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SILICON VALLEY FIRST CUP OF COFFEE SEMINAR SERIES

UPCOMING SEMINARS:

Artificial Intelligence (AI) Boot Camp

January 12	Computer-Implemented Inventions in Biotechnology and Healthcare, Patentability from European and US Perspective
January 13	M&A and Investment into AI Companies
January 19	AI in Healthcare, An Overview of Key FDA Policies and Developments
January 20	Patent and Trade Secret Protection for Inventions That Use AI
January 21	AI in Hiring and Recruiting
January 28	AI and Copyright

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UPCOMING SEMINARS:

Artificial Intelligence (AI) Boot Camp

February 2	The Ethics of Artificial Intelligence for the Legal Profession
February 3	AI and Data Privacy
February 4	Patents for Medtech AI: Opportunities and Pitfalls
February 9	IP Landscape of AI Hardware Startups
February 10	The Risks of Bias and Errors in AI-Enabled Decision-Making
February 11	AI in Digital Advisory Offerings: Regulatory Considerations
February 16	Bias Issues and AI

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M&A INVESTMENT INTO AI COMPANIES

Tony Chan, Robert C. Bertin, and Andrew J. Gray IV

January 13, 2021

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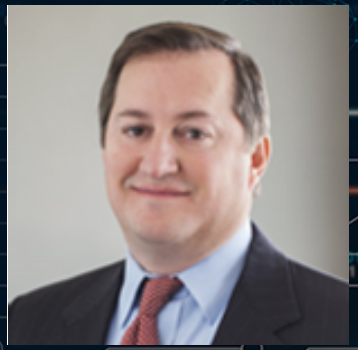
Presenters

Tony Chan



Robert C. Bertin

Andrew J. Gray IV

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What is AI?

- Technology that simulates human intelligence
  - Analyze data to reach conclusions about it, find patterns, and predict future behavior.
  - Learn from data and adapt to perform certain tasks better over time.
- Algorithms (sets of code with instructions to perform specific tasks) that makes predictions

Executive Order on AI

- On February 11, 2019, President Trump announced the "American AI Initiative" which is "a concerted effort to promote and protect national AI technology and innovation."
- It directs Federal agencies to "pursue a multipronged approach to advance AI, including: promoting sustained AI R&D investment, enhancing access to high quality cyberinfrastucture and data, removing regulatory barriers, ensuring that America leads in the development of technical standards for AI, providing education and training opportunities to prepare the American workforce for AI and implementing an action plan to protect our technological advantage in AI."

How does AI Work?

- AI works by combining large amounts of data with fast, iterative processing and intelligent algorithms, allowing the software to learn automatically from patterns or features in the data.
- Not "AGI"
- Based on data and training
- Many different varieties

Types of AI

- Algorithm and data driven
- Computer Vision
- NLP
- Neural Networks
- Machine Learning
- Supervised Learning
- Unsupervised Learning
- Reinforcement Learning
- Deep Learning

How is it different?

- Auditability/Transparency (“Black Box”)
- Bias/Discrimination
- Vaporware
- Regulatory Compliance
- Reputational Risk
- IP Ownership
- Data Privacy/Training Data
- Cybersecurity
- Liability

FTC Guidance

- On April 8, 2020, the FTC issued guidance in its Tips and Advice blog on how organizations can manage consumer protection risks that arise from artificial intelligence use, emphasizing that AI algorithms should be:
  - Transparent;
  - Explainable;
  - Fair;
  - Empirically sound; and
  - Foster accountability.

Fairness

- The blog post focused on fairness and accountability and stressed the following items:
  - Don’t discriminate based on protected classes.
  - Focus on inputs, but also on outcomes.
  - Give consumers access and an opportunity to correct information used to make decisions about them.
  - Ask questions before you use the algorithm.
  - Protect your algorithm from unauthorized use.
  - Consider your accountability mechanism.

How is AI used?

- How does the target utilize AI?
  - Offer as a standalone product, service or license
  - Offer as part of a larger offering, including integrated with hardware
  - Internal Uses
    - Part of product or service development
    - Compliance
    - Other functions (Sales, Marketing, Analytics, Customer Support, HR, etc.)
- "Off-the-Shelf" solutions
- Need to understand scope in order to develop diligence plan, representations and warranties and gauge risks.

AI Companies

- Cloud Providers
  - AWS
  - Google Cloud
  - IBM Cloud
  - MSFT Azure
- Robotics and Hardware
  - Tesla
  - Pony.ai
  - Nvidia
  - Amazon
  - Apple

AI Companies

- SaaS Model
  - Sift
  - Salesforce
  - HyperScience
- Healthcare
  - Flatiron Health
  - Watson
- Research
  - OpenAi
  - Deepmind

Types of Transactions

- Investments
  - Minority
  - Majority
- Licenses
  - Exclusive
  - Non-exclusive
- Partnerships and JV’s
- M&A

Applicable Laws

- Regulated Industries (Banking, Financial Services, Healthcare, etc.)
- Data Protection and Privacy, GDPR/HIPAA
- Consumer Protection Laws
  - Fair credit reporting
  - Equal opportunity
  - Fair trade practices
- Anti-Discrimination
- Anti-Competition Laws
- IP and Copyright Laws
- Trade Secrets Act
- Local Laws (e.g., Facial Recognition Restrictions)
- CFIUS
- Export Controls

Diligence

- Code Audit/Open Source
- IT Audit
- IP/Ownership
- Training Data
- Licenses
- Warranties
- Product Liability
- Data Protection and Privacy
- Compliance with Laws
- Insurance

Representations and Warranties

- Definition of AI
- Scope of AI Usage (Products, Services, etc.)
- IT Systems and Cybersecurity
- Data Protection and Privacy
- Ownership of IP and Improvements
- Licenses
- Compliance with Laws
- Training Data
- Transparency
- Accountability/Bias

IP

- IP Diligence In AI is largely driven by the reasons for the Transaction:

    1. To acquire innovative technology.

    2. To access or use proprietary data that may not be available through licensing.

    3. To acquire talent that may be difficult to grow internally or bring in on a piecemail basis.

- Use an integrated technical and commercial diligence team.
- Might need product managers, data scientists, technologists, and IT experts on the team for AI diligence.
- Diligence checklists are a good idea.

IP – Acquiring Innovative AI Technology

- How material is IP to the target company's business/AI Technology?
    - Determines the level of detail for the diligence and areas of focus.
    - Does the IP provide a competitive advantage?
        - Identify the IP assets (patents, copyrights, software, data)
        - Are there commercially available alternatives?
        - Does the company own or license its IP, what is its provenance?
        - Review IP – related agreements, including out-licenses, in-licenses, R&D agreements, employment and consulting agreements.

IP – Acquiring Innovative AI Technology

- Has or will a University be involved in the transaction?
  - Look at role of the University or professor involved in the development of the technology.
    - Get a copy of the University's IP policy.
    - Was any federal funding used to develop the IP?
  - Will the University or professors continue to be involved?
  - What steps can be taken to clarify IP rights from future collaboration?
    - Might need a three way agreement with target and University
- Is Detailed Software or Patent Diligence Required?
  - Open source vs proprietary software.
  - Patent coverage of target's products and competitor's products.

IP – Acquiring Innovative AI Technology

- Does the technology operate in an ethical manner?
  - Consider IEEE and European Commission guidance on AI ethics.
    - Consider:
      - Compliance with privacy laws and regulations
      - Interpretability, transparency and accountability of the AI system
      - Biases, diversity, fairness
      - Well being of people that will interact with the AI from legal, policy and health and wellness perspectives
      - Embedded values within autonomous and intelligent systems
      - Societal and environmental well-being
- Reps and warranties covering ethical considerations tailored to the AI system should be included in addition to more routine reps and warranties.

IP – Acquiring Data Used in AI Transactions

- Often the value of an AI Player has more to do with the data used to train the AI system than the AI technology itself.
  - Do not underestimate the value of the data in AI systems.
  - Consider the sources of the data.
    - Does the target have lawful access to or ownership of the data?
    - Does the target have any necessary licenses or consents to use the data?
    - Are there any embedded privacy issues associated with using the data by the company now, after the transaction is completed, or given the way in which the data or AI system may be used in the future?
    - Copyrights in images, audio, and text can potentially be implicated depending on the AI system
- Robust reps may be needed with respect to the data if the value of the data is high and verification of its provenance is difficult to ascertain.

IP – Acquiring Talent in AI Transactions

- Who are the key players at the AI Target?
  - Get them involved in the diligence process to answer technical and ethical questions.
  - Did they have prior employers?
    - Look at prior employment and non-compete agreements.
    - Do they have any prior confidentiality agreements that may limit the scope of their activities after the acquisition?
    - Are there any restrictions that will prevent them from being productive on the acquiring company's team?
- Are any key players not part of the deal?
- Do any founders or third parties own IP that is essential for the company outside of the target being acquired?

Post-Closing

- Integration
- Retention of Key Employees
- Transparency/Interpretability
- Assistance with Regulatory Inquiries
- Documentation
- Confidentiality
- Non-Compete
- Protection of Code/Models

Conclusion

- Raises many of the same issues as software and Saas companies, but some notable differences
- Proliferation of AI "enabled" or "enhanced" products/services
- Imperfect fit as existing legal paradigms are applied to novel technologies
- Investors and advisors to understand the legal issues implicated, especially as:
  - Underlying technology continues to develop;
  - Lawmakers and Regulators seek to address issues raised by the technology;
  - Companies continue to deploy or implement AI solutions

Coronavirus COVID-19 Resources

We have formed a multidisciplinary **Coronavirus/COVID-19 Task Force** to help guide clients through the broad scope of legal issues brought on by this public health challenge.

To help keep you on top of developments as they unfold, we also have launched a resource page on our website at **www.morganlewis.com/topics/coronavirus-covid-19**

If you would like to receive a daily digest of all new updates to the page, please visit the resource page to **subscribe** using the purple "Stay Up to Date" button.

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Biography

Tony Chan
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Tony Chan is the leader of the firm's interdisciplinary corporate practice in Washington, DC, where he advises clients on public and private company mergers and acquisitions (M&A), private equity, growth equity, and venture capital transactions, as well as on corporate governance, joint ventures and corporate finance. Tony's clients include global strategic buyers and sellers as well as financial sponsors and their portfolio companies in the life science, healthcare, investment management, technology, and video game sectors. He also regularly advises on complex international and cross-border transactions.

Biography

Robert C. Bertin
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Rob Bertin has over 20 years of experience negotiating transactions involving IP, litigating patent, trademark, trade secret and copyright cases throughout the United States, and counseling clients on intellectual property (IP). He has represented clients at the center of some of the largest patent portfolio sale and licensing events in the high tech industry and leverages a technical background to represent large and small companies on IP issues.

Biography

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Serving as the leader of Morgan Lewis's semiconductor practice and as a member of the firm's fintech and technology practices, Andrew J. Gray IV concentrates his practice on intellectual property (IP) litigation and prosecution and on strategic IP counseling. Andrew advises both established companies and startups on Blockchain, cryptocurrency, computer, and Internet law issues, financing and transactional matters that involve technology firms, and the sale and licensing of technology. He represents clients in patent, trademark, copyright, and trade secret cases before state and federal trial and appellate courts throughout the United States, before the US Patent and Trademark Office's Patent Trial and Appeal Board, and before the US International Trade Commission.

Our Global Reach

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Asia Pacific
Europe
Latin America
Middle East
North America

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Frankfurt
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Hong Kong*
Houston
London
Los Angeles
Miami
Moscow
New York
Nur-Sultan
Orange County
Paris
Philadelphia
Pittsburgh
Princeton
San Francisco
Shanghai*
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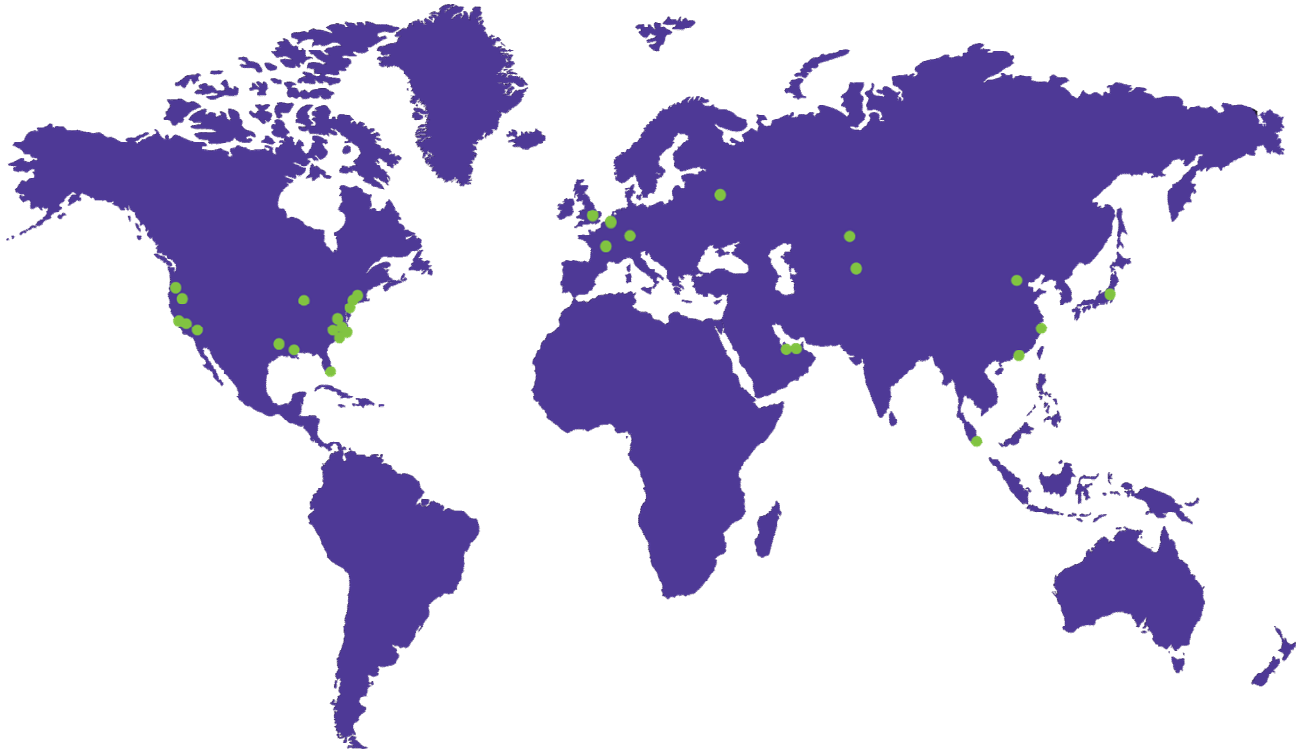

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