PUBLIC CITIZEN
215 Pennsylvania Avenue, SE • Washington, D.C. 20003 • 202/546-4996 • www.citizen.org

# Securities Artificial Intelligence Regulation Recommendations

This document lays out three areas where artificial intelligence (AI) presents threats to the United States' financial services sector and provides recommendations for securities regulators to consider in attempting to resolve these AI concerns. This is not an exhaustive list of concerns or remedies.

**Fiduciary Duty Concerns**: AI investment systems, which are sets of algorithms that conduct common brokerage firm/investment advisor duties such as providing investment advice to customers, may not always act in the best interest of the consumer. This may be due to the AI being inadvertently or purposefully designed to serve the best interest of its owner. This can result in upselling. Regulators should ensure that AI investment systems are held to the same standard as human investment brokers/advisors. Any AI investment system must act in the best interest of the consumer.

- <u>Proposed regulation fixes:</u>
  - **Redefine** the fiduciary duty to explicitly cover AI driven financial advice
  - **Mandate** the external review of black box data of AI investment algorithms to ensure the AI serves the best interest of investors and empower the SEC to prevent/punish the development/use of AI financial algorithms that don't serve the fiduciary interest
  - **Mandate** investment brokerages establish and publicly share their policies for identifying and eliminating conflicts of interest that may arise with their use of AI, such as an AI investment advisor upselling the value of a stock to a consumer's portfolio because a stock purchase would benefit the brokerage that provides the AI system

**Financial Systemic Stability Concerns**: Misused AI has the potential to damage our financial system. Inaccurate AI generated investment advice could impact systemically important companies' investment choices, or a pervasive deep fake could cause a run on the market that impacts the economy overall. Regulators should work to prevent AI from destabilizing our financial system.

- <u>Proposed regulation fixes:</u>
  - **Mandate** investment brokerages/advisors create a working group that shares intel and best practices on preventing/stopping AI driven dis/misinformation in the stock market
  - **Require** AI investment system models to be regularly externally audited for groupthink pattern biases to prevent AI models from "herding" investment analysts/institutional investors to making decisions that would critically damage our financial system

PUBLIC CITIZEN

215 Pennsylvania Avenue, SE • Washington, D.C. 20003 • 202/546-4996 • www.citizen.org

    - **Establish** high standards for data inputs/usage and cybersecurity in AI investment systems and require regular independent audits of these systems
    - **Raise** with FSOC that the next crash may be precipitated by an AI run by Big Tech. This invites financial regulatory scrutiny of technology firms

**Retail Investor Concerns**: Regulators should develop rules on AI and the investment customer experience to safeguard the interests of retail investors. As AI-driven technologies start to play a significant role in shaping broker-customer interactions and investment decisions, regulations are needed to prevent potential abuses, biases, or manipulations in AI-driven customer experiences. These regulations are necessary to build trust and provide a fair playing field to retail investors.

- Proposed regulation fixes:
    - **Mandate** any customer facing AI-driven investment products (AI investment chatbots, AI produced investment analysis, etc.) or AI-driven customer communications/solicitations be prominently labeled/disclosed as being AI for the purposes of ensuring customer trust and preventing deception, and this should include disclosures from any public company to the 10-K form of the use of AI technology.
    - **Explore** authorities that securities regulators may have to prevent public companies from using biased or inaccurate AI that might impact retail investments.
    - **Create** regulations that require companies utilizing AI investment systems to justify to regulators the methodology for why the investment AI recommends certain stock portfolios to retail investors

As stated before, the goal of this document is to identify problems regarding AI integration into our financial system and the impacts on the markets and investors, and to provide securities regulators with ideas on how to solve these problems. Regulators must act now to prevent the full integration of AI into our financial system without the appropriate guardrails.