



IN SEARCH OF COOPERATIVE GOVERNANCE: A BRAZILIAN AGRICULTURAL CO-OP CASE STUDY

DANIELA MARIA POZZOBON

PhD Student at the University of Sao Paulo (USP), Brazil
Address: Rua Bela Cintra, 450/ap. 45, Cep 01415-000
São Paulo, SP, Brazil
Phone: (55) 11 9931-1559
E-mail: danielap@usp.br

CLÁUDIO ANTONIO PINHEIRO MACHADO FILHO

Professor of the Business Program at the University of Sao Paulo (USP), Brazil
And Director of Consulting Projects at PENSA (Agribusiness Intelligence Center)
Address: Av. Prof. Luciano Gualberto, 908 – FEA-1, Sala C-14, Cep 05508-900
São Paulo, SP, Brazil
Phone: (55) 11 3818-4005 – Fax: (55) 11 3091-5905
E-mail: capfilho@usp.br

Abstract

This research presents a brief discussion on governance and ethical behavior in cooperatives whereas more recently the cooperatives have faced survival challenges as a result of the governance problems and the governance of cooperatives is relatively under theorized in comparison with the governance of business corporations, where there is a large literature on corporate governance. Regarding even the answers for these problems have been not concluded yet in the private companies it is excellent that we think about governance inside of the cooperatives which are responsible companies for significant contribution in the economy of the countries. The chosen branch was the agricultural whereas this is one of the branches with bigger number of cooperatives and membership in Brazil it plays important role in the Brazilian economy and its participation in the Gross Domestic Product are important. The analyzed cooperative has a historical of almost fifty years of increasing development. Recently, however, the COTREL faced challenges of survival as resulted of the problems of ethical behavior of the members and the lack of mechanisms of governance.

Key Words: *Corporate Governance, Ethical Behavior, Agricultural Cooperatives.*



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1. Introduction

Brazilian agricultural cooperatives represent an important economic role in market economies. As per Brazilian's Cooperative Organization data available from year-end 2006, they numbered 1,549 with a total of 886,076 memberships and 123,890 employees (OCB, 2006). More recently, however, cooperatives, and in particular farm cooperatives, the subject of this study, have faced survival challenges as a result of governance problems such as mismanagement, unethical behavior, financial scandals or a failure of democracy. That has led to a questioning of their governance quality. The problems confronted by listed companies are great and are topics en vogue in business schools and firms. More than this, other companies, such as the non-listed familiar, cooperatives, organizations of the third sector, are faced with problems as important as those of the listed companies and they have not been recognized. In special, cooperatives possess particular characteristics as organizational forms which make them fragile in this regard.

It is important to analyze cooperatives that have had prominence insofar as they constitute an organizational form with particular characteristics, also being worth special studies. Cornforth (2004) evaluates that more studies are required to deal with the governance in cooperatives because, as the author points out, the debate on the governance of cooperatives in particular is relatively under theorized in comparison with that on business corporations, whose literature on corporate governance is large. As Zylbersztajn (2006) suggests, it is important to discuss the governance of cooperative organizations, whose problems of agency are still more sensitive than those of publicly traded firms. The example of agricultural cooperatives indicates the relevance of the theme, mainly as it involves thousands of farmers whose right of decision is unitary, not dependent on the cash flow generated for farmers in the cooperative.

1.1 Objective

In front of the evidences this study presents a brief discussion on governance and ethical behavior in cooperatives and its objectives to point problems about this in cooperatives. The chosen branch was the agricultural whereas this is one of the branches with bigger number of cooperatives and membership in Brazil it plays important role in the Brazilian economy and its participation in the Gross Domestic Product are important.

2. Literature Review and Theoretical References

2.1 Cooperatives

As the Cooperative Development Institute (2006) describes, "a cooperative is a business owned by its customers or its workers". This Institute affirms that cooperatives are characterized by the Rochdale Principles, named after the first successful cooperative started in Rochdale, England in the 1840's, of which a paraphrased version follows:

- *Open membership* - a cooperative does not discriminate. Anyone can join;
- *Democratic control* - the cooperative is owned and operated by its members. Each member gets one vote (unlike publicly-traded companies in which the member buys the most part of the stocks to reach the most votes);



- *Limited return on capital* - a cooperative does not intend to be a money-making enterprise for its members. Members may thus be paid only a "limited" amount of interest on any money they invest (most cooperatives have a very modest investment requirement);
- *Surplus belongs to members* - since the members are the owners, they receive any profit the cooperative makes. In many cooperatives the profits are reinvested into the business rather than being returned to the members;
- *Honest business practices* - cooperatives deal openly, honestly, and honorably with their members and the general public;
- *Ultimate aim is to advance the common good* - the ultimate aim of all cooperatives should be to aid in the participatory definition and the advancement of the common good.
- *Education* - cooperatives are expected to educate their members, officers, and employees and the general public in the principles and techniques of cooperation, both economic and democratic;
- *Cooperation among cooperatives* - cooperatives should actively cooperate in every practical way with other cooperatives.

The definition of the International Cooperative Alliance (2006) is the following: "a cooperative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise". According to Herbst and Prüfer (2005), "cooperatives resemble firms regarding the ability to pay out dividends, but they also have elements of a nonprofit as its members not only care about dividends but also have an interest in consuming the cooperative's good or service. Thus members have both their expected consumer surplus and the organization's revenues to finance operations. They hold both residual rights of income and control".

Specifically regarding this definition of agricultural cooperatives, Staatz (1987) considers they are defined as a business with the following characteristics:

1. the stockholders, who are farmers, are the major users of the firm's services;
2. the benefits a stockholder receives from committing capital to a cooperative are tied largely to patronage. There are three reasons for this: (a) the business pays a strictly limited dividend on equity capital invested in the organization; (b) net margins are distributed among stockholders in proportion to their patronage with the business rather than in proportion to their equity ownership in the firm; (c) stock of cooperative firms does not appreciate because there is a very limited or nonexistent secondary market for it. Therefore, capital gains are not a major benefit of stock ownership in cooperatives, in contrast to investor-owned firms;
3. the formal governance of the business by the stockholders is structured "democratically" in the sense that: (a) voting power is not proportional to equity investment. The limitation on "voting one's equity" may be in the form of one-member/one-vote rule, or voting may be proportional to patronage or stock ownership but subject to some limit such as restricting any one member from having more than 5 percent of the total votes; (b) there are strict limitations on the number of non stockholders who may serve on the board of directors.

Also considering farm cooperatives, Zylbersztajn (1994) cites some existing distinctions between their members and shareholders of non-cooperative companies:

- co-op members can have their income strongly connected to the cooperative or the latter can be seen as a channel of commercialization for their product, among other possibilities. In many cases, the cooperative is in fact the only channel for draining their products;



• by and large, the income of the membership does not depend significantly on the surplus at the end of the exercise period. part of this surplus is restrained by law, being limited the access of the membership to it, even in case of disconnection from the membership;

• company shareholders, even being minority, are interested in the corporation's performance, in which, in general, he does not conduct businesses. in conclusion, their return depends both upon capital valuation and eventual profits to be distributed;

• their shares provide great liquidity, especially in publicly traded companies. Differently from the membership, shareholders can leave the society at any time at minimum costs.

Machado Filho (2006) affirms that a cooperative has the following characteristics:

• it is a society of people where each member has the right to a single vote;

• residual property rights tend to be dispersed since all the members are partners;

• membership income arises much more from sale of products rather than from eventually distributed "surplus" at the end of the exercise. such fact results in less incentive for those so-called "principals" (members) to monitor the actions of the called "agents" (managers of the cooperative);

• at the same time (and contradictorily) members are owners and customers of the cooperative, which often gives rise to internal conflicts. for example, if on the one hand, they wish the highest possible price in the sale of his product, on the other hand, they ask for the lowest one in the acquisition of inputs;

• the strategic route can shift in each election because the directors' election is based on proposals and promises;

• the board gains importance in the governance of these organizations due to the fragility of the other forms of monitoring their activities. Despite this, this participation as a tool of control is less effective than in business-oriented companies. In addition, few of them act during out of the crisis moments. There is just little motivation of its members to monitor the organizations' results. Furthermore, its composition hardly takes into account the technical qualification and the representation of stakeholders.

2.2 Corporate Governance

As displayed by Tirole (2006), in 1932 Berle and Means (1932) wrote a path-breaking book documenting the separation of ownership and control in the United States. They showed that shareholder dispersion creates substantial managerial discretion, which can be abused. This was the starting point for the subsequent academic thinking on corporate governance and corporate finance. Subsequently, a number of corporate problems around the world have reinforced the perception that managers are unwatched. Most observers are now seriously concerned that the best managers may not be selected, and that managers, once selected, are not accountable.

In accordance with Tirole (2006), the topic of governance of corporations has attracted much attention in the past decade. Increased media coverage has turned "transparency", "managerial accountability", "corporate governance failures", "weak boards of directors", "hostile takeovers", "protection of minority shareholders" and "investor activism" into household phrases. Severe and constant agency problems impair corporate performance both in companies with strong managers and dispersed shareholders (as is frequent in Anglo-Saxon countries) and those with one controlling shareholder and minority shareholders (typical of the European corporate landscape).



To explain what it is understood in literature by “agency problems”, we need to deal with the concept of separation of ownership and control in companies (FAMA and JENSEN, 1983), which demonstrated the clear possibility of the decision agents do not bear the ownership of the corporation. Soon, if decision makers do not suffer the full impact of their decision, that will create a problem. This situation was referred to by economists as “agency problem”; shareholders were called “principals” and managers “agents” (ZYLBERSTAJN in MACHADO FILHO, 2006). In Fama and Jensen’s (1983) view, when organizations are more complex, they start to need specialized information. By reason of this fact, a contractual arrangement occurs to manage them. As a result, the implementation of the control becomes necessary, i.e., they set up a mechanisms for monitoring the managers to prevent them from harming shareholders.

But what is corporate governance? As Tirole (2006) points out, the dominant view in economics, articulated for example, in Shleifer and Vishny’s (1997) and Becht, Bolton and Röell’s (2002) surveys on the topic, is that corporate governance relates to the “ways in which the suppliers of finance to corporations assure themselves of getting a return on their investment”. In addition, it is concerned with the ways in which a corporation’s insiders can credibly commit to return funds to outside investors and can thereby attract external financing. This definition is, in Tirole’s (2006) analyses, of course, limited. Many politicians, managers, consultants, and academics object to the economists’ narrow view on corporate governance as being preoccupied solely with investor returns; they argue that other “stakeholders” such as employees, communities, suppliers, or customers, also have a vested interest in how the firm is run, and that these stakeholders’ concerns should somehow be internalized as well.

Therefore, in accordance with Clarke (2004), the significance of corporate governance for stability and equity of society is captured in the broader definition of the concept offered by Cadbury (2004): “corporate governance is concerned with holding the balance between economic and social goals and between individuals and communal goals. The governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals, corporations and society”.

The Brazilian Institute of Corporate Governance (2004) defines corporate governance as “the system in which the organizations are led and monitored, involving the relationships between shareholders, board of administration, direction, independent auditing and fiscal board. Its *Code of Best Practices of Corporate Governance* has the purpose to increase the value of the corporation, to facilitate its access to the capital and to contribute to its survival”.

Corporate Governance, as defined by the Brazilian Securities and Exchange Commission (2002) is “the set of acts with the purpose to optimize the performance of a company when protecting all the interested parts such as investors, employees and creditors, facilitating the access to the capital. The analysis of the “Best Practices of Corporate Governance” applied to the stock market involves mainly: transparency, equity of treatment of the shareholders and accountability”. The Brazilian Securities and Exchange Commission (2002) goes beyond the definition of the term to offer the following benefits companies can attain by using of Corporate Governance:

- *Viable alternative for capitalization* - the analysis of the practices of governance allows investors to make better investment decisions since governance determines the way and extent to which they can act in a company, thereby making it possible for them to influence it. The objective is to increase the value of the company since good practices of



corporate governance re-echo in the reduction of its cost of capital. That increases the viability of having the stock market as alternative of capitalization;

- *Protection against asset looting* - when investors finance the company, they are exposed to risking part of the profit of their investment to improper appropriation by majority shareholders or managers of the company. The adoption of good practices of corporate governance also constitutes a set of mechanisms through which investors, including majority shareholders, protect themselves against asset looting by individuals that have the power to influence or make decisions on behalf of the company;

- *Valuation of the company* - companies that have a governance system that protects all their investors tend to be more valued because investors recognize that the return of the investments will be equally made good use by all of them.

According to Tirole (2006), there are various ways in which the managers may not act in the firms' (their owners') best interests. For convenience, this author divides these into four categories, albeit readers should keep in mind that all of them are fundamentally part of the same problem. They are generically labeled by economists as "moral hazards", and comprise insufficient effort, extravagant investments, entrenchment strategies and self-dealing.

In his opinion, the overall significance of moral hazard is largely understated by the mere observation of managerial misbehavior, which forms the "tip of the iceberg". The submerged part of the iceberg is the institutional response in terms of corporate governance, finance and managerial incentive contracts. Yet, it is worth reviewing some of the recent controversies regarding dysfunctional governance. Several forms of dysfunctional governance have been pointed out as lack of transparency, level, tenuous link between performance and compensation, and accounting manipulations.

Following this line of thought, the Brazilian Institute of Corporate Governance (2004) enumerates the following four principles of corporate governance:

- *Equitable treatment* - it is characterized by fair and equal treatment of all minority groups, whether of owners or stakeholders, such as employees, customers, suppliers or creditors. Discriminatory attitudes or policies, under any pretext, are entirely unacceptable;

- *Responsibility* - council members and executives must watch over for the survival of organizations (vision of long term, sustainable organization) and, therefore, they must incorporate order considerations of social and environmental issues in the definition of the businesses and operations. Corporative responsibility is an ampler vision of the enterprise strategy contemplating all the relationships with the community where the society acts. The "social function" of the company must include wealth creation and job opportunities, qualification and diversity of the work force, promotion of scientific development through technology and improved standards of living by means of educational, cultural, social and environmental actions. The preferential act of contracting resources (work and inputs) that are offered by the proper community is included in this principle;

- *Transparency* - more than the "obligation to inform" the management must cultivate "desire to inform", knowing that good internal and external communication, particularly when spontaneous, frank and fast, results in a confident atmosphere, both internally and in the relations of the company with others. The communication does not have to be restricted to the economic and financial performance, it must also contemplate other factors (included the intangible) that guide the actions of the enterprise action and lead to value creation;

- *Accountability* - the agents of corporate governance must render accounts of their performance to those who elected them. Moreover, they must fully answer for all the acts they practice throughout their terms of offices.



2.3 Governance of the Cooperative Organizations

As analyzed by Lees (1995), Lees and Volkers (1996) and Cornforth (2004), mirroring developments in the private sector, a variety of problems have occurred in different cooperative societies across Europe, such as mismanagement, financial scandals and a failure of democracy. This has raised questions about the quality of governance within cooperatives. Cornforth (2004) adds that serious concerns have been raised about the democratic legitimacy of boards. Both the low levels of member participation and their effectiveness account for this fact, allied to the lack of expertise in effectively supervising senior managers, ensuring honor and protecting the interests of members and other relevant stakeholders.

Cornforth (2004) affirms that concerns like these have led to increased interest of professionals and academicians in organizational governance as well as to the growth of the body of literature and advice. Much of this literature has been prescriptive in nature and aimed at addressing the perceived shortcomings of governing bodies. Demb and Neubauer (1992), who have studied this subject, identified and examined three paradoxes which stem from the legal and structural aspects of the boards' formation. The first is "who governs", i.e. the tension between representative and expert boards. The second is "board roles", i.e. the tension between conformance and performance. The last one is "relationships with management", i.e. the tension between controlling and supporting.

Sundaramurthy and Lewis (2003) examine the paradox that boards face between controlling and empowering management. They recommend that organizations may experience a cycle of decline if boards put too much emphasis on control and not on collaboration. They suggest that too much stress on collaboration and partnership can lead to groupthink where management ideas and strategies are not adequately scrutinized and challenged. This can lead to strategic persistence in good times and a cycle of organizational decline as performance deteriorates.

Cornforth (2004) analyses that a variety of competing theories have been proposed to try to understand the role of boards in the private sector. Each implies a different model of how boards work and who should serve on them. He examined each of these theoretical perspectives and associated models. At the same time, the author analyzed how they can be usefully extended to throw light on the role of cooperative boards. He proposes that the theoretical boards that deal with the subject of governance come from six different sources. The perspectives that are studied by the many authors of the subject are Agency Theory, Stewardship Theory, Resource Dependence Theory, Stakeholder Theory, Managerial Hegemony Theory, and the Democratic Perspective, which the author includes and affirms that provides the dominant perspective over the role and practices of boards in cooperatives.

- *Democratic Perspective* - this theory considers that the job of board members is to represent the interests of the members of the organization. The role of the board is to resolve or choose between the interests of different groups and set the overall policy of the organization, which can then be implemented by the staff. The main point of this view is the idea of a non-professional board where anyone can stand for election as a board member. Expertise may be desirable but is not a central requirement, as it is in some other perspectives on governance;

- *Agency Theory* - the Agency Theory (JENSEN and MECKLING, 1976) suggests that a majority of directors of companies should be independent of the board. Even more, their primary role is to ensure the managerial compliance, i.e. to monitor and if necessary to control the behavior of management to ensure their acts in the shareholders' best interests. For cooperatives, as Cornforth (2004) analyzes, the board is the most important way that members



have to control managerial behavior, but at the same time this board has to operate in a context where it is likely to be more difficult to exert influence;

- *Stewardship Theory* - this theory proposes that senior management and shareholders (or members, in the case of cooperatives) are better seen as partners. Hence, the main function of the board is not to ensure managerial compliance with shareholders or members' interests, but to improve organizational performance. The role of the board is primarily strategic, but it also works with management to improve strategy and add value to top decisions. In this context it is not surprising that management ideas and practices should be applied to governance. From this perspective, board members should be selected on the basis of their expertise and contacts. Therefore, they are in a position to add value to the organization's decisions. Boards and managers should receive appropriated information, training and know-how to operate effectively as a team. In relation to this theory, observing the differences of the cooperative organizational form, Cornforth (2004) cites Sivertsen's work (1996) which affirms that there is no guarantee that those members elected to the board will have the skills that the board needs to be effective;

- *Resource Dependence Theory* - from the standpoint of this theory, the board is seen as a way of reducing uncertainty by creating influential links between organizations through, for example, interlocking directorates. The main functions of the board are to maintain good relations with key external stakeholders in order to ensure the flow of resources into and from the organization, and to help the organization respond to external change. From this perspective the board is part of both the organization and its environment. The role of the board is one of spanning boundaries. Board members are selected for the importance of their external links and the knowledge they can bring to the organization, and their attempt to seek external cooperation;

- *Stakeholder Theory* - from this perspective the board is characterized for incorporating different stakeholders. It is expected that organizations will be more likely to respond to broader social interests than the narrow interests of one group. The political role for boards is to negotiate and to resolve the potentially conflicting interests of different stakeholder groups in order to determine the objectives of the organization and set policies;

- *Managerial Hegemony Theory* - from this perspective the board ends up as little more than a "rubber stamp" for management's decisions. This function is essentially symbolic to give legitimacy, legality, validity to managerial actions. Berle and Means' (1932) thesis on the question of the separation between property and control in the organizations cites that although shareholders may legally own and control large corporations, they no longer effectively control them. Thus control has been ceded to a new professional managerial class. In addition, Cornforth (2004) makes reference to some works on this subject. Mace (1971), in his study of U.S. directors, concluded not only that boards did not get involved in strategy except in crises, but also that control rested with the C.E.O. rather than the board. Herman (1981) came to similar conclusions but argued that managerial power was always in the context of various constraints and the latent power of stakeholders such as external board members. Lorsch and Maciver (1989) concluded that although the functioning of boards has improved since Mace's study, their performance still leave much room for improvement.

3. Research Methodology

This research used a methodology approach of qualitative character. According to Malhotra (2001), it "provides the better vision and understanding of the context of the problem". For this author, the qualitative research is a methodology of non-structuralized and



exploratory research which is based on small samples that provide insights and an ampler understanding of the problem's context.

The method adopted for the development of this research was the case study proposed by Yin (1994) which can investigate contemporary phenomena within real contexts especially when the limits between the phenomena and the contexts are not clearly defined.

The sampling technique used was that of sampling judgment. According to Malhotra (2001), this technique is a non-probabilistic form of sampling for convenience, in which elements of a population are selected on the basis of the judgment of the researcher. In this case, the chosen branch was the agricultural, insofar as it is one of main representative branches of the Brazilian cooperatives. The case chosen for this study is that of the Erechim-based Wheat Growers Cooperative Limited (COTREL), in the state of Rio Grande do Sul, Brazil.

The data collection was carried out through documentary research on the Website of the cooperative and electronic publications from the governmental institutions pertinent to the objective of this study.

4. Results

4.1 Case Research: COTREL – Erechim Growers Wheat Cooperative Limited.

4.1.1 Brief Operating History of the COTREL

Erechim Wheat Growers Cooperative Limited (COTREL) is an agricultural cooperative located in southern Brazil. It was founded on September 25, 1957, in the city of Erechim. This cooperative arose from the need of agricultural producers to store and commercialize their products, mainly wheat, at that time the biggest crop grown in the cities around this cooperative.

Today, COTREL operates in thirty nine municipalities of the northwestern region of "Rio Grande do Sul" (Brazil's southernmost state) and, besides its head offices, it has nineteen branches. It counts on approximately 13,400 members, mostly comprising small growers.

COTREL not only industrializes and distributes products from farmers, but also adds value to their agricultural production. From this level, this cooperative supplies their products across the country. Its product line includes over two thousand items, such as derivatives of swine, beef, chicken, milk, artichoke and industrialized fruit.

COTREL undergoes continuous transformation through the implementation of advanced technology and product diversification. COTREL is considered the greatest agricultural cooperative in Rio Grande do Sul.

COTREL's history over the decades can be highlighted by the following events:

- *At the end of the 1950s to the beginning of 1960s* - start the activities of the cooperative for the necessity to join the producers during the cycle of the wheat;
- *1970s* - consolidation of the culture of the soy and construction of branch offices not only to receiving agricultural production but also to selling inputs as well as sorts of first necessity as well;
- *1980s* - introduction of the system of integrated production of chicken and swine with the acquisition and remodels of two industrial units for the processing. The maize culture was intensified;
- *1990s* - the COTREL not only continues high in its current activities but also increases much more the production and industrialization of swine and chicken. It also starts operating with milk, fruit, vegetables and reforestation;



• 2000s - in the northwest region of the "Rio Grande do Sul" approximately 80% of the producers are members of the COTREL. These members possess a set of advantages. In first place, the guarantee of commercialization of their production which is the main advantage. Likewise, the technician accompaniment and the supply of inputs as well;

4.1.2 Governance and Ethical Behavior at COTREL

According information from the state legislature of Rio Grande do Sul, the Judge of First Criminal Court of Federal Justice, in the city Porto Alegre city, received the denunciation from the Office of the Attorney General of the Republic involving ten people (among which directors of the COTREL and a group from São Paulo city comprising lawyers, accountants and dispatchers) for crimes against the National Financial System and for "money laundering".

Auditors of the National Social Security Institute (INSS) had evidenced the existence of counterfeited social security contribution payment slips used by the cooperative to renegotiate debts together with the agency. Not only the president of the Cooperative but also former-directors as well as the former legal advisor were among the denounced people.

In accordance with the Attorney General, COTREL obtained financing of a little over US\$ 8,5 million and a member of the group would have "washed" about US\$ 3 million with the purchase of economic goods for himself. Among the goods apprehended by the Federal Police are some immovable and cars.

A state representative recommended joining forces among all of the sectors of the society not only to select causes of and responsibility for this crisis, but also to create a recovery plan for COTREL, which provides jobs for over three thousand employees. COTREL answers economically for approximately sixty thousand people who are its associates, besides its employees and dependents. On June 6, 2005, in the tribune of the State legislature of the Rio Grande do Sul, a state representative called for a federal inquiry into COTREL, now undergoing severe financial and administrative crises. For the time being, according to the state representative, "the management is urged to tell the truth to it members and an official task force must find out the causes of and the responsibility for this almost unpayable debt".

The parliamentarian said that the information is still contradictory. At any rate, he informed that COTREL owes approximately US\$ 140,5 million to banks, producers, Social Security, Guarantee Fund for Length of Service, public power and suppliers. From the standpoint of this state representative, "even confronted with this critical scenario, all of the sectors of the region are convinced that the cooperative cannot declare insolvency". He also alerts that the twelve thousand family farmers associated with COTREL cannot be made responsible for attitudes of the management and for debts they are not aware of. He defends that "without a serious investigation to find out those responsible, we cannot allow that responsible, this is debited from the account of employees who pay with their dismissal or of associated farmers".

According to Parliamentarian's estimates, each member would have to pay US\$ 1,8 a thousand per year for twenty years to pay off the debt of US\$ 140,5. He affirms "it is not possible to settle an account that the farmers have not generated just because of the reckless management that did not have the courage to come forward to explain the true causes of the crisis". COTREL purchases and sells the main products of familiar agriculture: grains, milk and meat, representing 45% of the Gross Domestic Product of the region, as he points out. He participated in a meeting in the city of Erechim gathering four hundred leaders concerned with this scenario. The cooperative's associates who were present revealed their frustration for being the last to learn about the gravity of the problems of the organization.



COTREL's next C.E.O. hired a consultant who will be responsible for the recovery plan. He made a detailed communication of the measures put into practice while the consultant presented the strategy. To initiate, he explained that many factors contributed to shake COTREL financially. In his words, "all possible measures were taken and when our knowledge exhausted we hired an expert". "The expert has graduated in engineering and administration in the United States and specializes in diagnosis of companies in the same situation as COTREL.

5. Conclusions and suggestions for future research

The analyzed cooperative has a history of almost fifty years of constant development. Recently, however, COTREL faced a survival challenge resulting from problems of ethical behavior of the members and lack of governance mechanisms. Directors of the cooperative needed resign and were denounced for crime of expropriation. Moreover, they left the cooperative with high debts with banks, rural producers, government funds, public power and suppliers.

Scandals and expropriations demonstrate that control and ethical behavior are extremely important issues. The cooperative members were the last to know about the crime. Nevertheless, they also lacked ethical behavior while proprietors of the cooperative. Ethical behavior entails an attitude to intervene with the events, to take position, to move. Furthermore, it means not to act with indifference since the indifference generates disregard to others. Soon, the members will need to think more collectively.

An intelligent way to look at this subject is through the Theory of Constraints. In the future, organizations will be studied as a set of flows being managed one at a time. It is necessary for us to perceive that there is a restriction in each flow. When a restriction is always in the same place, it destroys the union and the culture of the company. And when the restriction of the company is the power, the way to undermine it is through governance.

In agricultural cooperatives, thousands of producers are usually the last ones to know when scandals such as the one related here happen, especially because they do not have incentives to monitor the agent of the cooperative. The main reason for this, by and large, is that the income of the producers derives to a greater extent from their products than from the eventual "distributed leftovers" at the end of the exercise. Soon, this fact results in little incentive for "principals" (members) to monitor the actions of the so-called "agents" (members elected to manager the cooperative). When this happens, producers suffer a great impact since they often have the cooperative as the only channel for draining their products.

Nonetheless, research shows that not only boards do not get involved in strategy except in crises but also that control remains with the director (C.E.O.) (MACE, 1971). Managerial power was always in the context of various constraints and the latent power of stakeholders such as the external board members (HERMAN, 1981). More than this, there is no guarantee that those members elected to the board will have the skills that the board needs to be effective (SIVERTSEN, 1996).

In case of the cooperatives, there is neither technical capacity nor incentive for monitoring because the cooperative is a property of the member. The executives (or "agents") are elected members in accordance to the democratic principle that conducts the cooperatives "one man, one vote" and the board mostly acts in the cooperatives just in critical moments.

The problems occurred at COTREL demonstrate that the conjunction not only of the cooperative's principles and particular characteristics, but also of weak mechanisms of



governance resulted in two convergent aspects: an inexistent or almost inexistent control and a lack of ethical behavior of the members.

Cooperatives are not yet used to (for representing a society of people, and without shares in the market) adopting "Best Practices of Corporate Governance". Soon, the basic principles of these Best Practices which include *transparency*, *equity*, *responsibility* and *accountability* are not argued and adopted internally in these organizations. As Zylbersztajn (2006) suggests, it is imperious to remember, however, that "some of the companies who were stage of scandals have been awarded prizes of corporate excellence in governance".

In publicly traded companies, the motivation driving the thought and the use of the Best Practices and the structure of corporate governance is the market, i.e. the valuation of the shares in the market. On the other hand, in cooperatives with particular characteristics, the motivations can even be the very principles of the cooperative. So, if the cooperative acts with transparency, equity, accountability and corporate responsibility, as the corporate governance proclaims, it will reach its cooperative principles easier than if it remains in the market. Thus, if on the one hand it is a company without shares in the market, on the other hand it is inserted in the market economy where it needs to find a competitive positioning.

As suggestions for future works, we recommend as crucial in accordance with Cornforth (2004), not only more studies examining how the influence of the contextual factors impact the board, but also more comparative studies that systematically compare governance in different sectors of organizations and fields of activity. Furthermore, it is extremely important to examine the differences in the composition, roles and relationships of the board. We need to better understand and to examine organizational factors such as the influence of the organizational size and nature of board. Without a doubt, more longitudinal case studies are necessary that examine the dynamics of the relationship between board and managers, and how they try to face their problems. Above all, we suggest that it is necessary to conduct fundamental research aimed at answering the following question: how should governance be treated in organizations of collective property, such as the cooperative form of organization?

6. References

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