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MISCONDUCT SYNERGIES

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ABSTRACT

Do corporate control transactions discipline the labor force? Consistent with synergies, new disclosures of employee misconduct in the investment advisory industry drop by between 17 and 22 percent following mergers. Both targets and acquirers have better pre-merger misconduct records than the industry's average firm and, within the subsample of merging firms, there is assortative matching on misconduct. Merger events facilitate further reductions in misconduct through separations of target firm employees with high misconduct. Many of these employees remain in the industry, suggesting that consolidation plays an important role in the redistribution of misconduct across firms.

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I. Introduction

The investment advisory industry has seen high levels of M&A activity and significant consolidation during the past 10-15 years.[1] Does this consolidation have implications for the level of misconduct in merging firms and for the distribution of misconduct across the industry? We use the investment advisory industry as a laboratory to test for evidence of "misconduct synergies" (i.e., reductions in disclosures of employee misconduct) following M&A transactions. The industry is of particular interest because it has seen rapid consolidation and because there is strong evidence of persistent misconduct, where some firms specialize in misconduct, while others do not (Egan, Matvos and Seru, 2019). Although the patterns are robust in the data, we still do not understand fully the underlying mechanisms driving them. Our main goal is to examine whether mergers can help explain the persistence and clustering of misconduct across firms in the investment advisory industry.

We find that, consistent with misconduct synergies, disclosures of new disciplinary events in the combined firm drops by between 17 and 22 percent following mergers that occurred during the 2011 through 2020 sample period. This reduction is driven mainly by separations of high misconduct employees at the target firm. Layoffs following mergers are a well-documented source of cost savings in M&A (e.g., Bhagat, Shleifer, Vishny, Jarrel and Summers, 1990; Haleblian, Devers, McNamara, Carpenter and Davison, 2009; Lee, Mauer and Xu, 2018); however, the question of whether the "right" employees leave is an open and important question on which this paper sheds light.

While plausible, the hypothesis that M&A changes the conduct of rank-and-file employees is difficult to test because employment records and instances of fraud and misconduct are generally unavailable at the individual employee level. The investment advisory industry is particularly useful because firms must report disciplinary and regulatory events, along with general information about business operations, to the SEC. In addition, because investment advisors are registered and licensed, information regarding advisors' individual employment histories and disciplinary events are reported to regulators and made available to the public via FINRA's BrokerCheck and the SEC's IAPD system.

Throughout the paper, we use the term "All Employee Disclosures" to describe any disclosure across the 23 categories of disciplinary events in the FINRA BrokerCheck and

[1] For press coverage of the consolidation trend, see e.g., Fidelity (2022), DeVoe (2019), and Nasdaq (2021).

the SEC's IAPD data. These include customer disputes, regulatory investigations and actions, certain criminal and civil proceedings, and bankruptcy filings.[2] It is important to emphasize that not all of these disclosures are evidence of employee wrongdoing. To account for this, we separately analyze the six categories of disclosures that Egan, Matvos and Seru (2019) consider to be most indicative of employee misconduct. We use "Employee Misconduct (EMS)" to describe this subset of less ambiguous disclosures. Even though the strict definition helps to clarify the overall interpretation, Egan, Matvos and Seru (2019) report that the advisors with disclosures outside of these six categories are also more likely to have engaged in misconduct under the stricter "Employee misconduct (EMS)" definition when compared to advisors without such disclosures. Therefore, we present our findings using both measures and we interpret changes in either "All Employee Disclosures" or "Employee Misconduct (EMS)" as indicative of changes in employee misconduct.

Ex ante, it is not obvious that misconduct is relevant in M&A, nor is it obvious that consolidation changes the level of misconduct within merging firms or the distribution of misconduct across firms in the industry. For example, a reasonable null hypothesis is that the merged firm requires employees to continue their work as they did when employed by stand-alone firms and that expected adviser misconduct in the merged firm is a weighted average of what we would have expected in the stand-alone firms. Alternatively, it could be that the anticipated merger synergies stem from business models that seek to avoid (or encourage) misconduct. This would result in less (or more) misconduct in the merged firm. Under the alternative hypothesis, business combinations could be an important channel through which misconduct is distributed (and redistributed) across firms within the industry. If so, mergers could help explain the misconduct persistence and specialization highlighted in Egan, Matvos and Seru (2019).

We begin by examining whether misconduct is relevant in M&A. The analysis reveals two interesting patterns. First, both targets and acquirers have lower levels of pre-merger employee misconduct relative to firms that do not engage in M&A. Second, within the sample of targets and acquirers, we find evidence of assortative matching where high misconduct acquirers tend to purchase high misconduct targets. This is consistent with a "like buys like" view of mergers where complementarities in human capital are important.[3] Assortative matching could reflect avoidance of costly culture clashes post-merger

[2] See the Appendix in Egan, Matvos and Seru (2019) for definitions of each disclosure category.
[3] Rhodes-Kropf and Robinson (2008) present a model where gains from M&A come from placing com-

(e.g., Gorton and Zentefis, 2023). It can also reflect strategies to manage the spread of misconduct among employees of the combining firms (Dimmock, Gerken and Graham, 2018). In a general setting, Easley and O'Hara (2023) show how unethical behavior can spread when markets are tightly connected. They also show that ethical behavior can persist when there are dense clusters of individuals who behave ethically. In our context, the implication is that target firms with a high density of low misconduct employees are desirable to acquirers wishing to maintain cultures of low misconduct.[4]

Our main finding is that new disclosures of misconduct fall significantly post-merger. To help interpret this, we compare each true merged firm to a matched pseudo merged firm based on pre-event disclosures, recent growth in disclosures, the number of registered employees, and the lines of business in which the advisory firm operates (i.e., a difference-in-differences approach). We find a large post-event reduction in misconduct in the true merged firm relative to the control.

What are the mechanisms driving the substantial decline in employee misconduct following M&A transactions that we observe? Are there more post-merger layoffs and separations among employees with disclosures? Or, do the improvements occur through better employee behavior following the merger? When we examine separation patterns following M&A transactions, we find that pre-merger employees of target firms are more likely than acquiring firm employees to separate from the combined firm. Moreover, we find that target employees with misconduct histories are especially likely to depart following a merger. Pre-merger, we observe lower sensitivities of separations to misconduct at the target firm relative to what we observe at the acquirer. Although all sensitivities increase post-merger, the increase ranges from 57% to more than 100% for target firm employees, depending on the misconduct measure. For acquiring firm employees, we observe either no increases or small decreases in sensitivities post-merger. Thus, a tightening in the disciplinary environment for target firm employees can explain the improvements in misconduct that we observe following the merger. We find only weak evidence of a reduction in new disclosures post-event for target firm employees remaining with the firm. In other words, employee turnover drives the main results, not changes in the behavior

plementarities assets under common control rather than substituting "bad" for "good," as in the traditional view of mergers (Manne, 1965). Unlike the misconduct focus in our paper, Rhodes-Kropf and Robinson (2008) focus on valuation. They report that acquirers and targets are typically less than one valuation decile apart, even after controlling for industry.

[4] Thanassoulis (2023) also provides a theoretical framework to explain the prevalence of misconduct. He focuses on the link between misconduct and the competitive structure of the market and finds that the type of demand and type of moral issue can explain this relationship.

of the remaining employees.

Most departing employees join different firms after separation. We use this fact to undertake counterfactual analysis, in which we track the misconduct disclosures of departed employees to help understand what misconduct patterns we would have observed had they stayed at the combined firm post-merger. When we compare the hypothetical firm to the actual combined firm, we see that we would have observed much flatter variation in misconduct had the departing employees remained. High misconduct employees continue to have high levels of disclosures after separation. Egan, Matvos and Seru (2019) report that some firms "specialize" in misconduct and others do not. Our findings show that mergers are an important driver of the redistribution of misconduct across firms in the investment advisory industry.

The remainder of the paper is organized as follows. In Section 2, we discuss related literature and a framework for examining the role of consolidations in employee misconduct. In Section 3, we describe the source of data on registered investment advisors, the sample of merger events, and measures of misconduct. We provide descriptive statistics in Section 4. In Section 5, we report results of the main regression analyses. Section 6 concludes.

II. Related literature and framework

A. Literature

Existing work on M&A as a potential disciplinary mechanism focuses mainly on the departures of top managers (Martin and McConnell, 1991; Agrawal and Walkling, 1994; Hartzell, Ofek and Yermack, 2004; Wulf and Singh, 2011). Ours is one of the few papers in the empirical finance literature to ask whether M&A brings improvements among rank-and-file employees of combining firms and how departures of employees near merger events are distributed. Wu and Zang (2009) and Lee, Mauer and Xu (2018) are the closest papers to our work in that both are interested in changes in human capital near merger events. Wu and Zang (2009) document high turnover of sell-side financial analysts near mergers. Unlike our paper, these studies find that departures from the analyst ranks are concentrated among top performers; however, more consistent with our paper, they find that top performers are more likely to be promoted internally post-merger. Lee, Mauer and Xu (2018) are motivated by some of the same ideas on complementarities that our paper draws on (Rhodes-Kropf and Robinson, 2008), but they are not able to follow

individual employees. Instead, their paper is an examination of cost savings from mergers when firms have more and less similarly skilled work forces. They find that merging firms with more similar workforces see increased valuations following mergers.

Like our paper, recent papers in the labor economics literature use worker-level data following acquisitions, but they focus primarily on employee wages (e.g., Prager and Schmitt, 2021; Arnold, 2021; Arnold, Milligan, Moon and Tavakoli, 2023). For example, Arnold, Milligan, Moon and Tavakoli (2023) use Canadian data to examine target firm turnover and worker wage dynamics following acquisitions. They report high worker turnover and lower wages (by 8% relative to the control firm) post-merger.[5]

Our paper is also related to the growing literature on fraud and misconduct by financial advisers. Several studies show that brokers and advisers respond to commissions and other incentives that are unrelated to the welfare of their clients (Bergstresser, Chalmers and Tufano, 2008; Mullainathan, Noeth and Schoar, 2012; Christoffersen, Evans and Musto, 2013; Guercio and Reuter, 2014; Anagol, Cole and Sarkar, 2017; Guiso, Pozzi, Tsoy, Gambacorta and Mistrulli, 2018; Robles-Garcia, 2019; Charoenwong, Kwan and Umar, 2019; Garrett, 2020). Egan, Matvos and Seru (2019) document widespread misconduct in the financial advisory industry. Although they report evidence of some discipline following misconduct events, they find that approximately half of all advisors who commit misconduct remain employed at the same firm following misconduct. Of those who depart, just under half find jobs at other firms (the rest leave the industry). Our finding that targets and acquirers tend to match on misconduct is consistent with the conclusion in Egan, Matvos and Seru (2019) that some firms "specialize" in misconduct and others do not. Our paper further shows that M&A is an important mechanism through which this specialization occurs.

Egan, Matvos and Seru (2022) also report widespread and persistent misconduct in the advisory industry. We use the framework in Egan, Matvos and Seru (2022), in which the authors report increased sensitivity of separations to misconduct for female advisers, to conduct adviser-level analysis of the sensitivity of separations to misconduct of employees at the target and acquirer firms. Similar to Egan, Matvos and Seru (2022), we interpret sensitivities to indicate the strength of discipline following misconduct.

[5] The data in Arnold, Milligan, Moon and Tavakoli (2023) contain information on the reason for separation. They find that half of workers leave for unknown reasons. Among the other half, 75% of target firm worker departures are involuntary. This provides some empirical support for the assumption in our paper that separations following recent misconduct are indicative of a stronger disciplinary environment.

Dimmock, Gerken and Graham (2018) also study advisory firm mergers. They exploit variation in the location of firm branches to identify misconduct spillovers across employees. They report that the probability of a new instance of misconduct increases if a new coworker has a history of misconduct. On the surface, the negative spillovers in Dimmock, Gerken and Graham (2018) may seem inconsistent with evidence of large improvements in misconduct following acquisitions that we report in this paper.[6] However, separations can create a setting in which misconduct spreads among employees while overall firm-level misconduct declines. If the employees who remain at the firm post-merger tend to be those with cleaner records (which we find), this can reduce the future spread of misconduct. Moreover, if the firms engaging in M&A are the types of firms for which low misconduct is desirable, the evidence in Dimmock, Gerken and Graham (2018) that misconduct is contagious can explain why many combining firms may choose to accelerate separations of high misconduct employees.[7]

Finally, our paper is related to the corporate governance literature that relates shareholder returns in mergers to differences in governance between the target and acquirer. One general finding is that, when acquirers have stronger shareholder rights relative to targets, the gains to M&A are higher (e.g., Wang and Xie, 2009). Martynova and Renneboog (2008) and Bris and Cabolis (2008) both report evidence that improved governance from acquirers is associated with increases in value in cross-border deals.[8] These findings all support the idea that governance mechanisms can drive variation in returns to M&A, but the data do not allow the authors to observe the effects of governance improvements within the combined firm following transactions. By contrast, our paper uses employee-level data on allegations of wrongdoing, which allows for a close-up view of a mechanism through which improvements in governance (in the form of employee monitoring and discipline) might impact firm outcomes.

We focus our work on the investment advisory industry, but the challenge of managing corporate fraud and misconduct is a broad one (Dyck, Morse and Zingales, 2010).

[6] The data in Dimmock, Gerken and Graham (2018) are from 1999 through 2011, so the overlap between their sample and ours is only one year. Moreover, their identification strategy requires target firms to have multiple branches. They report overall increases in employee misconduct at the branch level (not the advisory firm level, which is the focus of our paper). It may be that increases in misconduct in their sample were concentrated in firms with a large number of branches.

[7] Our finding that pre-merger misconduct of both targets and acquirers is lower than firms that do not engage in M&A suggests that high levels of misconduct are generally not optimal for this group of firms.

[8] There is even evidence that these governance effects spill over to related non-target firms (Albuquerque, Brandão-Marques, Ferreira and Matos, 2019).

Employee wrongdoing exposes corporations to legal and regulatory risk and can damage firms' reputations. The changes in misconduct that we document here can increase our broader understanding of how wrongdoing is distributed within an industry and of the sources of synergies in M&A.

B. Framework

As we emphasized in the introduction, it is not obvious ex ante that misconduct is relevant in M&A, nor is it obvious that consolidation changes the level of misconduct within merging firms or the distribution of misconduct across firms in the industry. We examine four possibilities, which we list below. Distinguishing them requires understanding whether there are systematic differences in the types of firms that engage in M&A, whether there is evidence that combining firms "match" on misconduct, and whether there is evidence of post-merger changes in employee misconduct.

1. **No Role:** Misconduct could be unrelated to potential synergies in any given transaction and to firms' ability to achieve them. Under this hypothesis, we would expect no systematic differences in the misconduct records of advisers at either the target or acquirer relative to the average firm in the industry.

2. **Legal or Risk Considerations:** It could be that legal or regulatory risk makes imperfectly informed counterparties less willing to transact. If high misconduct at the firm level is a proxy for legal and regulatory risk, we would expect to observe lower levels of misconduct at targets relative to the industry average.[9]

3. **High Misconduct Business Model:** Acquirers could have business models that rely on improper business practices. Under this hypothesis, we would expect acquirers to have high levels of misconduct relative to the average firm. Target firms could have higher or lower levels of misconduct, depending on the acquirer's post-merger strategy:

    (a) High misconduct targets could complement the high misconduct acquirer's existing model (i.e., we would expect "matching" on high misconduct); or

[9] Under this hypothesis, we might also observe lower levels of misconduct at acquirers in instances where target firm owners maintain continuing equity interest post-transaction.

(b) Low misconduct targets could be attractive to high misconduct acquirers wishing to introduce improper business practices to match their high misconduct business models. In this case, we would expect high misconduct acquirers to purchase low misconduct targets and, following the merger, we would expect misconduct of the combined firm to increase.

4. **Low Misconduct Business Model:** Acquirers could have business models that rely on maintaining a high level of integrity and clean business practices. In this case, we would expect acquirers to have low levels of misconduct relative to the average firm. Target firms could have higher or lower levels of misconduct:

   (a) Low misconduct targets could be attractive to acquirers whose business models already rely on advisers with clean records. In this case, we would expect both targets and acquirers to "match" on low levels of misconduct; or

   (b) High misconduct targets could be attractive to low misconduct acquirers wishing to "clean up" a high misconduct firm. In this case, we would expect targets to employ high misconduct advisers and misconduct to drop post-merger.

To distinguish the explanations above, we begin with an analysis of whether the pre-merger employee misconduct in targets and acquirers is similar to the overall population of investment advisory firms. Then, within the sample of merging firms, we ask whether firms tend to match on pre-transaction misconduct. Finally, we test for evidence of post-merger changes in misconduct.

III. Data

We combine several data sources to construct the database of advisory-firm characteristics, mergers, employee disclosures, and misconduct measures. Below, we describe each of these databases along with the various filters that we impose.

A. Advisory Firm–Level data

The Investment Advisers Act of 1940 requires all advisers managing more than $25 million or that have 15 or more U.S. clients to register with the SEC.[10] These firms

[10] This threshold was changed to $100 million in 2012, following the Dodd-Frank Act.

must file a Form ADV at least annually. We download from the SEC's website all Form ADVs filed since 2009. We extract information on the investment adviser's business lines, type of clients, and total assets under management from Part I of the form.[11] There are 26,644 unique investment advisory firms in the data. The analysis includes all investment advisory firms that filed a Form ADV between 2009 and 2022 and that have data on employee employment history (which we describe below).

We establish the data coverage period using the date a company submits its Form ADV and the month they report as their fiscal month. Because fiscal year is not included in the data, we infer it. If a company submits a Form ADV between the end of its fiscal month and December, we consider the submission year as the fiscal year. If not, we use the previous year.[12] For example, consider a firm that submitted its Form ADV in August 2017, reporting December as its fiscal year end. Here, the fiscal year would be set at 2016 because the submission was before the fiscal month end, and the data coverage period is from January to December 2016. All broker disclosure measures we consider for the year 2016 must be recorded before December 2016.

B. Merger Events

We combine four data sources to construct the most comprehensive sample (to our knowledge) of mergers in the investment advisory industry. The data are from: Pitchbook, Securities Data Corporation (SDC), Investment News, and Form ADV-W.

We begin with the Pitchbook and SDC databases. We search Pitchbook for all mergers of asset managers operating in the financial services sector. We require that both the target and acquirer are located in the United States, that the merger date is available, and that the deal status is complete. We search SDC for U.S. targets in the Investment & Commodities Firms, Dealers, Exchanges sector with non-missing deal effective dates. We add to the combined Pitchbook and SDC data using two additional sources.

We use *Investment News*, a website covering news events in the investment advisory industry, as a third data source.[13] We search for all *Investment News* articles about mergers and acquisitions activity during the sample period. We then confirm the merger events based on a search of Factiva and company websites. We require a second information source for all *Investment News* mergers.

[11] See www.adviserinfo.sec.gov.
[12] If an advisory firm makes more than one filing in a fiscal year, we keep the latest filing for that year.
[13] https://www.investmentnews.com/topic/mergers-acquisitions

Our final source of merger data is the SEC's Form ADV-W. This form is filed by advisory firms when they withdraw their registrations with the SEC.[14] Form ADV-W data include flags to indicate that a firm is closing for merger-related reasons. However, it does not identify the acquirer, nor does it indicate the date of the merger. We identify target-acquirer pairs by identifying targets as those firms that report merger-related reasons in the "Reasons for closure" field of Form ADV-W and where we are able to identify an acquiring firm based on either employee movements or web searches using the target name (or both).[15]

Table I shows the sample of 510 merger events by year for the period beginning January 2011 and ending December 2020. We choose this sample period to ensure at least two years of pre-merger and post-merger data for the combining firms. There are a total of 510 events involving 510 unique targets and 383 unique acquirers. Table I shows a general increase in merger activity over the sample period, with a peak in 2019. This pattern is generally consistent with the broad trend in global M&A activity.

[INSERT TABLE I ABOUT HERE.]

We then combine the ADV data with merger information, defining the year before a merger (year $t-1$) as the last data coverage period that ended prior to the merger year.

C. Misconduct at the Adviser Level

We use adviser-level data to track the total number of registered employees and employees with misconduct records. The main explanatory variable of interest is the number of recent disclosures by employees of each investment advisory firm. These disclosures include customer complaints, allegations of fraud and negligence, excessive fees and commissions, regulatory actions, civil and criminal proceedings, and employment separations after allegations. The adviser-level disclosure data are from the SEC's IAPD (https://adviserinfo.sec.gov/) and FINRA's BrokerCheck (https://brokercheck.finra.org/) websites. To construct the misconduct measures, we use a python script to

[14] Unlike Form ADV, Form ADV-W was not available on the SEC's website. We filed a FOIA request with the SEC to obtain historical Form ADV-Ws.

[15] When more than 70 percent of employees move to another firm in the year following the ADV withdrawal, we use the post-closure employment records of target firm employees during the year of closure to generate a list of potential acquirers. We then manually search news articles. We keep only those Target/Acquirer pairs for which we can confirm the mergers.

scrape employment and misconduct histories of 1.3 million current and previously registered investment advisers and brokers (whom we collectively refer as "advisers").

We create an adviser-year panel of employment and disclosures from 2009 through 2022 (or the year of the adviser's last employment record, whichever is earlier). We begin the sample in 2009 to ensure full coverage of brokers.[16] The unit of observation in the adviser data is an adviser-firm-year.[17] We code disclosures using FINRA's 23 categories of disclosures. We also separately track the six FINRA categories of disclosures that Egan, Matvos and Seru (2019) consider to be the most indicative of adviser misconduct. For each adviser, we first sum the number of new disclosure events in each category and year. When there are no disclosures, the values are equal to zero. The cumulative sum of all 23 disclosures is designated *All* and the sum of 6 less ambiguous misconduct disclosures (from Egan, Matvos and Seru, 2019) is designated *EMS*." Both *All* and *EMS* measure recent disclosures, defined as all those made over the current year and the previous two years. We analyze both measures since Egan, Matvos and Seru (2019) report that the advisors with disclosures in some of the 17 categories outside of their strict misconduct definition are also more likely to have engaged in misconduct under the stricter 6-category definition when compared to advisors without such disclosures. Therefore, we interpret changes in either *All* or *EMS* as indicative of changes in employee misconduct.

D. Firm-Level Employee Misconduct

We calculate employee misconduct at the advisory-firm level by summing new disclosures for individual advisers within the firm in each fiscal year.[18] For each advisory firm, we divide this raw count by the number of all registered employees working at the advisory firm during year t. We create two measures of misconduct at the firm level: *Employee Disclosures (All)* is the count of disclosures based on the 23 FINRA categories for each registered representative over the current year and previous two years, divided

[16] Individuals are not included in BrokerCheck if they have not been registered with FINRA, a securities exchange, or state regulator within the last 10 years and have not been subjects of regulatory, criminal, or civil complaints. We first downloaded the adviser-level data in December 2018, and we begin the sample period 10 years prior to the first download. We thank an anonymous referee for emphasizing this feature of the data.

[17] Individual advisers can concurrently register with more than one advisory firm. Approximately 26.6% of advisers are registered with more than one firm in a given year of our sample. This overlap is due to concurrent employment relationships (often with affiliated firms), as well as some turnover in employment within a given calendar year.

[18] If a given adviser is registered with multiple firms, her misconduct will count in the totals for each of her employers.

by the total number of registered employees working for the advisory firm in that year; *Employee misconduct (EMS)* includes only 6 (of the 23) categories of disclosures that Egan, Matvos and Seru (2019) consider most indicative of misconduct. Both *Employee Disclosures (All)* and *Employee misconduct (EMS)* are measured over periods $t-2$, $t-1$, and t so that they capture only recent employee disclosures. We merge the firm-level employee disclosure data to our panel of advisory-firm characteristics and merger events to create the final sample.

IV. Descriptive statistics

Table II presents summary statistics for the sample of targets and acquirers as of year $t-1$ relative to the merger. The right-hand-side columns show the standardized mean difference between targets and acquirers to allow for meaningful comparisons of differences across rows. Not surprisingly, we find that acquirers are larger than target firms, with more employees, clients, and assets under management (AUM). We also observe that acquirers have experienced more recent growth in AUM and clients compared to targets. We also find that, while acquirers have employees with more disclosures and more misconduct than their targets, they have also experienced significantly greater recent growth in employee misconduct. These patterns are clear in the Appendix Figure A1, which shows the density of AUM, employees, clients and disclosure events among acquirer and target firms.

[INSERT TABLE II ABOUT HERE.]

V. Empirical Analysis

A. Is Misconduct Relevant in M&A?

To motivate our focus on potential changes in employee misconduct following M&A, we begin the analysis by asking whether misconduct is relevant in the M&A market. We conduct descriptive tests that document the relationship between employee misconduct and the probability that a firm is a target or an acquirer. As discussed in Section II.B, if misconduct is relevant in M&A, it is important to understand: (i) whether there are systematic differences in the types of firms that engage in M&A; (ii) whether there is evidence of firms "matching" on misconduct; and (iii) whether there are post-merger changes in employee misconduct. Doing so can help clarify whether (and why) corporate control transactions discipline the labor force.

Why might misconduct matter in M&A? One possibility is that misconduct captures firm type. Under the traditional view of market discipline, in which good firms purchase bad ones, we might expect acquirers to purchase firms with different levels of misconduct than their own business models dictate and then make changes that result in moving target firm employees closer to their own models. If instead there is assortative matching on misconduct (for example, due to complementarities in cultures or incentive systems) we would expect high (low) misconduct firms to purchase other high (low) misconduct firms. Ex ante, there is no clear expected relationship between adviser misconduct and the likelihood that a given firm is a target or acquirer. We use the full sample of investment advisors to estimate the following reduced-form model by pooled OLS:

$$\begin{aligned} \mathbb{1}(\textbf{Target})_{i(t+1)} = \quad & \beta_1 \text{Misconduct}_{it} + \beta_2 \text{Retail clients}_{it} \\ & + \beta_3 \text{Ln(Assets under management)}_{it} + \beta_4 \text{Ln(Firm Age)}_{it} \\ & + \beta_4 \text{Ln(Number of employees)}_{it} \\ & + \lambda_j + \eta_t + \epsilon_{it}. \end{aligned} \tag{1}$$

The unit of observation is an advisory-firm year. The dependent variable is an indicator that equals one if an advisory firm is acquired in the year following its current Form ADV filing, $\mathbb{1}(Target)_{i(t+1)}$. The primary independent variable is employee $Misconduct_{it}$, which we define in two ways, as described in the previous section. In the full sample, the mean *Employee Disclosures (All)* measure is 3.30% percentage points, and the standard deviation is 11.40% percentage points. The mean *Employee misconduct (EMS)* is 1.50%, and the standard deviation is 6.80%.

We include line of business and time fixed effects in all specifications.[19] Other controls comprise: $Retail\ clients_{it}$, a dummy equal to one if the firm serves retail clients; $Ln(Assets\ under\ management)_{it}$, the natural log of assets under management; $Ln(Firm\ Age)_{it}$ the natural log of firm age; and $Ln(Number\ of\ employees)_{it}$, the natural log of the number of registered employees. The sample period for t runs from 2011 to 2019 to match the

[19] Line of businesses include: financial planning services, portfolio management for individuals and/or small businesses, portfolio management for large businesses, portfolio management for investment companies, portfolio management for pension consulting services, selection of other advisers, publication of periodicals or newsletters, security ratings or pricing services, market timing services, and other advisory services. In Appendix Table A.1 and Table A.2, we show the estimated coefficients on each industry fixed effect.

merger data (we are predicting year-ahead mergers, which end in 2020).

Table III presents results of estimating Equation 1. Columns (1) and (2) show results for the *Employees Disclosures (All)* measure, and Columns (3) and (4) show results for the *Employees Misconduct (EMS)* measure. We standardize all continuous covariates to have a mean of zero and a standard deviation of one to ease the comparison of relative effects.

[INSERT TABLE III ABOUT HERE.]

It is clear from Table III that firms with more disclosures per employee are significantly less likely to be acquisition targets. For example, estimates in Column (1) imply that a one-standard deviation increase in the number of disclosures of employee disciplinary events (this maps to a 11.40 percentage point increase) is associated with a .098 percentage point reduction in the probability that an advisory firm is acquired. Relative to the unconditional mean rate of acquisitions of 0.74 percentage points, this represents a 13.2% decrease in the probability that a firm is acquired in the following year. The coefficient estimate of 0.082 in the column 2 specification that includes all control variables implies a 11.1% decrease in the probability that a firm is acquired (relative to the unconditional mean) following a one standard deviation increase in the misconduct measure. When we consider the stricter definition of misconduct in columns 3 and 4, we find that a one standard deviation increase in the *EMS* measure (this maps to a 6.80% percentage point increase) is followed by decrease of between 8.0 and 10.1% in the probability that a firm is acquired (relative to the unconditional mean).

In Table IV we focus on acquirers. We change the dependent variable in Equation 1 to an indicator that equals one if a firm makes an acquisition in the year following their year t ADV filing ($\mathbb{1}(\textbf{Acquirer})_{i(t+1)}$). From Table IV, we find that firms with more disclosures per employee are less likely to be acquirers. The estimated coefficients on the misconduct variables are all significant, negative, and similar in economic magnitude to Table III. For example, the estimated coefficient of -0.076 on the *Employees with Misconduct (All)* measure in column 2 implies that a one standard deviation increase in *EMS* is followed by decrease of .076 percentage point decrease in the probability that the firm makes an acquisition in the next year. This represents a decline of 13.1% relative to the mean probability of making an acquisition of 0.58%. The estimated coefficient of -0.064 on the *Employees with Misconduct (EMS)* measure in column 4 implies that a one standard deviation increase in *EMS* is followed by a .064 percentage point decrease in the probability that the firm makes an acquisition in the next year. This represents a decline

of 11% relative to the mean. Overall, it appears that targets and acquirers both have business models that result in employees with fewer disclosures than the average firm in the industry. This is inconsistent with misconduct playing no role and with acquirers that rely on higher-than-average misconduct business models (Possibilities 1 and 3 in Section II.B, respectively).

[INSERT TABLE IV ABOUT HERE.]

The results in Table III and those in Table IV show that both targets and acquirers have employees with cleaner-than-average records. Within the sample of merging firms, Table II shows that the unconditional means of misconduct per employee are higher for acquirers than for targets. Why might this be the case? Easley and O'Hara (2023) show that, in tightly connected markets, unethical behavior can spread. Moreover, Dimmock, Gerken and Graham (2018) show that misconduct in the investment advisory industry spills over from one advisor to another when they are in close proximity. If the managers of low misconduct acquirers wish to maintain cultures of low misconduct, acquiring a firm that already has low misconduct employees can be a way to limit the spread of misconduct.[20]

Tables III and IV also reveal that younger firms are more likely to make acquisitions, while older firms are more likely to be acquired. This could be driven partly by founders' retirement.[21] We also find that both acquirers and targets are less likely to serve retail clients than other firms. We control for retail clients in the analysis that follows.[22]

In sum, the evidence suggests that misconduct is relevant in M&A and that firms with lower levels of misconduct are more likely to be acquired. This is clear in Figure 1, which shows the fraction of employees with any history of disclosures as a function of whether

[20] The finding that targets have fewer disclosures is in line with Jennings (2023) who argues that, in the case of potential criminal liability, criminal successor liability can put an acquirer at risk for the target's pre-transaction acts. This might result in an inefficient lack of marketability of potential targets with any potential criminal exposure (i.e., the legal and risk considerations highlighted in Possibility 2 in Section II.B may be important).

[21] Ameritrade (2019), an industry report discussing various motives for advisory firm mergers, notes that founder retirement is a key motivation for 30% of advisory firms considering a merger. Jenter and Lewellen (2015) also show that takeovers are more likely near CEO retirement age.

[22] The specifications in Tables III and IV all control for the firms' lines of business. However, the lines of businesses themselves are independently interesting. Appendix Tables A.1 and A.2 show the estimated coefficients on the individual line of business dummies. Focusing on the full specification (with controls) in columns 2 and 4, we find that firms offering financial planning services, portfolio management to individuals and small businesses, and stock selection services are more likely to be targets. Firms offering ratings and pricing services are less likely to be targets. The same patterns hold for acquirers.

the firm is a target, acquirer, or other firm (where "other firm" is defined as any firm that has not participated in a merger during the sample period). The figure shows that both acquirers and targets have lower levels of misconduct than the average firm. This pattern is consistent with legal risk considerations (i.e., Possibility 2 in Section II.B). It is also consistent with potential complementarities in business models, where combining people, monitoring, and disciplinary mechanisms can be beneficial (i.e., Possibility 4 described in Section II.B). We investigate this idea in the next section.

B. Matching on Misconduct (Sample of Targets and Acquirers)

In this section, we test the hypothesis that there is positive assortative matching on misconduct among investment advisory firms. In an ideal test of whether acquirers and targets with similar employee misconduct levels merge, we would observe the different targets that a given acquirer considers. We would then test whether the selected target differs from the potential targets (i.e., those firms that are considered but not selected) in that its level of misconduct-related disclosures is more similar to the acquirer's, holding the other characteristics of the target fixed. Because we only observe equilibrium matches, we approximate the ideal test by adopting an approach similar in spirit to Rhodes-Kropf and Robinson (2008). We create counterfactual mergers that pair every target with all potential acquirers in the merger year. We define potential acquirers as all those firms that acquired another asset management firm during year t. The idea is that these firms are most likely to be the ones considering acquisitions at t.

Figure 2 provides some visual evidence. The figure plots the probability that a potential target and acquirer pair merge, as a function of whether the potential acquirer or target has any disclosure of a disciplinary event. The indicator *Some Disclosure* equals one if any employee of the target or acquirer has one of the 23 categories of FINRA disclosures over the past two years (including the current year); *Probability of Merger (%)* is the fraction of pseudo plus real target-acquirer pairs in each quadrant that are true merging firms. The evidence in Figure 2 is suggestive of positive assortative matching on misconduct, especially in situations in which the acquiring firm has employees with prior disclosures. For example, 4.29 percent of all pairs in the *Some Disclosure* for the acquirer and *Some Disclosure* for the target quadrant are real matches. This value is 100% greater than the unconditional merger rate of 2.14 percent.

[INSERT FIGURE 2 ABOUT HERE.]

For a more rigorous test, we estimate the following linear probability model, in which we test the hypothesis that targets and acquirers with similar misconduct records are more likely to pair:

$$\begin{aligned}\mathbb{1}(\textbf{Merged})_{i(t+1)} = \quad & \beta_1 \text{Acq \& Target Disclosure}_{it} + \beta_2 \text{Retail clients}_{it} \\ & + \beta_3 |\text{Ln(AUM Acq)} - \text{Ln(AUM Tar)}|_{it} + \beta_4 |\text{Ln(Age Acq)} - \text{Ln(Age Tar)}|_{it} \\ & + \beta_5 |\text{Ln(Emp Acq)} - \text{Ln(Emp Tar)}|_{it} \\ & + \beta_6 \text{Same state} + \lambda_j + \eta_t + \epsilon_{it}.\end{aligned} \tag{2}$$

The unit of observation is a target-acquirer pair, where pairs include both true merging firms and pseudopairs.

Recall that pseudo pairs are formed by pairing all targets in a given year with all acquirers making acquisitions in the same year. The dependent variable ($\mathbb{1}$(Merged)) is an indicator that equals one if the target-acquiring firm pair actually merge, and zero otherwise. The explanatory variables of interest are the measures of disclosure and misconduct similarity within each pair. We set dummy variables *Acq & Tar Employees with misconduct (All)* and *(EMS)* to equal one if the acquirer and the target both have employees with recent disclosures (i.e., in years $t-2$, $t-1$, or t). If there is assortative matching on misconduct, we expect that this similarity measure between target and acquirer employee misconduct will make a match more likely. Similar to the misconduct similarity variable, *Retail Clients* is a dummy equal to one if both firms serve retail clients. We express the other control variables in terms of acquirer-target similarity by taking the absolute difference of acquirer to target values for AUM, age, and number of registered advisers. Finally, we define *Same State* as an indicator that equals one if a target and acquirer pair are located in the same state because firms sharing geographic markets might be more likely to merge and because of the Parsons, Sulaeman and Titman (2018) finding that there is a geographic component to misconduct. As in previous specifications, η_t are year fixed effects and λ_j are matching line of business fixed effects, indicators that equal one when the target-acquirer pair are in the same line of business.

Results are in Table V. Columns (1) and (2) present results using the "All" measure, and Columns (5) and (6) show results using the "EMS" measure. As in the earlier tables, we standardize all continuous covariates to have a zero mean and a standard deviation of one to ease comparisons of magnitudes across covariates. In extended specifications (Columns 3 and 7), we add controls to account for whether both the target and acquirer

are small or large. We do this to address any potential concerns that the *Acq & Tar Employees with misconduct* dummy variables are capturing similarity in size. We further extend the specifications in Columns (4) and (8) to include indicators for whether both firms have been involved in regulatory, civil, or criminal events. We expect these variables to capture additional factors related to potential matching on misconduct.

[INSERT TABLE V ABOUT HERE.]

We find strong evidence of assortative matching on misconduct. For example, the estimates using the "All" measure in Column (1) imply that, if both firms have instances of recent employee disclosures, a potential acquirer-target pair is 1.96 percentage points more likely to be a true pair. Once we add control variables in Column (2), the estimate is 1.88 percentage points and it is also significant statistically. Relative to the unconditional merger rate of 2.14 percentage points within the sample, these estimates represents an increase of between 88 and 91 percent in the probability of a match when levels of employee misconduct between target and acquiring firms are similar. The estimated coefficients on the control variables show that pairs serving similar clientele and headquartered in the same state are more likely to merge. Firms of more similar sizes (as captured by AUM and employees) are less likely to merge.[23] The estimated coefficients using the "EMS" measure in Columns (5) and (6) are larger but very consistent with what we observe in Columns (1) and (2).

When we extend the specifications in Columns (3) and (7) to include controls to account for whether both the target and acquirer are small or large, the estimated coefficients on *Acq & Target Disclosure* remain stable, and we do not find an independent effect of "both small" or "both large" beyond what is captured in the size similarity measures using the absolute differences in AUM and employees. When we include additional regulatory and legal events in Columns (4) and (8), the main effects remain; however, we find that mergers are more likely if both firms report recent regulatory or civil events.

The evidence that targets are low misconduct firms is consistent with acquirers seeking to avoid new legal risks (Possibility 2, outlined in Section II.B). However, the matching on misconduct findings in Table V and in Figure 2 suggest that there is much more to the story. Business models based on low misconduct (Possibility 4a in Section II.B) are

[23] The specifications in Table V control for dummies that indicate matches on lines of business. Appendix Table A.3, shows the estimated coefficients on the industry match dummies. We find that firms in financial planning, investment companies, and those offering pension consulting services are most likely to merge.

also likely to play a role. The evidence is also consistent with the idea in recent work by Gorton and Zentefis (2023) that corporate culture defines the boundary of the firm. In their setting, culture clashes are costly and can make mergers fail. Our findings support the idea that different misconduct cultures could be costly to integrate. Anecdotally, in an industry survey of financial advisory firms (Ameritrade, 2019), advisors noted that "a critical ingredient for any successful transaction is compatibility, from both a culture and business model perspective." The results are also related to the idea in the organizations literature (e.g., Datta, 1991; Teerikangas and Very, 2006) that differences in management styles or culture are associated with post-acquisition performance. There, the empirical evidence is mixed (Teerikangas and Very, 2006).

C. Does M&A Discipline Employee Behavior?

We now turn to the paper's main economic question: Do mergers play an important role in the redistribution of misconduct across firms in the industry? In our context, we use the term "misconduct synergies" to describe post-merger changes in firm-wide misconduct. These changes could occur through employee turnover or through the transfer of systems that help curb the future misconduct of existing employees.[24]

To examine the misconduct synergies hypothesis, we compare the disclosure measures in the three years before the merger to disclosures in the three years following the merger. We calculate pre-merger variables by creating a synthetic merged firm. We estimate combined misconduct by taking the weighted average of misconduct measures for the target and acquiring firm, where the weights are based on the number of advisers at each firm. We keep only target-acquiring firm pairs with the requisite data in each pre-merger year and where we have at least one year of post-merger data for the combined firm (this leaves 474 target-acquirer pairs). We then average each characteristic over the three years preceding the merger and the three years following the merger.

Table VI reveals a substantial decline in disclosures following merger events. For example, if we focus on *Employee disclosures (All)* in Row (2) Table VI, the average recent disclosures (per employee) of the combined firm drops from 2.79 percentage points in the years before the merger to 2.19 percentage points in the years following the merger. This

[24] Disciplinary and monitoring systems governing misconduct could come from either the target or acquirer. Note that reductions in misconduct that are tied to business models that rely on employees with clean records and is much more specific than across-the-board layoffs to reduce costs and eliminate redundancies.

represents a 22% decline. The *Employees with misconduct (EMS)* measure in Row (3) shows a similar decline of 17%, from 1.11 to 0.92 percent. Table VI also shows a significant increase in the number of registered employees following the merger, along with an increase in in AUM.[25] This is consistent with M&A reducing expected transactions costs (e.g., regulatory fines) and potentially enhancing firms' "clean" reputations.

[INSERT TABLE VI ABOUT HERE.]

To improve the interpretation of the post-merger declines in new disclosures that we observe in Table VI, we construct a placebo merged firm. This allows us to check whether we are simply picking up marketwide trends in disclosures following merger events. Each placebo firm consists of two non-merging firms, one matched to the target and the other matched to the acquiring firm. To construct matches, we rely on the entire database of ADV firms. We create the following variables: an indicator that equals one for firms with above median employee disclosures (*Misconduct*); an indicator equal to one for firms with above median change in employee disclosures (*Misconduct Change*); ten bins based on the number of employees at the firm (*Employee Decile*); and a line of business category.[26] We then match each target and acquirer to the sample of non-merging advisory firms that share the same values of *Misconduct*, *Misconduct Change*, *Employee Decile*, and *Line of Business Category*, as of the year of the merger. Within the set of potential matches for each target and acquirer, we create a final match with the firm that has the closest level of employee disclosures.

The pre- and post-event characteristics of the pseudo merged firms are in Table VII. Unlike in the case of true mergers, we observe insignificant (using the "All" measure) or small increases in employee disclosures (using the "EMS" measure). Like our treated sample, we also observe increases in the number of registered employees and AUM. It will be important to control for each of these in the regression analysis. Of course, matches are not perfect. For example, the pseudo merged firms are smaller with fewer employees, AUM, and clients than the true merged firms. These differences in characteristics

[25] The increases in the number registered employees and AUM in the years surrounding the merger are clear in Appendix Figure A3 and Appendix Figure A2, respectively.

[26] Firms often operate in several lines of businesses. We use the frequency of line of business combinations within the full sample to construct five broad primary industry categories from which we select same-industry matches. These are: financial planning and portfolio management services; portfolio management services to individuals and small businesses (with no financial planning services); portfolio management services to pooled investment vehicles (with no financial planning services); any portfolio other management services (with no financial planning); and other services (with no financial planning).

should not impact the overall interpretation. Moreover, we control for size differences in regressions.

[INSERT TABLE VII ABOUT HERE.]

In Table VIII, we conduct a difference-in-differences analysis in which we compare post-merger changes in disclosures in the true merged firm to that of the pseudo merged firm. We use annual data for the three years prior through three years following the mergers. The dependent variables are *Employee Disclosures (All)* and *Employee misconduct (EMS)*, defined as in previous tests. We introduce *Merged*, a dummy equal to one if the firm is the true combined firm. The coefficient of interest is on the *Merged* × *Post* interaction, which estimates the difference in the post-event change in misconduct between the real and pseudo merged firms. The estimated coefficient on this interaction is negative and statistically significant in all four regression specifications shown in Table VIII, implying a significant post-event reduction in new employee disclosures in the true merged firm relative to the control. As in Table VI, the magnitudes are significant economically as well. For example, in column 2, the estimated coefficient of -0.702 on *Merged* × *Post* implies a 26.5% decline in misconduct in the merged firm (relative to the sample mean of 2.65 percentage points) in the years following the merger.[27]

[INSERT TABLE VIII ABOUT HERE.]

To provide a closer look at the evolution of disclosures following merger events, in Figure 3 we present the coefficients from a regression of *Employee Disclosures (All)* against an indicator variable (*Merged*) interacted with event time dummies for $t-3$, $t-2$, t, $t+1$, $t+2$, and $t+3$. The coefficients are calculated relative to $t-1$, where t represents the merger year. From the figure, we observe a clear decline in disclosures beginning in year 0 and extending to at least 3 years following the merger. From Figure 3, it is clear that disclosures at the combined firm start to decline by the end of merger year 0 and continue to do so in the years following the merger. In the Appendix Figure A5, we plot the raw data. Consistent with Figure 3, the plots show a larger post-merger gap in disclosures compared to the pre-merger years.

[27] It is possible that some acquirers specialize in implementing changes that result in misconduct reductions. Recall from Table I that of the 510 mergers in our sample, there are 383 unique acquirers. Appendix Table A.4 lists the 32 acquirers that purchase more than two target firms during our sample period. Mercer Global Advisers is the most active, with 21 acquisitions. In Appendix Table A.5, we test whether the drop in misconduct is driven by frequent acquirers, but we do not find any evidence to support that hypothesis. If anything, the results are somewhat weaker among serial acquirers.

[INSERT FIGURE 3 ABOUT HERE.]

What drives the significant declines in disclosures following mergers? It may be that average employee disclosures decline after the merger because target and/or acquiring firm employees reduce their misconduct following the merger. If the acquiring firm adopts the monitoring and disciplinary practices of the firm with the better record (in our setting, this would be the target firm since we find that acquirers tend to have higher recent growth in disclosures than targets), the stricter disciplinary environment could cause employees' behavior to improve. Incentives for employees to reduce their misconduct might be particularly strong in M&A settings when the acquiring firm's business model involves a low level of employee misconduct, as there are redundancies and increased competition among employees who wish to keep their jobs (Fulghieri and Sevilir, 2021).

A second possibility is that there is a high concentration of separations among employees with misconduct records. If misconduct is a relevant variable that new owners consider when reducing redundancies, we might expect misconduct to improve post-merger through separations (rather than a change in the behavior of existing employees). In the next section, we examine how M&A might discipline misconduct. We consider how the probability of adviser job separation changes after mergers, as a function of recent disclosures. We interpret increased sensitivity of separation to disclosures as increased monitoring and discipline. We interpret no change in sensitivity as evidence that the average disclosure declines observed at the firm level are a result of existing employees improving their behavior. We also examine annual changes in disclosures among employees who remain with the combined firm post-merger.

D. What Drives the Decrease in Adviser Misconduct following M&A?

In this section, we test whether advisers with disclosures working for either the target or acquirer are more likely to separate from the merged firm following the merger. Thus far, we have focused the analysis at the firm level. Here, we examine data at the adviser-year level. We estimate the following linear probability model:

$$\begin{aligned} \mathbb{1}(\textbf{Separation})_{if(t+1)} = \quad & \beta_1 \text{Misconduct}_{ift} \times \text{Post} + \beta_2 \text{Misconduct}_{ift} \\ & + \beta_3 \text{Post}_f + \beta_4 \text{Ln}(\text{experience})_{ift} \\ & + \beta_5 \text{Ln}(\#\ \text{Qualifications}) + \eta_{ft} + \epsilon_{ift}. \end{aligned} \tag{3}$$

In Equation 3, we predict year-ahead separations at the individual adviser level as a function of adviser misconduct, timing relative to the merger event, and control variables. Each observation is an adviser-year. We include annual data for years from $t-3$ through $t+3$ relative to the merger year, and we focus the analysis on all employees who are working either at the target or acquiring firm f at any time during the three years (t) preceding (and including) the year of the merger. The dependent variable ($\mathbb{1}$**(Separation)**) is an indicator that equals one if an adviser that worked for the target or acquirer in year t no longer works for either the target or acquirer in year $t+1$. The primary explanatory variables of interest are the *Employee misconduct (All)* $\times$ *Post* and *Employee misconduct (EMS)* $\times$ *Post* interactions: *Employee disclosures (All)* and *Employee misconduct (EMS)* are dummies equal to one of the adviser has a disclosure in the current year; *Post* is an indicator that equals one for the year of the merger and the years following the merger. We also control for the experience and qualifications of the adviser by including *Ln(experience)*, the natural log number of years of experience in the advisory industry, and *Ln(# Qualifications)* the adviser's total number of certifications. Finally, η_{ft} are advisory firm by year fixed effects, which control for differences in separations across firms and time.

Table IX presents results from estimating Equation 3, which we estimate separately for target and acquiring firm employees. Doing so helps us understand potential changes in the disciplinary environments for each of these firm types. Columns (1) and (2) show the estimated coefficients using the *Employee disclosures (All)* measure, and Columns (3) and (4) show results for *Employee misconduct (EMS)*. For target firm employees (Panel A), we observe large increases in merger sensitivity of separations to employee misconduct following the merger. The estimated coefficients of 5.138 and 4.711 (Columns 1 and 2) on the *Employee misconduct (All)* $\times$ *Post* and *Employee misconduct (EMS)* $\times$ *Post* interaction variables suggest large increases in sensitivities of separations to misconduct relative to the mean pre-event sensitivities of 7.145 and 8.290 percentage points, respectively. Thus, we observe increases in separation sensitivities to misconduct of between 57 and 72 percent. Those employees with disclosures in one of the six Egan, Matvos and Seru misconduct categories become between 13.893 and 14.473 percentage points more likely to separate (Columns 4 and 3, respectively) than employees without such disclosures. These are increases of more than 100% relative to the mean pre-event sensitivities of 10.353 and 9.002, respectively.

In the case of acquiring firms (Panel B), the pre-merger sensitivities of separations to misconduct are higher. However, unlike what we see for target-firm employees, we do

not observe any post-merger increases in sensitivities. In fact, under the EMS measure, sensitivities decline somewhat following the merger (so that the total sensitivities are similar for employees previously employed by the target and those previously employed by the acquirer).[28]

Our primary focus in Table IX is on the change in the sensitivity of separation to misconduct post-merger. However, we also note that the baseline effects (i.e., coefficients on the *Employee misconduct* variables in Table IX are smaller than those reported in Egan, Matvos and Seru (2019). In M&A settings, the base rate of separation is high, with all employees departing for a variety of reasons unrelated to employee misconduct. This can lead the marginal likelihood that an employee with misconduct is terminated to appear lower that in more ordinary times.

The estimated coefficients on the other control variables in Table IX are consistent with intuition. For example, more experienced and qualified advisers are less likely to leave.

[INSERT TABLE IX ABOUT HERE.]

The findings in Table IX reveal that the decline in employee misconduct that we observe following merger events is driven by separations of high misconduct employees, particularly at the target firm. We can see this visually in Figure 4, where we show separations during the years surrounding the merger event. In line with the results in Table IX, Figure 4 shows not only that target-firm employees drive the post-merger separations, but also that those target-firm employees with disclosures are more likely to depart post-event (i.e., the gap between advisers with and without disclosures widens beginning in year 0). These patterns are absent when we examine acquiring firm employees. If anything, the gap among acquiring firm employees narrows post-merger.[29] Our findings reveal that, even though target employees have slightly better records than the employees of acquiring firms, those target employees with disclosure histories are more likely

[28] The natural question to ask is whether acquirers with better or worse misconduct histories are driving the improvements that we observe. In Appendix Table A.6, we introduce a dummy variable *HDA*, which equals one if the acquirer has above median pre-merger employee disclosures. We focus on the triple interaction of *HDA* with *Employee misconduct (All)* $\times$ *Post* and *Employee misconduct (EMS)* $\times$ *Post*. We find that the triple interaction is statistically insignificant in all specifications.

[29] The rate of separation in Figure 4 is somewhat lower than the separations of very top managers that have been documented in the earlier literature on managerial turnover and corporate control (e.g., Hartzell, Ofek and Yermack, 2004, report that approximately half of target firm CEOs depart the combined firm) but qualitatively in line with the observation that target firm CEOs tend to lose their jobs during or shortly after a takeover (Martin and McConnell, 1991; Agrawal and Walkling, 1994; Hartzell, Ofek and Yermack, 2004; Wulf and Singh, 2011).

to separate post-merger. Thus, it appears that mergers tighten the disciplinary environment and can improve misconduct through the accelerated shedding of high misconduct employees within relatively low misconduct target firms.

[INSERT FIGURE 4 ABOUT HERE.]

One way to examine the hypothesis that the disciplinary environment changes for target firm employees post-merger is to look at whether target firm top management or owners remain following the change of control. We expect that departures at the very top will remove job protection that employees with misconduct may have enjoyed pre-merger. In Table X, we test whether the findings in Table IX are sensitive to whether target firm owners and manager depart. We introduce *NM*, a dummy equal to one when none of the target firm's managers or owners remain in their roles at the combined firm post-merger. In the year prior to the merger, we record all control persons listed on Form ADV at the target firm. After the merger, we verify whether any of these control persons remain listed as such at the acquiring or combined firm in the following years. The results in Table X are striking. We find that all of the increase in sensitivities of separations to misconduct of target firm employees occurs at firms where managers and owners depart following the merger. These findings suggest that mergers provide a disciplinary mechanism that serves to reduce misconduct at the combined firm through turnover of top managers and employee separations.[30]

[INSERT TABLE X ABOUT HERE.]

We observe clear increases in separations by employees with disclosures of disciplinary events, but what is the magnitude of the contribution of separations to the decline in firmwide misconduct? Is zero change the right benchmark? To help answer this question, Figure 5 conducts counterfactual analysis in which we show the time series of new disclosures by all employees of the combined firm, under the assumption that separated employees who remained in the industry also remain employed by the target and acquirer.

[30] Table X also provides some insights as to why the effects are concentrated among target firm employees, even though target firms tend to have somewhat better records than their acquirers (Table II): It may be difficult for acquiring firm managers to part with their own employees with whom they may have built relationships. We investigate this in Table A.8, where we show a similar regression for when all of the acquiring firm managers depart (the "no managers remaining" dummy is less than 5% for acquirers). Table A.8 shows no difference in post-transaction sensitivities for acquiring firm employees when all acquiring firm managers depart post-transaction. However, this may be driven by the fact that most (about 95%) of the acquiring firm managers remain following the transaction.

We then compare this time series to the actual new disclosure events at the target, acquirer, and combined firm. From the figure, it is clear that separated employees generally continue to engage in more misconduct than employees who remain at the firm, even absent a merger. However, the gap between the counterfactual firm and the real firm expands sharply following the merger.[31] This suggests that mergers accelerate the shedding of high misconduct employees and facilitate the redistribution of misconduct across firms in the advisory industry.

The results from the counterfactual analysis are in line with the finding in Egan, Matvos and Seru (2019) that one quarter of advisors with misconduct records are repeat offenders and suggests that the shedding of target firm employees with misconduct records is a significant driver of the post-merger decline in misconduct that we observe. In Appendix Table A.7, we tabulate job transitions among target and acquiring firm advisers following the merger. There are two primary observations. First, advisors with misconduct are less likely to remain with the firm. Second, of those advisors who leave the firm, target firm employees with misconduct are actually more likely than those without misconduct records to join a different firm in the year following departure.

[INSERT FIGURE 5 ABOUT HERE.]

It is clear from the analysis in Table IX, Table X and Figure 5 that separations of target firm employees contribute significantly to the decline in employee misconduct that we observe post-merger. What about those target firm employees who remain at the combined firm? Table XI shows results of difference-in-differences regressions where we condition the sample on all employees of the target firm or the pseudo target in at least one of the three years leading up to the merger. We then examine annual new disclosures (*Flow Misconduct*) in the real and pseudo target firms during the post-merger period. The unit of observation is the adviser-year. Table XI shows only marginally significant and small reductions in misconduct among existing employees. Thus, the Table VIII results are not driven by changes among existing employees. Instead, they are driven by changes due primarily to employee turnover.[32]

[INSERT TABLE XI ABOUT HERE.]

[31] We begin the separation analysis at year $t-3$ in order to distinguish the impact of separations in general versus employee separations that follow merger events. As in Table VI, we combine data on employees of the target and the acquirer for the pre-merger years.

[32] The results in Figure 5 and Table XI reveal persistence in misconduct at the adviser level, suggesting that variation in misconduct across firms is driven by firm type and incentives, where some firms attract and retain advisers with low misconduct.

E. Is Misconduct Value-Relevant in the Investment Advisory Industry?

In interpreting this paper's main findings that misconduct declines substantially post-merger, it is natural to ask whether misconduct is value-relevant in the advisory industry. As noted earlier, both targets and acquirers have better misconduct records than the industry's average firm. Moreover, within the subsample of merging firms, we find evidence of assortative matching. This is consistent with the argument in Egan, Matvos and Seru (2019) that some firms specialize in misconduct and others do not. Firms' business models and incentives that result in either low or high misconduct are likely chosen because they are value-enhancing, given other characteristics of the firm. Thus, the separations of high misconduct employees that occur following mergers may be value-enhancing.

We start with the observation that regulatory and civil fines paid by firms are a direct cost of employee misconduct. Figure A4 plots the average regulatory and civil fines paid in each year by firms with at least one employee disclosure. For firms with disclosures, the average yearly fine is approximately $973,950.

Outside of fines, the relationship between misconduct and advisory firm value is not obvious. We provide descriptive analysis below using data from the full sample of advisory firms and with a focus on AUM and firm closure. AUM is closely linked to value within the investment advisory industry because advisers typically charge fees that are a percentage of the value of AUM.[33] Misconduct disclosures might cause clients to withdraw their funds, resulting in lower AUM. Misconduct might also reflect differences in managerial skill and performance, which would be reflected in assets under management (AUM).

Firm closure is related to value in that failures might be costly to customers and employees when there are adjustment costs. As in the earlier analysis, we can only capture detected misconduct, not misconduct that goes undetected. The underlying assumptions are that detected misconduct is proportional to undetected misconduct and that there is no systematic relationship between undetected misconduct and the performance variable of interest, beyond what is captured in detected misconduct, which is what we observe.

[33] Huberman (2007) reports that asset management firms trade at between one and four percent of their AUM. Based on the assumptions of continuous fees and unlimited capacity, he finds that they might be priced at 20–35 percent of AUM. Joenvaara and Scherer (2017) also relate AUM to value through fees, but they relax the unlimited capacity assumption.

We estimate the following reduced-form model by pooled OLS:

$$\begin{aligned} Outcome_{i(t+1)} = \quad & \beta_1 \text{Misconduct}_{it} + \beta_2 \text{Retail Clients}_{it} \\ & + \beta_3 \text{Ln(Firm Age)}_{it} + \beta_4 \text{Ln(Number of employees)}_{it} \\ & + \lambda_j + \eta_t + \epsilon_{it}. \end{aligned} \tag{4}$$

The unit of observation is an investment advisory firm-year. The main dependent variables (*Outcome*) are: $Ln(\frac{AUM}{Employees})$, the natural log of next year's assets under management per registered adviser, and $(Failed)_{i(t+1)}$, an indicator that equals one if the advisory firm closes in the year following its period t Form ADV filing. We obtain data on advisory-firm closures from a FOIA request to the SEC for all Form ADV-W's. Form ADV-W is a notice of withdrawal from registration filed by investment advisers. On this form, firms list the reason for their deregistration. We define a firm as *Failed* if the reason for withdrawal is business closure.[34]

In the AUM regression (Panel A of Table XII), we include firm fixed effects to absorb unobservables at the firm level. We also include time fixed effects. Other controls are: $Ln(Number\ of\ employees)_{it}$, the natural log of the number of registered advisers; *Retail clients*, a dummy equal to one if the firm serves retail clients; and $Ln(Firm\ Age)_{it}$ the natural log of firm age. We standardize all continuous covariates to have a mean of zero and standard deviation of one.

From Panel A of Table XII, we observe a significant and negative relationship between employee misconduct and next-period AUM per employee. For example, the estimated coefficient of 0.013 on *Employees with misconduct (All)* in column 2 of Panel A implies a 1.3 percent reduction in next period AUM per employee following a one standard deviation increase in employee misconduct (the standard deviation of this variable is .106).[35]

[34] Specifically, using the reasons for closure section of Form ADV-W, we define a firm as failed if it lists one of the following reasons for closure: "No longer conducting advisory activities," "No longer in business or closing business," "Ceased conducting advisory business," "Termination of business," "Going out of business," or "Closed business."

[35] It is possible that changes in AUM and employee misconduct are driven by common unobservables. To help clarify the interpretation, we exploit increased regulatory scrutiny that occurred in Massachusetts. On June 16, 2016, following the release of Egan, Matvos and Seru (2019), the securities regulator in Massachusetts (RICE) sent notices to 241 broker-dealer firms that were registered in Massachusetts and that had a higher-than-average percentage of advisers with at least one current misconduct disclosure on their records. RICE inquired about how these firms treat advisers with misconduct. The inquiries were widely publicized. In Appendix Table A.9, we repeat the analysis from Table XII, but we replace the misconduct measures with the MA treatment variable equal to one for firms with at least one employee registered in Massachusetts prior to 2015. We interact *Treated* with *Post*, an indicator equal to one following June 2016. The analysis assumes that this increased scrutiny lowered client expectations

The firm closure findings in Panel B of Table XII are even more striking. For example, the estimated coefficient of 0.234 in column 2 of Panel B implies a 0.234 percentage point increase in closure probability following an increase by one standard deviation in the misconduct measure. This is meaningful economically, given that the mean annual closure rate in the sample is 1.08 percentage points. Panel B shows costs that extend beyond those incurred at the individual adviser level. Firms with high levels of employee misconduct are much more likely to close their doors.

[INSERT TABLE XII ABOUT HERE.]

Taken together, the results in this section reveal strong links between misconduct and proxies for value in the investment advisory industry. Firms with more disclosures have lower levels of assets under management, they pay more regulatory and civil fines, and are more likely to close. Given this, it is not surprising that some firms choose to follow low misconduct business strategies and that further reductions in misconduct follow mergers.

VI. Conclusion

Using the investment advisory industry as a laboratory, we test the hypothesis that mergers can have implications for the level of misconduct in merging firms and for the distribution of misconduct across the industry. Consistent with misconduct synergies, we find substantial declines in new disclosures following mergers. Disclosures in the combined firm drop by between 17 and 22 percent during the first three years following the merger. Our findings shed light on a role for consolidation in both the level of misconduct at merging firms and in the distribution of misconduct across the industry. Egan, Matvos and Seru (2019) present striking evidence that misconduct persists in the investment advisory industry, with some firms specializing in misconduct. This paper helps uncover some of the mechanisms driving the clustering of misconduct across firms.

We find that both targets and acquirers have better misconduct records than the average firm in the industry. Moreover, within the subsample of merging firms, we find evidence of assortative matching (Rhodes-Kropf and Robinson, 2008) on misconduct, consistent with complementary business models where misconduct plays an important role.

about future misconduct. Similar to Table XII, we find that AUM per employee is higher following regulatory scrutiny that likely decreased the chances of high future misconduct for treated firms.

Merger events facilitate further reductions in misconduct through separations of target-firm employees with high misconduct. These separations are more likely when target-firm owners and top managers leave the combined firm, which suggests that improvements are through increased discipline of target-firm employees. Many of the departing employees remain in the industry and continue to have more disclosures than employees who remain with the combined firm. Thus, mergers serve to redistribute misconduct across firms. Already low misconduct firms see further improvements following the transactions, while high misconduct employees often leave to join other firms.

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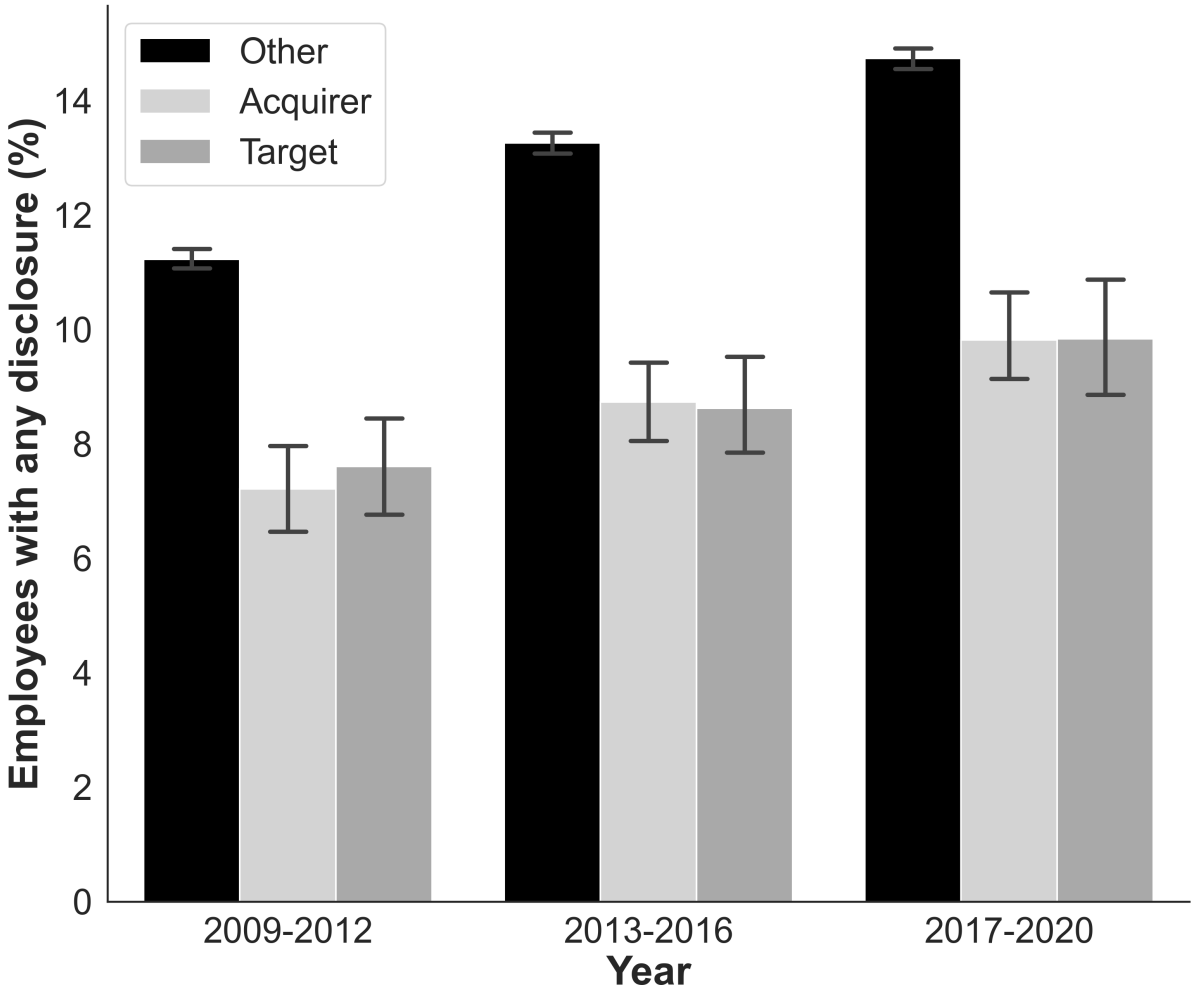


Figure 1: Employee disclosure events and advisory firm mergers

This figure shows the average percentage of employees with at least one disclosure of a past disciplinary event. The sample is split into three groups: employees at firms that were targets of an acquisition, employees at firms that have acquired another business, and employees at advisory firms that have never participated in a merger. The figure also provides 95 percent confidence intervals for each subsample.

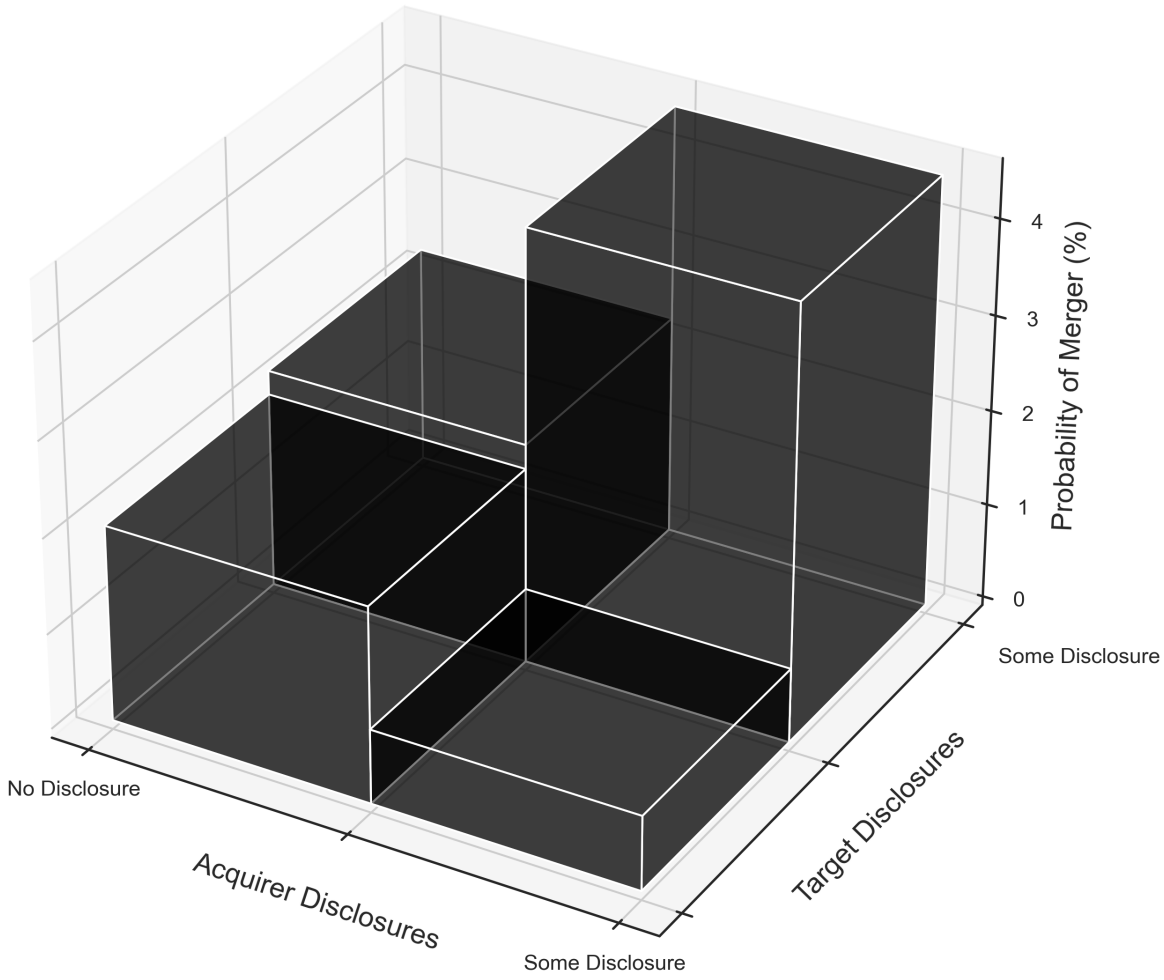


Figure 2: Matching on misconduct

This figure plots the probability that a potential target and acquirer are a true merging pair, as a function of whether the potential acquirer or potential target have recent disclosures of disciplinary events. The indicator *Some Disclosure* equals one if any employee has a disclosure of any one of FINRA's 23 categories over the past two years (including the current year). For each year, we create counterfactual mergers that pair every target with all potential acquirers. We define potential acquirers as those firms that have acquired another asset management firm during the year t, in which the target was acquired. The term *Probability of Merger (%)* is the fraction of target-acquirer pairs in each quadrant that are true merging pairs.

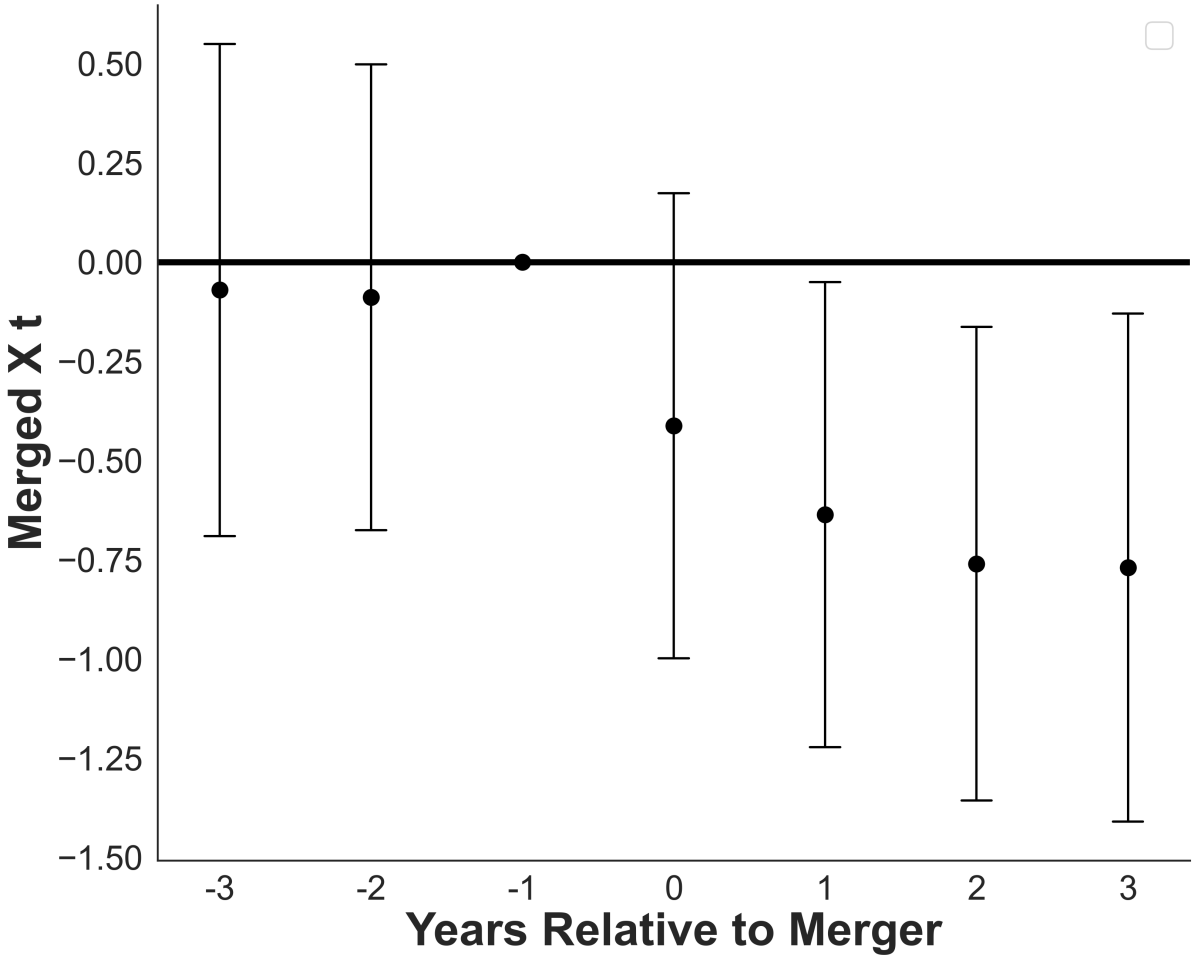


Figure 3: Employee disclosures at the combined firm

This figure presents the coefficients from a regression of *Employee Disclosures (All)* against an indicator variable (*Merged*) interacted with event time dummies for $t-3$, $t-2$, t, $t+1$, $t+2$, and $t+3$. The coefficients are calculated relative to $t-1$, where t represents the merger year. Please refer to Table VIII for a detailed explanation of the sample construction and the selection of pseudo merging firms for which (*Merged*) equals zero. The sample is restricted to mergers that occurred from 2011 to 2020 to ensure each merged and pseudo merged firm has sufficient pre- and post-merger data. The bars represent 95 percent confidence intervals.

Panel A: Employment separation by employees of the target firm

Panel B: Employment separation by employees of the acquiring firm

Figure 4: Employment separation by employees of the target and acquiring firms

This figure plots the annual probability of employment separation for target and acquiring firm registered advisers from year −3 relative to merger year 0, through year +3. The indicator *Has Disclosures* equals one if an employee of the target or acquirer has one of FINRA's 23 categories of disclosures in the current year. The shaded bands show 95 percent confidence intervals.

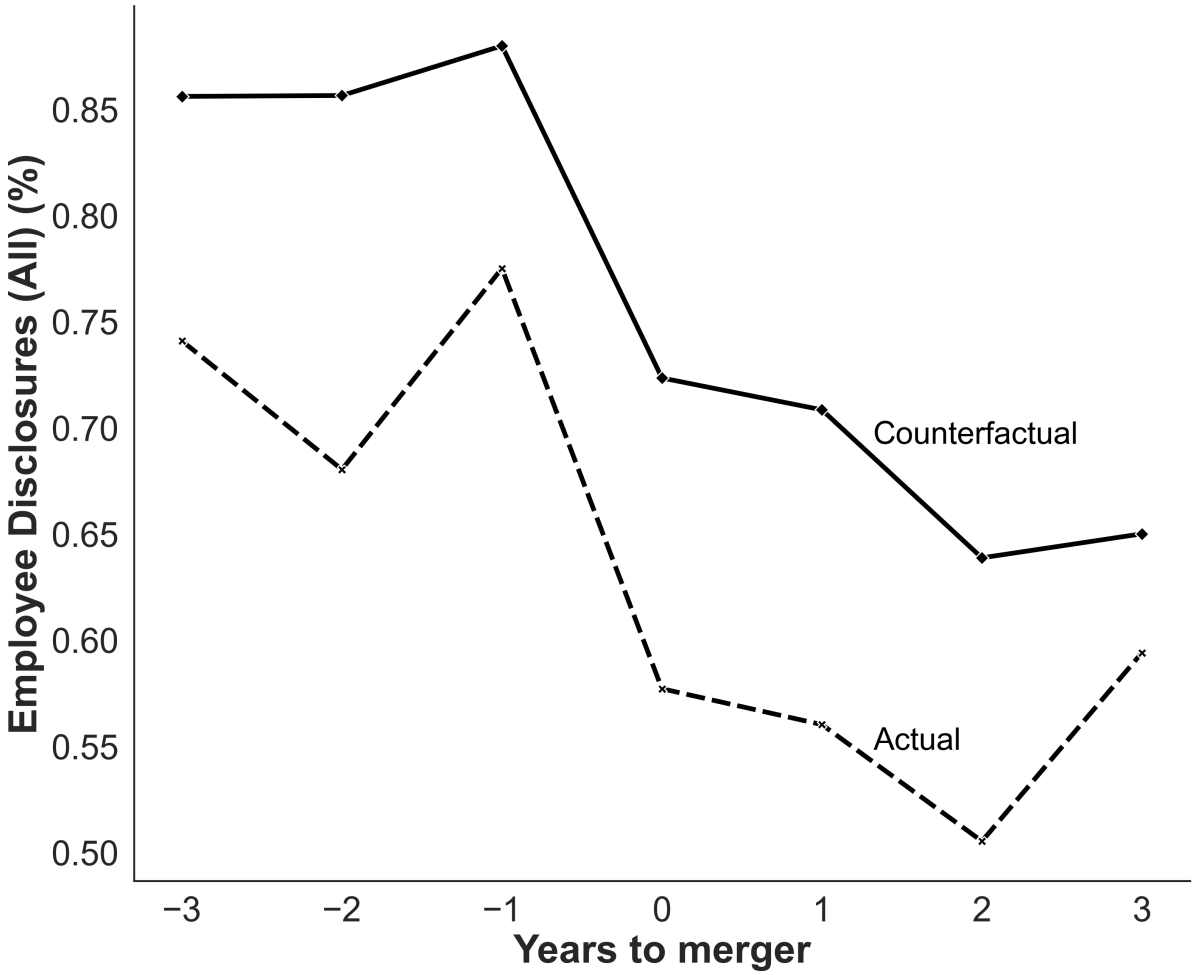


Figure 5: Actual and counterfactual employee disclosures at the combined firm

This figure shows the time series of disclosure events from three years prior to the actual merger year (year 0) for the combined target and acquiring firm. The combined firm in the pre-merger years is constructed based on data from the stand-alone targets and acquirers. The *Counterfactual* series represents all disclosures of employees from the target and acquirer firms, where all employees include those who separated from the entities within the three-year period before and after the merger. The *Actual* series represents disclosures only from those employees who are employed by the combined entity during a given period t. The percentage *Employee Disclosures (All)* is calculated as the count of disclosures across FINRA's 23 categories of disclosure events for each registered representative over the current year, divided by the total number of registered employees in the advisory firm for that year.

Table I: Sample of merger events by year

This table shows the annual count of mergers in the sample, along with the number of unique target and acquiring firms in each year.

Year	# Mergers	# Unique Targets	# Unique Acquirers
2011	13	13	11
2012	23	23	21
2013	31	31	25
2014	32	32	29
2015	53	53	46
2016	51	51	40
2017	61	61	50
2018	63	63	46
2019	114	114	71
2020	69	69	44
Total	510	510	383

Table II: Characteristics of targets and acquirers

This table shows summary statistics for the sample of investment advisory firms that participated in mergers between 2011 and 2020. The term *Employee Disclosures (All)* is the total count of disciplinary events across 23 categories for each adviser over the current year and the previous two years, divided by the total number of registered employees in the advisory firm for that year; *Employee Misconduct (EMS)* includes only 6 out of the 23 categories of disclosures that Egan, Matvos and Seru (2019) consider to be the most clear-cut cases of employee misconduct. Next, *Any Employee Disclosures (All)*, which is similar to *Employee Disclosures (All)* in the disciplinary events we consider, is the number of employees with any disclosure (regardless of when the disclosure occurred), divided by the total number of registered employees in the advisory firm for that year; *Any Employee Disclosures (EMS)* is the total number of employees with any disclosures in the 6 categories used in the EMS measure, (regardless of when the disclosure occurred), divided by total registered employees. Both *Disclosure Growth* and *Misconduct Growth* are the first differences between the total number of disclosures for all employees in the current year and the previous year, scaled by the current number of registered employees working for the advisory firm. The table presents statistics for targets and acquirers separately. Each characteristic of the target and acquirer is measured as of year $t-1$ relative to the merger; *Diff* is the standardized mean difference between a given characteristic for an acquirer and a target, which allows for comparisons of differences across rows.

	Target		**Acquirer**		**Tests**	
	N = 510		**N = 510**			
	Mean	Std. Dev.	Mean	Std. Dev.	Diff	T-stat
# Employees	50.13	277.53	849.43	3360.55	0.34	5.33***
Employee disclosures (All)	1.59	5.36	2.79	5.43	0.22	3.55***
Employee misconduct (EMS)	0.73	2.97	1.06	2.69	0.11	1.83*
Disclosure growth (All)	0.42	1.90	1.07	2.43	0.30	4.71***
Misconduct growth (EMS)	0.19	1.07	0.43	1.22	0.21	3.27***
Any Employee disclosures (All)	8.12	13.76	8.87	9.07	0.06	1.03
Any Employee misconduct (EMS)	4.69	10.22	4.94	6.17	0.03	0.47
AUM ($ Billions)	1.91	10.19	26.28	59.57	0.57	9.07***
AUM growth	10.58	28.64	38.43	68.32	0.53	8.46***
# Clients (000s)	2.35	9.53	59.26	199.77	0.40	6.40***
Client growth	24.38	114.41	62.20	193.47	0.24	3.79***

Table III: Is misconduct relevant in M&A? Predicting targets

This table reports estimates from a linear probability model, predicting the probability that an advisory firm is acquired in a given year. The unit of observation is an advisory firm-year and the sample period is from 2011 through 2019. The indicator *Target* equals one if an advisory firm is acquired by another firm during year $t+1$. The term *Employee Disclosures (All)* is the count of disclosures across the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), for each adviser over the current year and the previous two years, divided by the total number of registered employees working for the advisory firm in that year; *Employee Misconduct (EMS)* includes only 6 (of the 23) categories of misconduct that Egan, Matvos and Seru (2019) consider to be the least ambiguous cases of employee misconduct. Other independent variables include *Retail clients*$_{it}$, a dummy equal to one if the firm serves retail clients; *Ln(Assets under management)*$_{it}$, the natural log of assets under management; *Ln(Firm Age)*$_{it}$ the natural log of firm age; and *Ln(Number of employees)*$_{it}$, the natural log of the number of registered employees. The indicators *Line of business FE* are for the advisory firm's line of business, as reported on Form ADV. We cluster standard errors, which we report in parentheses, by advisory firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}(\textbf{Target})_{t+1} \times 100$				
	(1)	(2)	(3)	(4)
Employees with misconduct (All)	-0.098***	-0.082***		
	(0.021)	(0.022)		
Employees with misconduct (EMS)			-0.075***	-0.059***
			(0.021)	(0.021)
Retail clients		-0.160**		-0.164**
		(0.077)		(0.077)
Ln(Assets under management)		0.015		0.019
		(0.040)		(0.039)
Ln(Firm Age)		0.244***		0.247***
		(0.030)		(0.030)
Ln(Number of employees)		0.086**		0.079*
		(0.042)		(0.041)
Observations	68,402	68,402	68,402	68,402
Adjusted R^2	0.002	0.003	0.002	0.003
Year FE	X	X	X	X
Line of business FE	X	X	X	X

Table IV: Is misconduct relevant in M&A? Predicting acquirers

This table reports estimates from a linear probability model, predicting the probability that an advisory firm makes an acquisition in a given year. The unit of observation is an advisory firm-year and sample period is from 2011 through 2019. *Acquirer* is an indicator that equals one if an advisory firm acquires another firm during year $t+1$. *Employee Disclosures (All)* is the count of disclosures across the 23 categories of disciplinary events in the FINRA data for each adviser over the current year and the previous two years, divided by the total number of registered employees working for the advisory firm in that year; *Employee misconduct (EMS)* includes only 6 (of the 23) categories of disciplinary events that Egan, Matvos and Seru (2019) consider to be the most indicative of employee misconduct. Other independent variables include *Retail clients*$_{it}$, a dummy equal to one if the firm serves retail clients; *Ln(Assets under management)*$_{it}$, the natural log of assets under management; *Ln(Firm Age)*$_{it}$ the natural log of firm age; and *Ln(Number of employees)*$_{it}$, the natural log of the number of registered employees. *Line of business FE* are indicators for the advisory firm's line(s) of business, as reported on Form ADV. We cluster standard errors, which we report in parentheses, by advisory firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}$**(Acquirer)**$_{t+1} \times 100$				
	(1)	(2)	(3)	(4)
Employees with misconduct (All)	-0.042**	-0.076***		
	(0.021)	(0.021)		
Employees with misconduct (EMS)			-0.049***	-0.064***
			(0.018)	(0.018)
Retail clients		-0.175**		-0.179**
		(0.086)		(0.086)
Ln(Assets under management)		0.566***		0.569***
		(0.062)		(0.062)
Ln(Firm Age)		-0.149***		-0.147***
		(0.034)		(0.034)
Ln(Number of employees)		0.602***		0.596***
		(0.089)		(0.088)
Observations	68,402	68,402	68,402	68,402
Adjusted R^2	0.007	0.019	0.007	0.019
Year FE	X	X	X	X
Line of business FE	X	X	X	X

Table V: Matching on misconduct

This table reports estimates from a linear probability model predicting the probability that a given pair of firms will merge in a given year. The unit of observation is a potential target-acquirer pair. For each year, we create counterfactual pairings of every target with all potential acquirers. We define a dummy that equals one when the acquirer and the target both have employees with recent disclosures (*Acq & Tar Employees with misconduct (All)*) or misconduct (*Acq & Tar Employees with misconduct (EMS)*). *All* is the count of disclosures across the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), for each adviser over the current year and the previous two years, divided by the total number of registered employees working for the advisory firm in that year; *(EMS)* includes only 6 (of the 23) categories of disciplinary events that Egan, Matvos and Seru (2019) consider to be the most indicative of employee misconduct. We combine *Assets under management*, *Firm Age*, and *Number of employees* by taking the absolute difference of the natural logs of the acquirer and target values. *Same state* (*Retail Clients*) is an indicator that equals one if the target and acquirer are headquartered in the same state (are both retail focused). *Matching Line of business FE* are indicators that equal one when the target-acquirer pair are both in the same line of business. The lines of business categories are from those reported on Form ADV. *Target & Acquirer Small* (*Large*) are indicators for whether the target and acquiring firm pair are both in the bottom (top) quintile of the AUM distribution in a given year. In the extended specifications in columns (4) and (8), we include indicators for whether both firms report regulatory, civil, and criminal events. *Regulatory Events Both* is an indicator set equal toone if both the target and acquirer have been involved in a regulatory action or proceeding with the SEC, CFTC, federal state or foreign regulatory agency, or FINRA. *Civil Events Both* is an indicator that equals if both firms report civil actions over the past ten years. The indicator *Criminal Misdemeanor Both* (*Criminal Felony Both*) is set to one if the firm or its affiliates have been convicted, charged, or pled guilty to a misdemeanor (felony) in the past 10 years. We cluster standard errors, which we report in parentheses, by acquiring firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	$\mathbb{1}$**(Merged)** $\times$ 100							
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Acq & Tar Employees with misconduct (All)	1.956***	1.880***	1.888***	2.372***				
	(0.642)	(0.645)	(0.646)	(0.646)				
Acq & Tar Employees with misconduct (EMS)					3.657***	3.404***	3.411***	3.973***
					(1.054)	(1.061)	(1.061)	(1.062)
Regulatory Events Both				1.103***				1.087***
				(0.236)				(0.236)
Civil Events Both				0.789*				0.828**
				(0.403)				(0.401)
Criminal Misdemeanor Both				-0.649				-0.641
				(0.799)				(0.799)
Criminal Felony Both				0.391				0.414
				(0.599)				(0.601)
Retail clients		0.890***	0.892***	0.847***		0.888***	0.890***	0.842***
		(0.223)	(0.223)	(0.222)		(0.223)	(0.223)	(0.222)
|Ln(AUM Acq) − Ln(AUM Tar)|		0.213*	0.204*	0.206*		0.210*	0.205*	0.213*
		(0.110)	(0.124)	(0.124)		(0.110)	(0.123)	(0.123)
|Ln(Age Acq) − Ln(Age Tar)|		-0.193**	-0.195**	-0.194**		-0.189**	-0.190**	-0.187**
		(0.092)	(0.092)	(0.092)		(0.091)	(0.092)	(0.092)
|Ln(Emp Acq) − Ln(Emp Tar)|		0.025	0.027	0.306**		0.016	0.018	0.296**
		(0.099)	(0.101)	(0.122)		(0.099)	(0.101)	(0.122)
Same state		10.224***	10.226***	10.254***		10.202***	10.204***	10.229***
		(0.938)	(0.939)	(0.938)		(0.939)	(0.939)	(0.939)
Target & Acquirer Small			0.021	-0.073			-0.006	-0.110
			(0.264)	(0.267)			(0.264)	(0.267)
Target & Acquirer Large			-0.044	0.076			-0.047	0.080
			(0.265)	(0.266)			(0.265)	(0.266)
Observations	22,111	22,111	22,111	22,111	22,111	22,111	22,111	22,111
Adjusted R^2	0.009	0.034	0.034	0.036	0.009	0.035	0.035	0.036
Year FE	X	X	X	X	X	X	X	X
Matching Line of business FE	X	X	X	X	X	X	X	X

Table VI: Characteristics of combined target and acquirer pre and post merger

This table reports summary statistics for a sample of investment advisory firms that were in a merger between 2011 and 2020. We report statistics for the combined advisory firms three years before and three years after the merger. Before the merger, we combine characteristics for the target and acquirer as follows: First, we combine *Employees*, *AUM*, and *Clients* by summing these variables for the target and acquirer in each year. Second, we combine *Employee misconduct (All)*, *Employee misconduct (EMS)*, *Disclosure growth (all)*, *Misconduct growth (EMS)*, *AUM growth*, and *Client growth* by taking the weighted average of each measure for the target and acquirer, weighted by the number of registered advisers of each firm. The sample of mergers ends in 2020 to ensure the availability of post-merger data. We calculate *Disclosure Growth* and *Misconduct growth* as the difference between the total number of disclosures for all employees in the current year and the previous year divided by the current number of registered employees working for the advisory firm; *Diff* is the standardized mean difference between a given variable in the pre- versus the post-period.

	Pre-Merger		**Post-Merger**		**Tests**	
	N = 474		**N = 474**			
	Mean	Std. Dev.	Mean	Std. Dev.	Diff	T-stat
# Employees	899.45	3372.21	1084.29	3997.41	0.05	4.54***
Employees misconduct (All)	2.79	4.73	2.19	3.92	-0.14	-4.36***
Employees misconduct (EMS)	1.11	2.41	0.92	2.05	-0.09	-2.38**
Misconduct growth (All)	1.04	2.58	0.80	2.36	-0.10	-2.57**
Misconduct growth (EMS)	0.46	1.61	0.40	1.91	-0.03	-0.81
AUM ($ Billions)	25.87	57.17	43.91	98.28	0.22	8.39***
AUM growth	27.82	60.54	16.61	31.84	-0.24	-4.93***
# Clients (000s)	56.74	184.46	82.63	255.12	0.11	6.71***
Client growth	44.31	127.76	23.14	83.53	-0.20	-4.93***

Table VII: Characteristics of combined pseudo target and acquirer pre- and post-merger

The table reports statistics for the pseudo merged advisory firms (i.e., matched sample of firms that are not involved in a merger) three years before and three years following the merger. Before the merger, we combine variables for the pseudo target and pseudo acquirer as follows: First, we combine *Employees*, *AUM*, and *Clients* by summing these characteristics for the pseudo target and acquirer in each year. Second, we combine *Employee Disclosure (All)*, *Employee misconduct (EMS)*, *Disclosure growth (all)*, *Misconduct growth (EMS)*, *AUM growth*, and *Client growth* by taking the weighted average of each characteristic for the pseudo target and acquirer, where the weight is the number of registered employees. The sample of mergers ends in 2020 to ensure sufficient post-merger data. *Disclosure growth* and *Misconduct growth* are calculated as the difference between the total number of disclosures for all employees in the current year and the previous year, divided by the current number of registered advisers working for the advisory firm; *Diff* is the standardized mean difference between a given variable in the pre- versus the post-period. Standardized differences facilitate comparison of differences across rows.

	Pre-Merger		**Post-Merger**		**Tests**	
	N = 474		**N = 474**			
	Mean	Std. Dev.	Mean	Std. Dev.	Diff	T-stat
# Employees	356.47	1323.72	397.48	1463.44	0.03	3.29***
Employees misconduct (All)	2.86	4.80	2.83	4.89	-0.01	-0.18
Employees misconduct (EMS)	1.00	2.18	1.20	2.65	0.08	2.34**
Misconduct growth (All)	1.02	2.34	1.25	4.78	0.06	1.48
Misconduct growth (EMS)	0.42	1.48	0.57	2.53	0.07	1.85*
AUM ($ Billions)	9.10	32.71	12.50	48.64	0.08	3.61***
AUM growth	28.56	68.03	15.02	26.71	-0.28	-5.02***
# Clients (000s)	17.87	65.29	19.07	54.86	0.02	1.00
Client growth	38.41	128.19	20.82	77.21	-0.17	-3.59***

Table VIII: Post-merger misconduct at the combined firm

This table reports results from a regression predicting disclosures of the combined target and acquiring firm (*Merged*) relative to a pseudo merged firm. A unit of observation is a real or pseudo target-acquirer pair during year t (where we measure t from $t = -3$ to $+3$ relative to the merger year 0). To create the pseudo merged firm, we first generate the following variables: an indicator that equals one for firms with above median employee disclosures (*Disclosures*), an indicator that equals one with above median change in disclosures (*Disclosure Change*), number of employees decile (*Employee Decile*), and line of business (*Industry*). We match each target or acquirer to advisory firms that were never in a merger on *Disclosures*, *Disclosure Change*, *Employee Decile*, *Industry*, and year, where year is the year of the merger. Within the set of matched firms, we keep the firm with the closest level of employee misconduct. We create pseudo mergers by combining the matched target to the matched acquiring firm. Each year, we combine misconduct of the merged pair by taking the weighted average employee misconduct of the target and acquiring firm. The *Post* indicator is for the years following the merger. The term *Employee Misconduct All* is the count of new disclosures (in year t, $t-1$, and $t-2$) in the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), for each adviser divided by the total number of registered employees working for the advisory firm in that year; *Employee Misconduct (EMS)* includes only 6 (of the 23) categories of new disciplinary events (in year t, $t-1$, and $t-2$) that Egan, Matvos and Seru (2019) consider to be most indicative of employee misconduct. We cluster standard errors, which we report in parentheses, by cohort. A cohort comprises a target and acquiring firm and a pseudo target and pseudo acquiring firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	Employee misconduct (All)		**Employee misconduct (EMS)**	
	(1)	(2)	(3)	(4)
Merged X Post	-0.565***	-0.702***	-0.396***	-0.432***
	(0.189)	(0.193)	(0.109)	(0.110)
Merged	-0.073	-0.023	0.114	0.161**
	(0.051)	(0.081)	(0.071)	(0.076)
Post	0.850***	1.086***	0.451***	0.559***
	(0.278)	(0.264)	(0.139)	(0.132)
Retail clients		1.334***		0.638***
		(0.346)		(0.176)
Ln(Assets under management)		-0.497***		-0.209***
		(0.068)		(0.033)
Ln(Firm Age)		-0.609***		-0.317***
		(0.208)		(0.118)
Ln(Number of employees)		1.467***		0.437***
		(0.101)		(0.046)
Observations	6,292	6,292	6,292	6,292
Adjusted R^2	0.032	0.145	0.009	0.061
Year FE	X	X	X	X

Table IX: How does M&A discipline employees?

This table reports estimates from a linear probability model predicting the probability that a given advisor leaves their current job as a function of whether the advisor worked for the target (Panel A) or the acquirer (Panel B) in the three years before the acquisition. The dependent variable is *Separation*, an indicator equal to one if a representative that worked for the target or acquirer in year t no longer works for the target, acquirer, or combined firm in year $t+1$. The sample includes all advisers working either for the target or acquirer in the three years preceding the merger year. The regressions are run at the individual advisor-year level using data for years -3 to $+3$ relative to the merger event at $t=0$. *Employee Disclosure (All)* is an indicator that equals one if the adviser has a disclosure in any of the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), in the current year; *Employee Misconduct (EMS)* is an indicator that equals one if the adviser has a disclosure in any of the 6 categories of disciplinary events defined as misconduct in Egan, Matvos and Seru (2019). *Post* is an indicator that equals one for the year of the merger and the three years following the merger; *Firm* $\times$ *Year FE* are target or acquiring firm by year fixed effects. We cluster standard errors, which we report in parentheses, by firm. $^{***}p<0.01$ denotes significance at the 1% level, $^{**}p<0.05$ denotes significance at the 5% level, and $^{*}p<0.10$ denotes significance at the 10% level.

	$\mathbb{1}$**(Separation)**$_{t+1}$			
Panel A	**Target Employees**			
	(1)	(2)	(3)	(4)
Employee misconduct (All) × Post	5.138**	4.711**		
	(2.189)	(2.236)		
Employee misconduct (EMS) × Post			14.473***	13.893***
			(3.308)	(3.333)
Employee misconduct (All)	7.145***	8.290***		
	(1.797)	(1.482)		
Employee misconduct (EMS)			9.002**	10.353***
			(3.848)	(3.447)
Ln(Experience)		-1.005***		-0.999***
		(0.326)		(0.328)
Ln(# Qualifications)		-2.086***		-2.078***
		(0.697)		(0.693)
Observations	100,027	100,027	100,027	100,027
Adjusted R^2	0.146	0.151	0.147	0.151
Target Firm × Year FE	X	X	X	X
Panel B	**Acquirer Employees**			
Employees with misconduct (All) × Post	-0.680	-0.619		
	(0.493)	(0.514)		
Employees with misconduct (EMS) × Post			-4.985***	-4.861***
			(1.401)	(1.376)
Employees with misconduct (All)	12.605***	13.229***		
	(1.219)	(1.170)		
Employees with misconduct (EMS)			30.896***	31.647***
			(3.592)	(3.522)
Ln(Experience)		-2.195***		-2.193***
		(0.193)		(0.192)
Ln(# Qualifications)		-0.809***		-0.822***
		(0.272)		(0.270)
Observations	1,829,089	1,829,089	1,829,089	1,829,089
Adjusted R^2	0.036	0.043	0.039	0.046
Acquiring Firm × Year FE	X	X	X	X

Table X: Employee separations when target firm managers depart

This table presents estimates from a linear probability model predicting the likelihood that a registered investment advisor departs from their current position. The specification is identical to that in Table IX except we introduce *NM*, an indicator set equal to one if none of the target firm's top managers or owners remain in their roles at the combined firm post-merger. The dependent variable is *Separation*, an indicator equal to one if a representative who worked for the target in year t no longer works for the target, acquirer or combined firm in year $t+1$. The *Employee Disclosure (All)* indicator is one if the advisor has a disclosure in any of the 23 categories of disciplinary events from Egan, Matvos and Seru (2019) in the current year. The *Employee Misconduct (EMS)* indicator is one if the advisor has a disclosure in any of the 6 categories of disciplinary events defined as misconduct in Egan, Matvos and Seru (2019). The *Post* indicator is one for the year of the merger and the three subsequent years. We cluster standard errors, which we report in parentheses, by firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	$\mathbb{1}$**(Separation)**$_{t+1}$			
	Target Employees – Lost Old Managers			
	(1)	(2)	(3)	(4)
Employee misconduct (All) × Post × NM	25.265***	24.893***		
	(5.546)	(5.843)		
Employee misconduct (All) × Post × NM			25.440**	24.118*
			(12.749)	(13.061)
Employee misconduct (All) × Post	-19.216***	-19.283***		
	(5.086)	(5.402)		
Employee misconduct (EMS) × Post			-9.927	-9.228
			(12.338)	(12.682)
Employee misconduct (All) × NM	-4.285	-4.013		
	(4.066)	(3.953)		
Employee misconduct (All) × NM			-0.014	1.059
			(7.020)	(6.738)
Employee misconduct (All)	11.312***	12.192***		
	(3.645)	(3.614)		
Employee misconduct (EMS)			9.015	9.325
			(5.795)	(5.723)
Ln(Experience)		-1.006***		-1.000***
		(0.326)		(0.328)
Ln(# Qualifications)		-2.085***		-2.077***
		(0.698)		(0.693)
Observations	100,027	100,027	100,027	100,027
Adjusted R^2	0.146	0.151	0.147	0.151
Target Firm × Year FE	X	X	X	X

Table XI: Post-merger employee disclosures

This table reports estimates from a regression predicting disciplinary disclosures of target firm employees (*Target*) relative to employees of a pseudo target firm. A unit of observation is an adviser working for the real or pseudo target firm in the three years before the merger. To create the pseudo merged firm, we first generate the following variables: an indicator that equals one for firms with above median employee disclosures (*Disclosures*), above median change in disclosures (*Disclosure Change*), employee decile (*Employee Decile*), and line of business (*Industry*). Then we match each target to advisory firms that were never in a merger on *Disclosure*, *Disclosure Change*, *Employee Decile*, *Industry*, and year, where year is the year of the merger. Within the set of matched firms, we keep the pseudo target with the closest level of employee misconduct. The indicator *Post* is an indicator for the years following the merger. *Flow Misconduct (All)* equals one if the adviser has a disclosure (only in year t) in the 23 categories of disciplinary events from Egan, Matvos and Seru (2019); *Flow Misconduct (EMS)* includes only 6 (of the 23) categories of new disciplinary events (in year t) that Egan, Matvos and Seru (2019) consider to be most indicative of employee misconduct. This table includes only those advisers working for the target or pseudo target firm *before and following* the merger. We cluster standard errors, which we report in parentheses, by cohort. A cohort comprises a target and a pseudo target firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	Flow Misconduct (All)		**Flow Misconduct (EMS)**	
	(1)	(2)	(3)	(4)
Target × Post	-0.174	-0.192	-0.147	-0.158
	(0.136)	(0.134)	(0.118)	(0.117)
Target	0.140	0.157	0.251**	0.257**
	(0.103)	(0.103)	(0.106)	(0.102)
Ln(Experience)		0.187		0.139
		(0.168)		(0.097)
Ln(# Qualifications)		0.263**		0.139***
		(0.111)		(0.048)
Observations	296,942	296,942	296,942	296,942
Adjusted R^2	0.004	0.005	0.008	0.009
Cohort × Year FE	X	X	X	X

Table XII: Is misconduct value-relevant in the investment advisory industry?

This table presents regression estimates of the relationship between past employee misconduct and year-ahead firm performance. The performance variables are assets management per employee (AUM/Employees) and firm closure. The sample includes all investment advisory firms that filed a Form ADV from 2010 to 2021. In Panel A, the dependent variable is the natural logarithm of AUM divided by the number of advisers the firm employs in year $t+1$, $Ln(\frac{AUM}{Employees})_{t+1}$. In Panel B, the dependent variable is an indicator equal to one if a firm files a Form ADV-W with the SEC, stating the closure of the business or cessation of advisory activities as the reason for closure, $Failed_{t+1}$. The variable *Employee Disclosures (All)* measures the number of disclosures across 23 categories of disciplinary events, as defined by Egan, Matvos and Seru (2019), for each adviser over the current year and the previous two years, divided by the total number of registered employees working for the advisory firm in that year. The variable *Employee Misconduct (EMS)* includes only 6 of the 23 categories of disciplinary events that Egan, Matvos and Seru (2019) identify as most representative of employee misconduct. The *Line of Business FE* are line of business indicators, as reported on Form ADV. Standard errors are in parentheses and are clustered by advisory firm; $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

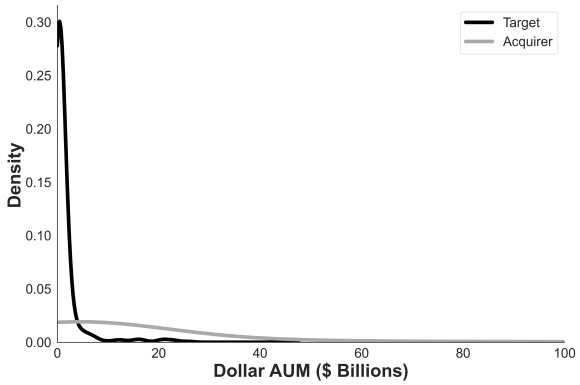
Panel A:	$\mathbf{Ln(\frac{AUM}{Employees})_{t+1}}$			
	(1)	(2)	(3)	(4)
Employees with misconduct (All)	-0.029***	-0.013***		
	(0.004)	(0.003)		
Employees with misconduct (EMS)			-0.019***	-0.008**
			(0.004)	(0.003)
Retail clients		-0.053***		-0.053***
		(0.008)		(0.008)
Ln(Firm Age)		0.260***		0.260***
		(0.015)		(0.015)
Ln(Number of employees)		-1.028***		-1.029***
		(0.018)		(0.018)
Observations	80,090	80,090	80,090	80,090
Adjusted R^2	0.903	0.926	0.903	0.926
Year FE	X	X	X	X
Firm FE	X	X	X	X

Table XII - *continued*

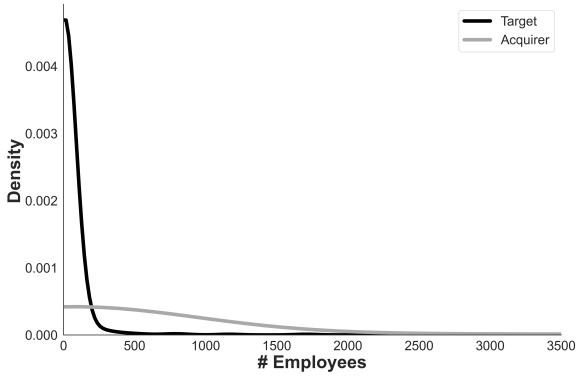
Panel B:	$\mathbb{1}$**(Failed)**$_{t+1}$			
	(1)	(2)	(3)	(4)
Employees with misconduct (All)	0.227***	0.231***		
	(0.049)	(0.050)		
Employees with misconduct (EMS)			0.165***	0.164***
			(0.045)	(0.046)
Retail clients		0.140		0.158*
		(0.089)		(0.088)
Ln(Firm Age)		-0.028		-0.038
		(0.037)		(0.037)
Ln(Number of employees)		-0.084**		-0.066*
		(0.039)		(0.039)
Observations	81,512	81,512	81,512	81,512
Adjusted R^2	0.004	0.004	0.003	0.004
Year FE	X	X	X	X
Line of business FE	X	X	X	X

Misconduct Synergies

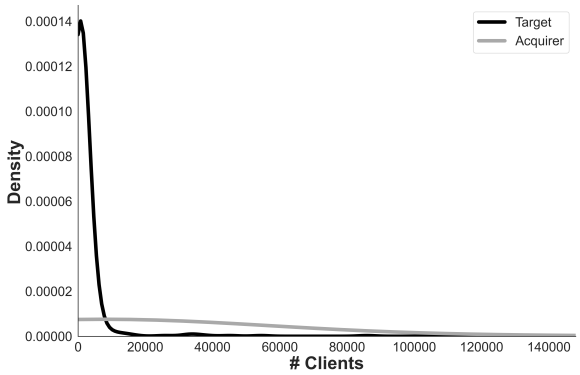
Internet Appendix



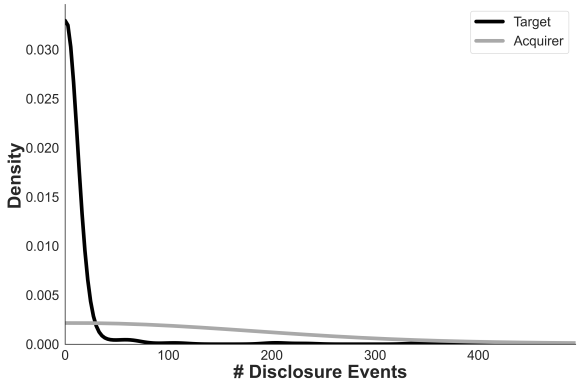
Panel A: Distribution of Assets Under Management



Panel B: Distribution of Employees



Panel C: Distribution of Clients



Panel D: Distribution of Disclosure Events

Figure A1: Distribution of key variables for target and acquiring firms

This figure shows the distribution of Assets Under Management (*AUM*), number of employees (*Employees*), number of clients (*# Clients*), and the number of past disclosure events (*# Disclosure Events*) for target and acquiring firms in our sample, where these variables are taken from the Form ADV filed by the target or acquiring firm as of year *t-1* relative to the merger.

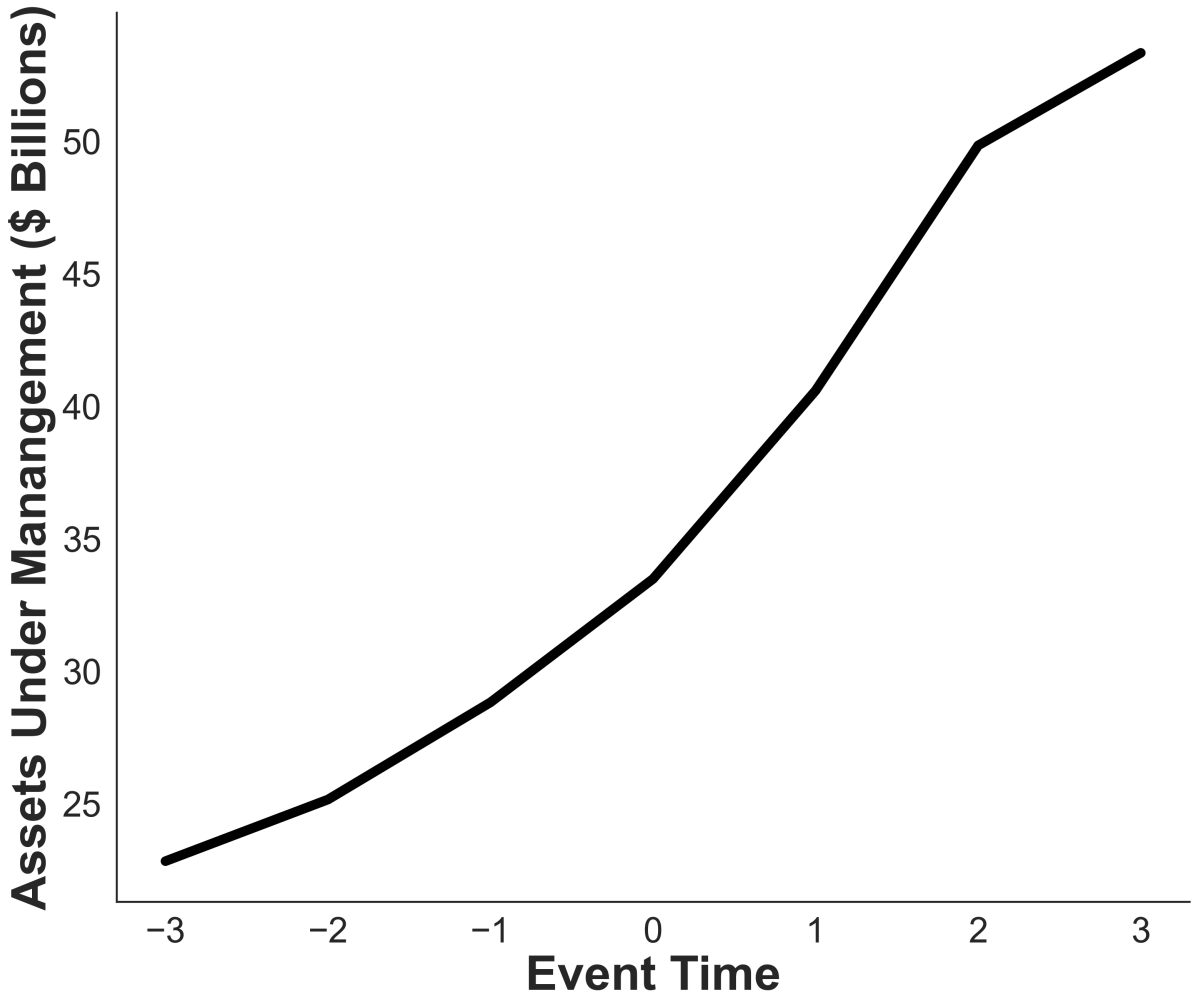


Figure A2: Assets under management (AUM) of combined firm in event time

This figure plots average assets under management for the combined target and acquiring firm for the sample of investment advisory firms that merged in year zero.

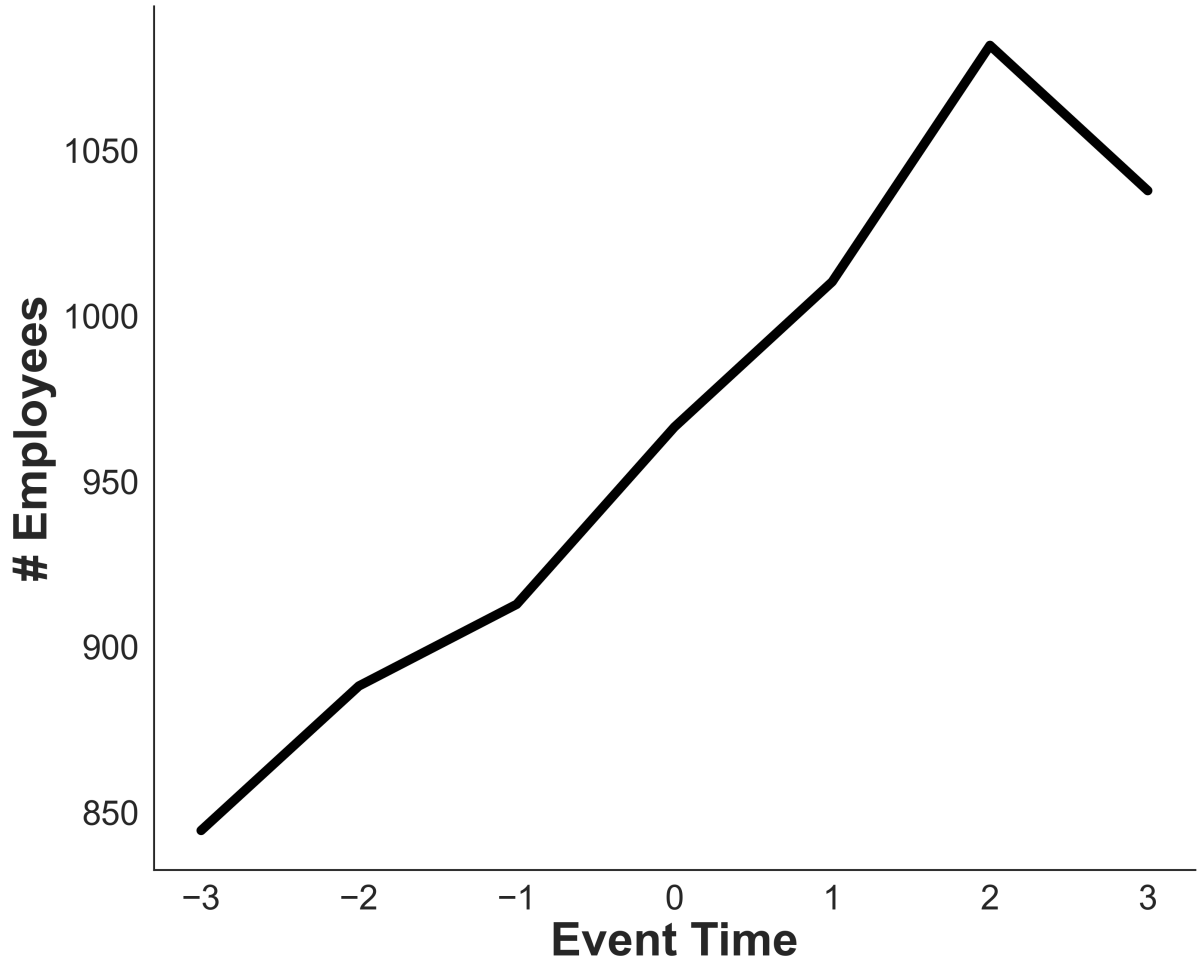


Figure A3: Number of employees of combined firm in event time

This figure plots the average number of registered advisers for the combined target and acquiring firm for the sample of investment advisory firms that merged in year zero.

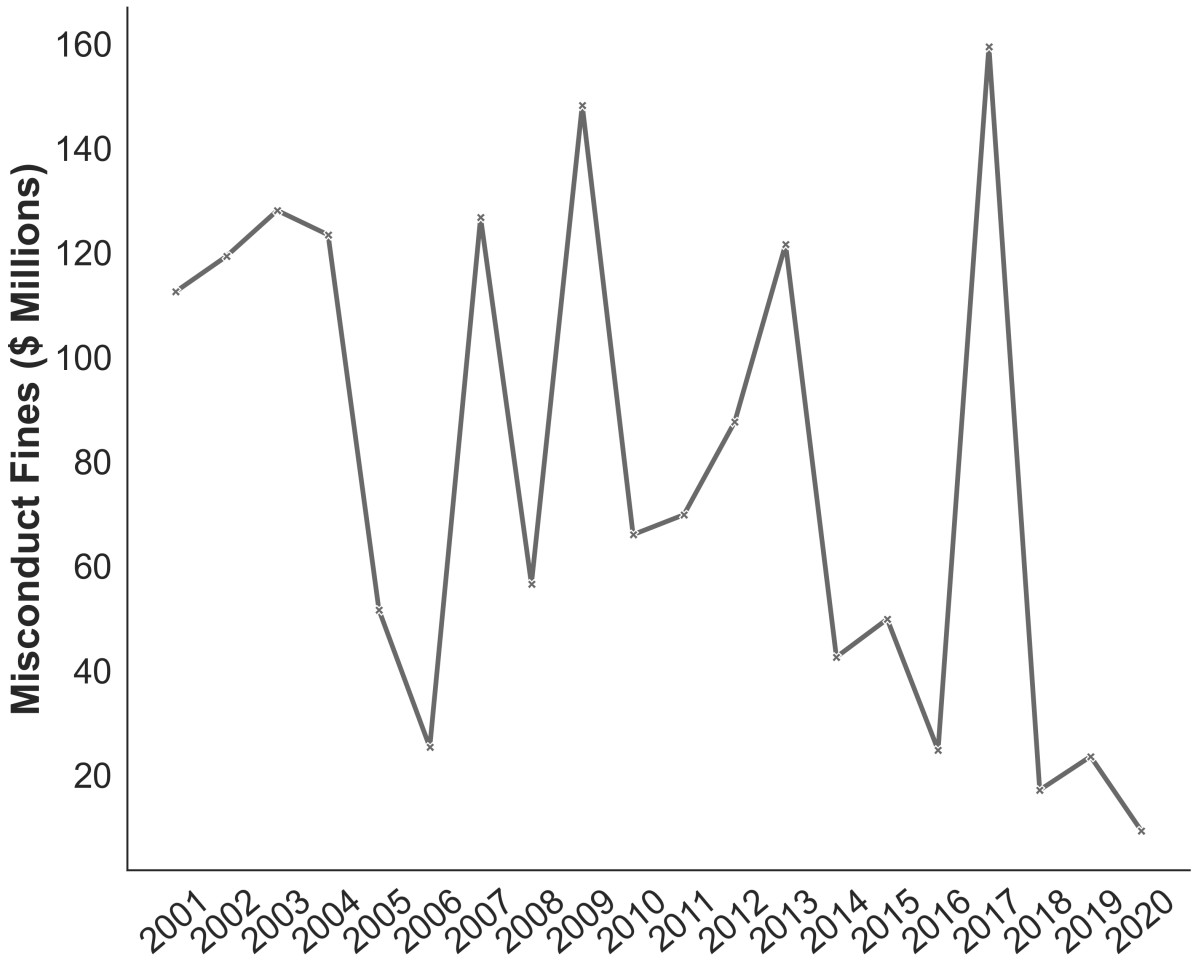
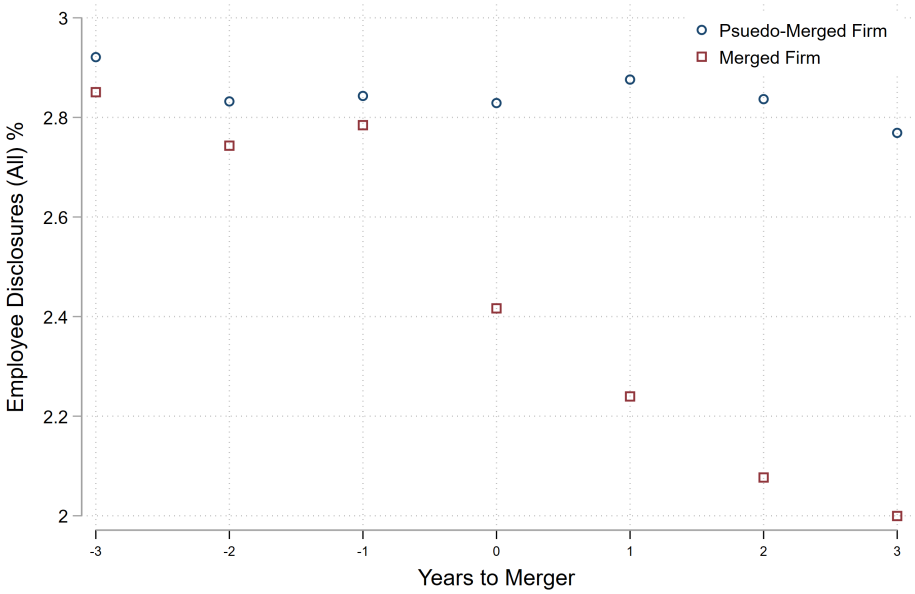
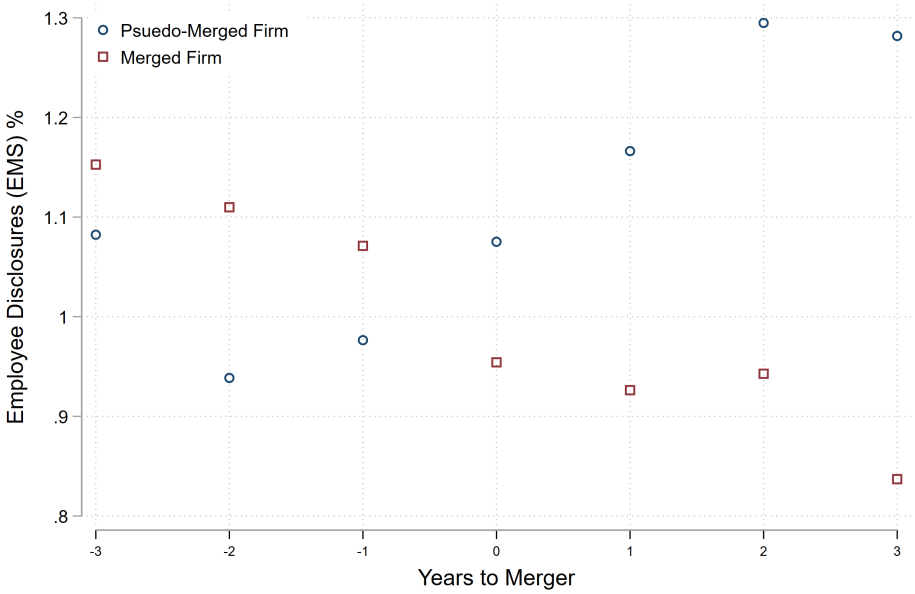


Figure A4: Direct costs of employee misconduct

This figure plots the total yearly fines paid by advisory firms whose employees had at least one disclosure.



Panel A: Employee disclosures (All) at the combined firm



Panel B: Employee disclosures (EMS) at the combined firm

Figure A5: Employee disclosures at the combined firm

This figure shows employee disclosures following the merger for the combined firm, by whether the combined firm is a real (*Merged Firm* equals one) or a pseudo-merging firm (*Merged Firm* equals zero). Panel A focuses on the Employees with misconduct (ALL) measure, and Panel B focuses on the Employees with misconduct (EMS) measure. Please refer to Table VIII for a detailed explanation of the sample construction and the selection of pseudo merging firms for which (*Merged Firm*) equals zero. The sample is restricted to mergers that occur between 2011 to 2020 to ensure each merged and pseudo merged firm has sufficient pre- and post-merger data.

Table A.1: Is misconduct relevant in M&A? Predicting targets (Line of business fixed effects)

This table shows the line of business fixed effect estimates from Table III, which estimates the probability that an advisory firm is acquired in a given year. *Target* is an indicator that equals one if an advisory firm is acquired by another firm during year t+1. The sample period is from 2011 through 2019. *Employee Disclosures (All)* is the count of disclosures across the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), for each adviser over the current year and the previous two years, divided by the total number of employees working for the advisory firm in that year. *Employee misconduct (EMS)* includes only 6 (of the 23) categories of misconduct that Egan, Matvos and Seru (2019) consider to be the least ambiguous cases of employee misconduct. The lines of businesses indicate the advisory firm's line(s) of business, as reported on Form ADV. *Financial Planning* is an indicator for advisory firms providing financial planning services. *Individuals and Small Businesses* is an indicator for portfolio management services to individuals and small businesses. *Investment Companies* is an indicator for portfolio management services for investment companies. *Pooled Funds* is an indicator for portfolio management services for pooled investment vehicles but not investment companies. *Large Businesses* is an indicator for portfolio management services for non-small businesses and other institutional clients that are neither investment companies nor pooled investment vehicles. *Pension Consulting* is an indicator for pension consulting services. *Selection Advisers* is an indicator for the adviser selection services (including private fund managers). *Publication Periodicals* is an indicator for the publication of periodicals or newsletters. *Market Timing* is an indicator for market timing services. *Other* is an indicator for advisers that provide educational seminars or other lines of business not covered in the categories above. *Other Controls* are the other control variables defined in Table III. We cluster standard errors (reported in parentheses) by advisory firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}(\textbf{Target})_{t+1} \times 100$				
	(1)	(2)	(3)	(4)
Employees with misconduct (All)	-0.098***	-0.082***		
	(0.021)	(0.022)		
Employees with misconduct (EMS)			-0.075***	-0.059***
			(0.021)	(0.021)
Financial Planning	0.102	0.125	0.097	0.123
	(0.075)	(0.077)	(0.075)	(0.077)
Individuals Small Business	0.301***	0.260**	0.303***	0.265**
	(0.098)	(0.103)	(0.098)	(0.103)
Investment Companies	-0.016	-0.126	-0.014	-0.127
	(0.103)	(0.108)	(0.103)	(0.108)
Large Businesses	0.023	-0.076	0.023	-0.077
	(0.069)	(0.070)	(0.069)	(0.070)
Pension Consulting	0.079	0.075	0.077	0.075
	(0.081)	(0.082)	(0.081)	(0.082)
Selection Advisers	0.235***	0.201***	0.229***	0.198**
	(0.076)	(0.078)	(0.076)	(0.078)
Publication Periodicals	0.149	0.095	0.150	0.096
	(0.145)	(0.145)	(0.145)	(0.145)
Ratings and Pricing	-0.574***	-0.640***	-0.588***	-0.645***
	(0.074)	(0.102)	(0.072)	(0.100)
Market Timing	0.052	0.010	0.045	0.006
	(0.151)	(0.151)	(0.151)	(0.151)
Other	0.307***	0.268***	0.309***	0.269***
	(0.102)	(0.103)	(0.102)	(0.103)
Observations	68,402	68,402	68,402	68,402
Adjusted R^2	0.002	0.003	0.002	0.003
Year FE	X	X	X	X
Other Controls		X		X

Table A.2: Is misconduct relevant in M&A? Predicting acquirers (Line of business fixed effects)

This table shows the line of business fixed effect estimates from Table IV, which estimates the probability that an advisory firm acquirers another firm in a given year. *Acquirer* is an indicator that equals one if an advisory firm acquires another firm during year $t+1$. The sample period is from 2011 through 2020. *Employee Disclosures (All)* is the count of disclosures across the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), for each adviser over the current year and the previous two years, divided by the total number of employees working for the advisory firm in that year. *Employee misconduct (EMS)* includes only 6 (of the 23) categories of misconduct that Egan, Matvos and Seru (2019) consider to be the least ambiguous cases of employee misconduct. The lines of businesses indicate the advisory firm's line(s) of business, as reported on Form ADV. *Financial Planning* is an indicator for advisory firms providing financial planning services. *Individuals and Small Businesses* is an indicator for portfolio management services to individuals and small businesses. *Investment Companies* is an indicator for portfolio management services for investment companies. *Pooled Funds* is an indicator for portfolio management services for pooled investment vehicles but not investment companies. *Large Businesses* is an indicator for portfolio management services for non-small businesses and other institutional clients that are neither investment companies nor pooled investment vehicles. *Pension Consulting* is an indicator for pension consulting services. *Selection Advisers* is an indicator for the adviser selection services (including private fund managers). *Publication Periodicals* is an indicator for the publication of periodicals or newsletters. *Market Timing* is an indicator for market timing services. *Other* is an indicator for advisers that provide educational seminars or other lines of business not covered in the categories above. *Other Controls* are the other control variables defined in Table III. We cluster standard errors (reported in parentheses) by advisory firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}(\textbf{Acquirer})_{t+1} \times 100$				
	(1)	(2)	(3)	(4)
Employees with misconduct (All)	-0.042**	-0.076***		
	(0.021)	(0.021)		
Employees with misconduct (EMS)			-0.049***	-0.064***
			(0.018)	(0.018)
Financial Planning	0.240***	0.110	0.238***	0.108
	(0.074)	(0.074)	(0.074)	(0.074)
Individuals Small Business	0.079	0.240**	0.080	0.244**
	(0.097)	(0.104)	(0.097)	(0.105)
Investment Companies	0.880***	0.183	0.880***	0.182
	(0.159)	(0.167)	(0.159)	(0.167)
Large Businesses	0.281***	-0.049	0.281***	-0.050
	(0.081)	(0.076)	(0.081)	(0.076)
Pension Consulting	0.532***	0.339***	0.532***	0.339***
	(0.119)	(0.106)	(0.119)	(0.106)
Selection Advisers	0.647***	0.259***	0.646***	0.257***
	(0.092)	(0.078)	(0.092)	(0.078)
Publication Periodicals	0.707***	0.637***	0.706***	0.638***
	(0.243)	(0.234)	(0.243)	(0.234)
Ratings and Pricing	-0.788***	-1.323***	-0.792***	-1.328***
	(0.148)	(0.349)	(0.148)	(0.348)
Market Timing	-0.163	-0.335**	-0.165	-0.339***
	(0.127)	(0.130)	(0.127)	(0.131)
Other	0.499***	0.368**	0.499***	0.369**
	(0.158)	(0.149)	(0.158)	(0.149)
Observations	68,402	68,402	68,402	68,402
Adjusted R^2	0.007	0.019	0.007	0.019
Year FE	X	X	X	X
Other Controls		X		X

Table A.3: Matching on misconduct: Line of business fixed effects

This table reports the line of business fixed effect estimates from the model in Table V, which predicts whether a pair of firms will merge in a given year. A unit of observation is a potential target-acquirer pair. For each year, we create counterfactual mergers—pairings of every target with all potential acquirers in that year. We measure misconduct similarity of the target and acquirer by defining a dummy that equals one when the acquirer and the target both have employees with recent disclosures (*Mean Acq & Tar Employees with misconduct (All)*) or Misconduct (*Acq & Tar Employees with misconduct (EMS)*). The lines of businesses indicate the advisory firm's line(s) of business, as reported on Form ADV. *Financial Planning* is an indicator for advisory firms providing financial planning services. *Individuals and Small Businesses* is an indicator for portfolio management services to individuals and small businesses. *Investment Companies* is an indicator for portfolio management services for investment companies. *Pooled Funds* is an indicator for portfolio management services for pooled investment vehicles but not investment companies. *Large Businesses* is an indicator for portfolio management services for non-small businesses and other institutional clients that are neither investment companies nor pooled investment vehicles. *Pension Consulting* is an indicator for pension consulting services. *Selection Advisers* is an indicator for the adviser selection services (including private fund managers). *Publication Periodicals* is an indicator for the publication of periodicals or newsletters. *Market Timing* is an indicator for market timing services. *Other* is an indicator for advisers that provide educational seminars or other lines of business not covered in the categories above. *Other Controls* are the other control variables defined in Table III. We cluster standard errors (reported in parentheses) by acquiring firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}$**(Merged)** $\times$ 100				
	(1)	(2)	(3)	(4)
Acq & Tar Employees with misconduct (All)	1.925***	1.835***		
	(0.642)	(0.645)		
Acq & Tar Employees with misconduct (EMS)			3.609***	3.207***
			(1.054)	(1.059)
Financial Planning	1.115***	1.095***	1.128***	1.129***
	(0.204)	(0.202)	(0.204)	(0.201)
Individuals Small Business	-0.014	0.022	-0.030	0.022
	(0.365)	(0.364)	(0.365)	(0.364)
Investment Companies	1.000***	1.131***	0.999***	1.189***
	(0.233)	(0.236)	(0.233)	(0.237)
Pooled Funds	0.598***	0.696***	0.587***	0.680***
	(0.208)	(0.210)	(0.208)	(0.210)
Large Businesses	0.504**	0.505***	0.515***	0.460**
	(0.196)	(0.194)	(0.196)	(0.193)
Pension Consulting	0.943***	0.914***	0.953***	0.914***
	(0.197)	(0.195)	(0.197)	(0.194)
Selection Advisers	0.376*	0.372*	0.360*	0.331*
	(0.194)	(0.191)	(0.194)	(0.191)
Publication Periodicals	0.022	0.135	0.006	0.131
	(0.222)	(0.220)	(0.222)	(0.220)
Market Timing	0.261	0.074	0.352	0.161
	(0.893)	(0.873)	(0.890)	(0.873)
Other	0.083	0.131	0.088	0.138
	(0.200)	(0.196)	(0.200)	(0.197)
Observations	22,111	22,111	22,111	22,111
Adjusted R^2	0.009	0.035	0.010	0.036
Year FE	X	X	X	X
Other Controls		X		X

Table A.4: Frequent acquirers in our sample

This table shows the acquirers in our sample that made more than two acquisitions of other advisory firms between 2011 and 2020.

Acquirer Name	# Unique Targets
MERCER GLOBAL ADVISORS INC.	21
HIGHTOWER ADVISORS, LLC	16
UNITED CAPITAL FINANCIAL ADVISERS	11
LPL FINANCIAL LLC	10
THE WEALTH ENHANCEMENT GROUP, INC.	10
EP WEALTH ADVISORS	10
CREATIVE PLANNING	9
CAPTRUST	9
BUCKINGHAM STRATEGIC WEALTH	8
MARINER WEALTH ADVISORS	7
STIFEL, NICOLAUS & COMPANY	7
THE COLONY GROUP, LLC	6
THE MATHER GROUP, LLC	6
SAVANT CAPITAL MANAGEMENT	6
BANYAN PARTNERS, LLC	4
BROWN ADVISORY	4
HIGHTOWER ADVISORS LLC	4
MAI CAPITAL MANAGEMENT, LLC	4
THE MATHER GROUP, LLC	4
WEALTHSPIRE ADVISORS	4
ALLWORTH FINANCIAL, L.P.	3
BLACKROCK INVESTMENT MANAGEMENT, LLC	3
BUCKINGHAM STRATEGIC WEALTH, LLC	3
EATON VANCE MANAGEMENT	3
HBKS WEALTH ADVISORS	3
LOVELL MINNICK PARTNERS LLC	3
PATHSTONE FEDERAL STREET	3
PROSPERA FINANCIAL SERVICES, INC.	3
ROBERT W. BAIRD & CO. INCORPORATED	3
VICTORY CAPITAL MANAGEMENT INC.	3
WEALTH ENHANCEMENT GROUP LLC	3
WUNDERLICH SECURITIES, INC.	3

Table A.5: Post merger misconduct (Frequent acquirers)

This table reports results from a regression predicting disclosures of the combined target and acquiring firm (*Merged*) relative to a pseudo merged firm. A unit of observation is a real or pseudo target-acquirer pair during the three years before and three years following the merger. To create the pseudo merged firm, we first create the following variables: an indicator that equals one for firms with above median employee disclosures (Disclosures), above median change in disclosures (Disclosure Change), employee decile (Employee Decile), and line of business (Industry). Then we match each target or acquirer to advisory firms that were never in a merger on Disclosure, Disclosure Change, Employee Decile, Industry, and year, where year is the year of the merger. Within the set of matched firms, we keep the firm with the closest level of employee misconduct. We create pseudo mergers by combining the matched target to the matched acquiring firm. Each year, we combine misconduct of the merged pair by taking the weighted average employee misconduct of the target and acquiring firm. *Post* is an indicator for the years following the merger. *Frequent* is an indicator for true acquiring firms that made more than one acquisition over our sample period. *Employee misconduct (All)* is the count of new disclosures (in year t, t-1, and t-2) in the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), for each adviser divided by the total number of employees working for the advisory firm in that year. *Employee misconduct (EMS)* includes only 6 (of the 23) categories of new disciplinary events (in year t, t-1, and t-2) that Egan, Matvos and Seru (2019) consider to be most indicative of employee misconduct. We cluster standard errors, which we report in parentheses, by cohort. A cohort comprises a target- and acquiring firm and a pseudo target- and acquiring firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	Employee misconduct (All)		**Employee misconduct (EMS)**	
	(1)	(2)	(3)	(4)
Merged X Post X Frequent	0.037	0.179	0.226	0.310*
	(0.266)	(0.269)	(0.156)	(0.159)
Merged X Post	-0.579**	-0.806***	-0.496***	-0.574***
	(0.251)	(0.251)	(0.153)	(0.154)
Merged	-0.220	0.373**	0.114	0.315**
	(0.171)	(0.170)	(0.122)	(0.124)
Post	0.885***	1.009***	0.466***	0.544***
	(0.287)	(0.270)	(0.146)	(0.137)
Frequent	0.326	-0.910***	-0.001	-0.347*
	(0.371)	(0.333)	(0.199)	(0.189)
Retail clients		1.362***		0.650***
		(0.346)		(0.176)
Ln(Assets under management)		-0.473***		-0.207***
		(0.068)		(0.033)
Ln(Firm Age)		-0.602***		-0.315***
		(0.206)		(0.117)
Ln(Number of employees)		1.545***		0.453***
		(0.102)		(0.048)
Observations	6,292	6,292	6,292	6,292
Adjusted R^2	0.033	0.148	0.009	0.062
Year FE	X	X	X	X

Table A.6: How does M&A Discipline Employees? (Does acquirer misconduct matter?)

This table reports estimates from a linear probability model, predicting the probability that a registered investment advisor leaves their current job. The dependent variable is *Separation*, an indicator set equal to one if a representative that worked for the target or acquirer in year t no longer works there in year $t+1$. The *Separation* indicator is zero for target firm employees that move to the acquiring firm following the merger. The sample includes all registered representatives working either for the target or acquirer in the three years preceding the merger year and the regressions are run at the individual advisor-year level. We estimate the model for years -3 to +3 relative to the merger event at t=0. Panel A shows results for the target firm employees and Panel B shows results for acquiring firm employees. *Employee Disclosure (All)* is an indicator that equals one if the registered representative has any of the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), over the past two years (including the current year). *Employee misconduct (EMS)* is an indicator that equals one if the representative has any of the 6 categories of disciplinary events defined as misconduct in Egan, Matvos and Seru (2019). *Post* is an indicator that equals one for the year of the merger and the three years following the merger. Each merger year, we sort all acquirers on *Employee Disclosure (All)* measured in the year before the merger and define an indicator, *HDA* (high disclosures acquirer), that equals one if the acquirer has above median employee disclosures. Note that *HDA*×*Post* and *Post* are absorbed by target firm by year fixed effects, *Target Firm* × *Year FE*. We cluster standard errors, which we report in parentheses, by firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}$**(Separation)**$_{t+1}$				
	(1)	(2)	(3)	(4)
Employees disclosures (All) × Post × HDA	3.852	2.840		
	(5.173)	(5.260)		
Employees disclosures (EMS) × Post × HDA			-7.463	-8.470
			(8.203)	(8.030)
Employee misconduct (All) × Post	2.122	2.606	3.517	3.847
	(4.414)	(4.443)	(3.046)	(2.989)
Employee misconduct (EMS) × Post			16.818*	16.847**
			(8.791)	(8.568)
Employees disclosures (All) × HDA	-2.492	-1.889		
	(4.148)	(4.040)		
Employees misconduct (EMS) × HDA			2.199	2.979
			(7.294)	(7.072)
Employee misconduct (All)	9.185**	9.342**		
	(3.681)	(3.680)		
Employee misconduct (EMS)			7.092	7.269
			(5.771)	(5.678)
Ln(Experience)		-2.686***		-2.686***
		(0.298)		(0.297)
Ln(# Qualifications)		2.018***		2.023***
		(0.265)		(0.264)
Observations	100,027	100,027	100,027	100,027
Adjusted R^2	0.146	0.150	0.147	0.151
Target Firm × Year FE	X	X	X	X

Table A.7: Labor market outcomes following mergers

This table displays the average annual job turnover among financial advisers. Observations are at the adviser-by-year level. Leave the Industry is defined as an adviser not being registered as a financial adviser with any other advisory firm in subsequent years. If the adviser is employed by the acquirer following the merger, *Join a Different Firm* is zero. The job transitions are broken down by whether the adviser received a misconduct disclosure in the previous year.

Panel A: Target Firm Employees	No Misconduct		Misconduct	
	Pre	Post	Pre	Post
Remain with Firm	88%	83%	80%	70%
Leave Firm	12%	17%	20%	30%
Left Industry	31%	36%	34%	29%
Join a Different Firm	69%	64%	66%	71%
Panel B: Acquiring Firm Employees				
Remain with Firm	90%	91%	78%	79%
Leave Firm	10%	9%	22%	21%
Left Industry	42%	44%	40%	43%
Join a Different Firm	58%	56%	60%	57%

Table A.8: Employee separations when acquiring firm managers depart

This table presents estimates from a linear probability model predicting the likelihood that a registered investment advisor departs from their current position. The specification is identical to that in Table IX except we introduce *NM*, an indicator set equal to one if none of the acquiring firm's top managers or owners remain in their roles at the combined firm post-merger. The dependent variable is *Separation*, an indicator equal to one if a representative that worked for the acquirer in year t no longer works for the target, acquirer, or combined firm in year t + 1. The *Employee Disclosure (All)* indicator is one if the advisor has a disclosure in any of the 23 categories of disciplinary events from Egan, Matvos and Seru (2019) in the current year. The *Employee misconduct (EMS)* indicator is one if the advisor has a disclosure in any of the 6 categories of disciplinary events defined as misconduct in Egan, Matvos and Seru (2019). The *Post* indicator is one for the year of the merger and the three subsequent years. We cluster standard errors, which we report in parentheses, by firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	$\mathbb{1}$**(Separation)**$_{t+1}$			
	Acquirer Employees – Lost Old Managers			
	(1)	(2)	(3)	(4)
Employee misconduct (All) × Post × NM	-0.527	-0.598		
	(3.098)	(3.085)		
Employee misconduct (All) × Post × NM			3.753	3.789
			(7.109)	(7.043)
Employee misconduct (All) × Post	-0.648	-0.579		
	(0.433)	(0.461)		
Employee misconduct (EMS) × Post			-5.353***	-5.232***
			(1.171)	(1.142)
Employee misconduct (All) × NM	1.970	1.871		
	(2.830)	(2.722)		
Employee misconduct (All) × NM			-6.649	-6.837
			(6.449)	(6.347)
Employee misconduct (All)	12.434***	13.067***		
	(1.333)	(1.280)		
Employee misconduct (EMS)			31.572***	32.343***
			(3.608)	(3.529)
Ln(Experience)		-2.194***		-2.194***
		(0.193)		(0.191)
Ln(# Qualifications)		-0.809***		-0.822***
		(0.272)		(0.270)
Observations	1,829,089	1,829,089	1,829,089	1,829,089
Adjusted R^2	0.036	0.043	0.039	0.046
Acquiring Firm × Year FE	X	X	X	X

Table A.9: Is misconduct value-relevant in the investment advisory industry? Massachusetts 2016 regulatory inquiries

This table presents regression estimates of the relationship between advisory firms with Massachusetts employees and future assets under management (AUM) per employee. The sample includes all investment advisory firms that filed Form ADV from 2013 to 2018 and for which we have employee data from BrokerCheck or IAPD. The dependent variable is the log of assets under management per employee, $\text{Ln}(\frac{\text{AUM}}{\text{Employees}})_{t+1}$. *Treated* is an indicator for advisory firms that had at least one employee registered in Massachusetts prior to 2015. On June 6, 2016, the securities regulator in Massachusetts (RICE) sent notices to 241 broker-dealer firms registered in Massachusetts, each employing at least ten agents registered in Massachusetts who had a higher-than-average percentage of agents with at least one current misconduct disclosure (a "Disclosure Incident"), inquiring how these firms treat advisers with misconduct. The inquiries were widely publicized. The analysis assumes that this increased regulatory scrutiny lowered client expectations about future misconduct by employees of MA firms. Accordingly, we define *Post* as an indicator for the years 2016, 2017, and 2018. We cluster standard errors, which we report in parentheses, by advisory firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

	$\mathbf{Ln(\frac{AUM}{Employees})_{t+1}}$			
	(1)	(2)	(3)	(4)
Treated X Post	0.207***	0.118***	0.133***	0.142***
	(0.046)	(0.043)	(0.025)	(0.025)
Treated	0.144	0.268***		
	(0.091)	(0.085)		
Retail clients		-0.672***		-0.040***
		(0.029)		(0.009)
Ln(Firm Age)		0.414***		0.273***
		(0.014)		(0.022)
Ln(Number of employees)	-0.804***	-0.819***	-1.107***	-1.150***
	(0.025)	(0.024)	(0.022)	(0.022)
Observations	38634	38634	37655	37655
Adjusted R^2	0.200	0.291	0.949	0.950
Year FE	X	X	X	X
Firm FE			X	X

Table A.10: How does M&A discipline employees? (Sample of targets)

This table reports estimates from a linear probability model predicting the probability that a given advisor leaves their current job as a function of whether the advisor worked for the target in the three years before the acquisition. The dependent variable is *Separation*, an indicator equal to one if a representative that worked for the target in year t no longer works for the target, acquirer, or combined firm in years $t+1$, $t+2$, or $t+3$. The sample includes all advisers working either for the target or acquirer in the three years preceding the merger year. The regressions are run at the individual advisor-year level using data for years -3 to +3 relative to the merger event at t=0. *Employee Disclosure (All)* is an indicator that equals one if the adviser has a disclosure of any of the 23 categories of disciplinary events from Egan, Matvos and Seru (2019), over the current year and the previous two years. *Employee misconduct (EMS)* is an indicator that equals one if the adviser has a disclosure of any one of the 6 categories of disciplinary events defined as misconduct in Egan, Matvos and Seru (2019). *Post* is an indicator that equals one for the year of the merger and the three years following the merger. *Firm × Year FE* are target or acquiring firm by year fixed effects. We cluster standard errors, which we report in parentheses, by firm. $^{***}p < 0.01$ denotes significance at the 1% level, $^{**}p < 0.05$ denotes significance at the 5% level, and $^{*}p < 0.10$ denotes significance at the 10% level.

$\mathbb{1}$**(Separation)**$_{t+1,t+2,t+3}$				
Panel A	**Target Employees**			
	(1)	(2)	(3)	(4)
Employee misconduct (All) × Post	11.637***	10.750***		
	(3.736)	(3.367)		
Employee misconduct (EMS) × Post			24.624***	23.431***
			(3.606)	(3.366)
Employee misconduct (All)	2.629	5.002		
	(4.039)	(3.244)		
Employee misconduct (EMS)			-0.344	2.447
			(5.208)	(4.351)
Ln(Experience)		-1.863***		-1.844***
		(0.548)		(0.546)
Ln(# Qualifications)		-4.604***		-4.591***
		(1.052)		(1.049)
Observations	100,027	100,027	100,027	100,027
Adjusted R^2	0.198	0.209	0.198	0.209
Target Firm × Year FE	X	X	X	X