Navigating AI's Impact on Intellectual Property Law:

A Checklist for Negotiating AI Transactions

by Erica N. Goven

I. Introduction

Artificial intelligence (AI) technology is everywhere. It is deployed into the technology we use every day. However, the legal frameworks within intellectual property law have not kept pace with AI development.

Attorneys must stay up to date on AI developments and how to counsel clients in their adoption of AI to mitigate potential legal risks. This article provides (i) an introduction to negotiating AI provisions in contracts, (ii) a practice checklist on key issues when reviewing AI related agreements, and (iii) a glossary of commonly used AI terms to assist in negotiations with vendors. The outlined practice points in this article are drafted for the perspective of working from the vendor's agreement.

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II. Perspective for Review of AI Elements of Agreements

Agreements for the purchase or license of AI-enabled technologies require careful consideration and negotiation due to the unique risks inherent to such offerings. Attorneys will need to consider and draft unique contractual provisions to allocate risk between parties. As attorneys, we can best counsel clients in the negotiation of these contracts through a focus on understanding the unique aspects of the AI technology being licensed and the specific use case for which a client wants to procure a right to use the AI technology.

Helpful initial questions to ask when negotiating an agreement for AI-enabled technologies include:

(1) Does the product actually incorporate AI technology? Marketing materials and buzzwords used by a vendor in reference to AI does not always equate to actual incorporation of AI technology in the product.

(2) How will your client use the AI product?

(3) What data will be entered by your client into the AI product?

(4) What is your client's use case for the output from the AI product?

(5) Is the vendor using your client's data to train the AI model? If so, will the model be a closed AI model just for your client or a shared model

where the training benefits not only your client but also third parties?

III. Considerations for Negotiating AI Transactions

After establishing a baseline understanding of your client's use case, you should consider, discuss, and negotiate the following key issues to mitigate your client's risk in the adoption of AI products. While this is not a comprehensive list of items, the items are listed based upon typical order of topics addressed in agreements except indemnification and limitation of liability, which are discussed at the end of this section because these provisions are usually the last outstanding issues within a negotiation.

• **Due Diligence**. Given the speedy development of AI technologies, numerous vendors are offering AI products. However, many vendors have built their AI products on a handful of AI platforms, most notably, OpenAI (which has a strategic partnership with Microsoft). Given the rapidly evolving AI space, it is important to conduct basic due diligence on the proposed vendor to ensure the vendor is well capitalized and can meet its contractual obligations.

- Practice Point: Perform basic due diligence on the potential vendor. For example, request a Dun & Bradstreet report, perform a Google search, perform a brief investigation about the vendor and its investors, and ask basic questions about the vendor's capitalization and structure. Alternatively, your client may have a vendor management process already in place.

- Practice Point: Ask for the vendor's information privacy and security policies and procedures at the outset of negotiations, especially if the vendor will have access to personal information or other sensitive information.

• **Non-Static Terms**. AI technology is constantly changing and with it, vendors want to change the governing legal terms of a relationship quickly and unilaterally. Vendors will frequently propose click through agreements that can be updated at will by the vendor.

- Practice Point: Ideally, you will be able to negotiate static terms on behalf of your client, but if you are unable to obtain static terms, attempt to negotiate (i) a notification period for changes, or (ii) a termination and refund right if your client objects to changes. As a last resort, your client should set up a system for periodic review and risk assessment of the governing legal terms and any changes to the legal terms.

- Practice Point: If a static agreement includes web links to additional terms and the vendor is unwilling to remove the web links, attempt to mitigate the risk by ensuring the order of precedence within the agreement places any web linked terms at the bottom of the order of precedence.

• **Ownership, License, and Related Rights to Input and Output from AI Models**. To utilize AI products, typically, the user inputs prompts or instructions to the AI product, and the trained AI model provides output based upon the prompts or instructions. It is important that the underlying agreement between your client and the vendor clearly delineates the rights in input and the output.

- Practice Point: The agreement should clearly specify that your client owns all content input into the AI product. Title to inputs should remain with your client.

- Practice Point: Ideally, title to all output from the AI product is assigned to your client. This provides your client the broadest ability to use the output to support the client's business. If the vendor is unwilling to transfer title to the output, you should attempt to negotiate the broadest possible license rights for your client.

- Practice Point: Understand what licenses and rights your client is granting to the vendor. For

example, does the vendor retain a license to use your client's input and output, including the right to train the AI product? The scope of rights granted to the vendor will be dependent upon the client's specific use case, but the goal should typically be to negotiate the narrowest scope of rights possible to the vendor while still allowing the vendor to provide the AI product. However, vendors oftentimes include broad license rights to input and output.

• **Data Protection and Privacy Compliance**. Understand what type of data will be input into the vendor's AI product. There have been numerous claims against Generative AI vendors for failure to comply with applicable data privacy laws. The Federal Trade Commission even took steps in January of this year to remind vendors to uphold their privacy commitments.[1]

- Practice Point: If your client is inputting personal data, financial or payment information, or protected health information into vendor's AI product, additional provisions should be considered. Given the regulatory complexities of these issues, subject matter experts should be consulted.

- Practice Point: At minimum, ensure the vendor has an obligation to comply with all applicable laws, including applicable data protection laws and regulations and has adequate data privacy and security measures in place.

• **Insurance**. A vendor's indemnification and other contractual obligations are only as good as the vendor's ability to financially stand behind them. You should ensure the vendor has robust insurance coverage and contractually require the vendor to retain and provide proof of insurance coverage for the term of the relationship and a tail period. In particular, the vendor should have meaningful cyber liability and technology errors and omissions insurance.

• **Warranties and Metrics**. Marketing materials and a vendor's sales pitch could make significant claims about the features and functionalities of the vendor's AI product.

- Practice Point: Work closely with your client's business stakeholders to understand the business expectations of the vendor's AI product and attempt to include quantitative measurable performance metrics within the agreement so a failure to meet the requirements will provide your client remedies and/or a termination right. If the vendor fails to meet these agreed upon metrics, your client has a clear path toward terminating the relationship.

• **Internal Controls**. Upon the conclusion of the negotiation with the vendor, your client should ensure that it has internal mechanisms to properly educate the users of the AI product to ensure compliance with the agreed upon terms and mitigate potential risk. Risk mitigation could include ensuring that only authorized users are using the AI product, having internal controls to ensure the correct scope of data is being input into the AI product, and having a human review the output of the AI product.

• **Disclaimer of Warranties and Limitation of Liability**. Vendors will oftentimes include a broad disclaimer of warranties and a one-sided limitation of liability favoring the vendor. The use of AI product and the potential damages that could arise by your client's use of an AI products is broad and unpredictable (especially given the numerous lawsuits currently pending related to training of AI models), and vendors seek to minimize their risk via disclaimer and limitation of liability provisions within the agreement. These attempts can include

a complete disclaimer of the vendor's consequential-type damages and a one-sided cap on direct damages favoring the vendor at an amount your client paid for the AI product.

- Practice Point: If the vendor includes a broad disclaimer of warranties, propose an "except as otherwise provided for in the agreement" carve out. This will prevent a vendor relying on its general disclaimer of warranties if a vendor breaches an express warranty within the agreement.

- Practice Point: Attempt to negotiate a mutual exclusion of consequential-type damages and a mutual cap on direct damages.

- Practice Point: Attempt to negotiate a meaningful direct damages cap. Ask your client the direct financial impact if the vendor decides to stop providing the AI product or otherwise breaches the agreement and understand the amount your client is paying for the AI product. These should be helpful metrics to understand an appropriate direct damages cap. The direct damages cap should be set to at least an amount that will disincentivize the vendor from breaching the agreement.

- Practice Point: In addition, attempt to uncap (or agree upon a secondary super cap) certain items from the exclusion of consequential-type damages and direct damages cap (e.g., the vendor's intellectual property indemnification obligations, breaches of confidentiality and data privacy and security obligations, breaches of representations and warranties, gross negligence, violation of law, fraud, and willful misconduct).

• **Vendor Indemnification**. Ensure a robust intellectual property indemnification obligation is carved out of all limitation of liability caps. Vendors will attempt to not include or limit vendor intellectual property indemnification obligations. Though other vendor indemnification obligations should be considered, it is crucial, given the uncertain landscape of AI that the vendor provides a broad intellectual property indemnification to your client if the vendor's AI product or output infringes, violates, or misappropriates a third party's intellectual property.

- Practice Point: Ensure broad intellectual property indemnification protections. If not, your client could be responsible to defend and pay resulting judgements for your client's use of the vendor's AI Product.

- Practice Point: Carefully review the exclusions to the vendor's intellectual property indemnification obligations. If a vendor provides an intellectual property indemnification, vendors oftentimes include broad exclusions and carve outs for any types of modifications or combinations of the AI product with third party products. These exclusions to a vendor's intellectual property indemnification obligations sometimes swallow the entirety of a vendor's obligations. For example, the nature of most AI products requires the AI product be combined with input data as well as other systems like the internet and computer operating systems. If the vendor is excused from its intellectual property infringement obligations if the AI product is combined with any other third party product — the vendor can utilize this language to excuse itself from its intellectual property infringement obligations, even if the combination was unrelated to the infringement claim.

• **Client Indemnification Obligations**. In addition to vendors not including vendor indemnification obligations or proposing narrow obligations, vendors will attempt to shift risk to your client. Vendors will sometimes include broad indemnification obligations on your client covering all inputs placed into the AI product as well as any of your client's breaches of the agreement.

IV. Selected Terms of Art in AI

The below are selected terms which are frequently used in AI technology. Thes terms will hopefully assist during conversations and negotiations with vendors that provide AI products.

1. **Algorithm**: A step-by-step set of instructions that a computer must execute to solve a problem or execute a specific task.[2]

2. **Artificial Intelligence**:[3] (1) A branch of computer science devoted to developing data processing systems that performs functions normally associated with human intelligence, such as reasoning, learning, and self-improvement.[4] (2) Technology that enables computers and digital devices to learn, read, write, talk, see, create, play, analyze, make recommendations, and do other things humans do. It is a field which combines computer science and robust datasets to enable problem-solving.[5]

3. **Deep Learning (DL)**: Systems learn from large amounts of data to subsequently recognize and classify related, but previously unobserved, data. DL approaches have been used in systems across many areas of AI research, from autonomous vehicles to voice recognition technologies.[6]

4. **Generative AI**: Refers to deep-learning models that can take raw data — say, all of Wikipedia or the collected works of Rembrandt — and "learn" to generate statistically probable outputs when prompted. At a high level, generative models

encode a simplified representation of their training data and draw from it to create a new work that's similar, but not identical, to the original data.[7]

5. **GPT**:[8] Generative Pre-trained Transformer.

a. **Generative**: These models can produce or "generate" outputs — in the case of GPT, primarily text.

b. **Pre-trained**: Before being fine-tuned for specific tasks, the models undergo extensive training on vast datasets, learning language structures, facts about the world, and even some reasoning abilities.

c. **Transformer**: This is the underlying neural network architecture that the GPT models use. Transformers have revolutionized the field of machine learning due to their efficiency and capability to handle large datasets.

6. **Machine Learning**[9] **(ML)**: (1) An application of AI in which computers use algorithms embodied in software to learn from data and adapt with experience.[10] (2) A field of study with a range of approaches to developing algorithms that can be used in AI systems. AI is a more general term. In ML, an algorithm will identify rules and patterns in the data without a human specifying those rules and patterns. These algorithms build a model for decision making as they go through data. (You will sometimes hear the term machine learning model.) Because they discover their own rules in the data they are given, ML systems can perpetuate biases. Algorithms used in machine learning require massive amounts of data to be trained to make decisions.[11] There are three types of machine learning:

a. Supervised machine learning recognizes patterns within pre-defined data sets or training data.

b. Unsupervised machine learning recognizes patterns without known outputs or pre-defined data.

c. Reinforcement learning (RL) "rewards" the computer to create correlations.[12]

7. **Natural Language Processing (NLP)**: A field of Linguistics and Computer Science that also overlaps with AI. NLP uses an understanding of the structure, grammar, and meaning in words to help computers "understand and comprehend" language. NLP requires a large corpus of text (usually half a million words). NLP technologies help in many situations that include scanning texts to turn them into editable text (optical character recognition), speech to text, voice-based computer help systems, grammatical correction (like autocorrect or Grammarly®), summarizing texts, and others.[13]

8. **Narrow AI**: Intelligent systems for one particular thing (e.g., speech or facial recognition).[14]

Endnotes

1 https://www.ftc.gov/policy/advocacy-research/tech-at-ftc/2024/01/ai-companies-uphold-your-privacy-confidentiality-commitments.

2 https://www.bloomberglaw.com/external/document/XBN8DHMK000000/tech-telecom-glossary-artificial-intelligence-ai-terms-for-lawye.

3 Artificial Intelligence is said to have been coined in 1955 by John McCarthy, where he defined it as "the science and engineering of making intelligent machines."

4 https://csrc.nist.gov/Topics/technologies/artificial-intelligence#:~:text=artificial%20intelligence%20AI&text=%22(1)%20A%20branch%20of,learning%2C%20and%20self%2Dimprovement.

5 https://www.ibm.com/topics/artificial-intelligence.

6 https://crsreports.congress.gov/product/pdf/R/R46795.

7 https://research.ibm.com/blog/what-is-generative-AI.

8 https://community.ibm.com/community/user/ai-datascience/blogs/youssef-sbai-idrissi1/2023/08/09/understanding-gpt-models-a-deep-dive-into-generati GPT Models have been applied in numerous domains including, for example (i) Content creation: generating articles, poetry and stories, (ii) Coding: assisting developers by auto-completing code, (iii) Education: providing tutoring services, (iv) Entertainment: creating dialogues for video games and scripts for movies, and (v) Business: automating customer support with chatbots.

9 "The distinction between AI and ML is a subject of debate among computer scientists, but for purposes of their application in legal work, AI and ML are more or less interchangeable terms, with machine learning being more accurately descriptive of systems and processes currently in use." (https://www.bloomberglaw.com/external/document/XBN8DHMK000000/tech-telecom-glossary-artificial-intelligence-ai-terms-for-lawye).

10 https://jolt.law.harvard.edu/digest/a-primer-on-using-artificial-intelligence-in-the-legal-profession.

11 https://circls.org/educatorcircls/aiglossary#:~:text=Artificial%20Intelligence%20(AI)%3A%20AI,in%20the%20field%20of%20AI.

12 https://www.bloomberglaw.com/external/document/XBN8DHMK000000/tech-telecom-glossary-artificial-intelligence-ai-terms-for-lawye.

13 https://circls.org/educatorcircls/aiglossary#:~:text=Artificial%20Intelligence%20(AI)%3A%20AI,in%20the%20field%20of%20AI.

14 https://hai.stanford.edu/sites/default/files/2020-09/AI-Definitions-HAI.pdf.