

Consumer Direct

**PERSONALIZATION:
MANAGING OPPORTUNITY AND RISK
IN THE CONSUMER DIRECT CHANNEL**



PEPPERS | ROGERS
GROUP
marketing 1to1, inc.



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Institute for the Future/Peppers and Rogers Group

Consumer Direct

April 2001

SR-728

ACKNOWLEDGEMENTS

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Table of Contents

List of Figures and Tables	v
Preface	vii
CHAPTER 1	
The Consumers' View of Personalization	1
CHAPTER 2	
A Closer Look: Personalization in Online Grocery Shopping	17
CHAPTER 3	
Opportunity and Risk in the CD Channel	25
CHAPTER 4	
Protecting Consumers' Privacy: Regulatory Responses in the United States and Europe	37
CHAPTER 5	
Managing the Opportunities and Risks of Personalization: Key Business Strategies	49

List of Figures and Tables

Figure	1-1	An Overwhelming Majority of Consumers Shop Through CD Channels	2
Table	1-1	The Basic Business-Consumer Value Exchange: Selection, Service, and Price	3
Table	1-2	Real-time Interactions and Easy Communication Are Important Benefits	5
Table	1-3	Most Consumers Don't Expect Personalized Benefits	5
Table	1-4	Coupons or Discounts Most Useful	7
Figure	1-2	The Shopping Process	8
Table	1-5	Personalization in the Shopping Process	9
Figure	2-1	Consumers Are Willing to Share Sensitive Information for Targeted, Relevant Offerings	22
Table	3-1	Planning a Cruise: "Booking-to-Embarkment" Dialog	27
Figure	3-1	Some Actively Seek to Remain Anonymous	29
Figure	3-2	Privacy Concerns Have Increased in the Past Two Decades	31
Figure	3-3	CD Shoppers More Concerned About Privacy	31
Figure	3-4	Privacy Concerns May Be Leveling Off in the United States	32
Figure	3-5	Fear of Credit Card Fraud Decreases Dramatically with Experience	32
Table	3-2	Sensitive Information	33
Table	3-3	The Information Hierarchy	34
Figure	3-6	Consumers Have High Confidence in Banks; Little Confidence in CD Companies	35
Figure	4-1	The United States Takes a Bottom-Up Approach	38
Table	4-1	A Few of the Online Privacy Bills in the 107th Congress	42
Figure	4-2	The European Top-Down Approach	43

PREFACE

Today's shoppers are comfortable in their anonymity. For the most part, consumers view their relationships with companies as impersonal—and see themselves as just part of the crowds of customers that pass anonymously through megastores every day. In general, as the retail and services industries evolved in the past century from small local stores and branches to large international enterprises, these impersonal relationships have come to dominate.

But anonymity has its drawbacks. The personal relationships once associated with local store proprietors who knew customers and their families by name, and could anticipate exactly what those customers needed any day of the week, have become mostly figments of nostalgia. Many of today's shoppers find it difficult to get a high level of customer service and to navigate an increasingly complex multichannel retail environment. To resolve simple issues, they must visit stores, write letters, go online, and call customer service centers. Today, many people yearn for the more personal shopkeepers of the past.

In focus groups conducted by the Institute for the Future (IFF) and the Peppers and Rogers Group (PRG), shoppers commented on their growing dissatisfaction. One woman described her frustration at being forced to move back and forth between a company's call center and online site to resolve a simple credit card issue:

I wanted to let them know [about a credit card change] so I tried the automated phone service, but there was no option for that. Then I tried waiting on the phone and it was just taking too long, so I went online...but they weren't set up for that type of inquiry...and I was confusing them by sending them an e-mail...so I had to get back on the telephone.

*—Advanced CD shopper,
married female, early 50s*

Therein lie the biggest opportunities and risks for companies doing business in consumer direct (CD) channels. For companies struggling with declining customer loyalty and diminishing margins in an increasingly cutthroat marketplace, the return to more personal relationships with customers, or more precisely, the reinvention of such relationships in 21st-century form, can be a real competitive advantage.

A recent survey of Global 1000 executives...found that 87% of respondents are planning to sustain or increase investments in customer management initiatives despite the economic downturn.

While the burgeoning list of consumer direct channels—Web sites, catalogs, kiosks, mobile devices, interactive television, networked appliances, and so forth—creates more opportunities than ever to interact directly with individual consumers and provide a broader range of personalized services and offerings, there are many uncharted territories yet to be mapped.

Given the past year's shakeout of the New Economy, hundreds of online companies have already come and gone. Survivors in the channel must integrate what was learned from the failures and move on to leverage the strengths of the new channels. Creating unique and personalized experiences for customers remains one of the most compelling strengths of the CD channel and provides a competitive advantage for those who do it well. But several questions remain to be answered: What kinds of personalization are most meaningful to shoppers? What is the appropriate channel mix for delivering personalized offerings? What information do companies really need from customers to offer personalization? What information are shoppers willing to share?

Smart companies are quickly moving new technologies and communication channels that promise a more interactive, personal relationship with their customers to the top of the "business-critical" list. In fact, a recent survey of Global 1000 executives conducted by Advanced Marketing Research found that 87% of respondents are planning to sustain or increase investments in customer management initiatives despite the economic downturn.

On one hand, these new technologies empower consumers to access information through any channel, to make more informed purchasing decisions at virtually any time or place they desire. They can search for information about products and services, and buy them at the best price. By demanding better service, products, and prices in this way, consumers are taking control of the marketplace with the help of these technologies.

On the other hand, businesses employ these technologies to collect more detailed information about consumers in order to understand them, not just in the aggregate, but at the individual level. With this information, businesses can create customer profiles, communicate more targeted and relevant information, and customize products. The more information about the customer businesses have, the more value they can provide the customer, if they use the information appropriately.

But using information appropriately is a big stumbling block for companies learning what it takes to succeed in this new commercial landscape. What seemed to be a win-win proposition for consumers and businesses has quickly turned into a double-edged sword. As companies feel their way through the dark, their early attempts at creating more customer interaction and providing more tailored information have, in some cases, heightened consumers' suspicions and increased their fear of privacy violations.

In this new world, where personal information is the currency of exchange, many consumers want to regain control of their

information—to choose when to be anonymous, what types of information to share, and how to exchange information for value-added benefits. In the absence of this ability to control the flow of personal information, the most sophisticated shoppers are learning to utilize technology to defend themselves against the misuse of their information, unwanted solicitations, and invasions of privacy.

To make sure they're not cut off from their customers by these actions, and to take full advantage of the opportunities that using consumer information provides—increased customer loyalty, profits, new markets—CD businesses must lead the way in addressing customers' concerns about privacy. Consumers aren't going to let businesses use their information unless businesses persuade them of the clear benefits of doing so. This makes building Learning Relationships—a company's ability to track each contact with a customer, learn from that customer's feedback, and tailor product, service, or communication based on that feedback—all the more important.

The simplest way for businesses to attain a high level of consumer trust is to put control of consumer information back into consumers' hands, to gather their personal data only with permission, and to tell consumers exactly when and how that information will be used.

Even with efforts like these, concern about the protection of personal privacy will continue to dominate public discussion. Throughout the North Atlantic nations, both public and private sectors are attempting to

set rules and guidelines. What is clear from these efforts is that any approach to protecting consumers' privacy must be adaptive and flexible for the good of everyone involved.

This report, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, will explore shoppers' attitudes about personalization, assess the opportunities and risks for companies that use consumer information collected through consumer direct channels, and discuss innovative strategies for creating more effective personalized experiences for consumers.

- Chapter 1 sets the stage by presenting the consumer view on the value of personalization throughout the shopping cycle.
- Chapter 2 takes a closer look at how personalization can enhance everyday shopping activities, by exploring online grocery activities.
- Chapter 3 explores the opportunities and risks in utilizing the consumer direct channel to create more personalized experiences for consumers, and examines consumers' growing concerns about privacy and security in the marketplace.
- Chapter 4 lays out the public and private responses to regulating privacy protection in the North Atlantic nations.
- Chapter 5 forecasts which business practices will succeed in collecting, storing, and using personal information while protecting privacy and providing high-value personalization to customers.

The simplest way for businesses to attain a high level of consumer trust is to put control of consumer information back into consumers' hands...

THE CONSUMERS' VIEW OF PERSONALIZATION

Emerging technologies supply many new ways to provide personalized services and offerings to consumers beyond traditional face-to-face contact. Business is “reaching out” to the consumer on Web sites with individualized pages, by e-mail with targeted messages and services tailored to specific needs, or through call centers that track a customer’s history of interactions with the company. Businesses that use CD channels remain at the frontline of the learning curve on building and maintaining relationships with consumers by means of these and other new communication channels. CD companies also stay in touch with consumers via chat rooms, instant messages, mobile phones, and personal digital assistants (PDAs) to name just a few on the growing list of new ways to communicate.

Despite technological advances, however, the fundamental principles of customer relationship building still hold true. In fact, they have become more important than ever in bridging the gap between the promise of technology and consumers' perception of the value they receive from companies trying to build these new types of relationships.

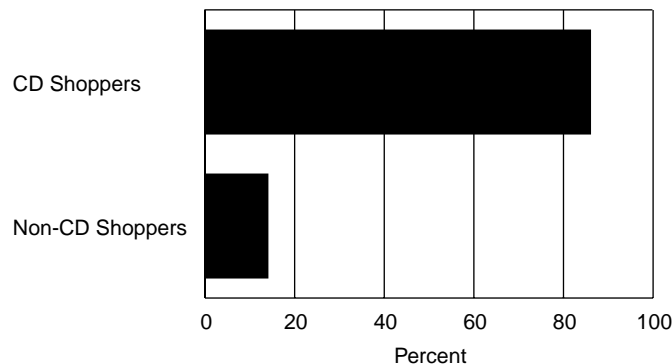
PERCEIVED VALUE

As consumers begin to shop in a greater variety of channels, many more options for personalized services are available. To better understand consumers' perspectives on personalization, IFTF and PRG conducted a series of surveys and focus groups (see sidebar, "Research Methodology"). We examined the attitudes and behaviors of consumer direct shoppers, who make up 86% of the U.S. population (see Figure 1-1). This group includes those who have shopped in the last 12 months by the more traditional CD

methods, including catalogs, direct mail ads, newspaper/magazine ads, television, radio, or the yellow pages, as well as those who have made purchases through newer CD channels such as online services or remote-order, home-delivery grocery services.

In our survey, we asked consumers what kinds of benefits they receive from stand-out companies they enjoy doing business with—companies with which they have established good relationships. Not surprisingly, selection, service, and price ranked high across all consumers including CD shoppers (see Table 1-1). These three offerings, the core components of the basic value exchange between business and consumers, represent the fundamental expectations consumers have of business. If companies can deliver good selection, service, and price consistently, consumers are likely to be loyal (at least until something better comes along).

Figure 1-1
An Overwhelming Majority of Consumers Shop Through CD Channels
(Percent of U.S. adults)



Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

*Table 1–1
The Basic Business-Consumer Value Exchange: Selection, Service, and Price
(Percent of U.S. adults who strongly agree with the statement indicating why they enjoy
doing business with a company)*

	Total	CD	Non-CD
They have the brands I like	70	70	69
I always receive good customer service	60	59	64
I always get a good deal when I do business there	50	49	56

Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

Research Methodology

Together, IFTF and PRG conducted a series of surveys and focus groups examining consumers' attitudes toward personalization and their willingness to share personal information. Data-gathering efforts included:

- *International Household Survey.* During the summer of 2000, IFTF and PRG surveyed a representative cross-section of 6,613 households throughout the North Atlantic countries, including Canada, France, Germany, Netherlands, Sweden, the United Kingdom, and the United States.

- *U.S. Household Survey.* In November and December 2000, IFTF and PRG commissioned a survey of 1,500 households in the United States. The survey was conducted with a national random sample of U.S. adults.

- *Focus Groups with CD Shoppers.* In January 2001, IFTF and PRG conducted eight focus groups with consumer direct shoppers in cities across the country, including Seattle, Chicago, Washington, D.C., and Raleigh, North Carolina.

Real-time interaction with a live person and the ability to choose how to communicate also ranked high with consumers in the survey. Most U.S. respondents valued being able to interact with a real person when they want to, and they also preferred to be able to communicate with a company by the method they choose (see Table 1–2). As the number of communication channels proliferates—store, phone, mail, Web, and e-mail, among others—people want to be able to communicate on their own terms, by the method they prefer, when and where they want.

What surprised us, however, is that value-added benefits associated with more personalized offerings such as targeted promotions and one-to-one service—where businesses know something about the customer and respond accordingly—were not among the top reasons most consumers enjoyed doing business with a company (see Table 1–3). Non-CD shoppers tended to rate these benefits higher than CD shoppers, but still rated them lower overall. This difference between non-CD and CD shoppers may demonstrate that those who get a high level of personalized services in the store environment feel less need to turn to alternative shopping channels for value or convenience.

Do consumers fail to give these benefits high marks because they don't want them, or because they feel they have no chance of getting them? We've found that consumers don't consider these benefits of the highest importance for a simple reason—many businesses don't even offer such services. Most consumers aren't given the option of having

just one person handle all their business, for instance, and most promises of personalized information targeted to consumers' individual needs go unfulfilled. For example, many consumers in our focus groups commented on the difficulty of establishing a personal relationship with local retailers, especially large chain stores. One woman described a typical relationship with a local grocery store:

I don't think grocery stores now are that personal.... You go in and you don't even see the same person from time to time...you've got a different checker every time...you don't know them well enough.

—Female, primary household shopper, late 40s

Others complained that they were quickly overwhelmed with messages after providing information to a company about topics that interested them. For many, potentially useful information was lost in the sheer volume of messages received.

I did [a profile] and I thought, "This will be a great resource," and I checked the box "you can send me information." I got so many e-mails that week, that now I don't open them. I delete them right away.

—Advanced CD shopper, married female, early 30s

*Table 1–2
Real-time Interactions and Easy Communication Are Important Benefits
(Percent of U.S. adults who strongly agree with the statement indicating why they enjoy doing business with a company)*

	<i>Total</i>	<i>CD</i>	<i>Non-CD</i>
I can easily reach a person whenever I want to	60	59	67
I can easily communicate with the company through whatever method I prefer	55	56	53

Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

*Table 1–3
Most Consumers Don't Expect Personalized Benefits
(Percent of U.S. adults who strongly agree with the statement indicating why they enjoy doing business with a company)*

	<i>Total</i>	<i>CD</i>	<i>Non-CD</i>
They know what I like and keep me posted on deals I might be interested in	37	36	50
They give me special discounts and benefits not available to other consumers	23	23	26
They have one employee who knows me and handles all my business	21	19	34

Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

As sophistication among CD shoppers grows, expectations of the value associated with personalized offerings increases as well.

Moreover, in a recent study, Jupiter Research found that only 40% of online companies used some form of personalization software in 2000. Another study conducted by Rubric found that only one in four online sites recognize repeat buyers. These decided gaps in service reinforce the notion that old ways of doing business—knowing the person who handles your transaction or getting special treatment because you are a good customer—are no longer major reasons consumers choose businesses. But the focus groups also clearly suggest that consumers would like to get such “old-fashioned” personal service. This deficit represents an important opportunity for CD companies to use new technologies to leverage direct contact with their customers and provide more value.

DELIVERING ADDED VALUE THROUGH PERSONALIZATION

Consumer direct shoppers are among the most experienced with the new forms of personalization available online, through catalogs, or by means of other CD channels. In our surveys, we asked consumers about the kinds of benefits they received from companies with whom they shared their personal information. While we found that many consumers, especially CD shoppers, are willing to share information for a variety of reasons, they valued some benefits more than others (see Table 1–4). Coupons and discounts topped the list, followed by product announcements and quick-and-easy purchases.

We see some dramatic differences between CD and non-CD shoppers, however. Almost five times as many CD shoppers as non-CD shoppers named product announcements as a useful benefit. Moreover, 16% of CD shoppers selected quick-and-easy purchases as the most useful benefit, compared to only 9% of non-CD shoppers. This response underscores the potential benefits of using information about customers to respond directly to their individual needs and interests with value-added (customer-satisfying) services.

The data also imply that as sophistication among CD shoppers grows, expectations of the value associated with personalized offerings increases as well. In the future, companies will need to offer much more than targeted coupons or discounts if they want to deepen their relationship with their customers. In our focus groups, consumers agreed that for them to continue sharing their personal information, companies would have to improve the value exchange.

If I give [personal] information out I expect something more in return than coupons or a discount on a future purchase. That sounds too much like they are just trying to entice you to spend more money. If I were to get a rebate, a genuine rebate, X% back, or \$X back, that would mean more to me.

—Advanced CD shopper, female

**PERSONALIZATION NEEDS VARY
THROUGHOUT THE SHOPPING CYCLE**

The goal of our focus groups was to get beneath the survey numbers and deepen our understanding of the value of different forms of personalization to CD shoppers. In our discussions with shoppers, the tension between releasing personal information and getting value from personalized offerings and services became very clear.

As shoppers conduct more shopping-related activities outside the traditional store—online, through catalogs, by direct mail, on mobile devices, and so on—they are trying to find the right balance between the desire to remain as anonymous as possible in the bricks-and-mortar environment and the need to reveal their identity in the CD channel to accomplish anything. For the most part, consumers are making the transition between these two paradigms and are willing to ex-

*Table 1–4
Coupons or Discounts Most Useful
(Percent of U.S. adults that named ... as the most useful benefit provided by a company they have shared personal information with)*

	<i>Total</i>	<i>CD</i>	<i>Non-CD</i>
Coupons or discounts	34	33	37
Announcement of new products and services	17	19	4
Quick-and-easy purchases	15	16	9
Better customer service	12	12	11
Comparisons of products or services	6	6	46
Have never shared personal information	17	14	35

Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

change some information about themselves for extra value and for the convenience of making a purchase when and where they want, but they are selective about which companies they release their information to. As one CD shopper put it:

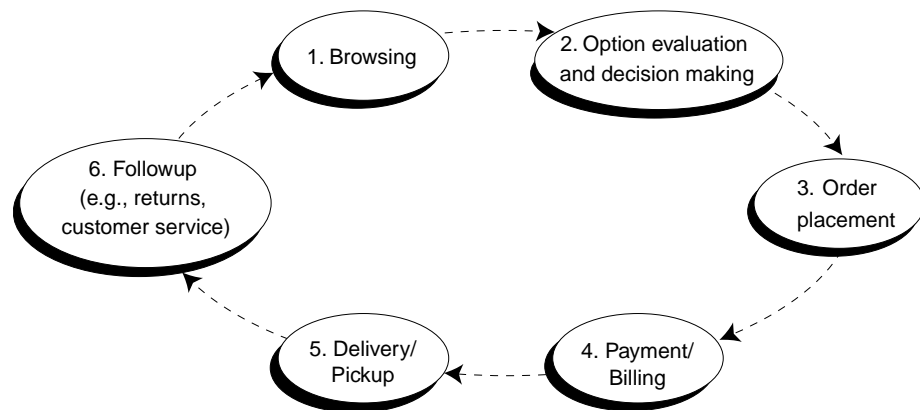
If I'm just browsing online and the site starts asking me for information, forget it. If I like the product and I want to buy it, well, now we have a give and take going. I want your product, you want some information.... Then I will make my decision as we proceed and I will give up some information for that convenience. But if they want information I don't want to give, then I'll go in the store and buy it.

—Advanced CD shopper,
married male, mid-40s

In the early part of the shopping process (see Figure 1–2), shoppers prefer to access a wide assortment of information from resources of their own choosing rather than a narrower set selected by someone else. They are willing to share generic, nonidentifiable information about their interests or preferences in order to access relevant materials that will help them make a purchase.

However, in the later stages of the process, shoppers want a personal touch from the company they have chosen to do business with. At this point, they are willing to share the personal information necessary to complete the transaction. Efforts to personalize customers' experiences during these later stages can reinforce the value of the overall relationship for shoppers who have decided to engage in some form of give-and-take with a company, whether it is an exchange of information or money (see Table 1–5).

Figure 1–2
The Shopping Process



Source: Institute for the Future and Peppers and Rogers Group.

Table 1–5
Personalization in the Shopping Process

Stage in Shopping Cycle	Personalization Need
Browsing	<ul style="list-style-type: none"> • Interactive, “do-it-yourself” tools • Allow individuals to specify their own search parameters as well as what types of information they would like to receive in response to their search queries
Option Evaluation	<ul style="list-style-type: none"> • Interactive tools that enable customers to specify the characteristics they want compared • Provide single-point access to a wide variety of vendors and brands
Order Placement	<ul style="list-style-type: none"> • The ability to change an existing order • Advice on items that they should order • Want confirmation of current availability or notification of backorder status before placing order • Access to live assistance for purchasing items that are not listed on the Web site, but are available through other channels such as bricks-and-mortar stores
Payment and Billing	<ul style="list-style-type: none"> • Ability to select the payment method they prefer • Helpful to keep payment information on file, but want to be able to change this information easily • Personal attention to deal with problems that arise; many shoppers don't feel comfortable using electronic media to solve payment and billing problems • Access to service reps to ensure accountability and an immediate solution to any issues that arise
Delivery and Pickup	<ul style="list-style-type: none"> • Want e-mail confirmations with the details of their order, including shipping and delivery status • Want choices on fulfillment (e.g., can pick up at store rather than have it delivered to home)
Customer Service	<ul style="list-style-type: none"> • High degree of personalization required • Follow-up communication to ensure that shopping experience was satisfactory • Do not send a form letter in response to a problem • Access to a live service agent who can empathize with their problem and offer real solutions
Follow-up	<ul style="list-style-type: none"> • E-mails targeted to their specific interests that come infrequently

Source: Institute for the Future and Peppers and Rogers Group.

Many shoppers prefer to browse and comparison shop on their own, but are very interested in interactive or “do-it-yourself” tools that empower them to find the information they need.

“Do-It-Yourself” Personalization

When consumers are looking for a product, especially a big-ticket item, they feel compelled to do their own extensive research to make an informed purchase. Any less effort and they feel they have let themselves or their families down by doing poor research. As a result, many shoppers prefer to browse and comparison shop on their own, but are very interested in interactive or “do-it-yourself” tools that empower them to find the information they need during these early stages of the shopping process. Shoppers find most helpful the do-it-yourself tools that allow them to set specific parameters for the kinds of information, services, or products they need.

Browsing

For example, shoppers want help finding specialized items that are unique and difficult to find. Often search engines bring back 500 links in response to an inquiry, but the majority are not very helpful because they lead to low-quality sites or sites that are not even commerce-enabled. Some shoppers want a search engine that lets them specify the kinds of information they want from their search query, such as product reviews or purchase locations. One consumer described a Web site that provides him with interactive tools that helped him find a rare book:

I've done it at Half.com [which has since been purchased by eBay].... I've been looking for a couple of books that are kind of hard to find. They're out of

print now, hardcover books, and I've asked [the site] to notify me when they get one... You can very specifically set the parameters like, “I don't want to pay more than 50% of the cover price,” and “they have to be hardcover,” and “they have to be in good or excellent condition.”

—*Novice online shopper, male*

A few consumers said they prefer the Web to a store for receiving personalized help in tracking down hard-to-find items. For example, one woman was looking for an older model of a particular car. Although she called many dealerships for help, she didn't trust that the dealers would call back. So she went to a few auto Web sites where she could enter her specific request. She trusted the Web service more than the dealerships to alert her once a car that matched her description became available because she was able to enter the information into the system herself.

I don't know why it feels more likely to me that we would hear from AutoByTel [than the dealership], but it just did. Maybe it's because you're typing it, you're writing it down, and you're thinking it is in their system somewhere.

—*Advanced CD shopper, married female*

Option Evaluation

Once shoppers finish browsing and decide on the item they want to purchase, they compare prices to find the best deal. Do-it-yourself tools that give shoppers the flexibility to check prices at different stores, Web sites, and catalog companies are considered very valuable for this process. Several shoppers mentioned CNET.com as a Web site that offers do-it-yourself tools they used to access the exact information they needed for comparison shopping.

I bought [a new hard drive for my computer] online and did all my shopping through a company called CNET.com, which actually does most of the shopping for you because they allow you to comparison shop. They've got reviews of the various products...allow you to comparison shop between about 15 and 20 online stores so you can absolutely get the best price you're going to get.

—Advanced CD shopper,
male, early 40s

Another customer wanted help in comparison shopping for insurance. He used a Web site that required him to provide his insurance history only once in exchange for rates from multiple companies. This service transformed the company hosting the Web site from being a simple order taker to being a highly regarded value-added agent. This

type of personalized tool helped the shopper find the exact information he wanted and thus avoid spending time on the phone.

...you can get insurance quotes from 30 companies... It's all one form, send it all in, and then find out who's got the best deal.... I've found that very convenient.... Rather than call 30 companies.... [Insurance companies] want to know everything about you. How many miles you've got, how many cars you've got.... Fill out one form [on the insurance quotes Web site] and you're done.

—Advanced CD shopper,
male

The Balance Between Technology and the Human Touch

When consumers are shopping—whether in a store or through a CD channel—there are times when they need more information than what is available on the store shelf, Web site, or catalog page. They want personalized attention from someone who can help them resolve their issues in real time, or they want up-to-the minute information that keeps them informed on the status of their order. The human component of these interactions is especially important at the later stages of the shopping cycle—as the deal heads toward closing.

Placing an Order

When a customer is ready to place an order, issues may arise that would be addressed most easily by real-time interaction with a person. For example, a customer may want to negotiate the price or may have a few last-minute questions about availability or product features. Most CD shoppers have not found a good online substitute for person-to-person contact, and will often resort to calling a customer service agent or going into a store.

Others found they needed a human agent when the product they wanted to order was not available on the Web site. They wanted access to a person who could find the product in one of the company's stores and add it to the order. In this situation, a human agent can help create a seamless experience for the customer who wants access to *all* the company's products regardless of which sales channel they choose to use. Even if the Web site and the bricks-and-mortar store do not carry the same stock, a human agent can help move the ordering process along. One shopper described how her grocery delivery service customized her order by pulling items that were not available on the Web site off the grocery store shelf:

Peapod shops from the store that I shop at.... So I know what's on those shelves. I used to be able to call them or e-mail them and say, "I'd like one of this and one of this, even though you don't seem to

be offering it on the Web site, I know you sell it in the store," and they would bring it with my order.

—Advanced CD shopper,
married female

Payment and Billing

Once a shopper chooses to engage a company in some form of transaction, her expectations for personalized service increase. For now, most shoppers appear to be most comfortable with some form of person-to-person contact—they rely on the phone to check on order status, solve billing questions, or determine the right product to buy. Often this real-time communication provides the consumer an opportunity to explain her issue in more detail, or to have all of her questions answered, as contrasted with an e-mail, which is viewed as a "one-shot" communication.

Woman: [If there is a problem,] you can get deeper into the issue on the phone —and ask "Well, why isn't it here?— And what is going on?" You can dig deeper.

Man: Yeah, you can get a person a little bit more on your side, to empathize with you a little bit more, as opposed to getting an e-mail.

—Advanced CD shoppers; male,
early 40s, and female, early 30s

The ability to call a customer service center and talk with a service agent also assured shoppers that a company was legitimate—not a fake hiding behind a Web site.

We bought [my son's birthday present] online through a credit card. And I did talk to a sales agent. We went on the site, and then they had a number that you could call.... I wanted to confirm that this was the actual site that I was giving my credit card to.

—Advanced CD shopper,
married female, late 40s

Delivery and Pickup

Sending messages such as e-mails or faxes to continue the flow of communication once an order is placed is a prime opportunity to provide real added value to shoppers and alleviate some of the uncertainty of purchasing through the CD channel. Shoppers like to be updated on the status of their orders and contacted directly if a problem arises. One man described how a company exceeded his expectations with effective follow-up communication:

The company followed up with an e-mail confirmation of the order, an order number, estimated delivery date, and even the UPS tracking number that I could use to log onto a site that would show me on a map where the thing was as it was

traveling across the country. But they were wrong. They estimated three days for delivery and it came in two.

—Advanced CD shopper,
married male, mid-40s

Another component of personalization that consumers support would be very valuable at this stage of the shopping process—the ability to place an order over the Internet and pick it up at a local store. Many consumers agree this would be a valuable benefit of an online service:

If you could just call up and order your groceries, then just have them waiting for you so you could just drive through and zip in and zip out.

—Married female with children,
late 30s

Customer Service

For complex service situations, many shoppers found it difficult to reach a person who could help them. In these cases, shoppers preferred going to a store and talking to someone face-to-face about their problems. Being physically present in a store allowed shoppers the opportunity to explain the situation, and use their physical presence to insist on a satisfactory solution, which they did not think was possible online or on the phone. Automated customer services such as menu-driven telephone systems and auto-response e-mails increased consumers' frustrations as they tried to resolve thorny issues.

Shoppers like to be updated on the status of their orders and contacted directly if a problem arises.

Once consumers engage a company in an exchange of information or currency, their service expectations increase.

On the phone, I found that the first person that answers really doesn't know squat about what you're talking about but they're trying to screen you.... [After two months dealing with people on the phone] I finally went back to the store I very calmly told them exactly what I had done, the steps that I had taken. I showed them what I had done and they asked me what I wanted. And I said, "I want either my money back or a new computer if you can." So they gave me a new computer which also didn't work, so I brought it right back. I finally got one that worked.

—Advanced CD shopper,
divorced male, 50 years old

Although most shoppers did not want to use electronic media when they expected a high degree of personalization, some were open to the possibility if a company offered live chats or some other way to interact with a person. In any case, shoppers wanted a medium that allows a real-time, two-way dialog, and offers the flexibility to negotiate, haggle, and persuade.

Follow-up

Most shoppers expressed an interest in receiving follow-up communications from companies they had purchased from, or those which had provided useful information. The communications that were most valuable to shoppers were those whereby the company (1) sent information—e-mails, faxes, paper mail, and so forth—infrequently, giving the consumers a chance to read them, and (2) sent information related to upcoming sales of items in which the customer had explicitly expressed an interest.

Female: They were interesting, but I never had the time to really look at them and read everything. And so I end up just deleting them.

Male: I had the opposite experience. CDNow.com let me know when this is going to happen or that's going to happen. Every once in awhile, I get an e-mail and it usually pans out as productive.

Female: I think if I was getting them infrequently, then I'd be more inclined to spend the time and read it and look at it. But when you're getting three a week I just say forget it.

—Advanced CD shoppers;
female, early 30s, male,
early 40s

KEY LESSONS:

FOCUS ON THE VALUE TO CONSUMERS

The primary lesson from these surveys and focus groups is that companies should let their customers—and even help them—dictate the information exchange. Some of the following efforts might be useful:

- *Balance technology with personal touch.* Throughout the shopping cycle, CD companies have many opportunities to add value for consumers with more personalized services. However, providing personalization does not imply a single approach, but rather a balanced mix of cost-saving technology solutions and human interaction. Even though technologies provide opportunities to service more customers in cost-efficient ways, companies must be careful not to alienate customers by relying too much on technology and depersonalizing the interaction.
- *Provide do-it-yourself personalization tools.* In the early stages of the shopping cycle, consumers prefer to look for what they want by configuring interactive tools to work on their individual needs. These tools allow individuals to personalize their own experience by specifying the parameters most important to them as they browse and evaluate products.

- *No substitute for real-time interaction.*

Once consumers engage a company in an exchange of information or currency, their service expectations increase. At the later stages of the shopping cycle, the ability to interact with a live agent and access real-time information becomes paramount in resolving issues, tailoring satisfactory solutions to problems, and providing a personal touch that engenders trust and loyalty.

- *Reinforce relationships through ongoing communication.* Targeted communication can be an important tool as long as it is not overused. Consumers get the most value from communications that are relevant to their interests and needs and that come infrequently, giving them a chance to digest them and respond.

This basic framework outlines the way consumers' needs for personalization change depending on where they are in the shopping cycle, but other variables must be considered as well. The type of product or service and the amount of research and investment required to make the best purchase are all important factors. The next chapter takes a closer look at the kinds of personalization that are most meaningful to consumers in their everyday shopping activities.

A CLOSER LOOK: PERSONALIZATION IN ONLINE GROCERY SHOPPING

Against the backdrop of tumultuous change in the online marketplace, the goal of this year's research is to understand the fundamental shifts that will drive the growth of the CD channel. Online businesses have come and gone, but the migration of consumers into the CD channel continues. More shoppers are gaining experience in the channel, and more are becoming educated about how to use interactive tools in their shopping activities. Their expectations for what companies can offer, both off- and online, will continue to expand over time. Opportunities to leverage the capabilities of new channels to differentiate customers and tailor their shopping experiences will become increasingly important.

In general, consumers are most interested in getting personalized information and services for big-ticket items (computers, cars, appliances), hobbies or personal interests (music, gourmet coffee, vintage automobiles), work-related interests (business news, occupational materials), and special needs (allergies, other medical conditions). The types of personalization most meaningful to shoppers differ across product categories.

In order to better understand the dynamics of personalization and its role in defining the CD market, we explored how companies might leverage new interactive capabilities to create a more personalized experience for

everyday shopping activities. Because it represents the first large-scale effort to move a significant portion of a household's regular purchases into the CD channel, we focused specifically on remote grocery shopping in our surveys and focus groups.

Consumer preferences for personalization in online grocery shopping fall into several key categories:

- Pull-not-push personalization
- Interactive expert recommendations
- More options, more control
- Person-to-person contact

Online businesses have come and gone, but the migration of consumers into the CD channel continues.

PULL-NOT-PUSH PERSONALIZATION

Regular purchases of low priced items like groceries do not warrant intensive information searches on the part of consumers. Indeed, most browsing and comparison shopping take place walking down store aisles. For this reason, most consumers were not interested in receiving information from their grocer (that is, push). They would rather have the ability to access the information they think would help them better plan shopping trips or accommodate their household's particular needs and preferences (that is, pull). Although many consumers were still unwilling to give up in-store grocery shopping, even for the convenience of home delivery, many were also looking for hybrid solutions that leveraged the online channel to enhance their grocery shopping experience.

Put Product Information on the Web

Many consumers wanted the ability to access product information, including nutrition content, size, and price, on the Internet before making a purchase or stepping foot in a store. More consumers are health-conscious and were interested in collecting information about their grocery purchases so they could develop better shopping strategies. One consumer wanted a Web site that displays the nutrition labels of products carried in his local grocery store so he could read the labels in the comfort of his home rather than spending additional time in the store.

...it would be nice to [go to a Web site and] type in what you're going to look for that day, and then have these nutrition labels pop up online so you can automatically go out there without having to look at every product in the store... when I go shopping I'll look at the nutrition items before I purchase it. It'd be nice to know before I go out...

—Male, early 30s

Send Coupons and Notice of Store Sales for Regularly Purchased Items

Most shoppers are aware that grocery stores track their purchases by means of loyalty and reward card programs. Some online grocery shoppers indicated that they would like companies to use that information to offer them coupons and promotions on the particular items and brands they regularly purchase. For example, for a shopper who regularly purchases Braeburn apples, a discount on Braeburns is much more valuable than a discount on Golden Delicious or Granny Smith apples. Likewise for branded products—shoppers who prefer Coca-Cola would rather receive discounts for Coke than for a competing brand such as Pepsi. Grocers can provide a valuable service by using purchasing history information in this way. One online grocery shopper indicated interest in getting help from her grocery delivery service in identifying good deals on the items she normally purchases.

I want a good buy. And if it's something that I like, go ahead and send it to me. When I shop for groceries online I'm trying to find a good deal. You know, it's a lot of work and I prefer somebody to just say, "Oh here, it's 20% off." Well, thank you. I prefer not to do the work.

—Advanced CD shopper,
married female with young child,
late 20s

Other shoppers expressed interest in receiving coupons or notices for upcoming sales on the products they regularly purchase. They would use this targeted information to plan their shopping schedule in order to get the best deals.

[The grocers could] show you what's going to be on sale on their Web site, and they show you throughout the month when you can buy something. For example, if you've got to buy in quantity and they have something like pork chops that are going to be on sale at the end of the month and you go there and pay full price now, can you wait and buy them when they go on sale.

—Male, early 60s

Meet Special Needs with Personalization

Consumers who could gain the most direct benefit from personalization may be those with special nutrition or health needs that require more information to manage particular conditions such as food allergies, diabetes, and high cholesterol. Individuals or households with special needs were the most willing participants in our studies to share personal information in exchange for discounts, resources, and tailored recommendations. One woman wanted more customized information to help her manage her young daughter's dairy allergies:

A lot of the foods that my husband and I eat include dairy foods, so my daughter can't eat them...the Food Allergy Network has a cookbook for \$20.... But it includes [recipes for] allergies from eggs, wheat, nuts, everything else. I don't need all of those recipes.... But if I could go on a Web site and tell them my daughter is this age, the food has to be age-appropriate for her...and this is her particular allergy, could you give me some recipes for that, instead of me searching it out. So if I could say, I need this, this and this, you give it to me.

—Advanced CD shopper,
married female with young child,

INTERACTIVE EXPERT RECOMMENDATIONS

Other shoppers are interested in going one step further to get help managing their diets and attaining health goals. For example, many shoppers are interested in sharing information about their health goals in exchange for recommendations on the kinds of foods they should purchase and ideas on how to use them in a healthy diet. One man described how helpful this kind of interactive service would be for different kinds of health-related goals:

If I was playing football...[and] I wanted to get certain kinds of foods to help myself get larger, that would be very helpful. If I had high cholesterol and I needed help finding foods that are in my category, that also would be very helpful.

—Male, under 35

Nutrition Recommendations

Some consumers wanted an interactive approach with the ability to define the parameters of the information they would receive from their grocer. Instead of getting recommendations and discounts based on past purchases, some wanted to be able to specify the aspects of their diet that they need the most help managing.

I'd like to see an interactive service—you tell [your grocer] what you're looking for—because I would like to be able to say, "Okay—I really need to

get more green vegetables" or something in my diet. And then they can give you recipe ideas or something like that. And it wouldn't be based on what I already buy because I need help with that. So the interactive thing would be better.

—Female, under 55

Recipe Recommendations

Still others wanted the ability to access information related to the items available in their local store via a Web site. One woman described a service that would post sale items linked to recipe ideas for how to use them.

I would just like to go into a Web site...here's Costco and this is what they have on sale, "We're featuring pork chops this week, if you're interested, here are ten ways to use them."

—Female, 43 years old

MORE OPTIONS, MORE CONTROL

In general, consumers were interested in online services that would create more options for different kinds of shopping experiences, save time, and reduce the hassle associated with weekly grocery shopping.

Anytime, Anyplace Access

A key benefit of current online grocery models is that consumers can shop whenever and wherever they want. In this way, remote shopping is a personalized tool that provides shoppers with more flexibility to organize their schedules—they don't have

to wait for the store to open. Consumers appreciated having the option to place orders, and also noted that being able to change or add onto orders is an important feature of the do-it-yourself toolkit offered by online grocery services. One avid online grocery shopper commented:

You can put in your order any hour, whether the store is opened or closed. It's really great if you're a night owl. You can do your shopping at an hour when you really wouldn't want to be out...you can keep adding to the order up until about half a day before it's delivered. I've got groceries coming tomorrow at four o'clock and I have until midnight tonight to make any last-minute changes.

—Advanced CD shopper,
married female with young child

Auto-Replenish the Basics

A few consumers were attracted to the option of having their basic purchases automatically replenished, though many others were concerned about the additional cost for the service. Others worried that if people no longer had to go to the grocery store that such a service would help erode the social fabric of local communities. However, a small group of consumers, namely working mothers with small children, as well as young professionals, saw automatic replenishment services as an option that promised real convenience and timesaving. One woman describes why such a service might be valuable:

By the time you get home from work, you've got to schlep to the grocery store. I have a little one and my husband works a lot of long hours. It's just tough for me to schlep my son to the grocery store. It's an extra-added thing. By the time I get home it's 6:00 and it's another hour at the grocery store.

—Married female with young child, late 30s

Others agreed that the service could be useful, as long as they had the ability to control the schedule.

Sometimes you don't want toilet paper at the time, but you might need paper towels, you may need milk—certain things you're going to need. If you have the opportunity to adjust it, then it would work.

—Male, primary household shopper, early 30s

Remove the Hassle

Some of our respondents were attracted to options that would remove the hassle and inconvenience of in-store grocery shopping, namely walking up and down the store aisles to find the products they want. Services that would expedite shopping, such as allowing consumers to pre-order routine items for pickup (thereby providing more time for shoppers to focus on products they want to hand pick), promised some consumers real added value.

A few consumers were attracted to the option of having their basic purchases automatically replenished, though many others were concerned about the additional cost.

Through the Internet you can access your grocer. Just plug in your order and tell them what you want. When you show up, it's already bagged. You don't have to spend your time looking through the aisles but you may not want to be waiting at home for delivery either...if you know you're going to be going grocery shopping, you get online and come up with your list. You send it, and it'll be there within an hour or so. You can go do some running around or whatever you have to do and then just swing by that grocery store to pick it up.

—Male, under 55

PERSON-TO-PERSON CONTACT

The evolution of grocery shopping in the past few decades has helped to shape the modern shopping paradigm—where the goal is to get in and out as quickly as possible. Gone are the small-town grocery stores and the friendly grocer whom shoppers could trust with information about themselves and their families. But in an era dominated by large chain stores and impersonal store clerks, many shoppers balk at the notion of sharing personal information with their grocer, despite the potential for more collaborative relationships regarding nutrition and health maintenance.

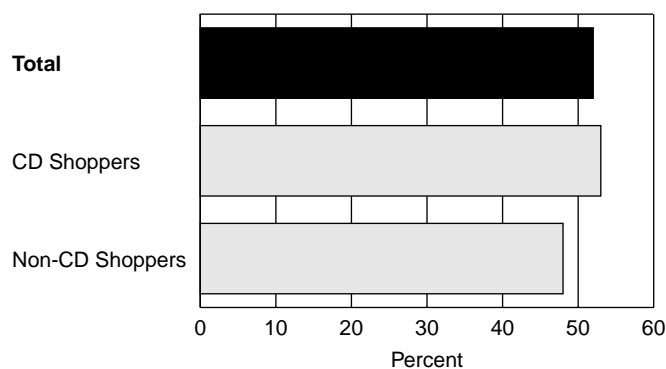
Surprisingly, over 50% of people in our surveys reported that they are willing to share medical information—which we know is among the most sensitive pieces of personal information (see Chapter 3)—with their regular grocer in exchange for targeted, value-added benefits like promotions or discounts on products related specifically to a need or interest (see Figure 2–1). However, this is a highly qualified willingness, as we found in our group discussions with consumers.

Relationships Matter

Consumers' willingness to share information depends on their relationship with their grocer. In small-town grocery stores, shoppers have more opportunities to establish a personal relationship with store clerks and managers, for example. The rapport that shoppers build with store employees becomes the basis for trust in deepening the Learning Relationship. One woman described how she would be more willing to share information with the grocer from her hometown than the large chain store in her neighborhood.

Figure 2–1
Consumers Are Willing to Share Sensitive Information for Targeted, Relevant Offerings
(Percent of adults in each group that are “very willing” or “somewhat willing” to ...)

Give your regular grocer information about a medical condition such as diabetes for example, in order to get special products or services related to your condition.



Source: Institute for the Future/Peppers and Rogers; *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, U.S. Household Survey, 2000.

[I would not share information] if you're talking about a chain store, because the chain stores generally speaking are very impersonal. Now, I lived in Lakeside for a long time and I went to the Vons there. They knew me by heart. Every one of the employees knew who I was—because I'd go in and I'd talk with them all and spend time there. But that's a small town with a small-town grocery store. If you go up to the big Vons, nobody knows who you are. So you'd have to have more of a personal grocer to do that with.

—Female, late 50s

Expert Knowledge Establishes Credibility

Others were willing to share information about their health and medical needs with their grocery provider only when experts were available to respond with information or advice. As one focus group participant put it, “only if they had a bona fide nutritionist in the store.”

Most consumers do not perceive their local chain grocers as experts in nutrition, even though the stores supply households with most of their food-related needs. Specialty food retailers like Whole Foods are better positioned as experts, since good nutrition is part of their brand proposition. Consumers expect the specialty providers to

have knowledge and expertise the large chains don't have.

I don't think I'd trust Dominic's as much as going to Whole Foods or something like that... I don't consider Dominic's particularly health conscious.... But Whole Foods, yeah. I would see [a health nutrition service] associated with them.”

—Female, primary household shopper, early 40s

The combination of trusted brand names and more personalized service are important components in establishing deeper Learning Relationships with consumers.

Person-to-Person Service Online

Whether they shop in the store or online, customers agree that live service is an important component of the experience. Online grocery shoppers, especially, say live service helps them develop a trusted relationship with their providers. Some mentioned that being able to reach a service agent on the phone or online for help with purchase decisions is what makes them comfortable with online grocery delivery service.

I always ask questions and things like that, and then they're more than happy to serve me. There's always a live person on the line, to answer questions, which is really good.

—Advanced CD shopper, single professional female, early 20s

Whether they shop in the store or online, customers agree that live service is an important component of the experience.

Trust and collaboration are the basis for successful personalization in the online grocery arena.

**KEY LESSONS:
EFFECTIVE PERSONALIZATION
REQUIRES COLLABORATION**

The key lesson from our research with consumers is that personalization is not something companies give to consumers, it's something companies work with consumers to achieve together, in some of the following ways:

- *Bridge the gap between desire and trust.* Consumers value information that empowers them to manage their households better. In fact, most consumers are willing to share sensitive personal information in exchange for value-added information targeted to very specific needs. But in reality there are few providers that consumers trust to have the expertise and the capabilities to deliver on their promises.
- *Collaboration is key to building trust.* Trust and collaboration are the basis for successful personalization in the online grocery arena. Tools that help grocery shoppers do a better, more efficient job are welcome, and expert advice on ways to enhance the health and nutrition of households provides real added value to the experience. For now, most grocery shoppers do not feel it necessary to have someone shop for them. Rather, they prefer more personalized interactions to enhance rather than replace their sometimes impersonal in-store experiences.
- *Trusted agents needed to meet individual needs.* Some shoppers have very specific needs such as allergies or medical conditions that require specialized information to help them manage effectively. Others seek general advice on meeting health or nutrition goals. In either case, companies have an

opportunity to become the consumer's trusted agent by helping them to obtain information, products, and services to better meet their unique needs.

- *Break through the comfort of anonymity.* Most shoppers, accustomed to large, impersonal chain grocers, are reluctant to take advantage of convenience-based services like grocery home delivery and unwilling to share information with their grocers without a strong foundation of trust. For most people, this trust is built on personal interactions that allow them to get to know the people working at the store. Companies must try to reproduce the online equivalent of this kind of trust.
- *Leverage channel strengths for an integrated approach.* An integrated, hybrid solution offers more value than either pure online or in-store-only shopping. Marrying in-store personal service with the interactive capabilities of online tools that help consumers access relevant information and engage in information exchanges with live experts is a potentially powerful combination. But such a combination requires businesses to strike a very delicate balance.
- *Success requires a well-balanced approach.* Strategies for creating more personalized experiences for shoppers are by no means straightforward. Any successful approach requires a balanced measure of effective technology, personal interaction, and trust.

The next chapter will discuss the opportunities and risks that businesses face in implementing successful personalization strategies.

OPPORTUNITY AND RISK IN THE CD CHANNEL

In the online world, the most common benefit a consumer gets for sharing information is “personalization,” or an online experience tailored particularly for that consumer. A 1999 Cyber Dialogue survey found that 29% of online adults have provided personal information (for example, the names of stocks in their portfolios, zip codes, health issues, or news and entertainment interests) to Web sites in order to create personalized Web content. A survey conducted by the Personalization Consortium in March 2000 found that 51% of Web users are willing to share information “to receive an online experience truly personalized for me.”

Many industry leaders maintain that the ability to personalize information, services, products, and experiences for individual consumers is the future of commerce. Moreover, many would argue that the future is here today, with the interactive capabilities of the Internet, enormous databases of customer information, and myriad applications for managing different kinds of Learning Relationships with customers.

But consumers have a different perspective.

As we discussed in previous chapters, consumers are becoming increasingly skeptical of companies that claim to offer “personalized” benefits in exchange for information. Although many consumers are willing to share information in exchange for value-added benefits, others have been left cold by superficial form letters, poorly targeted communications, unwanted information from

unknown companies, and media coverage of the many corporate “abuses” of their personal information.

Thus, what seemed like a win-win proposition for CD businesses just over a year ago is really much more complicated. It’s still an opportunity for many companies, but one that requires significant investments in both technical and human service components. CD businesses need to work toward integration across information systems and customer channels, collaboration with consumers, and deeper understanding of consumer needs and desires.

Indeed, companies still have many opportunities to pursue more personalized relationships with customers in the CD channel, but to be successful, they must manage the risks effectively.

TAKING ADVANTAGE OF THE OPPORTUNITIES

The customer marketplace is coming full circle—from the corner store of yesterday to the industrialized mass market, and now back to the high-tech version of the corner store, enabled by the Internet and database technologies. As companies enter this new commercial environment, opportunities abound for redefining the value exchange and forging new relationships with customers.

Help Consumers Cut Through the Clutter

Many companies err on the side of sending messages too frequently, with the goal of maintaining a constant flow of communication. Not a bad goal in itself, but when companies send several messages a day, for instance, they overwhelm consumers and push them into implementing management strategies for reducing the clutter—that is, deleting messages without reading them. One consumer's comment exemplified the frustration many consumers have with the volume of messages:

I dislike it. I don't know. I get 25 e-mails a day just off of five registrations. I find myself all day going to my site, starting at the top to the bottom, click them all—delete.

—*Novice CD shopper, male*

As consumers receive e-mails, faxes, and paper mail more frequently from companies, they begin to view the content as intrusive, rather than valuable. Consumers we surveyed considered communications that arrive less frequently and concentrate on their expressed interests the most valuable, simply because these communications allow the consumers to focus on the information provided.

Deepen Knowledge of Consumer Needs and Desires

Technology solutions such as campaign management applications allow companies to engage consumers in ongoing dialogs about their needs, learn a little more about the customer with each exchange, and respond in a very targeted way. For example, application developers such as Broadbase, E.piphany, Revenio, Siebel, and Teradata help companies get the most from their data stores of consumer information. Tools such as Revenio Dialog's "Traffic Cop" help to manage the ongoing dialog between businesses and their customers, thereby allowing for better personalization (see textbox "Managing Communication Traffic").

Efforts such as limiting the number of messages so the customer is not overwhelmed by unwanted information, or making sure the company does not request the same information twice, enable companies to leverage the power of personalization to deepen customer relationships rather than put customers off.

Managing Communication Traffic: Revenio Dialog

Online companies such as Flooz.com, myTeam.com, and Lycos are using Revenio's software to set up electronic dialogs that anticipate customers' questions, and engage customers in online discussions that collect a bit of customer information with each communication. Revenio developed a scenario to illustrate how the software could be adapted to help travel agencies deepen their customer relationships (see Table 3-1).

This ongoing exchange enables the company to uncover the interests, needs, and preferences of its customers. At appropriate times (when a customer needs more assistance, for example), the software can bump the dialog to another communication channel, such as a call center. Thus, these interactive exchanges are managed as "conversations" that enable companies to respond with highly personalized communications.

Table 3-1
Planning a Cruise: "Booking-to-Embarkment" Dialog

Confirm Booking Through Customer's Most Preferred Channel

The dialog is triggered when a customer books a cruise through the call center. An e-mail confirms the arrangement. If the e-mail cannot be delivered, Revenio Dialog automatically queues its letter shop and sends the confirmation by direct mail.

Customize Trip to Customer Preferences

Revenio Dialog automatically sends an e-mail, asking for customer preferences like dinner times, and links the customer to the agency's Web site, which offers a choice of excursions. If the e-mail cannot be delivered, a phone call is placed to set up the itinerary.

Offer Unique Incentive Based on Customer Value

The travel agency sends repeat customers an offer for a free onboard show, using the information about preferred dinner times to determine which show best fits the customer's schedule.

Extract Additional Value

To increase profitability, the agency encourages customers to upgrade their cabins. Customers most likely to upgrade are determined by a scoring model and sent a special offer. The cabin upgrade is confirmed with a phone call.

Build Loyalty and Generate Repeat Business

After the cruise, the travel agency continues to nurture loyalty by asking for feedback on the cruise experience and by personalizing communications to keep their cruise experience alive, thus starting a new dialog with the customer.

Source: Revenio Inc., www.revenio.com, 2000.

Build Value-Added Learning Relationships

With personalization, companies can enhance the value exchange of the business-consumer relationship. We are already seeing new technology-enabled, information-based relationships emerging that help businesses respond directly to an individual consumer's needs and preferences. One consumer described how targeted information and promotional samples enhanced her shopping experience and solidified her ongoing relationship with the company by stimulating repeat purchases.

The company that I order from sends me a monthly newsletter and free samples. It's very cool. I enjoy that. So I buy more stuff—it's fun. I can't wait to get that every month!

—Advanced CD shopper, married female, early 30s

MANAGING RISK EFFECTIVELY

Although new methods of personalization offer many opportunities, there are also many risks in bridging the gap between the old and the new worlds. In order to take advantage of the possibilities of gaining value-added benefits, customers must engage in more than a simple exchange of money for goods and services. Whereas most consumers are comfortable walking into a store, selecting the products they want to purchase, paying in cash, and never once having to reveal who they are to anyone, new opportunities for personalization won't work if consumers are unwilling to share information. Companies must develop a deep understand-

ing of the dynamics of information use and exchange in order to implement successful personalization strategies.

Use Information Appropriately

Fortunately, most consumers, especially CD shoppers, are willing to share information if they receive something of value in return. However, just as in relationships with friends, there are certain kinds of information that are off limits in business-consumer relationships. One consumer commented that he is willing to share almost anything about himself—as long as it isn't too personal.

... the virtual world is just a cornucopia of stuff.... You might as well take advantage of it all. ... So any [information] that I can give them to help me, as long as I don't find it too personal I guess, I don't mind at all.

—Advanced CD shopper, single male, early 40s

“As long as I don't find it too personal” is a big exception, however. When companies ask for information that doesn't appear to be relevant to the inquiry or purchase being made, consumers are likely to bristle—to interpret the request as invasive and disrespectful. One online shopper commented on his frustration when a company would not let him complete his order without giving his home phone number.

I was ordering a book today, in fact. And I have no qualms about giving my work phone number, but I skipped the blank where they wanted my home

phone number. And it (the order form) flips to the next screen and it says, "Oh, you've left out your home phone number." And I said, "No kidding." Well, you can't buy the book unless you give them your home phone number.

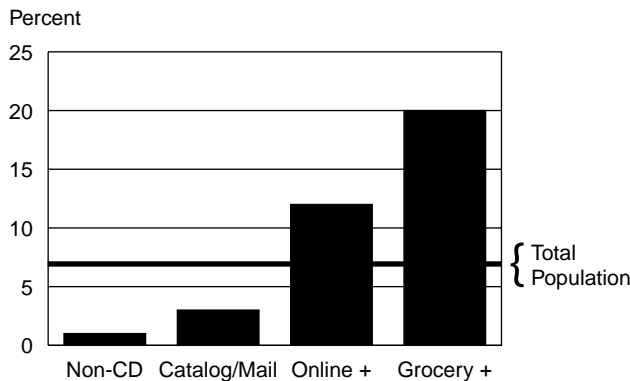
—Advanced CD shopper,
married male with older
children, mid-50s

Such requests for information do more damage than companies realize. Indeed, companies that insist on collecting information a consumer isn't willing to share are encouraging suspicious consumers to falsify information. Since a database is only as good as the information that goes into it, this

is counterproductive at best. In fact, survey data indicate that a small number (7%) of consumers are submitting false information to Web sites and stores to protect their privacy (see Figure 3–1).

We looked at different CD shopper groups (see textbox, "Exclusive Categories of Consumer Direct Shoppers" on page 30) to explore possible differences among people who shop in the CD channel. We found that the most sophisticated CD shoppers, including Online+ and Grocery+ shoppers—those sophisticated, relatively affluent customers most companies are trying to attract—were much more likely to have provided false information than non-CD and catalog/mail shoppers. (About 12% of Online+ and 20% of Grocery+ shoppers falsified their information.)

Figure 3–1
Some Actively Seek to Remain Anonymous
(Percent of consumers who have given false or incorrect information to Web sites or stores in the last 12 months)



Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

Address Heightened Privacy Concerns

The privacy issue is especially hot in the North Atlantic countries because people are afraid the technological advances of the digital revolution are eroding their privacy. Indeed, the vast majority of U.S. residents are concerned about their privacy, a concern that has been increasing for the past two decades. In a 1978 survey, 64% of respondents were either “very concerned” or “concerned” about such threats; by the year 2000, more than 80% expressed such fears (see Figure 3–2).

Privacy concerns are higher for CD shoppers than for non-CD shoppers in the United States. Our survey shows 86% of CD shoppers are concerned about threats to their

privacy while only 76% of non-CD shoppers are concerned (see Figure 3–3). Among CD shopping groups, we don’t see much difference—concerns are high across the board, ranging from 84% of the Online+ shoppers to 87% of the Catalog/Mail shoppers.

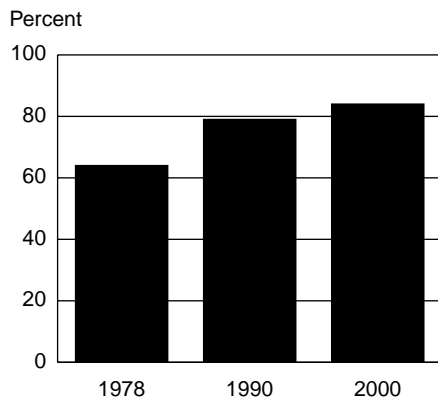
Concerns May Be Leveling Off

While there seems to be plenty of concern about threats to privacy and reasons for consumers to shy away from sharing information online, the news is not all bad. Although general concerns about privacy have been on the increase for many years, a closer examination indicates that, as online experience grows, privacy concerns seem to be leveling off in the United States.

Exclusive Categories of Consumer Direct Shoppers

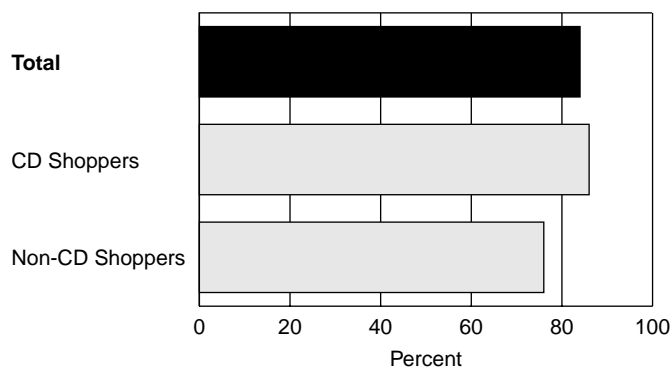
- *Non-CD*. Households that have not made a remote purchase in any CD channel in the last 12 months.
- *Traditional Catalog/Mail*. Households that have shopped from catalogs, direct mail ads, newspaper/magazine ads, television, radio, or the yellow pages in the last 12 months. Excluded are those who have also engaged in the more sophisticated channels of online or grocery delivery shopping.
- *Online+*. Households that have shopped online in the last 12 months, excluding those households who use a grocery delivery service. Most of these households also use the traditional CD channels.
- *Grocery+*. Households that have used some form of remote-order home-delivery grocery service in the last 12 months. These households also use other CD channels.

Figure 3–2
Privacy Concerns Have Increased in the Past Two Decades
(Percent of U.S. residents who are “very concerned” or “concerned” about threats to their personal privacy)



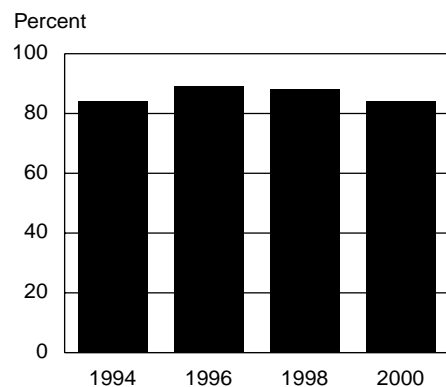
Source: Louis Harris & Associates and Alan Westin, Privacy Surveys; Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

Figure 3–3
CD Shoppers More Concerned About Privacy
(Percent of population that is “very concerned” or “concerned” about threats to personal privacy)



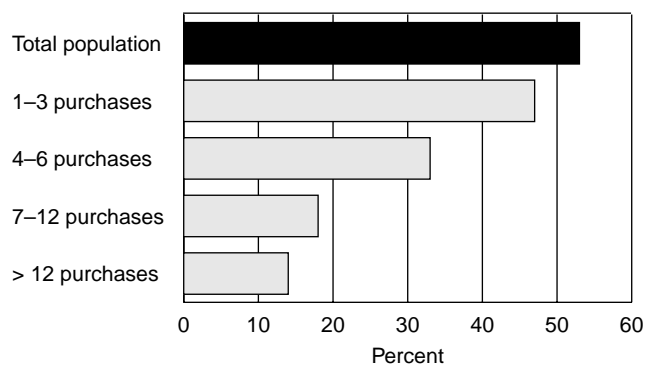
Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

Figure 3–4
Privacy Concerns May Be Leveling Off in the United States
 (Percent of consumers “very concerned” and “concerned” about threats to their personal privacy)



Source: Louis Harris & Associates and Alan Westin, *Privacy Surveys*; Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

Figure 3–5
Fear of Credit Card Fraud Decreases Dramatically with Experience
 (Percent of Online+ shoppers saying that fear of providing credit card information online is an extremely important reason for not shopping online more frequently or at all, by purchases/year)



Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, International Household Survey, 2000.

In the past few years, the number of people fearing threats to their privacy has declined slightly. Although small, this decline may indicate a general leveling off of concern. Indeed, alarm about loss of privacy in the United States peaked in 1996 at nearly 90% when the Internet was young, and declined to 84% in 2000 (see Figure 3–4). As more people become more familiar with the Internet and the practices of online companies, privacy concerns may decline even further. This is a good sign for online and other CD businesses.

Experience in the CD Channel Quells Fears

Experience online—and with other forms of remote shopping such as catalogs—seems to quell one of the biggest fears of CD shoppers: credit card fraud. We asked consumers in the United States why they don’t shop online more often or at all. The major reason for 53% of the population is that they are afraid to provide their credit card numbers online, but the percentage goes down significantly for those who shop online most frequently (see Figure 3–5). While nearly half of all infrequent Online+ shoppers cited fear of credit card fraud as an extremely important reason for not shopping online more often, only 14% of frequent Online+ shoppers did.

Not All Information Is Equal

Not all kinds of personal information are equal. Some are far more sensitive in nature, and the types of information considered personal or sensitive often vary by individual. However, most people in the United States agree that financial information, medical and health information, and especially

their Social Security Numbers are sensitive (see Table 3–2).

Consumers Are Sensitive to the Information Hierarchy

Focus group participants ranked their comfort levels in sharing these different kinds of information with companies. The analysis of these rankings reveal a hierarchy of information consumers are willing to share (see Table 3–3 on page 34). At the early stages of a relationship (evident in Tier 1 and Tier 2), consumers prefer to remain anonymous. As a consumer decides to make a purchase from a company, he or she is willing to share more information as deemed appropriate. Most shoppers are willing to share information with trusted companies at early stages of the relationship, if the information request is limited to demographic or categorical information and does not require them to reveal their identities.

CD Companies Are Not Among the Trusted Elite

Consumer comfort in providing information to companies varies by industry. Louis Harris and IBM conducted a survey of consumers in the United States, as well as Germany and the United Kingdom, which asked consumers how much confidence they had in different types of companies and organizations that collect information to provide products or services. Banks, which deal with some of the most sensitive information, earned the highest levels of trust, with 33% of respondents saying they were “very confident” that banks handled their personal information properly (see Figure 3–6 on page 35). In the United States, this

*Table 3–2
Sensitive Information
(Percent of online users “always” or “usually” comfortable providing ... to Web sites)*

Very Sensitive	
Social Security Number	1
Credit card	3
Phone number	11
Income	17
Medical information	18
Hit or Miss	
Postal address	44
Full name	54
Computer information	63
Age	69
Comfort Zone	
E-mail address	76
Favorite snack	80
Favorite TV show	82

Source: AT&T Labs-Research, Beyond Concern: Understanding Net Users’ Attitudes About Online Privacy, Technical Report TR99.4.3.

Table 3–3
The Information Hierarchy

Tier 1: Remain Anonymous

Consumers are willing to share information that does not reveal their identities. This type of information includes favorite snack, TV show, or hobbies. Some mentioned they would share their name, but only the first name, since a last name might mean companies could track them down and contact them.

Tier 2: Share Categorical Information

Consumers are willing to share demographic or categorical information, such as age or job title. Some were willing to share information that helped the company classify them, without giving the company the ability to identify them as individuals. For example, they might share their zip code, but not their phone number.

Tier 3: Share Relevant Purchase Information

Many consumers placed qualifications on when they would be willing to share more personal information. For example, when they were about to make a purchase, most were willing to share information relevant to the purchase like address or phone number, in case of a problem with the order.

Tier 4: Not Willing to Share at All

The Social Security Number is the piece of information consumers are least willing to share; they do not perceive it as being relevant to a purchase. If the Social Security Number fell into the wrong hands, many consumers fear they could become victims of identity theft.

Source: Institute for the Future/Peppers and Rogers Group, *Personalization: Managing Opportunity and Risk in the Consumer Direct Channel*, Focus Groups with CD Shoppers, January 2001.

probably reflects the great trust placed in the cash and checking systems and the astounding accuracy of these systems backed by guarantees of the Federal Reserve.

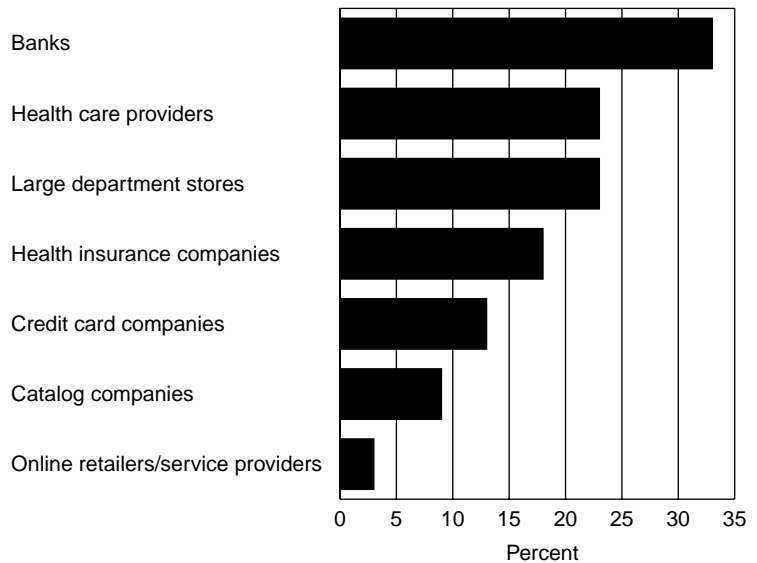
In contrast, health insurers and credit card companies have dramatically lower confidence ratings, 18% and 13% respectively. CD companies have a challenge to overcome—catalog and online retailers come in at the bottom of the list, with only 9% and 3%, respectively, having confidence in them. Worse yet, a cynical 30% said they are “not at all” confident with online retailers! The extremely low rating for online retailers may reflect the newness of the market and the remoteness of its interactions, but the fact that the two biggest CD channels landed at the bottom of the list emphasizes the importance to the CD industry of addressing privacy concerns.

**CONCLUSION:
PRIVACY CONCERNS ARE MAJOR
ROAD BLOCKS**

Although technology solutions open the door for new kinds of opportunities to create more personalized relationships in new channels, consumer concerns about how personal information will be used continue to be a major barrier. Indeed, privacy and trust issues will continue to plague CD businesses until they tackle the problem head on.

If these companies don’t act on their own initiative, government regulators may step in and require compliance from all companies dealing with customer information. The next chapter explores the public debate over privacy protection and discusses the wide range of regulatory approaches in effect across the North Atlantic region.

*Figure 3–6
Consumers Have High Confidence in Banks; Little Confidence in CD Companies
(Percent who are “very confident” that ... handle their personal information properly and confidentially)*



Source: Louis Harris & Associates, *IBM Multi-National Consumer Privacy Survey*, November 1999.

PROTECTING CONSUMERS' PRIVACY: REGULATORY RESPONSES IN THE UNITED STATES AND EUROPE

Many believe that personalization is the CD channel's most powerful marketing feature. In order to reap its benefits, however, as well as survive into the future, companies must be able to respond to consumers' growing concerns about the privacy of their personal information.

As new media for interacting and conducting transactions with shoppers proliferate, a monolithic infrastructure is emerging that allows the seamless flow and ubiquitous availability of information on a global network. Indeed, the Internet has introduced a new dimension to the ongoing discussions about privacy. That new dimension has implications for the continued growth of newer CD channels as well as the vitality of more established CD players such as catalog and direct mail companies. As the CD market continues to evolve, growth opportunities for companies will become less bounded by the need to have a physical global presence, but disparities across regulatory requirements in different countries restricts their ability to utilize information consistently across national borders. Many argue that the profit-making opportunities for CD companies depend on their ability to gather, process, and utilize information effectively and efficiently. In that case, the extensive information infrastructure is the life support system of the CD channel.

Therein lies the crux of the issue for regulators—what role does the government play in creating a balance between protecting the privacy of individuals and supporting the evolution of an increasingly global digital marketplace? In fact, there is a whole spectrum of regulatory responses, national and international, attempting to tackle this issue. Proposed solutions range from industry self-regulation to government-imposed regulatory guidelines.

THE CHALLENGE OF REGULATING A GLOBAL MARKETPLACE

Since there is no way (yet) to control and guarantee the security of personal information, discussion at the regulatory level revolves around guidelines, best practices, and minimum standards more than liability and enforcement. The existing foundation of privacy protection regulation addresses, first and foremost, threats to personal privacy posed by governments. But as personal information becomes the lifeblood of modern com-

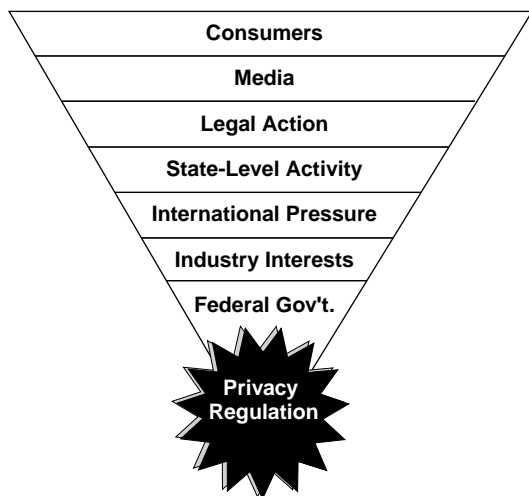
merce, the need to extend privacy protections to the private sector becomes paramount. Regulators must address the challenge of balancing the commercial opportunities in the networked global marketplace against real threats to consumer privacy. It is not a surprise that the regulatory responses to threats against consumer privacy have been varied, as they reflect a wide spectrum of diverse cultural values, political processes, and commercial interests across the North Atlantic.

U.S. APPROACH: BOTTOM-UP

In addressing growing concerns about information privacy, abuses, and violations, the U.S. government uses a sectoral approach that relies on a combination of government regulation, legislation, and self-regulation (see Figure 4–1). The Federal Trade Commission (FTC) is responsible for organizing the federal government's effort to create a more comprehensive online privacy policy. The FTC has turned to the policies on broader privacy issues presented in the Department of Health, Education, and Welfare (HEW) report *Records, Computers, and the Rights of Citizens*, released in 1971. These policies, which define the ethics of fair information practices for government use of data, have become the foundation for discussions of privacy protection in the private sector as well. They include:

- *Notice*. Data collectors must disclose their information practices before collecting personal information from consumers.
- *Choice*. Consumers must be given options with respect to whether and how personal information collected from them may be used for purposes beyond those for which the information was originally provided.
- *Access*. Consumers should be able to view and contest the accuracy and completeness of data collected about them.
- *Security*. Data collectors must take reasonable steps to ensure that information collected from consumers is accurate and secure from unauthorized use.

Figure 4–1
The United States Takes a Bottom-Up Approach



Source: Institute for the Future

In general, the government has been hesitant to pass new regulations, and has, for the most part, supported industry self-regulation, which aims to have businesses implement processes in line with the fair information practices outlined by the FTC, without governmental intervention. However, in the wake of several well-publicized, major privacy violations involving high-profile players in the New Economy, including RealNetworks, Toysmart, and Netscape, and public outcry over threats to personal privacy, support for some form of national legislation has mounted.

In the last year, as a result of growing consumer mistrust, companies responsible for leading self-regulatory efforts, such as Amazon and DoubleClick, have been closely scrutinized. This has led to swarms of negative publicity about seemingly harmless, routine business activities (a privacy policy update and proposed new service announcement, respectively) as opposed to actual violations. Perhaps in response to this general atmosphere of mistrust, many industry leaders such as Hewlett-Packard, Intel, and America Online have shifted course in favor of using national legislation to set minimum standards of privacy protection, while industry consortia and groups like the U.S. Chamber of Commerce and Direct Marketing Association remain strongly opposed to any federal online privacy legislation. Add to this mix of competing interests numerous state initiatives and pressures from privacy advocacy groups and trading partners, and the complexity and momentum behind this issue become obvious.

Current State of Affairs

For the most part, the foundation of privacy protection in the United States is built on laws and court rulings from the predigital age. More recently, at both the federal and state levels, legislators have focused on specific cases of abuse rather than comprehensive legislation addressing consumers' privacy concerns.

Federal Legislation

There are a number of federal laws on the books that touch on the issue of privacy regulation (see textbox, "Current Laws..." on page 40). But in general, these laws have been enacted to cover specific aspects of privacy law as they arise, as in the case of the Right to Financial Privacy Act (RFPA), which targets the financial industry. Most of these laws were enacted more than two decades ago, before the digital revolution.

As new issues emerge in the digital economy, we are witnessing more of the same—federal legislation on specific aspects of the privacy issue. The U.S. Congress has passed the Children's Online Privacy Protection Act (COPPA), the Health Information Portability Act (HIPA), and the Gramm-Leach-Bliley Act (GLB), governing the use of information by financial institutions. Although numerous other bills and initiatives have been introduced at the federal level, the only bills that seem to work their way through the law-making process are those that deal with specific issues of abuse.

For the most part, the foundation of privacy protection in the United States is built on laws and court rulings from the predigital age.

Current Laws Shaping U.S. Privacy Policies

- *Fair Credit Reporting Act of 1970 (FCRA)*. The FCRA broadly regulates the consumer reporting agencies in the interest of protecting the confidentiality and privacy rights of the consumer. The FCRA requires credit investigations and reporting agencies to make their records available to the subjects of the records, provides procedures for correcting information, and permits disclosure only to authorized customers.
- *The Privacy Act of 1974*. This act requires federal agencies to adopt minimum standards for collecting and processing personal information, and to publish detailed descriptions of these procedures. It also limits making such records available to other public and private agencies or parties and requires agencies to make records on individuals available to those individuals upon request, subject to certain conditions and exclusions. The act was last amended in 1989.
- *The Right to Financial Privacy Act of 1978 (RFPA)*. The RFPA provides some confidentiality regarding financial records of bank depositors by governing the transfer of financial records. The RFPA attempts to strike a balance between the privacy interests of consumers and the interests of law enforcement officials. Generally, banks are prohibited from disclosing client payment information to the government without a court order.
- *The Electronic Communications Privacy Act 1986 (ECPA)*. The ECPA extends the coverage of Title III of the Omnibus Crime Control and Safe Street Act (commonly known as the Wiretap Act) to new forms of voice, data, and video communications. These include cellular phones, electronic mail, computer transmissions, and voice and display pagers. This act makes illegal the interception and use of private data transmissions.

State Legislation

State governments have been quicker to respond with legislation addressing consumer concerns about privacy. In fact, most of the experimentation with different regulatory approaches to the privacy issue takes place at the state level. Indeed, the states often set the national legislative agenda, especially large states such as California, Michigan, New York, and Texas.

In 1998 alone, state governments introduced 2,367 consumer privacy bills, and more than 700 were enacted into law. However, state legislation also has dealt with specific online privacy issues, such as prohibiting business from refusing service to consumers who do not want to provide personal information. Drafting effective online privacy protection legislation at the state level is extremely challenging given the borderless nature of the Internet. As at the federal level, state governments have so far avoided broad, comprehensive privacy legislation. But as state legislation regarding consumer privacy protection proliferates, the federal government comes under pressure to harmonize the disparate state laws.

Privacy Protection Through Legal Recourse

Without comprehensive laws governing the protection of an individual's privacy, U.S. consumers have only the judicial system to remedy violations. Currently, there are two forms of action a company accused of violating consumers' privacy might encounter. First, the FTC might investigate and file a complaint as it did in the case of Toysmart, which was accused of violating its stated privacy policy by auctioning its customer databases

as an asset during bankruptcy proceedings. Or, second, companies could face a class-action lawsuit filed on behalf of consumers seeking remuneration for damages incurred as a result of privacy violations.

For example, in 1999, Minnesota and 38 other states sued U.S. Bancorp on behalf of consumers enraged over the company's practice of sharing customer account information with third parties. Consumers argued that U.S. Bancorp sold their information to companies like MemberWorks, a telemarketer of nonfinancial products and services, which billed them for goods they never ordered. U.S. Bancorp settled these suits by paying over \$6 million in consumer restitution and monetary damages, and agreeing to stop the practice of sharing customer information with third parties.

Similarly, the class-action suit filed against RealNetworks in November 1999 was the first to target an online player and cast the spotlight on threats to people's privacy in the networked world of the Internet. In this case, RealNetworks was accused of violating customers' privacy when it was revealed that its RealJukebox software was covertly collecting information about its users. The software allows users to download and play MP3 files from the Internet, convert regular music from CDs into digital files, build personalized playlists, and transfer music to portable devices. However, most users were not aware that the RealJukebox software also transmitted daily updates to RealNetworks about their musical preferences and listening habits. At the time, this practice of collecting information was not disclosed in the company's privacy policy. Since then, numerous other online

Without comprehensive laws governing the protection of an individual's privacy, U.S. consumers have only the judicial system to remedy violations.

companies have come under attack by state attorneys general for actions outside the scope of stated privacy policies or for using tracking technologies such as cookies or Web bugs.

Although some might argue that the judicial system in the United States provides adequate recourse for consumers in the event of a privacy violation, others maintain that individuals risk further exposure and loss of privacy in pursuing legal action, since much of their personal information becomes part of the public record. For instance, in a case where a man's HIV+ status was improperly disclosed to his ex-wife by a Long's Drug-store pharmacist, he opted to settle his suit out of court rather than risk further exposure through the court record and media coverage of the case.

What's Next on the U.S. Legislative Agenda

As the new presidential administration settles into office, and the dot.com economy continues its downslide, many believe that privacy legislation will sit on the back burner in the near term. Currently, the 107th Congress is scheduled to address numerous bills on the topic (see Table 4–1). However, many experts do not believe that the proposed bills will make their way through the legislative process in the near future.

Some privacy experts anticipate more piecemeal legislation to emerge eventually, addressing such privacy hot-button issues as “spam,” customer profiling, and the sale of Social Security numbers. Moreover, bottom-up forces, including high levels of consumer concern, increasing state legislative

Table 4–1
A Few of the Online Privacy Bills in the 107th Congress

Online Privacy Protection Act of 2001 (HR 89)	Requires the FTC to create regulations to protect the privacy of personal information. <i>Sponsor:</i> Rep. Rodney P. Frelinghuysen (R-NJ)
Electronic Privacy Protection Act (HR 112)	Prohibits the making, sale or use of an information-collection device without proper labeling or notice and consent. <i>Sponsor:</i> Rep. Rush D. Holt (D-NJ)
Consumer Internet Privacy Enhancement Act (HR 237)	Protects the privacy of consumers who use the Internet. <i>Sponsor:</i> Rep. Anna G. Eshoo (D-CA)
Consumer Online Privacy and Disclosure Act (HR 347)	Requires the FTC to create regulations to protect the privacy of personal information collected from and about individuals on the Internet. <i>Sponsor:</i> Rep. Gene Green (D-TX)
Privacy Commission Act (HR 583)	Establishes the Commission for the Comprehensive Study of Privacy Protection. <i>Sponsor:</i> Rep. Asa Hutchinson (R-AK)

Source: Electronic Privacy Information Center

activity, high-profile cases of industry privacy violations, pressure from European trading partners, and concessions by industry leaders, indicate the potential for reaching consensus in support of national legislation setting standards for a minimum level of consumer privacy protection.

EUROPEAN APPROACH: TOP-DOWN

In 1981, following the Organisation for Economic Co-Operation and Development's (OECD) publication of guidelines concerning personal data collection and management, the Council of Europe convention established basic principles for the processing of such data. During the 1980s, many countries in Europe adopted their own data protection laws, each varying in scope and strength.

In order to harmonize the various national laws, the Commission of the European Union proposed the EU Data Protection Directive. Its goals are to ensure that all member states concurrently promote commerce among them and protect privacy by restricting the transfer of personal information. After much discussion, the directive was passed in 1995 and went into effect in October 1998. Each of the 15 member states is required to enact national policy that follows the provisions of the directive. The directive establishes basic minimum rules for privacy but allows member states some autonomy to customize national laws (see Figure 4-2).

A Consumer's Right to Privacy

As in the United States, the basic rules of the directive draw on a common core of basic principles regarding privacy protection.

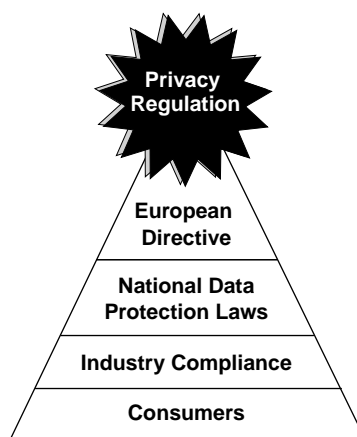
However, the notion of an individual's right to privacy is much stronger in Europe, and this is reflected in the EU's interpretation of the basic privacy principles. The directive asserts that:

Member states shall protect the fundamental rights and freedoms of persons, and in particular their right to privacy with respect to the processing of personal data.

The EU interpretation of the core principles of privacy protection defines certain consumer rights and requires an administrative body to oversee data collection and processing activities. Guidelines in the directive include:

- Data should be collected by data controllers *for a specific purpose*; it can only be used for this purpose, and it should be accurate, relevant, and up to date.

Figure 4-2
The European Top-Down Approach



Source: Institute for the Future

This view of an individual's fundamental right to privacy sets a much higher standard for consumer privacy protection in Europe than in the United States.

- Subjects of the data collection have a *right to access the data*, and have a right to have incorrect data corrected.
- Data subjects are entitled to be informed about the identity and purpose of data controllers, and have a *right to object to the processing of their personal data*.
- Each country will have an *independent data supervisory authority* to enforce the rules and to register the activities of data controllers.

This view of an individual's fundamental right to privacy sets a much higher standard for consumer privacy protection in Europe than in the United States. In fact, the directive requires that the transfer of personal data from the EU to a non-EU country can take place only if there is "adequate protection" of that data. There are some exceptions: for example, if the data subject has consented, if the transfer is necessary for a contract, and if the transfer is necessary to protect the interests of the data subject. The EU considers most non-EU countries, such as Switzerland and Hungary, which have some form of national data protection law in place, to have adequate protection. The United States, which currently has no national legislation protecting an individual's privacy, falls into this category.

Data Streams Protected by EU Directive

According to the EU, the directive may be used to block the flow of personal information from Europe to countries that do not have adequate protection. Protected data flows

include online and offline data transfers, human resource records, customer directories, and other data integral to business processes.

In effect, this restriction would mean that businesses from countries that fail to meet the directive's adequate protection standard would not be allowed to collect information about European citizens. This would affect any company, most notably CD companies, that collect personal data. Multinational corporations will have an especially difficult time, since even basic data about their overseas employees and customers would not be transferable to offices in a country that does not meet the adequate protection requirement.

Moreover, European companies operating in the U.S. may be at a potential disadvantage to their U.S. competitors since they are subject to the terms of the directive. For instance, Royal Ahold—a Dutch grocery retailer which operates over 1,000 supermarkets in the United States and owns a majority stake in the online grocery retailer, Peapod—is subject to the EU's data protection requirements. This puts Ahold's U.S. operations at a disadvantage as they compete against U.S. retailers (such as Wal-Mart) that rely heavily on customer information to gain a competitive advantage in the marketplace.

A good example of what can come out of the conflict between different international approaches to privacy protection is the lawsuit the Swedish government filed against American Airlines. In 1995, the Swedish government ordered American Airlines to remove all health and medical data about Swedish passengers, including special di-

etary needs, from their Sabre reservation system. Although the information was held by Sabre in the United States and seemed to be in the interest of the consumer, the Swedish courts ruled against American Airlines.

In an effort to protect trade with the EU (which the White House estimates to be \$120 billion a year), the United States proposed a “Safe Harbor” agreement—a voluntary agreement by companies that operate in Europe to collect and maintain personal data of Europeans according to the EU rules (see textbox, “Taking Refuge...” on page 46). After two years of talks, the EU Commission accepted the Safe Harbor agreement, which became effective in November 2000. However, the EU still maintains that the United States needs some form of national legislation to ensure the enforceability of the Safe Harbor terms.

The Impact on Consumer Direct: Limited, For Now

The data protection standards set by the EU will undoubtedly have major repercussions for the data privacy policies of businesses operating in the EU. No company building a serious global presence—online or offline—can ignore the \$7 trillion European market. Even on the other side of the regulatory spectrum, in the United States, where the government has backed business self-regulation efforts, there seems to be some potential for the interested players to reach consensus on some form of national legislation setting minimum standards for privacy protection.

But how will data protection impact the CD channel? In the short term, expect the impact to be limited. Major challenges in

interpreting differences across international data protection laws, and conflicting opinions on the actual cost of compliance to businesses will minimize the immediate impact on CD companies.

The Challenge of Interpretation

Fortunately for CD companies targeting the European market, actual litigation like the Swedish case with American Airlines is rare. The EU has not yet strictly enforced the directive even within its own borders. In general, the issue of interpretation remains a challenge not only between the EU and the United States, but on a global level as well. An IFTF workshop with experts on privacy regulation in Europe highlighted ambiguities in the law and the difficulties in applying it to business practices. Across different countries and industries, key words and phrases at the heart of the directive, such as “personal data,” “consent,” “specified purpose,” and “access,” are subject to different interpretations, making enforcement, especially in the online world, nearly impossible.

For instance, some regulators maintain that the business objective of keeping a good relationship with a customer is not necessarily a specified purpose as defined by the directive. The law requires that a business’s specified purpose for data collection and processing be made clear to the consumer, not only specifying the benefits the consumer receives in exchange for the information, but also regarding how the company plans to use the information in its internal business practices or with its partners and suppliers.

Most companies provide clear information on the benefits consumers get in ex-

The EU has not yet strictly enforced the directive even within its own borders.

Taking Refuge in Safe Harbor

Under the terms of the Safe Harbor agreement, companies must abide by the following key privacy principles:

- *Notice*. Consumers must be informed of what information is being collected.
- *Choice*. Consumers must be able to stop the use of that information.
- *Onward transfer*. Information can be forwarded to a third party only if the third party agrees to comply with the notice and choice requirements.
- *Security*. Measures must be taken to make sure data is secure.
- *Data integrity*. A company can use the data only for the intended purpose and must ensure that the data is accurate, complete, and current.
- *Access*. Consumers must have the ability to view the data collected about them.
- *Enforcement*. There must be processes in place to resolve disputes.

Companies engaged in trans-Atlantic data exchange with EU member states must apply for Safe Harbor status and membership in the U.S. Department of Commerce's registry of self-regulating companies in order to satisfy the adequate protection requirement under the EU Directive. Businesses that comply with the terms of the Safe Harbor agreement must (1) agree to be monitored by U.S. federal agencies, (2) join a self-regulating body, monitored by the FTC, and (3) report to a data-protection authority in Europe.

As an alternative to Safe Harbor, companies may opt to enter into a data contract that will govern information use. In January 2001, the EU released its latest draft of model contract provisions to be used by U.S. organizations as an alternative to compliance with the EU Directive on Data Protection. The U.S. government voiced its objections to the standard contract clauses proposed by the EU and continues to negotiate the terms that U.S. companies will have to meet.

change for their information, as within the context of a loyalty program, but there is seldom disclosure on how businesses plan to use the information for profiling, data sharing with partners, and other business practices. Though regulators have taken a flexible approach to interpreting the law, business practices such as loyalty programs—cornerstones in many corporate marketing and customer retention strategies—can be an example of unfair data collection under the law if consumers are not adequately informed of the different uses of their private information.

This ambiguity concerning key components of the directive is complicated by the diversity of practices allowed in countries outside the EU. For example, Switzerland, which is not an EU member but has been designated as having adequate data protections in place, does not require the same level of explicit consent for specified purposes. Rather, businesses that obtain a Swiss customer's consent to collect information are free to use the information for customer relationship building activities as long as the company does not sell the collected data.

Similarly, Canada's Personal Information Protection and Electronic Documents Act was designed to meet EU privacy standards. However, it stops short of requiring adequate protection from trading partners because of the economic repercussions of its trade with the United States. Therefore, companies from other countries that are collecting information or sending unsolicited e-mails from outside Canada are not subject to Canadian enforcement. Without international standards for data collection

and processing, conflicting interpretations of the basic principles of privacy protection will make enforcement of the laws very difficult in an increasingly global marketplace.

The Cost of Compliance

There is much debate over what the cost of complying with governmental restrictions on data use may be. A recent industry-sponsored study, *The Impact of Data Restrictions on Consumer Distance Shopping*, released by the Information Services Executive Council, paints a bleak picture for catalog and Internet merchants who rely heavily on customer information as an integral component of their business models. The study estimates that restrictions on data use could increase the total costs of conducting business in CD channels dramatically. Specifically, the study evaluated potential costs for catalog and online apparel retailers and forecasted cost increases between 3.5% and 11%. Researchers assert that these cost increases would result in a \$1 billion "information tax," as retailers pass on the burden of rising costs to consumers.

On the flip side of the coin, if nothing is done to regulate the use of consumers' private data, a recent study released by Forrester Research estimated that Internet businesses could lose over \$12.2 billion in annual sales due to consumers' privacy concerns. Not surprisingly, proponents of fair information practices and permission-based marketing techniques are more optimistic about the potential costs associated with compliance. Many believe that initial investments in information systems and privacy-enhanc-

Many believe that initial investments in information systems and privacy-enhancing technologies to bring companies into compliance will result in more sustainable, long-term customer relationships.

ing technologies to bring companies into compliance will result in more sustainable, long-term customer relationships. Advocates argue that increased loyalty from a company's most valuable customers will generate return on these initial investments and pay off in the long run.

In fact, many argue that compliance will become a competitive advantage in the marketplace. Companies such as Hewlett-Packard are supporting legislation to set minimum standards for privacy protections and have adjusted their own privacy policies and practices out of "enlightened self-interest" or rather, as an effort to protect their customer relationships. Others argue that as customer data rises in relative value as a company asset, companies will be better served by protecting the security of this data. In this way, a company and its customers share the desire to protect the customer's privacy.

Many expect that as consumers become more aware of their privacy options, compliant companies will begin to market their data protection practices as a means of building and reinforcing consumer trust.

**CONCLUSION:
IN A REGULATED WORLD,
CONSUMERS WILL BE THE ENFORCERS**

Even in a regulated environment, policing data protection violations will be extremely difficult as globalization continues and personal information flows well beyond

the boundaries of the North Atlantic. Without international standards, even though countries have privacy laws in place, the actual impact of such regulations may vary significantly across national borders. New laws have given the data protection authorities in the EU and Canada more real power (for example, power to issue injunctions and halt data processing), but so far they have used their powers in very limited ways. Most are opting instead to work with industries and partners to develop solutions for working within the guidelines of the law.

In the end, most experts concede that in practice, governments do not have the ability to track businesses' use of information, especially in an increasingly global marketplace. However, a regulated environment will place pressure on businesses to conform to minimum standards such as obtaining consent from consumers to use their information, and providing consumers with access to their information profiles. Indeed, permission-based marketing practices may become the cost of entry for participating in global commerce. Some experts anticipate that regardless of the regulatory framework, only the most egregious privacy violations will be prosecuted. Ultimately, enforcement power will reside with consumers. A regulated environment empowers consumers to seek recourse if they feel that businesses have abused their personal information or invaded their privacy.

MANAGING THE OPPORTUNITIES AND RISKS OF PERSONALIZATION: KEY BUSINESS STRATEGIES

“Companies will understand the value of the information and will never compromise the customer information if they treat it as a valuable asset.”

—*Executive for direct marketing technology company*

In this increasingly complex world, information fuels economic growth and creates new opportunities for businesses. The ability to balance the appropriate use of new technologies and personal service, manage the flow of information, provide a secure marketplace, and protect consumer privacy will be critical components of success. As information flows across global networks, there is an increasing threat of abuse, as well as growing consumer awareness of how their personal information is used and what value it has in the marketplace. Regulatory frameworks will emerge to protect consumers against privacy violations and also provide them a method of recourse.

In a competitive market, where a company's most valuable assets are its customers, building and maintaining trusted relationships is imperative. Companies that rely on information in building these Learning Relationships must address consumer privacy concerns, or risk their most valuable asset.

Key strategies for success include:

- Prepare for technological change.
- Create mutually beneficial Learning Relationships with customers.
- Utilize information to meet individual needs.
- Create an organizational structure to support data compliance.
- Leverage technology to enhance privacy protection.
- Give consumers control over their information.

PREPARE FOR TECHNOLOGICAL CHANGE

One of the greatest challenges facing businesses and regulators is the pace of technological change. In a relatively short time, the Internet has transformed information into a free-flowing river easily accessible to virtually anyone with a modem and computer. Moreover, technology developers are creating new types of information, new devices for collecting information, and new ways to make information profitable. Given this rapid pace of technological development, no one is quite sure how to control—much less protect against—misuse.

Create Flexible Approaches to Data Protection

Privacy is a strategic issue for organizations across a wide spectrum of industries. Investing in understanding how new information can be used, and the privacy implications of its use, will be critical for companies who leverage data compliance as an asset. To win the trust of consumers, companies must work with industry associations to agree to higher standards than the minimum set by regulators.

Integrate Privacy Protection Functions into Technology Design and Implementation

Companies must consider the implications of new technologies on customer privacy before implementing them. As we move to a more regulated environment, integrating privacy functions into new technology designs will be critical for meeting privacy protection standards. As consumers become aware of options for privacy protection, they will look for companies that provide them control over the flow of their information. Businesses will do well to use technologies that empower consumers to control their own information so they can negotiate access to benefits or products and services.

CREATE MUTUALLY BENEFICIAL LEARNING RELATIONSHIPS WITH CUSTOMERS

Technology now enables companies to leverage consumer data and provide a much higher level of service, including information, products, and services tailored to an individual's specific needs. However, to cre-

ate an ongoing, trusted relationship with customers, companies must be able to articulate a clear value exchange so that consumers will choose to share their information.

Getting Consumer Consent Reinforces the Value Exchange

Consumers do not want their private time invaded by people they don't know, especially for things they don't want. They want to be certain that if their information is used, it will be in their own interests. As companies look to build profitable customer relationships, informing customers about how their information will be used and obtaining their consent becomes a useful tool in making the value exchange explicit.

Invest in Deepening Customer Relationships

Building, maintaining, and deepening customer relationships require substantial investment in developing the right balance of cost-saving technology solutions and high-value, high-cost personal service. Although the Internet has opened up many more options for providing consumers access to services at incredible cost savings, it has not completely eliminated the need for human interaction, especially for services. This balance of technology with the human component is critical to fostering trust with skeptical consumers concerned about invasions of privacy. Establishing an ongoing, interactive dialog allows businesses to adapt their offerings to the changing needs of their customers, while building the foundation of trust in the relationship.

UTILIZE INFORMATION TO MEET INDIVIDUAL NEEDS

Companies now have access to far more information than they can possibly use. Gartner Group estimates that by 2004, the average company will have collected 120 terabytes (120,000 gigabytes) of customer data. It is no wonder that consumers are concerned about privacy, since they are bombarded from numerous directions with requests for information, not to mention the myriad ways that businesses collect information unbeknownst to consumers. Yet many see little direct return on that information exchange. The most challenging question for businesses is not how to get the data but what to do with it.

Provide Value in Exchange for Information

Increasingly, consumers are becoming aware of the value of their information in the marketplace and are using it as a form of currency to gain access to a diverse range of benefits. Many companies today use discounts or coupons to attract customers and interest them in sharing their information. But companies looking to build long-term customer relationships will provide more value by using customer information to respond directly to an individual's specific needs.

Ask Only What Is Necessary

To minimize the possibility of offending a customer by asking for sensitive information, CD companies should always ask themselves if, to complete a transaction, they *need* each bit of information they are asking

Privacy is good for business. It forces the company to be customer-centric.

for. If the answer is no, they shouldn't ask. Consumers are smart. They know what information isn't needed and immediately become suspicious. One of the best ways to avoid offending a customer is to employ the "drip irrigation" technique—with each subsequent interaction with a customer, you ask for a little more information, always keeping in mind that what you ask for has to make sense to the customer. Over time, companies can collect a wealth of information about their customers that can be used to provide better service and products...and all of this can be done without violating anyone's privacy.

CREATE AN ORGANIZATIONAL STRUCTURE TO SUPPORT DATA COMPLIANCE

Privacy is good for business. It forces the company to be customer-centric. Companies need company-wide policies on how to handle privacy—that's critical to the success of an organization. Technology is a small part of this, though. People need to modify it—it's the people who are important.

*—Executive for direct
marketing technology company*

Companies need to understand what they have to lose by mishandling consumer information. To manage this data effectively often requires a new organizational structure where responsibility and authority for data compliance issues are clear.

Appoint Customer Information Officers

The issue of privacy is an integral component of a company's overall strategy for managing customer information. Although businesses may make significant investments in technologies that enable secure transactions or protect the exchange of personal data, ultimately privacy must be addressed by all parts of an organization through all points of contact with the customer. Customer information officers should provide a central voice for privacy within the organization, as well as maintain responsibility for the value and quality of the ongoing information exchange with customers.

Integrate Data Protection Efforts Across Channels

Consumers view a company that uses multiple channels (bricks-and-mortar stores, online services, call centers, and so on) as one entity. Thus, information shared with the company should be protected under a standard set of data protection practices regardless of which channel is used. Although much of the discussion on data protection revolves around the electronic data available online, businesses face an even greater challenge in dealing with the protection of data collected offline (for example, sales force information, manual records, and so on). As companies utilize technology to integrate sales and communications channels, their data-handling processes will become more transparent to consumers. Protecting customer data and making it accessible to consumers across multiple channels will be critical for maintaining consumer relationships.

Address Information-Sharing Concerns

The issue of sharing customer information with partners and other entities along the supply chain will become even more important as companies implement processes to provide personalization and customization to their customers. This means that every partner up and down the supply chain who has access to the information must treat it with the same respect and care that the company with the primary customer relationship does. In addition to informing customers of their own information-sharing practices, companies will need to address such issues as accountability for misuse by partner organizations and responsibility for cross-border complaints. This may be one of the most important elements of future partnership or vendor agreements.

LEVERAGE TECHNOLOGY TO ENHANCE PRIVACY PROTECTION

If privacy is accepted as a fact of life, then it is smart business to develop products that are privacy enhancing rather than privacy encroaching.

—*European data protection officer*

Much of the current discussion about information privacy is driven by new ways of collecting and analyzing new forms of information such as clickstreams, geographic location, usage patterns for products and services, consumer preferences inferred from purchasing behaviors, and so on. Much of the criticism companies have endured is for fairly harmless activities that simply take

place unbeknownst to the consumer. However, more companies are developing creative solutions that will use technology to enhance privacy protection rather than compromise it.

Build In Privacy Protection Options

For the most part, consumers do not object to sharing information with companies. However, they do object when companies don't inform them they are collecting or processing that information, or if they feel information is being collected unnecessarily. Several technologies are emerging that create options for protecting privacy, ranging from anonymous surfing to customer-controlled data profiles. By utilizing these technologies to reinforce Learning Relationships, a company can offer customers a wider range of choices about how they would like to interact with companies and share information. For instance, a customer may be interested in sharing personal information to receive additional product information or services for an upcoming purchase decision. But that same customer may prefer to conduct searches anonymously for other products or types of information. Allowing individuals to choose how they want to interact and use their information will help increase trust and encourage customers to share more information.

Use Technology to Protect Sensitive Information

Consumers are more concerned about some types of information than others. For instance, financial information ranks high on U.S. consumers' list of highly sensitive information. Many credit card companies like

Allowing individuals to choose how they want to interact and use their information will help increase trust and encourage customers to share more information.

New tools are emerging that will allow businesses to let consumers decide on the level of privacy protection they prefer.

American Express and Visa are using new smart card technologies or one-time use card numbers—otherwise known as disposable credit cards that allow consumers to access a unique card number to make a single purchase, which then becomes invalid so no other purchases can be charged—to protect this important data. Other companies offer customers the option of securely storing information such as credit card numbers and shipping addresses, in order to make purchasing easier and encourage repeat buying.

GIVE CONSUMERS CONTROL OF THEIR INFORMATION

You should be able to pull your data out of a company like you can pull your money out of a bank.

—*Online company executive*

In the absence of any one organization's or government's ability to control the flow of personal information, it makes sense to allow consumers to take responsibility for controlling their own information. In fact, as companies adapt to the requirements of a regulated environment, minimum standards concerning basic privacy principles like notice, consent, and access will emerge.

Consumers want to know what companies will do with the information they disclose. Although consumers understand that information is a necessary cost for some services, they *do* want more control over how the information is used or shared. For example, many believe that DoubleClick could

have avoided the outpouring of negative publicity involving its intention to link online data with offline data simply by informing customers up front how they intended to use the information. In the future, successful companies will empower consumers to take control of their own information.

“Opt-in” Solutions

When they are given a choice about how they want their information used, consumers prefer “opt-in” to “opt-out” solutions—that is, they want a company to ask them up front for permission to use their information rather than to assume the right to use it until the consumers tell them otherwise. Many businesses fear the opt-in approach would prove too costly, restricting their ability to attract potential customers or cross-sell products. However, allowing consumers to indicate their interest by opting in enables marketers to target extremely qualified leads. Companies like Lifespire, an online medical information provider, build and reinforce trusted relationships with their customers by allowing them to “opt in” and retain control of how they would like their information used. Providing the opt-in option also saves money; companies don't waste resources communicating with people who are not interested in what they have to offer.

“Volume Dial” Approach

Protecting consumer privacy does not have to be an all or nothing proposition. New tools are emerging that will allow businesses to let consumers decide on the level of privacy protection they prefer. For ex-

ample, Microsoft recently announced its plans to build P3P (Platform for Privacy Preferences) technology into Version 6 of its Internet Explorer Browser. These technology applications would allow consumers to choose the level of privacy they wish to maintain.

Consumers know that to get the benefits associated with the value and convenience provided by CD companies, they must share information. All they want is some say in how that information is used beyond that transaction. Increasingly, companies will have the ability to provide consumers more privacy options by allowing them to decide what kinds of information they would like to receive (e.g., news, product announcements, articles), how often they want to receive it (e.g., daily, weekly, monthly), and through what communication method messages should be sent (e.g., mail, phone, e-mail).

Provide Access

Allowing consumers to access their data profile encourages them to keep records accurate and up to date, and also to provide more information. New information intermediaries like Lumeria or Persona are emerging to allow consumers to build a complete data profile that no one else can access—not even the intermediary. Information is stored on a secure server and can only be unlocked by the owner of the profile. The intermediary can then facilitate the exchange of that information with businesses when the consumers want to, and in some cases compensate the consumers for sharing their personal

information. This creates new incentives for consumers to share information and maintain accurate data profiles.

Give Consumers the Option to Be Anonymous

Most consumers are willing to provide information in exchange for something they want—whether it be information, a product, or a service. However, before they are ready to engage in an exchange, they prefer to maintain their anonymity. At the end of the day, companies must respect consumers' wishes. It may well be that people don't want a world in which they have to keep their information locked up tight, but one in which their personal information is used effectively and respectfully in their interest, with their consent, and under their ultimate control.

Let Consumers Decide When to Start a New Relationship

Many consumers are interested in having a relationship with reputable companies, but they want to control the relationship by choosing when and whom to engage, to interact with and, ultimately, to give their business to. Yet many CD businesses today are forcing consumers into a relationship just to window shop, by requiring them to reveal personal information they don't want to give, or exploiting the relationship by selling their information to third parties. Many consumers in the focus groups expressed their frustration with companies in this new world of shopping. One man explained:

That's the thing that I really dislike when I go to online businesses. Everybody is trying to collect my information.... I want to be able to browse, the same as if I were able to walk into a normal store, without having to give you my driver's license and credit card number and everything else.

—*Novice CD shopper,
male, 42 years old*

Many consumers agreed that companies that require them to relinquish seemingly unnecessary personal information were, in fact, taking control away from them. Ultimately, consumers want to be in the driver's seat in order to make decisions about when, where, and to whom they give their information—and, ultimately, their business.