

## **Re-establishing the Legitimacy after Fraud: Does Corporate Governance Matter?**

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### Abstract

Recent corporate financial misconducts have shaken the investors' trust in the credibility of financial reports. Given the significance of the association between the quality of governance structure and reliability of financial reporting mechanism, we evaluate this relation to evidence whether firms accused of financial misconduct improve their credibility. Applying a sample of firms cited for violations of SECP rules, we affirm a positive relation between fraud disclosure and successive improvements in governance structure. We further notice a positive relation between the buy-and-hold abnormal returns and the intensity of increase in outside director percentage after three years of fraud detection. These empirical assertions extend our understanding of the aftereffects of manipulating financial reports and may be handfull to regulators debating corporate governance rules and to management when crafting policies to reinstate investors' trust after fraud revelation.

**Keywords:** Corporate fraud, corporate governance, credible financial reporting, investor trust, agency costs