

ARTIFICIAL INTELLIGENCE AND M&A DUE DILIGENCE

CURRENT TRENDS

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1. INTRODUCTION

The purpose of this paper is to provide a brief overview of the use of artificial intelligence (AI) in M&A due diligence.

AI is [t]he theory and development of computer systems able to perform tasks normally requiring human intelligence, such as visual perception, speech recognition, decision making and translation between languages (Oxford English Dictionary). Central to AI is the ability of a computer to carry out human tasks. Does this mean that lawyers will be replaced by computers? Today, the answer must be negative and this is not likely to change in the future. However, there are certain advantages in the use of AI that could help us to improve our efficiency as lawyers.

This explains why the use of AI is increasing in the legal profession. Essentially, clients demand more legal services in a reduced period of time and are willing to pay less fees for low-value added services. AI becomes an opportunity to increase competitiveness and that is why it is now frequent to be asked “*is your firm using AI?*”.

Corporate clients are also aware of the benefits of AI, as they are using it in other areas, including document management and extraction of information (*e.g.*, big data). Therefore, they expect that law firms use AI to render more efficient services.

2. ARTIFICIAL INTELLIGENCE AND M&A DUE DILIGENCE

One of the areas where AI has proven to be useful in the legal profession is M&A due diligence.

In M&A transactions, due diligence has several goals: understand the target’s business, identify and allocate potential risks, design and use risk-protection mechanisms (representation and warranties, insurance, specific indemnities, escrows, etc.), etc.

To achieve these goals, lawyers need to review hundreds of documents. This process is burdensome and tedious (on average, a virtual data room in an acquisition contains more than 35,000 pages¹), but has evolved to gain more efficiency over the years. For example, we have moved from physical data rooms, where many lawyers spent hours reviewing documents in a room with limited capacity and opening hours, to virtual data rooms, where multiple teams can work at the same time with no physical limitations (no closing times, no need to travel, access to a certain document by various lawyers at the same time, etc.).

However, over the years, more challenges appeared: multi-jurisdictional deals, larger targets with more employees, complex legal environments. All of these factors result in increased costs.

How can AI help in the M&A due diligence process? AI currently assists in identifying, classifying, organizing, prioritizing and highlighting documents that are relevant in the context of the transaction in a more effective (time) and efficient (cost) manner.

From the target/seller's standpoint, AI can be used in two different phases of the transaction:

- Gathering documents for the due diligence exercise: AI can assist in categorizing and gathering documents that will be later uploaded to the virtual data room.
- Disclosure schedules: AI would classify documents that should be listed on the disclosure schedules of an SPA in order to limit the seller's liability.

Turning to the purchaser, since software is currently able to automatically read, interpret and extract key information that may be useful, AI can assist in reviewing documents and highlighting and categorizing potentially relevant provisions.

AI can also be used in managing and streamlining the due diligence process. AI can assist in reviewing near-identical documents and can help identify the differences between them, which will also allow to classify the documents according to different categories. In areas where a large number of similar documents appear (for example, human resources), AI allows to conduct a full review of those, avoiding sampling. AI can also automatically detect language, thus allowing to engage outside counsel from other jurisdictions at an earlier stage.

¹ Intralinks and M&A Research Centre at Cass Business School, *When no one knows: Preannouncement M&A activity and its effect of M&A outcomes*, 2013 p. 11.

Finally, AI is also useful to identify anomalies, when a particular document deviates from a pattern or from the market standards.

3. RISKS RESULTING FROM THE USE OF AI IN M&A DUE DILIGENCE

AI could help to automate the due diligence process, leading to cheaper and faster transactions that are managed more efficiently. However, the use of AI implies certain risks:

- The main risk is liability. AI can help to analyze in a more efficient manner standard and unambiguous terms in agreements (*e.g.*, the boilerplate). The review of ambiguous and not highly standardized terms requires further training of the system and may result in overlooking documents or provisions or in their misinterpretation. This may be caused by a failure in the software (*i.e.*, the algorithm) or by an insufficient training of the program. The firm is obviously exposed to liability, but could the software manufacturer be liable too?
- By using AI, the firm could be the subject of cyber attacks, which may expose sensitive and confidential information.
- In certain jurisdictions, it could also be questioned whether the use of AI may affect the attorney-client privilege.

Law firms should also be conscious of the implications that the use of AI has. Latest developments in AI result in a computer being able to digest large amounts of information, learn from it and apply knowledge. But for this to happen, two elements are required: a model and human training that results in machine learning. Therefore, firms willing to use AI in rendering their legal services need to be ready to invest not only in the software, but also in the human resources that are required to train and develop such software and in the training that the firm's lawyers require to use the software.

4. CONCLUSIONS

- Considering its current development status, AI can be certainly used to improve and streamline M&A due diligence processes.
- However, AI should be regarded as a tool, not as a substitute of lawyers. We are not yet in the legal-robot era.

- Law firms should be mindful of the risks that the use of AI in rendering legal services implies. Of particular concern is the liability in which a law firm may incur as result of malfunctions of the systems or misinterpretations of their findings.
- AI is intense in the use of capital and human resources. Firms should be ready not only to spend money in the software, but also to have available the human resources that the use of AI requires.

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