CORPORATE GOVERNANCE IN LUSO-BRAZILIAN NAVIGATION, TRADE, AND SLAVE-TRAFFICKING COMPANIES OF THE 18TH CENTURY.

Abstract

This article revisits historical interpretations regarding the evolution of corporate governance practices of the first two Luso-Brazilian navigation, trade, and slave-trafficking companies that were founded in the northern and northeastern regions of Brazil – the Companhia Geral do Grão-Pará e Maranhão and the Companhia Geral de Pernambuco e Paraíba – during the mid 18th century. Historical facts allows to better understand the establishment and refinement of corporate governance practices, which can be attributed to the changes in the company’s socio-economic arena and to internal factors such as the broadening of the rights of minority shareholders.

Keywords: Corporate Governance, Grão Pará and Maranhão General Trading Company, Pernambuco and Paraíba General Trading Company.

Introduction

This article develops a historical revision of the evolution of corporate governance practices in the two navigation, trade, and slave-trafficking companies active in the Brazilian north and northeast in the mid 18th century.

Corporate Governance (hereafter, CG) refers to the monitoring and control systems put in place to ensure that decisions by managers and owners regarding allocation of resources are aligned for the purpose of sound entity management (Jensen & Meckling, 1976; Fama & Jensen, 1983; Sleifer & Vishny, 1997). The dissociation between property and effective capital control permeates the corporate governance debate on various economic fronts. This conflict was addressed by both Smith (1776), in the mercantilist context, and Berle and Means (1932), with the contemporary capitalist scenario as an analytical point of reference. The set of difficulties that the “firms” encountered in both economic circumstances, taking into account the singularities of each historical context, required the adoption of measures meant to reestablish balance.

The manner in which the companies are managed is a result of a set of habits, procedures, and techniques that were developed in the past, being linked to a nation’s culture and society. According to Zubiri (1963), what we are today is the grouping of possibilities that we possess because of what we were yesterday. Consequently, the historical analysis of entities can provide information for a contemporary debate on this subject (Lloyd-Jones et al., 2005; Maclean, 1999).
The separation of property and control and its subsequent effects were also a reality experienced by the first incorporated Brazilian companies as early as the mid 18th century. The administration of the Marquis of Pombal saw the creation of two companies active in the Brazilian north and northeast: the Companhia Geral do Grão Pará e Maranhão (hereafter, CGPM) and the Companhia Geral de Pernambuco e Paraíba (hereafter, CGPP). An analysis of companies’ documents allows for an identification of traces of what is known now in literature as CG practices.

Framework

The assessment of governance practices in a historical framework – the research purpose of this work – is still a nascent topic (Toms & Wilson, 2003). Among the studies focusing on colonial Brazil, two are worthy of note: the pioneering initiative of Rodrigues et al. (2007), who analyzed the statutory minutes of the CGPM; and the comparative analysis of Santos et al. (2008) of the statutory minutes and the final, approved version of the statute of that company. Based on that first evidence, this study aims to broaden the scope of the analysis by including other CGPM documents as well as CGPP ones, making possible to observe “standard” CG practices adopted by privileged Portuguese trade companies active in Brazil.

Despite being novices, authors like Lloyd-Jones et al., (2005) mentioned the relevance of analyzing governance practices from a historical perspective. Maclean (1999) argues that, in this context, matters such as board selection, board performance, familial control, and shareholder maneuvers can contribute to the current debate. Jong et al. (2006) have been developing a research project aimed at systematically analyzing the development of corporate governance during the entire 20th century by means of a sole group of data from Dutch companies, whose commercial paper was negotiated on the Amsterdam stock exchange. In order to address questions of efficiency and the long-term effects of different governance rules, that data is being linked to the performance of companies currently being studied.

The debate involving the CG topic emerges from intra-firm conflicts between agents. What is known in literature as CG is formed by the group of internal and external mechanisms that assures sustainability, the increase in social value, the securing of lower cost capital, organizational longevity, and corporate decision-making that maximizes the probability for investors (principals) of obtaining the best
return on their investment for themselves Governance practices enhance the credibility of firms vis-à-vis their investors in the international market, broadening the modalities of business financing. In this way, the companies avoid depending exclusively on internal financing or self-financing (Jensen & Meckling, 1976).

In addition, the presence of different types of shareholders (majority and minority) also sets the stage for conflict. The most common complaints from minority shareholders involve the lack of decision-making power and the reduced or non-existent participation of such shareholders in managing the company (Fama & Jensen, 1983).

La Porta et al. (1999) investigated the property structures of large companies in 27 countries and determined that few companies have their property scattered as described by Berle and Means (1932), except in large economies immersed in a common-law legal arrangement. In nearly every country analyzed, the companies that prevail are controlled by a small number of shareholders, whose voting rights usually supersede cash flow rights. Thus, the dialectic of CG mechanisms would no longer reside in protecting shareholder interest with respect to managers, but rather in shielding minority shareholders against possible expropriation by controlling shareholders. An understanding of the control structure is critical in demonstrating the nature of a potential branch problem in the management of the firm. Different property structures become different agency problems, which in turn require particular mechanisms to insure the well-being of the weaker component. In the next session, the two Luso-Brazilian companies’ structures are described.

The Case of the CGPM and CGPP Companies

The reign of Joseph I of Portugal was noted for its efforts towards administrative reorganization, economical and political restoration, aiming at aligning Portugal’s economy with then current European economic ideals. Notable among the initiatives taken was the rational exploitation of colonies, through trade carried out by companies wielding considerable capital during large part of the 18th century (Chaunu, 1978; Mauro, 1980, 1960).

As prime minister, the Marquis of Pombal established two companies in colonial Brazil: the CGPM, in 1755, and the CGPP, four years later, in 1759. The companies operated in the Brazilian north and northeast respectively. Their main objective was to reaffirm the colonial pact, discourage smuggling as well as British
influence, and integrate agricultural development in the colonies with industrialization in the kingdom (Carreira, 1983).

The two regions that each company operated were very different regarding economic development. Since the 16th century, Pernambuco, in the northeast, had an export-oriented economy that was important for the colony and its main trading product was sugar. Rio de Janeiro, Bahia, and Pernambuco accounted for 83.7% of Brazilian colonial exports to Portugal. Exports from Pernambuco also included tobacco and cotton. Moreover, extensive cattle farming made for a strong activity in the region. Under the operation of the CGPP, other northeast states (Paraíba and Ceará), despite being two of the three regions of lesser importance regarding overseas trade, had more significant export movement than the African colonies (Marques & Serrão, 1986).

On the other hand, the situation in the states at the north (Grão-Pará and Maranhão) was precarious. Agriculture was at a subsistence stage and labor was lacking. In that geographical area, for instance, the circulating form of currency until 1749 – in light of the shortage of numismatic metal – was cotton cloth and cocoa seeds. In 1751, the new captain-general of Grão-Pará and Maranhão, Francisco
Xavier de Mendonça Furtado, began demanding immediate measures to change the underlying crisis by sending a significant number of letters to the Marquis of Pombal (Dias, 1970; Salazar, 1991).

The CGPM was responsible for fomenting local production and trade, and centered its activities on ship building, cattle raising, cultivation of rice, cotton, coffee, cocoa, vanilla, etc., rice processing, exploration of salt deposits, slave traffic, and trade of products imported from Europe and Asia.

**An Analysis of the CGPM**

The social purpose of the company centered on monopolizing trade and navigation in the region of the state of Grão-Pará and Maranhão (§ 22) and in slave traffic (§ 30). The company received monopoly privileges for 20 years, subject to an additional 10-year extension (§ 51). Company capital totaled 1,200,000 cruzados\(^1\), divided in 1,200 stocks of 400$000 thousand réis each. The amount needed to purchase one share of stock was the annual salary of a Latin grammar professor in the captaincy of Pernambuco – one of the highest-paid positions in the school system (AHU_ACL_CU_015, Cx. 219, D. 14849).

In an attempt to protect company continuity, the statute included a social capital durability clause. That is to say, withdrawal of partners' stakes, once integrated, was not authorized while the company was in operation (§ 51). The statute, however, guaranteed shareholders the right to stock sale (§§ 50 and 51).

The issuance of capital at the CGPM was compulsory by popular subscribed. Stock integralization took place on a cash-only basis. A capital attraction policy is defined in § 39 through the concession of several privileges for people who entered the company with a minimum of 10,000 cruzados. These individuals would have, among other benefits, the possibility of acquiring a noble title, a status that exempted them from paying taxes.

There were three distinct shareholder categories. The holders of ten or more shares were in the most privileged class. They were the only ones eligible for the Board and their names had to remain concealed "in the secrecy of Company books" (§ 48). Below these, were the holders between five and nine shares. They have the

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\(^1\) The monetary unit was the *real* (plural *réis*, and abbreviated to *rs.*). To indicate one thousand *réis* a “$” sign was written, followed by three zeros. Thus, 2,000 *réis* was written as 2$000. One *cruzado* is equivalent to 400 *réis*. 

privilege to vote (§ 3). The last ones were the holders of less than five shares, who
could gather their resources to attain the total number of shares required to cast one
vote (§ 3).

Foreign capital was not excluded for the purposes of company capital
formation (§ 50). Foreigners were not, however, eligible for the right to hold
managerial posts (§ 2), although it was their prerogative as stakeholders to share in
earnings (§ 54). Nevertheless, the analysis cited by Dias (1970, p.230-234) of the list
of the company’s founding shareholders shows that of the 145 signatories few were
foreigners.

Company management was the purview of a Board made up of a
superintendent (president), eight deputies, a secretary, and three counselors (§ 1). Apart
from these, the remaining board members were to be native or naturalized
Portuguese, tradesmen, and reside in Portugal (§ 3), in addition to the
aforementioned minimum number of shares. The statute also mentions the length of
time spent in administrative positions. Except for the first board, which was the
responsibility of the king, all other such posts abided by the yearly system,
guaranteeing a rotating arrangement for company leadership (§§ 3 and 5).

The compensation system of company management positions was based
completely on variable remuneration contingent on fleet expeditions, as a way of
aligning the interests of the parties (§ 25). However, in 1760, the company replaced
variable-based payment to managers in the Bissau and Cacheu (African trade
communities) by a fixed yearly stipend of 1:200$000 reis.

The then governor of the state of Grão-Pará and Maranhão, Manuel
Bernardo de Melo e Castro, argued in on of his letters that the managers in Africa
sent ships with slaves that had no condition to work (AHU_ACL_CU_013, Cx. 43, D.
3958). Thus, the change in the type of remuneration was an attempt to avoid this
problem (Dias, 1970).

Dividends were distributed on annual basis, except for the first payment, which
was delayed for three years (§ 52). Moreover, there was a statutory arrangement for
the “examination of accounts”, what could be compared to a internal audit conducted
by two of the eight deputies (§ 6).

According to an internal regulation in the city of Belém do Pará, known as the
“Economic Directorate for Company Management”, at the end of each year,
managers were required to make a full list of items at farms and storehouses. The
bookkeeping process had to cover all merchandise. In addition, board members
demanded a list of unpaid debts, recognizing them at the balance sheet (Dias, 1970, p.271).

One item to be highlighted in the statute is the definition of a "private caretaker judge" (§ 7), who had to make decisions regarding all legal matters in which any company member was a defendant or a plaintiff – analogous to what is today known as a council of arbitration.

Despite the private nature of social capital, the CGPM enjoyed a semi-public identity, as the estate assets and the monopoly privileges were granted indirectly by the Crown. In other words, alongside the capitalist profile of satisfying partners' profit interests, there was also an obligation to take on governance tasks of colonial management in certain regions (Marcos, 1997).

The above-mentioned situation is aligned to the philosophy of an absolutist state. The company was not a simple commercial enterprise; it comprised a group of managers closely tied to the influential protection of the monarchy (§ 4). This contributed for the economic restoration of the Portuguese Empire (Mauro, 1980).

The state intervention in CGPM led to conflicts of interest, because some decisions were not the best ones for shareholders protection. For example, if farmers wanted to deal directly with Portugal and other markets, the CGPM had an obligation to send the goods free of charge § 19. Those conflicts are described by Smith (1776), Carlos (1991, 1992), Carlos and Nicholas (1988, 1990, 1993).

The general management principles were defined by the company's statute and other complementary documents addressed specific topics that had to the approved by the majority of all the shareholders (§ 6).

An Analysis of the CGPP

The CGPP was founded four years later that the CGPM and its statute followed the same principles of the first company. Thus, in this topic only differences between the two statutes will be addressed.

Regarding to the administrative structure of the analyzed companies, the CGPP presented a different structure from that of the CGPM, with a board and two administrative bodies. Based in Lisbon, the board consisted by a superintendent, ten deputies, one secretary, and three counselors. The administrative bodies were subordinated to the board. Each administrative body, one based in Porto and other in Pernambuco, consisted of one manager and six deputies. In terms of election for the
board, CGPP applied the same criteria of CGPM. The only difference was that minority shareholders could elect one counselor (§ 3). Thus, it is possible to observe an evolution of CG practices.

\[\text{Figure 2} \quad \text{CGPP administrative structure} \]
\[\text{Source}: \text{Adapted from Ribeiro Júnior (1976)}\]

The total amount of company’s capital was 3,400,000 cruzados, consisting of 3,400 shares (§ 53). One important difference from CGPM was that not only cash but also properties and goods at market value could be used to buy stocks (§ 54).

Despite the confidentiality requirement applied for both companies regarding the number of shares held by each individual, CGPP developed a different approach for the election. The electoral process began with the formulation of an alphabetical list of members, with two, one, or no asterisks preceding the name of a given shareholder. Individuals qualified to hold superintendent and deputy positions had two asterisks by their name. One asterisk identified isolated members who had voting rights. Shareholders without an asterisk did not hold a sufficient number of shares to vote. These individuals could make an agreement, summing up their stocks in order to have the right to vote (AHU_ACL_CU_015, Cx. 139, D. 10311).

The asterisk system thus identified who could vote and who could receive votes, while taking care not to display publicly the distribution of shares.
The appointment of the CGPP board and the auditing of accounts from the previous administration followed the same standards set by the CGPM. Remuneration for directors varied (§ 29); directors in Lisbon and Porto received 4% of the value of goods not only sent to the colony but also brought back. Superintendents in Pernambuco and Paraíba enjoyed a 2% markup on the value of goods sold in those markets. Because of unequal treatment, colonial directors sought to increase their commission. However, the board warned on August 29, 1760, that – as was the case with the CGPM – the directors would be replaced unless they accepted the commission established in the statute (Ribeiro Junior, 1976, p.108).
A “caretaker judge” (§§ 7 and 8) was also appointed to CGPP, but he was granted with a lifetime term, different from CGPM practices. The same privilege was later extended to the “caretaker judge” at CGPM (§ 9).

The founders of CGPP had additional rights to CGPM shareholders. They were exempted to fight in the war (§ 43) and had the right for passive retirement² (§ 44) (Royal Permit of January 31, 1818).

A minimum dividend of 5% of company’s profits was distributed every two years.

Conclusion

This work sought to expand on previous literature on corporate governance in a historical context by adding a new example of governance practices in Luso-Brazilian navigation, trade, and slave-trafficking companies of the 18th century. Their organization at the height of mercantilism presents a connection between property and control subsidized by governance practices in order to simultaneously address private and royal interests.

By comparing the CG practices between the two companies, it was possible to observe an evolution in CGPP regulations, based on its new privileges (to draw more large-scale shareholders, with at least ten shares) and the broadening of minority shareholders’ rights. In the first case, the result was the total integration of capital in only three years of operation by the CGPP, in contrast to the CGPM. In the second case, minority shareholders had the opportunity to participate in the company management process.

A letter from Governor Luis Diogo to the Marquis of Pombal explains the reason for including minority shareholders in company’s administrative bodies. In 1757, before the foundation of CGPP, the governor announced his intent of establishing a company in Pernambuco with an identical purpose of CGPM and in which control of 75% of the capital would be controlled by local merchants (AHU_ACL_CU_015, Cx. 84, D. 6948). Additionally, the instability of the captaincy, given to separatist revolts, it was the intention of the Crown to defend its own

² In colonial Brazil, citizens had to give their houses upon request of a royal guest. The passive retirement was the right given to some citizens to remain at their homes and only to receive the royal guest.
interests and to include local merchants in management positions; otherwise, it would create a lobby against the installation of the company.

For a more in-depth analysis of corporate governance practices, it would be interesting for future research to detail possible internal conflicts that existed, as well as to broaden the comparative analysis with other foreign companies placed in the same context.

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