a Controlling Shareholder (167)	Companies Without a Controlling Shareholder (73)	Total Sample (240)
<b>Panel A</b>				
Board Size	Mean	6.06	6.85	6.30
	Minimum	2	3	2
	Maximum	16	16	16
Number of Companies With	00-05 directors	80	26	106
	06-10 directors	72	39	111
	11-16 directors	15	8	23
<b>Panel B</b>				
Outsiders	Average percentage	77.07	79.32	77.75
	less than 10%	0	1	1
	10% – 50%	16	4	20
	50% – 60%	8	1	9
	60% – 70%	49	19	68
	70% – 80%	32	15	47
	80% – 90%	18	12	30
	greater than 90%	44	21	65
<b>Panel C</b>				
CEO as Chairman		65	24	89

Table 5

## Cross Classification of Companies by Board Size and Total Value of Equity

Number of Directors	Social Capital (In Millions of Brazilian Reais)					Total
	Less Than 50	50 – 100	100 – 250	250 – 500	More Than 500	
05 or Less	53	18	19	8	8	106
06 – 09	20	17	22	14	26	99
10 – 12	4	3	5	7	6	25
13 – 15	0	2	1	0	5	8
16 – 19	0	0	0	0	2	2
20 or More	0	0	0	0	0	0

Table 6

## Average Board Size for the Ten Largest Industrial Sectors

Industry Category	Number of Firms	Average Board Size
Diversified holding companies	42	6.45
Telecommunications	21	7.43
Textiles	18	6.28
Metallurgy	18	5.56
Steel	9	8.33
Petrochemical, Plastics & Rubber	8	8.00
Auto parts	6	5.33
Pulp and Paper	6	7.33
Food	5	4.60
Civil Construction	5	5.60

sample. In this respect, table 6 documents that companies in the steel, petrochemical and telecommunications industries have the largest boards: 8.33, 8.00 and 7.43 directors on average, respectively. This may be explained by the fact that these sub-groups are all capital-intensive industries and that board size continues to be a function of asset size. The argument is that the larger the company, the greater its potential growth opportunities and agency cost, and the more complex its governance conditions. Moreover, these industry groups also have the lowest average proportion of voting capital owned by a single shareholder. Hence, these findings may suggest that the relatively lower levels of ownership concentration and the use of debt financing tend to positively impact board size by representing a more diversified group of stakeholders on the board.

## 5.2. Outside directors

An important attribute of board composition is the distribution of members according to their primary allegiance, which

Table 7

## Largest Boards

Number of Directors	Company	Industry Category
16	Net Serviços de Comunicação S.A.	Diversified holding companies
	Tele Norte Leste Participações S.A.	Telecommunications
15	Bunge Brasil S.A.	Diversified holding companies
14	Inepar S.A. Indústria e Construções	Heavy Construction
	Embraer-Empresa Bras. de Aeronáutica S.A.	Aircraft Material
	Tekno S.A. Construções Ind. e Com.	Metallurgy
	Politeno Indústria e Comércio S.A.	Petrochemical, Plastics & Rubber
	Ferrovias Centro-Atlântica S.A.	Transportation
13	Cia. Vale do Rio Doce	Minerals — Miscellaneous
	Cia. Fiação Tecidos Cedro Cachoeira	Textiles

may be either to shareholders (outside) or managers (inside). In this respect, the governance literature suggests that an inside director, either a top executive or important stakeholder, may not support the same value-creation strategy as an outside director<sup>(7)</sup>. Outside directors are considered professional referees who unbiasedly assess the performance of managers, determine their remuneration and replace them if necessary (BARKEMA and GOMEZ-MEJIA, 1998). Thus, the board's effectiveness in monitoring the actions of managers is assumed to be a positive function of its proportion of outside, unrelated directors (GAGNON and St-PIERRE, 1995; CORE, HOLTHAUSEN and LARCKER, 1999).

In view of the demand for decision-making expertise, coupled with the requirement for detailed firm-specific knowledge, it is natural for boards to contain senior managers from within the organization. However, as discussed above, the inclusion of inside board members leads to conflicts with the decision control function of the board of directors. Along this line, recent research also suggests that high levels of managerial stock ownership can be costly to other stockholders (ANDRÉ and SCHIEHLL, 2004). For example, owner-managers may lack the managerial skills required to maximize the value of the firm. They may also have incentives to make value-reducing decisions at the expense of minority stockholders. Such incentives can arise from the undiversified nature of human and financial capital that may lead to wealth-decreasing diversification and the avoidance of opportunities that are perceived as risky. They can also arise from the power that owner-managers have to expropriate wealth from minority stockholders by paying themselves excessive salaries, negotiating deals with other companies that they control, withdrawing corporate funds, consuming perquisites or borrowing from the firm at below market interest rates. These agency problems are likely to be further compounded by the reduced discipline to which owner-managers firms are subject in the market for managerial labor and corporate control. As such, firms with ownership concentration and/or owner-management should attempt to provide credible signals to outside investors concerning entrenchment-related behavior. The proportion of outside directors on the board is one such governance attributes.

As documented in table 4, Panel B, the average percentage of outside directors on the board is slightly greater in the group of firms without a majority shareholder in their ownership structure. The difference in the proportion of outside directors on the board between the group of firms with and without a majority shareholder is greater when the data is analyzed by levels of outside directors. For example, table 4, Panel B, documents that the proportion of firms having a percentage of outside directors greater than 60%, or a majority, is significantly greater in the subgroup of firms without majority shareholders. As expected, the findings are consistent with the argument that board independence is inversely related to the firm's ownership concentration. In addition, as documented in table 3,

the group of companies without a majority shareholder also has ownership structure concentrated in the hands of few shareholders. Hence, the relatively lower percentage of outside directors in this sample of Brazilian companies may be explained by the fact that large controlling shareholders tend to participate in and/or appoint family members to the firm's board and management, thereby negatively affecting board independence. A further analysis of the relative independence of the board of directors would benefit from establishing whether the majority shareholder is a founding family, an industrial company or a financial institution. In this respect, previous research on this issue has already provided evidence that the impact of large shareholders on board composition and firm performance depends on their fiduciary responsibilities (ANDRÉ and SCHIEHLL, 2004)<sup>(8)</sup>. Moreover, one may raise the question of whether an outside director can be an effective monitor when serving on boards dominated by large shareholders, such as in this Brazilian sample. In a context of ownership concentration, one may argue that outside directors lack independence because, despite their impartial status and ability to offer advice on some decisions, outside directors have little influence over decisions involving family members and other large shareholder matters. Second, the tendency of large shareholders to appoint to their boards outside directors who are close friends and/or happen to have a fiduciary relationship with the firm may compromise the outside directors' independence and monitoring efforts.

### 5.3. CEO duality

CEO duality is characterized by firms that have combined the positions of CEO and Chairman of the Board of Directors. This dual function has been criticized as an inappropriate way to define one of the most critical power relationships in publicly-traded firms (COLES, McWILLIAMS and SEN, 2001). This view asserts that CEO's who are also board chairs have a concentrated power base that permits decision-making in their own self-interest and at the expense of shareholders. Along this line, proponents of separating the positions of CEO and Chairman of the Board argue that the ability of the board to monitor independently and effectively tends to be compromised when the CEO is also the Chairman of the Board. The governance literature suggests that separating the CEO and Chairman positions tends to improve the decision-making process and the overall governance of the firm in several ways. First, the relationship between the board of directors (the overseer of management) and management is clarified. Second, having independent leadership improves the board's effectiveness and organization. Third, the board's responsibility to look after shareholders' interests moves to the forefront. In contrast, combining the CEO/Chairman position (CEO duality) may have some compensatory advantages. For example, a combined CEO/Chairman role would enhance the information flow be-

tween the board and management and improve co-operation and co-ordination between the two bodies.

As expected, table 4, Panel C, documents that in this sample of Brazilian publicly-traded companies the proportion of companies combining the positions of CEO and Chairman of the Board is significantly higher in the subgroup of firms with a majority shareholder (65 out of 167 firms or 39%) than in the subgroup of firms without a majority shareholder (24 out of 73 firms or 32%). This result suggests that ownership concentration also leads to power concentration in the hands of the same executive, who is probably (or related to) the majority shareholder.

The results documented in table 4, Panel C, seem to indicate that the incidence of a combined leadership structure (CEO duality) in this Brazilian sample of publicly-traded companies is smaller (37%)<sup>(9)</sup> than those of the United States or Canada. In similar samples of United States and Canadian public firms, the incidence of CEO duality is somewhere between 60% and 70% (see for example, GAGNON and St-PIERRE, 1995; CORE, HOLTHAUSEN and LARCKER, 1999; ANDRÉ and SCHIEHL, 2004). Three competing arguments may explain the lower incidence of CEO duality in this sample, which might constitute a subject for further research. One possible explanation is that increasing concern with appropriate managerial monitoring has led to the widespread adoption of a separate leadership structure in Brazilian publicly-traded companies. On the other hand, one may argue that the impact of CEO duality is closely related to the use of alternate governance mechanisms such as the proportion of outside directors, governance and compensation board committees, and executive performance-contingent compensation. The use of such alternative governance mechanisms appears to be greater in the United States and Canada, and may compensate for the negative impact of a combined leadership structure. Finally, a third possible explanation is that in some companies of this sample where duality was not identified, the positions of CEO and Chairman of the Board are held by two people with family links. This might be possible given the ownership structure and high level of family ownership in this sample<sup>(10)</sup> of Brazilian publicly-traded companies. Such situation leads to an equivalent power concentration than CEO duality. In fact, further data analysis based on the names of the board members seems to partially support this argument. For example, in 21<sup>(11)</sup> out of 102 companies among the group with a controlling shareholder and without CEO duality (table 4, Panel C / N = 167 — 65 = 102), the CEO and the Chairman of the Board belong to the same family. Similarly, in 9<sup>(12)</sup> out of 49 companies among the group without a controlling shareholder and without CEO duality (table 4, Panel C / N = 73 — 24 = 49), the CEO and the Chairman of the Board have family links. Considering these companies the overall level of CEO duality in this sample increases to about 50%. This finding has an implication for further research. The measurement of CEO duality or power concentra-

tion should also take into account situations where CEO and Chairman of the Board are members of the same family links.

## 6. CONCLUSION

This study provides preliminary descriptive evidence on the ownership structure and composition of boards of directors in Brazilian publicly traded companies. The attributes of the boards of directors and ownership structures investigated include board size, proportion of outside directors and CEO duality. The study focused on Brazilian public firms because of the greater presence of large shareholders as well as family members in the ownership structure, and because very little evidence is found in the literature on the use of governance mechanisms in the Brazilian capital market.

This study's descriptive and preliminary evidence on ownership structure and board composition provides several contributions to the governance literature on Brazilian companies. The findings regarding the ownership structure of Brazilian publicly-traded companies as of the end of 2002 suggest that the voting privileges and total capital of Brazilian publicly-traded companies remain strongly concentrated. Corporate governance in Brazil appears to follow the insider model, where the separation of ownership and decision control is not the most important agency issue. In contrast, the data suggest that controlling shareholders in Brazilian public companies are very likely to be executives or directors of the corporation. This implies that a controlling shareholder who is an executive or director (or both) may derive either pecuniary or non-pecuniary benefits from occupying the position of executive/director, and may wish to retain control in order to maintain the flow of these benefits, which are not shared by minority shareholders. Hence, the potential for conflicts of interest and the expropriation of minority shareholders by controlling shareholders is high and may represent greater risk for outside investors. This provides an interesting setting for further empirical investigation of governance issues.

The findings also suggest that the firm's proportion of outside directors on the board is greater in the absence of a majority shareholder in the ownership structure. Similarly, this study documents that the proportion of firms having boards with a majority of outside directors is significantly greater among the subgroup of firms without a single shareholder owning more than 50% of the voting capital. This is consistent with the argument that board independence is inversely related to the firm's ownership concentration. Also, the evidence suggests that the number of directors on the board tends to be positively associated with the firm's equity size. However, the findings also suggest that the board size in this sample of Brazilian companies is small compared to samples of publicly-traded companies from the United States and Canada. This result may provide preliminary evidence that a concentration of ownership and voting privileges negatively impacts the number of direc-

tors on the board of the Brazilian public firms. Surprisingly, the incidence of CEO duality in this Brazilian sample is significantly smaller than in similar samples of public companies from the United States and Canada. This may suggest that CEO duality is closely related to the use of alternate governance mechanisms such as the proportion of outside directors, governance and compensation of board committees and executive performance-contingent compensation. However, whether these alternative governance mechanisms offset the negative impact of combining the positions of CEO and Chairman of the Board in Brazilian public companies remains an empirical issue for future research.

While this study has provided a preliminary step in the examination of the associations between the governance mecha-

nisms of Brazilian publicly-traded companies, there are undoubtedly a number of important empirical issues left to investigate. For example, one interesting extension to this study would be to refine the classification of large shareholders to take into account the voting privileges and fiduciary responsibilities of other large shareholders in the ownership structure. Furthermore, incorporating financial variables and investigating the sensitivity of the firm's performance to the board composition may provide some answers to the question of whether controlling shareholders use board composition to entrench themselves and extract non-justified pecuniary benefits. Further research in these directions could provide a very important contribution to both the study and practice of corporate governance in Brazilian companies. ♦

NOTES

- (1) These segments have been officially adopted by the Brazilian Securities Commission (*Comissão de Valores Mobiliários*).
- (2) This classification follows the study by Leal, Da Silva and Valadares (2002).
- (3) As provided by the study of Leal, Da Silva and Valadares (2002).
- (4) Twenty-four companies with the largest shareholder holding between 20% to 30% of the voting capital, plus 18 companies with the largest shareholder holding between 30% to 40% of the voting capital.
- (5) For example, Bardella S.A. Indústrias Mecânicas has five minority shareholders with family links, Schulz S.A. and Baumer S.A. have three minority shareholders with family links.
- (6) See for example the studies by Zeckhauser and Pound (1990) and Barnhart and Rosenstein (1998).
- (7) The corporate governance guidelines of the Toronto Stock Exchange (TSE, 1994) have motivated the measure used to proxy for boards' efforts in monitoring managerial decisions. Guideline n.3, for example, suggests that every corporation's board of directors be constituted with a majority of individuals who qualify as "unrelated" directors. An unrelated director is a director who is independent of management and free of any interest, business, or other relationship that could, or could reasonably be perceived to materially interfere with the director's ability to monitor management.
- (8) Institutional investors, for example, have emerged as an important group of shareholders in the United States and Canada, with an active governance role and the potential to limit managerial discretionary power. The literature suggests that, unlike individual investors, institutions invest **other people's money** and have legal fiduciary obligations to take proactive monitoring actions. These actions may consist of influencing executive compensation packages, percentage of inside ownership, and board structure (ANDRÉ and SCHIEHLL, 2004). In short, since the previous evidence documents that the incentive and influence to engage in monitoring activities remains a function of equity stake and shareholder fiduciary responsibilities, future studies of the Brazilian capital market and governance structures may benefit from focusing on the identity of large shareholders, whether individual and/or institutional investors.
- (9) According to table 4, Panel C, 65 out of 167 companies (39%) with a controlling shareholder present CEO duality and 24 out of 73 companies (33%) without a controlling shareholder.
- (10) As discussed in Section 4 of this paper.
- (11) Some examples are: Duratex S.A., Itaotec Philco S.A., and Nadir Figueiredo Indústria e Comércio S.A.
- (12) Some examples are: GPC Participações S.A., Iochpe Maxion S.A., and Monteiro Aranha S.A.

- ANDRÉ, P.; SCHIEHL, E. Insider-outsider large shareholder monitoring, alternative governance mechanisms and firm performance. *Finance, Contrôle, Stratégie*, Toulouse, v.7, n.2, p.165-194, June 2004.
- BARHEMA, H.G.; GOMEZ-MEJIA, L.R. Managerial remuneration and firm performance: a general research framework. *Academy of Management Journal*, Briarcliff Manor, v.41, n.2, p.135-145, Apr. 1998.
- BARNHART, S.; ROSENSTEIN, S. Board composition, managerial ownership, and firm performance: an empirical analysis. *The Financial Review*, Tallahassee, v.33, n.4, p.1-16, Nov. 1998.
- BUCHHOLTZ, A.K.; YOUNG, M.N.; POWELL, G. Are board members pawns or watchdogs? The link between CEO pay and firm performance. *Group & Organization Management*, Beverly Hills, v.23, n.1, p.6-26, Mar. 1998.
- COLES, J.W.; McWILLIAMS, V.B.; SEN, N. An examination of the relationship of governance mechanisms to performance. *Journal of Management*, New York, v.27, n.1, p.23-50, Jan. 2001.
- CONYON, M.J.; PECK, S.I. Board control, remuneration committees, and management remuneration. *Academy of Management Journal*, Briarcliff Manor, v.41, n.2, p.135-145, Apr. 1998.
- CORE, J.E.; HOLTHAUSEN, R.W.; LARCKER, D. Corporate governance, chief executive officer remuneration, and firm performance. *Journal of Financial Economics*, Amsterdam, v.51, n.3, p.371-406, Mar. 1999.
- DEMSETZ, H.; LEHN, K. The structure of corporate ownership: causes and consequences. *Journal of Political Economy*, Chicago, v.93, n.6, p.375-393, Dec. 1985.
- FAMA, E.F. Agency problems and the theory of the firm. *Journal of Political Economy*, Chicago, v.88, n.2, p.288-307, Apr. 1980.
- GAGNON, J.M.; St-PIERRE, J. Alternative mechanisms for corporate governance and board composition. In: RONALD, J.D.; MORCK, R. *Corporate decision-making in Canada*. Calgary: University of Calgary Press, 1995. p. 149-188.
- GIBSON, M.S. Is corporate governance ineffective in emerging markets? *Journal of Financial and Quantitative Analysis*, Seattle, v.38, n.1, p.231-250, Mar. 2003.
- INSTITUTO BRASILEIRO DE GOVERNANÇA CORPORATIVA (IBGC). *Relatório de resultado de pesquisa sobre a governança corporativa no Brasil*. São Paulo: IBGC, 1998.
- JENSEN, M.; MECKLING, W. Theory of the firm: managerial behaviour, agency costs and ownership structure. *Journal of Financial Economics*, Amsterdam, v.3, n.1, p.305-360, Jan. 1976.
- KORN/FERRY INTERNATIONAL. *Corporate board governance and director compensation in Canada: a review of 2003*. Vancouver: Patrick O'Callaghan & Associates in partnership with Korn/Ferry International, 2004. p.105.
- LEAL, R.P.C.; DE OLIVEIRA, C.L.T. An evaluation of board practices in Brazil. *Corporate Governance*, Bradford, v.2, n.3, p.21-25, May 2002.
- LEAL, R.P.C.; DA SILVA, A.L.C.; VALADARES, S.M. Estrutura de controle das companhias brasileiras de capital aberto. *Revista de Administração Contemporânea*, Curitiba, v.6, n.1, p.7-18, jan./abr. 2002.
- LEHMANN, E.; WEIGAND, J. Does the governed corporation perform better? Governance structures and corporate performance in Germany. *European Finance Review*, Netherlands, v.4, n.2, p.157-195, Apr. 2000.
- SCHULZE, W.S.; LUBATKIN, M.H.; DINO, R.N.; BUCHHOLTZ, A.K. Agency relationship in family firms: theory and evidence. *Organization Science*, Litchfield, v.12, n.2, p.99-116, Mar./Apr. 2001.
- TORONTO STOCK EXCHANGE COMMITTEE ON CORPORATE GOVERNANCE IN CANADA (TSE). *Where were the directors?* Toronto, Canada: TSE, 1994.
- WEIMER, J.; PAPE, J.C. A taxonomy of systems of corporate governance. *Corporate Governance*, Bradford, v.7, n.2, p.152-166, Apr. 1999.
- ZECKHAUSER, R.J.; POUND, J. Are large shareholders effective monitors? An investigation of share ownership and corporate performance. In: HUBBARD, R.G. *Asymmetric information, corporate finance, and investment*. Chicago, IL: University of Chicago Press, 1990. p.149-180.

ABSTRACT

**Ownership structure and composition of boards of directors: evidence on Brazilian publicly-traded companies**

The purpose of this study is to provide preliminary evidence on the ownership structure and composition of the board of directors of Brazilian publicly traded companies. The ownership structure of the firms investigated, along with the attributes of the boards of directors, including board size, proportion of outside directors and CEO duality. This study documents that voting privileges and the total capital of Brazilian publicly-traded companies remain strongly concentrated, suggesting that the separation of ownership and decision-making control is not the most relevant agency issue. The findings also suggest that majority shareholders in Brazilian public companies are most likely to be either executives and/or directors of the corporation. This leads to the argument that potential conflicts may exist, as well as potential expropriation of minority shareholders by the controlling shareholders. Accordingly, the evidence suggests that the proportion of outside directors on the board is lower among firms having a single controlling shareholder in the ownership structure, which is consistent with the argument that board independence is inversely related to the firm's ownership concentration. In addition, the study documents that the number of directors on the board in this sample is smaller than comparable samples of publicly-traded companies from the United States and Canada. Surprisingly, the incidence of CEO duality in this sample is significantly smaller than in similar samples of public companies from the United States and Canada.

**Uniterms:** corporate governance, ownership structure, board of directors.

RESUMEN

**Estructura de control accionario y composición del consejo de administración: evidencia sobre empresas brasileñas de capital abierto**

El objetivo de este estudio es proveer evidencias preliminares sobre la estructura de control accionario y la composición de los consejos de administración de las empresas listadas en la Bolsa de Valores de São Paulo (Bovespa). Los atributos del consejo de administración investigados, al lado de la estructura de control accionario de las empresas, son el tamaño del consejo, la proporción de miembros externos y la dualidad del director general. Se constató que los privilegios de voto y el capital total de las empresas mencionadas permanecen fuertemente concentrados, lo que sugiere que la separación entre el control accionario y el control de decisión no es el tema de agencia más relevante. Los resultados también sugieren que, en general, el consejo de administración de esas empresas está compuesto predominantemente por accionistas mayoritarios y ejecutivos. Eso da base al argumento de que pueden existir conflictos de interés entre accionistas minoritarios y mayoritarios, así como oportunidades para la expropiación de accionistas minoritarios por parte de controladores y/o ejecutivos. Además, se observó que la proporción de miembros externos en el consejo de administración es menor entre empresas que poseen sólo un accionista controlador en su estructura de propiedad, lo que es consistente con el argumento de que la independencia del consejo de administración está inversamente relacionada con la concentración del control accionario de las empresas. Además, el estudio señala que el número de miembros del consejo en la muestra brasileña es menor en comparación con el de muestras de compañías abiertas de Estados Unidos y Canadá, y que, asimismo, es significativamente menor la incidencia de la dualidad del director general.

**Palabras clave:** gobierno corporativo, estructura del control accionario, consejo de administración.



Com os êxitos alcançados nos dois primeiros anos deste programa, além das duas turmas de fevereiro, a FIA iniciou o curso pré-vestibular turma de maio com 55 vagas, em parceria firmada com a Prefeitura de São Paulo / Secretaria Municipal do Desenvolvimento, Trabalho e Solidariedade e a UNESCO.

A Fundação tem por objetivo multiplicar essa iniciativa, estimulando ações de responsabilidade social na área da educação, a partir de parcerias com organizações em geral para a formação de novas turmas do cursinho pré-vestibular, para que possa atingir maior número de jovens e contribuir para a inclusão social por meio do acesso às universidades públicas.

Visite o nosso site [www.fia.com.br/cursinho](http://www.fia.com.br/cursinho)



Programa FIA de Acesso à Universidade  
Unidade Técnica - R. Valsón Lopes, 101 - Butantã - São Paulo- SP CEP 05360-020  
Tel: (11) 3732-4495 - e-mail: [cursinho@fia.com.br](mailto:cursinho@fia.com.br) - [www.fia.com.br/cursinho](http://www.fia.com.br/cursinho)