Does it Matter if Stockbrokers Get Caught Cheating? Consequences of Misconduct on Careers in the Securities Industry

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ABSTRACT

This analysis investigates the consequences of misconduct on the careers of U.S. stockbrokers. The basic expectation is that, besides official penalties, individual-level misconduct results in reputational damage and impaired future labor market opportunities. However, the consequences of misconduct seem mild on Wall Street where misconduct could be perceived by employers as a sign of aggressiveness or a cost of doing business. To address this ambiguity, we investigate the career consequences of one form of Wall Street misconduct where stockbrokers cheat their customers by generating higher fees through conducting unnecessary, unsuitable, or unauthorized transactions. Specifically, we examine whether visible instances of misconduct are associated with higher/lower likelihood of exiting the profession and being able to leave one’s current employer. We also examine whether a stockbroker’s tenure moderates the consequences of misconduct since misconduct may be a weaker signal to the market the more experienced the stockbroker is. We use the records of the Financial Industry Regulatory Authority (FINRA) which include stockbrokers’ employment history and any involvement in formal disputes with customers. We measure misconduct as disputes resulting in settlements or restitution payments to customers. Our sample includes 4,810 stockbrokers randomly selected from FINRA’s population of 1.3 million stockbrokers with employment spells at 1,940 brokerage firms during 1980-2013. Using robust linear probability models and accounting for individual, firm, and time unobserved heterogeneity, we find that stockbrokers with recent misconduct suffer negative labor market consequences. Particularly, stockbrokers who experience settlements or restitution payments are 3.7% more likely to exit the industry and 15.4% less likely to be able to change employers over the next three years than those without such judgments. We also find that higher tenure appears to weaken these negative consequences of misconduct. Ongoing analysis will help us refine and expand our findings and inform regulatory policy in the securities industry.

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INTRODUCTION

Ex ante, the career consequences of misconduct on Wall Street are ambiguous. On the one hand, in a review of organizational misconduct research, Greve, Palmer and Pozner (2010) summarize and articulate a baseline expectation that organizations and individuals who are judged to have committed wrongdoing will suffer two types of punishments: an “official” monetary or symbolic penalty, as well as impaired future prospects, either in the form of withdrawal of business partners for organizations or limited labor market opportunities for individuals. This occurs in part due to the reputational damage and negative stigma associated with misconduct. In fact, recent empirical studies indicate that officers and directors of firms implicated in accounting fraud suffer loss of positions with the focal firm and diminished subsequent job opportunities (Pozner 2008; Arthaud-Day & Certo 2006; Srinivasan 2005).

Greve, Palmer and Pozner (2010) also note that research on the consequences of misconduct for individual organizational members is limited, particularly below the officer and director level. They specifically note that “more work also needs to be done on how organizational misconduct affects organizational members below the top management level” (Greve, Palmer, & Pozner, 2010, p. 91). And they point to the substantial variance in who does or does not get punished as an opportunity for valuable research insights.

On the other hand, there are reasons to doubt this baseline expectation for financial services professionals. We have seen complaints in recent business press post-2008 financial crisis, where for all the appearance of rotten behavior, there is a concern that individuals who are caught cheating their clients are not being punished. That is, in the case of misconduct on Wall Street specifically, there has been a groundswell of concern that the consequences are mild at
best. While the U.S. government has extracted settlements and fines from financial firms, the amounts are seen as a slap on the wrist, dwarfed by the overall size of the firms/banks’ profits. Furthermore, few individuals at the implicated firms have been penalized, either monetarily or via criminal prosecutions (Frontline 2014), raising concerns that there are no consequences for individuals – punishment is borne only by shareholders (Rushton 2014).

In fact, recent work by Roulet (2014) offers interesting theory and evidence suggesting that behavior which is criticized by the society at large might be rewarded by a specific industry. In particular, he finds that firms which are more criticized by the press tend to get more business in investment banking. This finding suggests that we should not expect negative consequences to misconduct for stockbrokers if the firms in the securities industry on Wall Street do not negatively stigmatize those individuals and merely view misconduct as a sign of aggressiveness.

These contradictory arguments and evidence, then, portrays an open question when it comes to the consequences of misconduct for individuals on Wall Street – particularly for those below the top management level. To make progress on this opportunity, we investigate the career consequences of one form of Wall Street misconduct: stockbrokers cheating their customers by generating higher fees through conducting unnecessary, unsuitable, or unauthorized transactions. Being caught cheating customers may damage the reputation of both the stockbroker and her employer, which could lead to loss of current position and adverse future labor market outcomes. But it could alternatively be perceived by current and potential employers in a positive light – a sign of aggressiveness – or at least a neutral light – a cost of doing business or an unlucky experience with a disgruntled client. Our primary question, then, is whether visible instances of misconduct have an impact on stockbroker careers. In particular, are they associated with higher
or lower likelihood of exiting the profession and/or of being able to leave one’s current employer? Exiting the industry and not being able to leave one’s current employer are considered unfavorable outcomes for individuals in the securities industry where generally high mobility is expected and is associated with higher pay.

We also address Greve, Palmer and Pozner’s (2010) question about sources of variance in the consequences of misconduct. In this respect, Arnold and Hagen (1992), for instance, show that client complaints against lawyers are more likely to be prosecuted the less experienced the lawyer is. This suggests misconduct may be a stronger signal to the market the less experienced the stockbroker is. Our second question, then, is whether a stockbroker’s tenure moderates the impact of misconduct on the likelihood of exiting the industry or changing current employer.

To empirically examine our research questions, we draw on records of the Financial Industry Regulatory Authority (FINRA), the professional association and regulatory body for the U.S. securities industry. FINRA maintains records of every registered securities stockbroker. These records include employment history and any involvement in formal disputes with customers. We measure misconduct as disputes with customers which result in settlements or stockbrokers (and/or their employers) making restitution payments to customers.

Our sample includes 4,810 stockbrokers randomly selected from FINRA’s population of 1.3 million stockbrokers. The resulting panel runs yearly from 1980 to 2013 which includes employment spells at 1,940 brokerage firms.

Using robust linear probability models and accounting for individual, firm, and time unobserved heterogeneity, we find that stockbrokers with recent misconduct suffer negative labor market consequences. Particularly, stockbrokers who experience settlements or restitution
payments are 3.7% more likely to exit the industry and 15.4% less likely to be able to change employers over the next three years than those without such judgments. One interpretation of these results – which we are probing in more detail – is that stockbrokers who are caught cheating are disadvantaged in a way that they are driven from the profession and in a way that they cannot circulate to other firms. We also find that tenure does appear to moderate the effect of misconduct – such that higher tenure dampens the negative consequences of misconduct.

Future analysis will help establish more robust interpretations to build our theories of organizational misconduct as well as to inform regulatory policy in the securities industry.

We next provide a theoretical background for our investigation, describe the setting of our empirical study in more detail, provide details on our data and estimation model, present the results, and finally discuss our results and their implications.

**THEORY**

To theorize about the career consequences of misconduct on Wall Street, we draw from two sets of literatures which seem to offer contradictory insights – the literature on organizational misconduct and the literature on institutional logics. On the one hand, the longstanding arguments in the organizational misconduct literature seem to suggest that organizations and individuals who engage in misconduct will be penalized in two ways upon getting caught. First, they suffer an official monetary or symbolic penalty, imposed to them by a “social control agent” such as the government or a regulatory body (Greve, Palmer, & Pozner, 2010). Second, they suffer impaired future prospects, either in the form of withdrawal of business partners for organizations or limited labor market opportunities for individuals (Greve,
Palmer, & Pozner, 2010). Recent empirical studies support this expectation in the way they find that officers and directors of firms implicated in accounting fraud suffer loss of positions with the focal firm and diminished subsequent job opportunities (Pozner 2008; Arthaud-Day & Certo 2006; Srinivasan 2005).

While the former punishment in the form of official penalties is of interest to legal scholars, the latter punishment in the form of limited labor market opportunities is of significant interest to scholars in organizational studies. In this respect, these scholars have proposed various theoretical mechanisms to explain the negative career consequences of misconduct. In one line of reasoning, Lorsch and MacIver (1989), for example, argue that misconduct signals to the market certain inadequacies, including unfavorable performance and quality, which will then limit future labor market opportunities for the individuals involved. In another line of reasoning, Pozner (2008), for instance, argues that to the extent to which misconduct represents deviation from accepted rules, regulations, and norms in general, it comes with reputational damage and negative stigma. The resulting stigma in turn reduces the social acceptability of those who are involved with misconduct (Carter & Feld, 2004; Kurzban & Leary, 2001) in a way that would limit their subsequent career opportunities, as others seek to dissociate themselves to lessen the threat to their identities and image (Pozner 2008). This line of reasoning further suggests that the more controllable is the deviation from the acceptable norms, the greater will be the extent to which an individual faces stigmatization (Goffman, 1986). That is to say, if the market perceives an individual to be in control of the act of misconduct, the greater will be the extent to which the market would seek to dissociate.
Taken together, these arguments seem to suggest that stockbrokers who are caught cheating their clients suffer negative consequences in two specific ways career-wise. First, they are more likely to exit the industry because the perceived inadequacies in their performance will lessen their market value or simply because they seek to “avoid difficult interactions with the untainted” (Pozner, 2008, p.145). Second, they are less likely able to change employers because other brokerage firms do not wish to associate – particularly because stockbrokers have high level of discretion/control in what they do and therefore their act of misconduct will be of a greater negative signal. In this respect then, we hypothesize that stockbrokers’ visible instances of misconduct lead to negative career consequences:

**Hypothesis 1a:** stockbrokers’ visible instances of misconduct are associated with higher likelihood of exiting the profession.

**Hypothesis 1b:** stockbrokers’ visible instances of misconduct are associated with lower likelihood of being able to leave current employer.

These arguments can also inform Greve, Palmer and Pozner’s (2010) call for examining the sources of variance in the consequences of misconduct. In particular, these arguments seem to further suggest that the negative consequences of visible misconduct are weakened for those stockbrokers with higher tenure for two reasons. First, misconduct may be a weaker signal of inadequacies to the market the more experienced the stockbroker is since the market has more historical information on the performance and qualities of a more experienced individual to go by. Second, in a similar fashion, misconduct may be a weaker stigmatizing signal to the market for more experienced stockbrokers. In this case, in the aftermath of misconduct, others might think that such experienced perpetrators have been around long enough to know better, so there must have been something else that facilitated misconduct above and beyond their control. Arnold and Hagen’s (1992) finding provide some support for these arguments as they show that
client complaints against lawyers are more likely to be prosecuted the less experienced the lawyer is. In light of this, we hypothesize that higher tenure dampens the negative career consequences of stockbrokers’ visible instances of misconduct:

Hypothesis 2a: higher tenure weakens the positive relationship between stockbrokers’ visible instances of misconduct and likelihood of exiting the profession.

Hypothesis 2b: higher tenure weakens the negative relationship between stockbrokers’ visible instances of misconduct and likelihood of being able to leave current employer.

On the other hand, the literature on institutional logics provides reasons to doubt the baseline expectation around the negative consequences of misconduct for financial services professionals on Wall Street. In this respect, recent research suggests that certain behavior in an industry which is criticized by the society at large might be rewarded by that industry itself. In doing so, for example, Roulet (2014) notes that “if loyalty to resistant logics is valued enough by crucial groups of stakeholders, it might be better for an actor to preserve the vilified logics rather than change” (Roulet, 2014, p. 26). He in fact finds that firms which are more criticized by the press for their societally perceived questionable behavior tend to get more business in investment banking. At the core of it, the argument is that when there is conflict between behavioral norms that an actor can adapt (e.g., engage in misconduct or not), the actor will benefit most from adapting to the norm that is local to them as opposed to the norm that is distant but is perhaps more universal (i.e., being loyal for better evaluation by peers).

These arguments seem to suggest that we should not expect negative but rather expect positive career consequences to misconduct for individuals in the securities industry on Wall Street where being caught cheating customers could be perceived by current and potential employers in a positive light – a sign of aggressiveness – or at least a neutral light – a cost of
doing business or an unlucky experience with a disgruntled client. That is to say misconduct does not disadvantage stockbrokers to drive them from the profession, and that they are able to circulate to other firms. In this context, we therefore expect and hypothesize that stockbrokers’ visible instances of misconduct lead to positive career consequences:

**Hypothesis 1a**: stockbrokers’ visible instances of misconduct are associated with lower likelihood of exiting the profession.

**Hypothesis 1b**: stockbrokers’ visible instances of misconduct are associated with higher likelihood of being able to leave current employer.

As for Greve, Palmer and Pozner’s (2010) question about sources of variance in the consequences of misconduct, these arguments seem to further suggest that the positive consequences of visible misconduct are weakened for those stockbrokers with higher tenure. That is to say, misconduct early in the career will provide a greater signal of aggressiveness and loyalty to the local norms and ultimately will enhance future labor market opportunities, whereas misconduct later in the career will provide a lesser signal of aggressiveness and will raise doubt on the loyalty of the individual involved to the local norms (i.e., it will be too late to signal one’s aggressiveness/loyalty later during the career to the industry). We therefore expect that higher tenure dampens the positive career consequences of stockbrokers’ visible instances of misconduct:

**Hypothesis 2a**: higher tenure weakens the negative relationship between stockbrokers’ visible instances of misconduct and likelihood of exiting the profession.

**Hypothesis 2b**: higher tenure weakens the positive relationship between stockbrokers’ visible instances of misconduct and likelihood of being able to leave current employer.

These contradictory theoretical arguments raise an open question when it comes to the consequences of misconduct for individuals on Wall Street – particularly for those below the top management level – which set the stage for an empirical investigation.
EMPIRICAL SETTING

To empirically make progress on this opportunity, we investigate the career consequences of one form of Wall Street misconduct, namely stockbrokers cheating their customers by generating higher fees through conducting unnecessary, unsuitable, or unauthorized transactions, in the context of the U.S. securities industry.

We chose the U.S. securities industry as the setting for our empirical analysis because it satisfies several characteristics that facilitate the examination of our research questions: well-defined misconduct, relatively cheap mechanisms by which to seek visible adjudication of alleged misconduct, archives of individuals’ employment history and records of misconduct, and relatively high mobility across employers.

At its core, the securities industry consists of firms that buy and sell financial securities on behalf of clients. This includes not only buying and selling existing securities, but also underwriting new securities issues; hence, the industry includes both stockbrokerages and investment banks. The boundaries of the industry are reasonably well-defined in the U.S. because securities trading is regulated under the provisions of the Securities Exchange Act of 1934. Any company that trades securities for its own account or on behalf of clients is required to register as a “broker/dealer” with the Securities and Exchange Commission (SEC) and with one of the industry’s self-regulatory organizations (SROs), either FINRA or a specific stock exchange.

Employees who act as agents of broker/dealer firms (i.e., stockbrokers) must also be registered with the SEC and one of the SROs. Hence, they are often referred to as “registered representatives” (RRs). Registration as a stockbroker requires passing an exam to establish
knowledge of financial securities, securities order processing, and ethical responsibilities to clients and for acceptable conduct.

As part of its mandate to regulate the licensing and professional behavior of securities stockbrokers, FINRA maintains a database of every person who is or has been registered as a securities broker, including their employment history within the securities industry and any involvement in formal customer disputes that entered the mandatory arbitration process and/or disciplinary actions by regulators. This database is publicly available, in order to allow investors to check the licensing, training, and dispute history of a potential stockbroker. In a similar way, the employers review these records when they are recruiting.

For a given stockbroker, the FINRA database includes information on who the stockbroker has been employed by (as a stockbroker) and for how long. It also includes information on whether the stockbroker has been involved in any customer disputes or regulatory actions, and what the outcomes of such disputes or actions have been.

Within the U.S. securities industry, stockbrokers’ actions are governed by a set of conduct rules maintained and enforced by the SROs (principally, FINRA). These rules establish a range of ways in which stockbrokers can be responsible for failing to protect clients’ interests, either through fraud or negligence (Astarita, 2008). The most common bases for disputes between customers and their stockbrokers include customers’ claims of: churning, in which stockbrokers transact securities on behalf of clients solely for the purpose of charging commissions; unauthorized trading, in which stockbrokers buy or sell securities without the client’s knowledge or approval; unsuitability, in which stockbrokers recommend securities that are not appropriate for the client’s age or stated investment objectives; misrepresentation, in
which a stockbroker fails to disclose important facts about or even misrepresents the nature of an investment; and negligence, in which a stockbroker has simply “failed to use reasonable diligence in the handling of the affairs of the customer” (Astarita, 2008).

Remedies for alleged violations of these conduct rules may be pursued in two ways: through private action by customers via a mandatory arbitration process or through public investigation and sanction by the regulator, FINRA.

Since 1989, standard contracts between customers and their stockbrokers require that disputes be resolved through mandatory binding arbitration rather than through lawsuits in the courts (Choi & Eisenberg, 2010; Choi, Fisch, & Pritchard, 2010). In arbitration, both sides represent their case to a panel of three arbitrators. The panel of arbitrators includes two public arbitrators and one industry arbitrator, where public arbitrators have minimal ties to the securities industry (and are predominantly lawyers) and are intended to bring a neutral perspective, while industry arbitrators are securities industry participants (including stockbrokers or lawyers who also work with securities firms) and are intended to bring expertise (Choi & Eisenberg, 2010; Choi, Fisch, & Pritchard, 2010).

While the decisions of arbitrator panels are likely imperfect, they represent the judgment of a panel of experts as to whether a brokerage firm and/or an individual stockbroker treated a customer in contravention of the profession’s conduct code and thus seem a credible signal of whether misconduct occurred. Furthermore, this process is easier and less expensive to initiate than court-based private action. This suggests that customers likely pursue more cases than would be the case in many other settings in which the process is court-based. This then partially
mitigates the gap, endemic to misconduct research (e.g., Krishnan & Kozhikode, 2014), that exists between actual versus observed misconduct.

According to Section 15A of the Securities Exchange Act of 1934 and FINRA Rule 8310, FINRA can impose a variety of sanctions on stockbrokers and securities firms that are found guilty of an infraction, including limitation (where a respondent’s business activities are limited or modified), fine, censure, suspension (where a respondent’s business activities are suspended for a specific period of time or until certain act is performed), and bar/expulsion (where a respondent stockbroker or firm is barred from the securities industry).

**DATA, MEASURES, AND MODELS**

This section presents more detail on our data, our three different but related measurements of organizational misconduct, and the econometric models we used to estimate our effects of interest.

**Data**

From FINRA records, we drew a random sample of 4,810 individuals from the population of the 1,301,584 people who were registered with FINRA as a securities broker in the U.S. during 1980-2013, including their employment spells at 1,940 brokerage firms.

We then collected the selected stockbrokers’ complete work histories including instances of misconduct. We create a panel dataset from 1980 to 2013. The FINRA data identifies the dates of employment as a registered representative at any licensed stockbroker/dealer firm; the time when any customer disputes were filed and resolved; the manner in which those disputes
were resolved (dismissal, settlement, or monetary judgment against the stockbroker); and the
time that any regulatory actions were announced.

Our sample is unique because individual stockbrokers and their employers are identified
and followed over time and the employment relationship between a stockbroker and his/her
employer is continuously monitored.

Measures

As we discussed earlier, stockbrokers can cheat their clients by fraud or negligence.
There are two ways that misconduct can be investigated and enforced. The first way is through
formal complaints by clients which can either result in restitution payments after an arbitration
hearing (if not dismissed) or result in a settlement. That is, client disputes might result in some
kind of payment if not dismissed. The second way is through regulatory investigation which can
result in limitation of activities, censure, suspension, and bar. We summarize these processes in
Figure 1.

As shown in the figure with red circles, our measurement of organizational misconduct is
two-fold: (1) whether or not there are disputes with customers which result in settlements or
stockbrokers (and/or their employers) making restitution payments to customers; and (2) whether
or not there are regulatory actions against a stockbroker – in three years prior to any given year
for each individual.
We adopt a 3-year perspective in measuring misconduct to address a potential concern about reverse causality where one could argue that perhaps people first form intentions – e.g., “I’m going to leave this job or the profession soon” – then act accordingly – e.g., “since I’m going to leave, I can throw caution and cheat to make money without regard for future opportunities”. We also measure misconduct as a dichotomous variable in this study to isolate the qualitative effect of misconduct. But perhaps in our future work we could explore whether there is a bigger effect for those for whom it is a second or third or n’th offense – i.e., we could address the question: do repeat offenders/offenses send a stronger signal to the market?

We also measure two specific career outcomes. Exit is set to 1 for an individual in the year beyond which we do not observe that individual in our dataset, and is set to 0 for that individual prior to that year. Employer change is set to 1 for an individual in every year when she moves to a new employer, and is set to 0 for that individual in other years. While there is a caveat in using these outcomes where it is not clear why individuals exit and whether employer change is categorically favorable or unfavorable, exiting the industry and not being able to leave one’s current employer are generally considered unfavorable outcomes for individuals in the securities industry where generally high mobility is expected and is associated with higher pay. We are also collecting information on firm size and status to be able to determine if a stockbroker is perhaps “moving up or down” as they change employers.

We measure firm tenure based on the number of years an individual was employed with a firm and industry tenure based on the number of years an individual was employed in the securities industry.
**Estimation Model**

To test our hypotheses, we use linear probability models with robust standard errors. We do so because (a) for large number of observations it is a relatively close approximation of logistic regression which we had to use otherwise and (b) it is unbiased and does not suffer incidental parameter problem which is common for logistic models with too many fixed effects (Bennett, Pierce, Snyder, & Toffel, 2013). We also account for individual, firm, and time unobserved heterogeneity (Abowd & Kramarz, 1999a; Abowd & Kramarz, 1999b; Abowd, Kramarz, & Woodcock, 2008; Woodcock, 2011).

To do so, we estimate Equation 1:

\[
y_{it} = \theta_i + \psi_{J(i,t)} + T_t + x_{it}\beta + x_{it}\tau + \epsilon_{it}
\]

Equation 1

where the dependent variable is exit/change in year t for individual i (0 or 1), the function J(i,t) indicates the employer of stockbroker i at time t, the first component is the stockbroker fixed effects, the second component is the firm fixed effects, the third component is the year fixed effects, the fourth component is organizational misconduct (restitution or settlement in three years prior to year t for individual i), the fifth component is the interaction of misconduct and firm/industry tenure (number of years), and the last component is the statistical residual, orthogonal to all other effects in the model.
RESULTS

Basic Descriptive Statistics

Table 1 presents basic statistics of our variables in our sample. This table shows that our simple random panel consists of 4,810 stockbrokers (from which 2,507 move at least once during their career) and 1,940 firms in which these stockbrokers were employed sometime in their career during 1980-2013.

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Insert Table 1 about here
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This table also shows that 1.33% of the stockbrokers experience some kind of payment in 3-year periods. The average firm tenure is 5.5 years and the average industry tenure is 9.9 years. On average, 9.5% of the stockbrokers exit the industry every year while 21.5% of the stockbrokers change employers each year.

Linear Probability Regression Analysis

Table 2 summarizes the main results of our regression models for when misconduct is measured as restitution payment or settlement. The table reports results from two models applied to the sample. Model 1 reports the results for exit dependent variable. Model 2 reports the results for employer change dependent variable.

As this table shows, we find that stockbrokers with recent misconduct suffer negative labor market consequences. Particularly, stockbrokers who experience settlements or restitution payments are 3.7% more likely to exit the industry and 15.4% less likely to be able to change
employers over the next three years than those without such judgments. These figures are considerable given the baseline exit and employer change levels of 9.5% and 21.5% respectively.

We also find that, in all cases save one, tenure does appear to moderate the effect of misconduct. In particular, we find that higher firm tenure dampens the positive relationship between misconduct and exit by 0.27%. As well, we find that higher industry tenure dampens the negative relationship between misconduct and employer change by 0.72% while higher firm tenure dampens the negative relationship between misconduct and employer change by 0.79%.

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Insert Table 2 about here
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We summarize these findings in Figure 2.

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Insert Figure 2 about here
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Table 3 summarizes the main results of our regression models for when misconduct is measured as regulatory sanction. The table reports results from two models applied to the sample. Model 3 reports the results for exit dependent variable. Model 4 reports the results for employer change dependent variable.

As this table shows, when we measure misconduct by whether or not a stockbroker experienced a regulatory action in a year or not, we find no significant results for our hypothesized effects. But it is unclear if this is meaningful or is a result of having smaller number of these cases.
DISCUSSION, LIMITATIONS, AND IMPLICATIONS

Using robust linear probably analyses of a random sample of stockbrokers, we address an ambiguity in our understanding of the career consequences of misconduct on Wall Street and find that stockbrokers with recent misconduct suffer negative labor market consequences, i.e., we find support for hypotheses 1a and 1b. One interpretation of these results – which we are probing in more detail – is that stockbrokers who are caught cheating are disadvantaged in a way that they are driven from the profession and in a way that they cannot circulate to other firms. We also find that tenure does appear to moderate the effect of misconduct in the way that higher tenure dampens the negative consequences of misconduct, i.e., we find support for hypotheses 2a and 2b.

There are caveats when interpreting the findings of our study though. First, at this time we do not include any observable organizational factors in our models – beyond the variables we specified earlier. Inclusion of observable organization-level characteristics such as size and status as well as additional observable individual-level characteristics such as age and asset-under-management might affect the results of our study. Second, our sample potentially suffers from survivorship bias as well as from some of the endemic issues to the organizational misconduct research, including the facts that not all misconduct is discovered/punished. Third, our estimation models might raise general concerns about endogeneity and to address that in the future we could
consider doing a matched sample analysis or identifying some sample of stockbrokers that “almost” got caught cheating, as a control sample, to accurately identify the effect of getting caught itself. Our future work will refine and expand our analyses along these lines.

Notwithstanding these challenges, our study contributes to academic research on organizational misconduct. In addressing our research questions, our study validates Greve, Palmer, and Pozner’s (2010) articulated baseline expectations and adds additional nuance to them – by providing evidence from below top management level and by identifying sources of variance in the consequences of misconduct. And more broadly, our study addresses calls by prominent scholars in the field of organizational misconduct by offering a systematic/objective analysis of panel data over a long period of time (rather than cross-sectional data) from actual organizations (rather than student samples) (Smith-Crowe, Tenbrunsel, Chan-Serafin, Brief, Umphress, Joseph, 2014; Craft, 2013; Kish-Gephart, Harrison, & Trevino, 2010; Tenbrunsel & Smith-Crowe, 2008). Future analysis will help establish more robust theories of organizational misconduct as well as to inform regulatory policy in the U.S. securities industry.
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TABLE 1

Basic Descriptive Statistics

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<th>Value</th>
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<td># firms</td>
<td>1940</td>
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<td># mover persons</td>
<td>2507</td>
</tr>
<tr>
<td>Year</td>
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<tr>
<td>Average recent misconduct (payment)</td>
<td>1.33%</td>
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<tr>
<td>Average firm tenure</td>
<td>5.5 years</td>
</tr>
<tr>
<td>Average industry tenure</td>
<td>9.9 years</td>
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<tr>
<td>Average exit</td>
<td>9.5%</td>
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<tr>
<td>Average employer change</td>
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# TABLE 2

Misconduct Measured as Restitution Payment or Settlement

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| Robust | Yes | Yes |
| Person FE | Yes | Yes |
| Firm FE | Yes | Yes |
| Time FE | Yes | Yes |
| # observations | 50569 | 50569 |
| # persons | 4810 | 4810 |
| # firms | 1940 | 1940 |
| # mover persons | 2507 | 2507 |
| FE F-test significant? | Yes | Yes |
| r-squared | 0.6726 | 0.2641 |

Notes: Figures in smaller type are estimated robust standard errors. + p<0.10; * p<0.05; ** p<0.01
### TABLE 03

**Misconduct Measured as Regulatory Sanction**

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| Robust | Yes | Yes |
| Person FE | Yes | Yes |
| Firm FE | Yes | Yes |
| Time FE | Yes | Yes |
| # observations | 50569 | 50569 |
| # persons | 4810 | 4810 |
| # firms | 1940 | 1940 |
| # mover persons | 2507 | 2507 |
| FE F-test significant? | Yes | Yes |
| R2 | 0.6726 | 0.2636 |

Notes: Figures in smaller type are estimated robust standard errors. + p<0.10; * p<0.05; ** p<0.01
FIGURE 1
Misconduct

- Misconduct
  - Churning
  - Unsuitability
  - Misrepresentation
  - Unauthorized trading
  - Negligence

- Private action by client: i.e., formal complaint

- Regulator investigation

- Arbitration hearing

- Restitution if not dismissed

- Settlement

- Sanction if not dismissed
  - Limitation
  - Censure
  - Suspension
  - Bar
FIGURE 02

Misconduct Measured as Restitution Payment or Settlement

Recent misconduct → Exit

-0.27%*

Firm tenure

Industry tenure

Baseline exit: 9.5%
Exit model R²: 67%

Recent misconduct → Employer change

-15.41%**

Firm tenure

Industry tenure

Baseline change: 21.5%
Change model R²: 26%

Robust: Yes
# observations: 50569
FE F-test significant? Yes
* p<0.05; ** p<0.01