TARGET

October 10, 2006

By E-Mail to Comments@FDIC.gov

Mr. Robert E. Feldman
Executive Secretary
Attn: Comments
Federal Deposit Insurance Corporation
550 17th Street NW
Washington D.C. 20429

**RE: Target's Response to Request for Comment on Industrial Banks**

The Federal Deposit Insurance Corporation ("FDIC") has issued a Notice and Request for Comment regarding the ownership and regulation of industrial loan companies and industrial banks. Target commends the FDIC for its reasoned approach in gathering the facts before taking a position on what has become a politically charged issue and thanks the FDIC for the opportunity to submit our views.

Target is the second-largest general merchandise retailer in the United States, with more than 1400 stores in 47 states and annual sales of $52 billion. Target has an industrial bank subsidiary, Target Bank, which was chartered under Utah law in 2004, as well as a limited purpose credit card bank, Target National Bank, which was chartered under federal law in 1994. As a commercial company with 12 years' experience owning an FDIC-insured depository institution, Target is well-qualified to speak to this issue.

The FDIC requests responses to 12 specific questions, but the gist of the inquiry can be distilled to this: Does commercial company ownership of an industrial bank (a) pose greater risk than traditional bank holding company ownership, and/or (b) give the industrial bank an unfair competitive advantage over other banks?

Target submits that the answer to these fundamental questions is no. History has proven that industrial banks in general, and commercial-owned industrial banks in particular, pose no more risk – and in many cases, less risk – than other banks. Moreover, as the traditional financial services industry continues to evolve and, in many aspects, consolidate, commercial ownership of banks is a powerful avenue to *preserve* competition in banking.

Target Stores offered commercial credit for a number of years in response to customer demand. The program was used primarily by tax-exempt entities (such as schools) purchasing supplies and by social services agencies providing clothing and household items to low-income people and victims of fire or natural disaster. The program was limited in scope, extremely manual, and inefficient for both Target and its customers. Through its industrial bank, Target was able to expand the business credit program into a national product with consistent terms and greater utility. In addition to the schools, not-for-profits and social service agencies who converted from the old program to the new one, Target Business Card customers include small business owners who desire a limited purpose credit card to establish a business credit rating and allow controlled purchasing power for their employees at Target Stores. The Target Business Card is a valuable service to these customers which was not available through any other financial institution and would not be available if Target did not own an industrial bank.

Target's experience in chartering an industrial bank and the regulatory environment in which Target Bank operates offer a clear illustration of how the current structure imposes appropriate controls and sufficient ongoing oversight. The FDIC and the State of Utah in approving the Target Bank charter imposed a number of conditions and requirements to protect the safety and soundness of the bank and to ensure independence from inappropriate parental influence. Among other things:

- Target was required to establish that its industrial bank would not have an adverse effect on existing institutions, would promote the public need and convenience, and had a reasonable opportunity of success.

- Target Bank was and remains subject to minimum capital requirements. In addition, the FDIC required that Target Corporation enter a Capital and Liquidity Maintenance Agreement to ensure that the Bank remains at all times adequately capitalized and able to meet its short and long term liquidity needs.

- A majority of Target Bank's directors are required to be independent of the parent. Bank board members are experienced in financial services and were subject to FDIC approval after background checks and review of their qualifications.

Like all insured institutions, Target Bank is subject to regular Compliance, Safety and Soundness, and Community Reinvestment Act examinations. Along with the investigation of the Bank's financial condition, a significant component of the safety and soundness examination is an in-depth review of all transactions between Target Bank and its affiliates. In addition, because Target provides information systems for the Bank, the FDIC and the State of Utah perform a Bank Information Systems examination of Target itself. In sum, the regulators have all the authority they could need and the system as currently structured is wholly adequate to guard against risk as effectively for industrial banks as it does for any other financial institution.

In fact, Target Bank itself actually has no risk of loan loss. Under current regulations, all of its loans are considered to be affiliate transactions because they finance purchases at the affiliate retailer. As a result, Target is required to secure those extensions of credit. Target Bank has a security interest in a deposit held at the Bank to protect it from loss. This is a perfect example of how the circumstances of each institution determine the level of risk, not the nature of the institution or its parent. To the extent the FDIC's concern is to control risk and avoid bank failure, it makes no sense to eliminate the safest possible institution.

Ownership of industrial banks by commercial companies is entirely consistent with healthy competition. Target is, first and foremost, a retailer. Target Bank was formed to provide a service to Target customers that was not otherwise available. Target Bank's services may expand as additional customer needs are identified that can be served more effectively or efficiently by a Target-owned institution, but there is little chance that it will expand into products and services unrelated to Target's retail operations. The reason is that customers are unlikely to accept Target as a full-service financial service provider. The market, rather than artificial regulatory requirements, can and should determine the arena within which Target Bank can compete.

Similarly, traditional banks saw an opportunity to expand into other financial activities, such as investment and insurance services, to take advantage of existing customer relationships and provide a comprehensive range of financial services in a convenient and efficient manner. In short, they provide services that customers expect from full service banks, capitalizing on their customer relationships, their strengths, and their position in the marketplace, just as Target does. This is the very essence of competition.

One aspect of the current debate which has received little attention is the interest of traditional financial institutions in keeping industrial banks from competing in the relatively new arena of healthcare spending accounts. Billions of dollars are poised to be managed through these accounts, and the largest banks would benefit the most if they could eliminate the competition of industrial banks owned by healthcare companies. The elimination of competition when these products are in their infancy is not likely to be in the best interest of consumers.

The preceding comments generally address the issues raised by the FDIC. We also want to highlight our responses to certain of the specific questions in the FDIC Request. For ease of reference, the questions are reproduced below.

**1. Have developments in the ILC industry in recent years altered the relative risk profile of ILCs compared to other insured depository institutions? What specific effects have there been on the ILC industry, safety and soundness, risks to the Deposit Insurance Fund, and other insured depository institutions? What modifications, if any, to its supervisory programs or regulations should the FDIC consider in light of the evolution of the ILC industry?**

The recent growth of the industrial bank industry may reflect increasing recognition of the ILC charter as a vehicle to provide financial services, but there is no evidence to suggest that ILCs are relatively more risky than other institutions. Industrial banks are subject to the same requirements for capitalization, safe and sound operations, and qualified management, as well as the same restrictions on transactions with affiliates, as any other insured institution. The regulators of the industrial bank, which include both the state banking department and the FDIC, have the power to examine all aspects of the bank's business and any other matters that impact the bank, including the activities of the bank's affiliates with respect to the bank.[1]

[1] "Section 10(b)(4) of the [Federal Deposit Insurance] Act authorizes FDIC examiners in the course of examining insured banks 'to make such examinations of the affairs of any affiliate of any depository institution as may be necessary to disclose fully – (i) the relationship between such depository institution and any such affiliate; and (ii) the effect of such relationship on the depository institution.'" Chapter 4.3, page 4.3-1, Manual of Examination Policies, Federal Deposit Insurance Corporation (rev. March 2004).

History supports the conclusion that there is nothing about the powers of industrial banks or the supervisory structure within which they operate which results in greater risk to the integrity of the bank, the insurance fund, or the industry. There have been few industrial bank failures and the resulting losses were minimal. To our knowledge, those who challenge the industrial bank industry have been unable to cite any specific examples, either real or theoretical, of a risk that is not adequately addressed by the current supervisory structure.

**2. Do the risks posed by ILCs to safety and soundness or to the Deposit Insurance Fund differ based upon whether the owner is a financial entity or a commercial entity? If so, how and why? Should the FDIC apply its supervisory or regulatory authority differently based upon whether the owner is a financial entity or a commercial entity? If so, how should the FDIC determine when an entity is "financial" and in what way should it apply its authority differently?**

Whether the owner of the industrial bank is a financial or a commercial company has no inherent impact on the bank's level of risk. The parent company may increase or decrease the bank's risk, or may be a neutral factor, but the impact is particular to the circumstances of the individual institution, not the nature of the parent. Indeed, the question how the FDIC can even determine whether an entity is "financial" or "commercial" becomes increasingly interesting as traditional banks continue to expand the scope of their permitted activities. The Gramm-Leach-Bliley Act in 1999 dramatically expanded the power of traditional banks to engage in non-traditional activities such as securities, investment and insurance services. Today, the financial services industry is lobbying heavily to expand its ability to engage in real estate brokerage activities. As time goes on, the distinction between "financial" and "commercial" activities will become increasingly blurred. That Congress has seen fit to allow traditional banks to expand into previously unavailable lines of business also reflects the recognition that banking and commerce can, in fact, be combined to provide comprehensive, convenient and cost-effective financial services without added risk.

**3. Do the risks posed by ILCs to safety and soundness or to the Deposit Insurance Fund differ based on whether the owner is subject to some form of consolidated Federal supervision? If so, how and why? Should the FDIC assess differently the potential risks associated with ILCs owned by companies that (i) are subject to some form of consolidated Federal supervision, (ii) are financial in nature but not currently subject to some form of consolidated Federal supervision, or (iii) cannot qualify for some form of consolidated Federal supervision? How and why should the consideration of these factors be affected?**

Industrial bank regulators have the authority to supervise all activities of the bank, as well as any activities of the bank's affiliates which impact the bank. In addition, they have the ability to monitor and impose restrictions with respect to the bank's capitalization and its relationship with its affiliates. There is no need for consolidated Federal banking supervision of activities of the parent which do not impact the bank; indeed, it is difficult even to conceive of what that supervision might look like.

**4. What features or aspects of a parent of an ILC (not already discussed in Questions 2 and 3) should affect the FDIC's evaluation of applications for deposit insurance or other notices or applications? What would be the basis for the FDIC to consider those features or aspects?**

The FDIC should consider the same features and aspects of an industrial bank's parent as it does of any other financial institution's ownership and affiliations. The analysis must be specific to the entities at hand, not driven by artificial distinctions based on features that may or may not impact the bank in any given instance.

**5. The FDIC must consider certain statutory factors when evaluating an application for deposit insurance (see 12 U.S.C. 1816), and certain largely similar statutory factors when evaluating a change in control notice (see 12 U.S.C. 1817(j)(7)). Are these the only factors FDIC may consider in making such evaluations? Should the consideration of these factors be affected based on the nature of the ILC's proposed owner? Where an ILC is to be owned by a company that is not subject to some form of consolidated Federal supervision, how would the consideration of these factors be affected?**

Please see Target's response to Questions 3 and 4. Industrial bank applications, whether by commercial or financial owners, should be evaluated on the same basis as any other application.

**6. Should the FDIC routinely place certain restrictions or requirements on all or certain categories of ILCs that would not necessarily be imposed on other institutions (for example, on the institution's growth, ability to establish branches and other offices, ability to implement changes in the business plan, or capital maintenance obligations)? If so, which restrictions or requirements should be imposed and why? Should the FDIC routinely place different restrictions or requirements on ILCs based on whether they are owned by commercial companies or companies not subject to some form of consolidated Federal supervision? If such conditions are believed appropriate, should the FDIC seek to establish the underlying requirements and restrictions through a regulation rather than relying upon conditions imposed in the order approving deposit insurance?**

Please see Target's response to Questions 3 and 4. There is no reason to treat industrial banks as a category differently from other financial institutions, and no reason to treat industrial banks with commercial owners differently from those with financial owners.

**7. Can there be conditions or regulations imposed on deposit insurance applications or changes of control of ILCs that are adequate to protect an ILC from any risks to safety and soundness or to the Deposit Insurance Fund that exist if an ILC is owned by a financial company or a commercial company? In the interest of safety and soundness, should the FDIC consider limiting ownership of ILCs to financial companies?**

Please see Target's response to Questions 3 and 4. There is no evidence and no reason to believe that industrial banks pose a greater risk than other financial institutions, or that commercial entity ownership of an industrial bank poses a greater risk than financial entity ownership.

**8. Is there a greater likelihood that conflicts of interest or tying between an ILC, its parent, and affiliates will occur if the ILC parent is a commercial company or a company not subject to some form of consolidated Federal supervision? If so, please describe those conflicts of interest or tying and indicate whether or to what extent such conflicts of interest or tying are controllable under current laws and regulations. What regulatory or supervisory steps can reduce or eliminate such risks? Does the FDIC have authority to address such risks in acting on applications and notices? What additional regulatory or supervisory authority would help reduce or eliminate such risks?**

Industrial banks owned by commercial companies are subject to the same anti-tying regulations and affiliate transaction restrictions as other financial institutions. Affiliate transactions, including opportunities for tying, are examined at the bank level, and consolidated Federal supervision would not provide any additional protection in this regard.

**9. Do ILCs owned by commercial entities have a competitive advantage over other insured depository institutions? If so, what factors account for that advantage? To what extent can or should the FDIC consider this competitive environment in acting on applications and notices? Can those elements be addressed through supervisory processes or regulatory authority? If so, how?**

There is no evidence, and no credible examples have been cited, to support the theory that permitting commercial companies to own banks under the current regulatory structure gives them an unfair competitive advantage. Companies with different regulatory structures compete with each other every day – the most common example is probably public companies that are subject to myriad SEC requirements and restrictions competing with private companies that are relatively unfettered.

Parent companies that are not subject to consolidated regulation by the Federal Reserve may be subject to regulation by the SEC, may fall under the jurisdiction of agencies such as the Federal Trade Commission, and/or may be subject to a variety of other regulatory and administrative regimes. It is simply not relevant to fair competition in general whether the competing businesses are structured or regulated in the same manner. In this particular instance, there is no indication that the Federal Reserve's regulation of bank holding companies impairs the ability of those companies' subsidiary banks to compete on a level playing field with industrial banks owned by commercial companies.

The FDIC should be extremely careful in evaluating the effects on competition as a factor, whether in considering individual applications or in considering changes to current regulatory authority. If the regulatory environment does not create a competitive imbalance, it is not appropriate to use the regulatory process to manipulate market power in the private sector. Indeed, imposing restrictions on industrial banks may well have the effect of reducing competition in financial services, in light of the increasing concentration of market power in the largest institutions.

**10. Are there potential public benefits when a bank is affiliated with a commercial concern? Could those benefits include, for example, providing greater access to banking services for consumers? To what extent can or should the FDIC consider those benefits if they exist?**

As a general principle, greater diversity in the types of companies that can be involved in banking will almost certainly increase the variety and availability of financial products and services. Commercial companies are often in a better position to identify needs and deliver products tailored to specific consumer and business banking needs. The opportunity for greater competition in banking services, particularly in the absence of any evidence that commercial ownership of banks creates additional risk or places certain banks at an unfair competitive advantage, should be a primary consideration for the FDIC in evaluating this issue.

**11. In addition to the information requested by the above questions, are there other issues or facts that the FDIC should consider that might assist the FDIC in determining whether statutory, regulatory, or policy changes should be made in the FDIC's oversight of ILCs?**

The FDIC should take great care in evaluating the responses to its request for comment. Opponents of the ILC industry, and of commercial ownership of industrial banks, make broad and conclusory statements about increased risk, the need for consolidated Federal supervision, and unfair competition, but we are not aware of any specific examples, either of fact or theory, cited to support their position. Most participants in the debate have an economic interest in the outcome, as Target certainly does, and it is extremely important that any determination be made on the basis of objective fact rather than unsupported generalities.

**12. Given that Congress has expressly excepted owners of ILCs from consolidated bank holding company regulation under the Bank Holding Company Act, what are the limits on the FDIC's authority to impose such regulation absent further Congressional action?**

The FDIC does not currently have the authority to supersede the legislative determination to exempt the owners of industrial banks from the Bank Holding Company Act. The exemption is both necessary and appropriate, particularly when the owner is engaged in businesses totally unrelated to financial services. A banking regulator's expertise, as well as its area of concern, is the operation of the bank, and regulators currently have the authority to examine the bank and any activities of its affiliates that impact the bank. That authority is sufficient in theory, and has proven sufficient in fact, to monitor and control risk for industrial banks as effectively as for traditional banks.

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In summary, it is Target's position that the current regulatory and supervisory structure provides adequate oversight and control over industrial banks, including those owned by commercial entities. Industrial banks categorically pose no different or greater risk than traditional financial institutions, and regulators currently have the authority to examine any activity of the parent which impacts the bank, even if the parent is not subject to consolidated Federal supervision. Moreover, nothing about the current supervisory structure gives industrial banks an unfair competitive advantage Indeed, limiting the powers of industrial banks, or the ability of commercial entities to own industrial banks, is more likely to impair competition in financial services, to the detriment of consumers and the economy in general

Sincerely,

**Target Corporation**

By Terrence J Scully
President, Target Financial Services