

5 AI Risks For Corporate Boards To Examine

By **James Gatto and Tiana Garbett** (January 18, 2024, 5:52 PM EST)

The use of artificial intelligence is booming.

In the last year, AI chatbots, like Open AI's ChatGPT, have seen some of the fastest-growing user bases, with ChatGPT reaching over 100 million users only a few months after its launch. As of the end of 2023, it reportedly had over 180 million monthly users and 100 million weekly active users.

And that is just one of the many AI tools in the market.

Investors and companies are pouring cash into the space, and particularly into generative AI. Some companies are investing tens or hundreds of millions of dollars or more into generative AI.

Whether companies are building their own AI technology and training their own AI models, or leveraging third-party tools, there are significant legal issues and business risks that directors need to consider as part of their fiduciary obligations and corporate governance.

Five of the top issues to understand and consider are addressed in this article, but many other issues could arise.

A wave of litigation and enforcement actions has swelled. Boards should get educated on these issues and ensure appropriate policies and corporate governance are implemented to manage business and legal risks.

And the White House executive order on AI issued in October 2023 will likely result in additional agency actions, including potential rulemaking, agency guidance and increased enforcement over the next year.[1] This will require that companies continue to monitor developments and update their policies as new events occur.

1. Algorithmic Disgorgement

Many companies are sitting on a trove of customer data and realizing this data can be valuable to train AI models. However, what some companies have not thought through is whether they can actually use that data for this purpose. Sometimes this data is collected over many years, often long before a company thinks of using it for training AI.

One of the potential perils is that companies rush to launch a generative AI solution without proper planning, and the result is they are subject to algorithmic disgorgement. This is a remedy the Federal Trade Commission has imposed a number of times — e.g., for improperly using data to train AI models — that requires deletion of the data and the models and algorithms built using that data.

Algorithmic disgorgement can wipe out the entire value of those multimillion-dollar investments. This remedy can be imposed, even if the data was properly obtained, albeit without proper disclosure that it would be used for training AI models.

This is what happened to Everalbum Inc. and other companies. The FTC filed an administrative complaint against Everalbum in January 2021. Everalbum provided a photo album and storage application but used the customers' photos and videos for other purposes.



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Although the photos and videos were voluntarily uploaded by customers, Everalbum created new datasets, often without user permission, that it used to train its AI models to develop facial recognition technology for a different application. It also did not delete photos and videos from users who deactivated their accounts. The FTC **settled** with Everalbum for AI and privacy violations, with the result being algorithmic disgorgement — Everalbum had to destroy the data, algorithms and models.

Key Takeaway

Boards need to understand that generative AI is a data-intensive endeavor, and before it authorizes multimillion-dollar investments into a generative AI solution, it should make sure that the company has policies and procedures to ensure that it properly obtains the data needed and that it has the right to use the data as intended.

2. Tainting of Proprietary Software Developed With AI Code Generators

Software developers are increasingly using AI code generators, which are a powerful application of generative AI that assist developers by using AI models to auto-complete or suggest code. The AI models for these tools are typically trained on open-source software.

Open-source software is typically free to use, but that freedom is based on a license that accompanies the open-source software. Many licenses come with conditions that can lead to legal issues.

One of the most severe issues that can arise, which can devalue a company's investment in its software, is "tainting." Some open-source licenses require that any software that includes or is derived from any part of the open-source software must be licensed under the open-source license and the source code for that software must be made freely available.

This permits others to copy, modify and redistribute the software for free. This is an example of tainting. For companies that develop software planning to license it for a fee, this can be a showstopper and can cause inadequate return on the money invested in developing that software.

Many licenses come with other compliance obligations which also need to be managed.

Key Takeaway

Boards need to understand that while AI code generators offer tremendous assistance to developers, their use can cause tainting which can lead to significant loss on the investment in the software developed. All companies should have open-source policies.[2]

Even if your company has one, it needs to be updated to safeguard against tainting and other legal issues that can arise with AI code generators.

3. Inability to Obtain Intellectual Property Protection for AI-Generated Content

For companies that monetize content, strong intellectual property protection is needed to protect that content. While generative AI excels at cost-effectively creating new content, the problem is that the U.S. Copyright Office has published guidance that it will not register generative AI works because they are not human-authored.

That a user created the prompt to cause the output does not change the result because prompts typically are deemed to be ideas rather than expression, and copyright only covers expression.

The guidance further indicates that applicants must disclose the inclusion of AI-generated content in a work submitted for registration, briefly explain the human author's contributions to the work, and disclaim any AI-generated content that is more than de minimis.

Applicants who have already received registrations for works containing AI-generated material must check that the information provided to the Copyright Office adequately disclosed that material. If not,

they need to correct their information or risk losing the benefits of the registration. If the Copyright Office learns information essential to its evaluation of registrability "has been omitted entirely from the application or is questionable," it may take steps to cancel the registration.

Key Takeaway

Boards need to ensure that content-based businesses have effective policies in place that address when employees can safely use generative AI to create content, particularly when the company needs to ensure strong copyright protection for its content.

4. Loss of Valuable Trade Secrets

Employee use of public generative AI tools is ubiquitous. Many employees do not realize the inputs they enter into some tools are not confidential. Even worse, some generative AI tools' terms of use expressly grant the tool provider a license to use that input.

If the input includes trade secret or sensitive business information, this can lead to losing trade secrets or at least a diminution in the value of the information. Many employees routinely accept the terms of use without reading them, thus they are unaware that they are putting the company's valuable information at risk.

This is one compelling reason why all companies should immediately adopt a corporate policy on employee use of generative AI. One aspect of these policies involves a legal assessment of the terms of use for different generative AI tools and selective whitelisting of the tools that present less legal risk. Many other issues need to be addressed.

For example, the terms of use for some generative AI tools require the user to indemnify the tool provider if the tool generates content that infringes third-party IP. Conversely, some terms of use indemnify you if their tool produces infringing content for your employee.

These issues can extend beyond employee use. For companies that hire outside contractors to create content and other materials, it is important that your contractor agreements address issues with the use of generative AI tools on your projects. While many companies have well-drafted independent contractor or work-for-hire agreements that address the traditional issues that need to be covered under these arrangements, these agreements need to be updated to address some of the generative AI-related issues.

Key Takeaway

Boards need to ensure that their companies develop and enforce a corporate policy on employee and contractor use of generative AI to protect corporate assets and avoid unnecessary liabilities.

5. Avoiding Bias and Other Issues On the FTC's Watchlist

The FTC has been active in enforcements involving various AI-related issues, besides the Everalbum enforcement.

On Nov. 21, 2023, the FTC **authorized** the use of compulsory process for AI-related products and services. Through the omnibus resolution, set to take effect for 10 years, FTC staff will be able to readily issue civil investigative demands to require companies to provide documents, information and testimony in AI investigations.

In example of its active enforcements efforts, the FTC **instituted** an investigation into the generative AI practices of OpenAI through a 20-page investigative demand letter in July 2023.[3] The FTC also previously issued a report[4] to Congress in June 2022 warning about various AI issues.

The report outlines significant concerns that AI tools can be inaccurate, biased and discriminatory by design and can incentivize relying on increasingly invasive forms of commercial surveillance.

The report notes that AI tools can reflect biases of its developers that lead to faulty and potentially illegal outcomes, provides analysis as to why AI tools produce unfair or biased results and includes

examples of instances in which AI tools resulted in discrimination against protected classes of people or over-blocked content in ways that can reduce freedom of expression. It also addresses various other issues.

Boards' obligations to ensure their companies avoid bias is not just good corporate citizenship, it is necessary to avoid illegal conduct. Some companies are not aware of the potential for bias in generative AI tools, particularly if they rely on third-party tool providers. In such cases, companies often are not aware of the data on which these tools are trained and whether the data contains or results in biased or discriminatory results.

Examples of some of the FTC-related issues that companies should include in their generative AI-related corporate governance can be gleaned from the FTC's investigative demand letter to OpenAI.

Some of the AI-related topics about which the FTC asks include:

- What is the company's corporate governance model?;
- The accuracy and reliability of outputs generated by their products;
- How the company retains or uses information collected by users of the products;
- Disclosures and representations about their AI products;
- The data used to train its models, how it is obtained, the sources of the data, whether it is derived from public websites, the extent to which the company assesses or reviews the data and other data related questions;
- The individuals or departments responsible for training the models;
- The process and circumstances under which the company retrains their models, including to remediate hallucinations or the revelation of personal information;
- The policies and procedures the company follows to assess risk and safety before the company releases a new model or product based thereon, including the risks considered; and
- The policies and procedures relating to the privacy and security of personal information, including steps taken to prevent personal information from being used in training data or outputting personal information or false or disparaging information about a person, and how users or other individuals can opt out of having their personal information used, and more.

As should be apparent from these issues, a company should have appropriate policies and procedures in place to address these and other questions in the instance it faces an FTC investigation.

Key Takeaway

Boards need to be aware of the potential bias, discrimination, privacy and other issues that can arise

with generative AI tools and ensure the company develops proper safeguards to avoid these and other issues on the FTC's radar. These safeguards should be included in the corporate policies and governance on the use of generative AI.

Conclusion

Generative AI does not alter the fiduciary duties directors owe to their companies as traditionally understood.

The duty of care requires directors to take informed and deliberative actions based on all material information reasonably available. Directors have an obligation to inform themselves on the potential benefits and risks inherent with generative AI, so they can make responsible decisions.

Boards should be presented with information on the legal issues that can arise with generative AI to help inform them of the potential risks and to assist them in ensuring their companies adopt policies and governance that foster responsible use of generative AI while mitigating legal risks and waste of corporate assets.

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[1] Resource Guide for the White House Executive Order on Artificial Intelligence, <https://sites-sheppardmullin.vuturevx.com/69/2362/landing-pages/resource-guide-for-the-white-house-executive-order-on-ai-1123.pdf>.

[2] Open Source Software Policies – Why You Need Them And What They Should Include. <https://www.jdsupra.com/legalnews/open-source-software-policies-why-you-47053/>.

[3] FTC Investigative demand letter to OpenAI. <https://www.washingtonpost.com/documents/67a7081c-c770-4f05-a39e-9d02117e50e8.pdf>.

[4] FTC Report to Congress. <https://www.ftc.gov/reports/combating-online-harms-through-innovation>.