

MEMORANDUM

TO: Paul Allen
Linda Baker
Vic Dahir
Roz Fisher
Bob Heller

Brad Morgan
Wes Tallman
B. Ray Traweek
John Van Aken

FROM: Sue Simon *pas*

DATE: March 5, 1993

SUBJECT: U.S. MANAGEMENT RETREAT SUMMARY
February 22-24, 1993

Board Presentation

At our offsite meeting last week we agreed to the following approach for the June U.S. Board presentation:

Go to Board with:

- B. Ray's presentation sets the historical context.
- Present conceptually:
 1. Business as usual,
 2. Differentiation within current non-duality environment,
 3. Whole hog differentiation (non-duality legislated or with heavy incentives).
- For these three scenarios:
 - What does it look like to the Member?
 - What is the level of investment?
 - What are the benefits to the Member?
- Management Team perspective is that non-duality is best for the future. However, as an association, we need the buy-in of our Members/owners. Our perception is that we do not yet have that buy-in. So, we would propose that mid-term we take medium step rather than Business as Usual.
- Given the complexity of the issue, we want to come back to the Board on the issue of non-duality/duality with business case and implications.

P-0069

GOVERNMENT
DEPOSITION
EXHIBIT
363

Victor Dahir

OUTSIDE COUNSEL ONLY - HIGHLY CONFIDENTIAL SUBJECT TO PROTECTIVE ORDER

1124450

Working Groups

To accomplish this we agreed on an approach using three working groups. Those groups and their tasks are:

- **Business Case Group**
 - **Task:**
 - Conceptualize and quantify to the best extent possible the costs/benefits to Members of duality (base line) and non-duality for presentation at October 1993 Board meeting.
 - **Members:**
 - Hagadorn
 - Gustafson
 - Schall
 - Miller
 - Schmidt
 - Soderstrom
 - Ruder

- **Functional Groups**
 - **Task:**
 - Take B. Ray's matrix as a template.
 - Look at functional areas opportunities for differentiation:
 - In terms of "drivers" of three groups"
 - Members,
 - Merchant,
 - Consumers;
 - In terms of big wins... "sustainable superiority",
 - In terms of fiscal '94 (sizing) and years two and three
 - For presentation at June 1993 Board meeting.
 - **Members:**
 - "Auberge" Group

- **Ad Hoc Advisors Group**
 - **Task:**
 - Reality check,
 - Refinement,
 - Enrichment,
 - Pre-selling management position for June meeting.
 - **Members:**
 - "Laguna Niguel" group,
 - EVPs attend,
 - Wes chairs.

Schedule

The key dates in the lead up to the presentation for the June Board meeting are:

March 10	Heller meeting with U.S. SVPs
March 22	U.S. Management group meeting to review functional groups' differentiation priorities.
By April 30	Ad Hoc Advisors group meeting to review/refine differentiation priorities.
By May 15	U.S. Management group to review draft Board presentation.

Communication

As to communicating the results of this meeting we agreed on three key points:

- Bob would meet with the U.S. Senior VPs to discuss how their work in developing differentiation priorities fits with what we're doing with the board and to stress the importance of the activity.
- We will use the word "loyalty" rather than "non-duality" in talking about the context for a differentiation strategy.
- Each member of the management team will lead his/her group in the process of developing differentiation priorities.

Discussion of Differentiation Options

Our lengthy discussion of differentiation options led to the continuum we developed across the front wall of the meeting room. The transcription of those charts is attached.

Also attached are:

The "needs driven motivators" we referenced during the meeting, and

The matrix B. Ray used in his presentation.

We agreed that we would use both of these as tools in creating differentiation priorities for our respective areas of the company.

Continuum of Differentiation Options

LEGISLATED NON-DUALITY

Definition

- There is no new MasterCard solicitation by Members of Visa.
- Exception: Acquisition of MasterCard accounts through buying a bank.
- Members could reissue MasterCard to existing accounts.
- Portfolios with MasterCard could be acquired.
- Duality still prevails for POS acquirers.

Products

- There is elimination of some of our current product enhancements.
 - Members control enhancements
 - Enhancements which cost a lot of money and do little for consumers are eliminated.
 - e.g., Extended purchase protection, collision damage.
- Over time, all products are non-dual.
 - Anyone not in Visa camp cannot offer new products from Visa.
 - A move from Cirrus to Plus is required.
- Visa provides more innovative products for Members to sell.
 - Members have an exclusive on these products.
 - Innovative products are created which add value for the consumer and which are unique.
- Markets are developed for Visa/Members rather than for the category.
 - Market development (on acquirer side) is more parochial/exclusive.
 - The other guy is kept out.
- Visa does a complete examination of its rules in order to be more market driven than standards driven.
- There is an aggressive move away from standards; the approach is more performance and market driven.
 - Example: Doing automatic referral process just for Visa rather than also for MasterCard will have a real consumer benefit.

- Example: Chargeback rules. There was a merchant/customer benefit when Visa used to mean a guaranteed payment that wasn't seen again.
- Visa plastic (travelers cheques) is exclusive to Visa banks.
 - But, there is non-duality of acquirer situation.

Marketing

- Imagery is not blended.
 - e.g., Citibank MasterCard/Visa.
 - There is more reality that it is a different product.
- Reality-based claims are used.
 - There are real features to talk about to support the superiority story.
 - There are tangible versus intangible benefits.
- There is greater latitude for Member Relations and therefore merchant advantages to talk about.
- Member Relations acts more effectively because the focus is on Visa rather than countering MasterCard presentations.
 - [Note: Need to discuss budget implications of this, reallocation of resources.]
- There is a new way of thinking. Being on a team with Members means more focus on Visa and benefits.
- Overall, Visa as a company is refocused towards competitive advantages instead of having defensive, commodity based thinking.
- There is a potential requirement to deal with brands per segment.
 - e.g., Upscale brand.
 - Positioning of products is controlled better.

Systems

- Members have one back office.
 - Cost will be more to Members at first, but ultimately it will cost Members less as they will be supporting only one system.
 - Since there will be grandfathering, some Members will still have two back office operations.
- System innovations occur quicker.
 - There are more enhancements for loyal Visa Members.

Operations

- As with systems, the cost may initially be more but eventually will be lower.
- Risk control moves quicker resulting in Visa being a safer brand.
 - A move to cardholder identification and card authenticity could occur more rapidly.

ATMs

- Consolidation of brands is speeded up.
- Visa provides new products via ATMs.
- Visa Members cannot give MasterCard cash advances; this results in Visa getting the advantage of its brand leadership in terms of accessibility to consumer cash.
 - The negative side of this is that you don't want to block your customer's accessibility.

Legal

- A move to legislated non-duality would probably result in Visa being sued, but Visa would win the suit.
- The likelihood of government intervention due to utility status would be reduced.
 - Government would like the move to non-duality as it would be viewed as pro competition.
- Visa Membership could be restructured.
 - The company could be restructured so that "good guys" get more benefit (e.g., dividends).
 - A restructuring would affect decision making and the priorities of the company.
 - The company could be restructured as a banking depository institution.

Overall

- + Members expend less management time, confusion decreased, and staff training simplified/decreased.
- + Members rely on Visa to do more for them.
- All of the Members eggs are in one basket.

- There would be less flexibility.
 - If the one system went down, it could create difficulties.
- + Non-banks could be restricted more.

June Board Meeting

- We want to give them a range and say what we recommend.
- The approach needs to be framed in terms of the banks.
- The question here is whether you are moving faster against American Express, Discover, checks and cash.
- Does it need to be qualitative or quantitative?
 - We could take an educated guess and say that reallocation of resources could take us quite a ways.
 - We owe them year one initiatives that would go into the '94 budget.
- It would be fine with the Board to just present concepts, but that would not give us any commitment to the dollars to do it.

AGGRESSIVE DIFFERENTIATION

Definition

- **Loyalty pricing provides motivational, financial incentive to declare loyalty to one issuer. Carrot/stick concept. Loyalty pricing elements might be:**
 - **Volume,**
 - **Growth per year,**
 - **New solicitations only for Visa,**
 - **Interlink.**
- **The same institution cannot service on board advisory groups of both Visa and MasterCard.**
 - **This applies to entire slate of advisory groups. A bank is either on Visa advisory groups or is on MasterCard advisory groups.**
 - **Metaphor: You're either a Democrat or a Republican.**
- **Any new product is non-dual.**
 - **e.g., Business Card.**
 - **And, maybe you get to complete non-duality over time.**
- **Any new market development is initially non-dual.**
- **There is no dual advertising.**

Marketing

- **There is no blending of imagery.**
 - **There is no use of Visa/MasterCard logos on the same document of any form, e.g., customer bill.**
- **Co-branding (strictly, 100% with Visa) that is considered by the Board to be of value to the Membership gets (for instance) 20 basis points on interchange as their incentive.**
- **Marketing uses reality-based imagery.**
 - **Real features are built which Marketing talks about.**
- **There is an effort to seek value-added continuity programs that accrue across all Visa cards in a consumer's wallet, i.e., Favorite Brands Program presented to Board by Brad.**
- **Visa develops and issues valuable Merchant reports:**

- Merchants can compare their sales, etc. against their industry.
 - Issuers need to give more information about merchants.
 - To get the merchant reports, merchants have to meet certain requirements, e.g., display sign "We prefer Visa."
 - Merchants receive consumer usage reports.
 - Spending patterns are tracked (without name/address of consumer attached).
 - Privacy issue is avoided.
 - Note: It used to be against the law to use a customer's social security number for tracking information.
- Marketing is subject to defensive strategies.
 - Secondary or other brands are developed to market to segments.
 - Visa taps into Member creativity on value-added programs.
 - Response: We get these offers now, but they generally don't turn out to be for the benefit of the whole Membership.

Legal

- Equity among current Members is shifted based on loyalty.
 - (Note: Equity for Visa is now closed, so this would be a shifting of equity.)
 - Equity could be tied to measurements such as movement to Visa or number of Visa transactions.
 - A pool of value could be created and rebated according to loyalty.
 - The sliding scale could be redone.
 - The problem with the sliding scale is that it's so rich now that it can't be tilted in favor of loyalists.
 - Might be able to work with combining service and transaction fees.

Systems

- Note: In many cases, Systems deals with third party processors rather than Members.
- There is different Systems pricing tied to loyalty concept.
- Eventually, you get close to having one back office.
- Loyal Members could connect just to Visa; Visa does MasterCard clearing and authorization.

- However, MasterCard could retaliate and say that any MasterCard Members who did that would then lose their MasterCard rights on the transaction.
- There is card acceptance technology.
- There is early fraud detection because Visa has more information earlier.

Overall

- Aggressive differentiation has the same benefits as legislated non-duality, except it just takes longer.
 - Shift is done on the Member's time frame.
 - Response: We don't think that the Board really wants to do even aggressive differentiation.
- First Members get the benefit of conversion (being more efficient), but then money should go to fund programs.
- Aggressive differentiation gets Members behind a common cause.
 - Promote business for banks.
 - Members gain efficiencies.
 - Market share is grabbed from MasterCard.
 - Undermining efforts are stopped.
 - Currently, Visa spends money to differentiate its brand, and then Members spend money to blend.
- If Visa does not match a MasterCard move, the Board Members need to tell their people not to shift to MasterCard.
- There is a lot hidden in loyalty pricing.
 - A lot of gains are there.
 - New Members, however, would not share in an equity program, and would therefore be disadvantaged and consequently might not know why they should join Visa.
- Loyalty pricing:
 - Could be tied to transaction processing and thus based on who gets value.
 - If you want to Banks to shift from MasterCard to Visa, it has little to do with average outstandings.
 - The elements of loyalty pricing depend on what you want to do.
 - If you want to increase the number of cards issued it would be framed one way, whereas

- If you want average outstandings, it will be structured another way.
- Can we take interchange fees and use it to incent issuers?
- It might be a good idea to have a bonus to encourage an increase in volume, not just an increase in the number of cards.

VOLUNTARY LOYALTY

Definition

- From Members' perspective: "Make your brand more exciting and that will make us favor you."
- Institutions continue to be able to serve on advisory boards for both Visa and MasterCard.

Systems

- Some Systems innovations are permitted that don't need to be shared.

Relative Product Evaluation Consumer Perspective

	Amex	Visa	MasterCard	Discover
Product	-	++	++	+
Price	-	+	+	++
Position/ Perception	+	++	+	-
Performance	++	-	-	+

Page 2/3

Relative Product Evaluation Merchant Perspective

	Amex	Visa	MasterCard	Discover
Product	+	+	+	+
Price	-	+	+	++
Position/ Perception	+	+	+	+
Performance	++	-	-	+

Relative Product Evaluation Member Perspective

	Amex	Visa	MasterCard	Discover
Product	NA	=	=	NA
Price	NA	= +	= -	NA
Position/ Perception	NA	=	=	NA
Performance	NA	=	=	NA