

Efficient Confidentiality for Privacy, Security, and Confidential Business Information

Peter P. Swire

This article addresses my observation, based on my experience in government service, that those trained in economics are much less likely to consider privacy protection important than those trained in other disciplines. The core economist intuition comes from the basic model of a competitive market, where a market is considered more efficient the closer it comes to perfect information. Full information allows the efficient matching of buyers and sellers. Limits on information, such as privacy rules, raise the costs of exchange and may even promote fraud by concealing negative information.

This article addresses that economists' intuition in a number of ways. Part I highlights the substantial history of confidentiality in banking. Many economists believe that persistent features of markets are likely adaptive and efficient. The history of confidentiality thus raises a rebuttable presumption that confidentiality has important efficiency characteristics. Part II places the privacy debate into settings where economists are likely to have positive intuitions that confidentiality is efficient. First, consider in the security context whether it is efficient to disclose the combination to a bank safe or other security information. Second, consider whether it is efficient for a bank to disclose confidential business information about a corporate borrower to that company's competitors. Third, consider, given the risk of identity theft, whether it is efficient for a bank to reveal a customer's online password or other information that acts as a key to the customer's account. The likely efficiency of keeping this key security information confidential thus can strengthen the intuition that confidentiality may also be efficient when it comes to sensitive personal information, or the "keys to the heart."

The article next suggests reasons why economists have tended to undervalue the harms from unwanted disclosures of information. Economists, who themselves may on average care little about privacy, may have misgauged the tastes of other people. Significant externalities may lead to an inefficiently high use of telemarketing and other business activities that rely on information sharing. The technique of cost/benefit analysis likely tends to emphasize the costs of privacy protections, which are more easily monetizable, instead of the benefits. Certain sorts of harms, including long-run societal harms from lack of privacy, have also likely not received full weight. Fourth, a Ponemon Institute study provides new evidence about revealed behavior, and not simply about poll responses, when it comes to financial services and privacy. The most significant finding is that customers that trusted their financial institution on privacy were substantially more likely to engage in online banking. Additional research would be helpful, but this data supports the possibility that individuals will participate more in some financial services where confidentiality is provided.

The article also places the economic efficiency analysis into broader debates about the desirability of privacy protection. Many non-economist scholars, and the legal system, have stressed the violations of rights that occur when important data about individuals is disclosed without their agreement. Economic analysis gives no independent weight to the violation of rights. Economists have thus systematically given less weight than those trained in other academic disciplines to many of the strongest arguments for privacy protection.