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Analysis of the compliance of Brazilian firms with good corporate governance practices

Análisis del cumplimiento de las empresas brasileñas a las buenas prácticas de gobierno corporativo

Análise do c*ompliance* das empresas brasileiras às boas práticas de governança corporativa

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Abstract

Purpose: Studies report that the adoption of good corporate governance practices tends to improve firm value. However, the results of such adoption seem to be conditioned by specific institutional and legal characteristics of each country. This study aims to analyze compliance with good corporate governance practices in the context of publicly traded companies in the Brazilian market.

Methodology: The sample is made up of 1336 annual observations of 167 companies listed on the B3 (Brasil, Bolsa, Balcão) in the period 2010-2017. The practices recommended by the main corporate governance codes in Brazil were used as benchmark. Tests for the difference in means (t-test) and in proportions (z-test) were used to compare the observed situation in the group of firms and the recommendations in the Brazilian market.

Results: Despite the adoption of many of the best practices recommended, there is still space for advancement in the Brazilian firm corporate governance. The results indicate noncompliance of the Brazilian firm with the recommendations regarding the audit committee and fiscal council, which may particularly weaken transparency and control of firm's internal activities. In addition, adherence to distinguished market segments is associated to a greater trend to observe the suggestions emanating from the codes, which may be due to the perception of a favorable cost-benefit ratio of the adoption of corporate governance practices.

Contributions of the Study: The work provides additional contribution by presenting a detailed analysis of the current scenario of the Brazilian firm corporate governance captured from the evaluation of the degree of adoption of each practice recommended individually.

Keywords: Corporate governance. Good practices. Compliance. Soft Law. Brazil.

Resumen

Objetivo: La literatura indica que la adhesión a las buenas prácticas de gobierno corporativo agrega valor a la empresa. Sin embargo, los resultados de tal adhesión parecen estar condicionados a características institucionales y legales específicas de cada país. Este trabajo tiene como objetivo analizar el cumplimiento de las buenas prácticas de gobierno corporativo en el contexto de las compañías de capital abierto en el mercado brasileño.

Metodología: La muestra está compuesta por 1336 observaciones anuales de 167 empresas cotizadas en la B3 (Brasil, Bolsa, Balcão) en el período 2010-2017. Se ha utilizado como referencia las recomendaciones de los principales códigos de gobierno corporativo existentes en Brasil. Se ha hecho prueba de comparación de media (test t) y de proporción (prueba z) entre lo observado en el conjunto de empresas y las recomendaciones en el mercado brasileño.

Resultados: A pesar de la adhesión a muchas de las buenas prácticas recomendadas todavía hay espacio para la empresa brasileña avanzar. Los resultados indican inobservancia de la empresa brasileña a las recomendaciones referentes al comité de auditoría y consejo fiscal, lo que puede debilitar en especial la transparencia y control de los hechos internos de la empresa. Además, la adhesión a niveles diferenciados de mercado está asociada a una más alta inclinación a la empresa observar las sugerencias emanadas de los códigos, lo que puede ser debido a la percepción de una favorable relación costo-beneficio de la adopción del gobierno corporativo.

Contribuciones del Estudio: Como contribución del trabajo se tiene el análisis detallada del actual escenario del gobierno corporativo de la empresa brasileña a partir de la evaluación del grado de adopción de cada práctica recomendada individualmente.

Palabras clave: Gobierno corporativo. Buenas prácticas. Cumplimiento. Soft Law. Brasil.

Resumo

Objetivo: Estudos relatam que a adesão às boas práticas de governança corporativa agrega valor à empresa. No entanto, os resultados de tal adesão parecem estar condicionados a características institucionais e legais específicas de cada país. Este estudo objetiva analisar o *compliance* às boas práticas de governança corporativa no contexto das empresas de capital aberto do mercado brasileiro.

Metodologia: A amostra é composta por 1336 observações anuais de 167 empresas listadas na B3 (Brasil, Bolsa, Balcão) no período 2010-2017. Utilizaram-se como referência as recomendações dos principais códigos de governança corporativa existentes no Brasil. Fez-se teste de comparação de média (teste t) e de proporção (teste z) entre o observado no coletivo de empresas e as recomendações no mercado brasileiro.

Resultados: Apesar da adesão a muitas das boas práticas recomendadas ainda há espaço para a empresa brasileira avançar. Os resultados indicam inobservância da empresa brasileira às recomendações referentes ao comitê de auditoria e conselho fiscal, o que pode fragilizar em especial transparência e controle dos atos internos da empresa. Ademais, a adesão a níveis diferenciados de mercado está associada a uma maior inclinação a observar as sugestões emanadas dos códigos, o que pode ser devido à percepção de uma favorável relação custo-benefício da adoção da governança corporativa.

Contribuições do Estudo: Como contribuição do trabalho tem-se a análise detalhada do atual cenário da governança corporativa da empresa brasileira a partir da avaliação do grau de adoção de cada prática recomendada individualmente.

Palavras-chave: Governança Corporativa. Boas práticas. *Compliance*. *Soft Law*. Brasil.

1 Introduction

The Agency Theory intends to explain the conflicts between firm ownership and firm management due to the separation between them, becoming necessary a set of contracts between firm owners and managers in order to minimize the costs resulting from these conflicts (Fama & Jensen, 1983). In the agency context, the contract between shareholders (principal) and the chief executive officer (agent) is seen as the central element, being the unit of analysis in the context of Agency Theory (Eisenhardt, 1989). The existence of agency conflicts and the resulting costs make the company seek strategies to minimize them (Jensen & Meckling, 1976). The adoption of good corporate governance practices has been indicated as a good strategy to minimize agency costs.

Good corporate governance practices have been adopted by companies looking for a better relationship with their stakeholders. In this context, there is a set of legal mandatory rules that have uniform application. On the other hand, several institutions, such as regulatory bodies, market institutions, executive associations, investors and pension funds, have proposed good corporate governance practices that are not compulsory but that are well-regarded by the market, being flexible - a specific type of soft law, usually condensed into codes of good corporate governance practices. Thus, the company chooses the set of practices that best suits your needs (Abbud, 2014; Guest, 2008; Hooghiemstra & Van Ees, 2011).

The implementation of a corporate governance system in the company, comprising a set of good practices, has been defended as able to improve firm management, firm performance, and firm relationship with the market. In this context, studies have documented that, in fact, companies with better corporate governance practices present more favorable performance than the others, both in the Brazilian (Crisóstomo & Melo Júnior, 2015;

Fernandes, Dias & Cunha, 2010; Lima, Oliveira, Cabral, Santos & Pessoa, 2015; Macedo & Corrar, 2012; Procianoy & Verdi, 2009; Srour, 2005) and international scenario (Alves and Mendes, 2004; Azeez, 2015; Black, Jang, & Kim 2006; Brick & Chidambaran, 2010; Drobetz, Schillhofer, & Zimmermann, 2004; Duru, Iyengar, & Zampelli, 2016; Elsayed, 2007; Franco & Montalván, 2010; Goncharov, Werner & Zimmermann, 2006, Haniffa & Hudaib, 2006; Henry, 2010). Despite these results, previous research in Brazil has found results in the direction that companies still do not envision a favorable cost-benefit relation with the adoption of recommended corporate governance practices, which may be constraining the advance in adopting good corporate governance practices (Brandão & Crisóstomo, 2015; Sonza & Kloeckner, 2014).

Higher degree of compliance with good corporate governance recommendations may be suggestive of the importance given to the issue by the company. In this sense, the evaluation of the degree of adoption of good corporate governance practices on the set of companies in a given market is relevant. In the case of Brazil, from this research one can consider whether the Brazilian company presents good compliance with the good corporate governance practices recommended by the market. The present study has as research problem knowing the degree of compliance of the Brazilian company with the recommendations of good corporate governance practices, looking for an answer to the following question: **Is the Brazilian firm adopting corporate governance practices recommended by the Brazilian market**?

Given the uncertainties regarding the effectiveness of corporate governance practices, which contrasts with the strong market pressure that recommends a broad range of corporate governance practices, this study aims to analyze the Brazilian company's compliance to good corporate governance practices in the context of publicly traded companies.

In this study, the empirical analysis of compliance with the recommendations focuses on the main firm corporate governance structures - board of directors, executive board, board committees, and fiscal council - since the scope of corporate governance is the firm Executive Summit and its system of strategic decisions (Bertucci, Bernardes, & Brandão, 2006; Roe, 2008; Rossoni & Machado-da-Silva, 2010).

For a sample composed of 167 publicly traded companies in the period 2010-2017, the results indicate that the Brazilian company tends to adopt a broad set of good corporate governance practices although there is still difficulty in the compliance with some recommendations regarding the structure of the audit committee and fiscal council operating, which may lead to weaknesses in the control and supervision of the executive management. As expected, the fact that the company signals the adoption of a set of good governance practices through the adherence to a distinguished B3 corporate governance segment is associated with a higher trend to observe good practice suggestions emanating from corporate governance codes in the Brazilian market.

As far as we are aware, there is no work in Brazil that evaluate the adherence of each corporate governance practice to its recommendation by market institutions individually. In an important work, Nascimento, Moura, De Luca, & Vasconcelos (2013) analyzed the proportion of companies adopting certain practices of corporate governance related to the Board of Directors of companies in the so-called "New market" of B3, in a cross-section for the year 2010. In this context, this paper advances research in Brazil by conducting a detailed study on compliance with the various corporate governance practices related to the board of directors, advisory committees to the board of directors, the fiscal council, and the executive board, in a long period of eight years, comparing the situation of the group of companies with the recommendations of the Brazilian market and, moreover, doing a comparison between companies from distinguished segments and the other firms. The work also differs from previous ones given that it does not look for antecedents and/or consequences of corporate governance, but rather verifies whether each recommended practice is being adopted by the set of Brazilian companies.

The remainder of the paper is arranged as follows. Section 2 discusses the related literature and presents research hypotheses. Section 3 contains the methodological strategy design and describes the sample data. In section 4, hypotheses regarding the compliance to good governance practices of Brazilian companies are contrasted and results are discussed. The conclusions are presented in Section 5.

2 Prior research

2.1 Recommended Corporate Governance Practices

The separation between firm ownership and control, due to its natural process of growth in size and complexity, gave rise to conflicts of interest between firm ownership and management and the need to circumvent such conflicts through properly drawn up contracts as proposed by the Agency Theory (Fama & Jensen, 1983; Jensen & Meckling, 1976). The costs arising from agency conflicts due to the relationship between imperfect agents and incomplete contracts motivate the search for strategies that will reduce their negative effects on the firm (Eisenhardt, 1989; Jensen & Meckling, 1976). The adoption of a corporate governance system that integrates good practices for monitoring firm management has been proposed as a good strategy in this regard. Under the Agency Theory framework, corporate governance can be seen as a system composed of a set of mechanisms capable of contributing to the alignment of interests between shareholders and the firm executive management and thus to minimize conflicts and agency costs (Claessens & Yurtoglu, 2013; Love, 2011; Shleifer & Vishny, 1997).

Facing the need to protect the firm and their interests as owners, shareholders bear the costs of a corporate governance system. In this process, there is a trend that shareholders with higher proportions of firm shares are more interested in the implementation of this system as proposed by the free-rider problem (Shleifer & Vishny, 1997). Given that it involves costs, the adoption of corporate governance practices is a free choice for the firm, being its decision to adopt a small or ample set of governance mechanisms. However, markets have advanced to make certain governance mechanisms mandatory through some legal instrument or, in most cases, recommendations. In this sense, such recommendations have been compiled to compose the so-called Good Corporate Governance Practices Codes that have been disseminated in several markets (Aguilera & Cuervo-Cazurra, 2004, 2009).

As a result of financial scandals in USA in the early 2000s, the US market imposed a set of corporate governance practices through the Sarbanes-Oxley Act in 2002. However, the most usual is to have the recommendation of practices that are voluntary, such as what happened in England through the approval of the Cadbury Report in 1992 (Aguilera, Cuervo-Cazurra, 2009). In other markets, such as in Germany, for example, despite the adoption of good practices is voluntary, companies should explain the reason for not adopting best practices by following the “comply or explain” principle (Aguilera, Cuervo-Cazurra, 2009; Silveira et al., 2009).

The Corporate Governance Best Practices Codes were designed to promote the improvement of corporate governance systems by proposing a set of recommended governance standards on the role and composition of corporate governance structures (Efigénia, 2015). The codes were designed to correct weaknesses in the corporate governance system by recommending a set of practices related to the board of directors, executive management, including hiring and remuneration policies for members of both, investor relations, auditing and information disclosure. In general, the codes aim to improve firm management and governance, and strengthen firm responsibility to its shareholders, while maximizing the firm value to shareholders and stakeholders as a whole (Aguilera & Cuervo-Cazurra, 2004).

Since the issuance of the Cadbury report ("The Financial Aspects of Corporate Governance") in the United Kingdom in 1992, the publication of codes of good practice has grown considerably. In this context, it becomes relevant to analyze how these codes affected firms' governance structures (Aguilera & Cuervo-Cazurra, 2009; Cuomo, Mallin, & Zattoni, 2016; Zattoni & Cuomo, 2008). Concern about the strengthening of the capital markets led them to act in the composition of codes, acting effectively like exogenous forces leading companies to pay attention to their corporate governance systems. In this process, codes have become part of the vast majority of institutional environments in which firms operate (Aguilera & Cuervo-Cazurra, 2004, Burton, 2000, Hooghiemstra & van Ees, 2011 and Seidl, 2007). Claensses and Yurtoglu (2012) consider that the codes of good governance are contributing to a convergence of the set of what would be good practices of corporate governance independently of the market, although the practices adopted are still heterogeneous between companies.

It is recommended that a good quality corporate governance system, implemented through the adoption of a set of good corporate governance practices, is capable of generating several benefits to the firm, such as creating value and improving firm performance by enhancing the firm management. In this context, there is evidence already documented, in different markets, of a positive effect of the quality of the corporate governance system on firm value (Brick & Chidambaran, 2010; Drobetz et al., 2004; Lima et al., 2015) and on economic-financial performance (Haniffa & Hudaib, 2006; Macedo & Corrar, 2012). In parallel, there are results that indicate that better corporate governance is capable of improving firms financial structure (Aras & Furtuna, 2015; Crisóstomo & Melo Júnior, 2015). There is also evidence that good corporate governance practices are associated with both lower cost of equity and debt (Fonseca & Silveira, 2016; Zhu, 2014). The expected reduction of agency costs resulting from a high-quality corporate governance system has also been confirmed (Henry, 2010). On the other hand, although there is a smaller volume of research, there are also studies that do not find positive results due to the company's effort to have a good set of corporate governance practices (Fernandes et al., 2010).

In Brazil, as in most results from other markets, the findings indicate that there are benefits to the company as a result of the adoption of good corporate governance practices (Aras & Furtuna, 2015, Crisóstomo & Melo Júnior, 2015; Fonseca & Silveira, 2016; Zhu, 2014).

In addition to this set of results, the literature also presents arguments in the sense that the results of adherence to good corporate governance practices are contingent since they depend on the legal and institutional environments to which markets are subject (Aguilera & Cuervo-Cazurra, 2009; Aguilera & Jackson, 2003; Fan & Yu, 2016; Haniffa & Hudaib, 2006; La Porta, Lopez-De-Silanes, & Shleifer, 2008; Rossoni & Machado-da-Silva, 2010). In this context, as above mentioned, there are three possible approaches to the legal obligation of good corporate governance practices. The hard law, endowed with legal coercivity; the soft law approach, which is based on rules of conduct recommended as it occurs in environments of codes of governance practice; and finally, there is an approach that can be described as the fusion of characteristics of the first two, there being a set of mandatory and other recommended practices. The trend of code adoption has been strong, recommending corporate governance practices and requiring firms to justify non-adoption under the well-known "comply or explain" principle adopted in the UK, Germany, and the Netherlands, for example (Albuquerque, 2008; Efigénia, 2015). A major debate in international corporate governance is on what might be the best strategy for achieving the best level of adherence to good governance practices by companies in all countries, whether by market by soft law, or through "comply or explain" (Abbott & Snidal, 2003; Aguilera & Cuervo-Cazurra, 2009; Hooghiemstra & van Ees, 2011; Keay, 2014; Liu, 2017; Parisi, Mathur, & Nail, 2009; Rejchrt & Higgs, 2015; Salterio, Conrod, & Schmidt, 2013).

2.2 Hypothesis development

Under the trend of corporate governance practices codes, regulatory agencies and market institutions establish a code of good practices to be voluntarily adopted by companies. The best practices are added to those that are compulsory, which are established by some legal instrument. Each market has its specificities associated with the institutional environment (Aguilera & Cuervo-Cazurra, 2009, Aguilera & Jackson, 2003, Fan & Yu, 2016, Haniffa & Hudaib, 2006, La Porta, Lopez-De-Silanes, & Shleifer, 2008; Rossoni & Machado-da-Silva, 2010).

In Brazil, the legislation advanced and strengthened the CVM (*Comissão de Valores Mobiliários*, the Brazilian SEC) through 10.411/2002 Act by establishing the fixed tenure and stability of its directors and giving financial autonomy to the institution, and more power in controlling the activities of companies on the market and in controlling the activities of Stock Exchanges in Brazil. The Brazilian Corporate Law provides a minimum set of mandatory practices, such as a minimum dividend or minimum free float. A broad range of recommended corporate governance practices is voluntarily adopted. Market institutions have also taken a more active role in this process. In this scenario, the Brazilian Stock Exchange (B3, former BM&FBovespa) and the Brazilian Corporate Governance Institute (IBGC) are worth mentioning.

The IBGC is a national, non-profit association that was founded on November 27, 1995, as an organization entirely dedicated to promoting good corporate governance in Brazil. IBGC brings together people from the financial market, companies and the academia with the aim of encouraging the adoption of good corporate governance practices by companies and stimulating the debate on the subject in Brazil. The IBGC has published the *Código das Melhores Práticas de Governança Corporativa* that is in its 5th edition (IBGC, 2015). In addition to the IBGC code, two other relevant institutional initiatives to promote corporate governance in Brazil should be mentioned: the *Código PREVI de Melhores Práticas de Governança Corporativa*, prepared by the board of directors of the Banco do Brasil Employees' Pension Fund (PREVI); and the *Cartilha de Boa Governança*, published by the Brazilian Securities and Exchange Commission (CVM).

The movement of these institutions in the sense of promoting corporate governance in the Brazilian company has been remarkable. The recommendations contained in IBGC's code have become very relevant in the market. Companies became interested in widely disseminating their high degree of attention to good governance through the dissemination of practices adopted. From 2010 on, it became mandatory for the public Brazilian company to disclose information on corporate governance and firm control to the CVM in the Firm Reference Form (*Formulário de Referência*). In this document, the firm corporate governance practices defined in the General Annual Meeting (AGO), which occurs in the first months of the year (Brandão & Crisóstomo, 2015), should be informed. This disclosure is an important instrument able of reducing informational asymmetry on governance practices of all publicly traded companies in Brazil. Given that this disclosure is mandatory, we can consider this

CVM action as an important tool to encourage the adoption of good governance practices by the Brazilian firm, since the firm will make an effort to signal that it is interested in high corporate governance standards.

In the present international scenario, characterized by strong recommendation for the adoption of good corporate governance practices, the aforementioned process of advancement in Brazil is taking place, with the action of the Brazilian Stock Exchange (B3), CVM and IBGC. Pressure from institutions and market stakeholders, such as funding providers and shareholders, for the improvement of corporate governance system contributes to a proactive movement by firms to improve such a system through the highest level of compliance with the recommendations stemmed from corporate governance codes. Thus, it is hypothesized that Brazilian firms are making an effort to improve their corporate governance system with the inclusion of good practices recommended by the codes, as summarized below:

Hypothesis 1: Brazilian firms have complied with the recommendations of the codes of good corporate governance practices.

The implementation of the distinguished segments of corporate governance of Brazilian Stock Exchange (B3) was considered an important landmark in the Brazilian company's corporate governance since 2001. In this process, B3 created the so-called Special Corporate Governance Segments - Level 1, Level 2 and *Novo Mercado*, inspired by the German *Neuer Markt*. By signing the participation agreement to be listed in a certain segment, the company assumes that it will adopt the set of good governance practices required by B3 for the specific corporate governance segment - Level 1, Level 2 and *Novo Mercado* (Procianoy & Verdi, 2009). Such practices include the ones related to the composition and functioning of the board of directors, the set of board committees, functioning of the fiscal council, and composition and functioning of the executive management team. By taking on this commitment, the company positively signals to the market its commitment to improving the its management process and, on the other hand, expects the market to have a better appreciation of it given that, *a priori*, it will offer lower risk to its investors by adopting a good set of corporate governance practices (Carvalho, 2002; Crisóstomo & Melo Júnior, 2015). In fact, there is evidence that a market index composed of firms with better qualified corporate governance outperformed the Ibovespa index in the last decade (Matos, 2017).

A company that voluntarily adheres to a set of good corporate governance practices demonstrates to the market its willingness to improve its corporate governance system. In the case of distinguished segments B3, there has been common the migration for trading segments with more rigorous requirements. This stimulus to adopting better governance practices through the adherence to distinguished segments B3 and the migration between such segments to more demanding ones seems to be frequent. This search for better governance standards is aligned with the Agency Theory, which advocates the search for reduction of agency conflicts and the respective costs arising from them.

Under this scenario, it is plausible to propose that companies that have contractually adhered to a set of governance practices of distinguished segments also adopt, in parallel, other additional practices suggested by corporate governance codes. Thus, it is hypothesized that companies belonging to distinguished segments B3 have a higher degree of adherence to good corporate governance practices than those listed in the traditional market, in the following terms:

Hypothesis 2: Firms that make a formal commitment to a set of good corporate governance practices tend to expand the incorporation of good practices.

3 Methodological Procedures

3.1 Strategy and method of the research

Regarding the purpose of the present study, which is identifying the corporate governance practices adopted by the Brazilian company and its level of compliance with the recommendations presented by corporate governance codes in Brazil, this research is classified as descriptive, since it identifies the present status of the Brazilian firm, assessing the practices adopted in comparison to those recommended (Gray, 2012). Descriptive studies aim to describe how a given phenomenon occurs according to situations and events that are observed and reported (Sampieri, Collado, & Lucio, 2013).

With regard to procedures, the research is documentary. The levels of documentary information can be classified into three layers: primary sources, secondary sources, and tertiary sources. Primary sources are those that provide original research data not yet processed and is subject to some interpretation, such as data attributes of individuals, memos, letters, interviews or full speeches, laws, regulations, court decisions and census (Cooper & Schindler, 2011). Secondary sources provide data already submitted to some process of organization, grouping or interpretation, from the initial format obtained from the primary source, such as databases relating to a set of individuals of a population, encyclopedias, books, manuals (Cooper & Schindler, 2011). Tertiary sources, in turn, are more elaborate interpretations, even involving some analysis, such as indexes, bibliographies and other search assistants (Cooper & Schindler, 2011).

Considering the information feasibility, the source of firm data documents used in this research was secondary, being data collected from the CVM website, which stores and disseminates the Firm Reference Forms of several firms registered there, and from B3 (formerly BM&FBovespa), which discloses information on firm trading segment. From the point of view of the institutions that prepare documents on corporate governance practices in Brazil, we consulted the *Código das Melhores Práticas de Governança Corporativa*, published by IBGC; the *Código PREVI de Melhores Práticas de Governança Corporativa*, prepared by the board of participation of the Bank of Brazil Employees' Pension Fund (PREVI); and the *Cartilha de Boa Governança*, published by the Securities and Exchange Commission (CVM).

Regarding the approach, the research is classified as quantitative, since the data are organized and tabulated to be submitted to statistical tests of significance with the objective of empirically ascertaining the proposed hypotheses (Creswell, 2010; Martins & Theóphilo, 2009).

For the analysis of corporate compliance with the rules proposed by the Good Governance Codes, a detailed descriptive analysis of the level of adherence of corporate governance practices by firms was carried out. The observed values were then compared with the recommended benchmark values. In this case, the test for the difference between sample and benchmark was performed. Student's t-test for the difference in means, and z-test for the difference in proportions, were used, according to each practice. The second step, which intends to verify whether there are differences in the degree of adoption of good practices between firms that have committed themselves to a list of good practices, proxied by the adhesion to one of the distinguished segments of B3, and firms in the traditional segment with no governance requirements, is also basen on tests for comparison in means and proportions.

A review of the literature on the adoption of these recommendations and content analysis of corporate governance codes used in Brazil was carried out. Thus, the *Código das*

Melhores Práticas de Governança Corporativa, edited by IBGC; the *código PREVI de Melhores Práticas de Governança Corporativa*, prepared by the board of participation of the Bank of Brazil Employees' Pension Fund (PREVI); and the *Cartilha de Boa Governança*, published by the CVM (*Comissão de Valores Mobiliários*, i.e. the Brazilian SEC) were analyzed.

As a source of data collection, documentary research was undertaken, based on the examination of the Reference Form of firms analyzed and the set of good practices required in the contracts of each distinguished segment of B3.

In order to analyze firm compliance with the rules proposed by the codes of good practices, a detailed descriptive analysis of the group of firms is used, and tests are performed to compare the averages of observed values indicative of certain corporate governance practices and the recommended benchmark values. For some other practices, tests are performed comparing the proportions of firms that adopt and do not adopt certain recommended best practices. Subsequently, in order to verify if there are differences in the level of adoption of good practices between the traditional market and firms that are committed to a set of good practices, proxied by the adhesion to one of the distinguished segments of B3, tests to compare means and proportions for two samples were performed, comparing companies listed in special segments B3 with those of the traditional market.

3.2 Sample

A sample of 1336 annual observations of listed firms in the Brazilian stock exchange (B3) in the period 2010-2017 was used to contrast the proposed hypotheses. Sample data were obtained from the Economática® system and from the Brazilian Securities and Exchange Commission (CVM).

The sample comprises 167 firms with the highest market liquidity and presence in the Brazilian stock exchange (B3). The term liquidity indicates the ease with which firm share is traded, being related to the time the asset takes to be traded (Brealey, Myers, & Allen, 2013). The market liquidity factor has been considered relevant in stock exchange because the firm share price variation is associated with the trading volume of the firm share as well as with the adequate disclosure of information about the firm that may have an effect on the market's expectation on firm future (Terra & Lima, 2006). Relevant prior literature has pointed liquidity as a factor that may be related to the most appropriate firm market valuation since information disclosure will be better according to the best corporate governance standard (Terra & Lima, 2006). Liquidity may also be associated with corporate governance and insider trading, which should be inversely proportional to the corporate governance quality (Barbedo, Silva, & Leal, 2009). In this way, firms with low liquidity tend to face less pressure to have better governance standards compared to those with higher liquidity (Brandão & Crisóstomo, 2015). Thus, the sample comprises firms from different trading segments of B3. In addition, the sample is representative given that it is composed of firms from 10 different sectors, according to the classification of B3 (Table 1).

Table 1
Firms sample by industry

Industry	No. firm-year obs.	% Sample
Capital Goods and Services	200	14.97%
Consumer Cyclical	288	21.56%
Consumer Non-Cyclical	120	8.98%
Financial	232	17.37%
Basic Materials	168	12.57%
Oil, Gas, and Biofuels	48	3.59%
Health	56	4.19%
Information Technology	24	1.80%
Telecommunications	32	2.40%
Utilities	168	12.57%
Total	1336	100.00%

Source: *Research Data.*

4 Results and analyses

Codes of good governance in Brazil recommend the functioning of the fiscal council on a permanent basis - without it being necessary for non-controlling shareholders to meet the shareholding percentages required by law for the establishment of it. Table 2 shows the proportion of firms that adopt a set of corporate governance practices recommended in Brazil relative to the board of directors, executive management and fiscal council.

The fiscal council can be considered as an important body that contributes to the alignment of interest between shareholders and management as well as between controlling and minority shareholders. It is observed that 64.01% of Brazilian firms already have the fiscal council installed. However, among these, only 44.82% have it as permanent, and therefore, most of them are non-permanent, going in the opposite direction of the recommendation (Table 2). In fact, the proportion of firms with fiscal council installed is higher than that of those that do not have it, while, on the other hand, the proportion of companies with the permanent fiscal council is lower. Due to the necessary independence of the fiscal council, because of its duties, this council should not be subject to evaluation, except in the case of self-assessment. As can be seen, this practice has still been adopted by just a few firms (5.65%). Additionally, among the firms that have fiscal council installed, 15.88% do not have the representation of minority shareholders in it, contrary to such presence that is strongly recommended. A high proportion of the firms has only 1 minority representative (50.24%), and only 12.83% of them have 3 and up to 5 representatives of minority shareholders.

Table 2
Corporate governance practices

	Category of company	N	%	p-value z-test
Fiscal Council Installed	FC is installed	850	64.01	0.000
	No FC installed	478	35.99	
Permanent Fiscal Council	FC is permanent	381	44.82	0.000
	FC is not permanent	469	55.18	
Evaluation of the Fiscal Council	There is an evaluation of FC	48	5.65	0.000
	There is no FC evaluation	802	94.35	
Evaluation of the Executive Board	There is evaluation	953	71.76	0.000
	There is no evaluation	375	28.24	
CEO Duality	There is duality	145	10.95	0.000
	There is no duality	1179	89.05	
Evaluation of the Board of Directors	There is evaluation	482	36.35	0.000
	There is no evaluation	844	63.65	
Women on the Board of Directors	There are women	405	30.59	0.000
	There are no women	919	69.41	
Substitutes on the Board of Directors	There are substitutes	335	25.28	0.000
	There are no substitutes	990	74.72	

Source: *Research Data.*

Codes of good governance recommend that the board of directors annually make a formal evaluation of the performance of the executive board since it contributes to the strategic policy and to the monitoring of the firm’s executive management. This makes the board of directors, from the Agency Theory perspective, an important tool in promoting the alignment of interests between shareholders and firm management. It can be observed that, in fact, a higher proportion of companies (71.76%) follows this recommendation, despite the high proportion of firms that do not evaluate the firm’s executive board (28.24%) (Table 2). Nonetheless, although it is recommended that there is also the evaluation of the board of directors, this is only done in a few more than one third of the firms (36.35%). Since it is the board of directors itself that decides about its evaluation, the results signal a possible situation of entrenchment of the board members in the Brazilian firm.

The CEO duality - the same person being the board chairman and CEO - is largely not recommended by corporate governance codes. Duality signals excess power concentrated in the hands of one person, which may be a contributing factor to agency conflicts with outside investors. In Brazil, this practice is adopted by only a reduced proportion of firms (10.95%) that is far lower than that of firms that keep these position in different hands (89.05%), which is a positive signal for this group of firms.

Regarding the diversity in the composition of the board of directors, the presence of women in this body is recommended by the various codes of good corporate governance. However, the most Brazilian companies (69.41%) do not have female presence on their boards, a proportion that is statistically higher than that of companies that already have women on the board (30.59%). On the other hand, there is a trend in the Brazilian firm to follow the recommendation of no substitutes for directors, which is followed by 74.72% of the firms, which is a proportion that is statistically higher than that of firms that still have substitute board members (25.28%). Despite this trend towards the abolition of board substitutes, the number of companies that have the substitute figure is still high, which is seen as negative by the market.

Table 3 shows numbers related to the existence of the various advisory board committees held by the Brazilian firms. Such committees may exert a number of activities under the board competence, which may sometimes be overloaded with to much duties (IBGC, 2015; Spira & Bender, 2004). In this context, there is a low adhesion of firms to maintain such structures. The audit committee, the most recommended by good governance, is, in fact, the second most frequently constituted (49.77% of companies). The nomination/remuneration committee is the most common, being adopted by 50.38% of firms. This situation points out the importance given to hiring firm managers and directors. Regarding the set of committees, the recommendation is that the creation of committees should take into account firm industry and firm size, given that an excessive number of committees may generate inappropriate interference in the board, in addition to deadweight costs for the firm. This recommendation is aligned with the goal of reducing conflicts and agency costs. These goals should be sought through the optimal combination of board committees.

Table 3
Analysis of the advisory committees of the Board of Directors

Committee	Presence/existence	N	%	p-value z-test
Audit	No	665	50.23	0.815
	Yes	659	49.77	
Finance	No	1005	75.91	0.000
	Yes	319	24.09	
Compensation/Nominating	No	657	49.62	0.697
	Yes	667	50.38	
Risk	No	1012	76.44	0.000
	Yes	312	23.56	
Sustainability	No	1141	86.18	0.000
	Yes	183	13.82	
Governance	No	1088	82.18	0.000
	Yes	236	17.82	

Source: *Research Data.*

Figure 1 outlines the trend in the growth of adoption of each advisory committee to the board of directors in the Brazilian firm over time. As can be seen, since 2010, there has been an increase in these committees, which indicates the importance that has been given to the presence of these board components as advisory services to the board of directors as elements that are capable of strengthening the corporate governance system. In fact, relevant literature has advocated that the functioning of advisory committees to the board of directors is an adequate mechanism for the improvement of corporate governance by delegating specific tasks to smaller groups of members that carry out further analysis. The committees also allow for more contribution from firm non-executive members (Spira & Bender, 2004).

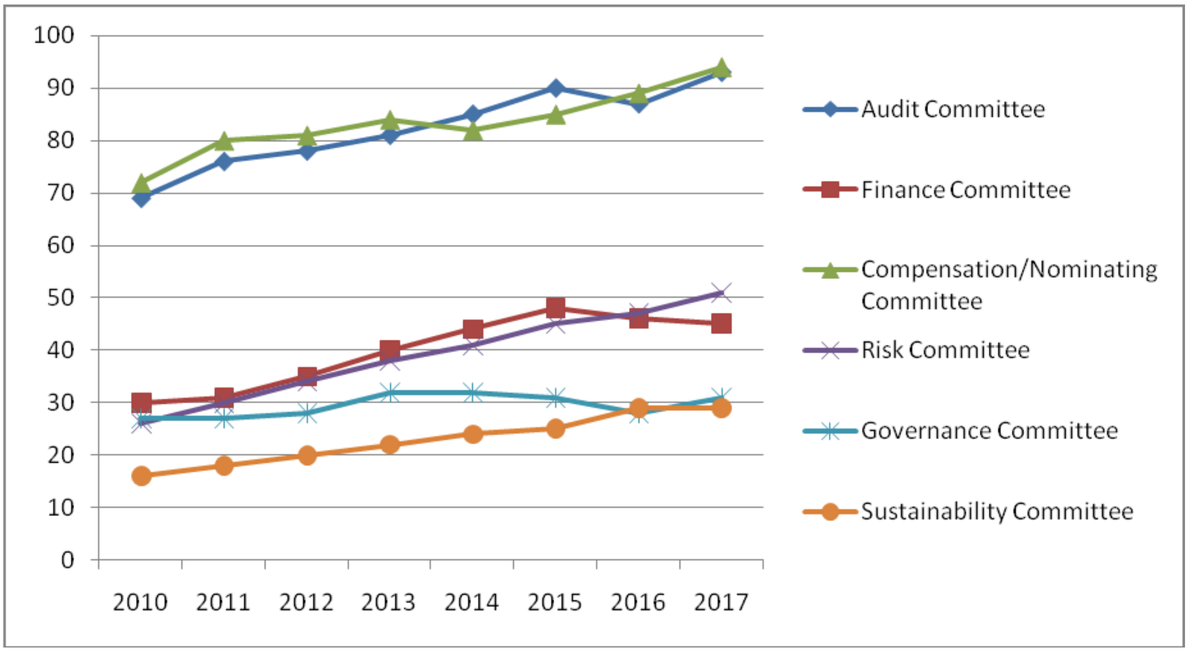

Figure 1 *Evolution of the presence of advisory committees to the Brazilian company's board of directors*
Source: *Research Data.*

Table 4 contains findings for the board of directors, the executive board and the audit committee, comparing the average of each indicator with the benchmark value recommended by the codes of good corporate governance practices in Brazil.

The results show that there is a certain trend of the Brazilian firm to follow recommendations of the codes of good practices regarding the mandate and size of the board of directors. The average mandate of 1.772 years is lower than the recommendation of a maximum of 2 years (p-value = 0.000) and is thus in accordance with the codes' proposition. Regarding the number of board members, the observed average (7.672 members) is within the recommended range, being statistically higher than the minimum of 5 (p-value = 0.000) and lower than the maximum of 11 (p-value = 0.000). The tenure of the executive board presents an average of 2.051 years which is also in line with the recommendation to be a maximum of 3 years. In fact, the mean of 2.051 is statistically less than 3 years (p-value = 0.000).

Codes of good corporate governance practices have emphasized the need for an optimal structure for the audit committee so that it may be able to provide effective advice to the board of directors on issues related to transparency in the firm's relationship with stakeholders. It is recommended that such a body has three to five members. The findings for the Brazilian company's audit committee show that the average number of members (3.376) is within the recommended range of 3 to 5. In fact, this average value is statistically higher than 3 (p-value = 0.000) and less than 5 (p-value = 0.000) which are the limits of the recommended interval.

As a strategic advisory body, it is recommended having board directors as members of the audit committee (IBGC, 2015). An average of 0.700 (70.0%) of audit committee members who were board members was found. This average is statistically lower than the recommended one (100%), which shows that, as a whole, Brazilian firms are not following this guideline. The codes also recommend that at least the majority of audit committee members (50%) be composed of independent directors - those who do not have any relationships that could significantly influence decision making in the best interests of the organization (IBGC, 2015). The average value of 0.219 independent members is statistically lower than the recommended minimum of 0.5 signaling that the Brazilian company is also failing to reach this minimum proportion of independent members of the audit committee.

Table 4
Comparison of averages of corporate governance practices between the recommended value and the average obtained by the companies

	N	Mean	Reference value (recommended by codes of good governance)	p-value	Std. deviation	C.V.	Min	Max
Tenure of the Board of Directors	1327	1.772	Maximum 2 years	0.000	0.587	0.332	1	5
Size of the Board of Directors	1325	7.672	From 5 to 11 directors	0.000 0.000	2.477	0.323	1	18
Tenure of the Executive Board	1319	2.051	Maximum 3 years	0.000	0.746	0.364	1	3
Size of the Audit Committee	603	3.376	From 3 to 5 members	0.000 0.000	1.043	0.309	1	8
Ratio of number of members of the audit committee who are directors and the total number of members of the audit committee	602	0.700	1	0.000	0.354	0.506	0	1
Ratio of the number of independent members to total members of the audit committee	602	0.219	0.5	0.000	0.013	1.485	0	1

Note: p-value indicates the significance of the difference between the mean and the reference value (recommended by codes of practice).
Source: *Research Data.*

A comparison was made between firms listed in the traditional B3 segment and those with listed in distinguished segments, in order to verify if, in fact, firms from distinguished segments present a higher trend to adopt better practices of corporate governance, as suggested by Hypothesis 2.

Table 5 shows average numbers for the board of directors, executive board, audit committee, and fiscal council, comparing firms listed in the traditional B3 segment with those listed in distinguished segments of corporate governance.

With respect to the board of directors' tenure, it can be observed that companies in distinguished, or special, segments have a tenure average lower than those in the traditional market, indicating that firms in distinguished segments are more attentive to the recommendations of good governance practices, as hypothesized. In fact, firms listed in the traditional market have an average term of 2.09 years, statistically above the recommended 2 years. In addition to better adherence to the recommendation on the board of directors' tenure, firms listed in distinguished segments also present numbers that signal more attention to recommendations in relation to several other good practices: board size; number of independent members of the board of directors; number of external members of the board of directors.

The number of members in the board of directors (size of the board of directors) is higher in firms listed in of distinguished segments B3, signaling that these companies are investing more in the structure of this collegiate. In addition, in line with the hypothesized, firms listed in special segments have boards of directors with more independent members and present a greater presence of external members, compared to the reality of firms listed in the traditional market. Also higher in firms listed in special segments B3 is the representation of minority shareholders in the board of directors, which is observed both by the number and average of the proportion of minority shareholders' representatives.

The fiscal council of firms listed in special segments B3 presents a higher average representation of minority shareholders (number of minority shareholders in the fiscal council, and the ratio of number of minority shareholders to total members in the fiscal council). Firms listed in distinguished segments B3 seem to be investing more to have a strong fiscal council.

As suggested, the tenure of the executive board is lower in firms listed in distinguished segments B3, being closer to the recommendation of a maximum of 3 years. This is beneficial to the firm by promoting more frequent reviews of the executive board. This set of elements indicates that, in fact, firms listed in special segments are making an effort to have a set of practices of corporate governance that contribute to the reduction of agency conflicts.

It is worth mentioning that, contrary to expectations, there is no significant difference between the composition of audit committees of firms listed in special segments B3 and those listed in the traditional segment. In addition, contrary to expectations, the recommendation on the participation of women on the board of directors is more observed in firms listed in the traditional market.

Table 5
Comparison of means of values associated with corporate governance practices between companies in the Traditional Market and Special (Distinguished) Segments

	Traditional Market		Distinguished Segments		
	N	**Mean**	**N**	**Mean**	**p-value**
Tenure of the board of directors	222	2.090	1105	1.707	0.000
Size of the board of directors (number of members)	221	6.805	1104	7.845	0.000
Number of women on the Board of Directors	221	0.516	1103	0.353	0.003
Number of external members on the board of directors	221	5.946	1103	7.173	0.000
Number of independent members on the board of directors	220	0.986	1104	2.322	0.000
Number of representatives of minority shareholders on the board of directors	221	1.837	1102	2.479	0.000
Size of the fiscal council (number of members)	115	3.573	735	3.696	0.192
Number of representatives of minority shareholders in the fiscal council	115	1.174	735	1.385	0.013
Ratio of the number of representatives of minority shareholders to the total number of members in the fiscal council	115	0.319	735	0.379	0.010
Tenure of the Board of Executive Officers	214	2.252	1105	2.013	0.000
Size of the Board of Executive Officers (number of members)	221	6.647	1104	6.616	0.958
Number of women on the Board of Executive Officers	221	0.457	1103	0.406	0.428
Size of audit committee (number of members)	77	3.311	526	3.386	0.524
Number of directors on the audit committee	76	2.487	526	2.304	0.245
Number of independent directors on the audit committee	76	0.816	526	0.654	0.289
Ratio of independent members to total members in the audit committee	76	0.265	526	0.212	0.300

Source: *Research Data.*

Table 6 shows the test for the difference in proportions (z-test) comparing the compliance of firms listed in the traditional segment B3 and the ones listed in special segments with respect to some corporate governance practices. The chi2 test (p-value = 0.000) shows that there is a significant difference in relation to the CEO duality between firms listed in the traditional segment and the ones listed in distinguished segments B3. It can be observed that, as expected, CEO duality is more pronounced in firms listed in the traditional market, since 25.91% of them still maintain duality, in contrast to only 7.97% of those listed in special segments B3. It is worth mentioning that the proportion of companies that no longer use duality (1179 observations, 89.05%) is much higher than that of companies that still maintain this situation (145 observations, 10.95%).

Regarding the evaluation of the executive board, it can be observed that the large majority of firms already adopt this practice (953 observations, 71.76%). In addition, the proportion of firms listed in special segments that evaluate the board (847 observations, 76.65%) is much higher than that of companies that do not (258 observations; 23.35%).

Contrary to the expected, the non recommended practice of having substitute members in the board of directors is still a reality for approximately 25% of the Brazilian firms. Also in the opposite direction of the expectation, among the firms that still adopt the substitution in the board of directors, 91.94% are of firms listed in distinguished segments B3.

In general, it was observed that listed in distinguished segments present a higher proportion of the presence of advisory committees to the board of directors. Specifically, the committees most frequently present in the Brazilian firm and that, in fact, present a more relevant presence in firms listed in distinguished segments are: audit committee, finance committee, remuneration/appointment committee, risk committee, governance committee, sustainability committee, fiscal council.

The audit committee – the most recommended by the codes of good corporate governance practices – is the second most frequently observed, being adopted by 49.77% of Brazilian firms, which is a fraction of firms not statistically different from those that do not have such a committee (50.23%) (p-value = 0.815, z-test). The significant difference in proportion is between the firms listed in distinguished segments and the firms listed in the traditional segment. It is observed that 62.10% of the firms listed in the traditional segment have no audit committee compared to the proportion of only 37.90% who have it. The situation reverses, however, when it is observed that 52.13% of the firms listed in distinguished segments have audit committee while 47.87% do not have it. Among the companies that have an audit committee, 87.40% are listed in distinguished segments.

Table 6
Comparison of proportions of corporate governance practices between companies in the Traditional Market and Special (Distinguished) Segments

		Traditional Market		**Distinguished Segments**		
Corporate governance practice	Situation	N	%	N	%	p-value
There is a duality of CEO	No	163	74.09	1016	92.03	0.000
	Yes	57	25.91	88	7.97	
Evaluation of the executive board	No	117	52.47	258	23.35	0.000
	Yes	106	47.53	847	76.65	
Presence of substitutes on the board of directors	No	194	87.78	796	72.10	0.000
	Yes	27	12.22	308	27.90	
Presence of the audit committee	No	136	62.10	529	47.87	0.000
	Yes	83	37.90	576	52.13	
Presence of the finance committee	No	199	90.87	806	72.94	0.000
	Yes	20	9.13	299	27.06	
Presence of the compensation/nominating committee	No	148	67.58	509	46.06	0.000
	Yes	71	32.42	596	53.94	
Presence of the risk committee	No	196	89.50	816	73.85	0.000
	Yes	23	10.5	289	26.15	
Presence of the governance committee	No	206	94.06	882	79.82	0.000
	Yes	13	5.94	223	20.18	
Presence of the sustainability committee	No	207	94.52	934	84.52	0.000
	Yes	12	5.48	171	15.48	
Fiscal council installed	No	108	48.43	370	33.48	0.000
	Yes	115	51.57	735	66.52	
Permanent fiscal council	No	168	75.34	777	70.32	0.131
	Yes	55	24.66	328	29.68	
Evaluation of the Fiscal Council	No	223	100	1052	95.23	0.001
	Yes	0	0	53	4.80	
Presence of substitutes on the board of directors	No	194	87.78	796	72.10	0.000
	Yes	27	12.22	308	27.90	

Note: p-value is the probability value for the chi2 test for the difference in proportions.
Source: *Research Data.*

It can be observed that only 24.09% of Brazilian firms adopt the finance committee, a proportion that is statistically lower than those of firms that do not implement it (75.91%) (p-value = 0.000, z-test). Within the group of firms that have a finance committee, 93.73% are from distinguished segments B3, showing the importance given to this body by firms that are making a more intense effort to advance in corporate governance practices. A similar situation is observed with regard to the compensation/nominating committee. In this case, the proportion of firms within distinguished segments that have this committee (53.94%) is statistically higher than that of companies that do not have it (49.06%) (p-value = 0.0528, z-test). In companies in the traditional segment, the proportion is much higher (67.58) for those who do not have the compensation/nominating committee compared to only 32.42% that has it.

The context for the presence of risk, governance and sustainability committees shows a higher proportion of firms that do not adopt them. However, when analyzing each one separately, we see the trend of more adoption of each of the three committees by firms within distinguished segments B3. About the firms that have a risk committee, 92.63% of them are listed in a distinguished governance segment. Among the firms that adopt a governance committee, 94.49% is listed in a distinguished segment. And among the ones that have a sustainability committee, 93.44% is within a distinguished segment B3.

The installation of the fiscal council is a more common practice in firm listed in distinguished segments B3 (64.01%) as opposed to only 35.99% of the traditional segment (p-value = 0.000, z-test). In the group of firms within distinguished segments, the proportion of firms that set up the fiscal council (66.52%) is also statistically superior to that of firms that do not install it (33.48%) (p-value = 0.000, z-test). Following the observed trend of adopting the various committees, among the companies that set up the fiscal council, 86.47% of them are listed in distinguished segments B3, in contrast to only 13.53% that are in the traditional market that do not have the fiscal council installed.

Regarding the fiscal council on a permanent basis, the picture is not statistically different between firms listed in the traditional market and the ones listed in distinguished segments. The vast majority of firms (71.16%) do not have a permanent fiscal council. And this trend is the same, whether among firms from the traditional market or from distinguished segments B3. Thus, it is seen that the resistance in having such a council in a permanent manner is still high for all firms. One possible explanation may be the replacement of the fiscal council by the audit committee.

The recommendation of no assessment for the fiscal council is followed by the great majority of Brazilian firms (96.01%) compared to a small group that adopts such practice (3.99%). Surprisingly, the small number of firms adopting this practice is from firms listed in distinguished segments B3, and this group of firms focused on the distinguished markets leads to a significant difference in the proportion of firms that do or do not perform this assessment (p-value = 0.001, chi2 test).

5 Final Considerations

This paper aimed to analyze the Brazilian firm's compliance with good corporate governance practices. For the analysis, the main corporate governance codes published in the Brazilian market were used as benchmark, with emphasis on the IBGC document. It was found that, in fact, there is a trend of Brazilian firms to seek to improve their corporate governance system quality through the adoption of good practices, although there is still a possibility of progress. In this context, it should be mentioned that there is a high proportion of firms with an audit committee and fiscal council, there is a higher proportion of firms that perform evaluation of the executive board and board of directors, and also a higher proportion of firms that do not allow duality between CEO and Chairman of the Board. In addition, only a few firms still have substitute members for the board of directors. The average tenure of board members, the size of the board of directors, the tenure of executive board members, the size of the audit committee, and the proportion of the audit committee members who are directors are consistent with the reference values recommended by the Brazilian Good Corporate Governance Practices Codes. It should also be mentioned the increasing adoption of more advisory committees to the board of directors. These results allow, in response to the presented research problem, to consider that, as a whole, the Brazilian firm presents a trend to adopt a set of good corporate governance practices recommended by the Brazilian market.

Naturally, there is space for improvement, as can be seen in the possibility of further implementation of audit committees and permanent fiscal councils. There may be an increase in audit committees in Brazil to the detriment of fiscal councils. The independence of members of audit committees also deserves to be increased. Similarly, the female presence on the board of directors can also be increased. The growth of advisory committees of the board of directors may also contribute to improving the corporate governance process of the Brazilian firm.

The argument that better corporate governance can stimulate its constant improvement found support in the process of comparing the degree of adherence to good corporate governance practices between firms listed in the traditional market and the ones in distinguished segments B3. In fact, firms that have voluntarily adhered to stricter corporate governance rules, through a contract with B3 to be listed at distinguished segments B3, tend to continue to improve their governance system through voluntary practices, while firms that do not firm such contract are less inclined to this, remaining listed in the traditional market segment. Such a propensity for the continued process of improving corporate governance may be due to the perception that, in fact, the proposition that there is a favorable cost-benefit relation in adopting corporate governance is true, generating benefits such as value creation and better economic financial performance. The set of results allows us to consider that the set of Brazilian firms is in the process of aligning their governance system to the best practices recommended by the Brazilian market and that this process is more intense in firms listed in distinguished segments.

It is considered that this paper contributes to studies on corporate governance in the Brazilian market by evaluating in detail the current scenario of Brazilian corporate governance, as well as indications about the effectiveness of codes of good governance as a form of soft law. The results obtained here on the scenario of good corporate governance practices of the Brazilian firm allow us to have this general view that points to this trend of compliance with the set of recommended practices which is important for academics interested in Brazil and corporate governance, as well as for market professionals, managers and business owners. Firm owners and managers can attend to this situation and prioritize the process of improvement of their firms' governance since the competition is strong and it is not recommended that a firm behave far from its competitors in relation to its set of management practices and governance.

As future work perspectives, we envision the possibility of evaluating specific determinants of certain practices that may be more associated with firms with peculiar characteristics. It is also interesting to evaluate the effects of specific governance practices on the firm's performance or financing capacity. Within the context of research on corporate governance assessment, it is also possible to evaluate the relevance of these practices, more recommended and adopted, within the corporate governance indices.

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