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Ten Fallacies About Web Privacy

We are not used to the Internet reality that something can be known and at the same time no person knows it.

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Privacy on the Web is a constant issue for public discussion—and Congress is always considering more regulations on the use of information about people's habits, interests or preferences on the Internet. Unfortunately, these discussions lead to many misconceptions. Here are 10 of the most important:

1) Privacy is free. Many privacy advocates believe it is a free lunch—that is, consumers can obtain more privacy without giving up anything. Not so. There is a strong trade-off between privacy and information: The more privacy consumers have, the less information is available for use in the economy. Since information helps markets work better, the cost of privacy is less efficient markets.

2) If there are costs of privacy, they are borne by companies. Many who do admit that privacy regulations restricting the use of information about consumers have costs believe they are born entirely by firms. Yet consumers get tremendous benefits from the use of information.
Think of all the free stuff on the Web: newspapers, search engines, stock prices, sports scores, maps and much more. Google alone lists more than 50 free services—all ultimately funded by targeted advertising based on the use of information. If revenues from advertising are reduced or if costs increase, then fewer such services will be provided.

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3) If consumers have less control over information, then firms must gain and consumers must lose. When firms have better information, they can target advertising better to consumers—who thereby get better and more useful information more quickly. Likewise, when information is used for other purposes—for example, in credit rating—then the cost of credit for all consumers will decrease.

4) Information use is "all or nothing." Many say that firms such as Google will continue to provide services even if their use of information is curtailed. This is sometimes true, but the services will be lower-quality and less valuable to consumers as information use is more restricted.

For example, search engines can better target searches if they know what searchers are looking for. (Google's "Did you mean . . ." to correct typos is a familiar example.) Keeping a past history of searches provides exactly this information. Shorter retained search histories mean less effective targeting.

5) If consumers have less privacy, then someone will know things about them that they may want to keep secret. Most information is used anonymously. To the extent that things are "known" about consumers, they are known by computers. This notion is counterintuitive; we are not used to the concept that something can be known and at the same time no person knows it. But this is true of much online information.

6) Information can be used for price discrimination (differential pricing), which will harm consumers. For example, it might be possible to use a history of past purchases to tell which consumers might place a higher value on a particular good. The welfare implications of discriminatory pricing in general are ambiguous. But if price discrimination makes it possible for firms to provide goods and services that would otherwise not be available (which is common for virtual goods and services such as software, including cell phone apps) then consumers unambiguously benefit.

7) If consumers knew how information about them was being used, they would be irate. When something (such as tainted food) actually harms consumers, they learn about the sources of the harm. But in spite of warnings by privacy advocates, consumers don't bother to learn about information use on the Web precisely because there is no harm from the way it is used.

8) Increasing privacy leads to greater safety and less risk. The opposite is true. Firms can use information to verify identity and reduce Internet crime and identity theft. Think of being called by a credit-card provider and asked a series of questions when using your card in an unfamiliar location, such as on a vacation. If this information is not available, then less verification can occur and risk may actually increase.

9) Restricting the use of information (such as by mandating consumer "opt-in") will benefit consumers. In fact, since the use of information is generally benign and valuable, policies that lead to less information being used are generally harmful.

10) Targeted advertising leads people to buy stuff they don't want or need. This belief is inconsistent with the basis of a market economy. A market economy exists because buyers and sellers both benefit from voluntary transactions. If this were not true, then a planned economy would be more efficient—and we have all seen how that works.

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