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The Board of Administrators or the Flesh is Weak? The dilemma of BRF S.A.

Abstract:
Objective and method: This teaching case pictures the Corporate Governance (CG) problems of BRF S.A. triggered by the Brazilian Federal Police's Operation Weak Flesh. The goal is to encourage discussions on the effectiveness of boards of administrators as CG mechanisms and in the stock investment decision process. The case can be applied in graduate courses, especially in subjects whose contents are related to the Capital Market, Finance, Corporate Strategy and CG, besides undergraduate courses in related subjects. The data on the origin and historical evolution of the company, as well as about the characteristics involved in the case, were obtained from websites, magazine articles and the company website. The information that was collected and transcribed was not adapted. The script and events actually happened. The investor's situation is fictitious.
Results and contributions: The case proposes the exercise of decision making, based on two viewpoints: from the company's perspective, the Board of Administrators is analyzed as an internal CG mechanism. And from the shareholder's viewpoint, an investor who trusted that company with his capital reserves. The case permits analyzing the effectiveness of the board of administrators as an internal governance mechanism, the information asymmetry, conflicts of interest and the property structure.
Key words: Board of Administrators; Shareholders; Corporate Governance.

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1. Introduction

Within the capital market, there are always at least two points of view: that of the company and that of the investor. From the company's perspective, there is BRF, a multinational company in the food sector, one of the world's largest producers of fresh and frozen protein. The organization resulted from the merger of two Brazilian companies, Perdigão and Sadia, which was announced in 2009 and completed in 2012. Both companies that composed it were family businesses. Perdigão was born in 1934, in the city of Videira (SC), and Sadia in 1944, in Concordia (SC). Both had underlying values: the family business, respect for work, care for the earth and valuation of technique. They grew and expanded, turning into major players in the food market in Brazil and later abroad. Their products include chicken and turkey, specialty meats, processed frozen foods, frozen ready meals, portions, sliced products, margarine, specialty desserts, sandwiches, mayonnaise and animal feed. The products reach more than 150 countries on five continents, through some of its established brands, such as Sadia, Perdigão, Qualy, Dánica and Paty. The company first went public in 1980 and it is currently listed on the B3 Novo Mercado (BRFS3), Brazil Stock Exchange, and also has its securities traded on the NYSE (BRFS), New York Stock Exchange, United States. Its revenues in 2016 increased by 4.9% compared to 2015, from 37.23 to 39.06 billion reais, when more than four million tons of food were marketed.

The company has more than 100,000 employees, distributed across more than 50 factories in eight countries. The largest representative is Abilio Diniz, chairman of the Board of Directors (BD). Abílio Diniz has a management background and is accustomed to dealing with complex situations in a wide range of executive arenas. He has led other companies and also passed through the Federal Government, serving on the National Monetary Council, the highest body of the National Financial System, for over ten years. Abilio learned a lot from his father, who had the same trade. As a young man, he accompanied his father in charge of a company that was founded in the 1970s and which became nationally known as Pão de Açúcar.

The fund manager Tarpon became BRF's largest private partner. Two members of Tarpon, Pedro Faria and Zeca Magalhães were advisors to the company, but they needed a new name to convince the majority of the board and shareholders to change the management. Entrepreneur Abilio Diniz embarked on the project when he bought about 3% of BRF shares and, with the support of Previ, a pension fund of Banco do Brasil employees, took over the presidency of the board, replacing Nildemar Secches in 2013 (Filgueiras, 2017, p. 81).

BRF's Board of Directors consists of nine members, six of them independent. The chairman of the board has no executive functions. It is defined in the bylaws that the chairman needs to have an unblemished reputation, not hold positions in competitors nor represent conflicting interests.

Chief Executive Officer Pedro de Andrade Faria is a financial expert and partner in BRF's largest private shareholder, Tarpon:

> At the age of 40, Pedro Faria took over BRF on January 2, 2015. Excited at the success of the first year of the new management, Faria began the second phase in the restructuring of BRF - a process that is now known internally as "tarponization - ambevization" of the company (Filgueiras, 2017, p.82).

From the shareholder's point of view, there is Marcelo, one of the thousands of BRF investors in Brazil and around the world. A Brazilian student and very curious about the capital market, Marcelo found in BRF S.A. the hope of multiplying his money. Between 2006 and 2015, BRF shares rose from R$ 10 to R$ 70. Marcelo analyzed the company's economic and financial information and found that, if he had invested all his money in BRF shares in that period, he would be a millionaire today. With this conclusion, he invested all his capital reserves in this company in February 2017. He thought he might even retire, why not? After much analysis, he started to trust the company and its entire structure.

But not everything is perfect. That Friday, March 17, 2017, a striking fact would undermine BRF's governance foundations and, consequently, the profitability of Marcelo's investments. The news was everywhere: the Federal Police had discovered a scheme through which BRF officials paid bribes to inspectors from the Ministry of Agriculture, Livestock and Food Supply (MAPA). The reason for this corruption was to avoid effective oversight in one of the company's factories and thus keep it running.

On the one hand, the Chairman of the Board of Directors of BRF, who should manage and monitor the company in constant and meticulous operations, seeking to maximize the shareholders' wealth, had yet another obstacle to solve, as he did not know about the illegal practice and the involvement of high-level employees and directors. In addition, the board of administrators had to investigate the facts. Decisions needed to be taken to achieve the best solution internally as well as to reduce the external repercussions.

On the other hand, there was Marcelo, one of the shareholders, who put his equity in one of the companies with the best governance structure in Brazil thus far. What was next? While both seek solutions, or at least understand the problem, the company shares are melting away on the stock exchange. Would the board of administrators be effective at representing the shareholders' interests, in its oversight and management of company strategies and operations, and would it stem this catastrophe? And Marcelo, should he maintain his shares in BRF or withdraw them, in order to mitigate the risk due to the information asymmetry?

2. Operation "Weak Flesh": Corruption involving BRF

The Federal Police (FP) had scheduled a special March 17. On that date, which marked the third anniversary of the Carwash investigations, the FP started its largest operation, called "Weak Flesh" (Filgueiras, 2017, p.88).

The FP exposed the corruption that took place between the company and the federal agency, as a result of two years of investigation, involving more than 1.1 thousand police officers. When the institution "[...] convened a press conference [...] to show the 353-page survey that resulted in Operation Weak Flesh, a situation came out that may have surprised most Brazilians. But not the federal agricultural tax auditors"(Caetano, 2017, p.32).

The FP's action resulted in a corruption scheme rooted in at least three state superintendencies of the Ministry of Agriculture, in Paraná, Minas Gerais and Goiás. In exchange for bribes, inspectors, veterinarians and heads of the ministry in these states issued false quality assurances for meatpackers who, with these certificates, were not concerned with meeting the minimum sanitary requirements established by law (Campbell, 2017, p.50).

At that point, the BRF chairman had to gather all the executives to confirm that not only he was not aware of this practice under his supervision. And also to contain the negative effects on the company's image as quickly as possible.

3. The complaint of corruption

The investigation pointed out that the meatpackers had a direct influence on the Ministry of Agriculture to choose the agents who would carry out the inspections in the company, through the payment of undue advantages (Folha, 2017).

According to FP, BRF officials had free access to the Ministry of Agriculture to access the inspection system the auditors used, with the acceptance of the former superintendent of the Ministry of Agriculture in Paraná, Daniel Gonçalves Filho, appointed as the head of the scheme (Campbell, 2017, p.50). The FP arrested a manager and a director of the company and the home of the vice president of corporate integrity was searched (Filgueiras, 2017, 79).

Amidst the economic and political crisis, losing money is like accelerating the car towards the abyss. But what worsened the whole story was the combination of the police operation with the expectation of the current board of directors, created when it took command four years earlier.

A conversation wiretapped by the FP revealed that the agent of the Ministry of Agriculture responsible for the on-site inspection stated that he would "kill in the chest" the notification to suspend the plant and that he would not warn Brasilia (Uol Economia, 2017).

For FP, a conversation between BRF's two directors showed that veterinarian Dinis Lourenço da Silva, head of the Inspection Service for Animal Products in Goiás, was asking for a 300,000 reais bribe to cover up some irregularities in the BRF unit in Mineiros, in the interior of the state. In exchange for the payment, the veterinarian would return to the Mineiros unit to redo the inspection and - surprise! - he would find that everything was in order that time (Bonin, 2017, 55).

4. Meeting of the Board of Directors

Less than two hours after the Federal Police launched Operation Weak Flesh, in the morning of Friday March 17, 2017, the top eight BRF executives had locked themselves in the main meeting room in the company's headquarters in São Paulo. Among them were the CEO, Pedro Faria, and the chairman of the board of directors, Abílio Diniz. The aim was to define a plan of action to stop the public bleeding of the company's reputation, accused of committing corruption to have its health oversight process loosened by the Ministry of Agriculture agents (Cilo & Drska, 2017, p.42).

Everyone was talking fast. Cell phones kept ringing. Every minute there, thousands of negative comments and jokes about the company were published and flooded the social networks (Cilo & Drska, p.42). In the face of that much news and comments spreading, the company had to react urgently. Thus:

> The sense of urgency, in the case of operation Weak Flesh, entailed almost immediate results. In little more than 20 minutes, the largest action plan in the history of BRF was ready. Even before they left the room, the executives decided to create a crisis management committee. They summoned the main creative thinkers from the publicity agency DM9, the directors of the public relations agency Loures Comunicação, the three law firms that provide legal support to the company and called upon the most experienced directors and top employees of BRF at full speed (Cilo & Drska, 2017, pp. 42-44).

Agriculture Minister Blairo Maggi, also worried about all the repercussions, contacted the company to inquire about its treatment of the problem. According to the article in the magazine Globo Rural, issue March 17, 2017, the minister talked with Pedro Faria and Abilio Diniz, and expressed his concern with the repercussion of the subject. The executives assured that there were internal procedures to deal with this and that, four years ago, they had no news of this type of misconduct and would work together to clarify the facts.

"*No one there was aware of the intensity and scope of that crisis. All we knew was that we had to act quickly and transparently*", an executive related to BRF told Cilo & Drska (2017, p. 42), who closely followed the reaction behind the scenes.

Soon after the creation of the committee, BRF published a web page - brf.com.br/portasabertas -, which contained a letter of clarification on the scandal. There was also a team to respond to consumers' comments on social networks, and a structure was set up to respond to the Brazilian and international press. Without wasting time and uninterruptedly, employees selected by the BRF top management contacted suppliers, customers and investors in order to play down the facts, to try to appease the situation (Cilo & Drska, 2017, p. 44).

5. A small investor

Marcelo is 26 years old and is taking an MBA in Capital Markets. The young man had been accompanying the companies listed on the Brazilian Stock Exchange (B3) for some time. He took great interest in Brazilian companies, to the extent that he decided to go for more profitable investments, as he had some knowledge on the subject and his colleagues already bought and sold shares. Marcelo was concluding his specialization, so it would be a good time for him to start. So he spent a few days analyzing the market, looking for a company to invest his capital in.

The young man got to the BRF shares with great interest in the investment, because his father had worked at Perdigão for more than 30 years (one of the merged companies that resulted in the creation of BRF) until he retired. He evaluated its main investors, its board members, their background and remuneration, as well as the company's contribution to the country, in economic and social value, so that he felt like a real partner.

At the end of 2012, BRF changed management. Majority shareholders criticized the slowness of the former administration. A group of shareholders, led by the manager Tarpon, joined Abilio Diniz to deal the cards at BRF. They changed everything, starting with the top of the company. Nildemar Secches left as chairman of the board, making room for Diniz. The changes in the board came next. Tarpon and its group criticized what they saw as slowness of BRF's management, considering the company as a giant that could be transformed into a global leader. Investors bought the idea that the shares, worth around 40 reais at that time, would be worth at least 100 reais in four years. Today, BRF shares are worth about 35 reais, therefore almost 20% less than they were worth four years earlier (Filgueiras, 2017, pp. 78-79).

Table 1 describes the profile of the BRF directors, representing the minority shareholders, analyzed by Marcelo.

Member	Function	Educational background
Abílio dos Santos Diniz	Chairman of the Board (independent)	Business Administration
Renato Proença Lopes	Deputy Chairman of the Board	Graduate degree in Business Administration and MBA in Wholesaling Business Management
Henri Philippe Reichstuk	Sitting member (independent)	Graduate degree in Economics
Luiz Fernando Furlan	Sitting member (independent)	Specialization in Financial Management
Manoel Cordeiro Silva Filho	Sitting member (independent)	Graduate degree in Economic Engineering and MBA in Finance
Walter Fontana Filho	Sitting member (independent)	Graduate degree in Economics
José Carlos Reis de Magalhães Neto	Sitting counselor	Business Administration
Aldemir Bendine	Sitting counselor	MBA in Top Executives and Finance
Vicente Falconi Campos	Sitting counselor	Ph.D. in Engineering

Picture 1. Composition of BRF Board of Administrators on April 22nd 2017

Source: the authors, based on Econoinfo and Website Relação com Investidores BRF, 2017.

Pedro Faria, the CEO, took charge of the company on January 2, 2015. Until then, he had been the Director of Investor Relations at Tarpon. He holds a degree in Business Administration at FGV-SP and an MBA from the University of Chicago (USA). In 2016, BRF paid all members of the Board of Administrators more than 7.5 million *reais*.

In Table 1, the corporate division of BRF, illustrating one of the research sources for Marcelo to define his investment, related to the ownership dispersion or concentration.

Table 1
Stock Composition of BRF on 05/31/2017

Stockholder	Number of ordinary shares	Ordinary shares(%)
Petros – Fundação Petrobras de Seguridade Social	92,716,266	11.41
Previ – Caixa Previdência Funcionários Banco do Brasil	86,691,252	10.67
Tarpon Gestora de Recursos S.A.	69,131,442	8.51
GIC Private Limited	51,913,800	6.39
BlackRock Inc.	40,867,404	5.03
Stock in Treasury	13,468,001	1.66
Others	457,684,835	56.33
Total	**812,473,000**	**100.00**

Source: the authors, based on Econoinfo, 2017.

Marcelo thoroughly investigated BRF, all of its history until the change of its management, the investor relationship website (*www.brf-br.com/ri*), financial statements, annual and sustainability reports, the economic-financial indices, the composition of the board of directors and shareholder composition. In addition, he researched on the bylaws, policies and regulations for BRF investors, such as dividend policies. He already felt a future investor: "The company is one of the best in governance that I analyzed. It has several independent members on the board, as well as the president. They are able to make good investment, financing and management decisions, always expecting to represent shareholders' rights". That is what Marcelo thought after his first days of appreciation.

The company was the first food and beverage company to comply with B3's New Market rules on April 12, 2006, which is the highly differentiated governance segment of the Exchange. That is further information that enhanced the company's credit towards the shareholders, indicating that it follows a pattern of transparency and governance.

The company is also highly regulated, even doubly regulated, its shares being traded on the São Paulo Stock Exchange and the New York Stock Exchange. The Company complies with the International Financial Reporting Standards (IFRS) and the regulations of the Financial Reporting Internal Control System (SCIRF) regulations, based on the Sarbanes-Oxley Act (SOX).

After hours of fundamental analysis, Marcelo came to the conclusion that he should invest in BRF. He defined the company as a great investment, took into account mainly the profile of its executives, made available by the company itself. In theory, it was a great team, well paid, highly advised. Marcelo then invested all of his capital reserves in February 2017, buying BRF shares. According to his testimony: "I confirmed a lot of information that made me bet on BRF as the best company to invest my money in. There is a small percentage, between 10 and 12% of shares concentrated in only one shareholder. The large majority of the board members has some background in Business Administration, Finance or Economics. In the last 10 years the value of the company's stock has jumped from about 10 *reais* to 70 *reais*. I believe that, with the new management, this level lies within reach again".

At one point, however, a problem arose that exists in several countries as something endemic: corruption. In this case, in the Brazilian society in which, due to weak historical social ethics, the more bureaucracy, the more rules there are. The strongest is the inspector who creates difficulties to sell facilities to an employee who thinks this normal way of operating in Brazil is wrong, but perhaps this operation has some educational effect.

According to Adeodato Volpi Netto, chief equity strategist at Eleven Financial Research, however, according to Gradilone (2017), what scares investors is not only the immediate effect of Operation Weak Flesh on the company's results, but its consequences. Prior to the transaction, Eleven considered BRF's shares to be one of the most promising in the sector.

Thus, the turbulent operation launched by the FP on March 17, 2017 harmed thousands of investors. Shareholders took losses of up to 10% in a few days. The shock was so great that it affected not only BRF, but also other companies in the sector, which saw their shares drop by up to 9% (Gradilone, 2017, p.48).

After hearing the news of the bribery case, however, what most concerned Marcelo was not only with the loss resulting from that investment, but also the fact that he saw the proportion the corruption case between company and inspection gained. He still had no idea what its effects on the company's immediate results would be. Marcelo, however, was starting to realize that the board of directors might have failed to perform its functions, as this internal corporate governance mechanism should seek efficiency in monitoring the company through constant scanning operations, always seeking to maximize shareholder wealth and help investors to define the best firms to invest in.

On March 16, 2017, one day before the disclosure of Operation Weak Flesh, the closing price of a BRFS3 share was 40.01 *reais*. On July 17, the stock started the trading session at the price of 38.00 *reais* and, at the end of the day, accumulated a loss of 7.30% in 24 hours, closing at 37.09 *reais*. This figure was recorded for the first time in the company's history. It reached its low on the 22nd, at the value of 35.58 *reais*. Not even the most pessimistic investor would be expecting such an event, even when considering the current national scenario. On April 18, 2017, one month and a day after the operation was triggered, the closing price of a BRFS3 share was 40.62 *reais* (Figure 1), even higher than the price on the day before the announcement of Operation Weak Flesh and its intensive media disclosure.

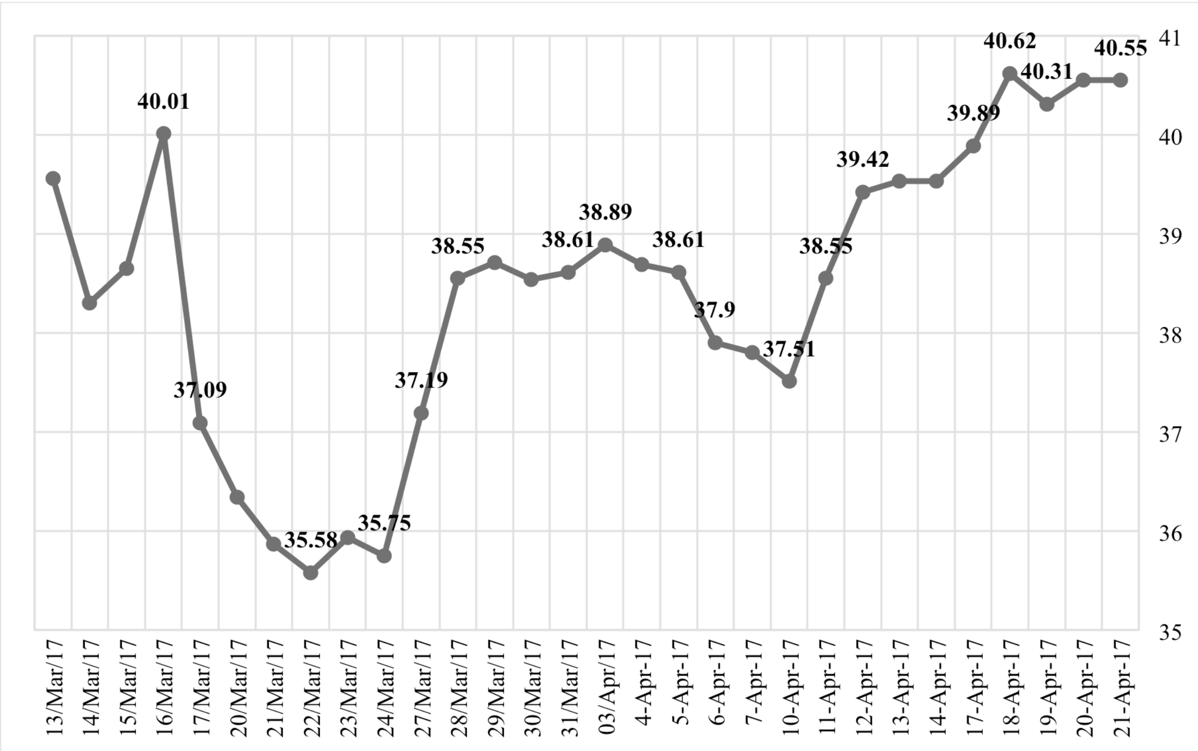

Figure 1. Closing prices of stock BRFS3 between March 13th and April 21st 2017

Source: Created by the authors based on ADVFN Brasil, 2017.

6. Bad things do not only happen to others

In Brazil, it is nothing new, and one should not think far to recall other cases of bribery, corruption, among other deviations of conduct, in which there is no praiseworthy act whatsoever. In this case, the board had more than one obstacle to be solved, starting with its ignorance of the practice and the involvement of senior officials and directors. All of this plus the need for investigation by the board of directors. There were decisions to be made to solve these facts in the best possible way, internally, as well as to mitigate the repercussion of external factors. On the other hand, a small shareholder, who entrusted his capital reserves to a company, hitherto without risk of significant losses, saw his equity be drastically reduced in a matter of a few hours. Hence, what mechanisms could mitigate the agents' conflict? Would the board of directors have been effective in representing the shareholders' interests in their role of oversight and management of strategies and operations? Should Marcelo keep his shares in BRF or withdraw them to mitigate his risk due to asymmetric information?

7. Teaching Notes

The Teaching Notes are of exclusive access to the teachers, aiming to direct the objectives, methodological strategies and evaluation of the case for teaching.

7.1 Data sources

The data source on the origin and historical evolution of the company, as well as on the characters involved in the case were obtained through websites, magazine articles and the company's website. The shareholder's point of view is fictitious, created through the character Marcelo. The data presented on the Operation Weak Flesh and its unfolding are real and were obtained from secondary sources, through reports in magazines, websites, policies, bylaws and regiments of the company (ADVFN Brasil, website B3, magazines Carta Capital, Época Negócios, Folha de São Paulo, EXAME, Isto é Dinheiro, VEJA, Dinheiro Rural, Globo Rural, and the websites BRF and EconoInfo). The period of data collection was from March 14, 2017 until August 29, 2017. First, all the magazines and newspaper articles that quoted the Weak Flesh operation were digitally cataloged. After this process, the excerpts that made up the teaching case were captured from this sample. The information collected and transcribed did not suffer adaptations or inclusions. The script and events actually happened.

7.2 Educational objectives

The dilemma of BRF S.A., reflecting a problem with international repercussion, was designed to grant knowledge about corporate governance and agency theory amidst a governance problem at BRF. The case permits analyzing the effectiveness of the board of directors as an internal governance mechanism, information asymmetry, conflicts of interest and ownership structure.

Decision making should be based on two points of view: that of the company and that of the shareholder. On the company side, the Board of Directors is observed as an internal corporate governance mechanism. Its efficiency in monitoring and its composition should help an investor to define the best companies to invest in, albeit in a scenario where they find great schemes of money laundering, bribes and the accumulation of bad management news.

And from the point of view of the shareholder, we observe an investor who entrusted his capital reserves to that company, in defining the expected return and appropriately choosing the types of investments that should compose his portfolio. The didactic emphasis is on finance, where risk is sovereign. A possible choice is investing in shares, although these continue to be seen as a black box. How to choose the right company? Which indicators should be analyzed? What characteristics of the company should be considered? The answers are many, and yet they are not definitive.

The central theme of the application of the case concerns corporate governance. We divide this theme into three main areas of program content: agency theory, board of directors and property structure. Students are invited to put themselves in the place, on the one hand, of the Chairman of the Board of Directors of a global company and, on the other hand, of a shareholder of that company.

Prior to the discussion of the case, it is recommended that the data sources and the referenced works be read in full. Through discussion of the case, especially debating on the proposed issues, participants are expected to be able to: identify conflict passages of the agents and suggest mechanisms that can mitigate this problem; judge BRF's board of directors, through its characteristics, such as the independence of the board, with a view to the actual effectiveness of the governing body; and relate the shareholder composition with the management problem and its consequences for investors, particularly for Marcelo, a minority investor.

The case further seeks the students' historical understanding of other cases of effectiveness problems in the board of directors, which may also have affected minority investors, contextualizing the discussion of the theme in another age and scenario.

The questions presented next can be used with the educational objective of discussing the thematic axes, fully or separately, according to the need of the application.

1. **Questions about Agency Theory:**
    a. One of the principles of agency theory is the idea that the agents may possess asymmetrical information, which enhances conflicts between the parties. Identify excerpts or situations in the case in which this may have happened.
    b. Another principle of agency theory is the idea that the agents' interests may differ from those of the principals, that is, the owners. Identify excerpts or situations in which this may have been the case at BRF.
    c. Mention possible mechanisms that could reduce the above problems, existing in the case or others you suggest.

2. **Questions about Board of Directors**
    a. Which are the general characteristics of the board at BRF?
    b. Which are the advantages or disadvantages of an independent chairman serving on the board of directors?
    c. And independent members? Do they help or not in good governance practices? If yes, how?
    d. How do the characteristics of the board, the presence of an independent chairman and members help or not to revalue BRF?

3. **Questions about Property Structure**
    a. Which are the main characteristics of the ownership composition of BRF?
    b. How can the ownership dispersion be related with the management problem in this case?
    c. What is the foreign partners' main reaction to the drop in share value provoked by a corruption problem?
    d. How could the minority investor Marcelo mitigate the risk in the short term?

7.3 Application of the case

The teaching case presented can be used for discussion in graduate courses, especially in subjects whose contents are related to the Capital Market, Financial Market, Corporate Strategy and Corporate Governance, more specifically in the discussion of internal Corporate Governance mechanisms and Agency Theory. In undergraduate classes, the case should be applied to students who are moving towards the end of their courses in Business Administration, Accounting, Management and who are familiar with Governance, Financial Market and Strategy themes.

To support the teacher to choose the audience, the arrangement in the class, the parts in the presentation of the case, among other actions, we suggest reading and analyzing the scale of difficulty levels. The case presents difficulty levels 3, 3 and 1 on the scale proposed by Leenders, Mauffette-Leenders and Erskine (2001), respectively, for the analytic, conceptual and presentation dimensions, in which 1 means easy, 2 regular and 3 difficult, divided per dimension, level, case layout, explanation of the difficulty level and goal, as displayed in Picture 2:

Dimension	Level	Case layout	Explanation of difficulty level	Goal
Analytic	3	In the case, the criteria are presented to decide on the form of the fact that occurred, the form of treatment thus far, on both sides, and the unknown factor regarding what action to take to attend to both parties	There is no outcome in the case. The dilemma for the students is to put themselves in the chairman of the board's and in a shareholder's place. Several decisions are possible, and one action by the company can influence the investor's decision.	In this dimension, the case readers' task is related to the key decision of the case. The analytic task depends on how the decision is presented in the case: as the alternative chosen, suggested alternatives or the reader should put himself in the context to decide on the best action.
Conceptual	3	Three thematic axes are outlined for the individual conception. The theoretical perspective is necessary to drive the action after the dilemma	More than one concept is present and these require in-class discussion and explanation, combining them with examples, problems or exercises, mainly concerning corporate governance	At this level, the concern is what theories, concepts or techniques can be useful to understand and/or solve the situation in the case. The difficulty of the theory itself and the number of concepts to be used simultaneously are taken into account
Presentation	1	The information is presented in popular language and the story is compelling	The case includes various media excerpts, which contributes to easy, organized and rapidly assimilated reading. Theoretical and technical information is restricted to the teaching notes	Offers an opportunity to develop skills during reading and structure information. Engages the reader from start to finish. Short, organized case containing all relevant information in a sample manner without odd data

Picture 2. Difficulty levels of the case

Source: Created by the authors, based on the criteria proposed by Leenders *et al.* (2001, p. 17).

To support the teacher with the application of the case in the classroom, the following script is suggested. It is important to guarantee that the students read the case carefully before the class. If that is not possible, 20 minutes can be reserved at the start of the class for the students to read the case in the classroom.

Estimated Time	Activity	Concepts Applied
0-15 min	General presentation of the case, detailing its objectives	Objectives
30-40min	Discussion on the consequences, contextualize the event for the company.	Context of the event with the country's political-economic situation, as well as its international repercussion.
60-90min	1. Suggestions: Organization of small groups. Distribution of thematic axes (presented further on) and surveying solutions or alternatives to face the problems. 2. Suggestion: Discussion between two groups with representatives, one playing the role of the company and another of the investor. 3. Suggestion: Creation of various pairs, in which half is responsible for answering the questions with positive assertions and the other part gives opposite answers.	• Corporate governance • Agency theory • Board of administrators • Property structure
20-30min	Closing off the class with proper decisions made thus far.	Company decisions on the case in the short, medium and long terms

Picture 3. Suggested lesson plan

Source: the authors.

7.4 Proposals to address the questions

1.

a) The case presents a problem caused by asymmetric information, in which the board of directors was unaware of the corrupt practice of paying bribes to inspectors of the Ministry of Agriculture to achieve the issuance of quality certificates. For Jensen (1993), serious information problems limit the effectiveness of board members in large corporations. For example, the CEO almost always determines the agenda and information given to the board. This limitation of information severely impairs even the ability of talented board members to effectively contribute to the monitoring and evaluation of the CEO and company strategy.

b) There was a conflict of interest in the case, as the board (agents) did not truly represent the interests of the shareholders (principal), because of their lack of effectiveness in formulating, directing and controlling policies, guidelines and strategies. The information presented shows that the council did not even know about the illegal practice, thus failing to resolve the problem of paying the bribe internally. Wiseman and Barton (2015) argue that a good first step would be for everyone to fully understand what a "fiduciary duty" means for a board member. Most legal codes emphasize two key aspects: loyalty (placing business interests above any other) and prudence (dedicating appropriate attention, skills, and diligence to business decisions). The role of a loyal and prudent board member is not to force the executive to maximize shareholder value in the short term, to the detriment of any other interest. Rather, it is that the member should help the company succeed for years on end.

c) The media acted as an external governance mechanism, activating the board of directors, internal mechanism, for the irregularity that existed in the company, and bringing to light the lack of effectiveness of this entity. For Aguilera, Desender, Bednar and Lee (2015), the media is considered an external mechanism because it can widely disseminate information. It exists to exert a controlling role, in which the threat, acting as negative media, can prevent managers from acting out of self-interest because they are afraid to damage their reputation, in addition to acting on agency theory of governance to enhance the effectiveness by increasing transparency and reducing information asymmetry. Based on the case, the media, as an external governance mechanism, activated the Board of Directors for the occurrence of a bribery practice, thus demonstrating the failure of the internal mechanism. The Federal Police also acted as an external mechanism, through the legal system, by triggering Operation Weak Flesh. According to Aguilera et al. (2015), the legal system is the set of structures and processes used to interpret and apply the existing law. It establishes how property rights are defined and protected and includes regulatory institutions, which oversee standards and rules that firms have to comply with.

2.

(a) The Council consists of nine members, six of whom shall be independent. The Chairman of the Board is one of the independent members. As a rule of BRF, the Chairman of the Board of Directors has no executive functions. There is no duality in command, with Pedro Faria serving as the CEO and Abilio Diniz as the Chairman of the Board. It is also defined, in the Bylaws, that the chairman should have an unblemished reputation, not hold positions in competitors nor represent conflicting interests. The large majority of the board members hold a degree in Business Administration, Finance or Economics.

(b) An independent chairman should strongly watch over his reputation and activity in the company, as he may be observed by other companies to sit on their Boards of Directors in the future. Thus, he is much more concerned with his reputation, so he uses all his expertise to maintain his reputation towards all companies. The Brazilian Securities Commission recommends that, among the good corporate governance practices, due to the fact that the Board of Directors has the function of supervising the directors' management, in order to avoid conflicts of interest, the Chairman of the Board of Directors should not also sere as the president of the Board of Executive Officers or its chief executive officer. According to Fama and Jensen (1983), it is expected that, to protect the flow of information to the board, senior executives, especially those who sit on the board, can only be actually dismissed with the consent of the board, being thus protected against retaliations of other senior executives. Corporate boards usually include external members, i.e. members who are not internal managers, and who often hold a majority of the seats.

c) According to the IBGC, the boards of directors of New Market companies have to be composed of at least five (5) members, elected by the general meeting, at least twenty percent (20%) of whom should be Independent Board Members. External board members act as arbitrators in disagreements between in-house managers and perform tasks involving severe agency problems between internal managers and residual claimants, for example, setting executive compensation or seeking substitutions for top managers. Effective separation between management and control of high-level decisions means that external directors have incentives to perform their tasks rather than colliding with managers to expropriate residual claimants. Most of the external directors of open corporations are either managers of other corporations or important decision makers in other complex organizations. The value of their human capital depends primarily on their performance as an internal decision manager in other organizations. One of the recommendations in the Brazilian Securities Commission's corporate governance booklet is also that the board should have as many members independent of the company's management as possible.

d) As shown in Figure 1, the value of the BRF shares one month and one day after the start of the operation was 40.62 *reais*, even surpassing the price prior to the announcement date of Operation Weak Flesh and its mass dissemination in the media. This recovery is mainly due to the plan of action developed at the meeting between the board and the CEO on March 17, 2017. The board members set up a crisis management committee. They summoned the top creative officials of the commercial agency DM9, the directors of the public relations agency *Loures Comunicação*, of the three law firms that provide legal support to the company, and also called upon the most experienced directors and senior officials of BRF. The case portrayed that the Board of Directors has little influence in the discovery of illegal practices, also considering the view that it is logically impossible to know everything. Good advice can shield the market value in the long term though, as seen with BRF's shares, which returned to even higher values little more than a month after the FP investigation was triggered.

3.
a) As shown in Table 1, the ownership composition of BRF is dispersed, the largest shareholder being Tarpon, an investment management company, which owns 11.94% of the shares. Then comes Petros, *Fundação Petrobras de Seguridade Social*, with 11.42%. The third largest shareholder is Previ, Banco do Brasil Employees' Pension Fund, with 10.65%. With 5.03%, BlackRock Inc. is the fourth largest shareholder, a global American investment company. GIC Private Limited owns 5.01% of BRF shares and is an investment company in Singapore. And 1.66% of BRF's shares were acquired by the company itself and thus named Treasury Shares. Minority shareholders hold the remaining 45.71% of the shares. It is noted that there is a high dispersion of ownership, which should lead to greater governance control and minimize internal interference.

b) The stock dispersion leads to the existing premise that diffuse control of the company results in greater demand for efficient business management. This minimizes internal interference, increasing independence, and generates more governance. In this case, the management problem occurred even though there was high dispersion of ownership. This feature requires greater administrative efficiency. The regulation of the New Market segment of the Brazilian Stock Exchange makes mention of the shareholding dispersion so that, in any and all public offering of shares, the company needs to make its best effort to achieve shareholding dispersion, with the adoption of special procedures, which will be included in the respective prospectus, such as: a) guarantee of access to all interested investors; or b) distribution to individual or non-institutional investors of at least 10% (ten percent) of the total to be distributed (BM & FBOVESPA, 2011). In the case of BRF, there is a concentration of large funds managing the BRF, although they are not majority shareholders (with more than 50% of the shares) and actively manage the decisions at BRF, including board members appointed by the funds themselves. Dispersion is good, but with limits. From this limit, there will be many shareholders who will want to be active in the company. Jensen and Meckling (2008) argue that most of the major conflicts are likely to stem from the fact that, as the managers' ownership rights decrease, their incentive to devote significant effort to creative activities, such as finding new profitable enterprises, also drops. They can actually avoid these ventures simply because they would involve a lot of concern or effort for the managers to administer them or learn new technologies. In conclusion, thus, ownership concentration benefits the corporations, as it can generate lower costs and enhances the monitoring of the management.

c) Foreign shareholders hired a North American law firm, which is preparing collective lawsuits for the shareholders to retrieve their losses. According to the article published in Época Negócios (2017), Rosen Law Firm is investigating potential accusations on behalf of shareholders, resulting from allegations that JBS may have issued materially misleading information to the investing public. This reaction partially remits to the Enron case in the United States, when executives manipulated the financial statements with the help of companies and banks, and thus hid 25 billion dollars in debt for two years on end, thus artificially inflating company profits.

d) First, in finance, an important concept for risk mitigation is the use of asset diversification. When buying shares (for example) of companies whose market oscillations are uncorrelated, Marcelo could prevent large market falls from reaching them. If his decision was nevertheless to invest in only one company, Marcelo did a good part of his homework by investing in a company with good corporate governance practices, having independent and qualified members in the Board of Directors, dispersed ownership , among other characteristics. A final strategy for Marcelo could have been smaller and gradual batches of investments, such as the partial purchase or sale of his shares according to the market's movements.

8. Closing

An alternative to close off the plenary discussion could be the proposition of a challenging situation: to raise another possible treatment the company could have given to the event and its repercussion. Also, on the part of the shareholder, to find the best attitudes, asking the students to put themselves in his place in view of his investment in BRF shares.

A case for teaching is not an exercise, there are no right answers, there are the best answers, which can lead to a better decision. We suggest closing off the case with an open question: what other cases of corporate corruption can be cited, as happened with BRF? With this question, it is intended to instigate students to think more about the subject, taking the discussion of the case beyond the classroom. The purpose is to leave an important lesson of understanding how failures in companies' corporate governance can lead to substantial value losses. Beyond what was illustrated by BRF, as well as other international companies, such as Enron, and the Brazilian companies Sadia, Aracruz and OGX

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