Local Gambling Preferences and Financial Advisor Misconduct

Yunzhe Zhu[‡], Harvey Nguyen[†], Mia Hang Pham[§], Jasmine Fang[‡]

Abstract

This paper examines whether local gambling preference culture influences financial advisor misconduct in the United States. Using a sample of more than 2.5 million advisor-year observations, we provide evidence that financial advisors and financial advisory firms operating in areas with high local gambling preferences are more likely to engage in misconduct. The results are significant at the individual and firm levels and remain robust after including firm and year fixed effects, financial advisor attributes, and regional control variables. The results are still consistent after adopting an instrumental variable approach and an alternative proxy for local gambling preferences. Our findings shed new light on local gambling preferences as an informal mechanism influencing unethical financial behaviors, offering valuable insights for practitioners and regulators.

Keywords: Financial advisor; financial misconduct; gambling attitudes; regional culture.

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[‡] School of Economics & Finance, Massey University, New Zealand, Email: y.zhu1@massey.ac.nz

[†] Massey Business School, Massey University, New Zealand, Email: h.nguyen3@massey.ac.nz

[§] School of Economics & Finance, Massey University, Email: m.h.pham@massey.ac.nz

[‡] School of Economics & Finance, Massey University, Email: j.fang@massey.ac.nz

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Abstract

This paper examines whether local gambling preference culture influences financial advisor misconduct in the United States. Using a sample of more than 2.5 million advisor-year observations, we provide evidence that financial advisors and financial advisory firms operating in areas with high local gambling preferences are more likely to engage in misconduct. The results are significant at the individual and firm levels and remain robust after including firm and year fixed effects, financial advisor attributes, and regional control variables. The results are still consistent after adopting an instrumental variable approach and an alternative proxy for local gambling preferences. Our findings shed new light on local gambling preferences as an informal mechanism influencing unethical financial behaviors, offering valuable insights for practitioners and regulators.

Keywords: Financial advisor; financial misconduct; gambling attitudes; regional culture.

1. Introduction

The financial advisory industry is economically and socially significant, with 64 million Americans seeking guidance from Registered Investment Advisors (RIAs), who manage 70% of household and nonprofit organization finances (Charoenwong, Kwan, & Umar, 2019; Linnainmaa, Melzer, & Previtero, 2021). According to the report[1] from the investment advisory industry, more than 600,000 clients in the U.S. turned to professionals for asset management planning and financial services, and financial advisors managed more than $10 trillion in assets in 2022. While financial advisors play a crucial role in the economy, the entire advisory industry suffers severe fraud and financial misconduct. The frequent occurrence of such misconduct can result in severe consequences, including damaging the household financial conditions, decreasing investment efficiency, and weakening financial stability in the long run. Even if regulatory authorities work together to curb misconduct, investors suffer severe losses due to unethical behaviors by financial advisors (Egan, Matvos, & Seru, 2019). Given this background, the determinants influencing unethical behaviors within the industry are attracting increasing attention from academia, the financial advisory sector and regulators (Szwajkowski, 1992; Bennett, Pierce, Snyder, & Toffel, 2013; Karpoff, Lee, & Martin, 2017; Amiram, Bozanic, Cox, Dupont, Karpoff, & Sloan, 2018).

The significance of culture on individual behaviors and corporate decisions has been widely studied in recent literature (Kumar, Page, & Spalt, 2011; Callen & Fang, 2015; Liu, 2016). One widely accepted concept proposed by Tylor (1871) defines culture as a complex whole containing knowledge, beliefs, art, morality, law, tradition, and all other capabilities and habits acquired by individuals within society, which represents the shared values of a specific

[1] The report is available at: https://www.mckinsey.com/industries/financial-services/our-insights/the-great-reset-north-american-asset-management-in-2022

group rather than individual characteristics (Boyd & Richerson, 1988; Schwartz, 2014). Firms and their employees interact with local customers, and the firms' management is inevitably influenced by the local environment and gradually conforms to local values and beliefs.

Recognizing the influence of culture on corporate operations, this study examines how local gambling preferences influence misconduct by financial advisors and financial advisory firms in the U.S. financial advisory sector. Current literature provides numerous determinants that influence financial advisor misconduct, such as the work and regulatory environment (Dimmock, Gerken, & Graham, 2018; Charoenwong et al., 2019), geographical characteristics (Parsons, Sulaeman, & Titman, 2018), negative real estate shocks (Dimmock, Gerken, & Van Alfen, 2021), social capital (Bai, Shang, Wan, & Zhao, 2021), and local competition and firm market power (Gelman, Khan, Shoham, & Tarba, 2021). However, the impact of local gambling culture on individual and firm misconduct behaviors is not yet clear. Inspired by an increasing number of studies on the effect of local gambling preferences on risk-taking tendencies, this paper aims to explore the association between local gambling preferences and financial advisor misconduct, filling a gap in the current research field.

The potential association between local gambling preferences and financial advisor misconduct is built on several compelling economic reasons. First, local gambling preferences are crucial in explaining people's willingness to take risks. Gambling preferences are characterized by opportunism, which encourages employees to become unthinkingly optimistic and take more risks, thus increasing the aggregate firm risk tolerance level (Chen, Podolski, Rhee, & Veeraraghavan, 2014). Second, gambling is considered an activity with a higher value reward in return, so gamblers regard gambling as a method of paying debts or solving financial difficulties. Individuals in this situation are not concerned about the future reputational damage and potential penalties associated with misbehaviors (Ursua & Uribelarrea, 1998). Therefore,

we speculate that financial advisors and financial advisory firms tend to be more likely to engage in misconduct when they are in areas with higher gambling acceptance.

We construct a proxy of financial advisor misconduct using a comprehensive sample of 2.2 million advisor-year observations and 238,774 firm-year observations from 2007 to 2015. We observe a comprehensive series of disclosure records, including customer disputes, disciplinary events and other financial issues involving each advisor. These records are classified into 23 different disclosure categories by the Financial Industry Regulatory Authority (FINRA). Since disclosures do not always imply misconduct, following Egan et al. (2019), we define misconduct as 6 out of 23 types of disclosures in this study: Customer Dispute–Settled, Regulatory–Final, Employment Separation after Allegations, Customer Dispute–Award/Judgment, Criminal–Final Disposition, and Civil–Final.

Commencing with the sample of advisors with disclosed misconduct, we estimate linear probability models at the individual and firm levels. Our main outcome variables are individual misconduct (*Ind_misconduct*) and firm misconduct (*Firm_misconduct*) each year, measured with a dummy variable representing whether financial advisor misconduct is disclosed and a variable representing the total amount of advisor misconduct in a firm, respectively. Our two main explanatory variables representing local gambling preferences are the binary variable *HighLottery* and the continuous variable *LotteryPerCapita*. We control for the individual-level and firm-level financial advisor characteristics and state-level control variables in our models to exclude the potential effects of these factors on local gambling preferences (Dimmock et al., 2018; Egan et al., 2019). We also include the firm-level and year-level fixed effects and standard errors are clustered by firm and year.

Our findings indicate that financial advisors and financial advisory firms operated in regions with higher local gambling preferences exhibit an increased propensity to engage in

misconduct. The significant influence shows that local gambling preference culture is a vital determinant of financial advisors' wrongdoings. We also adopt additional approaches to test the robustness of our findings. First, we reinforce a causal relationship between local gambling preferences and financial advisor misconduct by examining the instrumental variable approach to reduce potential endogeneity issues. We use the total natural climate disaster losses (*Disaster_Loss*) at the state level as an instrument variable for local gambling preferences and the results are consistent with the baseline regressions. Next, we employ an alternative gambling preference proxy to reduce the potential influence of specific variables. After accounting for all control variables and firm and year fixed effects, we obtain the same results, further confirming our main findings. In addition, we also explore the effects of the 2008 financial crisis and regional education attainment. We find that the positive effect of local gambling preferences on unethical behavior is attenuated when financial advisors face unexpected financial stress and are in areas with higher education levels.

This study contributes to the literature by expanding on the existing research on financial advisors' misconduct and corporate fraud, providing new insights into the driving forces and consequences of such behavior. Previous studies have explored market-level externalities influencing misconduct, such as adverse personal financial outcomes from real estate price fluctuations (Dimmock et al., 2021), social capital (Dong, Han, Ke, & Chan, 2018; Bai et al., 2021), and county-level market power and competition (Gelman et al., 2021). Other research has focused on individual and firm-level determinants, highlighting factors like utility maximization (Law & Zuo, 2021) and gender disparities in penalties (Egan, Matvos, & Seru, 2022). The influence of colleagues and corporate supervisors has also been examined (Dimmock et al., 2018; Kowaleski, Sutherland, & Vetter, 2021). Our study introduces novel evidence by demonstrating that local gambling preference culture, as a dimension of informal institutions, can significantly influence unethical behavior in individuals and firms.

Additionally, our research supplements the literature on the impact of local gambling preferences on financial decision-making. Prior studies have shown how gambling attitudes affect investors' portfolio choices (Kumar et al., 2011) and encourage firms to engage in riskier activities (Chen et al., 2014; Alharbi, Atawnah, Mamun, & Ali, 2022). However, there is limited research linking gambling culture to the financial advisory industry. Our empirical findings provide fresh evidence that local gambling preferences can influence the misconduct behaviors of financial advisors and financial advisory firms, aligning with insights from gambling psychology literature (Yeoman & Griffiths, 1996; Gupta & Derevensky, 1998).

The rest of the paper is organized as follows. Section 2 presents the related literature and hypothesis. Section 3 describes the data collection, sample selection, variable construction, and descriptive statistics. Section 4 discusses the results of baseline models and several robustness tests. Section 5 reports additional analyses and Section 6 concludes the paper.

2. Literature review and hypothesis development

North (1990) argues that culture is a community of shared ideologies and standard rules to which all people subscribe. Culture is a collection of beliefs, values, and social norms, referring to the rules and standards understood by group members (Hofstede, 2001). Specifically, this framework significantly shapes not only self-identity (Scott, 1987) but also the decision-making processes and utility considerations in financial choices at the individual and organizational levels (Williamson, 2000; Grinblatt & Keloharju, 2001; Stulz & Williamson, 2003; Guiso et al., 2006; Aggarwal, Faccio, Guedhami, & Kwok, 2016). Overall, culture plays a significant role in influencing the individual and firm decision-making process.

Gambling culture has received widespread attention in emerging studies (Kumar et al., 2011; Kumar, Page, & Spalt, 2016). At the individual level, gambling culture shapes cognitive biases and behaviors (Tang & Wu, 2012) as well as alters risk perceptions (Spurrier & Blaszczynski, 2014). In areas with a strong gambling culture, individuals tend to exhibit a greater tolerance for risks, leading to more aggressive business and investment choices. Specifically, Kumar et al. (2011) find that in areas with higher proportions of Catholic and Protestant gambling tolerance, investors display a positive tendency to hold lottery characteristic stocks, while their further research finds that investors driven by gambling motivations generate excess returns through trading in stocks with lottery characteristics (Kumar et al., 2016). Byun and Kim (2016) find that investors are willing to pay premiums for individual stock options resembling lotteries, while Doukas and Zhang (2013) document that managers who prefer gambling-like targets exhibit higher price premiums and target announcement returns. Moreover, studies indicate that people influenced by gambling culture tend to participate in risk-taking activities (Christensen, Jones, & Kenchington, 2018; Callen & Fang, 2020), exhibit excessive optimism about uncertainty (Spurrier, Blaszczynski, & Rhodes, 2015) and ignore long-term consequences (Marcus, 2003).

Concerning firms, extensive literature illustrates that in areas where gambling culture is more socially acceptable, firms will be more likely to undertake speculative activities and decisions, including embarking on riskier innovation projects (Chen et al., 2014; Adhikari & Agrawal, 2016), resulting in financial misreporting (Christensen et al., 2018), resulting in higher levels of audit fees (Callen & Fang, 2020), obtaining higher price premiums in acquisition process (Schneider & Spalt, 2011; Doukas & Zhang, 2013), and adopting aggressive tax avoidance strategies (Alharbi et al., 2022; Lei, Qiu, Yu, & Zuo, 2023). Similarly, Ji, Quan, Yin and Yuan (2021) prove empirical evidence that firms located in regions with stronger gambling preferences are more exposed to greater stock price crash risk, while Qian

and Wu (2021) show that local gambling preferences significantly increase the propensity of banks to engage in risk-taking activities. Collectively, local gambling culture is essential in shaping individual beliefs and influencing organizational decision-making processes.

Although the significance of financial advisors in the financial market is undeniable, empirical studies have shown that financial advisors are considered dishonest (Guiso et al., 2008; Zingales, 2015; Gurun, Stoffman, & Yonker, 2018; Dimmock et al., 2018; Egan et al., 2019). Their wrongdoing can lead to investors losing trust (Guiso et al., 2008), reducing market participation (Giannetti & Wang, 2016; Gurun et al., 2018) and ultimately damaging economic development (Bergstresser, Chalmers, & Tufano, 2008; Hackethal, Haliassos, & Jappelli, 2012; Mullainathan, Noeth, & Schoar, 2012; Dimmock et al., 2018; Chalmers & Reuter, 2020). Prior literature emphasizes that financial advisor misconduct behaviors are widespread and more severe in the financial sector than in any other sector of the economy (Kowaleski, Sutherland, & Vetter, 2020). Egan et al. (2019) also state that more than seven percent of advisors have misconduct records. Current studies have examined various external market-level determinants of financial advisors' misconduct that will constrain or motivate misconduct. Specifically, Dong et al. (2018) and Bai et al. (2021) show that social capital has a deterrent effect on financial advisor misconduct behaviors, while Gelman et al. (2021) demonstrate that firms with more substantial local market power and market competition are less likely to become involved in misconduct. Different from the external constraints, Dimmock et al. (2021) argue that negative housing price shocks are driving forces of financial advisor misconduct, while Parsons et al. (2018) document that regional heterogeneity, especially city-level social norms such as political corruption or spousal infidelity will increase the likelihood of financial misconduct. Also, changes in the external regulatory environment can increase financial advisor misconduct. Charoenwong et al. (2019) find that the probability of misconduct rises for mid-sized

investment advisory firms compared to other groups after the Dodd-Frank Act shifted regulatory jurisdiction over these firms from the SEC to state regulators.

In addition to these external market determinants mentioned above, existing literature also focuses on individual and intra-firm characteristic determinants that influence misconduct. Specifically, at the individual level, Egan et al. (2019) show that advisors with a past record of misconduct are more likely to engage in misconduct, and their further research demonstrates that female advisors are 20% more likely to lose their jobs than male advisors with similar undesirable activities and 30% less likely to find a new job (Egan et al., 2022). Kowaleski et al. (2020) document that investment advisors who receive comprehensive training in rules and ethics are less inclined to engage in misconduct. Additionally, Law and Zuo (2022) establish that minority advisors experience a higher likelihood of receiving complaints during periods of increased public attention to immigration issues, while Law and Zuo (2021) show an association between an advisor's probability of misconduct and their early career economic conditions. Additionally, at the firm level, Dimmock et al. (2018) find that individual's propensity to commit misconduct behaviors is impacted by their coworker behaviors, while Kowaleski et al. (2021) conclude that individual supervisors are twice as influential as firm-level factors in interpreting employee misconduct in firms.

Inspired by relevant determinants of financial advisor misconduct and local culture literature, this paper aims to explore the potential impact of such local gambling culture on the probability of misconduct among financial advisors. This study is built on several convincing theories. Figure 1 presents the frameworks between local gambling preferences and financial advisor misconduct. Specifically, imprinting theory emphasizes that the cognition and value preferences of individuals or organizations are primarily shaped by their growth environment and cultural soil (Marquis & Tilcsik, 2013). These cultural and environmental factors will form

a distinct “imprint” and continue to affect their subsequent economic practices. The concept of imprinting theory provides an important perspective for understanding how the surrounding environment of past life affects current behaviors. In addition, relevant sociological theories play a significant role in explaining individual behavior choices. Specifically, social cognitive theory emphasizes that human learning and behavior are largely influenced by the social environment, including the reactions and recognition of others (Bandura, 1986; Festré, 2010). This theory holds that cognitive processes are indispensable, in which individuals can observe others and the environment, reflect on their thoughts and behaviors, and correspondingly change their self-regulation function (Dweck & Leggett, 1988). Thus, it is predictable that individuals living in areas with high gambling preferences are influenced by the environment and shared values of the region. Therefore, financial advisors working in these areas will exhibit more adventurous tendencies, such as a higher probability of engaging in misconduct. These theories reveal that local gambling preferences can change employees' risk perceptions and preferences and further impact aggregate firm decisions.

The fraud triangle theory explains that the triggers for individuals to commit misconduct stem from motivation, opportunity and rationalization. When the potential benefits outweigh the potential risks, the likelihood of misbehavior increases (Cressey, 1953). local gambling preferences can increase individuals’ optimism regarding uncertainties (Spurrier et al., 2015) and thus amplify their tolerance for high risk. Motivated by the risk-taking culture, those opportunistic individuals are more likely to risk investor wealth in pursuit of high potential gains (Christensen et al., 2018) and make risk-taking decisions, such as investment in risky projects (Chen et al., 2014) and more tax avoidance activities (Alharbi et al., 2022). Another characteristic associated with local gambling preferences is the tendency of individuals to ignore the legal consequences of their behaviors, as they perceive their subjective misconduct as reasonable. As noted by Meyer and Stadler (1999), we infer that financial

advisors and firms in areas with high gambling preferences prefer risk-taking and rationalize engaging in misconduct due to unconcerned about legal and reputational consequences.

Therefore, based on the above arguments, we derive the hypothesis as follows:

Hypothesis: *Financial advisors and financial advisory firms operated in regions with higher gambling preferences are more likely to commit misconduct.*

[Insert **Figure 1** here]

3. Data and methodology

In this section, we illustrate the data construction process, describe the definitions of the key variables, and explain the empirical methodology employed in this study.

3.1 Data selection

To test our hypotheses, we require data on financial advisor misconduct, local gambling preferences, relevant financial advisor attributes and state-level demographic characteristics. We construct our misconduct sample by collecting financial advisor disclosure information from the FINRA BrokerCheck database (Egan et al., 2019). This public dataset also contains the detailed characteristics of each registered financial advisor. We collect state lottery data and state-level regional demographic data from the U.S. Census Bureau, while the religious data is obtained from the Association of Religion Data Archives (ARDA). After merging the financial advisor misconduct and state-level lottery sales records dataset, our study sample finally includes over 2.5 million advisor-year observations and 459,758 unique advisors.

3.2 Dependent variable – Financial advisor misconduct

We use a panel of financial advisor data in the United States from 2007 to 2015. The dataset includes publicly available data from the Financial Industry Regulatory Authority's (FINRA) BrokerCheck database, which includes detailed data related to each investment advisor's complete employment history. FINRA is the largest self-regulatory organization authorized by the U.S. Congress to guarantee the fair and ethical operation of the securities industry. Our study covers information on more than 400,000 registered and licensed investment advisors. Specifically, this information includes the advisors' full names and Central Registration Depository (CRD) identifiers, their employers (each firm has an Investment Adviser Registration Depository (IARD) identification number), tenures in their firms, the place of employment (city and state), qualifications and disclosed information. Financial advisors in this research are individuals who have been registered with FINRA, and each advisor has a unique CRD number that remains constant throughout the financial advisor's work history.

Following Egan et al. (2019), we employ this methodology to categorize financial advisor misconduct and construct the measures based on disclosure records. FINRA classifies disclosure incidents into 23 categories, from criminal offenses to customer disputes. Since disclosures do not always imply misconduct, our definition of misconduct is consistent with Egan et al. (2019), which includes criminal, regulatory, and internal investigations, and customer events that were resolved against the advisor. Specifically, our study focuses on 6 of the 23 categories: Customer Dispute–Settled, Regulatory–Final, Employment Separation after Allegations, Customer Dispute–Award/Judgment, Criminal–Final Disposition, and Civil–Final.

This research focuses on the association between local culture and financial advisor misconduct, and thus, we employ two main outcome variables to measure misconduct behavior at the individual level and the firm level within each state. At the individual level, we use a binary variable *"Ind_Misconduct*" to measure the occurrence of misconduct. This variable indicates whether a financial advisor receives any misconduct-related disclosures in a given year. According to our definition of financial advisor misconduct, an advisor with multiple misconduct disclosures in the same year is considered to have committed one instance of misconduct. Therefore, the dummy variable (*Ind_Misconduct*) takes the value of one if the advisor has misconduct in a year and zero otherwise. At the firm level, the dependent variable we examine is *Firm_misconduct*, computed from the cumulative number of advisor misconduct cases in a firm in a given year.

3.3 Independent variable – local gambling preferences

To measure the local gambling preferences, based on previous literature (Kumar et al., 2011; Kumar et al., 2016; Christensen et al., 2018), we employ two measurements to capture actual gambling activity using state-level data on per capita lottery expenditures. We expect that lottery sales records can reflect the local residents' acceptance and preference for gambling. More specifically, we use a dichotomous measure, *HighLottery*, that equals one when per capita residents' lottery expenditure in a state where the firm is operated is higher than the sample median and zero otherwise. In our sample, *LotteryPerCapita* is a continuous measure, calculated as the standardizing form of the total lottery expenditures in a state where the firm is operated in year *t* divided by the state's total population in the same year. We take the standardizing form to eliminate the outliers in all specifications. The superiority of the gambling preference measurements in our research is as follows. The two measurements based on state lottery sales are derived from actual gambling activities and are more observable and

accessible than other gambling classifications such as casino activities, horse racing and dog racing. (Christensen et al., 2018).

3.4 Financial advisor characteristic control variables

We consider several individual financial advisors' characteristics that have been demonstrated to influence misconduct. These attributes include gender, professional experience, and three specific certifications: Series 63, Series 65, and Series 66 (Egan et al., 2019; Egan et al., 2022; Bai et al., 2021). Specifically, as followed by prior research (Egan et al., 2019), we consider gender (*Male*) as a dummy variable to capture whether an advisor is male. In addition, we create an *Experience* variable, which represents the number of years of professional experience (*Experience*). Finally, we consider three important professional licenses: the Uniform Securities Agent State Law license (*Series_63*), which qualifies candidates as security agents; the Uniform Investment Adviser Law license (*Series_65*), which qualifies candidates as investment advisors; and the Uniform Combined Law license (*Series_66*), which qualifies candidates as both securities agents and investment advisors. They are dummy variables equal to one if a financial advisor has passed the respective qualification examinations, and zero otherwise. Detailed variable definitions can be found in the Appendix.

3.5 Firm characteristic control variables

To better explore the association between local gambling preferences and the misconduct of financial advisory firms, we create the firm-level characteristic control variables by aggregating each financial advisor's characteristics in each firm. In particular, we compute the proportion of male advisors within a firm (*Average_Male*), the average years of experience among all advisors (*Average_Experience*) within a firm in a given year, and the proportion of advisors with three professional certifications of Series 63, Series 65, and Series 66 (*Average_Series_63, Average_Series_65 and Average_Series_66*) in each firm in a given year.

Additionally, we also consider the number of advisors (*Number*) in a firm as a control variable, as behaviors among coworkers can be contagious (Dimmock et al., 2018).

3.6 State-level control variables

We also consider several demographic characteristics measured at the state level in our models. Firstly, following previous research (Kumar et al., 2011; Chen et al., 2014), we control the population of a state in our models and take the natural logarithms of the population in that state. Secondly, according to Egan et al. (2019), we consider the logarithm of median household income within a state. We take the log of population and median household income to reduce data variability. We take these two factors into account as they are directly related to people's willingness to gamble and adventure activities. Next, we account for the level of religiosity of the state in our models. Prior empirical research indicates that the prevalence of state lotteries in a particular area is influenced by the prevailing local religious beliefs (Berry & Berry, 1990; Martin & Yandle, 1990; Ellison & Nybroten, 1999). Therefore, we include the religious factor (*Religiosity*), which is captured by the number of adherents divided by the population in a state, consistent with Christensen et al. (2018). Finally, we contain the minority group ratio (*Nonwhite*), which refers to the proportion of nonwhite residents in a state. Previous studies have shown a link between race and financial misconduct (McDonald et al., 2018; Law & Zuo, 2022). Controlling for these demographic factors helps ensure we are measuring local gambling preferences specifically rather than other potentially underlying constructs, as noted in studies by Kumar (2009) and Christensen et al. (2018).

3.7 Descriptive statistics

We present the descriptive statistics for the key variables in our analysis in Table 1. Our sample covers approximately 2.5 million advisor-year observations and 238,774 firm-year observations from 2007 to 2015, covering 459,758 unique advisors. Specifically, the mean

value of *HighLottery* is 0.538, implying that more than half of the financial advisors and advisory firms operate in regions with high social acceptance of gambling, consistent with those reported by Christensen et al. (2018). The mean value of *Ind_Misconduct* is 0.009, suggesting that approximately 1% of financial advisors have misconduct records – it echoes the importance of studying misconduct determinants. All other descriptive statistics are also generally in line with the prior literature (Kumar *et al.*, 2011; Chen et al., 2014; Egan et al., 2019; Gelman et al., 2021).

[Insert **Table 1** here]

4. Models and results

4.1 Baseline models and results

In this subsection, to identify the association between local gambling preferences and financial advisor misconduct, following Egan et al. (2019), we adopt the linear probability baseline models at both individual and firm levels. The dependent variables are *Ind_misconduct* and *Firm_misconduct*, respectively, while the independent variables are *HighLottery* and *LotteryPerCapita*, which represent local gambling preferences. The baseline models include a number of control variables to capture the characteristics of the financial advisors at the individual level and the firm level, as well as state-level demographic characteristics to exclude the potential impacts of these factors. We also consider the firm-fixed effects and year-fixed effects to control for the unobserved time-invariant factors and firm-invariant factors in a given year. Standard errors are clustered by firm and year to solve serial correlation in the residuals. Our baseline regression models are as follows:

Individual level analysis:

$$Ind\_Misconduct_{i,s,t} = \alpha_0 + \alpha_1 Gamble_{s,t} + \alpha_2 Advisor\ Characteristics_{i,s,t} + \alpha_3 State\ Attributes_{s,t} + Firm\ FE + Year\ FE + \varepsilon_{i,s,t} \quad (1)$$

Firm level analysis:

$$Firm\_Misconduct_{f,s,t} = \beta_0 + \beta_1 Gamble_{s,t} + \beta_2 Firm\ Characteristics_{f,s,t} + \beta_3 State\ Attributes_{s,t} + Firm\ FE + Year\ FE + \varepsilon_{f,s,t} \quad (2)$$

Where *i* is the financial advisor, *f* is the firm, *s* represents the state, and *t* is the year. $Ind\_Misconduct_t$ is a dummy variable which equals one if the financial advisor *i* engaged in financial misconduct during year *t*. $Firm\_Misconduct_t$ refers to the sum of the financial advisor misconduct in firm f during year *t* $Gamble_{s,t}$ represents the two variables (*HighLottery and LotteryPerCapita*) we use to measure local gambling preferences of the financial advisor *i* and firm *f* in state *s* in year *t*. $Gamble_{s,t}$ represents the two variables (*HighLottery and LotteryPerCapita*) we use to measure local gambling preferences of the financial advisor *i* and firm *f* in state *s* in year *t*. $Advisor\ Characteristics_{i,t}$ and $Firm\ Characteristics_{f,t}$ represent financial advisor characteristics at the individual and firm levels in state *s* in year *t*, respectively. $State\ Attributes_{s,t}$ refers to the specific demographic characteristics in state *s* during year *t*. $Firm\ FE$ and $Year\ FE$ refer to the firm fixed effects and year fixed effects, respectively. $\varepsilon_{i,t}$ and $\varepsilon_{f,t}$ are the error terms. The sample period is from 2007 to 2015.

Table 2 reports the individual-level (Panel A) and firm-level (Panel B) baseline regressions. *HighLottery* and *LotteryPerCapita* are the key explanatory variables to predict the likelihood of financial advisor misconduct. Specifically, the dependent variable in columns (1) and (2) is *HighLottery* and in columns (3) and (4), it is *LotteryPerCapita*. Columns (1) and (3) include the firm and year fixed effects, while columns (2) and (4) include the firm×year fixed effects. The coefficient estimates for *HighLottery* and *LotteryPerCapita* are positive and statistically significant at the 1% level in explaining both the advisor and firm misconducts, which is consistent with our hypotheses. This positive relationship between local gambling preferences and financial advisor misconduct is also economically significant. Using *LotteryPerCapita* as an example, the estimated coefficient as shown in column (3) of Panel A is 0.0005, implying one standard deviation increase in *LotteryPerCapita* value in column (3) of Panel A is associated with a 5.56% (i.e., 5.56% = 0.0005 x 1/ 0.009) increase in the likelihood of advisor-level misconduct.

Regarding the control variables, the findings are mostly consistent with previous research (Egan et al., 2019; Egan et al., 2022). Specifically, male financial advisors and those with more professional experience are more likely to commit misconduct. It is noteworthy that regional religiosity mitigates the probability of financial advisors engaging in misconduct, as with the argument that the level of religiosity is positively associated with risk aversion (Chen et al., 2014).

The results contribute novel perspectives on the determining factors that influence disciplinary incidents in the financial advisory industry. After accounting for the fixed effects at the firm and year levels as well as a series of control variables, this study demonstrates that the influence of regional gambling preference remains robust regardless of the firm's internal

characteristics (Dimmock et al., 2018; Egan et al., 2019) and state geographical attributes (Kumar et al., 2011).

[Insert **Table 2** here]

4.2 Instrumental variable approach

To reduce the potential endogeneity issues, we further adopt a two-stage-least-square (2SLS) instrumental variable approach in this section. We use the total natural climate disaster losses (Disaster_Loss) at the state level as an instrumental variable for measuring local gambling preferences (Fan & He, 2023). We hypothesize that the negative economic and livelihood impacts and panic of extreme adverse events on individuals and communities can lead people to focus more on basic survival requirements than on pursuing recreational activities such as gambling. Previous research demonstrates that exposure to significant events such as natural disasters is associated with gambling activities (Scherrer, Xian, Kapp, Waterman, Shah, Volberg, & Eisen, 2007). In addition, there is no direct link between natural events and financial misconduct records. Our instrumental variable, therefore, satisfies the exclusion and relevance conditions according to Roberts and Whited (2013).

Specifically, we collect the data from the Spatial Hazards Events and Losses Database (SHELDUS) and mainly focus on the property and crop losses due to natural climate disasters. By aggregating annual county-level data to the state level, we obtain the instrumental variable, represented by the logarithm of total natural disaster losses. Previous research demonstrates that losses from natural climate disasters are correlated with local gambling preferences and there is no clear evidence of an association between financial advisor misconduct and natural

disaster losses. We apply the total natural climate disaster losses (Disaster_Loss) as the instrumental variable in our 2SLS analyses. We estimate the 2SLS regressions as follows:

$$Predicted\ Gamble_{s,t} = \alpha_0 + \alpha_1 Disaster\_Loss_{s,t} + \alpha_2 Advisor\ (Firm)\ Characteristics_{i(f),s,t} + \alpha_3 State\ Attributes_{s,t} + Firm\ FE + Year\ FE + \varepsilon_{i(f),s,t} \quad (3)$$

$$Misconduct_{i(f),s,t} = \alpha_0 + \alpha_1 Predicted\ Gamble_{s,t} + \alpha_2 Advisor\ (Firm)\ Characteristics_{i(f),s,t} + \alpha_3 State\ Attributes_{s,t} + Firm\ FE + Year\ FE + \varepsilon_{i(f),s,t} \quad (4)$$

Where $Predicted\ Gamble$ is the predicted value of local gambling preferences in state *s* in year *t*; $Disaster\_Loss$ refers to the natural climate disaster losses in state *s* during year *t*; $Advisor\ (Firm)\ Characteristics_{i(f),t}$ and $State\ Attributes_{s,t}$ represent the advisor or firm level and the state level control variables in state *s* during year *t*; $Firm\ FE$ and $Year\ FE$ refer to the firm and year fixed effects. $\varepsilon_{i,t}$ and $\varepsilon_{f,t}$ represents the error terms.

Table 3 presents the results of the instrumental variable approach at the individual level (Panel A) and the firm level (Panel B). Consistent with Fan and He (2023), the first-stage regression results in columns (1) and (3) reveal a negative association between total losses from natural climate disasters and local gambling preferences at individual and firm levels. Further, the F-statistics results from a Kleibergen-Paap weak identification test are 70.66 and 125.59 for the individual-level analysis and 65.30 and 120.14 for the firm-level analysis, respectively, which rejects the null that *Disaster_Loss* is weak instruments. In the second stage, we use the predicted value of two regional gambling measures generated from the first stage to estimate the likelihood of financial advisors and financial advisory firms engaging in misconduct. The results indicate that after controlling for potential endogeneity, local gambling preferences are

positively correlated with financial advisor misconduct. These results corroborate our hypothesis and underscore the significance of regional cultural factors in shaping financial advisor misconduct.

[Insert **Table 3** here]

4.3 Gambling preferences alternative measure

To mitigate potential biases associated with the gambling preference measures, we examine an alternative measure of local gambling preferences instead of *HighLottery* and *LotteryPerCapita*. Consistent with Adhikari and Agrawal (2016), we collect data on the current legal status of six gambling categories (charitable, pari-mutuel, state lottery, commercial, tribal, and racetrack) in all 50 states of the United States. We construct an index of a state's gambling culture, *Gambling_Index*, by calculating the four types of pari-mutuel, commercial, tribal and racetrack gambling allowed in that state. We exclude charitable gambling and state lottery, as the purpose of charitable gambling is to raise funds for charitable organizations instead of personal profit. Almost all firms operate in states where the lottery is currently legal, so that indicator has no variation. If these four gambling categories are legal in a state, they each score as 1; otherwise, they score as 0. *Gambling_Index* takes a value of 0 to 4 for a state and is time-invariant. We do not consider this gambling index in our baseline regressions because it has limited variation (0 to 4) and is time-invariant, while the *HighLottery* and *LotteryPerCapita* are the dummy variable and continuous variable, respectively, and the state-level per capita lottery spending data constitutes these two variables vary over time. We replace the original gambling indicators with *Gambling_Index* and regress our baseline models.

The outcomes are shown in Table 4 at the individual level (Panel A) and the firm level (Panel B). Specifically, the coefficients of *Gambling_Index* at the individual level are 0.0003 with the firm and year fixed effects and firm×year fixed effects, respectively, while the coefficients of Gambling_*Index* at the firm level are 0.0068 and 0.0085, respectively. All coefficient estimates of our alternative measure are positive and significant at the 1% level. We find that the outcomes are consistent with the baseline regression results. The estimated coefficient results of the control variables for financial advisor characteristics and state-level demographic attributes remain consistent with our baseline regression analyses. The results further emphasize that our conclusion is unaffected by specific variable selection; that is, financial advisors and firms operating in states with high gambling preferences are at a higher likelihood of participating in unethical behaviors.

[Insert **Table 4** here]

5. Further tests

5.1 Effect of the 2008 financial crisis on financial advisor misconduct

The current results display that local gambling preferences increase the likelihood of financial advisor misconduct. To expand our inquiry, we further examine how the effect of local gambling preferences on misconduct changes when financial advisors face external financial pressures. Specifically, previous research suggests that financial crisis reduces people's risk tolerance and long-term risk-taking behaviors (Law & Zuo, 2021). Building on their insights, we expect that as financial market unpredictability increases and awareness of job loss concerns

grows, financial advisors tend to adopt more conservative and risk-averse behaviors. Therefore, the incentive role of gambling preferences may be moderated during this period.

As such, we adopt a dummy variable *Crisis* which equals one for the years 2008 and 2009, and zero otherwise, and interact with *HighLottery* to examine whether gambling preferences play a different role during the financial crisis period. The interactive coefficients are negative and statistically significant, as reported in Panel A and Panel B of Table 4. The results demonstrate that the incentive impact of gambling culture on financial advisor misconduct is weakened by the 2008 financial crisis.

[Insert **Table 5** here]

5.2 Effect of education on financial advisor misconduct

In this section, we further explore the role of regional differences in educational levels in the impact of gambling preferences on financial advisor misconduct. Prior research shows that low levels of education are associated with gambling as gambling activities provide a chance to mitigate low-income status (Kumar et al., 2009; Haisley, Mostafa, & Loewenstiein, 2008). Following this reasoning, we expect that the influence of gambling preferences on financial advisor misconduct can be attenuated in areas with higher educational attainment.

To empirically test this argument, we obtain the education data from the Integrated Public Use Microdata Series (IPUMS) USA database. The education data have values between

0 and 11[2]. Following Call et al. (2017), the education variable (*Education*) is the weighted average education level of surveyed respondents in a given state. The coefficient estimates of the interaction between *HighLottery* and *Education* in column (4) of Table 4 are negative and statistically significant, which is consistent with our expectations. The results indicate that higher education levels reduce gambling addiction, thus moderating the impact of gambling preferences on financial advisors' and financial advisory firms' misconduct in the region.

[Insert **Table 6** here]

6. Conclusion

Theories related to local culture suggest that individual behaviors are influenced by the regional surrounding environment, where individuals in society observe the behavior of others and internalize the values of their social group (Bandura, 1986; Marquis & Tilcsik, 2013). When gambling preference culture is becoming prevalent and socially acceptable in that area, it will reshape individual choices and firm decision-making. In this paper, we explore the influences of local gambling preferences culture on financial advisor misconduct at individual and firm levels. We find strong empirical evidence that financial advisors and firms operated in higher gambling preference regions are associated with a significantly higher likelihood of misconduct behaviors.

We employ state-level per capita lottery spending to demonstrate the significantly positive association between local gambling preferences and financial advisor misconduct

[2] The classification of respondents' education attainment from 0 to 11 is as follows: 0 = no schooling; 1 = nursery school to grade 4; 2 = grade 5,6,7,8; 3 = grade 9; 4 grade 10; 5 = grade 11; 6 = grade 12; 7 = 1 year of college; 8 = 2 years of college; 9 = 3 years of college; 10 = 4 years of college; and 11 = 5 years of college.

behaviors. The results, which are significant after controlling for financial advisor characteristics, regional demographic attributes as well as firm and year fixed effects, are still robust to a wide variety of empirical tests such as an alternative proxy of local gambling preferences and several additional tests. This finding remains compelling after using the instrumental variable approach to address endogeneity issues. The results indicate that local culture, especially local gambling preferences, is a crucial determinant of unethical behaviors among individuals and firms. In addition, we conclude that the influence of gambling culture on misconduct is weakened when financial advisors face more significant financial stress due to unexpected market uncertainty and are in higher education level areas.

This study makes significant contributions to the existing theoretical frameworks. First, we extend the literature on misconduct by demonstrating the substantial impact of local gambling preferences in a state on financial advisor misconduct. We provide direct evidence of the influence of regional gambling culture on financial advisor misconduct. Second, our paper enhances the understanding of informal institutional theory from a gambling culture perspective by demonstrating that local gambling culture positively influences individual and corporate risk-taking behaviors and decisions. This study also has significant implications for policymakers and regulatory authorities. By understanding these determinants, policymakers can develop targeted interventions and regulations to reduce misconduct and enhance consumer protection. In addition, given the United States' prominence as one of the world's most influential financial markets, our study provides invaluable insights for global applicability. These findings contribute to measures to combat misconduct in other countries and provide a blueprint for regulators to develop corresponding policies and measures to promote integrity and transparency in financial markets.

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Appendix: Variable description

Variable	Definition	Source
Financial Advisor Misconduct		
Ind_Misconduct	If an advisor engages in misconduct actions in a year =1 and =0 otherwise	BrokerCheck database
Firm_Misconduct	The total number of recorded advisor misconducts of a firm in a given year	
Gamble Measure		
HighLottery	If the state in which a firm is operated has *LotteryPerCapita* above the sample median =1 and =0 otherwise	U.S. Census Bureau
LotteryPerCapita	The standardizing form of state lottery sales divided by state population	
Individual-level Variables		
Experience	The number of years since the advisor first started working with an investment advisor firm	BrokerCheck database
Gender_Male	If the advisor is male =1 and =0 otherwise	
Series_63	If the advisor has Series 63 license =1 and =0 otherwise	
Series_65	If the advisor has Series 65 license =1 and =0 otherwise	
Series_66	If the advisor has Series 66 license =1 and =0 otherwise	
Firm-level Variables		
Average_Experience	The average number of years of advisors' experience in a firm	BrokerCheck database
Average_Male	The average proportion of male advisors in a firm	
Average_series_63	The average proportion of advisors with Series 63 license in a firm	
Average_ series_65	The average proportion of advisors with Series 65 license in a firm	
Average_ series_66	The average proportion of advisors with Series 66 license in a firm	
Number	The total number of investment advisors employed by a firm	
State-level Variables		
Population	The log of the total state-level population	U.S. Census Bureau
Median_Income	The log of the median household income of the state	U.S. Census Bureau
Nonwhite	The proportion of state residents who are nonwhite	U.S. Census Bureau
Religiosity	The number of adherents divided by the population in a state	ARDA
Disaster_Loss	The log of annual property and crop losses due to natural climate disasters at the state level	SHELDUS
Gambling_Index	An index representing whether pari-mutuel, commercial, tribal, and racetrack are legal in a state, ranging from 0 to 4	Adhikari & Agrawal (2016)

Notes:

- *Ind_Misconduct = financial advisor individual misconduct;*
- *Firm_Misconduct=firm level misconduct;*
- *ARDA represents the Association of Religion Data;*
- *SHELDUS is the Spatial Hazards Events and Losses Database.*

Figure 1: Frameworks between local gambling preferences and financial advisor misconduct

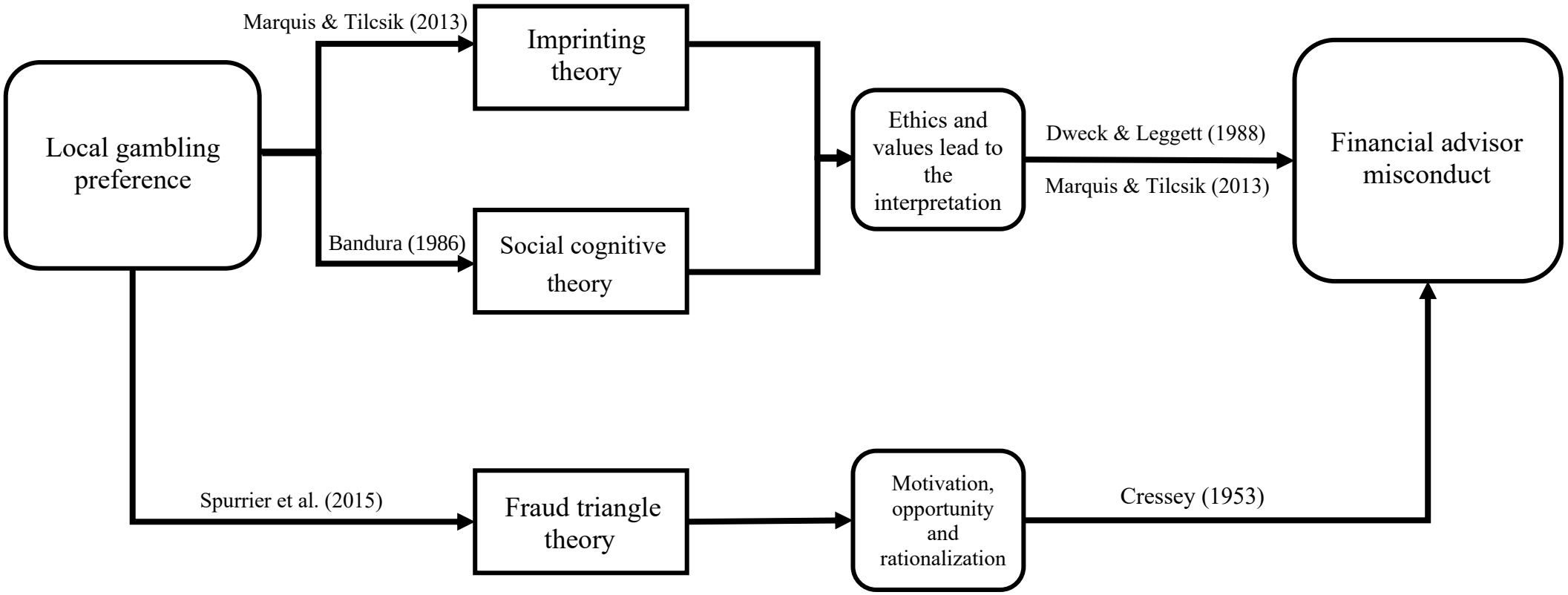

Table 1: Descriptive statistics and correlation matrix

Panel A shows the descriptive statistics for variables used in our regression analysis at the individual and the firm levels. For each variable, we display the mean value, standard deviation (S.D.), and the 25th, 50th and 75th percentile values. Panel B displays the correlation matrix of regression variables used in this study at the individual level and the firm level. * represents the correlation significance at the 5% level or better. The sample period is from 2007 to 2015. Variable definitions and data sources are in the Appendix.

Panel A: Descriptive statistics

Variables	Mean	p25	p50	p75	SD
State-level					
HighLottery	0.538	0	1	1	0.499
LotteryPerCapita	0	-0.754	-0.223	0.45	1
Population	16.11	15.57	16.11	16.79	0.89
Median_Income	10.89	10.78	10.88	11.01	0.147
Nonwhite	0.35	0.21	0.355	0.441	0.154
Religiosity	0.485	0.441	0.497	0.543	0.074
Education	7.506	7.344	7.483	7.673	0.247
Gambling_Index	2.601	2	3	3	1.092
Disaster_Loss	18.07	16.78	18	19.45	2.102
Individual-level					
Indi_Misconduct	0.009	0	0	0	0.096
Experience	6.813	3	6	10	5.283
Gender_Male	0.771	1	1	1	0.42
Series_63	0.652	0	1	1	0.476
Series_65	0.437	0	0	1	0.496
Series_66	0.42	0	0	1	0.494
Firm-level					
Firm_Misconduct	0.097	0	0	0	0.957
Average_Experience	7.128	4	6.667	10	4.562
Average_Male	0.845	0.778	1	1	0.281
Average_Series_63	0.587	0	0.698	1	0.419
Average_Series_65	0.558	0	0.571	1	0.415
Average_Series_66	0.211	0	0	0.351	0.331
Number	10.24	1	1	4	64.8

Panel B: Correlation matrix- individual level

	HighLottery	LotteryPerCapita	Experience	Gender_Male	Series_63	Series_65	Series_66	Population	Median_Income	Nonwhite	Religiosity
HighLottery	1										
LotteryPerCapita	0.6839*	1									
Experience	-0.0274*	-0.0293*	1								
Gender_Male	0.0245*	0.0243*	0.0654*	1							
Series_63	0.0063*	0.0015*	0.2637*	0.0635*	1						
Series_65	0.0294*	0.0293*	0.2047*	0.0768*	0.4286*	1					
Series_66	-0.0255*	-0.0173*	-0.3121*	-0.0897*	-0.5070*	-0.6775*	1				
Population	-0.1080*	-0.0793*	0.0222*	-0.0111*	-0.0207*	-0.0274*	-0.0010	1			
Median_Income	0.0655*	0.2667*	0.0444*	0.0037*	-0.0203*	0.0339*	-0.0062*	0.0968*	1		
Nonwhite	-0.2032*	-0.0899*	0.1152*	-0.0225*	-0.0326*	-0.0001	0.0295*	0.6004*	0.2601*	1	
Religiosity	0.0318*	0.2254*	-0.0408*	0.0318*	0.0199*	-0.0040*	-0.0096*	-0.0569*	-0.0093*	-0.0395*	1

Panel B: Correlation matrix- firm level

	HighLottery	LotteryPerCapita	Average_ Experience	Average_ Male	Average_ Series_63	Average_ Series_65	Average_ Series_66	Number	Population	Median_ Income	Nonwhite	Religiosity
HighLottery	1											
LotteryPerCapita	0.6605*	1										
Average_Experience	-0.0212*	-0.0070*	1									
Average_Male	0.0117*	-0.0048*	0.0055*	1								
Average_Series_63	0.0053*	-0.0106*	0.1434*	0.0224*	1							
Average_Series_65	0.0180*	-0.0034	-0.0694*	0.0477*	0.1211*	1						
Average_Series_66	-0.0237*	-0.0246*	-0.0897*	-0.0469*	-0.0925*	-0.4310*	1					
Number	0.0037	-0.0025	-0.0110*	-0.0416*	0.0245*	-0.0463*	0.0998*	1				
Population	-0.1078*	-0.1044*	-0.0172*	0.0366*	-0.0802*	-0.0300*	-0.0586*	0.0220*	1			
Median_Income	0.0972*	0.2998*	0.0788*	-0.0150*	-0.0567*	0.0094*	-0.0393*	-0.0035	0.0992*	1		
Nonwhite	-0.2085*	-0.1323*	0.0583*	-0.0004	-0.0630*	0.0188*	-0.0047*	0.0066*	0.5894*	0.2289*	1	
Religiosity	0.0810*	0.2593*	-0.0331*	0.0314*	0.0213*	-0.0087*	-0.0098*	0.0076*	0.0060*	-0.0377*	-0.0215*	1

Table 2: Gambling preference and financial advisor misconduct: Baseline results

This table reports regression results of the association between local gambling preferences and financial advisor misconduct at the individual level (Panel A) and the firm level (Panel B). The dependent variable in columns (1) and (2) is *HighLottery* and in columns (3) and (4) is *LotteryPerCapita*. Columns (1) and (3) include the constant term, firm and year fixed effects and columns (2) and (4) include the constant term, firm×year fixed effects. The t-statistics reported in parentheses are based on heteroscedasticity-consistent standard errors clustered by firm and year. *, **, and *** indicate $p < 0.1$, $p < 0.05$, and $p < 0.01$, respectively. Variable definitions and data sources are in the Appendix.

Panel A: Individual-level analysis

	Ind_Misconduct	*Ind_Misconduct*	*Ind_Misconduct*	*Ind_Misconduct*
	(1)	(2)	(3)	(4)
HighLottery	0.0013***	0.0014***		
	(6.621)	(7.191)		
LotteryPerCapita			0.0005***	0.0005***
			(4.924)	(5.476)
Experience	0.0003***	0.0003***	0.0003***	0.0003***
	(10.721)	(10.382)	(10.796)	(10.446)
Gender_Male	0.0048***	0.0048***	0.0048***	0.0048***
	(16.157)	(16.524)	(16.191)	(16.555)
Series_63	0.0031***	0.0030***	0.0031***	0.0030***
	(14.883)	(14.931)	(14.798)	(14.854)
Series_65	0.0012***	0.0012***	0.0012***	0.0012***
	(4.551)	(4.472)	(4.551)	(4.469)
Series_66	0.0002	0.0002	0.0002	0.0002
	(1.067)	(0.895)	(0.991)	(0.825)
Population	0.0004***	0.0005***	0.0005***	0.0006***
	(3.189)	(3.513)	(3.692)	(4.039)
Median_Income	-0.0020***	-0.0018***	-0.0023***	-0.0021***
	(-3.523)	(-3.121)	(-3.888)	(-3.594)
Nonwhite	0.0061***	0.0059***	0.0052***	0.0049***
	(6.931)	(6.608)	(5.949)	(5.590)
Religiosity	-0.0091***	-0.0090***	-0.0104***	-0.0104***
	(-7.279)	(-7.519)	(-8.111)	(-8.313)
Constant	0.0173**	0.0140**	0.0207***	0.0178***
	(2.567)	(2.076)	(2.973)	(2.576)
Firm FE	Yes	No	Yes	No
Year FE	Yes	No	Yes	No
Firm×Year FE	No	Yes	No	Yes
S.E. clustered	Firm, Year	Firm, Year	Firm, Year	Firm, Year
Observations	2,540,794	2,451,196	2,540,794	2,451,196
Adj R-squared	0.010	0.006	0.010	0.006

Panel B: Firm-level analysis

	Firm_Misconduct	*Firm_Misconduct*	*Firm_Misconduct*	*Firm_Misconduct*
	(1)	(2)	(3)	(4)
HighLottery	0.0246***	0.0321***		
	(4.064)	(4.792)		
LotteryPerCapita			0.0094***	0.0100***
			(3.462)	(3.626)
Average_Experience	0.0050***	0.0045***	0.0050***	0.0045***
	(6.007)	(5.820)	(6.044)	(5.822)
Average_Male	0.0222***	0.0218***	0.0228***	0.0230***
	(4.223)	(3.724)	(4.332)	(3.918)
Average_Series_63	0.0119***	0.0091*	0.0111***	0.0078
	(2.802)	(1.725)	(2.627)	(1.499)
Average_Series_65	0.0087*	0.0058	0.0089*	0.0061
	(1.768)	(0.982)	(1.804)	(1.047)
Average_Series_66	0.0014	-0.0042	0.0007	-0.0056
	(0.254)	(-0.555)	(0.126)	(-0.740)
Number	0.0111***	0.0111***	0.0111***	0.0111***
	(14.430)	(15.150)	(14.429)	(15.149)
Population	-0.0123	-0.0235**	-0.0106	-0.0208**
	(-1.348)	(-2.461)	(-1.162)	(-2.206)
Median_Income	-0.0830***	-0.0995***	-0.0890***	-0.1018***
	(-3.882)	(-4.622)	(-4.091)	(-4.642)
Nonwhite	0.2193***	0.3344***	0.2118***	0.3206***
	(7.253)	(8.261)	(7.010)	(7.955)
Religiosity	-0.2619***	-0.3017***	-0.2788***	-0.3196***
	(-6.629)	(-7.414)	(-7.083)	(-7.893)
Constant	1.0545***	1.3892***	1.1147***	1.4030***
	(3.590)	(4.822)	(3.739)	(4.798)
Firm FE	Yes	No	Yes	No
Year FE	Yes	No	Yes	No
Firm×Year FE	No	Yes	No	Yes
S.E. clustered	Firm, Year	Firm, Year	Firm, Year	Firm, Year
Observations	238,774	89,547	238,774	89,547
Adj R-squared	0.510	0.558	0.510	0.558

Table 3: Instrumental variable approach

This table presents the results of two-stage-least-square (2SLS) tests for regional gambling culture and misconduct at the individual level (Panel A) and the firm level (Panel B). The instrumental variable is the logarithm of total property and crop losses (*Disaster_Loss*) from climate disasters in the United States. We aggregate the annual county-level data at the state level. The constant term, firm and year fixed effects are contained in the regressions. The t-statistics reported in parentheses are based on heteroscedasticity-consistent standard errors clustered by firm and year. *, **, and *** indicate $p < 0.1$, $p < 0.05$, and $p < 0.01$, respectively. Variable definitions and data sources are in the Appendix.

Panel A: Individual level

	HighLottery	*Indi_Misconduct*	*LotteryPerCapita*	*Indi_Misconduct*
	(1)	(2)	(3)	(4)
Disaster_Loss	-0.0898***		-0.1675***	
	(-8.406)		(-11.207)	
HighLottery		0.0023***		
		(2.716)		
LotteryPerCapita				0.0012***
				(3.023)
Experience	-0.0031***	0.0003***	-0.0096***	0.0003***
	(-2.978)	(4.208)	(-5.790)	(4.256)
Gender_Male	0.0241***	0.0048***	0.0392***	0.0048***
	(11.067)	(5.760)	(8.499)	(5.768)
Series_63	-0.0083**	0.0031***	0.0082	0.0031***
	(-2.026)	(8.166)	(0.900)	(8.109)
Series_65	0.0059	0.0012***	0.0173	0.0012***
	(0.474)	(2.750)	(0.905)	(2.716)
Series_66	-0.0206	0.0002	-0.0223	0.0001
	(-1.436)	(0.544)	(-1.179)	(0.484)
Population	0.1739***	0.0004**	0.2347***	0.0005**
	(4.755)	(1.988)	(4.452)	(2.302)
Median_Income	0.0209	-0.0027***	1.0037***	-0.0039***
	(0.179)	(-4.289)	(6.324)	(-8.465)
Nonwhite	-1.1430***	0.0068***	-1.3384***	0.0058***
	(-5.265)	(4.632)	(-5.581)	(4.841)
Religiosity	0.0892	-0.0088***	2.8109***	-0.0121***
	(0.507)	(-6.478)	(8.082)	(-7.126)
Constant	-0.1983***	-0.0028***	-0.2922***	-0.0029***
	(-6.424)	(-11.363)	(-7.901)	(-13.080)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
S.E. clustered	Firm, Year	Firm, Year	Firm, Year	Firm, Year
N	2,542,227	2,542,227	2,542,227	2,542,227
Kleibergen-Paap Wald F statistic	70.66		125.59	

Panel B: Firm level

	HighLottery	*Firm_Misconduct*	*LotteryPerCapita*	*Firm_Misconduct*
	(1)	(2)	(3)	(4)
Disaster_Loss	-0.0473***		-0.1101***	
	(-8.081)		(-10.961)	
HighLottery		0.0496*		
		(1.651)		
LotteryPerCapita				0.0213*
				(1.764)
Average_Experience	-0.0027**	0.0022**	-0.0064***	0.0022**
	(-2.484)	(2.295)	(-3.605)	(2.242)
Average_Male	0.0579***	0.0226***	0.0891***	0.0236***
	(5.110)	(3.553)	(3.576)	(3.579)
Average_Series_63	-0.0115	0.0168***	0.0501***	0.0152***
	(-1.077)	(3.440)	(2.812)	(3.234)
Average_Series_65	0.0158	0.0061	0.0253	0.0063
	(1.164)	(1.029)	(1.086)	(1.067)
Average_Series_66	-0.0340**	-0.0029	-0.0078	-0.0045
	(-2.336)	(-0.307)	(-0.311)	(-0.456)
Number	-0.0000	0.0111***	-0.0001	0.0111***
	(-0.341)	(6.155)	(-0.750)	(6.155)
Population	0.1293***	-0.0129*	0.1544***	-0.0098
	(5.195)	(-1.670)	(4.488)	(-1.403)
Median_Income	0.3430***	-0.1094***	1.6302***	-0.1271***
	(3.939)	(-3.088)	(16.691)	(-3.379)
Nonwhite	-0.5785***	0.2103***	-0.7943***	0.1985***
	(-3.383)	(4.483)	(-5.029)	(5.003)
Religiosity	0.0959	-0.2455***	1.9817***	-0.2829***
	(1.256)	(-3.726)	(13.118)	(-3.564)
Constant	-0.1243***	-0.0083**	-0.2092***	-0.0100
	(0.000)	(-2.206)	(-10.187)	(.)
Firm FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
S.E. clustered	Firm, Year	Firm, Year	Firm, Year	Firm, Year
N	241,796	241,796	241,796	241,796
Kleibergen-Paap Wald F statistic	65.30		120.14	

Table 4: Robustness tests - Alternative measure of gambling preference

This table presents the results using an alternative measure of local gambling preferences at the individual level (Panel A) and firm level (Panel B). Following Adhikari and Agrawal (2016), we collect data on the current legal status of four categories of gambling (pari-mutuel, commercial, tribal, and racetrack) in all 50 states of the United States. If the four gambling types are legal in a state, they are recorded as one respectively, and they are recorded as 0 otherwise. This index (*Gmabling_Index*) takes a value of 0 to 4 for a state and is time-invariant. The constant term, firm and year fixed effects are contained in the regressions. The t-statistics reported in parentheses are based on heteroscedasticity-consistent standard errors clustered by firm and year. *, **, and *** indicate statistical significance at the 10%, 5% and 1% levels, respectively. Variable definitions and data sources are in the Appendix.

Panel A: Individual level

	Ind_Misconduct	*Ind_Misconduct*
	(1)	(2)
Gambling_Index	0.0003***	0.0003***
	(4.043)	(3.926)
Experience	0.0003***	0.0003***
	(10.613)	(10.255)
Gender_Male	0.0048***	0.0048***
	(16.195)	(16.550)
Series_63	0.0031***	0.0030***
	(14.910)	(14.957)
Series_65	0.0014***	0.0014***
	(5.196)	(5.107)
Series_66	0.0003	0.0002
	(1.079)	(0.858)
Population	0.0002*	0.0003**
	(1.865)	(2.144)
Median_Income	-0.0023***	-0.0020***
	(-3.916)	(-3.453)
Nonwhite	0.0056***	0.0054***
	(7.171)	(6.864)
Religiosity	-0.0057***	-0.0057***
	(-4.791)	(-4.987)
Constant	0.0217***	0.0184***
	(3.217)	(2.715)
Firm FE	Yes	No
Year FE	Yes	No
Firm ×Year FE	No	Yes
S.E. clustered	Firm, Year	Firm, Year
Observations	2,647,023	2,554,371
Adj R-squared	0.010	0.006

Panel B: Firm level

	Firm_Misconduct	*Firm_Misconduct*
	(1)	(2)
Gambling_Index	0.0068***	0.0085***
	(3.120)	(4.023)
Average_Experience	0.0047***	0.0042***
	(6.246)	(6.251)
Average_ Male	0.0225***	0.0232***
	(4.604)	(4.355)
Average_Series_63	0.0086**	0.0036
	(2.115)	(0.745)
Average_Series_65	0.0125***	0.0119**
	(2.636)	(2.165)
Average_Series_66	0.0018	-0.0030
	(0.334)	(-0.444)
Number	0.0110***	0.0110***
	(14.463)	(15.131)
Population	-0.0116	-0.0159*
	(-1.385)	(-1.892)
Median_Income	-0.0754***	-0.0837***
	(-3.885)	(-4.278)
Nonwhite	0.1989***	0.2643***
	(8.113)	(9.179)
Religiosity	-0.1579***	-0.1746***
	(-5.008)	(-5.550)
Constant	0.9147***	1.0587***
	(3.314)	(3.950)
Firm FE	Yes	No
Year FE	Yes	No
Firm ×Year FE	No	Yes
S.E. clustered	Firm, Year	Firm, Year
Observations	252,197	98,161
Adj R-squared	0.499	0.543

Table 5: The effect of the financial crisis on gambling preference and financial advisor misconduct

This table shows the influence of the independent variable *HighLottery* on financial advisor misconduct during the financial crisis (*Crisis*) at the individual level (Panel A) and firm level (Panel B). *Crisis* is a dummy variable that equals one for the years 2008 and 2009, and zero otherwise. The constant term, firm and year fixed effects are contained in the regressions. The t-statistics reported in parentheses are based on heteroscedasticity-consistent standard errors clustered by firm and year. *, **, and *** indicate $p < 0.1$, $p < 0.05$, and $p < 0.01$, respectively. Variable definitions and data sources are in the Appendix.

Panel A: Individual level

	Ind_Misconduct
	(1)
HighLottery*Crisis	-0.0009*
	(-1.741)
HighLottery	0.0011***
	(5.799)
Experience	0.0003***
	(10.729)
Gender_Male	0.0048***
	(16.136)
Series_63	0.0031***
	(14.886)
Series_65	0.0012***
	(4.540)
Series_66	0.0002
	(1.061)
Population	0.0004***
	(2.994)
Median_Income	-0.0021***
	(-3.610)
Nonwhite	0.0062***
	(6.718)
Religiosity	-0.0092***
	(-7.103)
Constant	0.0185***
	(2.724)
Firm FE	Yes
Year FE	Yes
S.E. clustered	Firm, Year
Observations	2,540,794
Adj R-squared	0.010

Panel B: Firm level

	Firm_Misconduct
	(1)
HighLottery*Crisis	-0.0156*
	(-1.739)
HighLottery	0.0215***
	(3.968)
Average_Experience	0.0050***
	(6.007)
Average_ Male	0.0222***
	(4.227)
Average_Series_63	0.0120***
	(2.812)
Average_Series_65	0.0086*
	(1.752)
Average_Series_66	0.0013
	(0.236)
Number	0.0111***
	(14.431)
Population	-0.0126
	(-1.374)
Median_Income	-0.0845***
	(-3.924)
Nonwhite	0.2222***
	(7.306)
Religiosity	-0.2628***
	(-6.655)
Constant	1.0780***
	(3.644)
Firm FE	Yes
Year FE	Yes
S.E. clustered	Firm, Year
Observations	238,774
Adj R-squared	0.510

Table 6: The effect of education on gambling preference and advisor misconduct

This table displays the results of education on gambling preference (*HighLottery*) and financial advisor misconduct at the individual level (Panel A) and the firm level (Panel B). The education data is collected from the Integrated Public Use Microdata Series (IPUMS) U.S. database, and the educational attainment of a respondent has values between 0 and 11. The constant term, firm×year fixed effects are contained in the regressions. The t-statistics reported in parentheses are based on heteroscedasticity-consistent standard errors clustered by firm and year. *, **, and *** indicate $p < 0.1$, $p < 0.05$, and $p < 0.01$, respectively. Variable definitions and data sources are in the Appendix.

Panel A: Individual level

	Ind_Misconduct
	(1)
HighLottery*Education	-0.0027***
	(-2.601)
Education	0.0028***
	(3.755)
HighLottery	0.0215***
	(2.714)
Experience	0.0003***
	(10.399)
Gender_Male	0.0048***
	(16.536)
Series_63	0.0030***
	(14.915)
Series_65	0.0012***
	(4.489)
Series_66	0.0002
	(0.921)
Population	0.0005***
	(3.699)
Median_Income	-0.0028***
	(-3.048)
Nonwhite	0.0070***
	(7.144)
Religiosity	-0.0071***
	(-5.520)
Constant	0.0022
	(0.240)
Firm×Year FE	Yes
S.E. clustered	Firm, Year
Observations	2,451,196
Adj R-squared	0.006

Panel B: Firm level

	Firm_Misconduct
	(1)
HighLottery*Education	-0.0903***
	(-2.855)
Education	0.0462*
	(1.811)
HighLottery	0.7089***
	(2.961)
Average_Experience	0.0045***
	(5.992)
Average_ Male	0.0219***
	(3.749)
Average_Series_63	0.0097*
	(1.842)
Average_Series_65	0.0064
	(1.133)
Average_Series_66	-0.0036
	(-0.484)
Number	0.0111***
	(15.151)
Population	-0.0238**
	(-2.500)
Median_Income	-0.0825*
	(-1.949)
Nonwhite	0.3490***
	(8.340)
Religiosity	-0.2557***
	(-6.604)
Constant	0.8405**
	(2.095)
Firm×Year FE	Yes
S.E. clustered	Firm, Year
Observations	89,547
Adj R-squared	0.558