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Fiduciary Duty Considerations For Boards Of Cos. Using AI

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January 3, 2020, 3:44 PM EST

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In an era of rapid development and deployment of artificial intelligence technologies, we stand witness to new, reactive regulation of key elements of these technologies, such as the California Consumer Privacy Act, or CCPA, effective this month. This comes in parallel with assertions by many corporate leaders that the proper focus of corporate purpose is the interests of employees, customers, suppliers, shareholders and society in general, rather than sole primacy of current shareholder interests.[1]

Companies' increasingly omnipresent use of AI technologies[2] as part of a product or service offering, or as a means to optimize operations, has correspondingly increased AI's importance to corporate strategic planning and governance.[3]

AI applications have also created new risks, adversely affecting companies' reputations and relationships with their workforce, from litigation attacking biased outputs of AI algorithms,[4] to a crowd-created discriminatory chat bot,[5] to protests against a newly constituted AI ethics board that was consequently disbanded.[6]

Recent shareholder proposals are calling upon boards to ensure proper AI governance, such as a shareholder proposal at Google Inc. calling for board-level oversight of AI technology through a "societal risk oversight committee."[7]

These developments have implications for the board oversight required for corporate activities involving AI, including quickly evolving regulatory schemes affecting AI deployment, such as the CCPA, which affects the collection and use of data often used for these technologies.

Yet, studies show that information technology expertise continues to be a vastly underrepresented boardroom skill,[8] and some companies still have no defined process for managing technology risk.

Within this landscape this article discusses why, and what considerations involving AI are likely to be important for the effective discharge of fiduciary duties by a board of directors.

Why It Matters

Directors of Delaware corporations are required by state corporate law to fulfill duties of loyalty and care. This includes the duty to exercise oversight over corporate risks. Judicial deference to board decisions, when challenged, is predicated on the board's acting and making decisions in good faith, informed by material facts and considerations relevant to the matter, and exercising their judgment on that basis.

Recent cases in Delaware reinforce the need for the board to actively engage in oversight, understand key risks, and establish and monitor a compliance program designed to produce information for reporting. Indeed, devotion of board attention to, and reporting and discussion of specific legal, regulatory and financial compliance and other considerations of AI may be critical.

When material, summaries of compliance reports should be provided to boards "on a consistent and mandatory basis," establishing a "board-level system of mandatory reporting."[9]

In addition, the current focus on stakeholder corporate governance to best serve corporate viability and long-term success would involve accounting for the interests of relevant stakeholders, including consumers, employees and the public, as well as shareholders.[10]

In light of these multifaceted expectations of boards, directors face additional pressure where employees or consumers oppose uses of AI technologies, such as as instance where employees of a large technology company demanded cancellation of a contract with the U.S. Army to supply augmented reality headsets for soldier training.

Board members should be prepared for AI technologies to affect their considerations not solely in respect of shareholders, but more broadly in light of various stakeholder interests.

What to Address

As a starting point, oversight should involve a strategy-level discussion to develop an initial understanding of certain AI-relevant subjects. For example, use and development of AI technology can be affected by various areas of law, including product liability, advertising concerns, unfair competition and sector-specific concerns, such as healthcare and fintech regulation.

Thereafter, significant changes or developments should be periodically reported to and reviewed by the board either directly or through an appropriate committee and subject to controls and processes to facilitate effective management. In such process, boards would consider the following:

AI's Disruption of the Industry and Company Model

The foundational inquiry is the current and potential impact of AI on a company — how it can transform or threaten its business model, and what related developments and general landscape exist in the sector in which the company operates driving this impact. For many companies, AI may not be fundamental to the current core business model, but important to optimizing performance.

While many companies use AI in their products and services — seen with advertisers and news aggregators — others are finding the use of AI to help internal operations become more efficient and intelligent.

For example, use of AI can streamline workforce roles, make operations safer for employees and users, find efficiencies to reduce spending, and augment information for board decision-making. Of course, attendant risks accompany adopting AI, some of which are further discussed below.

Privacy, Cybersecurity and Other Changing Regulations

Use of AI exacerbates the board's oversight responsibilities from a legal, regulatory and policy perspective due to the mere fact that AI requires significant amounts of data.[11]

Acquisition or use of data for AI requires understanding from where the data is derived (e.g., from the individual directly, reliable or unreliable third parties, etc.), what rights the company has to use the data, with whom the company shares the data, and how the data is secured, particularly if the data contains personal information.

And recent legislation is requiring businesses to heed these requirements, threatening steep penalties for noncompliance. For example, the General Data Protection Regulation, or GDPR, and the CCPA both require significant compliance efforts from companies collecting personal data, including for user control and data security purposes.[12]

The CCPA grants consumers a private right of action, with monetary penalties, for certain breaches of personal data, exposing a company to significant liability. In addition, the GDPR subjects wholly automated decision-making technologies that will result in a legal effect on the person to defined limitations.

Exercising sufficient oversight in light of these regulations where they meaningfully impact a business starts with receiving a report from the business detailing the data used for the AI technology, how it is used, where it originates, with whom it is shared, how such data is managed, secured, and assessed from a risk standpoint, and whether meaningful human involvement is incorporated into decisions made by AI.

Because of the constantly changing legal and regulatory environment (including in the realm of privacy and cybersecurity), investment, use or development of new AI technology can engender significant risk.

As government bodies consider whether and when to regulate AI — from temporarily banning facial recognition technology in law enforcement body cameras, to a newly proposed framework for AI and machine learning medical devices from the U.S. Food and Drug Administration[13] — boards should consider this dynamic regulatory environment while determining corporate risk tolerance, and be comfortable that the company is well prepared to adapt as circumstances change.

Resource and Talent Management

Use of AI will likely affect the size and composition of the corporate workforce, with some human-performed functions being replaced, and will often require adjusting, reskilling or upskilling talent. In these cases, investment in dedicated support from ancillary engineering, legal, compliance, ethics and risk management departments also will be necessary.

Board talent management similarly is significant.[14] Boards should periodically evaluate the skills of current and prospective board members, and consider whether the board includes members who have the technical facility to understand and raise concerns regarding the implementation, development and use of the AI and other relevant technologies.[15]

Whereas financial, legal and business acumen were key considerations of the past — and still should be — fluency in technology, cybersecurity and privacy represent skills of increasing importance for boards now and in the future.[16]

Ethics of Use of AI

There are, of course, ethical risks relating to replacement of the human workforce, but boards should understand that there is also a significant concern that automated decision-making can drive and augment biased outcomes,[17] particularly related to protected classes.

Examples of problematic and unexpected outcomes could include loan approval algorithms based on zip codes that disparately impact individuals of certain demographics, or where a credit card limit that appears to be biased based on gender offers women a lower credit limit than their husbands.

Boards should inquire whether the company sufficiently investigates use of the right data sets, employs bias-eliminating technology, closely monitors outcomes and remediates potential issues as needed. Discussion of inevitable unknowns and risks should be identified and presented to the board ahead of potential escalation in the public eye, and ongoing periodic reports from the business on risk-avoidance procedures employed will help the board execute this key oversight function to support corporate ethical integrity.

Messaging and Transparency

For a multitude of reasons — including consumer and stakeholder concern, and regulatory requirements on the one hand, and protection of confidential company information on the other — boards should

understand and consider the chosen level of transparency internally and externally regarding the company's AI use.

In light of the common expectation that AI will displace or shift many workers, and in anticipation of ethical fears, communication of the purpose and use of the AI will be important to a company's workforce. And customers, business partners and employees are understandably concerned that personal data may be accessed and misused or compromised.

Transparency and explainability of algorithmic decisions can ameliorate concern regarding biases and decision-making processes in AI, but this must be balanced with the black-box nature of various AI programs, and the need to protect intellectual property rights, including trade secrets.

Offering a legally compliant privacy policy and/or assuring that the company will abide by general privacy principles may be first steps toward striking this balance.

Concluding Thoughts

Beyond managing legal risks, development and use of AI requires a mindset that encompasses maintaining the trust of consumers, employees and other stakeholders, while supporting the long-term value of the corporation for its shareholders.

As the evolution of digital technology, cybersecurity and AI may define the opportunities, risks and needs of the company, so shall the board need to be informed of, and provide active oversight over the company's AI development and use.

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[1] See, e.g., World Economic Forum, "Davos Manifesto 2020: The Universal Purpose of a Company in the Fourth Industrial Revolution," Dec. 2019, available at http://www.wlrk.com/docs/weforumorgDavosManifesto2020TheUniversalPurposeofaCompanyinthe FourthIndustrialRevolution.pdf; "Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans,'" Aug. 19, 2019, available at https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans; Eduardo Gallardo, "On an Expansive Definition of Shareholder Value in the Boardroom," The CLS Blue Sky Blog, Oct. 22, 2019, available

at https://www.gibsondunn.com/wp-content/uploads/2019/10/Gallardo-On-an-Expansive-Definition-of-Shareholder-Value-in-the-Boardroom-CLS-Blue-Sky-Blog-10-22-2019.pdf.

[2] Per PWC Governance Insights Center, AI is an umbrella term for "smart" technologies that are aware of and can learn from their environments. Robotic process automation (RPA), machine learning, natural language processing and neural networks all incorporate AI into their operations.

[3] Indeed, references to AI in SEC risk factor disclosures for public companies have grown exponentially — from almost none in 2016 to more than 80 in 2019 — reflecting AI's broadening material impact on business risks and even entire business models.

[4] Thomas Beardsworth and Nishant Kumar, "Who to Sue When a Robot Loses Your Fortune," Bloomberg, May 5, 2019, available at https://www.bloomberg.com/news/articles/2019-05-06/who-to-sue-when-a-robot-loses-your-fortune.

[5] Daniel Victor, "Microsoft Created a Twitter Bot to Learn From Users. It Quickly Became a Racist Jerk," NY Times, March 24, 2016, available at https://www.nytimes.com/2016/03/25/technology/microsoft-created-a-twitter-bot-to-learn-from-users-it-quickly-became-a-racist-jerk.html.

[6] Jillian D'Onfro, "Google Scraps Its AI Ethics Board Less Than Two Weeks After Launch In The Wake Of Employee Protest," Forbes, Apr. 4, 2019, available at https://www.forbes.com/sites/jilliandonfro/2019/04/04/google-cancels-its-ai-ethics-board-less-than-two-weeks-after-launch-in-the-wake-of-employee-protest/#40f183776e28.

[7] https://www.fnlondon.com/articles/shareholders-quiz-google-on-ai-risks-20190618?mod=hp_LATEST.

[8] Agenda, "CIOs: Boards Don't Get IT" by Amanda Gerut, August 13, 2018.

[9] E.g., Marchand v. Barnhill, 212 A.3d 805, 813 (Del. 2019).

[10] Business Roundtable Statement on the Purpose of a Corporation, August 2019.

[11] Even more directly, in Singapore, the board has been liable for cybersecurity breaches, as an extension from the principle that it is responsible for the governance of risk. https://www.lexology.com/library/detail.aspx?g=e8e0c6b8-d81a-4dfc-a8fe-36a1dd3baa54.

[12] Rachel Metz, "California lawmakers ban facial-recognition software from police body cams," CNN Business, Sept. 13, 2019, available at https://www.cnn.com/2019/09/12/tech/california-body-cam-facial-recognition-ban/index.html.

[13] Food & Drug Administration, Proposed Regulatory Framework for Modifications to Artificial

Intelligence/ Machine Learning (AI/ML)-Based Software as a Medical Device (SaMD), at 2 (2 April 2019), available at https://www.fda.gov/media/122535/download.

[14] Boards should ensure that the company is sufficiently staffing not just the brains behind the AI, but also risk managers for AI-related risks, to help moderate issues from the ground up. An "ethical AI by design" program may be important.

[15] https://www.law.com/corpcounsel/2019/12/06/general-counsel-must-come-to-grips-with-artificial-intelligence/?kw=General%20Counsel%20Must%20Come%20to%20Grips%20With%20Artificial%20Intelligence&utm_source=email&utm_medium=enl&utm_campaign=weekendroundup&utm_content=20191208&utm_term=cc; European Community, Seven Essential Guidelines on ethics for AI; OECD Guidelines on the Protection of Privacy and Transborder Flows of Personal Data, available at https://www.oecd.org/internet/ieconomy/oecdguidelinesontheprotectionofprivacyandtransborderflowsofpersonaldata.htm.

[16] Chenxi Wang, "Corporate Boards Are Snatching Up Cybersecurity Talents," Forbes, Aug. 30, 2019, available at https://www.forbes.com/sites/chenxiwang/2019/08/30/corporate-boards-are-snatching-up-cybersecurity-talents/#491df65a479f.

[17] See, e.g., Bernard Marr, "Artificial Intelligence Has a Problem With Bias, Here's How to Tackle It," Forbes, Jan. 20, 2019, available at https://www.forbes.com/sites/bernardmarr/2019/01/29/3-steps-to-tackle-the-problem-of-bias-in-artificial-intelligence/#1dba77917a12.