

Chapter 2

Associating: Dee Hock and the Creation of the Organization

By 1968, the BankAmericard licensing program appeared on the surface as if it was a resounding success. In just two years, the number of licensee banks issuing card had grown from the initial 8 to 254, and each bank had further sub-licensed other agent banks in their territories to acquire BankAmericard transactions from local merchants. There were now 6 million cardholders, each of which could use their card at 155,000 merchants in 17 different states, as well as a few foreign countries. The system was processing \$458.9 million in sales volume, and growing each year.¹ And then in October of 1968, it very nearly disintegrated.

Unfortunately, these statistics were masking several serious problems in the BankAmericard system that were threatening to unravel it from the inside out. By October of 1968, these problems had become severe enough to cause a crisis amongst the licensees, and it was this crisis that instigated the creation of the organization that would soon be known as Visa. The purpose of this chapter is to analyze what was wrong with the BankAmericard licensing system, and explain how the new organization formed to take its place was fundamentally shaped by the particular philosophy of the organization's founder.

Problems in the Licensing Program

In many ways, it should not be surprising that the BankAmericard system faced a number of critical problems at this time. When any technological system rapidly grows in scope and volume, flaws in the initial design quickly manifest themselves, causing friction and instability. In many cases, these problems can be fixed easily enough without a major rupture in the organization: more techniques and artifacts can be employed to obtain more efficient operations; policies and procedures can be put in place to handle the growing complexity; new departments or committees can be added to track existing and identify new problems. If this is so, why did the

¹Burroughs Clearing House (1968).

BankAmericard licensees come to the conclusion that nothing short of a new organizational structure was necessary?

I will argue in this chapter that the licensees came to this conclusion primarily because the problems facing the system were both operational *and* organizational. Several key flaws in the organizational design led to a situation where the BofA could no longer control the licensee banks, and the licensees no longer trusted the BofA in return. Computer and telecommunication technology could certainly address the operational problems, but no technical device could overcome the breakdown in the organization.

A Typical Transaction in 1968

To understand the various operational and organizational problems, we must first understand what it was like to initiate, authorize, clear, and settle transactions in the BankAmericard system of 1968. This is best done by walking through the process of a typical domestic purchase. Note that in this example, we will discuss only the details that will help us understand the specific operational and organizational problems faced by the BankAmericard system; other interesting but less relevant details will be examined in later chapters. This example is also the ideal case; the unfortunate realities of the process will be noted in the following section.²

Imagine yourself in 1968, holding a shiny new BankAmericard. As discussed in the previous chapter, all cards had the same blue, white, and gold bands across the face of the card so that merchants could easily identify your card as acceptable, regardless of which bank actually issued it. Merchants also hung signs with the same marks in their windows, so that you could easily identify those that accepted the card, regardless of which bank represented the merchant in the system.³ You spy a merchant that you need to visit, select your items and present your BankAmericard for payment.

If your purchase amount is below the merchant's floor limit the merchant can complete the transaction immediately without authorization.⁴ The floor limit varied by merchant type and by card type: some cards had a star on the front, while others did not.⁵ The floor limit for a general merchant was typically \$50 for a non-starred and \$100 for a starred card, but airlines, hotels and other services were often granted higher floor limits.

²Unless otherwise noted, the information in this section comes primarily from interviews with Jutilla, Russell, Honey, and Derman, as well as Fisher et al. (1980) and Hock (2005).

³The merchant signs differed from the card in one strange way—the BankAmericard name was in the white band instead of the blue. This would be rectified later when the name of the system changed to Visa and the cards were redesigned.

⁴For a definition of the term *floor limit*, see p. 20 in the previous chapter.

⁵This star created a kind of early segmentation. Jutilla remarked that his friends quickly noticed the difference and would often ask him how they could get a star on their card.

If your purchase is above the merchant's floor limit, the merchant is required to call for authorization. The merchant dials the acquirer's authorization center and verbally conveys the transaction details to the authorization operator. The authorizer first determines if the card was issued by the same bank or another by looking at the first four digits of your account number. If it is the same bank, the transaction is known as *local* or *on-us*, otherwise it is known as an *interchange transaction*.

If this is an on-us transaction, the authorizer then consults a series of printed reports to determine if the transaction should be authorized. At this time, there were no interactive computer systems with CRT terminals installed at the BankAmericard authorization centers. When your bank became a BankAmericard licensee, it did receive some "computer software" from the Bank of America, but this was just a simple punch card-based accounting system. This system produced two reports to help the authorizers: a list of known *hot cards*, which were either stolen or on hold for some other reason; and a summary of each cardholder's account, listing their current balance, credit limit, purchase and payment history. The authorizer first searches through the hot card list to ensure your account number does not appear there. Then the authorizer manually wades through the massive binder of account sheets to find yours, reviews your details, and consults the hand-written list of authorizations already given since the report was last printed. If all is in order, the authorizer gives the merchant an authorization code, consisting of a few letters and digits, and the merchant writes that on to the sales draft.

If this is an interchange case, however, the merchant's authorizer does not have access to your records and is thus required to call or telex your bank's authorization center. The authorizer puts the merchant on hold, dials your bank's center and relays the transaction details. Your bank's authorizer then consults the same type of reports already discussed, and supplies an authorization code. The original authorizer then relays this code to the merchant.⁶

After authorization, the merchant then completes the sales draft. The draft is a multi-layer document: the top two layers are like tissue-paper, one for you and one for the merchant. The bottom layer is an IBM 80-column punch card, complete with the corner notch. The merchant puts your card and the sales draft into an imprinter, informally known as a "zip-zap machine," which squeezes the embossed characters on your card against the sales draft, thereby transferring your card number, expiration date and name onto each layer via carbon paper. The imprinter also holds another embossed plate containing the merchant's details. The merchant manually adds the transaction date and purchase amount to the draft, and you sign it to complete the purchase. The merchant is then required

⁶At this time, interchange was rare on the average, but there were localized exceptions to this. For example, the National Bank of Commerce in Seattle and Puget Sound National Bank in Tacoma experienced a high level of interchange due to the large amount of business that takes place between those two cities, which are roughly 30 miles apart. The authorization centers at these two banks simply called each other in the morning and kept a line open, allowing them to authorize interchange transactions quickly over a speakerphone (Jutilla interview).

to check the signature on the card against your signature on the draft to ensure that you are the proper cardholder, but few do. The merchant tears off the customer copy and hands it to you, putting the other two layers in the cash register.

On a regular basis, the merchant deposits the punch card layer just like a check. Unlike a check, however, the merchant receives an instant credit, less the discount, the amount of which is negotiated when the merchant signs the contract with the bank (merchant discounts at this time ranged anywhere from 0 to 8 percent, averaging 3.5 percent).⁷ From the merchant's perspective, the transaction is now complete, but the clearing and settlement process has in fact only just begun.

Although the drafts are computer punch cards, they are not yet machine-readable. Banks with very low volume may just manually sort and total the drafts, but others send them to the proofing and data-entry departments to be manually key punched and proofed.⁸ The drafts are then sorted by card number. On-us transactions are fed into the computer to update the cardholder accounts, and are then added by collation to the drafts already processed for each cardholder since the last billing cycle. At this time, most banks are still performing *country-club billing*, where the physical drafts are included with each statement.

All interchange drafts are then grouped and totaled by issuing bank. The merchant's bank completes a special *clearing draft* against the issuing bank for the total of all the sales drafts. The clearing draft looks very much like a cashier's check, complete with the magnetic ink routing characters, and can be submitted through the normal checkclearing system for payment. The physical sales drafts on the other hand are mailed directly to the issuing bank through the US postal system. The clearing draft is often processed before the individual sales drafts arrive at the issuer, so the issuer is forced to transfer funds, but must wait until the sales drafts arrive to reconcile and add the charges to the relevant cardholders' accounts. Once they arrive, the issuer reconciles the sales drafts against the settlement payments, and then performs the same actions the original bank did for the on-us case.⁹

Operational Problems

Within this simple transaction scenario, we can begin to see a number of operational problems that were greatly exacerbated by the system's increasing scope and sales volume.

⁷Jutilla (1973), pp. 49, 179.

⁸*Proofing* involves verifying that the drafts total to the same amount claimed by the depositor. This was often done by encoding the human-readable elements of a draft into machine-readable form, so that the drafts can be machine-totaled.

⁹In addition to merchant purchases, cardholders could also obtain cash advances directly from any BankAmericard bank. Although these transactions levied different fees and had no free period, they were processed in the same manner, with the bank providing the cash advance acting as the "merchant."

Authorization, Floor Limits, and Fraud

The first notable operational problem was the interaction of authorization, floor limits, and fraud. Payment card transactions differ from those in other payment systems in one important way: they are *guaranteed*. If the merchant follows the rules of the program, the merchant is guaranteed payment, even if the transaction was fraudulent. In the case of a personal check, the issuer simply returns the bad check and the merchant must absorb the loss; in a payment card transaction, the *issuer* must absorb the loss. This introduces a certain amount of risk to the issuing bank, and in an ideal world, the issuing bank would like to eliminate that risk by authorizing every transaction. This was not a realistic option in 1968, however, as the labor and telecommunication costs would easily outweigh the revenue gained from a low-value transaction. Additionally, authorizing every transaction would delay an already slow process, risking the use of cash or a check instead of the card.

The floor limit concept is essentially a cost/risk tradeoff made by the banks. Not all transactions are equally risky, and the easiest way to distinguish the higher-risk ones is by the combination of purchase amount and merchant type: a high-value purchase from a jewelry store is more risky than a low-value purchase from a shoe store. What most banks did not anticipate, however, was that criminals would quickly discover the various floor limits and make numerous under-limit charges, resulting in significant losses. A new card stolen from a mailbox could be used for a week or more before the issuing bank even saw the first sales draft, and over a month before the cardholder received the first statement for a card the customer did not even know was issued.¹⁰ Once detected, banks would notify other authorization centers and mail a postcard to merchants that might likely see the card.¹¹

But relying on the merchants to catch the cards was problematic. The main incentive for merchants to use the authorization system is the *guarantee of payment*, not the reward for catching a stolen card. The authorization process is more than just a technical function—it also formally transfers the responsibility for fraud from the merchant to the issuer. A merchant was (and still is) allowed to take a transaction above the floor limit without authorization, but the merchant then assumes the risk of fraud. If an issuer can prove that the merchant did not authorize the transaction, or that the bank warned the merchant about the card number prior to the transaction, the issuer can submit a *chargeback* into the system, which will eventually debit the merchant's account. Proving a chargeback required a manual audit, however, and most bankcard processing centers were already struggling to keep up with the sharply-increased sales volume.

¹⁰Often the cards were actually stolen by the postal sorters and carriers. The practice of mailing unsolicited cards to consumers was eventually banned by the US Congress in 1970, and most other countries have since passed similar laws.

¹¹Jutilla (1973), pp. 221–223. Eventually the Visa system produced a weekly booklet of hot card numbers, but this was ultimately replaced by online authorization via inexpensive point of sale dial terminals (see Chap. 7).

Merchants were also not inclined to call for authorizations due to the delay it would cause at the point of sale—sources from the time estimated that the average authorization took anywhere from five to twenty minutes, depending on how quickly the merchant could get through to the authorization center, and how quickly the merchant's bank could call or telex the issuing bank in an interchange case.¹² Stallwitz found that nearly all merchants in his study complained about the speed of authorization, and some admitted that they encouraged the use of cash or a check when the purchase was above their floor limit.¹³ Others would rely on their own assessment of the customer (often based on appearance) and take the card without authorization, or simply reuse an authorization code from a prior transaction as it was unlikely that the issuing bank would detect this under the manual system of the time.¹⁴ Stallwitz also found that suburban merchants in particular would avoid consulting the hot card lists and calling for authorization as it might offend their customers and risk the loss of the sale. Lastly, some merchants were themselves creating or participating in fraudulent transactions. Restaurant cashiers would make additional sales drafts with a customer's card, or less reputable merchants would submit under-limit drafts using a stolen card and split the proceeds with the thief.¹⁵

The actual amount of fraud occurring at this time is difficult to estimate as banks were not required to disclose such information, nor were they particularly eager to do so. Those that did were either inconsistent in the way they calculated and reported losses, or as Spencer Nilson claims "doctored the records so that it would come out to a ratio acceptable to their peers."¹⁶ Nevertheless, Nilson and others attempted to estimate how much the banks were losing on their card programs. Unfortunately, the estimates are difficult to compare as they are for different time periods, different sets of card programs (e.g., bankcards only, bank and T&E and retail, etc.), and different loss categories (total losses as opposed to losses specifically attributable to fraud). Nilson estimated that *fraud-specific* losses on bankcards increased from a mere \$140,000 in 1967 to \$2.2 million by 1969.¹⁷ Various Federal Reserve studies reported that *total* losses for bankcards rose from \$12 million in 1967 to \$115.5 million in 1970.¹⁸ Nocera claimed that throughout the late 1960s, the Chicago banks alone lost over \$25 million, and the New York banks over \$250 million.¹⁹

¹²"It took about 15 to 20 minutes to make a \$35 purchase, which didn't make you very popular at the point of sale" (Russell interview). See also Stallwitz (1968), pp. 44–45.

¹³Stallwitz (1968), p. 45.

¹⁴Reusing authorization codes became much easier to detect after NBI computerized both authorization and clearing and settlement, the story of which will be told in the next two chapters.

¹⁵Jutilla (1973), pp. 219–229, Nocera (1994), p. 30, Galanoy (1980), p. 149.

¹⁶Nilson (11 April 1977), Report No 161. The general accuracy of the Nilson Report was contested by many of my interview sources, so some of his claims and statistics should be approached with caution.

¹⁷Nilson (11 April 1977), Report No 161. Dollar amounts are in USD.

¹⁸1967 data from (Federal Reserve System July 1968); 1970 data reported in Brooke (18 May 1971).

¹⁹Nocera (1994), p. 61.

The growing amount of fraud was clearly a concern for those banks participating in the BankAmericard licensing program. Beyond the actual monetary losses, the shocking headlines were creating a *perception* that fraud was rampant and bankers were doing nothing to protect their cardholders.²⁰ This perception could not only erode the confidence of cardholders and merchants, but also attract the unwanted attention of lawmakers and regulators. Indeed the US Congress held hearings on the practice of mailing unsolicited cards in 1967 and was drafting legislation to not only prohibit it, but also protect consumers from the cost of fraudulent charges.²¹ As is typical, these hearings became a thinly-veiled public trial of the entire bank credit card industry, accusing the banks of fueling inflation and tempting innocent consumers to abandon the traditional values of thrift in favor of reckless debt spending.²²

Clearing and Settlement of Interchange Transactions

The second major operational problem area was the clearing and settlement of interchange transactions. Like a check, a payment card sales draft is a claim on funds that must be cleared and settled with the issuing bank. If a different bank would acquire that transaction, there would have to be a mechanism by which the draft can be routed to the issuer, and payment made to the acquirer.

As noted in the previous chapter, most banks at this time cleared and settled their checks through the national clearinghouse operated by the Federal Reserve. It would seem that using this same system to clear and settle credit card sales drafts, which were small in number compared to checks at this time, would be a sensible thing to do. The bankcard associations approached the Fed about processing credit card drafts, but the Fed refused to handle them.²³ Technically, it would have required

²⁰For example, see Galanoy (1980). Formerly the Director of Communications for NBI, Galanoy accused bankers of being blinded by their desire to build an all-encompassing electronic funds transfer system, ignoring the costs of fraud to consumers. For an example of this concern voiced in the popular press, see O'Neil (1970).

²¹These laws were passed in 1970 as an amendment to the Truth in Lending Act (Brandel and Terraciano 1980; Fisher et al. 1980, p. 257). The 1967 hearings are documented in 19th Congress, First Session (8 and 9 November 1967).

²²Dee Hock provided perhaps the best rebuttal to this in a 1979 interview: "Sure, consumer debt is high, but if you want the consumer to stay out of debt, business and government have to set the example. If we expect consumers to reduce debt and increase savings, then we must create an environment without inflation and with tax laws that favor saving and not debt. After all, interest paid on debt is tax deductible and interest earned on savings is taxed. How can that encourage thrift? We should not criticize the consumer who is learning to play the government invented game of buying now through debt and paying later with inflated dollars." Streeter (1979), p. 75.

²³Russell interview. Hock also commented on this in a 1974 speech: "Had the Federal Reserve agreed when asked (and they were) to clear bank card activity, would the service have evolved as it subsequently has? . . . It is clear there would be no BASE II and no INAS today had the Federal Reserve said yes, and clear that present bank card service would be radically different" (Hock 1974, p. 21).

some modifications to the automated systems: the sales drafts were 80 column IBM punch cards, larger in size than most checks of the day; and they encoded information as punched holes instead of magnetic characters printed along the bottom edge. But the technical reasons were secondary to the more ideological belief that debt instruments, especially those involving a discount, simply did not belong in the Federal Reserve's clearing system.²⁴ Recall that one of the Fed's goals was to eliminate discounts on cleared checks, so it is not surprising that they would refuse to process BankAmericard transactions.

With the Fed's refusal to handle credit card drafts, the BankAmericard Service Corporation (BASC) was faced with a problem: how should the licensee banks clear and settle their interchange transactions? One logical option would have been for the BASC to create their own centralized clearinghouse for BankAmericard transactions, but the BASC chose not to do this, partly because the amount of interchange was still very low in the late 1960s.²⁵ Instead, the BASC stipulated that acquiring banks must mail interchange drafts directly to the issuing bank, similar to the way they handled out-of-town checks in the nineteenth century. The issuing bank would then reimburse the acquiring bank, less a discount fee, called the *interchange reimbursement fee*.²⁶

This solved only the clearing half of the problem—the licensee banks still needed a way to settle those transactions (i.e., transfer “good and final funds” from the issuer to the acquirer). Recall that the Federal Reserve System eliminated the need to transfer physical currency between banks when settling payment transactions, and the BASC decided to leverage this system by creating a special *clearing draft*, which looked like a bit like a cashier's check. To receive payment for a set of interchange drafts, acquirers completed one of these clearing drafts against the issuer for the total amount of the sales drafts, less interchange fees, and submitted it along with their other inter-bank funds transfer requests.

This separation of the clearing draft from the sales drafts allowed banks to use their existing funds transfer mechanisms, but it also created a timing problem that jeopardized the functioning of the entire system. When the issuing bank received payment notice of the clearing draft, it would enter that amount into a suspense ledger and wait for the individual sales drafts to arrive in order to reconcile and bill the cardholder. Unfortunately, this often took quite a long time. This is how Visa's founder described it:

Meanwhile, the merchant bank, having already been paid and under immense pressure to handle its own cardholder transactions, had no incentive to process [interchange] transactions and get them to the issuing bank for billing to the cardholder. Since each bank was

²⁴Russell interview.

²⁵Sources estimated that it was between one and five percent of transactions at the most. There were of course localized exceptions to this. In regions where banks were not allowed to operate branches across an entire metropolitan area, the interchange level would naturally be higher.

²⁶Note that the laws governing checkclearing discussed in the previous chapter did not apply to credit card sales drafts. Any similarity in their clearing method was coincidental and not required by law. The legal basis for credit card sales drafts came from the contracts signed by licensee banks, cardholders, and merchants (Katz interview).

both a merchant-signing bank and a card-issuing bank, they began to play tit-for-tat, while back rooms filled with unprocessed transactions, customers went unbilled, and suspense ledgers swelled like a hammered thumb. It became an accounting nightmare.²⁷

This immense backlog in the system also compounded the fraud problems discussed earlier. Issuing banks would have no way of knowing if sub-floor-limit fraud was occurring on a card until the actual sales drafts arrived and were processed. By the time they arrived, thousands of dollars worth of fraud could have taken place.

Even when the sales drafts did arrive, it was often the case that their total did not match the clearing draft amount. Many smaller merchant banks would simply run an adding machine tape over the drafts instead of key punching them, and would inevitably make mistakes. Chuck Russell, who succeeded Hock as CEO, recalled that “Banks couldn’t balance from day to day because they couldn’t get their drafts drawn on other banks settled. It was a disaster.”²⁸ To provide a sense of the scale of the problem, he relayed this story:

I was shown a room that was warehoused-sized, full of IBM 80-column tab cards (which were the drafts) that they couldn’t settle. We’re talking millions and millions of dollars ... they had never got the debit or the credit side of the transaction through clearing because they couldn’t find them!²⁹

Finally, it should be noted that not all banks experienced problems to the degree described here. But the lack of a centralized clearinghouse, compounded with the timing problems introduced by the clearing drafts, created operational problems that were most definitely threatening the overall system’s stability and impeding its future growth.³⁰

Organizational Problems

Although the operational problems just described may have had potential solutions within a health franchising organization, the organization had problems of its own that further compounded the operational difficulties. It was these organizational problems, even more than the operational ones, that convinced the licensees that a new organizational structure was necessary.

The BankAmericard licensing system, like any cooperative payment system, faced a central organizational tension—balancing competition and cooperation.³¹

²⁷Hock (2005), p. 77.

²⁸Russell interview.

²⁹Russell interview. The “stacks of unprocessed drafts” story was also relayed by others in various forms.

³⁰Jutilla indicated that his bank was typically able to reconcile, but the delays in receiving the interchange drafts were especially dangerous due to fraud. He concluded that the system could not have survived the way it was as the transaction volume increased.

³¹Evans and Schmalensee (2005).

The licensing system created a new meta-organization comprised of *competing* financial institutions that needed to *cooperate*, at least to some degree, in order to provide a universal payment system that none could have realistically provided alone. Competing organizations in a marketplace normally seek their own self-interests in an assumed zero-sum game for market share. A cooperative organization, on the other hand, offers a different possibility—if all members cooperate, they can provide a larger, universal system that allows them all to benefit even more than if they chose not to cooperate. In other words, each participant's slice of the cooperatively baked pie would likely be larger than any pie the participant could have baked alone. To accomplish this, however, they need mechanisms that would create trust within the organization, mechanisms that balance out their power and interests and dictate how inter-organizational work will be accomplished. In other words, they need something akin to a constitution, as well as *operating regulations*, to which all member organizations agree. As we shall see, the licensing program's key organizational problems lay precisely in these balancing mechanisms and operating regulations.

Under the BankAmericard licensing system, BofA retained not only the ownership of the BankAmericard name and marks, but also all the power, and this led to a fundamental distrust between BofA and the licensees. The licensees knew that BofA would have opened branches in their territories if the banking regulations had allowed it, and if those regulations ever changed, BofA could easily revoke their license and become the sole BankAmericard issuer.³² The licensees also doubted if BofA had the desire and even the ability to solve the operational problems discussed earlier.³³ The licensees believed that any solutions developed by BofA would naturally be in BofA's best interest and not those of the licensee banks.

Although BofA retained nearly all the power in the system, their power to enforce and modify the operating regulations was neutered by two critical flaws in the license contracts. First, the contracts lacked mechanisms for financially punishing banks that skirted or bent the operating regulations, nor did they contain a method for resolving grievances between the licensee banks. The only recourse BofA had was to revoke a bank's license, but since most of these banks held large correspondent deposits with the BofA, and were dominant in their geographic area, this was not likely to happen. Second, the contracts also lacked a clause allowing BofA to change the operating regulations in response to new developments. If BofA needed to modify or add a rule, they had to re-negotiate a new contract. Again, BofA had no recourse if banks simply refused to sign the new license, which they often did if the rules were not in their best interests.³⁴

The fundamental distrust and the flaws in the contracts created a number of organizational instabilities. The most significant and pernicious was the tension over the

³²Hock (2005), p. 85. Of course, these regulations were abolished in the 1980s, but by then it was too late, as the Visa system had already been established.

³³Russell interview. The BofA paid very low salaries at the time, and the most talented operational people tended to go to their main local competitor, Wells Fargo, which was a member of the Interbank system.

³⁴Katz interview. See also Hock (2005), pp. 83–87.

interchange reimbursement fee. As noted earlier, this fee was paid by the acquirer to the issuer during the settlement of an interchange transaction.³⁵ At this time, the intent of the fee was to compensate the issuer for the cost and risk of extending the cardholder credit for the transaction. The rule established under the licensing system for interchange fees was essentially unenforceable. This is how Bennett Katz, Visa's long-time general counsel, described it:

When I came on board, the rule was... if a customer of your bank goes into a merchant belonging to another bank, outside of that territory, then the bank that signed the merchant has a choice as to what it sends to the issuer. It could send the amount of the discount that it received from the merchant less a processing fee (for processing the transaction), or if it didn't want to calculate each and every one... it could send the average discount it was getting from all of its merchants less a processing fee. Well they would say 'my average is two percent.' How are you going to audit that? And if the merchant put up a big deposit, their merchant discount might be close to zero, and the issuer would get almost nothing! So the issuer has all the costs because he's extending the credit and eating defaults, but he was getting almost nothing when the customer traveled. The losses were horrendous. It was literally chaos in the BankAmericard system.³⁶

Tensions Come to a Head

In October of 1968, the BASC called a special meeting of the licensees to discuss the operational and organizational problems facing the BankAmericard system. Card program managers from each of the licensee banks descended on Columbus, Ohio, but the BASC neglected to send their most senior officers. The licensees were incensed that the BASC apparently did not recognize the seriousness of the situation, and began to make accusations that the BASC was either unwilling or incapable of solving the system's problems. By the middle of the second day, the meeting had devolved into "acrimonious argument."³⁷ Unsure of how to rescue the situation, the BASC representatives attempted to create a committee of licensees that would look into the most critical problems. One of those selected to be on the committee, however, had a different idea of what it would take to solve the system's problems, and after lunch the rest of the licensees were greeted by the card-center manager from the Seattle National Bank of Commerce: Dee Ward Hock.

Dee Hock

To tell a complete history of Visa's origins, one must give significant time and credit to Dee Hock. Historians of technology are usually quite reticent to spend too much

³⁵The acquirer paid this out of the discount fee collected from the merchant in return for immediate and guaranteed payment. In the case of a cash advance, however, the flow is reversed: the issuer pays the acquirer, because the acquirer assumes all the costs.

³⁶Katz interview.

³⁷Hock (2005), p. 84.

time focusing on any single individual, fearing that they will fall foul of the dreaded “inventor-hero” myth. This sort of history, all too common in the popular press, simplifies technological history by focusing on one particular person (typically a man), often portraying that person as a forward-thinking genius heroically fighting against the stodgy and uninventive status quo. Through a flash of inspiration and sheer tenacity (as the story typically goes), the inventor-hero brings about a completely novel technique or device that forever changes a reluctant industry.

The trouble with this kind of heroic saga is that it typically falls apart when one starts to dig deeper into the case. As argued in the previous chapter, most technological systems are based upon, or at least shaped by, other innovations that came before. Most are the product of many different minds and hands, working and negotiating with each other over many years. Most require a legion of individual workers not only to build the initial system, but also to keep it in good repair and working over time. That is to say, despite our tendency to associate innovations with a single heroic figure, a more nuanced understanding of the case often reveals key contributions from many different people over longer periods of time.

In our effort to avoid the inventor-hero style of history, however, we have sometimes neglected to give proper credit where that credit is due. In the case of Visa, a deep study of the case does expose several other individuals who played key roles in bringing the system to life and keeping it running on a daily basis, but one still cannot escape the critical, and perhaps most important role played by Hock. He, more than anyone else, established the principles by which the organization was designed and intended to function, and set the agenda for that organization’s actions during its formative and most prolific years. Thus, it is appropriate to spend some time understanding not only who Dee Hock is, but also how his ideas on money and organizations shaped his vision for what Visa could become.

Hock’s Personality

All that said, it is still a difficult task to describe Dee Hock, as his character is frustratingly complex. Those that worked at Visa during Hock’s reign would invariably start telling “Dee stories” during our interviews, and since no single story could entirely capture his character, they just kept telling more of them. Tom Cleveland, who eventually became Visa’s Chief Financial Officer, wrote a series of sixteen stories totaling fifty pages in an attempt to capture what he called “the Dee Hock experience.”³⁸ Sources used a wide variety of adjectives, but none of them seemed to be sufficient: inspirational; intimidating; clairvoyant; clever; shrewd; aggravating; fair; brutal; demanding; and brilliantly eccentric. Many said he was the most decent human being they had ever met, and most said he was nearly impossible to describe fully.

³⁸Cleveland (1999), p. 1.

Interestingly, all of the stories combined to describe Hock as simultaneously having one character trait and its opposite. He was the most inspirational of leaders, but could also be the most denigrating. One employee said that he was like an “emotional roller-coaster”—he could completely demoralize you in one breath and then boost your ego to new heights in the next. Another employee remarked that he sometimes could be demanding to the point of being insensitive, but immediately came to her tangible assistance when personal tragedy struck. Hock advocated decentralized autonomy for his employees and gave them enormous leeway at times, but would ultimately micromanage every detail he could. Every piece of correspondence that left the Visa offices during the first few years was personally reviewed by Hock, and he reportedly obsessed about the design of each new office or data center space, even down to the location of the electrical sockets. In short, his personality is complicated and often paradoxical.

One way in which we might untangle his personality a bit is to examine the way Hock tells his own life story.³⁹ Hock’s autobiography is revealing, not only as a chronicle of his times at Visa, but also as a window into the way he views himself and thus a clue to his deeper, more unconscious motivations.⁴⁰ He opens his autobiography with his birth in 1929, at the start of the Great Depression. He describes his upbringing as part of a poor family in rural Utah, living in a cramped one-room cottage with no plumbing and a wood stove that doubled as a cooker and heater. He characterizes himself as a curious child, a voracious reader, and a keen study of nature. He notes that his penchant for books and long walks in the country began to estrange him from his family and friends and make him feel misunderstood, leading him into an interior world in which he dreamt of greater things. He recounts how in his youth he worked a number of harsh, manual-labor jobs, which as he reminds the reader, “proud men did, without whining. ‘Root, hog, or die’ was the homily of the day.” He describes how he learned to argue persuasively on his high school’s debate team, and how he was the first person in his family to attend college, at which he obtained an associates degree and an interest in the classics of Western thought. He ends the segment on his early life by marrying his childhood sweetheart, and taking an entry-level job in a small local consumer finance office to provide for his new family.⁴¹

Hock’s own portrayal of his early life, almost the stereotype of the pioneering self-made American man, makes several claims that I think are key to understanding not only his general character, but also the motivations behind a number of his actions that I will discuss in later chapters. First, he strongly emphasizes his *humble origins* in order to establish that he did not come from privilege. Second, he portrays himself largely as *self-taught*; his schooling was limited and when teachers enter the story, they merely expose or introduce him to sources that he alone then reads, interprets, and understands. Third, he highlights the hard-working nature of his community as well as his own experience with manual labor in order to

³⁹Hock (2005).

⁴⁰For issues surrounding the reading of autobiographies, see Smith and Watson (1996, 2001).

⁴¹Hock (2005), pp. 15–29.

self-identify as belonging to the working-class. Fourth, he hints at *feeling like an outsider*, misunderstood by those with more limited imaginations.

All of these claims combine to create one important yet unspoken overtone that runs throughout his entire autobiography: he wants to make it absolutely clear to the reader that he was *not a typical banker*. Hock was not born into an important or wealthy family, nor was he the son of a banker. He did not grow up in a suburb of New York, San Francisco, or any other banking capital. He did not attend the right schools, nor did he earn an MBA from a prestigious graduate school. Most telling of all, his first job was at a consumer finance company, not at a large commercial bank.

Although Hock would eventually become the CEO of a significant international banking organization, earn a commensurate salary, and commune with some of the most powerful bankers in the world, he continued to think of himself as that self-made, pioneering man from humble origins who would always remain somewhat of an “outsider” to the typical world of banking. In some ways, Hock enjoyed his outsider status: it allowed him to ignore conventions, take risks, and break down conceptual barriers that typical bankers considered immovable. In other ways, however, that outsider status sometimes drove Hock to seek acceptance amongst his banker-peers: as we shall see, his attempts to seem equal or even more important than his powerful member bankers created frictions that contributed to his eventual dismissal from Visa.

Views on Organizations

Hock’s first professional job was with a consumer finance company in Los Angeles starting in 1951, and it was here that he not only learned the business of lending, but also began to develop his concepts about organizations. During this time, Hock became increasingly suspicious and critical of what he called “mechanistic, command-and-control organizations.”⁴² These types of organizations are typified by the centralization of power, the creation of bureaucratic hierarchies, and the use of technology and highly-rationalized rules to control an increasingly specialized and deskilled set of workers.⁴³ For Hock, this concept of organizational design was bred from “industrial age thinking” and the “machine metaphor,” where an organization is viewed as a sort of machine with humans as the cogs and wheels.⁴⁴ Hock sees these organizations as fundamentally flawed—in these kinds of organizations, “purpose slowly erodes into process,” “procedure takes precedence over product,”

⁴²Hock (2005), p. 36.

⁴³Hock purposely does not cite his sources, but this is of course reminiscent of Burns and Stalker’s ‘mechanistic’ and ‘organic’ organizational spectrum. See Burns and Stalker (1961). One can also detect resonances with General System theory, Chaos theory, and what is now beginning to be called “ecological thinking.”

⁴⁴Hock (2005), pp. 37–38.

and “the doing of the doing” causes nothing of substance to get done.⁴⁵ Furthermore, Hock argues that command-and-control organizations are actually incapable of dealing with their increasingly complex and dynamic challenges, and because this is still the dominant organizational form, we are in “the midst of a global epidemic of institutional failure.”⁴⁶

Hock would eventually develop a different concept for organizations based on his observations of natural systems.⁴⁷ He created the neologism “chaordic” to describe his new concept and defined it as “The behavior of any self-organizing and self-governing organism, organization, or system that harmoniously blends characteristics of chaos and order.”⁴⁸ In contrast to the command and control organizations, chaordic organizations are decentralized, self-organizing, self-governing, exhibiting emergent properties. The obvious implication is that they are also more flexible and adaptive.⁴⁹ But this concept was still rather nascent in Hock’s mind at this time, and we shall see how he continued to develop it through the creation of the Visa organization, which he considered to be the first, albeit flawed, implementation of this new concept.⁵⁰

Hock began to implement some of these new organizational ideas while working for the consumer finance company in Los Angeles. Unfortunately for Hock, that organization did not share his vision, and they eventually parted ways. It was at this point that Hock learned his most important lessons about consumer lending. While he was still employed, he had gotten into “considerable debt” through the use of credit cards, and had no savings to live upon. Hock took multiple jobs to pay it off, and he and his wife vowed never to carry so much debt again. He wrote, “It is amusing now to remember how we shredded every credit card in our possession, swearing never to have another.”⁵¹ Although this makes an amusing anecdote, it also reveals Hock’s motivations for creating Visa’s first debit card soon after the organization was formed.⁵²

Hock moved to Seattle and interviewed for a job at the National Bank of Commerce in 1965.⁵³ He played several menial roles within the bank before being picked in 1966 to help start their newly-licensed BankAmericard program. He and his boss were given a ridiculously short time in which to start the program—90 days—and

⁴⁵Hock (2005), p. 36.

⁴⁶Hock (2005), p. 11.

⁴⁷Hock (2005), pp. 248–249.

⁴⁸Hock (2005), p. 13.

⁴⁹Burns and Stalker argue that this organic style of organization is more effective for firms in highly-dynamic markets, while the mechanistic style is best for stable markets. Hock, however, would question if any organization exists in a stable context, and point out that mechanistic organizations will ultimately fail due to their inherent flaws.

⁵⁰Hock (2005), pp. 248–249.

⁵¹Hock (2005), p. 40.

⁵²See Chap. 8.

⁵³Dougherty (1981), p. 13.

by the end of their training session in San Francisco, they realized that they were in “deep trouble.”⁵⁴ Hock discovered that there was “bad blood” between the BASC and BofA’s own card operations center, and that the card center “had no capacity to comply with rules prescribed in the licensing agreements.”⁵⁵ The training, provided by the marketing department, amounted to encouragements to mass-issue the cards, with no practical advice on how to handle the aftermath. Hock and his boss spent the next week visiting every card center they could in order to learn the realities of credit card operations. Hock summarized: “Within a single week, our original belief that the BankAmericard franchise would provide a well-marked, expeditious road to the future had been shattered by what we had learned.”⁵⁶

The highly dynamic, unpredictable nature of the endeavor provided Hock with another chance to try out some of his new organizational concepts. He suggested that they “abandon tradition, throw detailed planning to the winds, rely on a clear sense of direction, a few simple principles, common sense, trust in the ingenuity of the people, and let the answers emerge.”⁵⁷ Despite numerous setbacks, his new organizational style proved effective, and with great effort they issued 100,000 cards and signed up enough merchants, all within 90 days. Throughout the process, Hock had become a believer in the future of payment cards, but not because of their financing capabilities. Hock wrote that while he was organizing the new program, he was also reading about the possibilities of a more complete integration of computers and banking. “Giving people another way to borrow money interests me not at all,” Hock recalled, “What credit cards might become is something else again.”⁵⁸

Views on the Nature of Money

Hock had been slowly coming to the realization that “money” had become nothing more than “guaranteed alphanumeric data” and that a bank is nothing more than an “institution for the custody, loan, and exchange” of this data. Furthermore, that data was increasingly being stored and manipulated by computers, and would eventually “move around the world at the speed of light at minuscule cost by infinitely diverse paths.”⁵⁹ He then came to one of his most important conclusions:

Any institution that could move, manipulate, and guarantee alphanumeric data in the form of arranged energy in a manner that individuals customarily used and relied upon as a measure of equivalent value and medium of exchange was a bank. It went even beyond that. Inherent in all this might be the genesis of a new form of global currency.⁶⁰

⁵⁴Hock (2005), p. 61.

⁵⁵Hock (2005), p. 61.

⁵⁶Hock (2005), p. 61.

⁵⁷Hock (2005), p. 62.

⁵⁸Hock (2005), p. 69. Although these quotes come from a retrospective biography, his speeches from the 1970s contain similar sentiments.

⁵⁹Hock (2005), pp. 95–96.

⁶⁰Hock (2005), p. 96.

Hock realized that if this was actually the case, the implications were enormous:

If electronic technology continued to advance, and that seemed certain, two-hundred year old banking oligopolies controlling the custody, loan, and exchange of money would be irrecoverably shattered. Nation-state monopolies on the issue and control of currency would erode. . . . The vast preponderance of the system would fall to those who were most adept at handling and guaranteeing alphanumeric value data in the form of arranged particles of energy.⁶¹

Lastly, Hock realized that he, and most of his fellow bankcard managers, had misunderstood what business they were in:

It seems ordinary and obvious now. It was a revelation then. We were not in the credit card business. “Credit card” was a misnomer based on banking jargon. The card was no more than a device bearing symbols for the exchange of monetary value. That it took the form of a piece of plastic was nothing but an accident of time and circumstance. *We were really in the business of the exchange of monetary value.*⁶²

Creation of National BankAmericard Inc.

At the licensees meeting in 1968, Hock convinced the BASC representatives that merely investigating a few of the most serious operational problems would do nothing to save the system. Instead he proposed a “cohesive, coherent, self-organizing effort involving all licensees to examine all problems plaguing the system.”⁶³ The BASC representatives were naturally reluctant to agree, but they had little reason to object—Hock’s proposal did not require them to commit to any policy recommendations made by the licensees, nor could the BASC prohibit the licensees from meeting on their own and making plans that might exclude the BofA.

Hock created a matrix of committees to investigate the problems of the system. He divided the United States into eight regions and each region formed separate committees to focus on four functional areas: operations, marketing, credit, and computer systems. After performing some initial research, the committees began to report:

The complex of committees had but one redeeming quality: It allowed organized information about problems to emerge. It took only two cycles of meetings to realize that the problems were enormously greater than anyone imagined—far beyond any possibility of correction by the existing committees or the licensing structure—and growing at an astonishing rate. Losses were not in the tens of millions, as everyone had thought, but in the hundreds of millions and accelerating.⁶⁴

It quickly became obvious to Hock that the licensing system could not survive as it was structured. The problem was not a lack of technology—it was a *fundamental*

⁶¹Hock (2005), p. 97.

⁶²Hock (2005), p. 98. Emphasis in original.

⁶³Hock (2005), p. 87.

⁶⁴Hock (2005), p. 91.

flaw in the organizational design. If the licensing organization could barely function in the United States and a few other countries, it had no chance of expanding into the ubiquitous worldwide system that Hock envisioned. His new organizational ideas had been successful in the highly dynamic and chaotic context of starting a new card program at a particular bank, but could they also work to organize a system that involved hundreds, and eventually tens of thousands, of independent organizations spread across different countries, subject to different regulations? If so, there was an enormous opportunity:

Any organization that could guarantee, transport, and settle transactions in the form of arranged electronic particles twenty-four hours a day, seven days a week, around the globe, would have a market—every exchange of value in the world—that beggared the imagination. The necessary technology had been discovered and would be available in geometrically increasing abundance at geometrically diminishing cost. But there was a problem. No bank could do it. No hierarchical, stock corporation could do it. No nation-state could do it. In fact, no existing form of organization we could think of could do it. On a hunch I made an estimate of the financial resources of all the banks in the world. It dwarfed the resources of most nations. Jointly they could do it, but how? It would require a transcendental organization linking together in wholly new ways an unimaginable complex of diverse institutions and individuals.⁶⁵

Organizational Dreams

Hock selected three members of the national executive licensee committee, which had overseen the work performed by the regional committees, to help him think through a design for a new organization. They checked into the Alta Mira hotel in Sausalito, California for a week of discussion. The location was perhaps fitting—it is perched upon a hill across the bay from San Francisco's financial district, home of the BofA. It was here that Hock and his colleges, "the founding fathers," planned what amounted to a revolution against the BofA's licensing system.

Hock recounts that on the fourth night he began to realize that if the methods of biological evolution could produce such complex organizations as brains and immune systems, not to mention larger and more diverse systems such as rain forests, marine and weather systems, the same sort of principles employed by humans might be able to create the kind of complex, self-organizing system he wanted to achieve. He concluded, "What if we quit arguing about the structure of a new institution and tried to think of it as having some sort of genetic code?"⁶⁶ He continued, "If institutions have no reality save in the mind, might their genetic code have something to do with beliefs—with purpose and principles?"⁶⁷ What if they came to agreement on the purpose and principles of the new organization, and then let it self-organize according to those?

⁶⁵Hock (2005), pp. 98–99.

⁶⁶Hock (2005), p. 108.

⁶⁷Hock (2005), p. 109.

Hock presented his ideas the next morning and the group formed the following principles, which would in turn become the basis for the new organization's constitution:

What if ownership was in the form of irrevocable rights of participation, rather than stock: rights could not be raided, traded or sold, but only acquired by application and acceptance of membership?

What if it were self-organizing, with participants having the right to self-organize at any time, for any reason, at any scale with irrevocable rights of participation in governance at any greater scale?

What if power and function were distributive, with no power vested in or function performed by any part that could reasonably be exercised by any more peripheral part?

What if governance was distributive, with no individual institution or combination of either or both, particularly management, able to dominate deliberations or control decisions at any scale?

What if it could seamlessly blend cooperation and competition, with all parts free to compete in unique, independent ways, yet able to yield self-interest and cooperate when necessary to the good of the whole?

What if it were infinitely malleable, yet extremely durable, with all parts capable of constant, self-generated, modification of form or function without sacrificing its essential purpose, nature, or embodied principle, thus releasing human ingenuity and spirit?⁶⁸

Hock persuaded the other licensees to agree to these principles, but as he admits, this may have had more to do with their beliefs that the entire project was likely doomed to failure anyway. Hock recalled:

In the beginning, none of the licensees thought that the Bank of America would surrender ownership of a trademark and licensing system that assured them a quarter percent or more of the revenues of every participant in perpetuity. No one thought that banks would voluntarily surrender a portion of their autonomy to an external entity in order to act together for a common purpose. No one believed that such a horizontal grouping of competitors could exist within the spirit and constraints of antitrust laws. And no one dreamed the emerging ideas would bring together in common ownership and enterprise people and institutions of every race, language, custom, and culture—every economic, legal, philosophical, and religious persuasion in the world.⁶⁹

Hock then presented the principles and a rough idea of the new organization to Ken Larkin, BofA's Senior Vice President in charge of the BankAmericard program. Larkin's response was less than encouraging and the BofA initially resisted any attempts to curtail their power or control over the system. The BofA, however, actually had little choice but to capitulate and allow Hock to pursue the new structure. The system was clearly falling apart, and there was a very real danger that the licensees could organize a new competing system on their own and exclude the BofA, or simply join the rival Interbank network. Hock used his talents of persuasion to argue that it was actually in BofA's best interest to support the new organization, as it had the potential of generating far more revenue for them in the long run, and eventually they agreed to do so.

⁶⁸Hock (2005), pp. 109–110. Emphasis in original. Although Hock wanted to balance malleability and durability, the former seems to have won out over the latter. Visa restructured into a public stock-issuing corporation in 2008, essentially abandoning these principles.

⁶⁹Hock (2005), p. 112.

Hock began crafting the organization's structure, bylaws, and operating regulations. It would be a membership cooperative where the members would also be the joint-owners. In essence, the customers and owners would be the same, so there would be no divided loyalty. It would be non-stock, and membership would be non-transferrable, so that ownership and participation would forever be linked. Membership qualifications would be set by the Board, but then any organization meeting those criteria must be allowed membership. Both membership fees and voting rights were determined by the amount of volume a member generated, linking taxation and representation. Operating regulations dictated not only how inter-member work was to be accomplished, but also how members would be penalized when they violated them. But most importantly, members would agree to abide by a common set of bylaws and operating regulations "as they now exist or are hereafter modified."⁷⁰ Thus Hock ensured not only that the new organization could enforce the rules, but also that they could modify and extend them as needed without renegotiating contracts.

Interestingly, Hock claims that he always wanted to include participating merchants as full owners and members in the new organization, but the idea was always strongly resisted by the licensee banks.⁷¹ At the time, the licensee banks were concerned that giving merchants voting rights would endanger the merchant discount, which was a key source of revenue for acquirers. Hock also claims he wanted to include all the cardholders as owner/members, but that would have added a layer of complexity and chaos comparable to a democratic nation-state, and perhaps would have been unrealistic.

The bylaws acted like a kind of constitution for the new organization. They enshrined Hock's principles, and although they could be amended by the Board of Directors, doing so required an 80 percent majority vote. This ensured that the organization could adapt if the principles no longer made sense, but they also could not abandon them without an overwhelming consensus.

The Board of Directors for the new organization was also designed to balance the interests and power of all the members, regardless of size and location, and to provide the larger banks with "blocking power" on key issues such as budgets and fees.⁷² Each Board member would come from a different bank, so that no one bank could dominate policy regardless of volume. Each of the eight regions would be allocated one Director in order to ensure that all regions were equally represented. Five "at large" Directors would be elected by the general membership. One Director would be elected by the smallest banks in the system. Any bank that generated more than 15 percent of the sales volume would be able to appoint their own Director.⁷³ The president of the new organization (which would be Hock) would also have a seat on the Board, but could not serve as chairperson.

⁷⁰Hock (2005), p. 124.

⁷¹Hock (2005), p. 161.

⁷²Honey interview.

⁷³This was eventually reduced to five percent (Honey interview).

The functional committees would also remain in the new organization, though they would be split into two levels. Hock felt that it was important to keep the Board members occupied with the large and important policy decisions, while subcommittees handled the matters of minutia.⁷⁴ Thus he created a lower layer of “advisor groups,” which were comprised of card-center managers. These groups reviewed policy proposals made by the central organization’s staff, and occasionally drafted some of their own. The advisor groups then made recommendations to the Board-level committees, which were comprised of Directors, plus a member of the central organization’s staff. The Board-level committees then voted whether to bring the policy before the entire Board. Certain committees, however, such as the one for operations, were eventually given the power to approve changes to the operating regulations on their own without a full Board vote, as these changes were numerous.

In practice, the committees and advisor groups also provided the staff of the new organization with a testing ground for innovative ideas, enabling them “take the temperature” of the membership on important issues.⁷⁵ The staff could thus determine which issues would become politically contentious, which required some alteration, and which could be proposed with confidence at the full Board meetings. The relationship was symbiotic, as the committee and group members often became the champions of certain issues, enabling NBI’s staff to appear as neutral advocates for the needs of the system as a whole.

Organizational Realities

The complex structure of the Board and committees was certainly a political masterpiece, and in principle, it ensured that while groups had blocking power, no one bank or person could dominate the organization. In practice, however, the design did allow one person in particular to exert enormous influence: Dee Hock. By stipulating that the president of the new organization could not chair the Board, Hock had limited his own power to that of persuasion, but as Nocera remarked, “this was Hock at his most coy. It was precisely his ability to persuade that made him powerful.”⁷⁶ Chuck Russell, who would succeed Hock as CEO in 1984, noted that Hock also used the structure of the Board and committees to his advantage:

... [Hock] structured the Board in such a way that *he* ran the company and there was no question about it. What he did, he very cleverly split up the power of the big banks into different groups. And if you get a Board that is widely split, *management* runs the company. Dee understood that; he understood it very well, and he taught it to me very well, because when I took over, man I kept that thing split into smithereens. You want a Board of at least 25 guys, because they’ll never accomplish anything. Then you want to form lots of

⁷⁴Honey interview.

⁷⁵Honey interview.

⁷⁶Nocera (1994), p. 92.

committees to supposedly do something, but you very strategically put fighting banks on each committee.⁷⁷

A number of sources remarked that during the first decade of the Visa organization, it was in essence a dictatorship, and the only true power-broker was Hock. This was in part due to Hock's early successes in automating the core system processes, which will be discussed in detail in the upcoming chapters. In the minds of the member banks, Hock literally *saved the system* as well as their card programs, turning them from a source of major losses into a profit-making department. This gave Hock a large amount of influence with the Board, and its structure further ensured that he could shape the system toward his own vision: "the world's premier system for the exchange of value."⁷⁸

Convincing the two hundred fully-licensed banks, and their thousands of sub-licensees, to join the new organization was no easy task, but Hock was persuasive and persistent. In 1970, only 90 days after Hock began the formation process, all the licensees had agreed to join, and the new organization was legally formed as a Delaware membership corporation named National BankAmericard Incorporated (NBI). The BofA became just another member, though they retained five special seats on the Board for the first few years to recognize their unique contribution in forming the original system.⁷⁹

The exact legal description of the organization is a "for-profit, non-stock membership corporation."⁸⁰ This rather unusual classification is actually quite important. Banks at this time were not allowed to own stock in anything but a Bank Service Corporation (BSC), but BSCs were also subject to stringent regulation. By creating NBI as a non-stock membership corporation, Hock cleverly enabled the banks to "own" it through membership while at the same time avoided unwelcome government regulation.

Although NBI was legally formed as a for-profit enterprise, its owners were its customers, so it effectively operated as a non-profit entity. Because it did not issue any stock, and therefore had no market capitalization nor paid any dividends, any "accumulated net revenue" from member fees was used to finance the ongoing work of the organization. The Visa organization continued this structure and method of operation until its recent reorganization into a publicly-traded stock corporation. Although the member banks still own the majority of the corporation, non-member organizations and personal investors may now purchase shares in Visa, and consequently, will expect healthy returns on their investments. Only time will tell if this need to meet investor's return expectations will fundamentally alter Visa's motivations and priorities.

⁷⁷Russell interview.

⁷⁸According to Nocera, Hock actually convinced the Board to adopt a resolution with that exact wording, even though most of the members had no idea what he meant by that.

⁷⁹Nocera (1994), p. 92. These seats were reduced by one each year until Ken Larkin was the only remaining director from the BofA.

⁸⁰Katz interview.

An New Kind of Organization?

Although Hock's methods for arriving at the NBI organizational structure may have been novel, the resulting structure itself was not terribly unique. Most joint ventures in the banking industry, both before NBI and since, have taken similar approaches to ownership and governance, though NBI's complex representational design may have allowed more of a diversity of voices, at least in principle. The airlines had also created a similar organization for their Universal Air Travel Plan discussed in Chap. 1. This kind of structure can also be found in other industries besides banking and payments: for example, regional multiple listing services in the American real estate industry are typically owned by multiple competing brokerage firms, each of which owns and has representational governance over a central organization that provides informational services for the network.

But NBI was only the start of what would soon become the larger, multi-layered, worldwide organization eventually known as Visa. Starting in 1972, Hock began to implement the same sort of organizational design at the international level, resulting in a new kind of organization that has few if any parallels. For Hock, it was this worldwide version of the organization that was the first, albeit flawed, example of a "chaordic" organization, one that seamlessly blended elements of chaos and order. This worldwide organization went beyond the typical international joint-venture to encompass tens of thousands of financial institutions in hundreds of countries, dealing with a wide variety of currencies and banking systems. The members of this international organization were often themselves national systems like NBI, each of which was subject to the international rules, but could also enforce additional local rules that made sense for the specific country. I will describe the creation and structure of this worldwide organization in Chaps. 6 and 9.

Conclusion

In this chapter we examined what was wrong with the BankAmericard licensing system, noting that, while the operational problems may have had technical solutions within the existing organizational structure, that structure had severe problems of its own that made the existing structure untenable. This ultimately led Hock and his fellow licensees to revolt against the Bank of America and form a new, jointly-owned organization known as National BankAmericard Incorporated (NBI) in 1970.

In the next chapter we will turn our attention to NBI's first steps, especially how Hock and his new staff solved several of the most pressing organizational problems. At the heart of these solutions were the operating regulations, a series of rules that governed everything from the physical design of the card, to the fees each party must pay to process transactions, to the rights and responsibilities each party has during a transaction dispute. As we shall see, these rules, along with NBI's role as a kind of judiciary, helped restore not only order to the inter-organizational workflow, but also a minimal level of trust between the members that was necessary for the system to survive, function, and grow.



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