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Director Interlocks and Spillover Effects of Reputational Penalties From Financial Reporting Fraud

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Abstract

I examined the spillover of reputational penalties between firms in the context of financial reporting fraud. Drawing from signaling and attribution theories, I used financial event study methodology and found significant reputational penalties in 45 (18.4%) out of 244 firms with director interlocks to 30 firms accused of financial reporting fraud in the United States. Furthermore, logistic regression analysis suggested that firms thus associated with accused firms were more likely to experience significant reputational penalties when the interlocking directors held audit or governance chair positions in them. This likelihood decreased when these firms' observable governance structures signaled effective corporate governance.

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