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ADVANCED TOPICS IN
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AI Opportunities and Challenges

Speakers

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What Are "AI" and "Predictive Data Analytics"?

- Broad concepts without agreed-upon singular definitions

- **Predictive Data Analytics**
  - Using modeling and statistics to predict future outcomes
  - Looking at historical and/or current data patterns to determine the likelihood of recurrence
  - Actual Data + Statistical Analysis and Modeling = Future Predictions

- **Artificial Intelligence (AI)**
  - Machine learning from experience and patterns, so that nonhuman elements can adjust to environmental or data changes and perform human-like tasks
  - Deep learning and natural language processing
  - Self-driving cars, chess-playing computers, computer-generated content, sounds and images
  - Turing Test/Imitation Game: a test of a machine's ability to exhibit intelligent behavior equivalent to, or indistinguishable from, that of a human

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SEC Staff Sweep Exam Request Letter Definition

"Artificial Intelligence" or **"AI"** is a term used to describe computer systems and software programs designed to simulate human intelligence to perform tasks, such as investment analysis and decision-making, given a set of human-defined objectives.

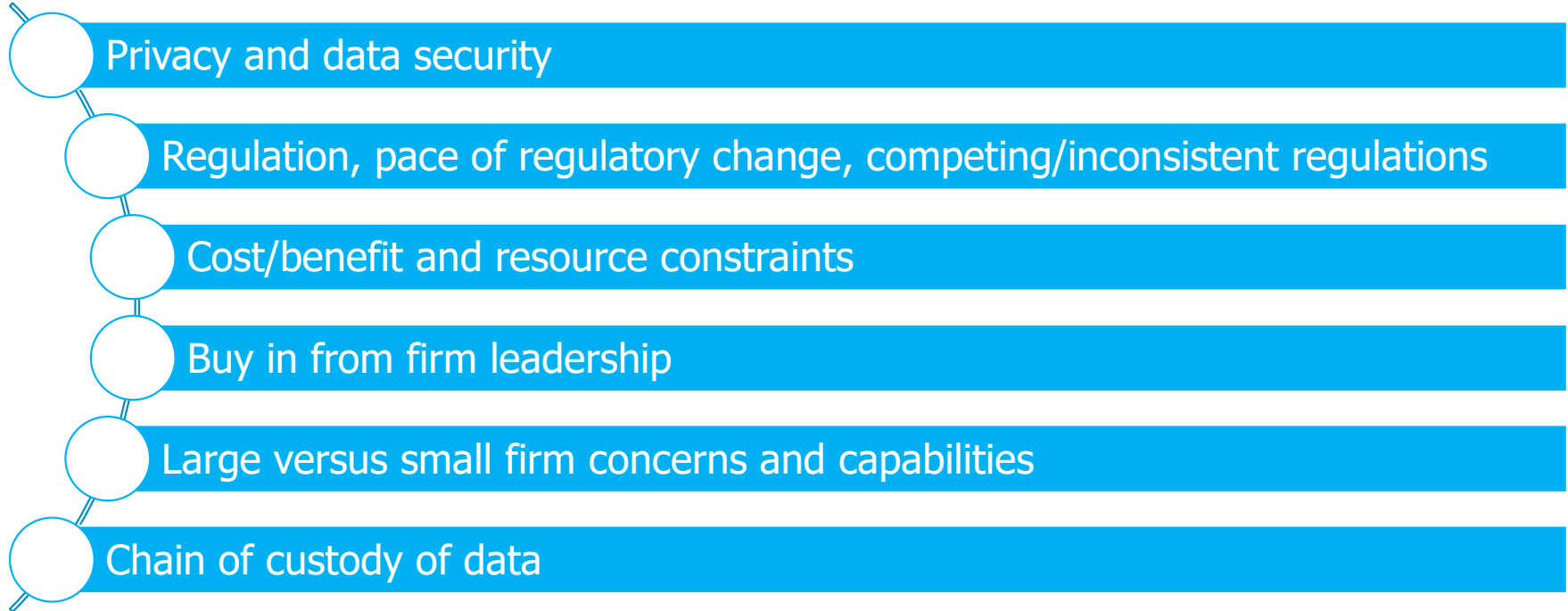AI models reach conclusions through reasoning and they self-correct to improve analysis.

AI programs may autonomously execute trading decisions or may assist staff in making trading decisions.

AI may include, but is not limited to, unsupervised machine learning, supervised machine learning, deep learning, reinforcement learning, natural language processing, and neural networks.

AI encompasses the idea of machines mimicking human intelligence, whereas (non-AI) computer algorithms are the specific instructions [from humans] that enable computers to perform tasks.

Algorithms are a component of AI, used to implement various AI techniques and approaches.

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AI Challenges

- Privacy and data security
- Regulation, pace of regulatory change, competing/inconsistent regulations
- Cost/benefit and resource constraints
- Buy in from firm leadership
- Large versus small firm concerns and capabilities
- Chain of custody of data

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AI Challenges

- AI technology monitoring, governance, risk management and error correction
  - Proper attribution, audibility, data security and integrity, and data provenance, including to address:
    - Training on incomplete, outdated, or unverified sources
    - Distortion, hallucinations and data poisoning
- Protection and confidentiality of firm and client information
- IP infringement

- Vetting of disclosures about AI use for precision, accuracy and balance
- Third-party risk management, including AI providers
- Business continuity plans
- AI-related cyberthreats
- AI risk-factor disclosures
- AI policies and procedures

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Regulatory Focus on AI in the US

- Presidential Executive Order on Safe, Secure, and Trustworthy Development and Use of AI (October 30, 2023)

- Treasury Report on Managing AI-Specific Cybersecurity Risks in the Financial Services Sector (March 2024)

- Treasury RFI on the Risks and Opportunities Regarding the Use of AI in Financial Services (June 2024)

- SEC
  - Proposed SEC rules on Predictive Data Analytics, Cybersecurity and Outsourcing
  - SEC Examinations Priorities Letter (2024) and exam sweeps (along with NFA) of AI use by regulated entities
  - SEC enforcement focus on "AI washing" by issuers, brokers and advisers
    - Settlements with Delphia (USA) Inc. and Global Predictions Inc. (March 2024)
  - SEC enforcement focus on technology governance generally

- CFTC Staff Request for Comment on the Use of AI in CFTC-Regulated Markets

- NIST, Artificial Intelligence Risk Management Framework (January 26, 2023)

- FINRA, Artificial Intelligence in the Securities Industry (June 2020)

- State Initiatives (e.g., New York DFS, Utah)

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AI (and non-AI) Opportunities

Cost to Produce

- ———————— +

Revenue Generation

Cost to Produce (vertical axis)

+

Internal – Proactive
- Preparing marketing leads
- Nudging cross-team collaboration
- Assisting portfolio management
- Summarizing prospects' status

External – Proactive
- Recommendations to clients
- Forming investment advice
- Driving substantive client interactions
- Tax advice and recommendations
- Analyzing account strength/weakness

Internal – Supportive
- Virtual assistants
- Internal data/knowledge management
- Trading and regulatory compliance tools
- Internal notetakers
- Meeting and deadline management

External – Supportive
- Chat bots and "Help" tools
- Smart investor onboarding solutions
- Improving investor admin experience
- Tax document support and delivery
- Account performance reporting tools

-

Business Risk (vertical axis)

+

-

Expense Reduction

- ———————— +

Business Risk

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