MEMORANDUM

Date: August 15, 1998

To: Ray Barnes
Tom Cleveland
Mark Tremont
John van Aken

cc: Carl Pascarella
Jan van der Voort

From: Vic Dahir VD

Subject: Incentive Plan Measurements

I am attaching for your consideration and discussion a paper written by Andrzej Lubowski, at my request, on measuring Visa's success. It was written in the context of Visa U.S.A., but I believe the concept and most of the ideas he discusses could easily be modified to apply to Visa worldwide.

What I like about this approach is that it provides a very logical, and I think compelling, link between Visa's mission and objectives and the measurement of our performance. Therefore, it provides a framework that I think everyone, directors included, will understand. I realize there is nothing radically new in the measures Andrzej suggests, and I am as guilty as anyone for dwelling on the problems related to these measures. However, if you agree that the approach is sound, perhaps we should think about how we begin to move towards adopting some or all of these measures rather than continuing to look for something else that probably doesn't exist. I look forward to discussing this with you.

P-0751

GOVERNMENT DEPOSITION EXHIBIT 353

To: Victor Dahir
From: Andrzej Lubowski Andrzej
Re: Measuring Visa's Success
Date: August 6, 1998

I believe that our system of measuring and rewarding for success would benefit from adopting the concept of the Balanced Scorecard. The Balanced Scorecard (see a generic framework as well as a Visa strawman attached to this memo) provides organizations and its executives with a comprehensive framework that translates a company's mission and strategy into a coherent set of performance measures, organized into four different perspectives: financial, customer, internal business process, and learning and growth.

The objective of this memo is to suggest an approach that would lead to:
building alignment between Visa's stated mission and its measures of performance.

Visa's stated mission is:

"to enhance Member profitability and preeminence"

Caveat: Visa's performance measures should reflect only those factors affecting Members profitability and preeminence which Visa can impact. For instance, we are not the ones who shape Members' credit policies, which obviously impact their overall profitability. We also have no say in their acquisition efforts which amount to a significant component of total cost, and hence influence the Members' bottom line. Therefore, it would be inappropriate to tie directly Visa's measures of success to Members' returns.

Given the nature of Visa as an association of competitors, there is no full agreement among all Members about what Visa should do and how it should do it. At the same time, however, all Members seem to agree on the following set of objectives, which should guide the development of our Balanced Scorecard:

Our Members want us to:

- expand product usage - open new and deepen existing markets;
- "keep the factory running smoothly" - assure systems and operations consistency and reliability;
- assure system efficiency - stay on the downward trend of cost curve;
- grow market share vs. non-bank-controlled brands.

Before I suggest a strawman of measures to be considered as a part of our Balanced Scorecard, let me offer a litmus test to apply in order to determine which of the suggested measures, or any other measures, would make a "good measure". A good measure should meet the following characteristics:

- ***Accurate***
  reliably expresses the phenomenon being measured
- ***Objective***
  not subject to dispute
- ***Easy***
  inexpensive and convenient to compute
- ***Harmless***
  does not induce dysfunctional behavior
- ***Holistic***
  avoids the perils of sub-optimization.

What follows is the strawman of measures along the dimension of Members' objectives listed before.

*1. **expand product usage** -*
PCE penetration seems to be a good measure of success in eliminating check and cash as Visa's competitors.

*2. **assure systems and operations consistency and reliability:***
100% up-time of the system should probably serve as a goal, with any deviation from this standard being a negative.

*3. **assure system efficiency:***
Aiming at reduction in unit cost should be one of the objectives, even though we may be approaching the limits of improvement. It is conceivable that occasionally we may even deteriorate on this dimension, given some necessary rework, incremental investments, etc.

That, however, does not negate the relevance of the measure. What really matters is whether Members view it as an important measure, and whether an emergence of a cheaper provider of similar service could affect our future.

There is nothing unique about our situation. When for-profit companies are using ROE, ROTA, EPS, unit cost, error rate or market share, they do not have any guarantee of an uninterrupted progress. Sometime they know up-front that they will deteriorate along some dimensions. When they are restructuring or investing heavily, they know that initially their return will drop. When they discontinue some products or exit some market they know that their overall share will decrease. They are doing what they are doing because they believe that ultimately that makes sense and will pay off in one form or the other.

Sometimes, just to maintain the status quo amounts to a success. Our targets in terms of unit cost, for instance, do not have to always show improvement. Sometimes, slight deterioration should be a reason for getting maximum rating, provided we convince ourselves and the Board why controlled deterioration should be viewed as success.

*4. **grow market share versus non-bank-controlled brands***

Our share of total volume of the general purpose cards or our share versus key non-bank owned brands (American Express and Discover combined) are two potential measures. The first one indirectly captures our relative performance versus MasterCard, the second one doesn't.

Our performance versus MasterCard can still be captured in more specific product categories, where our Members are truly choosing between two associations (debit).

To bring back the concept of four dimensions of the Balanced Scorecard and align our thinking about mission with practicality of our governance structure, consider the following set of measures:

FINANCIAL

Share of PCE
Share of GPC

Maximizing both of them, subject to resource constraints as determined in budget approved by the Board, seem to be superior to any measure of Net Income, which in our case is significantly less meaningful than for a for-profit company.

This approach, unlike a measure of deviation from budget, does not encourage a questionable behavior, nor does it penalize for a rational behavior and for unexpected success.

Viewing "hitting the budget" as a goal in itself, and penalizing for any deviation, may for instance discourage from taking advantage of a newly emerging opportunity to increase volume and consequently revenue (for instance, as a result of failure of a competitor, faster than anticipated growth in spending, better than anticipated reception of new product, success in advertising, etc.), or to reduce costs. The worst thing that can happen to the measurement system is to encourage irrational behavior.

I believe we should not reward ourselves for beating the budget, but we should not penalize ourselves for it either.

"Hitting the budget" may not get us any closer to the stated mission. One could easily imagine a situation when an organization "hits the budget" while it deviates from the course of the mission.

CUSTOMER

Customer satisfaction

Customer satisfaction is clearly one of the critical measures of success. Our challenge, however, is to make it as objective as possible, as statistically valid as possible, and as independent of caprices of some individuals within the Member community as possible.

Recognizing that not all Members are equal and equally important to our future, we should continue using some form of weighting, but make sure at the same time that we do not cater exclusively to the very biggest players, not always loyal to us. To mitigate the risk of an overall score being heavily impacted by very few outliers, we have to make sure that the score of "heavyweights" are truly results of multiple inputs; otherwise we should adjust weights accordingly.

INTERNAL BUSINESS PROCESSES

Transaction unit cost
System up-time
Global acceptance at POS and ATMs

Transaction unit cost may serve as a proxy for the efficiency of the factory. While the denominator is rather obvious, the numerator is subject to debate. One simple way is to deduct all advertising expenses from the total expense base. Another one is to be much more rigid in determining what is and what is not the cost of keeping the factory running. Consistency in this area is much more important than purity. System up-time and global acceptance at POS and ATMs, are both measures of effectiveness rather than efficiency. (*efficient* meets internal requirements, such as unit cost, cycle time, size of staff, rework, etc., while *effective* satisfies all customer requirements, such as on-time-delivery, price, reliability, durability, fit, etc.)

LEARNING & GROWTH

Market share in commercial cards
Incremental debit decisions vs. MasterCard (or rate of debit volume growth)

This dimension is usually the most difficult to measure. As a proxy for the learning and growth, we may use market share in commercial card, the product which is still relatively new to our offering, and where we have to close the functionality gap in order to successfully compete with American Express. Another new product, debit, provides us with one of the few opportunities to measure ourselves vis-à-vis MasterCard in a rational way. The share of incremental brand decisions is one way to do that, the rate of debit growth is another.

This memo lists 9 potential measures constituting the strawman of our balanced scorecard. Some of them may be easier to derive than others. I believe that any subset of these nine measures (minimum four, but the more, the better) would amount to a step in right direction.

As our ability to capture data and control operational processes improve, and as we introduce new products, we may adjust/enrich our balanced scorecard.

Balanced Scorecard
(generic)