AI: Its impact on procurement and contract management

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Introduction

In the spirit of reconciliation, Sparke Helmore acknowledges the Traditional Custodians of the country throughout Australia and their connections to land, sea and community. We pay our respect to their Elders past and present and extend that respect to all Aboriginal and Torres Strait Islander people today.

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Presentation agenda

1. The AI revolution
2. Common misconceptions
3. Risks and harms of AI
4. National response to AI
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7. Voluntary AI Safety Standard
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13. AI drafting examples
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The AI revolution

We … have a responsibility to prepare our citizens for the future. We'll see more technological change, I argue, in the next 2 to 10 years than we have in the last 50 years.

Artificial intelligence is going to change our ways of life, our ways of work, and our ways of war. It could usher in scientific progress at a pace never seen before. And much of it could make our lives better.

But AI also brings profound risks, from deepfakes to disinformation to novel pathogens to bioweapons.

The AI revolution (cont)

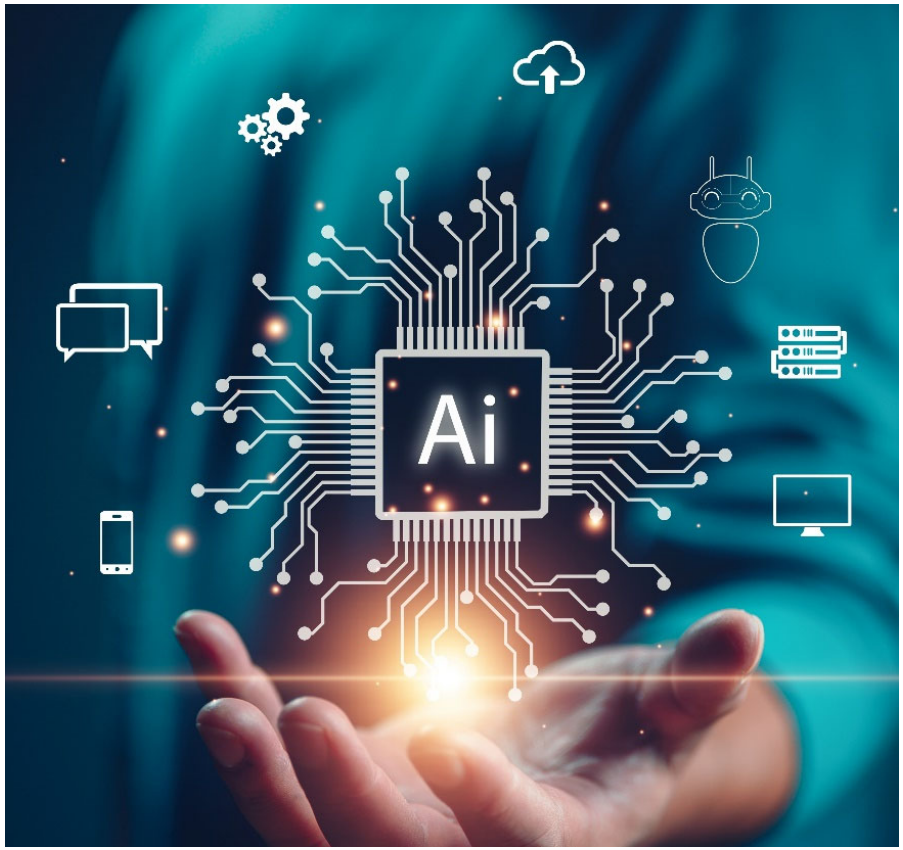
But let's be honest. This is just the tip of the iceberg of what we need to do to manage this new technology.

Nothing is certain about how AI will evolve or how it will be deployed. No one knows all the answers.

…

In the years ahead, there may well be no greater test of our leadership than how we deal with AI.

President Joe Biden, Address to the 79th Session of the United Nations General Assembly, 24 September 2024



Common misconceptions

Misconception 1: We are not going to market for AI – so no issue

Reality:

- AI is increasingly likely to be part of tendered solutions, even if not requested.
- Should build-in the possibility of AI at the drafting stage (difficult to ask question after tenders close).
- Should assume that AI may be included, until we know it is not.

Misconception 2: We are using the approved templates – so no issue

Reality:

- Most templates (I assume) are silent on AI, or assume that it is not included.
- Using a template is no defence to a decision based on an error or bias or breach of law or policy due to AI.

Common misconceptions (cont.)

Misconception 3: The best approach is to say we will not use AI

Reality:

- Governments' approach is to 'embrace' AI.
- Universities may decide not to expressly purchase AI – but this does not prevent AI being included in tendered solutions.

Misconception 4: We are not currently using AI

Reality:

- Are you sure you are not using AI? You may be using it but not know it.
- Have you checked if your current contractors, advisors or evaluators are using AI?

Common misconceptions (cont.)

Misconception 5: No insurance or risk implications.

Reality:

- AI risk is being likened to ‘silent cyber’ (were losses were covered by non-specific clauses).
- Policy proposals may soon ask if, where and why AI is being used and what you are doing to manage the risk.

Misconception 6: No security implications

Reality:

- The Government has banned the use of Deepseek.
- This may be the first of many bans.

Risks and harms of AI

Bias - AI systems can inherit biases, including political, ethical, racial, gender or sexual preference. Can result in discriminatory, unethical, non-inclusive practices.

Data privacy - AI systems use vast amounts of data and if private information is entered, it may be manipulated, transformed or disclosed.

Data security - Secure or classified information may be manipulated or transformed. Deepseek has been banned.

IP - This party owned IP may be transformed or reproduce without consent.

Risks and harms of AI (cont.)

Treasury is currently seeking views on whether the Australian Consumer Law remains suitable to:

- Protect consumers who use AI.
- Support the safe and responsible use of AI by businesses.

ASIC recently released a report *Beware the gap: Governance arrangements in the face of AI innovation* which looked at the ways Australian financial services and credit licensees are implementing AI and identified that:

- Not all had adequate arrangements in place for managing AI risk.
- Many relied on third parties and did not have adequate governance regimes in place.
- Governance arrangements varied widely and weaknesses were identified.

National response to AI

The key elements you should be aware of

Australia's 8 AI ethics principles

These are designed to ensure that AI is safe, secure and reliable.

The National Framework for the assurance of artificial intelligence in government

- A joint approach to safe and responsible AI by the Australian, state and territory governments.
- The governments are 'committed' to being 'exemplars' in the safe and responsible use of AI.

National response to AI (cont.)

The key elements you should be aware of

The Voluntary AI Safety Standard

Provides guidance to organisations on how to safely use and innovate with AI.

Policy for responsible use of AI in Government

- Reiterates that the public expects the government to be an exemplar of safe and responsible adoption and use of AI.
- *Ultimately, this means that government has an elevated level of responsibility for its use of AI and should be held to a higher standard of ethical behaviour.*

Safe and responsible AI in Australia Proposals paper for introducing mandatory guardrails for AI in high-risk settings

Proposal for mandatory guardrails on those 'developing' and 'deploying' AI.

- Deployer includes any individual that supplies or uses an AI system to provide a product or service.
- High risk (we will look at this shortly).

National response to AI (cont.)

State and territory-based regimes

- Beyond the scope of today's presentation to look at state and territory-based regimes.
- Broadly they are complementary to the National Framework.

Australia's AI Ethics Principles

The Framework maps practices to Australia's 8 AI Ethics principles

Australia's AI Ethics Principles (cont.)

Australia's 8 AI Ethics principles

Australia’s AI Ethics Principles

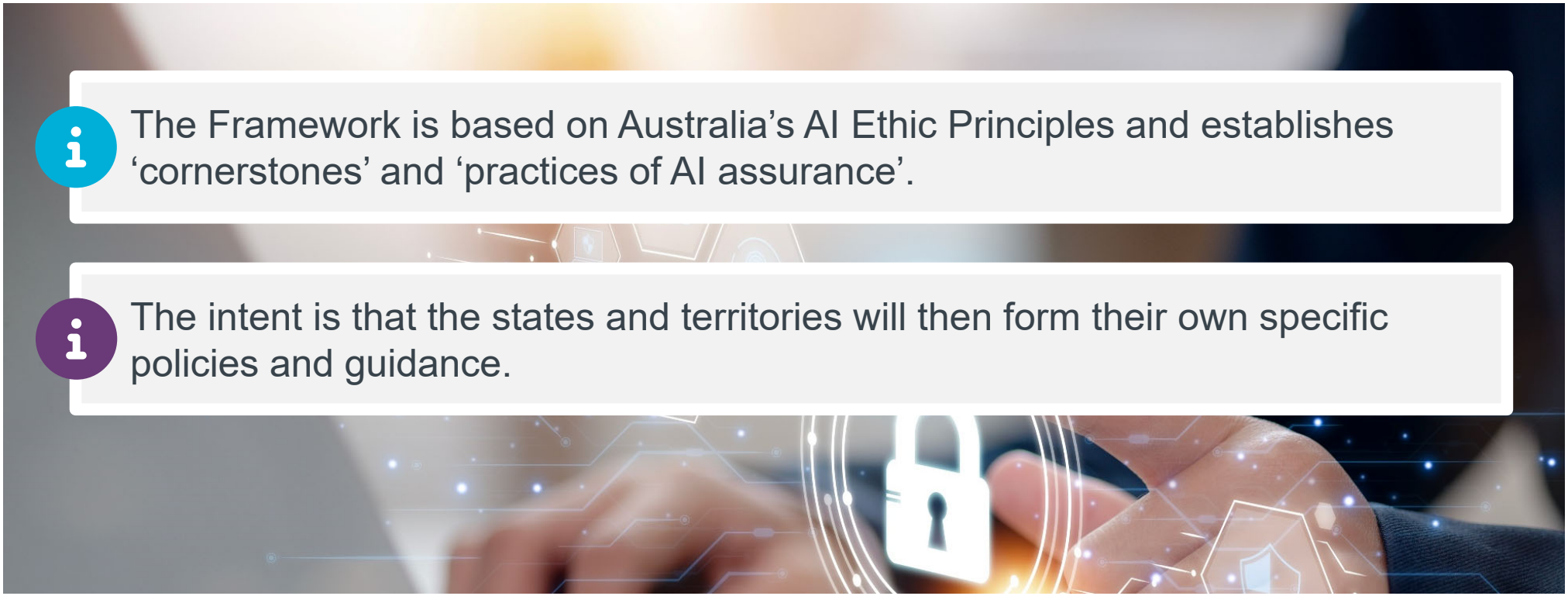
Australia’s 8 AI Ethics principles

National Framework

A joint approach to safe and responsible AI by the Australian, state and territory governments.

We recognise that public confidence and trust is essential to governments embracing the opportunities and realising the full potential of AI. To gain public confidence and trust, we commit to being exemplars in the safe and responsible use of AI. This requires a lawful, ethical approach that places the rights, wellbeing and interests of people first.

National Framework (cont.)



- The Framework is based on Australia's AI Ethic Principles and establishes 'cornerstones' and 'practices of AI assurance'.
- The intent is that the states and territories will then form their own specific policies and guidance.

National Framework (cont.)

Cornerstones of assurance

Governance

AI governance comprises the organisational structure, policies, processes, regulation, roles, responsibilities and risk management frameworks that ensures the safe and responsible use of AI in a way that is fit for the future.

Data Governance

The quality of an AI model's output is driven by the quality of its data.

A risk-based approach

The use of AI should be assessed and managed on a case-by-case basis. This ensures safe and responsible development, procurement and deployment in high-risk settings, with minimal administrative burden in lower-risk settings.

National Framework (cont.)

Cornerstones of assurance

Standards

Where practical, governments should align their approaches to relevant AI standards.

Procurement

*Careful consideration **must** be applied to procurement documentation and contractual agreements when procuring AI systems or products. This may require consideration of:*

- *AI ethics principles*
- *clearly established accountabilities*
- *transparency of data*
- *access to relevant information assets*
- *proof of performance testing throughout an AI system's life cycle*

National Framework (cont.)

Cornerstones of assurance

Procurement

It is essential to remain mindful of the rapid pace of AI advancements and ensure contracts are adaptable to changes in technology.

Governments should also consider internal skills development and knowledge transfer between vendors and staff to ensure sufficient understanding of a system's operation and outputs, avoid vendor lock-in and ensure that vendors and staff fulfill their responsibilities.

Due diligence in procurement plays a critical role in managing new risks, such as transparency and explainability of 'black box' AI systems like foundation models. AI can also amplify existing risks, such as privacy and security. Governments must evaluate whether existing standard contractual clauses adequately cover these new and amplified risks.

National Framework (cont.)

Cornerstones of assurance

Procurement

Consideration should be made to a vendor's capability to support the review, ongoing monitoring or evaluation of a system's outputs in the event of an incident or a stakeholder raising concerns. This should include providing evidence and support for review mechanisms.

Governments may face trade-offs between a procured component's benefits and inherent assurance challenges, and resolutions will vary according to use case and tolerance threshold.

Ultimately, procurement should prioritise alignment with ethics principles alongside delivering on a government's desired outcomes.

Voluntary AI Safety Standard

The standard:

assists with the safe and responsible use of AI in high risk settings

focuses on safety, ethics, and accountability at each stage of the procurement process

Voluntary AI Safety Standard (cont.)

Developer

An organisation or entity that designs, develops, tests and provides AI technologies such as AI models and components.

Deployer

An AI deployer is an individual or organisation that supplies or uses an AI system to provide a product or service. Deployment can be internal to the business or external. When deployment is external it can impact others, such as customers or other people, who are not deployers of the system.

Voluntary AI Safety Standard (cont.)

High-risk

Government has released a paper on proposals for mandatory guardrails in high risk settings.

It guides us in relation to the meaning of high risk.

High risk examples include AI used in medical, critical infrastructure, education, employment, law enforcement, border, administration of justice etc.

Voluntary AI Safety Standard (cont.)

Procurement Guidance

The Standard sets out specific procurement guidance – a good template for what we should do.

Tenderer information requirements:

Tenderers should be asked to detail:

- the AI system's design, capabilities, and limitations
- how potential risks associated with the deployment of the AI technology will be managed

Voluntary AI Safety Standard (cont.)

Procurement Guidance

The Standard sets out specific procurement guidance – a good template for what we should do.

Evaluations:

Universities should evaluate:

- the AI systems, including potential risks, such as data privacy concerns, security, biases and compliance with the AI ethical principles

- how the AI model has been trained and tested

Voluntary AI Safety Standard (cont.)

Procurement Guidance

The Standard sets out specific procurement guidance.

Contract requirements:

Draft contracts should include mechanisms for ongoing monitoring and accountability of AI systems after deployment. This includes having clear lines of responsibility for AI system performance and decision-making.

Mandatory guardrails

As mentioned, the government has released a paper on proposals for mandatory guardrails in high risk settings.

Point to note is that this will mandate guardrails for those deploying AI in Australia in high-risk settings.

Assume that this will be broadly aligned with the Voluntary AI Safety Standard.

Policy for responsible use of AI in Government

This policy is a first step in the journey to position government as an exemplar in its safe and responsible use of AI, in line with the Australian community's expectations. It sits alongside whole-of-economy measures such as mandatory guardrails and voluntary industry safety measures.

Ultimately, this means that government has an elevated level of responsibility for its use of AI and should be held to a higher standard of ethical behaviour.

Policy for responsible use of AI in Government

The policy includes mandatory requirements in relation to an AI transparency statement, including:

- compliance with the policy
- measures to monitor the effectiveness of deployed AI systems, and
- efforts to protect the public against negative impacts

Note: Good template for establishing a governance regime.

Policy for responsible use of AI in Government (cont.)

Using the risk matrix, determine the severity of the risks. In considering the consequence and likelihood consult with relevant stakeholders. The risk assessment should reflect the intended scope, function and risk controls of the AI use case.

		Consequence				
		Insignificant	**Minor**	**Moderate**	**Major**	**Severe**
Likelihood	**Almost certain**	Medium	Medium	High	High	High
	Likely	Medium	Medium	Medium	High	High
	Possible	Low	Medium	Medium	High	High
	Unlikely	Low	Low	Medium	Medium	High
	Rare	Low	Low	Low	Medium	Medium

The global response

We are not alone in seeking to manage AI risk

- The EU has approved the EU AI Act.
- The new UK government is looking at a principles based approach to AI.
- The US AI Safety Institute is looking to develop guidelines on evaluations and risk mitigations.
- Denmark laid out a framework that can help EU member states use generative AI in compliance with the European Union's new AI Act.

How do we respond?

Part 1 Assume that your procurements may include AI

- Unless you can be sure otherwise, build in the risk management in case AI is bid back.
  - Update your precedents and processes to manage the AI risk.

How do we respond (cont.)?

Part 2 Check if you are using AI in the tender process

- Are you using AI to develop the RFT?
- Are any of your external advisors / evaluators using AI? Have you asked?
  - If, yes you may need to advise respondents and provide a review mechanism.

How do we respond (cont.)?

Part 3 Check if any current contractors are using AI

- Write to you contractors and ask:
  - Are you using AI?
    - If yes, what is the AI and which contracts does it apply to?
- Consider whether any current contracts should be amended to manage the AI risk.

Procurement process changes

Procurement planning

1 Procurement Plan

- The likelihood that a tenderer may include AI in its solution.
- How AI risks by the successful tenderer will be managed.
- How Member AI risks will be managed (e.g. use of AI in drafting or evaluations)

2 Industry Engagement Plan

- What, if anything, will be said to industry about the use of AI by the Member.
- Will the use of AI as part of the development of the RFT or evaluations be disclosed to industry?

Tip: Use the Voluntary AI Safety Standard procurement as a guide to update your policy and precedents.

Procurement process changes

Procurement planning

3 **Probity Plan**

Is AI is going to be used by the Member during the evaluations?

- How will the risks of any biases or errors be managed?

Will any of the Member's project consultants or evaluators use AI?

- How will the probity risks be managed?

Question: You may be managing conflict of interest, but are you also identifying or managing possible AI related biases?

Procurement process changes (cont.)

Request documentation

Respondent information requirements (1 of 3)

The ATM should asked for information on the respondent's proposed:

Risk management process for any AI.

The process for identifying AI risks and potential harms.

Data management processes, including data quality, data provenance, privacy, security and cybersecurity practices. Is any banned AI being used (e.g. Deepseek)?

Procurement process changes (cont.)

Request documentation

Respondent information requirements (2 of 3)

The ATM should asked for information on the respondent's proposed:

Allocation of responsibility between the respondent (Contractor) and the Member for monitoring and evaluating the AI model.

Governance and oversight plan for human intervention if required.

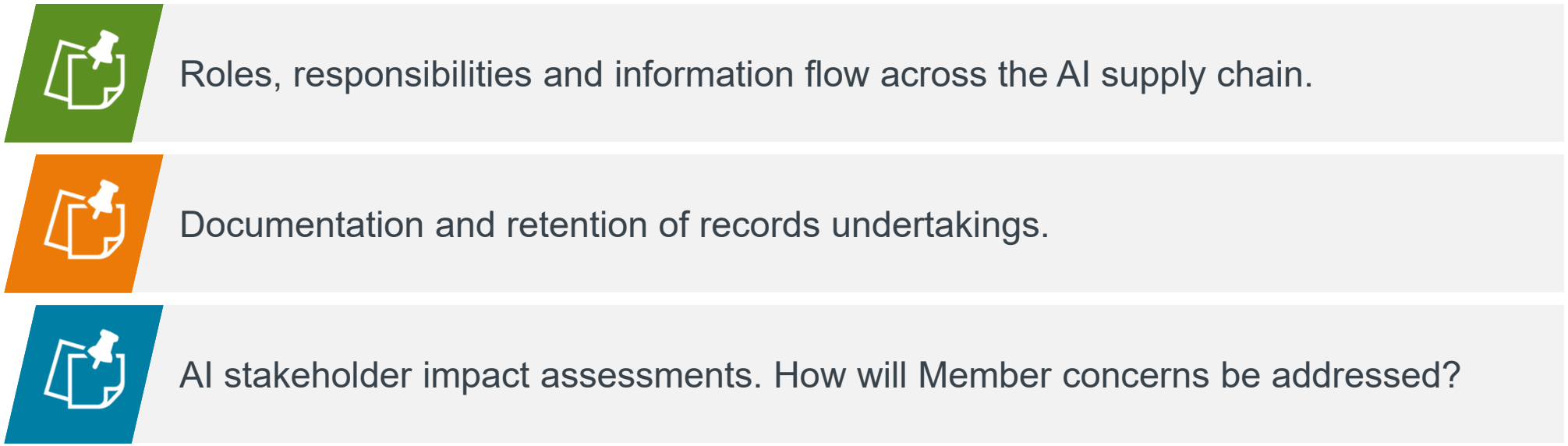
Public transparency and dispute mechanisms for the AI system.

Procurement process changes (cont.)

Request documentation

Respondent information requirements (3 of 3)

The ATM should asked for information on the respondent's proposed:



- Roles, responsibilities and information flow across the AI supply chain.
- Documentation and retention of records undertakings.
- AI stakeholder impact assessments. How will Member concerns be addressed?

Procurement process changes (cont.)

Request documentation

Conditions of tender

The evaluation criteria should allow detailed evaluation of AI related risks

Including how the respondent will ensure that the Member is an *exemplar of safe and responsible use of AI and compliant* with the AI ethical principles.

Remember: The procurement cornerstone requires us to prioritise alignment with the ethical principles alongside delivering the outcome.

Procurement process changes (cont.)

Request documentation

Draft Contract clauses

Part 1	Process for identifying potential AI risks and harms.
Part 2	Data management process, including data quality, provenance, privacy, security and cybersecurity.
Part 3	Governance and oversight of the AI.
Part 4	Responsibility for monitoring and evaluating the AI model.

Procurement process changes (cont.)

Request documentation

Draft Contract clauses

Part 5	Process for human intervention if required.
Part 6	Reporting obligations to inform end users of AI system use.
Part 7	Process for contestability of AI decisions by those affected.

Procurement process changes (cont.)

Request documentation

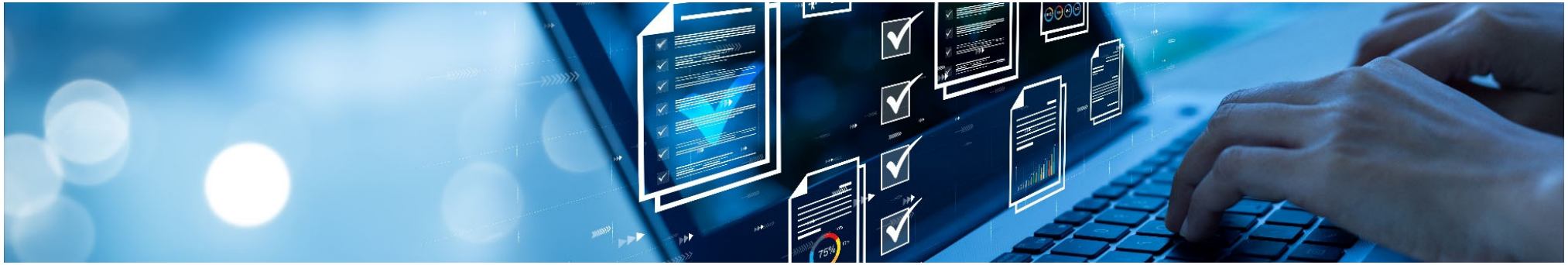
Draft Contract clauses

Part 8	Roles, responsibilities and information flow across the AI supply chain.
Part 9	Member impact assessments and how the contractor will remove biases and ethical prejudices.

Procurement process changes (cont.)

Contract management

Part 1	Work with your Contractor to undertake AI impact assessments.
Part 2	Understand how unwanted bias and ethical prejudices will be identified and removed.



AI drafting examples

Draft Deployed AI Risk Management Plan

1. *Respondents are to:*

   (a) *provide a draft risk management plan for each AI system used by the Respondent, and each subcontractor, in the provision of goods or services to the Member, (**Deployed AI**) including:*

      (i) *each potential risk and harm of the Deployed AI*

      (ii) *the Respondent's proposed risk tolerance for each potential risk and harm*

      (iii) *the Respondent's proposed impact assessment, risk assessment and treatment approach*

AI drafting examples

Draft Contract clause – Contractor not to use AI without prior consent

1. *The Contractor must not, and must ensure that each of its subcontractors do not, Use AI, without the prior written approval of the Member, which may include terms and conditions regarding the Use or Deployment of AI.*

Definition

***Use** means to utilise AI in a manner that the Member or its Customers:*

(a) consumes an AI-based product or service;

(b) interacts with an AI-based product or service; or

(c) is impacted by an AI-based product or service, after it is deployed.

AI drafting examples

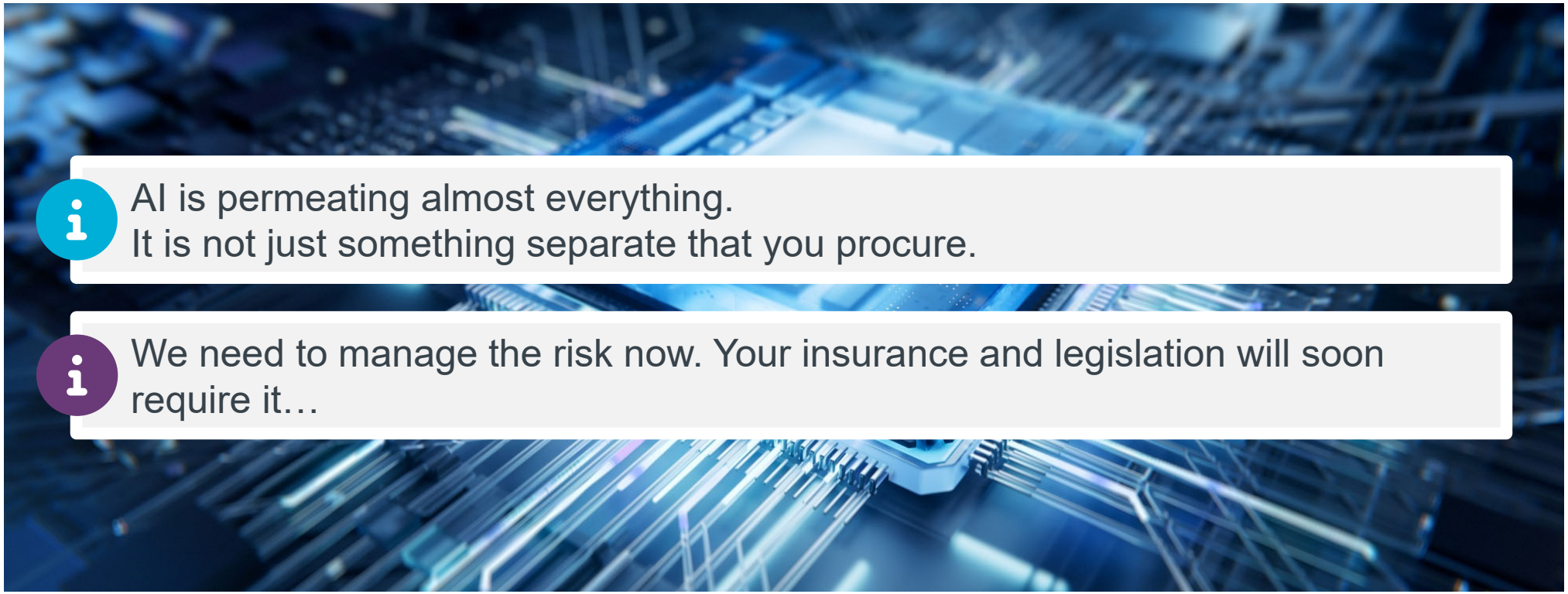
AI's proposed clause

1. Notification and Approval of AI Use

The Contractor must notify the Member in writing prior to deploying any Artificial Intelligence (AI) systems in the performance of this contract. This notification must outline the scope, purpose, and expected outcomes of the AI system, including its interaction with data and its role in decision-making processes. Approval from the Member be obtained in writing before the Contractor implements the AI system.

Key take-aways

AI is evolving and expanding



- AI is permeating almost everything.
  It is not just something separate that you procure.
- We need to manage the risk now. Your insurance and legislation will soon require it…

Questions

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