

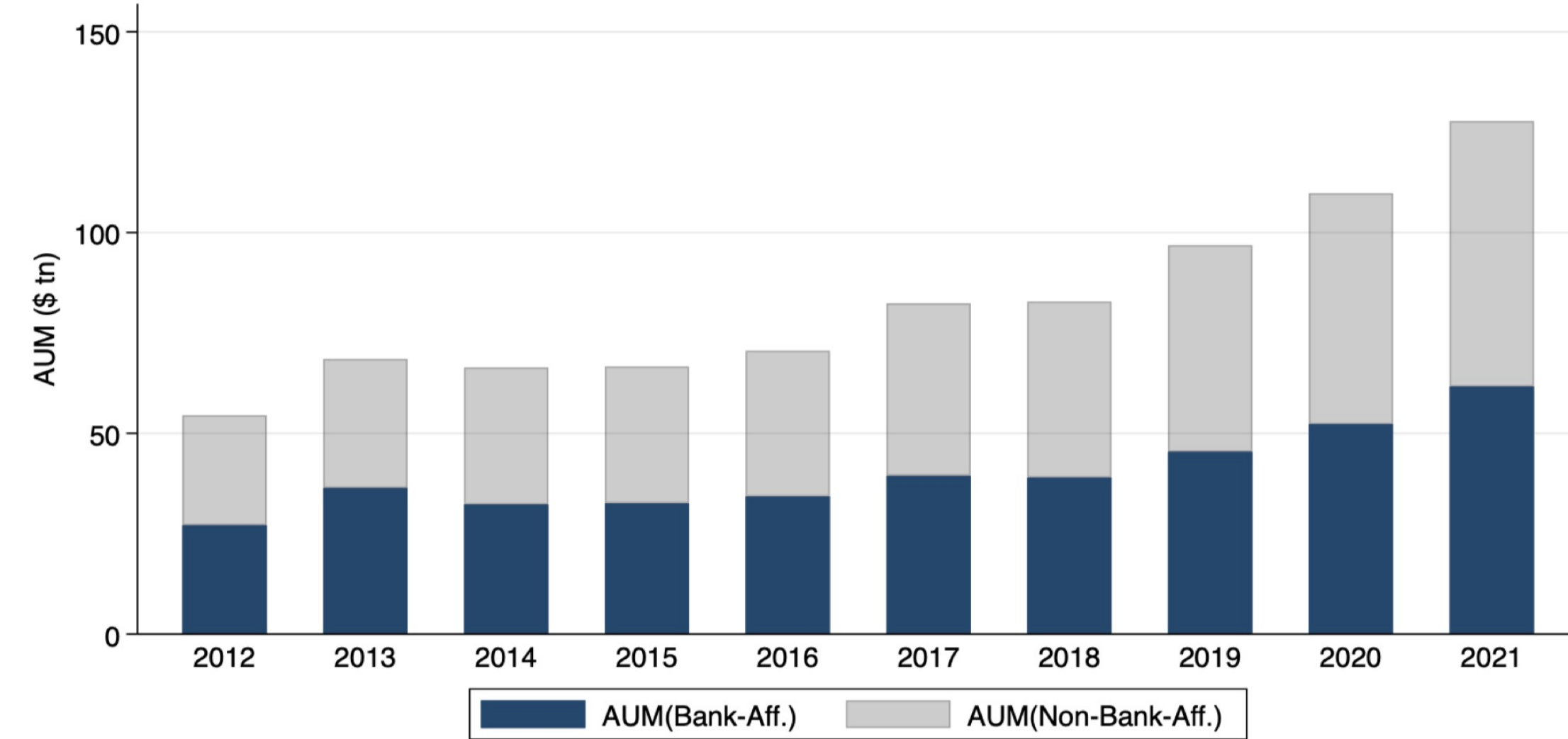
# DISTRUST SPILLOVER ON BANKS: THE IMPACT OF FINANCIAL ADVISORY MISCONDUCT

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## MOTIVATION

- >100% growth of AUM under bank affiliated investment advisory firms (RIA) in the past decade



- EU started to require 'operational risks' related to external events in its stress tests since 2014
- Fraud revelation invokes significant money outflows from fraudulent investment firms (Gurun et al. 2017, Liang et al. 2020)

## RESEARCH QUESTION

Does distrust from investment advisory fraud spillover to their affiliated banks?

- How does it impact in regional level?
- Which type of banks experience the impact?

## EMPIRICAL CHALLENGES

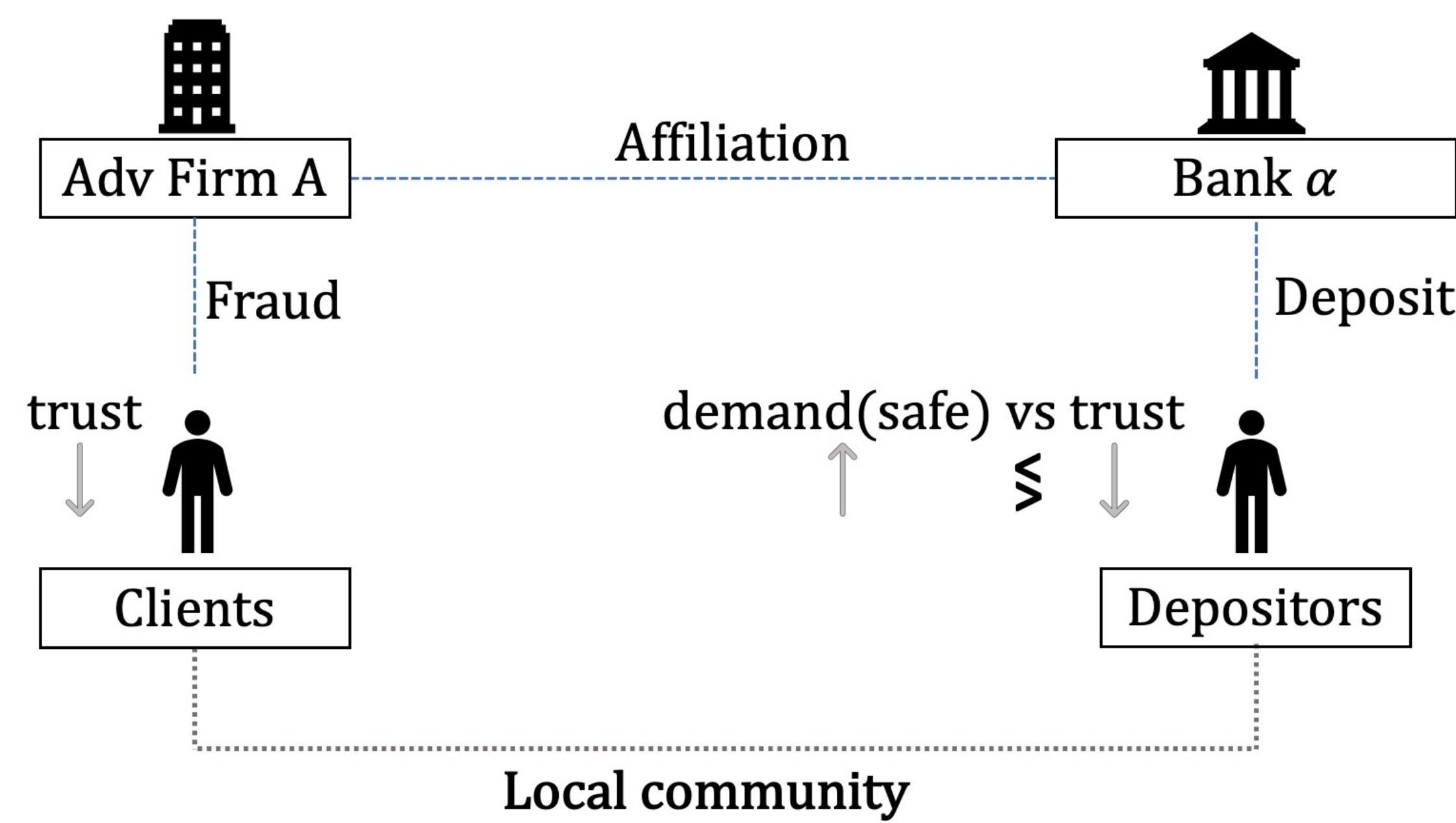
- Challenge 1:** Isolating distrust effect from concerns over potential financial distress
- Challenge 2:** Finding individual level of business affiliation links between commercial banks and RIAs
- Challenge 3:** Omitted variable that could bias the relationship between banks and advisory fraud

## SUGGESTED SOLUTION

Focus on the **deposit products**, that is perfectly insured by FDIC for average US households, so that motivation from concerns over financial distress might be insignificant.

Merge administrative data on SEC-registered RIAs to branch level data on the deposits of banks.

## CHANNEL



Supportive narrative	Trust on bank	Demand (safe asset)	Deposits
Distrust spillover	↓↓	↑	-
Deposits as safe-haven	↓	↑↑	+

## DATA

- SEC Form ADV (2012 – 2020)
- FDIC Summary of Deposits
- RateWatch

## AFILIATION LINK

Use mandatory annual reports filed to SEC If they "share business dealings" or "operations" or "refer clients"

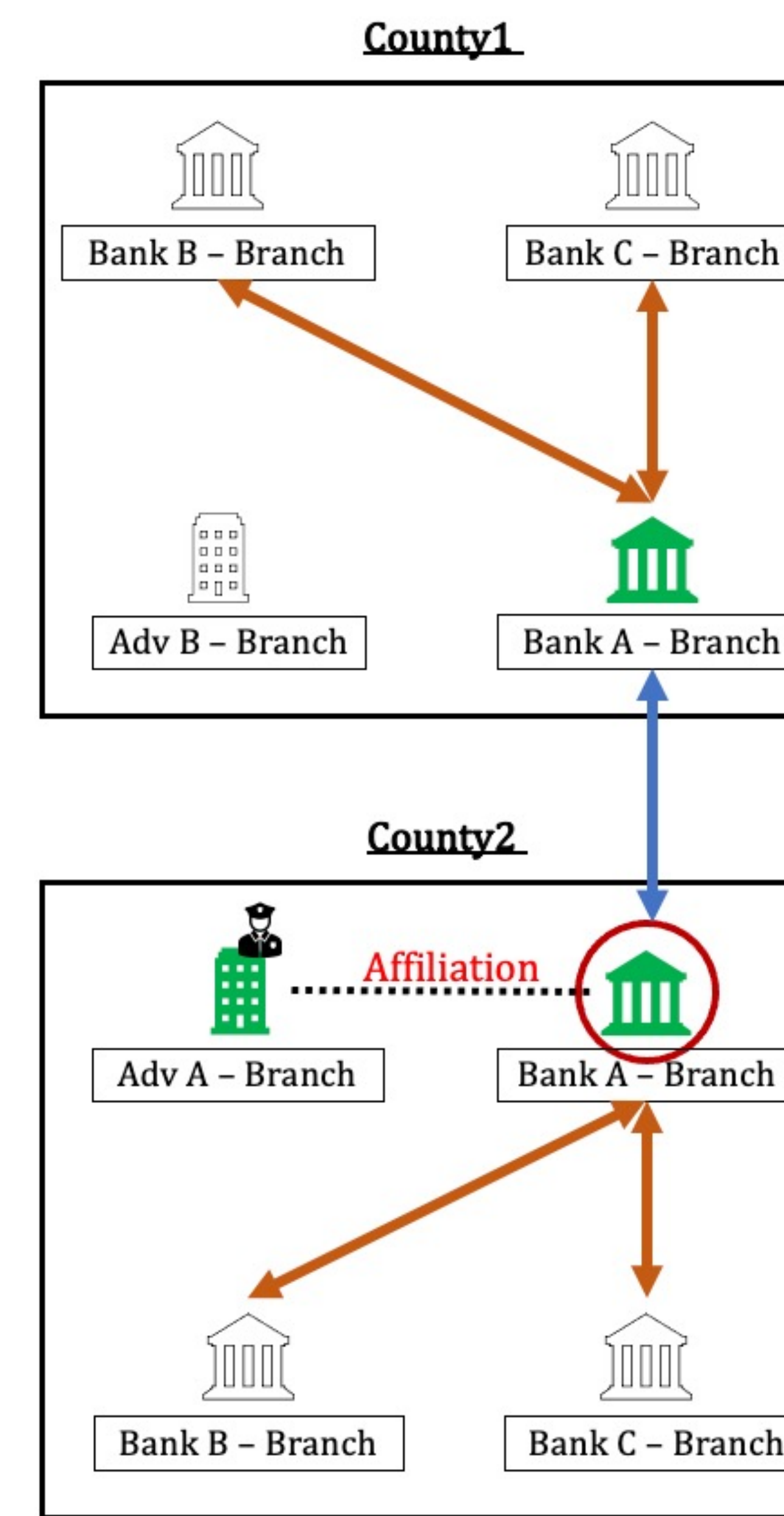
Name of RIA	Filing Date	Name of "affiliated bank"
CHASE INV. SRVC CORP	07/27/2012	JP MORGAN CHASE BANK
NIKKO ASSET MGT LLC	06/16/2012	SUMITOMO MITSUI BANK
HIGHBRIDGE CAPITAL MGT	07/21/2014	JP MORGAN CHASE BANK

## ADVISORY FRAUD

Comprehensive disciplinary actions against SEC-registered RIAs

Name of RIA	Init. Date	Agency	Allegation
CHASE INV SRVC CO	07/27/2012	CFTC	Unauthorized usage of client funds
NIKKO ASSET MGT	06/16/2012	FSA (Japan)	Insider trading
TCW INV MGT	07/21/2014	SFC (HK)	False information of fees

## IDENTIFICATION



## REGRESSION SPECIFICATION

$$y_{i,b,c,t} = \sum_{\tau=-4}^4 \beta_{\tau} I_{i,b,c,t} + BranchFE + CountyYrFE + BankYrF + \gamma' X_{i,t} + \epsilon_{i,b,c,t}$$

- $y_{i,t}$ : amounts of deposit at branch level
- Poisson regression (Cohen et al. 2022)

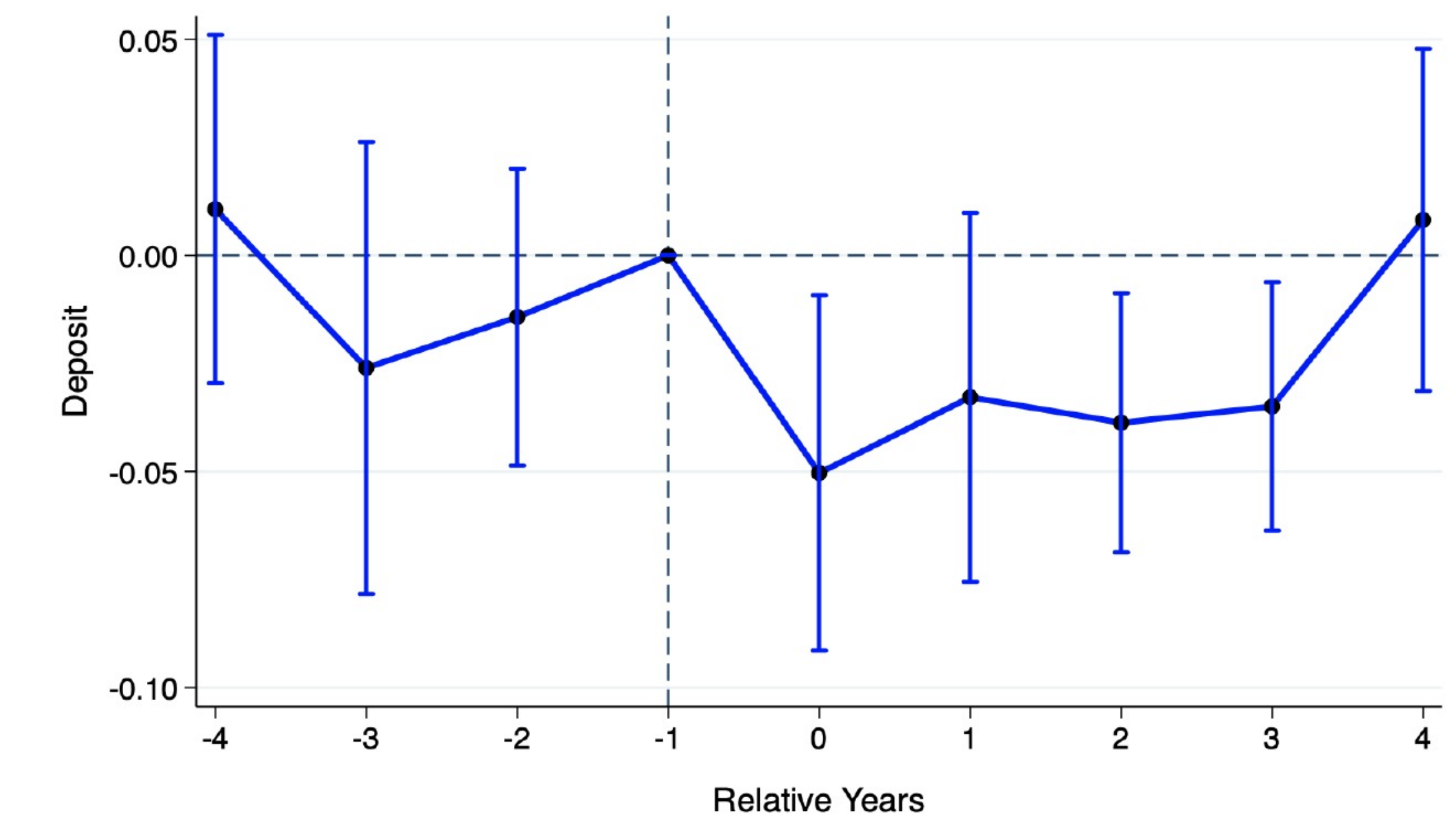
## NATURAL EXPERIMENT

- Mutual Fund Scandal in 2003
- Sudden detection initiated by a national-coverage media

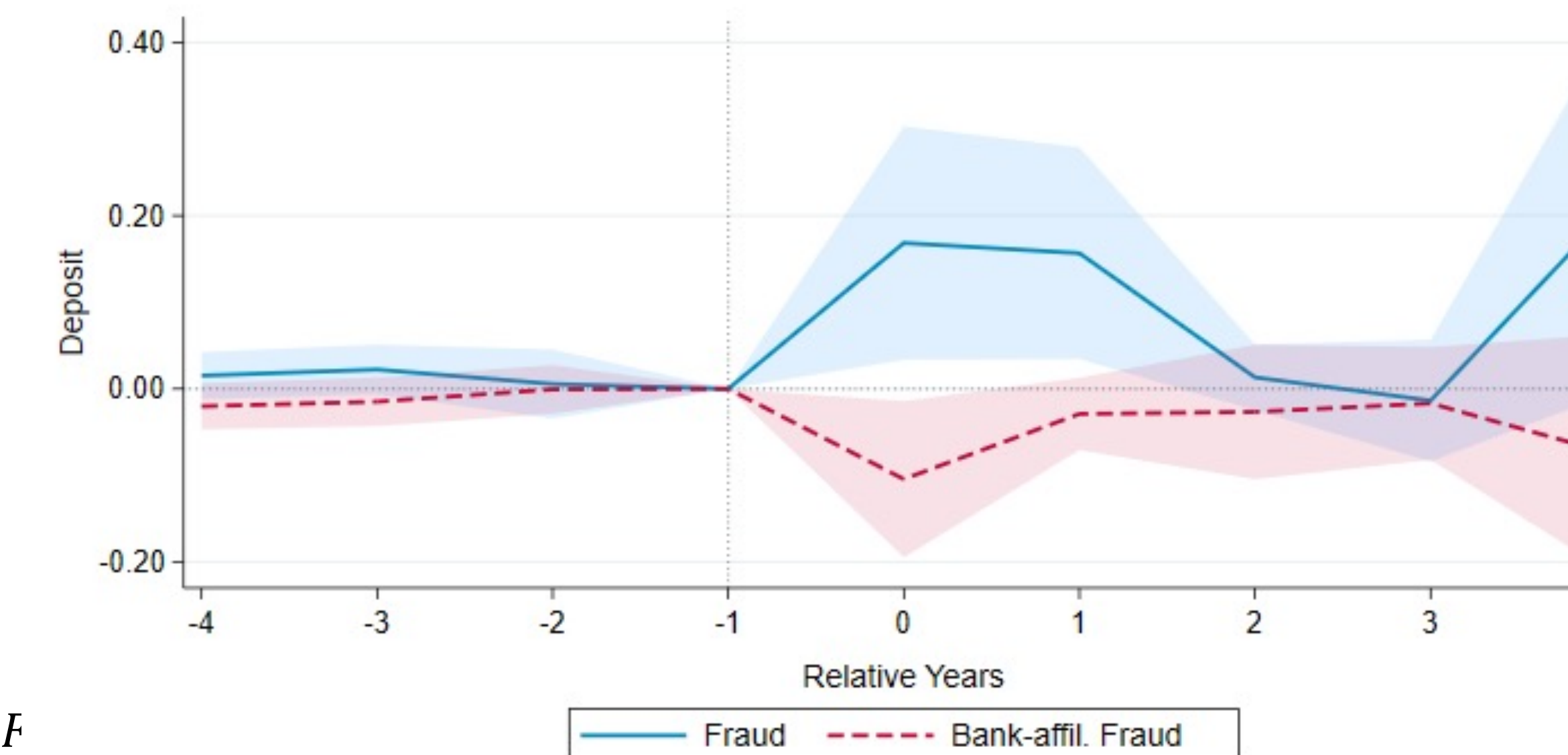
→ Can identify exact date of public recognition  
→ Exogenous variation to fraud revelation

## RESULTS

### 1. BRANCH LEVEL DEPOSITS



### 2. COUNTY LEVEL DEPOSITS



### 3. MECHANISM

Only banks share name with fraudulent RIAs experience deposit withdrawal

	Full sample		Fraudulent sample	
	(1)	(2)	(3)	(4)
Post	0.073 (0.062)	-0.036 (0.035)	0.051 (0.057)	-0.046 (0.037)
Post × Common Brand	-0.172** (0.067)	-0.067* (0.041)	-0.164*** (0.062)	-0.061 (0.043)
Controls	Yes	Yes	Yes	Yes
Branch FE	Yes	Yes	Yes	Yes
State × Year FE	Yes	No	Yes	No
County × Year FE	No	Yes	No	Yes
Bank × Year FE	Yes	Yes	Yes	Yes
Clutser	Branch	Branch	Branch	Branch
Corr(fine,common brand)	.073	.073	.073	.073
Pseudo R <sup>2</sup>	0.984	0.986	0.985	0.986
Observations	855,725	853,595	461,173	461,173