

# Finance Theory Referee Reports<sup>1</sup>

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*Comments and thoughts from all readers are welcome!*

This document is meant to provide guidance to journal referees of theoretical finance papers, particularly to those referees early in their career. To gather the ideas we spoke with editors of major journals and published theory authors, and then moderated a discussion session at the 4<sup>th</sup> meeting of the Finance Theory Group held at Stanford Graduate School of Business in May 2011. Below is a summary of the ideas gathered from all of these sources. Our hope is that the general wisdom gathered here can improve the quality of the reports we all write, and receive, making them more informative to authors and editors.

The inspiration for this session and summary came from the general complaint from theorists about the difficulty in getting theory published and the general perception that referees are sometimes too quick to dismiss theory papers because of an aspect that is peripheral to the main point. However, theorists are well aware that they themselves are the referees that are writing the reports and rejecting the papers.<sup>2</sup>

This paper is an attempt to gather ideas from the profession on what we could do to increase the quality and usefulness of the referee reports we receive and write. Thus, the following recommendations to referees contain both ideas about how to write a high quality report on a theoretical paper and also what to accept and reject. It is important to emphasize that this piece is *not* intended to dilute the quality of accepted theory papers (the acceptance rate in (at least) top journals is low and should be rightly so for all papers), but to raise the quality of reports, and to create a more collaborative and constructive research environment.

Given the number of people to whom we spoke, we received many and varied suggestions. We have generated a series of suggestions for writing reports distilled from ideas we heard most often. However, almost no one would agree with every point that we make – we are all academics after all. On areas with significant conflicting opinions we have tried to temper a point or discuss more than one perspective. However, we are sure that we will leave some readers unsatisfied – we strongly encourage

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<sup>1</sup> This document borrows a lot from the discussion on refereeing at the 4<sup>th</sup> meeting of the Finance Theory Group at Stanford in May 2011 and we would like to thank all the participants. We are also very grateful to Cam Harvey, Ken Singleton, Uday Rajan, Itay Goldstein, Gustavo Manso, Adriano Rampini and Matt Spiegel for their comments and suggestions. We believe the suggestions presented here are widely shared among most theorists and they definitely present our views on the subject -- all errors and omissions are, of course, our own.

<sup>2</sup> We know of no empirical support for the perception that these are problems suffered more by theorists. The general perceptions that we encountered was that they were more associated with theory, but some challenged this and suggested they were equally associated with both.

everyone to both write to us (to improve future revisions) and to produce alternative suggestions to referees.<sup>3</sup> We believe the debate can only improve the process.

We have broken our suggestions into four areas and posed the suggestions as answers to questions about the refereeing process. The first section relates to the ideas presented in the paper to be refereed. The second section focuses on implementation. The third section discusses the potential relation of the idea to data, while the final section considers the specifics of writing a report.

### **The Idea:**

- What is the key aspect of a theory paper that means it deserves an acceptance or revision rather than a rejection? Agreement was fairly universal that the best papers contained a new idea about an important subject with interesting implications. The fear of editors was that they would reject an important paper, not that they would accidentally accept a weak paper. Thus, we suggest that although the referee should consider all aspects of a paper and push authors to make the paper better, the referee should focus their key recommendation on whether the paper was able to make at least some progress on an important topic. And keep in mind that a little progress on a hard problem is ok.
- Do I have to agree with a paper in order to accept it? No, was the strong consensus. The paper is not written by the referee and does not have to be something the referee would have written. We would argue that a referee could disagree with the paper's main idea but if it is a new idea on an important topic with interesting implications, then the referee may push to make the paper clear, but that no one of us should be the arbiter of what is or is not the right idea about how something works. Let us *all* fight about the idea in the literature.
- Is the result too obvious? Theorists uniformly complained that their papers were rejected because the idea is 'obvious'. But many felt that the entire goal of great theory was to demonstrate a new idea in a simple way. The idea *should* be obvious once the theorist has made an extraordinary effort to create a model to most simply demonstrate the idea. We suggest that obvious is not generally a good criteria for rejection. Instead, if the idea is on an important topic and has not been clearly articulated before and has a set of rich implications, then it the referee may consider accepting even if it is obvious. After all many of the great ideas of economics are obvious now that we all know them. (The M&M Propositions offer a very good example). A test that a referee might follow is "ex ante" vs. "ex post:" an interesting contribution would be obvious after the paper is read but not entirely obvious prior to that.

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<sup>3</sup> Examples we are aware of include De Janvry and Sadoulet (2004) "Guidelines for Referee Reports" <http://are.berkeley.edu/courses/ARE251/2004/assignments/RRGuidelines.pdf> and Chapter 3 of Thomson (2001) A Guide for the Young Economist (MIT Press) both of which are excellent "how to" guides for new Ph.Ds. Hamermesh (1992) "The Young Economist's Guide to Professional Etiquette," Journal of Economic Perspectives, 6(1): 169-179 also includes some superb advice to young referees.

- I don't like the assumptions. Now what? This was an area of great frustration for both authors and editors. Almost all felt that the assumptions are not being made by the referee and the referee does not need to agree with them. We recommend that the referee ask that the assumptions be made clear as well as their impact on the results. However, many new ideas in economics can be brought out even if the assumptions are limited in their realism. But what, you may ask, if the key idea depends on an assumption I don't like? That is, what if the result does not hold if that assumption is changed? The strong consensus was that all models contain necessary assumptions for tractability and we will have to live with that. We suggest that the referee tell the author to make it clear that the result depends on the assumption, but in general referees should tend not to reject a paper over assumptions, particularly those needed for tractability.<sup>4</sup> If the paper is otherwise good then the ideas should be fought about in the literature rather than by the referee and the author.

### **Implementation:**

- How much should I ask the author to do? Almost all agreed that the goal should be to go one round with the authors, two *at most*. We advise referees to decide before the first report if the paper is fundamentally acceptable or not. If it is, then try to ask the authors to do a short list of doable things. Try not to ask the authors to write a completely different model or make a completely different point. Most people felt that only in extremely rare cases with papers having a very large potential should a referee engage the author in a very significant transformation of a paper. We advise that the referee report is not the place for a wish list of all the extensions possible – future work can build from here. A referee may want to ask the author to make the key ideas and assumptions clear, and help the authors to make the paper better by suggesting improvements, but potentially make suggestions separate from requirements. The consensus from editors, authors, and referees was that a short list of required adjustments (3-5 items) followed by a longer list of potential suggestions and editorial improvements was the most helpful kind of report to all involved.
- Is the model too complicated? This is an area that we feel a referee can help a paper significantly improve. Because many authors we spoke to are afraid that their work will be rejected as obvious, they said they tend to increase the model's complication in order to create a richer model with more implications. In doing this, sometimes the main idea becomes obfuscated. We propose that while this is not good practice, it is also not a good reason to reject a paper. Instead, referees may want to ask the authors to begin the paper with a simpler form of their model possibly with some channels shut down. Ask them to emphasize and make the new contribution clear even if it is simple. Once an author has gotten a revision and is thus no longer scared of "it's obvious" they may be much more willing and able to present a clear

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<sup>4</sup> In an extreme a silly assumption [like people want to minimize wealth] produces a silly result and should clearly be cause for a rejection. Each referee must set their own standard. Our point here is that most felt that this was an area in which theorists tended to be too harsh on each other.

and simple version of the idea. Increased complication can then be layered in to increase the richness of the implications.

- What if I would have modeled it in a different way? Some authors felt that referees tended to prefer one particular approach (discrete vs. continuous time, dynamic vs. two-period) and dislike other approaches (“two-period models are just toy models”, “no one needs dynamic stuff – you can show the same in two periods”]. This bias is then used as an excuse to pick on various “technical” assumptions. We encourage referees to remember that this is how the author chose to present the idea. A referee might suggest that a dynamic model could add additional insight or that a two period version might clarify the intuition but most people felt that requiring a switch seemed arbitrary and not the job of the referee.
- What if the result goes against my intuition? A result that goes against intuition can sometimes point to a flaw in the paper. Thus, we and others said that they focus carefully on counter-intuitive results. However, we suggest that if counter or unintuitive results do not stem from a flaw then they should probably not result in a rejection. Our intuition could clearly be wrong, as the theory just showed. We encourage referees to be quite willing to publish work that goes against their intuition. It is just this kind of work that challenges the way we think and pushes us all.

#### **Relation to data:**

- Should the results be testable? This was an area with some controversy (especially among empiricists) though most concluded that a paper did not have to have directly testable implications. We suggest that referees ask the authors to relate to empirical relevance if the model enables that, but this should not be a necessary condition for acceptance. Deep and new theoretical ideas may not have direct empirical implications although they are of immense empirical importance over the long-term.
- What if the paper has both empirical and theoretical contributions? Many authors felt that this was the most dangerous type of paper to write because it was very difficult to satisfy a referee on both parts. We would argue that if both parts of a paper were good enough to stand separately then a rational author would have separated them into two papers. Thus, there must be some reduction in the quality required for both parts of the paper which is overcome by ability to show support for the new idea in both theory and in the data. Many authors felt frustrated at being encouraged to scrap or significantly pare down the model and expand the empirical work. We suggest that as long as the author is proposing a new idea about an interesting subject, then future work can expand on either the theory or empirical work as needed.

- How can I increase paper's and field's impact? Editors complain that accepting theory lowers the impact score for their journal. Thus, accepting theory is an editorial sacrifice. This means theory papers start out with a mark against them that they must overcome. Since editors were concerned about impact, referees can also encourage authors to make changes to their papers that would increase the impact. That said, exactly how to do this was a controversial topic. Some suggested that the paper must be able to be read and understood by an empiricist. Alternatively, even if part of the paper was outside the interest of an empiricist, the paper should at least suggest appropriate empirical tests. Potentially a theory paper could even have simple summary statistics or a regression. Most felt that at the very least a theory paper should talk about real world situations even if those situations do not perfectly fit the model. There was, however, significant push back on these ideas. Many thought that some theory was pushing out the boundaries of financial theory and should still be published in a top journal even its relevance to an empiricist was not immediate. Immediate empirical test may not be obvious or possible with current data. We suggest that overall referees may want to encourage theory authors to relate their theories to data where possible, and to real world situations and empirical tests, but important theoretical contributions should not be overlooked because of a limited relationship to the data.

#### **Specifics on writing a report:**

- What should be the tone of my report? Overall many felt that referees should start with the mindset that they are trying to help the author improve the paper and to help the paper to get published – even if the referee ultimately suggested the paper is not right for the journal. Thus, we propose that referees use a tone of a supportive helper. We all know that it is much easier to tear down than it is to build up. We would like referees to think of themselves as part of the building process. In this light, referees might ask themselves, “why did the author write this paper? Why did they think it was important enough to spend a great deal of their limited time writing it?” Many authors felt that rejections often happen because the referee doesn't “get it”. On the one hand we believe it is the author's job to explain to the reader what and why, but on the other hand we suggest that it is the referee's responsibility to work HARD to try to understand why the author thought it was important. And overall everyone would enjoy the process more if the tone and mindset of the referee was supportive and helpful.
- What is the best way to reject the paper? Obviously, many papers must be rejected. Many referees noted that they tended to decide first whether to accept or reject and then to write the report second. If the referee were going to recommend a rejection they then picked the paper apart in an attempt to justify their rejection recommendation. This seems to lead to an enormous amount of frustration on the receiving end of the report. We propose that a paper be rejected for the same reasons one is accepted. Thus, a rejection would come with clear reasoning about why the idea is not new, not on an important topic or does not have interesting implications. The tone of the report can still be one of helping the author to eventually write a

paper that is new and important without tearing into every aspect of the paper. Authors said that they found a laundry list of complaints to be of very limited use as it became difficult for the author to know how to actually improve the paper. As an example of unjustified reason for rejection that does not need further elaboration, we cite the often-quoted line: “I went through the proof of Proposition 1 and am not convinced. This is against my intuition.”

- How do I increase the chance that my opinion is followed? Many authors feel frustrated at receiving positive referee reports and still being rejected by the journal. Therefore, as a referee we argue that we cannot view our role as simply a gate keeper that allows a paper to pass, but rather, if we recommend a revision or an acceptance we must make it clear to the editor why this is the right decision! We propose that referees essentially become an advocate for why their recommendation is correct. And as noted above, most people we spoke to felt that a new idea on an important subject were the most compelling reasons to move forward. We suggest that referees make sure that their recommendation to the editor is clear and in line with the feedback in the report.
- What do I do if I have a question? Authors also pushed for a greater interaction between the editor in charge of the paper and both the referee and the author. Many felt that at the journals that did the best job with theory submissions the editors often called or emailed back and forth with the referee to make sure they understood why the referee recommended a rejection or to understand what the referee wanted in a revision. Some felt that in a best case scenario the editor might simultaneously interact with the author to clear up misperceptions. We propose that as referees we could think about using the ability to ask the author a question. And as authors and editors ourselves we could encourage journals to become more interactive.
- How can I, as the referee, impress the editor? Many referees, particularly young referees, said that they view doing a referee report as a chance to impress the editor. However, they often felt that they could impress the editor by being extraordinarily tough on the paper. Editors talked about having to overrule theory referees in order to publish enough theory because the referee reports were so negative. We suggest that referees can potentially impress the editor by following some of the suggestions laid out in this document. At the end of the day the editor is likely to be most impressed with a coherent and well-articulated view about what is interesting and important and therefore, why this paper should be accepted or rejected. Referees can build reputations with editors, not by being picky and super critical of every paper, but by showing a balanced critical (both positive and negative) perspective on a paper.

While all of the above points focused on the referee, we as authors understand that editors and referees do not have sufficient time and energy to read our papers in detail unless we make it worthwhile for them to do so. Furthermore, we all recognize that referees rightly set a high hurdle in the first round. Polishing the paper and making it clearer surely increases the chance that the referee will read the paper more carefully, while unpolished papers make the barrier to understand the message very high –

and consequently easier to reject. Thus we suggest to authors that they respect the time of referees and work hard to make the message clear and easier for the referee to digest.

We hope that the above suggestions provide some guidance and help to those in our profession struggling to write better referee reports in order to be a supportive member of our community. Referees are a critical but thankless part of the process, so to all those who take the job seriously – thank you and good luck. We hope you get a good referee!