

Putting Your Money Where Their Mouth Is: Financial Advisors' Conflicts of Interest and the Limits of Disclosure

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Disclosure: a solution to COIs?

- Financial regulators advocate disclosure
 - SEC (USA), FSA (UK), AMF (France)
- Medicine
 - American Medical Association, Physician Payment Sunshine Act

Why is disclosure so popular?

- Consumers make informed decisions
 - Decreases information gap
- Advisors
 - For regulated, often lesser of evils
 - May limit firms' and regulators' liability -- '*Caveat Emptor*'
- Perceived to work!

But does it?

Does disclosure work?

- Consumers
 - Ignore it (Hampson et al. 2006)
 - Discount insufficiently or erratically (Tversky and Kahneman, 1974; Cain et al. 2011)
 - Do not seek second opinions (Foreman, 2001)
 - Feel increased pressure to comply (Sah et al. 2013, 2014)

Disclosing a conflict of interest



“Under disclosure rules, I’m required to tell you that I get paid by the fund manager whose investment I’m recommending to you.”

Increased pressure to comply

- Advisor discloses:
“I personally gain if you do X rather than Y”
- Consumer hears:
“Please do X because it will benefit me”

Hypotheses: The burden of disclosure

Sah et al. (2013) *JPSP*

- H1: With disclosure, the consumer will trust advice less

- H2: With disclosure, consumers feel increased pressure to act in their own best interest



consumers feel increased pressure to act in their own best interest



Lottery studies

Sah, S. et al (2013). The Burden of Disclosure: Increased Compliance with Distrusted Advice. *The Journal of Personality and Social Psychology*. 104(2),289-304.

- Choosers: pick between two different die roll lotteries, A or B
 - Advisors gave choosers advice on which one was best (A was more attractive)

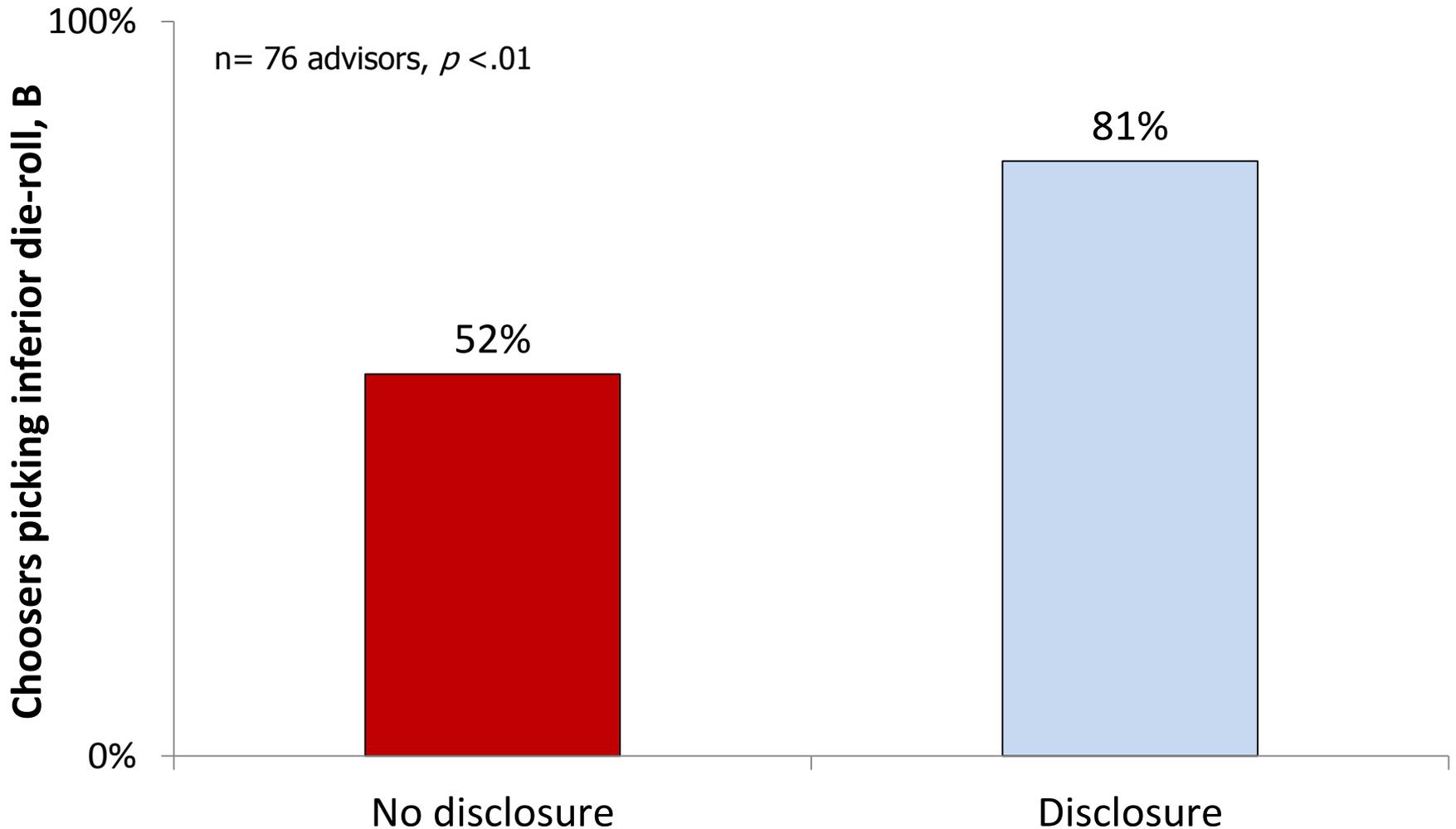


Lottery studies

- Conflict of Interest: Advisors rewarded if choosers decide to roll inferior die B
 - “Disclosure” condition
 - “No Disclosure” condition
- No-conflict condition

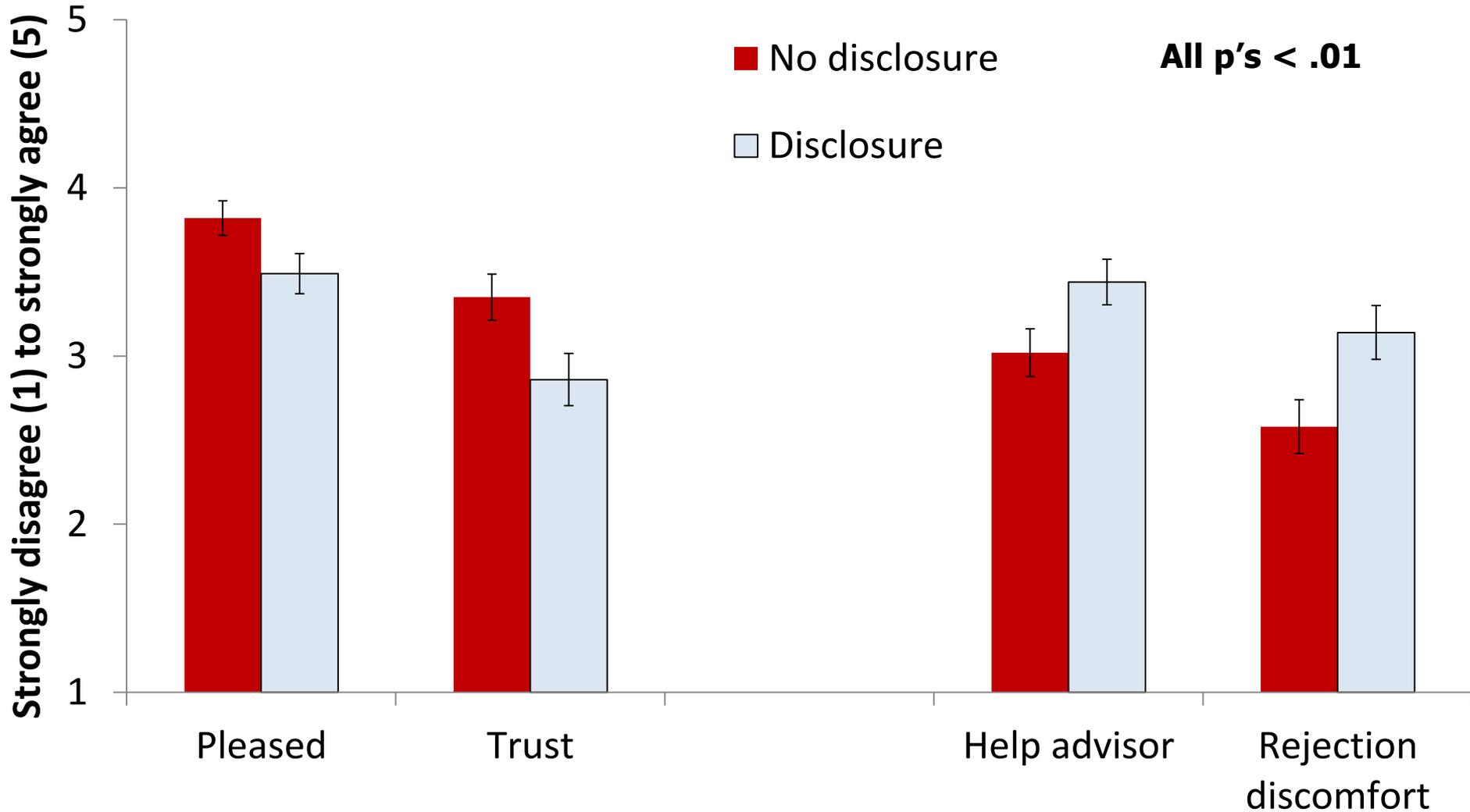


With ~~CO~~ disclosure, biased MORE likely to take biased advice





Opposing forces act on chooser



Additional studies: reduced pressure

- External Disclosure
- Private decisions
- Opportunity to change mind - 'cooling off' period

Sah, S. et al (2013). The Burden of Disclosure: Increased Compliance with Distrusted Advice. *The Journal of Personality and Social Psychology*. 104(2),289-304.

Sah, S. et al. Insinuation anxiety: Fear of signaling distrust after conflict of interest disclosures. (June 28, 2014). Available on SSRN.

Does disclosure work?

- Advisors

- Moral licensing

(Monin and Miller, 2001;

- Strategic exaggeration

Cain et al. 2011)

Advisors

Disclosure → advisors more reluctant to expose themselves to COIs so that they have “nothing to declare”?

- Disclosure may work best when it changes the behavior of advisors

Sah, S. & Loewenstein, G. (2014). Nothing to Declare: Mandatory and voluntary disclosure leads advisors to avoid conflicts of interest. *Psychological Science* 25(2), 575-584.

Evidence that...

- Disclosure can have perverse effects
 - Advisees: Increased pressure (burden of disclosure)
 - Advisors: Increase bias in the advice
- Disclosure can have benefits
 - Advisees: Decreased trust (reduce pressure)
 - Advisees: Increased trust if disclose the absence of COIs
 - Advisors: Advisors reject COIs
 - Advisors: Rein in bias if reminded of obligations

Thank You!

Research Papers

- Sah, S. (2014). Disclosure and strategic restraint: The appropriateness of biased advice in medical and business contexts. *Manuscript in preparation*.
- Sah, S., Loewenstein, G., & Cain, D. (2013). The burden of disclosure: Increased compliance with distrusted advice. *Journal of Personality and Social Psychology, 104*(2), 289-304.
- Sah, S., et al. (2013). Insinuation anxiety: Increased pressure to follow less trusted advice after disclosure of a conflict of interest. *Working paper. Available on SSRN*.
- Sah, S., & Loewenstein, G. (2014). Nothing to declare: Mandatory and voluntary disclosure leads advisors to avoid conflicts of interest. *Psychological Science 25*(2), 575-584.
- Sah, S., & Read, D. (2014). Consumers are too forgiving towards missing information. *Manuscript in preparation*.
- Sah, S., & Feiler, D. (2014) The disclosure penalty: Negative attributions from conflict of interest disclosure apply to both biased and honest advisors. *Manuscript in preparation*.
- Sah, S. (2012). Conflicts of interest and your physician: Psychological processes that cause unexpected changes in behavior. *Journal of Law, Medicine and Ethics, 40*(3), 482-487.

Published papers available at www.sunitasah.com/research