Negative: Investment Robo Advisors

By “Coach Vance” Trefethen

***Resolved: The United States federal government substantially reform the use of Artificial Intelligence technology***

Case Summary: The AFF plan puts regulations on the use of AI “Robo Advisors” that provide stock market / investment advice to the public. This brief argues that such regulations are not needed. Also, by raising costs and reducing demand for Robo Advisors, AFF would make the investment world worse off if people go by their emotional investing decisions rather than the safe and steady Robo advice they could be getting instead.

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Negative: Investment Robo Advisors

INHERENCY

1. Investors can choose

Investors can use hybrid robo/human advisors

Sean R. Walters 2019. (chief executive officer of the Investments & Wealth Institute) Five Robo Advisor Myths Debunked 12 July 2019 <https://www.wealthmanagement.com/technology/five-robo-advisor-myths-debunked> (accessed 3 Sept 2021) (“Ekberg” is Devin Ekberg, CFA, CPWA, CIMA, and chief learning officer and managing director of content development at the [Investments & Wealth Institute](https://investmentsandwealth.org/))

There doesn’t have to be a competition. In fact, many investment professionals use robo advising technology as part of their practice—and it works very well for clients. Ekberg emphasizes the research indicating that many investors prefer a hybrid approach. Even if they aren’t using a separate robo advisor, most clients expect their advisors to use technology to enhance their offerings. “Investors expect robo advisor platforms to supplement their interactions with a human advisor,” Ekberg says. “Clients expect technology to be used to augment the advisor’s role, especially in areas like investment management and tax advice.”

2. Status Quo regulations

Existing regulations completely cover all issues with fiduciary standards of Robo advisors within the Status Quo

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

Under established principles of fiduciary law, digital advisers are capable of fulfilling fiduciary standards that are consistent with the scope and nature of the advisory services they provide to clients. Rather than a radical departure, digital advice reflects the technological evolution of traditional advisory services and thus fits entirely within the existing regulatory framework governing investment advisers.

Digital advisors are not a departure from the existing regulatory framework, so no need for substantial reform

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

Digital advisers are a disruptive and competitive alternative to traditional advisers, but the advisory services they offer build upon the traditional advisory framework and its regulatory structure, rather than depart from it. The range of advisory services offered by digital advisers – from online asset allocation recommendations to discretionary managed accounts comprised of diversified portfolios of ETFs – follow well-worn regulatory paths governing the use of electronic media, the use of interactive websites to deliver advice, and the governance of separately managed account and wrap fee programs. Further, the history of these services underscore that the Advisers Act is a flexible and technologically neutral regulatory regime that has accommodated technological change, innovation in products and services, and evolving business models.

Robo advisors are already required to act in best interest of the client under the Investment Advisers Act of 1940

Robins-Kaplan LLP 2019. (nationwide US trial law firm) ROBO-ADVISORS HAVE THE ABILITY TO MEET FIDUCIARY STANDARDS, BUT NOT ALL DO, Winter 2019 https://www.robinskaplan.com/resources/legal-updates/real-talk-the-robins-kaplan-business-law-update/2019/real-talk-the-robins-kaplan-business-law-update-winter-2019/robo-advisors-have-the-ability-to-meet-fiduciary-standards-but-not-all-do

Robo-advisors, like traditional financial advisors, are required to act in the best interests of their clients.  The Investment Advisers Act of 1940 and analogous state statutes lay the groundwork for these fiduciary duties. While the SEC has not specifically defined the “contours of the fiduciary duty of investment advisers,” acting in the best interests of a client means to conduct “some degree of portfolio analysis when providing investment recommendations.”

2 examples of SQ “human” regulations being enforced on Robos: Wealthfront and Hedgeable in 2018

Robins-Kaplan LLP 2019. (nationwide US trial law firm) ROBO-ADVISORS HAVE THE ABILITY TO MEET FIDUCIARY STANDARDS, BUT NOT ALL DO, Winter 2019 https://www.robinskaplan.com/resources/legal-updates/real-talk-the-robins-kaplan-business-law-update/2019/real-talk-the-robins-kaplan-business-law-update-winter-2019/robo-advisors-have-the-ability-to-meet-fiduciary-standards-but-not-all-do

Although many critics may feel threatened by the new technology, robo-advisors are capable of meeting fiduciary duties. However, just because robo-advisors can meet fiduciary standards doesn’t mean they always do. In fact, as recent as December 21, 2018, the SEC settled cases against two robo-advisors — Wealthfront Advisers LLC and Hedgeable, Inc. — for making false statements about investment products and publishing misleading advertising. These actions were the first enforcement actions against automated investment advisors to date. While the companies neither admitted nor denied the accusations, Wealthfront is being forced to pay a $250,000 penalty and Hedgeable must pay $80,000.

SEC punished Robo advisor “SoFi” for conflict of interest

Melanie Waddell 2021. (journalist) SEC Fines Robo-Advisor SoFi Wealth Over ETF Conflicts 21 Aug 2021 <https://www.thinkadvisor.com/2021/08/19/sec-fines-robo-advisor-sofi-wealth-over-etf-conflicts/> (accessed 8 Sept 2021)

The Securities and Exchange Commission on Thursday filed a cease and desist order against robo-advisor SoFi Wealth and fined it $300,000 related to conflicts of interest associated with investing client assets in SoFi-sponsored ETFs. The SEC action charges SoFi with breaching its fiduciary duties and relates to SoFi’s April 2019 investment of assets of approximately 20,000 automated portfolio accounts into two new proprietary exchange-traded funds sponsored by its parent company, Social Finance Inc.

3. More study will solve

Link: More study needed on Robo advisors and how to regulate them

Tom Baker & Benedict Dellaert 2018 (Baker is William Maul Measey Professor at the University of Pennsylvania Law School; co-founder of Picwell, a data analytics company that makes insurance robo advisors. Dellaert is Professor, Department of Business Economics, Marketing Section, School of Economics, Erasmus University Rotterdam and a member of the board of supervisors of Independer.nl, the largest on-line insurance broker in the Netherlands) Regulating Robo Advice Across the Financial Services Industry <https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2742&context=faculty_scholarship> (accessed 7 Sept 2021)

Second, because there is so little research and analysis available to guide the regulation of robo advisors today and because the need for and corresponding returns to regulatory oversight will increase as the scale of robo advice increases, we propose a regulatory trajectory, rather than a regulatory agenda, that starts by building the necessary human capital. Only then will policymakers be equipped to set a regulatory agenda.

Solution: Securities & Exchange Commission (SEC) and Financial Industry Regulatory Authority (FINRA) will regulate soon once they have the data

Kurt Wolfe 2020 (*attorney with* *Troutman Sanders LLP*) “Robo-Advisors: Regulators May Be Closer Than You Think” https://www.thinkadvisor.com/2020/04/21/robo-advisors-regulators-may-be-closer-than-you-think/

Furthermore, several recent regulatory initiatives may intersect with the robo-advisory segment. For example, FINRA’s [Market Regulation Department has asked firms](https://www.finra.org/rules-guidance/guidance/targeted-examination-letters/zero-commissions) to provide information concerning their “decision not to charge commissions for customer transactions, the impact that not charging commissions has or will have on the firm’s order routing practices and decisions, and other aspects of the Firm’s business.” And the SEC’s Division of Enforcement is [conducting an investigation](https://www.sec.gov/news/speech/speech-avakian-2019-11-05) relating to firms’ cash sweep programs. In addition to these open lines of inquiry, recent market volatility may reveal new areas for regulatory scrutiny. For example, OCIE or FINRA exam teams may be interested in how robo-advisors manage downside risk and adjust/rebalance portfolios. Firms that offer electronic investment advice should note that regulatory priorities and programs are coalescing around — or are at least adjacent to — the robo-advisory model. Given the growth of the industry and the number of new market entrants, firms that offer robo-advisory services could be increasingly likely targets for regulatory scrutiny when the SEC and FINRA resume normal service. From compliance with Reg BI, to the new advertising rule, to nuts-and-bolts record-keeping requirements, regulatory scrutiny of robo-advisory platforms is closer than you think.

4. Don’t need higher standards

Status Quo standards of human advisors should not be raised higher for Robos

Tom Baker & Benedict Dellaert 2018 (Baker is William Maul Measey Professor at the University of Pennsylvania Law School; co-founder of Picwell, a data analytics company that makes insurance robo advisors. Dellaert is Professor, Department of Business Economics, Marketing Section, School of Economics, Erasmus University Rotterdam and a member of the board of supervisors of Independer.nl, the largest on-line insurance broker in the Netherlands) Regulating Robo Advice Across the Financial Services Industry <https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=2742&context=faculty_scholarship> (accessed 7 Sept 2021)

At the same time, however, it is important not to overreact by setting a higher bar for automated advisors than for human advisors. For now, the standard against which automated advisors should be compared is that of humans, whom we know are much less than perfect. Although a large body of research in diverse fields demonstrates that even simple algorithms regularly outperform humans in the kinds of tasks that robo advisors perform, and, thus, it may be appropriate to hold automated advisors to a super-human standard someday, their market share is too small and regulators have too much to learn to do so today.

Status Quo is flexible enough to handle Robos because they’re not that different from human advisors. Best policy is to leave them alone

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/pubs/2016/10/the-evolution-of-advice-digital-investment-advisers-as-fiduciaries> (accessed 8 Sept 2021)

This White Paper explores the application of fiduciary standards to digital advisers.  It concludes that fiduciary standards, such as those incorporated into the Advisers Act, are flexible principles that digital advisers and their nondigital counterparts (traditional advisers) are equally capable of satisfying. Investors benefit from this regulatory flexibility, which encourages innovation and permits the development of more varied services. Indeed, the Advisers Act already accommodates investment advisers with a wide variety of business models, investment strategies, and services. This White Paper also explains that the products and services offered by digital advisers are not unique, but instead are technologically enhanced versions of advisory programs and services that have long been subject to this flexible regulatory framework.

HARMS / SIGNIFICANCE

1. Humans still involved / not exclusively robo

Humans are still involved in investment advising even with Robos

Sean R. Walters 2019. (*chief executive officer of the Investments & Wealth Institute*) Five Robo Advisor Myths Debunked 12 July 2019 <https://www.wealthmanagement.com/technology/five-robo-advisor-myths-debunked> (accessed 3 Sept 2021)

The biggest myth around robo advising is that the robots (or the algorithms) are in charge. In reality, robo advisors have humans at the helm. While parts of portfolio creation are automated, the truth is that most robo advisors have teams of actual investment professionals guiding the process.

Real human beings are still involved, even with robo advisers

Demo Clarke 2020 (Assistant Vice President of Exchange Traded Funds (ETF) Operations at Bank of American Merrill Lynch) Robo-Advisors - Market Impact and Fiduciary Duty of Care to Retail Investors 13 Feb 2020 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3539122> (accessed 8 Sept 2021)

While many commentators focus on the computer and machine aspects of the roboadviser revolution, it is important not to lose sight of the fact that there are real life human beings behind every aspect of the platform— designing, modeling, programming, implementing, and marketing these automated advisers (Seidt, 2016). Indeed, in most instances, robo-advisors and traditional human advisers are utilizing the same technological tools to provide their service with the primary differences being the robo-advisors make their tools directly available to the investor without the human sales force. The false notion that algorithm, and not human advisors manage portfolios is a common misconception. Regardless of the degree of automation in a manager’s investment process, the adviser (and not models) signs investment management agreements, and is vested with the authority to exercise discretion in managing client assets, and has fiduciary obligations (Seidt, 2016). Whether they use third-party models, or proprietary models, investment personnel at quantitative firms, like those at traditional managers, make judgments about investment theories, data sets, and the investment strategy expressed in their models (Seidt, 2016).

2. A/T “Conflicts of interest”

Turn: Robos are LESS likely to have conflict of interest than human advisers

Robins-Kaplan LLP 2019. (nationwide US trial law firm) ROBO-ADVISORS HAVE THE ABILITY TO MEET FIDUCIARY STANDARDS, BUT NOT ALL DO, Winter 2019 https://www.robinskaplan.com/resources/legal-updates/real-talk-the-robins-kaplan-business-law-update/2019/real-talk-the-robins-kaplan-business-law-update-winter-2019/robo-advisors-have-the-ability-to-meet-fiduciary-standards-but-not-all-do

Robo-advisors are capable of meeting this aspect of their fiduciary duty, and some experts have even argued that, because of the automated nature of these services, robo-advisors can more easily avoid conflicts of interest when compared with their human counterparts who may “push investments that pay the highest commissions.” One indicator that a robo-advisor is not conflicted is if they sell products that are not their own. For example, Betterment, an online investment company, does not make their own products and uses this fact to promote their services.

Digital advisors are less likely to have conflict of interest than traditional advisors

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

Regulators have endorsed the position that the digital investment advice model eliminates many of the conflicts of interest presented by traditional advisers. DOL Secretary Thomas E. Perez has publicly remarked that digital investment advice platforms are able to provide fiduciary investment advice to lower balance investors, consistent with their best interests, at “significantly lower” fees than traditional advisers. Moreover, the DOL itself, in its highly anticipated final regulations (the “Fiduciary Rule”) expanding the definition of a fiduciary under ERISA, noted that “the marketplace for robo-advice is still evolving in ways that both appear to avoid conflicts of interest that would violate the prohibited transaction rules and minimize cost.”

3. A/T “Inappropriate investment advice / Not knowing the client”

Robos know the client as well or better than humans and may even be better at avoiding illegitimate deals

Robins-Kaplan LLP 2019. (nationwide US trial law firm) ROBO-ADVISORS HAVE THE ABILITY TO MEET FIDUCIARY STANDARDS, BUT NOT ALL DO, Winter 2019 https://www.robinskaplan.com/resources/legal-updates/real-talk-the-robins-kaplan-business-law-update/2019/real-talk-the-robins-kaplan-business-law-update-winter-2019/robo-advisors-have-the-ability-to-meet-fiduciary-standards-but-not-all-do

To create personalized investment portfolios, robo-advisors ask consumers their age and other questions relating to risk tolerance, goals, and time horizon. The answers are then run through an algorithm, and a risk level ranging from conservative to aggressive is assigned. Based on that, the robo-advisor presents the consumer with a variety of investments meeting the consumer’s criteria.Critics argue that the electronic questionnaires utilized by robo-advisors to gather client information cannot satisfy this fiduciary function, because only limited information about investors’ investment needs and risk tolerance is obtained. But the same can be said for human advisors, where it is incumbent upon them to elicit the proper information from their clients. If the robo-advisor asks the proper questions, it’s as capable of fulfilling the suitability requirement as humans. In fact, the Investment Advisers Act does not direct how much information must be obtained from a consumer in order for an advisor’s recommendation to be deemed appropriate. Also, because robo-advising platforms are based on computerized algorithms, some argue that they cannot be induced to make illegitimate deals.

Robo advisors are very skilled at adapting to specific customer needs

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

Finally, digital investment advice platforms are able to leverage behavioral finance insights to offer innovative services and account features in a timely and consistent way. Digital advisers may collect data and observations based on a client’s online behavior (either individually or in the aggregate) and use the information to enhance the client experience and promote positive investment outcomes. For instance, digital advisers may observe that investors who look at their accounts frequently are more inclined to rebalance their portfolios in the event of minor losses that result from normal intraday market movements. In this way, digital advisers are able to focus on the actual behavioral patterns of clients, and this observed behavior tends to offer insights that clients are not aware of or may not voice to their financial advisors. Digital advisers may leverage such observations to guide investors away from missteps that could lead to negative investment outcomes. In response to actions involving contributions to or transfers from advisory accounts, for example, digital advisers can provide personalized recommendations and reminders that promote positive financial behaviors.

Robos are safer and more reliable than human advisers: they make fewer errors

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

First, the algorithms used by digital advisers are developed by humans, and are monitored and overseen by investment and technology professionals. Rather than take human judgment out of the equation, the skill and investment expertise of these professionals is reflected in the algorithms used to manage client accounts. Digital advisers thus leverage technology to make the value provided by talented portfolio managers and investment professionals available to the broadest universe of clients. Further, digital advice presents strong advantages with respect to the consistency, precision, and predictability of advice. Unlike advice delivered exclusively by individual human financial advisors, digital advice can mitigate instances of distraction, fatigue, or human bias that can lead to negative client investment outcomes or costly trade errors.

Robo advisors are better at communicating with clients than human-only advisors

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

Second, humans are operationally present, and in certain instances supplement, digital advice. A number of digital advisers offer live customer support to assist clients and answer service-related questions. Some digital advisers offer a so-called “hybrid model” where clients have the ability to speak with live investment adviser representatives. Digital advisers also have the capability to communicate instantaneously through email, mobile applications and their web interfaces to clients at a scale that far surpasses what an individual human financial advisor would be able to accomplish. Such communication features can be used to provide real-time account data or tailored portfolio analysis to clients at intervals of their choosing. Whereas an individual human financial advisor may be unable to reach even a small subset of its clients in a timely manner, a digital adviser may provide important and personalized account updates to its clients on a real-time basis.

A/T “Robos don’t get enough info about the investor” – They collect information that meets the scope of their duty and focus on quality, not quantity, of info

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021) (brackets in original)

One of the central themes advanced by critics of digital advisers is that they do not collect sufficient information to provide personalized investment advice and thus are not meeting their fiduciary obligations. We disagree. As discussed below, under established regulatory principles the information captured in the client-profiling process must be evaluated in relation to the nature of the advice that is provided. Accordingly, the critics’ position appears to miss the mark in a number of ways. The Advisers Act does not dictate the minimum amount of information that must be collected to make a reasonable determination that investment advice is appropriate for a client. [**END QUOTE**] In fact, unlike FINRA Rule 2111, the Advisers Act does not prescribe the amount or types of client profile information that are required to be collected in any respect. In 1994 the SEC proposed, but did not adopt, a suitability rule that would have required investment advisers to conduct a reasonable inquiry into a client’s financial situation, investment experience, and investment objectives before providing advice. However, the proposing release makes clear that “the extent of the inquiry would turn on what is reasonable under the circumstances.” For instance, a “comprehensive financial plan” may, according to the proposing release, require extensive personal and financial information about a client, including current income, investments, assets and debts, marital status, insurance policies and financial goals. The implication is that an advisory program that is not offering comprehensive financial planning would not require the collection of such extensive information. [**THEY GO ON LATER IN THE CONTEXT TO WRITE QUOTE**:] What is required to make a reasonable determination is a qualitative, rather than a quantitative, inquiry, and the type or amount of information relied upon by an adviser to make a recommendation may vary without compromising the advice. SEC Chair Mary Jo White, in public remarks addressing digital advisers, has acknowledged that “[j]ust like a conversation with a ‘real person’ about a client’s financial goals, risk tolerances, and sophistication may be more or less robust, so too there is variation in the content and flexibility of information gathered by robo-advisors before advice is given.” Even the more prescriptive FINRA suitability rules provide broker-dealers with the flexibility to omit certain information from a customer profile if the broker-dealer determines that information would not be relevant to making a suitability determination in light of the applicable facts and circumstances.

DISADVANTAGES

1. Emotional trading #1 – Individuals harmed as fewer investors use Robo Advisors when costs go up

Link: Robo advisors cost less than traditional advisors

Diane Harrison 2018 (*principal and owner of Panegyric Marketing, a strategic marketing communications firm; over 25 years’ of expertise in hedge fund and private equity marketing*) 20 Apr 2018 “DON’T FEAR THE ROBO!” <https://caia.org/blog/2018/04/20/dont-fear-the-robo> (accessed 3 Sept 2021)

**FIRST, WHAT ARE SOME BENEFITS OF A ROBO?** Lower fees. Most of these robo advisors charge less than 1%, with some south of .20%, versus the standard investment advisor fee range of 1-3% on a client’s portfolio. This difference alone can make for a slight outperformance over traditional investment services for many individuals.

Link: Regulations raise costs

Kurt B. Harrison & Eric Girma 2016 (Harrison is a senior member of the Russel Reynolds Associates Financial Services Sector and is the Co-head of the Sustainability Practice. Girma - ​Russel Reynolds Associates Global Knowledge Leader for Financial Services) 7 Sept 2016 “The Digital Transformation of Asset and Wealth Management” <https://www.russellreynolds.com/insights/thought-leadership/the-digital-transformation-of-asset-and-wealth-management> (accessed 7 Sept 2021)

To meet the new wave of regulatory requirements, asset and wealth management firms will have to invest significantly in their legal and compliance capabilities, which will be a further drain on profitability. There is little room for error, as the ability to deliver a credible risk-governance model to the regulators has never been more important. Accurately measuring, monitoring and managing credit, counterparty and liquidity risks have become enterprise-wide imperatives, not only because of greater regulatory scrutiny, but also because of the overwhelming financial implications of non-compliance, which can threaten the very survival of an asset management firm.

Link: Low fees are key to growth of Robo advisor usage

Kurt Wolfe 2020 (*attorney with* *Troutman Sanders LLP*) “Robo-Advisors: Regulators May Be Closer Than You Think” https://www.thinkadvisor.com/2020/04/21/robo-advisors-regulators-may-be-closer-than-you-think/

Because robo-advisors charge low (or no) fees, typically require low minimum balances and include helpful features like automatic investing/rebalancing, they have become increasingly popular investment tools for retail investors.

Backup link: Small investors turn to Robos because of low cost. It’s a choice between Robo advice and No advice.

Jennifer Klass & Eric Perelman 2016 (Klass – Partner, Investment Management, with Morgan, Lewis & Bockius, an international law firm. Perelman is an Associate at ML&B) Oct 2016 “THE EVOLUTION OF ADVICE: DIGITAL INVESTMENT ADVISERS AS FIDUCIARIES” <https://www.morganlewis.com/-/media/files/publication/report/im-the-evolution-of-advice-digital-investment-advisers-as-fiduciaries-october-2016.pdf> (accessed 8 Sept 2021)

Moreover, any meaningful discussion of digital advice should acknowledge that it offers the investing public a high-quality, transparent advisory product that entails a different blend of services, at a lower cost, than traditional advisers. Digital advice can help achieve the important policy objective of addressing the retirement crisis by providing advice that is accessible to individual investors – both financially and technologically. That includes investors who do not qualify for, or may not be able to afford, traditional advice. For such investors, the choice is not between traditional advice and digital advice. The choice is between digital advice and no advice.

Link: Robos prevent emotional trading

Diane Harrison 2018 (*principal and owner of Panegyric Marketing, a strategic marketing communications firm; over 25 years’ of expertise in hedge fund and private equity marketing*) 20 Apr 2018 “DON’T FEAR THE ROBO!” <https://caia.org/blog/2018/04/20/dont-fear-the-robo> (accessed 3 Sept 2021)

Elimination of emotional trading. With a robo advisor executing a passively managed program, there is no chance of active management decision-making being affected by human emotional reaction to markets.

Impact: People lose money – on average 7%/year -- if they trade emotionally

Susie Poppick 2016 (journalist with CNBC) 26 Apr 2016 “This impulse makes investors sell low and buy high” <https://www.cnbc.com/2016/04/26/investors-fail-because-of-this-impulse.html> (brackets added) (accessed 7 Sept 2021)

If emotion is a major factor that drives investors to “sell low,” it can also explain why people “buy high.” A different [study](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2739963) [Univ. of Missouri professor Rui] Yao recently co-authored found that households who just experienced investment gains are twice as likely as others to invest all of their workplace retirement portfolio in stocks. Investing based on emotion has consequences: Over the last three decades, U.S. stock investors have lagged the S&P 500 by [more than 7 percentage points](http://www.cnbc.com/id/102929879) annually. Instead of holding on to earn market returns, investors shortchange themselves by trading in and out — at exactly the wrong times.

2. Emotional trading #2 – Systemic crash

Links: Cross apply all the links to emotional investing when Robo use decreases - from DA-1

Link: Emotional trading leads to stock market bubbles that burst

Barry Ritholtz 2015 (journalist) 3 Dec 2015 “The dangers of trading while under the influence of emotion“ GLOBE AND MAIL “<https://www.theglobeandmail.com/globe-investor/investor-education/the-dangers-of-trading-while-under-the-influence-of-emotion/article27579773/> (accessed 3 Sept 2021) (brackets added)

But the results are significant beyond the impact on any one individual trader. [University of California-Berkeley business professor] Mr. [Terrance] Odean observes that we can expand our understanding of how asset bubbles inflate: "As asset prices went up and investors got excited, they were more likely to do uncritical buying and drive prices up more." [**END QUOTE]** In other words, the thrill of a booming stock market can potentially generate even greater speculation and further inflate prices: Historical accounts suggest that rapid, unexpected increases in wealth during the appreciation phase of asset pricing bubbles can lead investors to experience intense, positive emotions. We document, in an experimental setting, that magnitude and amplitude of bubbles is greater when, prior to trading, traders experience the high-intensity, positive emotion of excitement than when they experience either the low- intensity, positive emotion of calm or the high-intensity, negative emotion of fear. [**HE GOES ON TO CONCLUDE QUOTE**:] Thus, the excitement generated by rapidly rising prices in real-world markets may trigger emotions that lead to larger asset pricing bubbles. Rapidly rising prices beget booms, which can turn into bubbles, all of which eventually burst.

Impact: Substantial losses for large numbers of investors

Gordon Scott, last updated 2021. (active investor and technical analyst of securities, futures, forex, and penny stocks for 20+ years; member of the Investopedia Financial Review Board ) Bubble Theory, last updated 30 Aug 2021 <https://www.investopedia.com/terms/b/bubble-theory.asp> (accessed 7 Sept 2021)

Bubbles that do crash create danger for investors because they remain [overvalued](https://www.investopedia.com/terms/o/overvalued.asp) for an indeterminate amount of time before crashing. When bubbles burst, prices decline and stabilize at more reasonable valuations, triggering substantial losses for large numbers of investors. The most recent example of bubble behavior can be observed in the price of Bitcoin from 2016 to 2019.