Bribing the Self
Self-Deception in Financial Advice

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Summary: Whenever we decide what product to buy, what investment to make, or what medical treatment to obtain, we often rely on expert advice. But, what happens when advisors receive bonus payments for recommending certain products, investments or treatments? In a series of experiments with university students, we provide evidence that advisors may in these cases engage in selfdeception, convincing themselves that the bonus product is also the better one, which allows them to maximize their payment while maintaining a moral selfimage.

Our life as modern consumers is not easy. Whenever we want to buy a new smartphone or car, decide how to invest our money, or even decide what treatment to obtain for our back issues, it is easy to find ourselves bedazzled by a plethora of options. In many cases, the number of possible alternatives can be simply overwhelming. For example, amazon.de currently lists over 1,500 items in the "smartphone" category. In other cases, it can be hard to evaluate the quality of different options even when there are few. For example, is the added storage space of the newest smartphone worth the extra cost? Or should we consider having back surgery instead of physiotherapy, when we don't know the advantage of each of these treatments?

In situations like these, we as modern consumers often rely on expert advice to help us make the best decisions. We ask salesmen to advise us on the type of car that best fits our needs. We ask financial advisors to tell us how to invest our money. And we ask doctors to recommend the best type of medication for our physical ailments. We benefit from the expert's knowledge, and the expert benefits from the fees we pay for their advice.

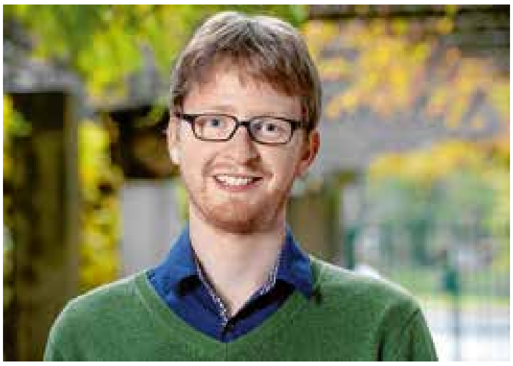
While this relationship is often mutually beneficial, in some cases we are not the only ones who pay the experts for their advice. Salesmen may get higher bonuses for selling certain types of (expensive) products. And financial advisors and doctors may get commissions or bonus payments from investment funds or pharmaceutical companies in exchange for convincing us to choose an expensive investment plan or treatment. This creates a potential tension in the advisor's mind. On the one hand, she may be internally motivated to give good advice, for example because she wants to adhere to professional standards or feels like it is the right thing to do. On the other hand, a high commission may also look appealing. In other words, there is a potential conflict between money maximization and a desire to behave honestly.

Homo oeconomicus vs. homo moralis

Uri Gneezy, Silvia Saccardo, Marta Serra-Garcia and I study the behavior of advisors in cases where such conflicts between money maximization and morality may exist. We differentiate between three types of advisors. First, there is *homo oeconomicus*, who cares only about his self-interest, and therefore always chooses the advice that comes with the highest commission. Second, there is *homo moralis*, who cares about behaving morally and therefore always chooses the advice that is in her client's best interest. Finally, there is an intermediate type of advisors who want to behave honestly but are not totally certain about what honest behavior entails. These advisors may in some cases be able to conveniently deceive themselves into believing that the advice that maximizes their self-interest is also the one that is most beneficial to the client. Specifically, these advisors may be able to convince themselves that the product or treatment that comes with the highest commission or bonus is also in their client's best interest. This allows them to retain a self-image as a moral person while still maximizing their income and thereby effectively get the best of both worlds.

We study self-deception in financial advice using a series of laboratory experiments done with students at the University of California, San Diego. The experiments were simple. Students were invited to a computer room and asked to take on the role of a financial advisor. Each financial advisor was presented with two products (A and B) on their computer screen. They were then asked to provide advice to a client using a simple written message: "I recommend you choose product A/B". Clients had no information on the quality of the two products, and therefore were completely dependent on their advisor's recommendation. We constructed the two products such that product A was less risky than product B, while product B had a higher rate of return. Hence, neither of the two products was clearly better than the other. Indeed, in a baseline version of the experiment where advisors did not receive a commission for either product, both products were recommended by a substantial portion of advisors.

In addition to a baseline without payments, we also introduced two versions where advisors obtained a bonus for recommending the less risky product (product A). These two versions differed only in when the advisors found out about the bonus payment. In the first case, we informed advisors about the bonus at the beginning of the experiment, before they first saw the products. In the second case, we first let them examine the products and only informed them about the bonus just before they made their decision. All other elements of the experiment, including the size of the bonus, were the same.



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Three types of advisors

How does changing the timing of the bonus payment information affect the advisor's decision? For *homo oeconomicus* and *homo moralis*, the timing is irrelevant. The *homo oeconomicus* will happily recommend the product with the bonus and the *homo moralis* will provide honest advice in both cases. Indeed, the timing only matters for the third type of advisors: those who engage in self-deception. When these advisors find out about the bonus at the beginning of the experiment, they can deceive themselves into believing that product A is in fact the better product. This allows them to recommend the product and follow their self-interest while retaining their self-image as an honest and moral person. By contrast, when advisors only find out about the bonus at the end of the experiment, self-deception is harder. Having already convinced themselves that one product is superior, it is no longer possible to choose the product with the bonus without compromising their self-image. Hence these types of advisors should be less likely to recommend the bonus product in cases where they only find out about the bonus at the end of the experiment.

Consistent with this line of reasoning, we find a sizable difference between the two versions of the experiment. When advisors find out about the bonus at the beginning of the experiment, approximately 60 per cent of advisors recommend the bonus product. When advisors only find out about the bonus at the end, this fraction falls to approximately 30 per cent, which is similar to the fraction observed without the bonus. This implies that approximately 30 per cent of advisors in our experiment engage in self-deception: they recommend the bonus product when self-deception is possible, but choose the other option when it is not.

Consumers should be aware of bonus effects

These results therefore demonstrate the existence of self-deception in financial advice among a sample of student participants. In so doing, our results illustrate that bonus payments may distort the decisions of expert advisors for two different reasons. The first is a direct effect: self-interested advisors will recommend the product with the highest commission simply because it is in their interest to do so. Our results also point to a second, more indirect effect: the commission may also change the advisor's judgment, convincing her that the product with the highest commission is also the better product. Hence, our results illustrate the potential of bonus payments to distort even the decisions of advisors who see themselves as honest people, by changing how they rank the two options. This also implies that as consumers we should be doubly wary of advisors who receive third-party commissions: even when they themselves genuinely believe that they are acting in our best interest, they may have deceived themselves, and may in fact may only be pursuing their self-interest.

Our results also suggest that subtle changes in the choice architecture –in our case, a slight change in the timing– can have important effects on the behavior of advisors. In follow-up work, we also show that moving to a more objective environment has the potential to limit, and possibly even remove, the scope for self-deception. For example, providing an expert with information on the types of products a client typically prefers may make it harder for the expert to convince herself that a bonus product is also the better one. Even in such cases, we as consumers would do well to be wary of expert advice and consider the role of self-deception on their behavior.

References
Gneezy, Uri/Saccardo, Silvia/Serra-Garcia, Marta/Veldhuizen, Roel van: "Bribing the Self." Mimeo.