

# Statement of Management's Responsibility for Financial Information

Bank of Montreal's management is responsible for presentation and preparation of the annual consolidated financial statements, Management's Discussion and Analysis ("MD&A") and all other information in the Annual Report.

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and the requirements of the Securities and Exchange Commission ("SEC") in the United States, as applicable. The financial statements also comply with the provisions of the *Bank Act* and related regulations, including interpretations of GAAP by our regulator, the Superintendent of Financial Institutions Canada.

The MD&A has been prepared in accordance with the requirements of securities regulators including National Instrument 51-102 of the Canadian Securities Administrators ("CSA") as well as Item 303 of Regulation S-K of the *Securities Exchange Act*, and their related published requirements.

The consolidated financial statements and information in the MD&A necessarily include amounts based on informed judgments and estimates of the expected effects of current events and transactions with appropriate consideration to materiality. In addition, in preparing the financial information we must interpret the requirements described above, make determinations as to the relevancy of information to be included, and make estimates and assumptions that affect reported information. The MD&A also includes information regarding the impact of current transactions and events, sources of liquidity and capital resources, operating trends, risks and uncertainties. Actual results in the future may differ materially from our present assessment of this information because future events and circumstances may not occur as expected.

The financial information presented elsewhere in the Annual Report is consistent with that in the consolidated financial statements.

In meeting our responsibility for the reliability of financial information, we maintain and rely on a comprehensive system of internal controls and internal audit, including organizational and

procedural controls and internal controls over financial reporting. Our system of internal control includes written communication of our policies and procedures governing corporate conduct and risk management; comprehensive business planning; effective segregation of duties; delegation of authority and personal accountability; careful selection and training of personnel; and accounting policies which we regularly update. This structure ensures appropriate internal control over transactions, assets and records. We also regularly audit internal controls. These controls and audits are designed to provide us with reasonable assurance that the financial records are reliable for preparing financial statements and other financial information, assets are safeguarded against unauthorized use or disposition, liabilities are recognized, and we are in compliance with all regulatory requirements.

We, as Bank of Montreal's Chief Executive Officer and Chief Financial Officer, will certify the Bank of Montreal's annual filings with the CSA and the SEC as required in Canada by Multilateral Instrument 52-109 (Certification of Disclosure in Issuers' Annual and Interim Filings) and in the United States by the *Sarbanes-Oxley Act*.

In order to provide their opinion on our consolidated financial statements, the Shareholders' Auditors review our system of internal controls and conduct their work to the extent that they consider appropriate.

The Board of Directors, based on recommendations from its Audit and Conduct Review Committees and its Risk Review Committee, reviews and approves the financial information contained in the Annual Report, including the MD&A, and oversees management's responsibilities for the presentation and preparation of financial information, maintenance of appropriate internal controls, management and control of major risk areas and assessment of significant and related party transactions.

The Shareholders' Auditors and the Bank's Chief Auditor have full and free access to the Board of Directors and its committees to discuss audit, financial reporting and related matters.



**F. Anthony Comper**  
President and Chief Executive Officer



**Karen E. Maidment**  
Senior Executive Vice-President  
and Chief Financial Officer

Canada  
November 29, 2005

## Shareholders' Auditors' Report

### To the Shareholders of Bank of Montreal

We have audited the consolidated balance sheets of Bank of Montreal as at October 31, 2005 and 2004 and the consolidated statements of income, changes in shareholders' equity and cash flows for each of the years in the two-year period ended October 31, 2005. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.



**KPMG LLP**  
Chartered Accountants

Canada  
November 29, 2005

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Bank of Montreal as at October 31, 2005 and 2004 and the results of its operations and its cash flows for each of the years in the two-year period ended October 31, 2005 in accordance with Canadian generally accepted accounting principles.

The consolidated statements of income, changes in shareholders' equity and cash flows for the year ended October 31, 2003, prior to an adjustment for changes in the Bank's accounting policy relating to the reclassification of financial instruments as liabilities and equity as described in Note 20 to the consolidated financial statements, were audited by KPMG LLP and PricewaterhouseCoopers LLP, who expressed an opinion without reservation on those statements in the shareholders' auditors' report dated November 25, 2003. We have audited the adjustments to the consolidated statements of income, changes in shareholders' equity and cash flows for the year ended October 31, 2003 and, in our opinion, such adjustments, in all material respects, are appropriate and have been properly applied.

# Consolidated Balance Sheet

As at October 31 (Canadian \$ in millions)

	2005	2004
<b>Assets</b>		Restated (see Note 20)
<b>Cash Resources</b> (Notes 2 and 27)	<b>\$ 20,721</b>	\$ 18,045
<b>Securities</b> (Notes 3 and 27)		
Investment (fair value \$12,933 in 2005 and \$15,103 in 2004)	12,936	15,017
Trading	44,309	35,444
Loan substitutes	11	11
	<b>57,256</b>	50,472
<b>Loans</b> (Notes 4 and 7)		
Residential mortgages	60,871	56,444
Consumer instalment and other personal	27,929	24,887
Credit cards	4,648	3,702
Businesses and governments	47,803	44,559
Securities borrowed or purchased under resale agreements	28,280	22,609
	<b>169,531</b>	152,201
Customers' liability under acceptances (Note 4)	5,934	5,355
Allowance for credit losses (Note 4)	(1,128)	(1,308)
	<b>174,337</b>	156,248
<b>Other Assets</b>		
Derivative financial instruments (Note 9)	31,517	25,448
Premises and equipment (Note 10)	1,847	2,020
Goodwill (Note 13)	1,091	1,507
Intangible assets (Note 13)	196	480
Other (Note 14)	10,567	10,974
	<b>45,218</b>	40,429
<b>Total Assets</b>	<b>\$ 297,532</b>	\$ 265,194
<b>Liabilities and Shareholders' Equity</b>		
<b>Deposits</b> (Note 15)		
Banks	\$ 25,473	\$ 20,654
Businesses and governments	92,437	79,614
Individuals	75,883	74,922
	<b>193,793</b>	175,190
<b>Other Liabilities</b>		
Derivative financial instruments (Note 9)	28,868	23,973
Acceptances (Note 16)	5,934	5,355
Securities sold but not yet purchased (Note 16)	16,142	10,441
Securities lent or sold under repurchase agreements (Note 16)	22,657	21,345
Other (Note 16)	12,203	12,156
	<b>85,804</b>	73,270
<b>Subordinated Debt</b> (Note 17)	<b>2,469</b>	2,395
<b>Preferred Share Liability</b> (Note 20)	<b>450</b>	450
<b>Capital Trust Securities</b> (Note 18)	<b>1,150</b>	1,150
<b>Shareholders' Equity</b>		
Share capital (Note 20)	4,618	4,453
Contributed surplus (Note 21)	20	10
Net unrealized foreign exchange loss	(612)	(497)
Retained earnings	9,840	8,773
	<b>13,866</b>	12,739
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 297,532</b>	\$ 265,194

The accompanying notes to consolidated financial statements are an integral part of these statements.  
Certain comparative figures have been reclassified to conform with the current year's presentation.



**F. Anthony Comper**  
President and Chief Executive Officer



**Jeremy H. Reitman**  
Chairman, Audit Committee

# Consolidated Statement of Income

For the Year Ended October 31 (Canadian \$ in millions, except as noted)

	2005	2004	2003
<b>Interest, Dividend and Fee Income</b>			
Loans	\$ 7,728	\$ 6,743	\$ 6,970
Securities (Note 3)	1,830	1,476	1,601
Deposits with banks	606	438	356
	<b>10,164</b>	8,657	8,927
<b>Interest Expense</b>			
Deposits	3,703	2,744	2,957
Subordinated debt	202	193	235
Preferred shares and capital trust securities (Notes 18 and 20)	97	124	122
Other liabilities	1,375	798	836
	<b>5,377</b>	3,859	4,150
<b>Net Interest Income</b>	<b>4,787</b>	4,798	4,777
Provision for credit losses (Note 4)	179	(103)	455
Net Interest Income After Provision for Credit Losses	<b>4,608</b>	4,901	4,322
<b>Non-Interest Revenue</b>			
Securities commissions and fees	1,092	1,055	894
Deposit and payment service charges	734	746	756
Trading revenues	413	200	275
Lending fees	313	317	293
Card fees	334	261	290
Investment management and custodial fees	305	307	303
Mutual fund revenues	437	378	321
Securitization revenues (Note 7)	113	177	244
Underwriting and advisory fees	357	343	268
Investment securities gains (losses) (Note 3)	165	175	(41)
Foreign exchange, other than trading	180	177	160
Insurance income	162	139	124
Other	447	276	333
	<b>5,052</b>	4,551	4,220
Net Interest Income and Non-Interest Revenue	<b>9,660</b>	9,452	8,542
<b>Non-Interest Expense</b>			
Employee compensation (Notes 21 and 22)	3,746	3,632	3,578
Premises and equipment (Note 10)	1,264	1,252	1,264
Amortization of intangible assets (Note 13)	94	104	105
Travel and business development	247	239	225
Communications	122	138	162
Business and capital taxes	107	99	106
Professional fees	243	262	255
Other	504	431	392
Total Non-Interest Expense	<b>6,327</b>	6,157	6,087
<b>Income Before Provision for Income Taxes and Non-Controlling Interest in Subsidiaries</b>	<b>3,333</b>	3,295	2,455
Income taxes (Note 23)	875	972	652
	<b>2,458</b>	2,323	1,803
Non-controlling interest in subsidiaries (Notes 16 and 18)	58	17	22
<b>Net Income</b>	<b>\$ 2,400</b>	\$ 2,306	\$ 1,781
Preferred share dividends (Note 20)	\$ 30	\$ 31	\$ 38
Net income available to common shareholders	\$ 2,370	\$ 2,275	\$ 1,743
Average common shares (in thousands)	500,060	501,656	496,208
Average diluted common shares (in thousands)	510,736	515,045	507,009
<b>Earnings Per Share</b> (Canadian \$) (Note 24)			
Basic	\$ 4.74	\$ 4.53	\$ 3.51
Diluted	4.64	4.42	3.44
<b>Dividends Declared Per Common Share</b>	<b>1.85</b>	1.59	1.34

The accompanying notes to consolidated financial statements are an integral part of these statements. Certain comparative figures have been reclassified to conform with the current year's presentation.

# Consolidated Statement of Changes in Shareholders' Equity

For the Year Ended October 31 (Canadian \$ in millions, except as noted)

	2005	2004	2003
<b>Preferred Shares</b> (Note 20)			
Balance at beginning of year	\$ 596	\$ 596	\$ 1,517
Impact of adopting new accounting requirements for liabilities and equity (Note 20)	–	–	(850)
Balance at beginning of year (as restated)	596	596	667
Translation adjustment on shares issued in a foreign currency	–	–	(71)
Balance at End of Year	596	596	596
	Number of Shares		
	2005	2004	2003
<b>Common Shares</b> (Note 20)			
Balance at beginning of year	500,896,857	499,632,368	492,504,878
Issued under the Shareholder Dividend			
Reinvestment and Share Purchase Plan (Note 20)	1,258,463	1,120,931	1,101,305
Issued under the Stock Option Plan (Note 21)	4,736,826	6,239,301	5,325,916
Issued on the exchange of shares of a subsidiary corporation (Note 20)	284,722	124,757	348,518
Issued on the acquisition of a business (Note 20)	–	–	634,551
Repurchased for cancellation (Note 20)	(6,957,800)	(6,220,500)	(282,800)
Balance at End of Year	500,219,068	500,896,857	499,632,368
<b>Contributed Surplus</b>			
Balance at beginning of year	10	3	–
Stock option expense (Note 21)	10	7	3
Gain on treasury shares, net of applicable income taxes (Note 1)	–	15	–
Common shares repurchased for cancellation (Note 20)	–	(15)	–
Balance at End of Year	20	10	3
<b>Net Unrealized Foreign Exchange Gain (Loss)</b>			
Balance at beginning of year	(497)	(195)	419
Unrealized loss on translation of net investments in foreign operations	(311)	(758)	(1,674)
Hedging gain	297	710	1,661
Income taxes	(101)	(254)	(601)
Balance at End of Year	(612)	(497)	(195)
<b>Retained Earnings</b>			
Balance at beginning of year	8,773	7,566	6,499
Cumulative impact of adopting new accounting requirements for Variable Interest Entities, net of applicable income taxes (Note 8)	(42)	–	–
Net income	2,400	2,306	1,781
Dividends – Preferred shares (Note 20)	(30)	(31)	(38)
– Common shares (Note 20)	(925)	(797)	(666)
Common shares repurchased for cancellation (Note 20)	(336)	(271)	(10)
Balance at End of Year	9,840	8,773	7,566
<b>Total Shareholders' Equity</b>	\$ 13,866	\$ 12,739	\$ 11,632

The accompanying notes to consolidated financial statements are an integral part of these statements.

# Consolidated Statement of Cash Flows

For the Year Ended October 31 (Canadian \$ in millions)

	2005	2004	2003
<b>Cash Flows from Operating Activities</b>			
Net income	\$ 2,400	\$ 2,306	\$ 1,781
Adjustments to determine net cash flows provided by (used in) operating activities			
Write-down of investment securities	11	63	153
Net gain on investment securities	(176)	(238)	(112)
Net (increase) in trading securities	(8,865)	(449)	(12,692)
Provision for credit losses	179	(103)	455
Gain on sale of securitized loans	(82)	(127)	(157)
Change in derivative financial instruments – (Increase) decrease in derivative asset	(6,069)	(4,232)	892
– Increase (decrease) in derivative liability	4,895	3,258	(1,380)
Amortization of premises and equipment	377	365	375
Amortization of intangible assets	94	104	116
Future income tax expense (benefit)	91	157	(37)
Net increase (decrease) in current income taxes	(369)	(1,096)	401
Change in accrued interest – (Increase) decrease in interest receivable	(230)	(30)	87
– Increase (decrease) in interest payable	155	7	(141)
Changes in other items and accruals, net	1,382	2,287	986
Gain on sale of Harrisdirect LLC (Note 12)	(49)	–	–
Gain on sales of land and buildings (Note 10)	(29)	–	–
<b>Net Cash Provided by (Used in) Operating Activities</b>	<b>(6,285)</b>	<b>2,272</b>	<b>(9,273)</b>
<b>Cash Flows from Financing Activities</b>			
Net increase in deposits	17,851	2,205	9,713
Net increase in securities sold but not yet purchased	5,701	2,186	601
Net increase (decrease) in securities lent or sold under repurchase agreements	1,312	(2,722)	(788)
Net increase (decrease) in liabilities of subsidiaries	(231)	491	(157)
Proceeds from issuance of securities of a subsidiary	447	595	–
Repayment of subordinated debt (Note 17)	(899)	(400)	(752)
Proceeds from issuance of subordinated debt (Note 17)	1,000	–	–
Redemption of preferred share liability	–	(400)	–
Proceeds from issuance of common shares	217	240	175
Proceeds from sales of treasury shares	–	149	–
Common shares repurchased for cancellation (Note 20)	(390)	(333)	(12)
Dividends paid	(955)	(829)	(704)
<b>Net Cash Provided by Financing Activities</b>	<b>24,053</b>	<b>1,182</b>	<b>8,076</b>
<b>Cash Flows from Investing Activities</b>			
Net (increase) decrease in interest bearing deposits with banks	(2,885)	1,974	(1,741)
Purchases of investment securities	(14,600)	(24,773)	(29,348)
Maturities of investment securities	8,335	12,699	18,999
Proceeds from sales of investment securities	8,246	16,334	9,298
Net (increase) decrease in loans, customers' liability under acceptances and loan substitute securities	(15,025)	(8,678)	189
Proceeds from securitization of loans	3,130	1,382	–
Net (increase) decrease in securities borrowed or purchased under resale agreements	(5,671)	(1,611)	2,959
Proceeds from sales of land and buildings (Note 10)	347	–	–
Premises and equipment – net purchases	(472)	(305)	(254)
Acquisitions (Note 11)	(194)	(385)	(91)
Proceeds from sale of Harrisdirect LLC (Note 12)	827	–	–
<b>Net Cash Provided by (Used in) Investing Activities</b>	<b>(17,962)</b>	<b>(3,363)</b>	<b>11</b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>(194)</b>	<b>91</b>	<b>(1,186)</b>
Cash and Cash Equivalents at Beginning of Year	2,606	2,515	3,701
<b>Cash and Cash Equivalents at End of Year</b>	<b>\$ 2,412</b>	<b>\$ 2,606</b>	<b>\$ 2,515</b>
<b>Represented by:</b>			
Cash and non-interest bearing deposits with Bank of Canada and other banks	\$ 1,309	\$ 1,558	\$ 1,693
Cheques and other items in transit, net	1,103	1,048	822
	\$ 2,412	\$ 2,606	\$ 2,515
<b>Supplemental Disclosure of Cash Flow Information</b>			
Amount of interest paid in the year	\$ 5,222	\$ 3,852	\$ 4,291
Amount of income taxes paid in the year	\$ 1,065	\$ 1,947	\$ 324

The accompanying notes to consolidated financial statements are an integral part of these statements. Certain comparative figures have been reclassified to conform with the current year's presentation.

# Notes to Consolidated Financial Statements

## Note 1 ▶ Basis of Presentation

We prepare our consolidated financial statements in accordance with Canadian generally accepted accounting principles (“GAAP”), including interpretations of GAAP by our regulator, the Superintendent of Financial Institutions Canada.

We reconcile our Canadian GAAP results to those that would result under United States GAAP. Significant differences in consolidated total assets, total liabilities or net income arising from applying United States GAAP are described in Note 29. In addition, our consolidated financial statements comply with applicable disclosure requirements of United States GAAP, except we do not provide disclosures related to the Canadian and United States GAAP differences described in Note 29.

### Basis of Consolidation

We conduct business through a variety of corporate structures, including subsidiaries and joint ventures. Subsidiaries are those where we exercise control through our ownership of the majority of the voting shares. Joint ventures are those where we exercise joint control through an agreement with other shareholders. All of the assets, liabilities, revenues and expenses of our subsidiaries and our proportionate share of the assets, liabilities, revenues and expenses of our joint ventures are included in our consolidated financial statements. All significant inter-company transactions and balances are eliminated.

We hold investments in companies where we exert significant influence over operating, investing and financing decisions (those where we own between 20% and 50% of the voting shares). These are recorded at cost and are adjusted for our proportionate share of any net income or loss and dividends. They are recorded as investment securities in our Consolidated Balance Sheet and our proportionate share of the net income or loss of these companies is recorded in interest, dividend and fee income – securities, in our Consolidated Statement of Income.

We hold interests in variable interest entities that are not included in our consolidated financial statements; these are more fully described in Note 8.

### Translation of Foreign Currencies

We conduct business in a variety of foreign currencies and report our consolidated financial statements in Canadian dollars. Assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the exchange rate in effect at the balance sheet date. Revenues and expenses denominated in foreign currencies are translated using the average exchange rate for the year.

Unrealized gains and losses arising from translating net investments in foreign operations into Canadian dollars, net of related hedging activities and applicable income taxes, are included in shareholders’ equity as net unrealized foreign exchange gain (loss). When we sell or liquidate an investment in a foreign operation, the associated translation gains and losses, previously included in shareholders’ equity as net unrealized foreign exchange gain (loss), are recorded in non-interest revenue as part of the gain or loss on disposal of the investment. All other foreign currency translation gains and losses are included in foreign exchange, other than trading, in our Consolidated Statement of Income as they arise.

From time to time, we enter into foreign exchange hedge contracts to reduce our exposure to changes in the value of foreign currencies. Realized and unrealized gains and losses on the translation of foreign exchange hedge contracts are included in foreign exchange, other than trading, in our Consolidated Statement of Income.

### Specific Accounting Policies

To facilitate a better understanding of our consolidated financial statements, we have disclosed our significant accounting policies throughout the following notes with the related financial disclosures by major caption:

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### Changes in Accounting Policy

Changes in accounting policy that resulted from changes by Canadian standard setters in the current year are disclosed as follows: Merchant banking investments – Note 3; variable interest entities – Note 8; and liabilities and equity – Notes 18 and 20. United States GAAP changes are described in Note 29. Changes in accounting policy in the two previous years are as follows:

#### Sources of GAAP

Effective November 1, 2003, we adopted new accounting requirements of the Canadian Institute of Chartered Accountants (“CICA”) that provide guidance on sources to consult when selecting accounting policies on matters not covered explicitly in Canadian accounting standards. As a result of these new requirements, we made the following changes to our accounting policies effective November 1, 2003:

#### (a) Mortgage Prepayment Fees

Mortgage prepayment fees are recognized in income when the related mortgages are prepaid or renegotiated at market rates. Prior to November 1, 2003, mortgage prepayment fees were deferred and amortized to income over the average remaining term of the related mortgages. In adopting this new policy we recorded in income an initial adjustment related to the balance of deferred mortgage prepayment fees as at November 1, 2003 of \$42 million before income taxes.

#### (b) Treasury Shares

Purchases and sales of Bank of Montreal shares by subsidiaries are recorded in shareholders’ equity, with any gain included in contributed surplus. Prior to November 1, 2003, these shares were recorded as trading securities at market value, with related dividends and realized and unrealized gains and losses included in trading revenues.

### (c) Software Development Costs

Costs of internally developed software are capitalized and amortized over the estimated useful life of the software (up to five years). Prior to November 1, 2003, only amounts paid to third parties related to internally developed software were capitalized and amortized over the estimated useful life of the software.

### (d) Preferred Shares

We are no longer changing the rate at which our U.S. dollar denominated preferred shares are translated into Canadian dollars. Prior to November 1, 2003, we adjusted the carrying value of these shares in shareholders' equity to reflect changes in the exchange rate.

The impact of these changes in accounting policy on our Consolidated Statement of Income for 2004 as compared to the policies followed in 2003 was as follows:

(Canadian \$ in millions, except as noted)  
For the Year Ended October 31, 2004

Increase (Decrease) to Income Before Provision for Income Taxes	
Interest, Dividend and Fee Income – Loans (a)	\$ 48
Non-Interest Revenue – Trading revenues (b)	(26)
Non-Interest Expense – Employee compensation (c)	51
Non-Interest Expense – Premises and equipment (c)	(4)
Non-Interest Revenue – Foreign exchange, other than trading (d)	3
Income Before Provision for Income Taxes	72
Income taxes	(25)
Net Income	\$ 47
Earnings Per Share (Canadian \$)	
Basic	\$ 0.09
Diluted	0.09

## Note 2 ▶ Cash Resources

(Canadian \$ in millions)	2005	2004
Cash and non-interest bearing deposits		
with Bank of Canada and other banks	\$ 1,309	\$ 1,558
Interest bearing deposits with banks	18,309	15,439
Cheques and other items in transit, net	1,103	1,048
Total	\$ 20,721	\$ 18,045

### Deposits with Banks

Deposits with banks are recorded at cost and include acceptances we have purchased that were issued by other banks. Interest income earned on these deposits is recorded on an accrual basis.

## Note 3 ▶ Securities

Securities are divided into four types, each with a different purpose and accounting treatment. The four types of securities we hold are as follows:

**Investment securities** are comprised of equity and debt securities that we purchase with the intention of holding until maturity or until market conditions, such as a change in interest rates, provide us with a better investment opportunity. With the exception of merchant banking investments, equity securities are recorded at cost and debt securities at amortized cost, after any write-down for impairment. Gains and losses on disposal are calculated using the carrying amount of the securities sold.

Interest income earned, the amortization of premiums and discounts on debt securities and dividends received on equity securities are recorded in our Consolidated Statement of Income in interest, dividend and fee income.

### Future Changes in Accounting Policy

The CICA has issued new accounting requirements for financial instruments, hedges and other comprehensive income. When we adopt the new requirements on November 1, 2006, we will report a new section of shareholders' equity called other comprehensive income. The new section will include gains and losses related to the mark-to-market of investment securities and cash flow hedges as well as the net unrealized foreign exchange gain that is currently included in shareholders' equity. The change in accounting policy as it relates to investment securities and derivatives is described in Notes 3 and 9, respectively. There will be no change in accounting policy for unrealized foreign exchange gains in shareholders' equity.

The impact of remeasuring certain investment securities and derivative financial instruments at fair value on November 1, 2006 will be recognized in opening retained earnings. Results for prior periods will not be restated. We cannot currently determine the impact that these changes in accounting policy will have on our consolidated financial statements once adopted, as this will be dependent on the fair values of the related financial instruments in the future.

See Note 24 for a discussion of the new accounting rules regarding earnings per share.

### Use of Estimates

In preparing our consolidated financial statements we must make estimates and assumptions, mainly concerning fair values, which affect reported amounts of assets, liabilities, net income and related disclosures. The most significant assets and liabilities where we must make estimates include measurement of other than temporary impairment – Note 3; allowance for credit losses – Note 4; accounting for securitizations – Note 7; financial instruments measured at fair value – Note 9; goodwill – Note 13; customer loyalty programs – Note 16; pension and other employee future benefits – Note 22; income taxes – Note 23; and contingent liabilities – Note 27. If actual results differ from the estimates, the impact would be recorded in future periods.

### Cheques and Other Items in Transit, Net

Cheques and other items in transit are recorded at cost and represent the net position of the uncleared cheques and other items in transit between us and other banks.

### Cash Restrictions

Some of our foreign operations are required to maintain reserves or minimum balances with central banks in their respective countries of operation, amounting to \$449 million as at October 31, 2005 (\$494 million in 2004).

Investment securities are reviewed at each quarter end to determine whether the fair value is below carrying value. When the fair value of any of our investment securities has declined below its carrying value, we assess whether the decline is other than temporary.

Impairment is evaluated taking into consideration a number of factors, and their relative significance varies from case to case. Factors considered include the length of time and extent to which fair value has been below carrying value, the financial condition and near-term prospects of the issuer, and our ability and intent to hold the investment for a period of time sufficient to allow for any anticipated recovery. If the decline is considered to be other than temporary, a write-down is recorded in our Consolidated Statement of Income in investment securities gains (losses).

At October 31, 2005, we had total investments with a book value of \$7,903 million (\$8,612 million as at October 31, 2004) where fair value was below book value by \$55 million (\$43 million as at October 31, 2004). The majority of unrealized losses in our investment portfolio resulted from increases in market interest rates and not from deterioration in the creditworthiness of the issuers. Management has determined that the unrealized losses are temporary in nature.

**Merchant banking investments** are securities held by our merchant banking subsidiaries. These subsidiaries account for their investments at fair value, with changes in fair value recorded in our Consolidated Statement of Income in investment securities gains (losses) as they occur. See change in accounting policy.

Merchant banking investments are classified as investment securities in our Consolidated Balance Sheet.

**Trading securities** are securities that we purchase for resale over a short period of time. We report these securities at their market value and record the mark-to-market adjustments and any gains and losses on the sale of these securities in our Consolidated Statement of Income in trading revenues.

**Loan substitute securities** are customer financings, such as distressed preferred shares, that we structure as after-tax investments to provide our customers with an interest rate advantage over what would be applicable on a conventional loan. These securities are accounted for in accordance with our accounting policy for loans, which is described in Note 4.

We did not own any securities issued by a single non-government entity where the book value, as at October 31, 2005 or 2004, was greater than 10% of our shareholders' equity.

Included in corporate equity are investments where we exert significant influence, but not control, of \$966 million and \$546 million as at October 31, 2005 and 2004, respectively.

#### Fair Value

For traded securities, quoted market value is considered to be fair value. For securities where market quotes are not available, we use estimation techniques to determine fair value. Estimation techniques used include discounted cash flows, multiples of earnings or comparisons with other securities that are substantially the same.

#### Change in Accounting Policy

On November 1, 2004, we adopted the CICA's new accounting requirements applicable to our merchant banking subsidiaries. The new rules require these subsidiaries to account for their investments at fair value with changes in fair value recorded in net income. Previously, these subsidiaries accounted for their investments at cost. The difference between cost and fair value has been recognized in the current period. The impact on our Consolidated Statement of Income, including the initial adjustment to fair value on November 1, 2004, was an increase of \$50 million in non-interest revenue – investment securities gains (losses), an increase in income taxes of \$18 million and an increase in net income of \$32 million for the year ended October 31, 2005. The impact on our Consolidated Balance Sheet was an increase of \$50 million in investment securities as at October 31, 2005.

(Canadian \$ in millions, except as noted)

	Term to maturity										2005		2004	
	Within 1 year		1 to 3 years		3 to 5 years		5 to 10 years		Over 10 years		Total book value	Yield	Total book value	
<b>Investment Securities</b>														
Issued or guaranteed by:		Yield %		Yield %		Yield %		Yield %		Yield %		Yield %		
Canadian federal government	\$ 18	3.04	\$ –	–	\$ –	–	\$ –	–	\$ 1	4.39	\$ 19	3.11	\$ 211	
Canadian provincial and municipal governments	2	3.30	–	–	–	–	–	–	1	4.97	3	3.86	–	
U.S. federal government	775	2.52	661	3.65	29	3.24	–	–	–	–	1,465	3.04	3,066	
U.S. states, municipalities and agencies	2,245	2.70	2,959	3.84	772	2.09	11	3.70	56	4.96	6,043	3.20	5,191	
Other governments	46	3.80	36	3.66	40	4.55	1	4.24	–	–	123	4.01	315	
Mortgage-backed securities and collateralized mortgage obligations	–	–	1	3.20	167	3.91	303	4.15	215	4.58	686	4.22	1,365	
Corporate debt	1,364	2.95	603	4.29	205	2.05	43	4.51	86	0.28	2,301	3.15	2,885	
Corporate equity	121	5.49	213	5.47	199	5.55	158	4.75	1,605	0.66	2,296	2.07	1,984	
<b>Total investment securities</b>	<b>4,571</b>	<b>2.83</b>	<b>4,473</b>	<b>3.95</b>	<b>1,412</b>	<b>2.88</b>	<b>516</b>	<b>4.35</b>	<b>1,964</b>	<b>1.20</b>	<b>12,936</b>	<b>3.04</b>	<b>15,017</b>	
<b>Trading Securities</b>														
Issued or guaranteed by:														
Canadian federal government	3,178		1,518		1,971		1,012		1,900		9,579		6,170	
Canadian provincial and municipal governments	425		267		145		539		1,177		2,553		2,288	
U.S. federal government	57		559		127		32		301		1,076		910	
U.S. states, municipalities and agencies	–		–		–		–		152		152		97	
Other governments	–		–		–		23		–		23		11	
Corporate debt	1,670		1,441		1,289		1,252		8,718		14,370		9,518	
Corporate equity	–		–		–		1		16,555		16,556		16,450	
<b>Total trading securities</b>	<b>5,330</b>		<b>3,785</b>		<b>3,532</b>		<b>2,859</b>		<b>28,803</b>		<b>44,309</b>		<b>35,444</b>	
<b>Loan Substitute Securities</b>	–		11		–		–		–		11		11	
<b>Total securities</b>	<b>\$ 9,901</b>		<b>\$ 8,269</b>		<b>\$ 4,944</b>		<b>\$ 3,375</b>		<b>\$ 30,767</b>		<b>\$ 57,256</b>		<b>\$ 50,472</b>	
<b>Total by Currency</b> (in Canadian \$ equivalent)														
Canadian dollar	4,843		2,916		3,087		2,050		16,050		28,946		26,006	
U.S. dollar	4,439		4,929		1,713		1,171		14,643		26,895		22,536	
Other currencies	619		424		144		154		74		1,415		1,930	
<b>Total securities</b>	<b>\$ 9,901</b>		<b>\$ 8,269</b>		<b>\$ 4,944</b>		<b>\$ 3,375</b>		<b>\$ 30,767</b>		<b>\$ 57,256</b>		<b>\$ 50,472</b>	

Yields in the table above are calculated using the book value of the security and the contractual interest or stated dividend rates associated with each security adjusted for any amortization of premiums and discounts. Tax effects are not taken into consideration.

The term to maturity included in the table above is based on the contractual maturity date of the security. The term to maturity of mortgage-backed securities and collateralized mortgage obligations is based on average expected maturities. Actual maturities could differ as issuers may have the right to call or prepay obligations. Securities with no maturity date are included in the over 10 years category.

### Future Change in Accounting Policy

As discussed in Note 1, we will adopt the CICA's new accounting requirements that will impact our accounting policy for investment securities other than merchant banking investments beginning November 1, 2006. The new rules will require us to classify these securities as held-to-maturity or available-for-sale. Available-for-sale securities will be measured at fair value with gains and losses recorded in a new section of shareholders' equity called other comprehensive income. There will be no change in accounting for held-to-maturity securities.

The impact of remeasuring available-for-sale securities at fair value on November 1, 2006 will be recognized in opening retained earnings. Results for prior periods will not be restated. We cannot currently determine the impact that this change in accounting policy will have on our consolidated financial statements once adopted, as this will be dependent on the fair values of our available-for-sale securities in the future.

### Unrealized Gains and Losses

(Canadian \$ in millions)

	2005				2004			
	Book value	Gross unrealized gains	Gross unrealized losses	Fair value	Book value	Gross unrealized gains	Gross unrealized losses	Fair value
<b>Investment Securities</b>								
Issued or guaranteed by:								
Canadian federal government	\$ 19	\$ -	\$ -	\$ 19	\$ 211	\$ -	\$ -	\$ 211
Canadian provincial and municipal governments	3	-	-	3	-	-	-	-
U.S. federal government	1,465	1	7	1,459	3,066	2	10	3,058
U.S. states, municipalities and agencies	6,043	13	30	6,026	5,191	21	13	5,199
Other governments	123	2	1	124	315	2	1	316
Mortgage-backed securities and collateralized mortgage obligations	686	3	10	679	1,365	8	4	1,369
Corporate debt	2,301	11	5	2,307	2,885	32	11	2,906
Corporate equity	2,296	22	2	2,316	1,984	64	4	2,044
<b>Total</b>	<b>\$ 12,936</b>	<b>\$ 52</b>	<b>\$ 55</b>	<b>\$ 12,933</b>	<b>\$ 15,017</b>	<b>\$ 129</b>	<b>\$ 43</b>	<b>\$ 15,103</b>

### Unrealized Losses

(Canadian \$ in millions)

	Investments in an unrealized loss position for 2005				Investments in an unrealized loss position for 2004			
	Less than 12 months	12 months or longer	Total		Less than 12 months	12 months or longer	Total	
	Gross unrealized losses	Gross unrealized losses	Gross unrealized losses	Fair value	Gross unrealized losses	Gross unrealized losses	Gross unrealized losses	Fair value
<b>Investment Securities</b>								
Issued or guaranteed by:								
Canadian federal government	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 25
U.S. federal government	5	2	7	1,334	8	2	10	2,527
U.S. states, municipalities and agencies	25	5	30	4,992	8	5	13	3,588
Other governments	-	-	-	30	1	-	1	177
Mortgage-backed securities and collateralized mortgage obligations	10	-	10	535	4	-	4	685
Corporate debt	5	-	5	847	9	2	11	1,506
Corporate equity	2	1	3	110	4	-	4	61
<b>Total</b>	<b>\$ 47</b>	<b>\$ 8</b>	<b>\$ 55</b>	<b>\$ 7,848</b>	<b>\$ 34</b>	<b>\$ 9</b>	<b>\$ 43</b>	<b>\$ 8,569</b>

Income from securities is included in our Consolidated Statement of Income as follows:

(Canadian \$ in millions)

	2005	2004	2003
<b>Reported in:</b>			
<b>Interest, Dividend and Fee Income</b>			
Investment securities	\$ 490	\$ 595	\$ 858
Trading securities	1,340	881	743
	<b>\$ 1,830</b>	<b>\$ 1,476</b>	<b>\$ 1,601</b>
<b>Non-Interest Revenue</b>			
Investment securities			
Gross realized gains	\$ 142	\$ 242	\$ 142
Gross realized losses	(16)	(4)	(30)
Merchant banking securities – net unrealized gains	50	-	-
Write-downs	(11)	(63)	(153)
Investment securities gains (losses)	<b>\$ 165</b>	<b>\$ 175</b>	<b>\$ (41)</b>
Trading securities, net realized and unrealized gains	<b>\$ 222</b>	<b>\$ 60</b>	<b>\$ 65</b>
<b>Total income from securities</b>	<b>\$ 2,217</b>	<b>\$ 1,711</b>	<b>\$ 1,625</b>

## Note 4 ▶ Loans, Customers' Liability under Acceptances and Allowance for Credit Losses

### Loans

Loans are recorded at cost net of unearned income and unamortized discounts. Unearned income includes prepaid interest and deferred loan fees. Interest income is recorded on an accrual basis, except for impaired loans, the treatment of which is described below.

Securities borrowed or purchased under resale agreements represent the amounts we will receive as a result of our commitment to resell securities that we have purchased back to the original seller, on a specified date at a specified price. We account for these instruments as loans.

### Loan Fees

The accounting treatment for loan fees varies depending on the transaction. Loan origination, restructuring and renegotiation fees are recorded as interest income over the term of the loan. Commitment fees are recorded as interest income over the term of the loan, unless we believe the loan commitment will not be used. In the latter case, commitment fees are recorded as lending fees over the commitment period. Loan syndication fees are included in lending fees as the syndication is completed, unless the yield on any loans we retain is less than that of other comparable lenders involved in the financing. In the latter case, an appropriate portion of the syndication fee is deferred and amortized to interest income over the term of the loan.

### Customers' Liability under Acceptances

Acceptances represent a form of negotiable short-term debt that is issued by our customers and which we guarantee for a fee. We have offsetting claims, equal to the amount of the acceptances, against our customers when the instruments mature. The amount due under acceptances is recorded as a liability and our corresponding claim is recorded as a loan in our Consolidated Balance Sheet.

### Impaired Loans

We classify residential mortgages as impaired when payment is contractually 90 days past due, or one year past due if guaranteed by the Government of Canada. Credit card loans are classified as impaired and immediately written off when principal or interest payments are 180 days past due. Consumer instalment and other personal loans are classified as impaired when principal or interest payments are 90 days past due, and are normally written off when they are one year past due.

Corporate and commercial loans are classified as impaired when we are no longer reasonably assured that principal or interest will be collected on a timely basis, or when payments are 90 days past due, or for fully secured loans, when payments are 180 days past due.

We do not recognize interest income on loans classified as impaired, and any interest income that is accrued and unpaid is reversed against interest income.

Payments received on loans that have been classified as impaired are recorded first to recover collection costs, principal and any previous write-offs or allowances, and then as interest income. Payments received on impaired consumer instalment loans are applied first to outstanding interest and then to the remaining principal.

A loan will be reclassified back to performing status when it is determined that there is reasonable assurance of full and timely repayment of interest and principal in accordance with the terms and conditions of the loan, and that none of the criteria for classification of the loan as impaired continue to apply.

From time to time we will restructure a loan due to the poor financial condition of the borrower. If no longer considered impaired, interest on these restructured loans is recorded on an accrual basis.

### Allowance for Credit Losses

The allowance for credit losses recorded in our Consolidated Balance Sheet is maintained at a level which we consider adequate to absorb credit-related losses on our loans, customers' liability under acceptances and other credit instruments (as discussed in Note 5). The portion related to other credit instruments is recorded in other liabilities in our Consolidated Balance Sheet.

The allowance comprises the following two components:

#### *Specific Allowances*

These allowances are recorded for specific loans to reduce their book value to the amount we expect to recover. We review our loans and acceptances, other than consumer instalment and credit card loans (which are written off when certain conditions exist, as discussed under impaired loans), on an ongoing basis to assess whether any loans should be classified as impaired and whether an allowance or write-off should be recorded. Our review of problem loans is conducted at least quarterly by our account managers, who assess the ultimate collectibility and estimated recoveries on a specific loan based on all events and conditions that the manager believes are relevant to the condition of the loan. This assessment is then reviewed and concurred with by an independent credit officer.

To determine the amount we expect to recover from an impaired loan, we use the value of the estimated future cash flows discounted at the effective rate inherent in the loan. When the amounts and timing of future cash flows cannot be estimated with reasonable reliability, the expected recovery amount is estimated using either the fair value of any security underlying the loan, net of expected costs of realization and any amounts legally required to be paid to the borrower, or an observable market price for the loan. Security can vary by type of loan and may include cash, securities, real property, accounts receivable, guarantees, inventory or other capital assets.

#### *General Allowance*

We maintain a general allowance in order to cover any impairment in the existing portfolio that cannot yet be associated with specific loans. Our approach to establishing and maintaining the general allowance is based on the guideline issued by our regulator, the Superintendent of Financial Institutions Canada.

The general allowance is reviewed on a quarterly basis.

A number of factors are considered when determining the appropriate level of the general allowance. A statistical analysis of past performance is undertaken to derive the mean (Expected Loss) and volatility (Unexpected Loss) of loss experience.

This analysis calculates historical average losses for each homogeneous portfolio segment (e.g., mortgages), while other models estimate losses for portfolios of corporate loans that can be referenced to market data. In addition, the level of allowance already in place and management's professional judgment regarding portfolio quality, business mix and economic as well as credit market conditions are also considered.

### Provision for Credit Losses

Changes in the value of our loan portfolio due to credit-related losses or recoveries of amounts previously provided for or written off are included in the provision for credit losses in our Consolidated Statement of Income.

### Foreclosed Assets

Property or other assets that we have received from borrowers to satisfy their loan commitments are recorded at fair value and are classified as either held for use or held for sale according to management's intention. Fair value is determined based on market prices where available. Otherwise, fair value is determined using other methods, such as analysis of discounted cash flows or market prices for similar assets.

Loans, including customers' liability under acceptances and allowance for credit losses by category, are as follows:

(Canadian \$ in millions)	Gross amount		Specific allowance		General allowance		Net amount	
	2005	2004	2005	2004	2005	2004	2005	2004
Residential mortgages	\$ 60,871	\$ 56,444	\$ 5	\$ 5	\$ 15	\$ 13	\$ 60,851	\$ 56,426
Credit card, consumer instalment and other personal loans	32,577	28,589	1	2	444	360	32,132	28,227
Business and government loans	47,803	44,559	163	291	473	595	47,167	43,673
Securities borrowed or purchased under resale agreements	28,280	22,609	—	—	—	—	28,280	22,609
Subtotal	169,531	152,201	169	298	932	968	168,430	150,935
Customers' liability under acceptances	5,934	5,355	—	—	27	42	5,907	5,313
Total	\$ 175,465	\$ 157,556	\$ 169	\$ 298	\$ 959	\$ 1,010	\$ 174,337	\$ 156,248
By geographic region (1):								
Canada	\$ 128,184	\$ 116,867	\$ 97	\$ 132	\$ 590	\$ 630	\$ 127,497	\$ 116,105
United States	45,287	38,934	66	134	369	380	44,852	38,420
Other countries	1,994	1,755	6	32	—	—	1,988	1,723
Total	\$ 175,465	\$ 157,556	\$ 169	\$ 298	\$ 959	\$ 1,010	\$ 174,337	\$ 156,248

(1) Geographic region is based upon the country of ultimate risk.

Loans are presented net of unearned income of \$158 million and \$45 million as at October 31, 2005 and 2004, respectively.

Restructured loans of \$2 million were classified as performing during the year ended October 31, 2005 (\$23 million in 2004). No restructured loans were written off in the years ended October 31, 2005 and 2004.

Included in loans as at October 31, 2005 are \$47,828 million (\$41,571 million in 2004) of loans denominated in U.S. dollars and \$265 million (\$312 million in 2004) of loans denominated in other foreign currencies.

Impaired loans, including customers' liability under acceptances and the related allowances, are as follows:

(Canadian \$ in millions)	Gross impaired amount		Specific allowance		Net of specific allowance	
	2005	2004	2005	2004	2005	2004
Residential mortgages	\$ 92	\$ 125	\$ 5	\$ 5	\$ 87	\$ 120
Consumer instalment and other personal loans	39	37	1	2	38	35
Business and government loans	673	957	163	291	510	666
Total	\$ 804	\$ 1,119	\$ 169	\$ 298	\$ 635	\$ 821
By geographic region (1):						
Canada	\$ 383	\$ 465	\$ 97	\$ 132	\$ 286	\$ 333
United States	397	560	66	134	331	426
Other countries	24	94	6	32	18	62
Total	\$ 804	\$ 1,119	\$ 169	\$ 298	\$ 635	\$ 821

(1) Geographic region is based upon the country of ultimate risk.

Fully secured loans with past due amounts between 90 and 180 days that we have not classified as impaired totalled \$51 million and \$95 million as at October 31, 2005 and 2004, respectively.

No impaired loans were foreclosed during the year ended October 31, 2005. Impaired loans foreclosed during the year ended October 31, 2004 totalled \$20 million, which resulted in the reversal of \$4 million of the allowance for credit losses.

Our average gross impaired loans and acceptances were \$1,011 million for the year ended October 31, 2005 (\$1,530 million in 2004). Our average impaired loans, net of the specific allowance, were \$738 million for the year ended October 31, 2005 (\$1,002 million in 2004).

During the years ended October 31, 2005, 2004 and 2003, we would have recorded additional interest income of \$65 million, \$68 million and \$78 million, respectively, if we had not classified any loans as impaired. Cash interest income on impaired loans of \$nil, \$1 million and \$8 million was recognized during the years ended October 31, 2005, 2004 and 2003, respectively.

### Concentration of Credit Risk

We are exposed to credit risk from the possibility that counterparties may default on their financial obligations to us. Credit risk arises predominantly with respect to loans, over-the-counter derivatives and other credit instruments.

Concentrations of credit risk exist if a number of clients are engaged in similar activities, are located in the same geographic region or have similar economic characteristics such that their ability to meet contractual obligations could be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate a related sensitivity of our performance to developments affecting a particular counterparty, industry or geographic location.

Information about our credit risk exposure is provided above in the classification of our loan assets both by type of loan and by geographic region.

A continuity of our allowance for credit losses is as follows:

(Canadian \$ in millions)	Specific allowance			General allowance			Total		
	2005	2004	2003	2005	2004	2003	2005	2004	2003
Balance at beginning of year	\$ 298	\$ 611	\$ 769	\$ 1,010	\$ 1,180	\$ 1,180	\$ 1,308	\$ 1,791	\$ 1,949
Provision for credit losses	219	67	455	(40)	(170)	–	179	(103)	455
Recoveries	67	131	88	–	–	–	67	131	88
Write-offs	(419)	(470)	(566)	–	–	–	(419)	(470)	(566)
Foreign exchange and other	4	(41)	(135)	(11)	–	–	(7)	(41)	(135)
Balance at end of year	\$ 169	\$ 298	\$ 611	\$ 959	\$ 1,010	\$ 1,180	\$ 1,128	\$ 1,308	\$ 1,791
Comprised of: Loans	\$ 169	\$ 298	\$ 605	\$ 959	\$ 1,010	\$ 1,180	\$ 1,128	\$ 1,308	\$ 1,785
Other credit instruments	–	–	6	–	–	–	–	–	6

## Note 5 ▶ Other Credit Instruments

We use other off-balance sheet credit instruments as a method of meeting the financial needs of our customers. Summarized below are the types of instruments that we use:

- Standby letters of credit and guarantees represent our obligation to make payments to third parties on behalf of our customers if our customers are unable to make the required payments or meet other contractual requirements;
- Securities lending represents our credit exposure when we lend our securities, or our customers' securities, to third parties should the securities borrower default on its redelivery obligation;
- Documentary and commercial letters of credit represent our agreement to honour drafts presented by a third party upon completion of specific activities; and
- Commitments to extend credit represent our commitment to our customers to grant them credit in the form of loans or other financings for specific amounts and maturities, subject to meeting certain conditions.

The contractual amount of our other credit instruments represents the maximum undiscounted potential credit risk if the counterparty does not perform according to the terms of the contract, before possible recoveries under recourse and collateral provisions. Collateral requirements for these instruments are consistent with collateral requirements for loans. A large majority of these commitments expire without being drawn upon. As a result, the total contractual amounts may not be representative of our likely credit exposure or liquidity requirements for these commitments.

The risk-weighted equivalent values of our other credit instruments are determined based on the rules for capital adequacy of the Superintendent of Financial Institutions Canada. The risk-weighted equivalent value is used in the ongoing assessment of our capital adequacy ratios.

Summarized information related to various commitments is as follows:

(Canadian \$ in millions)	2005		2004	
	Contract amount	Risk-weighted equivalent	Contract amount	Risk-weighted equivalent
<b>Credit Instruments</b>				
Standby letters of credit and guarantees	\$ 12,755	\$ 8,695	\$ 13,042	\$ 9,379
Securities lending	810	51	548	20
Documentary and commercial letters of credit	974	87	706	75
Commitments to extend credit – Original maturity of one year and under	70,695	–	66,826	–
– Original maturity of over one year	24,411	11,909	18,830	9,103
Total	\$ 109,645	\$ 20,742	\$ 99,952	\$ 18,577

Commitments to extend credit in respect of consumer instalment and credit card loans are excluded as the lines are revocable at our discretion.

## Note 6 ▶ Guarantees

Guarantees include contracts where we may be required to make payments to a counterparty based on changes in the value of an asset, liability or equity security that the counterparty holds. In addition, contracts under which we may be required to make payments if a third party fails to perform under the terms of a contract and contracts under which we provide indirect guarantees of the indebtedness of another party are considered guarantees.

In the normal course of business we enter into a variety of guarantees, the most significant of which are as follows:

### Standby Letters of Credit and Guarantees

Standby letters of credit and guarantees, as discussed in Note 5, are considered guarantees. The maximum amount payable under standby letters of credit and guarantees was \$12,755 million as at October 31, 2005 (\$13,042 million in 2004). Collateral requirements for standby letters of credit and guarantees are consistent with our collateral requirements for loans. In most cases, these commitments expire within three years without being drawn upon.

No amount was included in our Consolidated Balance Sheet as at October 31, 2005 and 2004 related to these standby letters of credit and guarantees.

### Backstop Liquidity Facilities

Commitments to extend credit, as discussed in Note 5, include backstop liquidity facilities. Backstop liquidity facilities are provided to asset-backed commercial paper programs administered by either us or third parties as an alternative source of financing in the event that such programs are unable to access commercial paper markets or, in limited circumstances, when predetermined performance measures of the financial assets owned by these programs are not met. The terms of the backstop liquidity facilities do not require us to advance money to these programs in the event of bankruptcy. Where warranted, we provide partial credit enhancement facilities to transactions within asset-backed commercial paper programs administered by us to ensure a high investment grade credit rating is achieved for notes issued by the programs. The maximum potential payments under these backstop liquidity facilities were \$38,491 million as at October 31, 2005 (\$36,769 million in 2004). Of these amounts \$3,331 million as at October 31, 2005 related to credit enhancement facilities (\$1,503 million in 2004). Credit enhancement was also provided in the form of program letters of credit; \$192 million and \$199 million were included in standby letters of credit and guarantees as at October 31, 2005 and 2004, respectively. The facilities' terms are generally no longer than one year, but can be several years. None of the backstop liquidity facilities or credit enhancement facilities that we have provided have been drawn upon.

No amount was included in our Consolidated Balance Sheet as at October 31, 2005 and 2004 related to these facilities.

### Derivatives

Certain of our derivative instruments meet the accounting definition of a guarantee when we believe they are related to an asset, liability or equity security held by the guaranteed party at the inception of a contract.

Written credit default swaps require us to compensate a counterparty following the occurrence of a credit event in relation to a specified reference obligation, such as a bond or a loan. The maximum amount payable under credit default swaps was equal to their notional amount of \$17,940 million as at October 31, 2005 (\$11,360 million in 2004). The terms of these contracts range from three months to 10 years. The fair value of the related derivative liabilities included in derivative financial instruments in our Consolidated Balance Sheet was \$37 million as at October 31, 2005 (\$15 million in 2004).

## Note 7 ▶ Asset Securitization

Periodically, we securitize loans for capital management purposes or to obtain alternate sources of funding. Securitization involves selling loans to off-balance sheet entities or trusts (securitization vehicles), which buy the loans and then issue interest bearing investor certificates.

Contracts with the securitization vehicles provide for the payment to us over time of the excess of the sum of interest and fees collected from customers, in connection with the loans that were sold, over the yield paid to investors in the securitization vehicle, less credit losses and other costs (the "deferred purchase price").

When the loans are considered sold for accounting purposes, we remove them from our Consolidated Balance Sheet.

We account for transfers to securitization vehicles as sales when control over the loans is given up. We recognize securitization revenues at the time of the sale, based on our best estimate of the net present value of expected future cash flows, primarily the deferred purchase price, net of our estimate of the fair value of any servicing obligations undertaken. The deferred purchase price is recorded in our Consolidated Balance Sheet in other assets. A servicing liability is recognized only for securitizations where we do not receive compensation for servicing the transferred loans.

Written options include contractual agreements that convey to the purchaser the right, but not the obligation, to require us to buy a specific amount of a currency, commodity or equity at a fixed price, either at a fixed future date or at any time within a fixed future period. The maximum amount payable under these written options cannot be reasonably estimated due to the nature of these contracts. The terms of these contracts range from one month to eight years. The fair value of the related derivative liabilities included in derivative financial instruments in our Consolidated Balance Sheet was \$606 million as at October 31, 2005 (\$118 million in 2004).

Written options also include contractual agreements where we agree to pay the purchaser, based on a specified notional amount, the difference between the market interest rate and the strike price of the instrument. The maximum amount payable under these contracts is not determinable due to their nature. The terms of these contracts range from one month to 25 years. The fair value of the related derivative liabilities included in derivative financial instruments in our Consolidated Balance Sheet was \$158 million as at October 31, 2005 (\$63 million in 2004).

In order to reduce our exposure to these derivatives, we enter into contracts that hedge the related risks.

### Indemnification Agreements

In the normal course of operations, we enter into various agreements that provide general indemnifications. These indemnifications typically occur in connection with sales of assets, securities offerings, service contracts, membership agreements, clearing arrangements and leasing transactions. These indemnifications require us, in certain circumstances, to compensate the counterparties for various costs resulting from breaches of representations or obligations under such arrangements, or as a result of third-party claims that may be suffered by the counterparty as a consequence of the transaction. The terms of these indemnifications vary based on the contract, the nature of which prevents us from making a reasonable estimate of the maximum potential amount we could be required to pay to counterparties. We believe that the likelihood that we could incur significant liability under these obligations is remote. Historically, we have not made any significant payments under such indemnifications.

No material amount was included in our Consolidated Balance Sheet as at October 31, 2005 and 2004 related to these indemnifications.

It is recorded in our Consolidated Balance Sheet in other liabilities. A servicing liability is recorded in securitization revenues over the term of the transferred loan.

For some of our securitizations, we are required to purchase subordinated interests or maintain cash amounts deposited with the securitization vehicle. This provides the securitization vehicle with a source of funds in the event that the sum of interest and fees collected on the loans is not sufficient to pay the interest owed to investors. We record these amounts in other assets in our Consolidated Balance Sheet. These interests, together with our deferred purchase price, represent our exposure with respect to these securitizations. Investors have no further recourse against us in the event that cash flows from the transferred loans are inadequate to service the interest related to the investor certificates.

On a quarterly basis, we compare the carrying value of assets on our Consolidated Balance Sheet arising from our securitizations to their fair value, determined based on discounted cash flows. When we identify a decline in value, the affected carrying value amount is written down to its fair value. Any write-down is recorded in our Consolidated Statement of Income as a reduction in securitization revenues.

During the year ended October 31, 2005, we securitized residential mortgages totalling \$3,137 million (\$1,390 million in 2004) for total cash proceeds of \$3,130 million (\$1,382 million in 2004) and recognized a gain of \$30 million (\$17 million in 2004). The key weighted-average assumptions used to value the deferred purchase price for these securitizations were as follows:

	2005	2004
Weighted-average term (years)	4.7	4.7
Prepayment rate	10.97%	11.26%
Interest rate	4.76%	4.29%
Discount rate	3.41%	5.79%

There are no expected credit losses as the mortgages are guaranteed by third parties. We retained responsibility for servicing these mortgages. We recorded deferred purchase price of \$123 million (\$49 million in 2004) and servicing liability of \$24 million (\$11 million in 2004) in our Consolidated Balance Sheet when these loans were securitized.

During the year ended October 31, 2005, \$800 million (\$400 million in 2004) of our credit card loan securitizations matured.

The impact of securitizations on our Consolidated Statement of Income for the three years ended October 31 was as follows:

(Canadian \$ in millions)	Residential mortgages			Consumer instalment and other personal loans			Credit card loans			Total		
	2005	2004	2003	2005	2004	2003	2005	2004	2003	2005	2004	2003
Gain on sales of loans from new securitizations	\$ 30	\$ 17	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 30	\$ 17	\$ -
Gain on sales of new loans sold to existing securitization vehicles	32	37	39	-	1	1	20	72	117	52	110	157
Other securitization revenue	3	8	14	4	(2)	20	1	28	43	8	34	77
Amortization of servicing liability	23	16	10	-	-	-	-	-	-	23	16	10
<b>Total</b>	<b>\$ 88</b>	<b>\$ 78</b>	<b>\$ 63</b>	<b>\$ 4</b>	<b>\$ (1)</b>	<b>\$ 21</b>	<b>\$ 21</b>	<b>\$ 100</b>	<b>\$ 160</b>	<b>\$ 113</b>	<b>\$ 177</b>	<b>\$ 244</b>

Cash flows received from securitization vehicles for the three years ended October 31 were as follows:

(Canadian \$ in millions)	Residential mortgages			Consumer instalment and other personal loans			Credit card loans			Total		
	2005	2004	2003	2005	2004	2003	2005	2004	2003	2005	2004	2003
Proceeds from new securitizations	\$ 3,130	\$ 1,382	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 3,130	\$ 1,382	\$ -
Proceeds from collections reinvested in existing securitization vehicles	1,895	2,667	2,662	-	54	59	1,343	4,941	7,351	3,238	7,662	10,072
Servicing fees collected	8	4	9	-	-	-	6	21	32	14	25	41
Receipt of deferred purchase price	88	78	80	-	5	18	20	85	138	108	168	236

The impact of securitizations on our Consolidated Balance Sheet as at October 31, 2005 and 2004 was as follows:

(Canadian \$ in millions)	Residential mortgages		Consumer instalment and other personal loans		Credit card loans		Total	
	2005	2004	2005	2004	2005	2004	2005	2004
Retained interests								
Investment in securitization vehicles	\$ -	\$ -	\$ 27	\$ 27	\$ -	\$ -	\$ 27	\$ 27
Deferred purchase price	213	134	-	-	4	9	217	143
Cash deposits with securitization vehicles	12	12	-	-	-	-	12	12
Servicing liability	50	34	-	-	-	-	50	34

### Credit Information

Information related to principal amounts, impaired amounts and net credit losses for all loans reported and securitized is as follows:

(Canadian \$ in millions)	2005			2004		
	Total loans	Impaired loans	Net write-offs <sup>(1)</sup>	Total loans	Impaired loans	Net write-offs <sup>(1)</sup>
Residential mortgages	\$ 69,801	\$ 103	\$ 4	\$ 63,227	\$ 132	\$ 4
Consumer instalment and other personal loans	28,118	31	69	25,494	28	78
Credit card loans	4,898	8	147	4,752	11	120
Business and government loans	47,803	673	155	44,559	957	174
Securities borrowed or purchased under resale agreements	28,280	-	-	22,609	-	-
<b>Total loans</b>	<b>178,900</b>	<b>815</b>	<b>375</b>	<b>160,641</b>	<b>1,128</b>	<b>376</b>
Less loans securitized:						
Residential mortgages	8,930	18	-	6,783	7	1
Consumer instalment and other personal loans	189	-	17	607	1	13
Credit card loans	250	1	6	1,050	1	23
<b>Total loans reported in the Consolidated Balance Sheet</b>	<b>\$ 169,531</b>	<b>\$ 796</b>	<b>\$ 352</b>	<b>\$ 152,201</b>	<b>\$ 1,119</b>	<b>\$ 339</b>

(1) Net write-offs represent write-offs in the current year net of recoveries on loans previously written off.

Our credit exposure to securitized assets as at October 31, 2005 was limited to our deferred purchase price of \$217 million (\$143 million in 2004), certain cash deposits of \$12 million (\$12 million in 2004) and investments in securitization vehicles of \$27 million (\$27 million in 2004).

Static pool credit losses provide a measure of the credit risk in our securitized assets. They are calculated by totalling actual and projected future credit losses and dividing the result by the original balance of each pool of assets. Static pool credit losses for the two years ended October 31 were as follows:

	2005	2004
Residential mortgages	—	—
Consumer instalment and other personal loans	3.13%	3.18%
Credit card loans	0.43%	1.84%

### Sensitivity Analysis

The following table outlines the key economic assumptions used in measuring the deferred purchase price and the sensitivity of the current value of the deferred purchase price as at October 31, 2005 to immediate 10% and 20% adverse changes in those assumptions. The sensitivity analysis should be used with caution as it is hypothetical and changes in each key assumption may not be linear. The sensitivities in each key variable have been calculated independently of changes in the other key variables. Actual experience may result

in changes in a number of key assumptions simultaneously. Changes in one factor may result in changes in another, which could amplify or reduce certain sensitivities.

(Canadian \$ in millions, except as noted)	Residential mortgages	Consumer instalment and other personal loans	Credit card loans
Carrying value of deferred purchase price	\$ 213	\$ —	\$ 4
Fair value of deferred purchase price	\$ 226	\$ —	\$ 4
Weighted average life (in years)	3.44	0.43	0.19
Prepayment rate (%)	8.0–29.57	4.0	99.83
Impact of: 10% adverse change (\$)	2.1–3.0	—	0.36
20% adverse change (\$)	4.2–5.8	—	0.66
Interest rate (%)	0.49–2.28	—	9.77
Impact of: 10% adverse change (\$)	8.4–13.5	—	0.4
20% adverse change (\$)	16.8–26.9	—	0.8
Expected credit losses (%)	0–0.1	9.09–22.31	1.82
Impact of: 10% adverse change (\$)	0.1–0	—	0.1
20% adverse change (\$)	0.2–0	—	0.2
Discount rate (%)	3.8–10.62	10.62	10.62
Impact of: 10% adverse change (\$)	0.95–0.8	—	—
20% adverse change (\$)	1.9–1.6	—	—

## Note 8 ▶ Variable Interest Entities

### Change in Accounting Policy

On November 1, 2004, we adopted the CICA's new accounting requirements on the consolidation of variable interest entities ("VIEs"). VIEs include entities where the equity is considered insufficient to finance the entity's activities or for which the equity holders do not have a controlling financial interest. The new rules require that we consolidate VIEs if the investments we hold in these entities and/or the relationships we have with them result in us being exposed to the majority of their expected losses, being able to benefit from a majority of their expected residual returns, or both, based on a calculation determined by standard setters. As discussed further below, we consolidated our customer securitization vehicles as at November 1, 2004. Results for prior periods were not restated for this change. On April 29, 2005, we completed the restructuring of our customer securitization vehicles. As a result of the restructuring, we are no longer exposed to the majority of their expected losses or able to benefit from a majority of their residual returns, and the vehicles have been deconsolidated.

### Customer Securitization Vehicles

Customer securitization vehicles (also referred to as multi-seller conduits) assist our customers with the securitization of their assets to provide them with alternate sources of funding. These vehicles provide clients with access to financing in the commercial paper markets by allowing them to sell their assets into these vehicles, which then issue commercial paper to investors to fund the purchases. The seller continues to service the transferred assets. If there are losses on the assets, the seller is the first to take the loss. We do not sell assets to or service the assets held by these customer securitization vehicles. We earn fees for providing structuring advice related to the securitizations as well as administrative fees for supporting the ongoing operations of customer securitization vehicles.

In general, investors in the commercial paper have recourse only to the assets of the related VIE and do not have recourse to us,

unless we have provided credit support for the investors or entered into a derivative transaction involving the VIE.

We provide liquidity and credit support to these vehicles either through backstop liquidity facilities or in the form of letters of credit and other guarantees. The total contractual amount of this support was \$28,125 million as at October 31, 2005 (\$27,019 million in 2004). Of these amounts, \$567 million as at October 31, 2005 (\$400 million in 2004) related to credit support. None of these facilities were drawn upon as at October 31, 2005 and 2004.

Derivative contracts entered into with these vehicles enable the vehicles to manage their exposures to interest and foreign exchange rate fluctuations. The fair value of our derivatives outstanding with these VIEs and recorded in our Consolidated Balance Sheet was a derivative asset of \$6 million as at October 31, 2005 (\$52 million in 2004).

Beginning November 1, 2004, we consolidated our customer securitization vehicles. The impact of consolidation on our Consolidated Balance Sheet as at November 1, 2004 was an increase in other assets of \$21,160 million, a decrease in derivative financial instrument assets of \$67 million, an increase in other liabilities of \$21,150 million, a decrease in derivative financial instrument liabilities of \$15 million and a decrease in opening retained earnings of \$42 million.

The impact on opening retained earnings arose because interest rate swaps held by our VIEs to hedge their exposure to interest rate risk did not qualify for hedge accounting prior to consolidation. As a result, the mark-to-market adjustments on those derivatives from their inception to November 1, 2004 would have been recognized in income. Since the new rules require us to reflect the results of the consolidated VIEs as if they had always been consolidated, without restatement of prior periods, the amount of mark-to-market losses prior to November 1, 2004 was recognized through our opening retained earnings. This adjustment was being amortized to income over the remaining life of the swaps. These derivatives qualified for hedge accounting after we started consolidating the VIEs.

On April 29, 2005, we completed the restructuring of our customer securitization vehicle VIEs by either terminating or changing the terms of our swaps with the VIEs and amending some of the rights of noteholders in the VIEs. As a result they no longer meet the criteria for consolidation. The impact on our Consolidated Statement of Income of deconsolidating these entities on April 29, 2005 was an increase in non-interest revenue – other of \$44 million, an increase in income taxes of \$7 million and an increase in net income of \$37 million, representing the reversal of the unamortized mark-to-market losses on swaps that had been charged against opening retained earnings.

We have significant variable interests in certain other VIEs that we are not required to consolidate. Our involvement with non-consolidated VIEs is summarized as follows:

#### Bank Securitization Vehicles

We use bank securitization vehicles to securitize our loans either for capital management purposes or to obtain alternate sources of funding. The structure of these vehicles limits the types of activities they can undertake and the types of assets they can hold, and they have limited decision-making authority. We are not required to consolidate our bank securitization vehicles under the CICA requirements. More information on our rights and obligations related to these vehicles can be found in Note 7. In addition to the interests described in Note 7, we also provide liquidity support to our securitization vehicles in the form of standby letters of credit and guarantees for up to 100% of the asset value transferred. The total contract amount of standby letters of credit and guarantees was \$5,000 million and \$3,750 million as at October 31, 2005 and 2004, respectively. No amount was drawn at October 31, 2005 and 2004.

#### Credit Investment Management Vehicles

Credit investment management vehicles provide investment opportunities in customized, diversified debt portfolios in a variety of asset and rating classes. We earn investment management fees for managing these portfolios. Until 2004, we had two types of credit investment management vehicles: High Yield Collateralized Bond Obligation Vehicles (“CBOs”) and High Grade Structured Investment Vehicles (“SIVs”).

During the year ended October 31, 2004, we sold our investment in the CBOs with minimal impact on net income. We were also replaced as asset manager. As a result, we no longer have interests in the CBOs.

We continue to hold our interest in the SIVs and act as asset manager. Assets held by the SIVs totalled \$21,886 million as at October 31, 2005 (\$19,502 million in 2004).

Our exposure to loss relates to our investments in these vehicles, derivative contracts we have entered into with the vehicles and the liquidity support we provide through standby letters of credit and/or commitments to extend credit. Our investment in the SIVs, which was recorded as investment securities on our Consolidated Balance Sheet, was \$146 million as at October 31, 2005 (\$128 million in 2004). The fair value of our derivative contracts outstanding with the SIVs and recorded on our Consolidated Balance Sheet was a derivative liability of \$24 million as at October 31, 2005 (\$37 million derivative asset in 2004). The total contract amount of letters of credit and commitments to extend credit was \$189 million as at October 31, 2005 (\$200 million in 2004); no amounts were drawn at October 31, 2005 and 2004. We are not required to consolidate these SIVs under the CICA requirements.

#### Compensation Trusts

We have established trusts in order to administer our employee share ownership plan. Under this plan, we match 50% of employees' contributions when they choose to contribute a portion of their gross salary toward the purchase of our common shares. Our matching contributions are paid into trusts, which purchase our shares on the open market for payment to employees once employees are entitled to the shares under the terms of the plan. We are not required to consolidate these compensation trusts under the CICA requirements.

#### Other VIEs

We are involved with other entities that may potentially be VIEs. This involvement can include, for example, acting as a derivatives counterparty, liquidity provider, investor, fund manager or trustee. These activities do not cause us to be exposed to a majority of the expected losses of these VIEs or allow us to benefit from a majority of their expected residual returns. As a result, we are not required to consolidate these VIEs under the CICA requirements. Transactions with these VIEs are conducted at market rates, and individual credit or investment decisions are based upon the analysis of the specific VIE, taking into consideration the quality of underlying assets. We record and report these transactions in the same manner as other transactions. For example, derivative contracts are recorded in accordance with our derivatives accounting policy as outlined in Note 9. Liquidity facilities are described in Note 6.

## Note 9 ▶ Derivative Financial Instruments

Derivative financial instruments are contracts that require the exchange of, or provide the opportunity to exchange, cash flows determined by applying certain rates, indices or changes therein to notional contract amounts. Derivative transactions are conducted either directly between two counterparties in the over-the-counter market or on regulated exchange markets.

#### Types of Derivatives

##### Swaps

Swaps are contractual agreements between two parties to exchange a series of cash flows. The various swap agreements that we enter into are as follows:

Interest rate swaps – counterparties generally exchange fixed and floating rate interest payments based on a notional value in a single currency.

Cross-currency swaps – fixed rate interest payments and principal amounts are exchanged in different currencies.

Cross-currency interest rate swaps – fixed and floating rate interest payments and principal amounts are exchanged in different currencies.

Commodity swaps – counterparties generally exchange fixed and floating rate payments based on a notional value of a single commodity.

Equity swaps – counterparties exchange the return on an equity security or a group of equity securities for the return based on a fixed or floating interest rate or the return on another equity security or a group of equity securities.

Credit default swaps – one counterparty pays the other a fee in exchange for that other counterparty agreeing to make a payment if a credit event occurs, such as bankruptcy or a credit rating change.

The main risks associated with these instruments are related to our exposure to movements in interest rates, foreign exchange rates, credit ratings, securities values or commodities prices, as applicable, and the possible inability of counterparties to meet the terms of the contracts.

### *Forwards and Futures*

Forwards and futures are contractual agreements to either buy or sell a specified amount of a currency, commodity or security at a specific price and date in the future. Forwards are customized contracts transacted in the over-the-counter market. Futures are transacted in standardized amounts on regulated exchanges and are subject to daily cash margining.

The main risks associated with these instruments arise from the possible inability of over-the-counter counterparties to meet the terms of the contracts and from movements in commodities prices, securities values, interest rates and foreign exchange rates, as applicable.

### *Options*

Options are contractual agreements that convey to the buyer the right but not the obligation to either buy or sell a specified amount of a currency, commodity or security at a fixed future date or at any time within a fixed future period.

For options written by us, we receive a premium from the purchaser for accepting market risk.

For options purchased by us, we pay a premium for the right to exercise the option. Since we have no obligation to exercise the option, our primary exposure to risk is the potential credit risk if the writer of an over-the-counter contract fails to fulfill the conditions of the contract.

Caps, collars and floors are specialized types of written and purchased options. They are contractual agreements where the writer agrees to pay the purchaser, based on a specified notional amount, the difference between the market rate and the prescribed rate of the cap, collar or floor. The writer receives a premium for selling this instrument.

## **Uses of Derivatives**

### *Trading Derivatives*

Trading derivatives are derivatives entered into with customers to accommodate their risk management needs, derivatives transacted to generate trading income from our own proprietary trading positions and certain derivatives that do not qualify as hedges for accounting purposes (“economic hedges”).

We structure and market derivative products to customers to enable them to transfer, modify or reduce current or expected risks.

Proprietary activities include market-making, positioning and arbitrage activities. Market-making involves quoting bid and offer prices to other market participants with the intention of generating revenues based on spread and volume. Positioning activities involve managing market risk positions with the expectation of profiting from favourable movements in prices, rates or indices. Arbitrage activities involve identifying and profiting from price differentials between markets and products.

We may also take proprietary trading positions in various capital markets instruments and derivatives that, taken together, are designed to profit from anticipated changes in market factors.

Trading derivatives are marked to market. Realized and unrealized gains and losses are recorded in trading revenues in our Consolidated Statement of Income. Unrealized gains on trading derivatives are recorded as derivative financial instrument assets and unrealized losses are recorded as derivative financial instrument liabilities in our Consolidated Balance Sheet.

### *Hedging Derivatives*

In accordance with our risk management strategy, we enter into various derivative contracts to hedge our interest rate and foreign currency exposures.

## **Risks Hedged**

### *Interest Rate Risk*

We manage interest rate risk through interest rate swaps and options, which are linked to and adjust the interest rate sensitivity of a specific asset, liability, firm commitment or a specific pool of transactions with similar risk characteristics.

Fair value hedges modify exposure to changes in a fixed rate instrument's fair value caused by changes in interest rates.

These hedges convert fixed rate assets and liabilities to floating rate. Our fair value hedges include hedges of fixed rate loans, securities, deposits and subordinated debt.

Cash flow hedges modify exposure to variability in cash flows for variable rate interest bearing instruments. Our cash flow hedges, which have a maximum term of 12 years, are primarily hedges of floating rate deposits as well as commercial and personal loans.

In order for an interest rate derivative to qualify as a hedge, the hedge relationship must be designated and formally documented at its inception, detailing the particular risk management objective and strategy for the hedge and the specific asset, liability or cash flow being hedged, as well as how effectiveness is being assessed. Changes in the fair value of the derivative must be highly effective in offsetting either changes in the fair value of on-balance sheet items or changes in the amount of future cash flows. Hedge effectiveness is evaluated at the inception of the hedge relationship and on an ongoing basis, both retrospectively and prospectively, primarily using quantitative statistical measures of correlation. If a hedge relationship is found to be no longer effective, or if the designated hedged item matures or is sold, extinguished or terminated, the derivative is reclassified as trading. Subsequent changes in the fair value of hedging derivatives reclassified as trading are reported in trading revenues.

Swaps and options that qualify for hedge accounting are accounted for on an accrual basis. Interest income received and interest expense paid on interest rate swaps are accrued and recorded as an adjustment to the yield of the item being hedged over the term of the hedge contract. Premiums paid on purchased options are amortized to interest expense over the term of the contract. Accrued interest receivable and payable and deferred gains and losses are recorded as derivative financial instrument assets or liabilities in our Consolidated Balance Sheet, as appropriate. Realized gains and losses from the settlement or early termination of hedge contracts or a hedging relationship are deferred and amortized over the remaining original life of the hedged item.

### *Foreign Currency Risk*

We manage foreign currency risk through cross-currency swaps. Cross-currency swaps are marked to market, with realized and unrealized gains and losses recorded in non-interest revenue, consistent with the accounting treatment for gains and losses on the economically hedged item.

We also periodically hedge U.S. dollar earnings through forward foreign exchange contracts to minimize fluctuations in our Canadian dollar earnings due to the translation of our U.S. dollar earnings. These contracts are marked to market, with gains and losses recorded as non-interest revenue in foreign exchange, other than trading.

## **Future Change in Accounting Policy**

As discussed in Note 1, we will adopt the CICA's new accounting requirements that will change our accounting policy for hedging derivatives beginning November 1, 2006. The requirements for identification, designation and documentation of hedging relationships are unchanged.

The new rules will require us to record all of our hedging derivatives at fair value. Changes in the fair value of hedging derivatives will be either offset in our Consolidated Statement of Income against the changes in the fair value of the risk being hedged, or recorded in a new section of shareholders' equity called other comprehensive income. If the change in fair value of the derivative is not completely offset by the change in fair value of the item it is hedging, the difference will be recorded immediately in our Consolidated Statement of Income.

The impact of remeasuring our hedging derivatives at fair value on November 1, 2006 will be recognized in opening retained earnings. Results for prior periods will not be restated. We cannot currently determine the impact that these changes in accounting policy will have on our consolidated financial statements once adopted, as this will be dependent on the fair values of our hedging derivatives in the future.

**Fair Value**

Fair value represents point-in-time estimates that may change in subsequent reporting periods due to market conditions or other factors. Fair value for exchange-traded derivatives is considered to be the price quoted on derivatives exchanges. Fair value for over-the-counter derivatives is determined using zero coupon valuation techniques further adjusted for credit, model and liquidity risks as

well as administration costs. Zero coupon curves are created using generally accepted valuation techniques from underlying instruments such as cash, bonds and futures observable in the market. Option implied volatilities, an input into the valuation model, are either obtained directly from market sources or calculated from market prices.

Fair values of our derivative financial instruments are as follows:

(Canadian \$ in millions)	2005			2004		
	Gross assets	Gross liabilities	Net	Gross assets	Gross liabilities	Net
<b>Trading</b>						
<b>Interest Rate Contracts</b>						
Swaps	\$ 8,431	\$ (8,820)	\$ (389)	\$ 10,655	\$ (10,485)	\$ 170
Forward rate agreements	101	(89)	12	105	(109)	(4)
Futures	1	(5)	(4)	4	(10)	(6)
Purchased options	1,504	(4)	1,500	1,548	(2)	1,546
Written options	–	(1,290)	(1,290)	–	(1,295)	(1,295)
<b>Foreign Exchange Contracts</b>						
Cross-currency swaps	1,342	(831)	511	940	(622)	318
Cross-currency interest rate swaps	2,779	(2,431)	348	3,341	(2,677)	664
Forward foreign exchange contracts	743	(1,212)	(469)	2,028	(3,023)	(995)
Purchased options	99	–	99	157	–	157
Written options	–	(91)	(91)	–	(156)	(156)
<b>Commodity Contracts</b>						
Swaps	6,221	(5,539)	682	3,514	(2,979)	535
Futures	121	–	121	–	–	–
Purchased options	8,895	–	8,895	2,156	–	2,156
Written options	–	(8,087)	(8,087)	–	(1,994)	(1,994)
<b>Equity Contracts</b>						
	485	(301)	184	391	(300)	91
<b>Credit Contracts</b>						
	129	(129)	–	75	(89)	(14)
Total fair value – trading derivatives	\$ 30,851	\$ (28,829)	\$ 2,022	\$ 24,914	\$ (23,741)	\$ 1,173
Total book value – trading derivatives	\$ 30,851	\$ (28,829)	\$ 2,022	\$ 24,914	\$ (23,741)	\$ 1,173
Average fair value (1)	\$ 25,184	\$ (24,169)	\$ 1,015	\$ 21,556	\$ (20,637)	\$ 919
<b>Hedging</b>						
<b>Interest Rate Contracts</b>						
Swaps	\$ 293	\$ (158)	\$ 135	\$ 437	\$ (284)	\$ 153
Forward rate agreements	–	–	–	1	(1)	–
Purchased options	23	–	23	20	–	20
Written options	–	(2)	(2)	–	–	–
<b>Foreign Exchange Contracts</b>						
Cross-currency interest rate swaps	461	(6)	455	394	(118)	276
Forward foreign exchange contracts	131	(6)	125	15	(59)	(44)
Total fair value – hedging derivatives (2)	\$ 908	\$ (172)	\$ 736	\$ 867	\$ (462)	\$ 405
Total book value – hedging derivatives	\$ 666	\$ (39)	\$ 627	\$ 534	\$ (232)	\$ 302
Average fair value (1)	\$ 1,019	\$ (320)	\$ 699	\$ 850	\$ (558)	\$ 292

(1) Average fair value amounts are calculated using a five-quarter rolling average.

(2) The fair value of hedging derivatives wholly or partially offsets the changes in fair values of the related on-balance sheet financial instruments.

Assets are shown net of liabilities to customers where we have an enforceable right to offset amounts and we intend to settle contracts on a net basis.

Derivative financial instruments recorded in our Consolidated Balance Sheet are as follows:

(Canadian \$ in millions)	Assets		Liabilities	
	2005	2004	2005	2004
Fair value of trading derivatives	\$ 30,851	\$ 24,914	\$ 28,829	\$ 23,741
Book value of hedging derivatives	666	534	39	232
Total	\$ 31,517	\$ 25,448	\$ 28,868	\$ 23,973

## Notional Amounts

The notional amounts of our derivatives represent the amount to which a rate or price is applied in order to calculate the amount of

cash that must be exchanged under the contract. Notional amounts do not represent assets or liabilities and therefore are not recorded in our Consolidated Balance Sheet.

(Canadian \$ in millions)

	2005			2004		
	Trading	Hedging	Total	Trading	Hedging	Total
<b>Interest Rate Contracts</b>						
Over-the-counter						
Swaps	\$ 717,849	\$ 31,650	\$ 749,499	\$ 680,570	\$ 36,424	\$ 716,994
Forward rate agreements	218,475	–	218,475	307,047	1,401	308,448
Purchased options	97,190	5,923	103,113	75,784	6,341	82,125
Written options	125,123	40	125,163	97,476	–	97,476
	<b>1,158,637</b>	<b>37,613</b>	<b>1,196,250</b>	<b>1,160,877</b>	<b>44,166</b>	<b>1,205,043</b>
Exchange-traded						
Futures	181,506	–	181,506	171,961	1,554	173,515
Purchased options	76,481	–	76,481	36,408	–	36,408
Written options	57,850	–	57,850	21,284	–	21,284
	<b>315,837</b>	<b>–</b>	<b>315,837</b>	<b>229,653</b>	<b>1,554</b>	<b>231,207</b>
Total interest rate contracts	<b>1,474,474</b>	<b>37,613</b>	<b>1,512,087</b>	<b>1,390,530</b>	<b>45,720</b>	<b>1,436,250</b>
<b>Foreign Exchange Contracts</b>						
Over-the-counter						
Cross-currency swaps	9,644	–	9,644	9,635	–	9,635
Cross-currency interest rate swaps	55,334	3,300	58,634	45,577	4,276	49,853
Forward foreign exchange contracts	91,819	3,183	95,002	87,855	8,804	96,659
Purchased options	5,790	–	5,790	5,865	–	5,865
Written options	6,306	–	6,306	6,950	–	6,950
	<b>168,893</b>	<b>6,483</b>	<b>175,376</b>	<b>155,882</b>	<b>13,080</b>	<b>168,962</b>
Exchange-traded						
Futures	4,015	–	4,015	886	–	886
Purchased options	2,016	–	2,016	2,063	–	2,063
Written options	675	–	675	283	–	283
	<b>6,706</b>	<b>–</b>	<b>6,706</b>	<b>3,232</b>	<b>–</b>	<b>3,232</b>
Total foreign exchange contracts	<b>175,599</b>	<b>6,483</b>	<b>182,082</b>	<b>159,114</b>	<b>13,080</b>	<b>172,194</b>
<b>Commodity Contracts</b>						
Over-the-counter						
Swaps	41,977	–	41,977	26,455	–	26,455
Purchased options	46,746	–	46,746	19,028	–	19,028
Written options	47,619	–	47,619	19,087	–	19,087
	<b>136,342</b>	<b>–</b>	<b>136,342</b>	<b>64,570</b>	<b>–</b>	<b>64,570</b>
Exchange-traded						
Futures	24,329	–	24,329	2,771	–	2,771
Purchased options	38,140	–	38,140	1,409	–	1,409
Written options	40,610	–	40,610	1,563	–	1,563
	<b>103,079</b>	<b>–</b>	<b>103,079</b>	<b>5,743</b>	<b>–</b>	<b>5,743</b>
Total commodity contracts	<b>239,421</b>	<b>–</b>	<b>239,421</b>	<b>70,313</b>	<b>–</b>	<b>70,313</b>
<b>Equity Contracts</b>						
Over-the-counter	19,969	–	19,969	19,384	–	19,384
Exchange-traded	8,212	–	8,212	5,342	–	5,342
Total equity contracts	<b>28,181</b>	<b>–</b>	<b>28,181</b>	<b>24,726</b>	<b>–</b>	<b>24,726</b>
<b>Credit Contracts</b>						
Over-the-counter	39,781	–	39,781	26,447	–	26,447
Total	<b>\$ 1,957,456</b>	<b>\$ 44,096</b>	<b>\$ 2,001,552</b>	<b>\$ 1,671,130</b>	<b>\$ 58,800</b>	<b>\$ 1,729,930</b>

Included in the notional amounts is \$796 million as at October 31, 2005 (\$1,039 million in 2004) related to the Managed Futures Certificates of Deposit Program. Risk exposures represented by the assets in this program are traded on behalf of customers, with all gains and losses accruing to them.

**Derivative-Related Credit Risk**

Over-the-counter derivative instruments are subject to credit risk. Credit risk arises from the possibility that counterparties may default on their obligations. The credit risk associated with derivatives is normally a small fraction of the notional amount of the derivative instrument. Derivative contracts generally expose us to potential credit loss if changes in market rates affect a counterparty's position unfavourably and the counterparty defaults on payment. The credit risk is represented by the positive fair value of the derivative instrument. We strive to limit credit risk by dealing with counterparties that we believe are creditworthy, and we manage our credit risk for derivatives using the same credit risk process that is applied to loans and other credit assets.

We also pursue opportunities to reduce our exposure to credit losses on derivative instruments, including entering into master netting agreements with counterparties. The credit risk associated with favourable contracts is eliminated by master netting agreements, to the extent that unfavourable contracts with the same counterparty cannot be settled before favourable contracts.

Exchange-traded derivatives have no potential for credit exposure as they are settled net with each exchange.

Terms used in the credit risk table below are as follows:

**Replacement cost** represents the cost of replacing all contracts that have a positive fair value, using current market rates. It represents in effect the unrealized gains on our derivative instruments. Replacement costs disclosed below represent the net of the asset and liability to a specific counterparty where we have a legally enforceable right to offset the amount owed to us with the amount owed by us and we intend either to settle on a net basis or to realize the asset and settle the liability simultaneously.

**Credit risk equivalent** represents the total replacement cost plus an amount representing the potential future credit exposure, as outlined in the Capital Adequacy Guideline of the Superintendent of Financial Institutions Canada.

**Risk-weighted balance** represents the credit risk equivalent, weighted based on the creditworthiness of the counterparty, as prescribed by the Superintendent of Financial Institutions Canada.

(Canadian \$ in millions)

	2005			2004		
	Replacement cost	Credit risk equivalent	Risk-weighted balance	Replacement cost	Credit risk equivalent	Risk-weighted balance
<b>Interest Rate Contracts</b>						
Swaps	\$ 8,724	\$ 12,955	\$ 2,995	\$ 11,092	\$ 14,994	\$ 3,541
Forward rate agreements	101	160	33	106	196	40
Purchased options	1,501	1,844	414	1,556	1,941	441
Total interest rate contracts	10,326	14,959	3,442	12,754	17,131	4,022
<b>Foreign Exchange Contracts</b>						
Cross-currency swaps	1,342	1,911	574	940	1,513	457
Cross-currency interest rate swaps	3,240	6,142	1,068	3,735	6,165	1,124
Forward foreign exchange contracts	874	1,997	586	2,043	3,275	951
Purchased options	88	159	58	145	224	80
Total foreign exchange contracts	5,544	10,209	2,286	6,863	11,177	2,612
<b>Commodity Contracts</b>						
Swaps	6,221	11,969	4,706	3,514	6,941	2,673
Purchased options	6,311	11,123	4,465	2,047	4,006	1,361
Total commodity contracts	12,532	23,092	9,171	5,561	10,947	4,034
<b>Equity Contracts</b>	328	1,776	604	391	1,649	669
<b>Credit Contracts</b>	129	1,740	377	75	1,195	254
Total derivatives	28,859	51,776	15,880	25,644	42,099	11,591
Impact of master netting agreements	(19,832)	(24,693)	(7,214)	(13,455)	(18,352)	(4,705)
Total	\$ 9,027	\$ 27,083	\$ 8,666	\$ 12,189	\$ 23,747	\$ 6,886

Included in the total derivatives are unrealized gains on hedging derivatives, which we include in the Consolidated Balance Sheet on an accrual rather than a mark-to-market basis. The excess of market value over book value for these items was \$242 million as at October 31, 2005 (\$333 million in 2004). Total derivatives does not include exchange-traded derivatives with a positive fair value of \$2,900 million as at October 31, 2005 (\$137 million in 2004).

Transactions are conducted with counterparties in various geographic locations and industries. Set out below is the replacement cost of contracts (before the impact of master netting agreements) with customers located in the following countries, based on country of ultimate risk:

(Canadian \$ in millions, except as noted)

	2005		2004	
Canada	\$ 7,852	27%	\$ 7,611	30%
United States	14,187	49	11,088	43
Other countries (1)	6,820	24	6,945	27
Total	\$ 28,859	100%	\$ 25,644	100%

(1) No other country represented 10% or more of our replacement cost in either 2005 or 2004.

Transactions are conducted with various counterparties. Set out below is the replacement cost of contracts (before the impact of master netting agreements) with customers in the following industries:

(Canadian \$ in millions)	Interest rate contracts		Foreign exchange contracts		Commodity contracts		Equity contracts		Credit contracts	
	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
Financial institutions	\$ 8,852	\$ 11,213	\$ 2,021	\$ 3,770	\$ 3,880	\$ 1,939	\$ 163	\$ 105	\$ 125	\$ 73
Natural resources	29	12	98	134	8,119	3,471	–	–	–	–
Other	1,445	1,529	3,425	2,959	533	151	165	286	4	2
<b>Total</b>	<b>\$ 10,326</b>	<b>\$ 12,754</b>	<b>\$ 5,544</b>	<b>\$ 6,863</b>	<b>\$ 12,532</b>	<b>\$ 5,561</b>	<b>\$ 328</b>	<b>\$ 391</b>	<b>\$ 129</b>	<b>\$ 75</b>

### Term to Maturity

Our derivative contracts have varying maturity dates. The remaining contractual term to maturity for the notional amounts of our derivative contracts is set out below:

(Canadian \$ in millions)	Term to maturity					2005	2004
	Within 1 year	1 to 3 years	3 to 5 years	5 to 10 years	Over 10 years	Total notional amount	Total notional amount
<b>Interest Rate Contracts</b>							
Swaps	\$ 216,186	\$ 230,576	\$ 140,808	\$ 130,795	\$ 31,134	\$ 749,499	\$ 716,994
Forward rate agreements, futures and options	551,355	150,248	31,843	25,630	3,512	762,588	719,256
<b>Total interest rate contracts</b>	<b>767,541</b>	<b>380,824</b>	<b>172,651</b>	<b>156,425</b>	<b>34,646</b>	<b>1,512,087</b>	<b>1,436,250</b>
<b>Foreign Exchange Contracts</b>							
Cross-currency swaps	1,259	1,852	1,048	3,135	2,350	9,644	9,635
Cross-currency interest rate swaps	11,347	18,848	12,132	13,216	3,091	58,634	49,853
Forward foreign exchange contracts, futures and options	105,711	6,153	1,427	497	16	113,804	112,706
<b>Total foreign exchange contracts</b>	<b>118,317</b>	<b>26,853</b>	<b>14,607</b>	<b>16,848</b>	<b>5,457</b>	<b>182,082</b>	<b>172,194</b>
<b>Commodity Contracts</b>							
Swaps	25,556	14,445	1,744	232	–	41,977	26,455
Futures and options	151,068	44,313	2,040	23	–	197,444	43,858
<b>Total commodity contracts</b>	<b>176,624</b>	<b>58,758</b>	<b>3,784</b>	<b>255</b>	<b>–</b>	<b>239,421</b>	<b>70,313</b>
<b>Equity Contracts</b>	<b>20,619</b>	<b>2,037</b>	<b>1,809</b>	<b>2,850</b>	<b>866</b>	<b>28,181</b>	<b>24,726</b>
<b>Credit Contracts</b>	<b>5,310</b>	<b>9,048</b>	<b>21,366</b>	<b>4,017</b>	<b>40</b>	<b>39,781</b>	<b>26,447</b>
<b>Total</b>	<b>\$ 1,088,411</b>	<b>\$ 477,520</b>	<b>\$ 214,217</b>	<b>\$ 180,395</b>	<b>\$ 41,009</b>	<b>\$ 2,001,552</b>	<b>\$ 1,729,930</b>

## Note 10 ▶ Premises and Equipment

We record all premises and equipment at cost less accumulated amortization except for land, which is recorded at cost. Buildings, computer equipment and software, other equipment and leasehold improvements are amortized on a straight-line basis over their estimated useful lives. The maximum estimated useful lives we use to amortize our assets are:

Buildings	40 years
Computer equipment and software	15 years
Other equipment	10 years
Leasehold improvements	Lease term to a maximum of 10 years

(Canadian \$ in millions)	2005			2004
	Cost	Accumulated amortization	Carrying value	Carrying value
Land	\$ 179	\$ –	\$ 179	\$ 271
Buildings	1,063	545	518	620
Computer equipment and software	2,366	1,676	690	676
Other equipment	679	455	224	247
Leasehold improvements	577	341	236	206
<b>Total</b>	<b>\$ 4,864</b>	<b>\$ 3,017</b>	<b>\$ 1,847</b>	<b>\$ 2,020</b>

Amortization expense for the years ended October 31, 2005, 2004 and 2003 amounted to \$377 million, \$365 million and \$375 million, respectively.

Gains and losses on disposal are included in non-interest revenue – other in our Consolidated Statement of Income.

On September 23, 2005, we sold the office tower located at 350 – 7th Avenue South West in Calgary. The gain on sale was \$58 million before tax, of which \$29 million was recorded in the Consolidated Statement of Income. The remaining \$29 million was deferred and will be recorded as a reduction in rental expense over the terms of our leases in the building, which expire between 2015 and 2025. The deferred gain as at October 31, 2005 was \$29 million.

On March 1, 2005, we sold the land and building located at 111 West Monroe Street in Chicago and concurrently entered into lease agreements at market rates for approximately 50% of the building. The gain on sale of \$5 million was deferred and will be recorded as a reduction in rental expense over the terms of our leases in the building, which expire between 2013 and 2035. The deferred gain as at October 31, 2005 was \$5 million.

We test premises and equipment for impairment when events or changes in circumstances indicate that their carrying value may not be recoverable. We write them down to fair value when the related undiscounted cash flows are not expected to allow for recovery of the carrying value. There were no write-downs of premises and equipment due to impairment during the years ended October 31, 2005, 2004 and 2003.

**Lease Commitments**

We have entered into a number of non-cancellable leases for premises and equipment. Our total contractual rental commitments as at October 31, 2005 were \$1,464 million. The commitments for each of the next five years and thereafter are \$202 million for 2006, \$181 million for 2007, \$149 million for 2008, \$130 million for 2009, \$109 million for 2010 and \$693 million thereafter. Included in these

amounts are the commitments related to 697 leased branch locations as at October 31, 2005.

Net rent expense for premises and equipment reported in our Consolidated Statement of Income was \$245 million, \$227 million and \$222 million for the years ended October 31, 2005, 2004 and 2003, respectively.

**Note 11 ▶ Acquisitions**

We account for acquisitions of businesses using the purchase method. This involves allocating the purchase price paid for a business to the assets acquired, including identifiable intangible assets, and the liabilities assumed, based on their fair values at the date of acquisition. Any excess is then recorded as goodwill.

Our acquisitions in 2005 and 2004 form part of our Retail and Commercial Banking reporting unit within the Personal and Commercial Client Group.

**Mercantile Bancorp, Inc.**

On December 30, 2004, we completed the acquisition of Indiana-based Mercantile Bancorp, Inc., a community bank, for total cash consideration of \$194 million. As part of this transaction, we also acquired a small real estate company, Lake Commercial Corp. (collectively "MBI"). The results of MBI's operations have been included in our consolidated financial statements since that date. The acquisition of MBI provides us with the opportunity to expand our community banking services into Northwest Indiana. As part of this acquisition, we acquired a core deposit intangible asset, which will be amortized on an accelerated basis over 10 years. Goodwill related to this acquisition is not deductible for tax purposes.

**New Lenox State Bank**

On June 1, 2004, we completed the acquisition of all outstanding voting shares of New Lenox State Bank ("NLSB"), a full-service community bank in Will County, Illinois, for total cash consideration of \$314 million. The results of NLSB's operations have been included in our consolidated financial statements since that date. The acquisition of NLSB is part of our expansion in and around the Will County, Illinois market. As part of this acquisition, we acquired a core deposit intangible asset, which will be amortized on an accelerated basis over 10 years. Goodwill related to this acquisition is deductible for tax purposes.

**Lakeland Community Bank**

On March 1, 2004, we completed the acquisition of all outstanding voting shares of Lakeland Community Bank ("LCB"), a full-service community bank in Lake County, Illinois, for total cash consideration of \$49 million. The results of LCB's operations have been included in our consolidated financial statements since that date. The acquisition of LCB is part of our further expansion in and around the Chicago, Illinois market. As part of this acquisition, we acquired a core deposit intangible asset, which will be amortized on an accelerated basis over 10 years. Goodwill related to this acquisition is not deductible for tax purposes.

The estimated fair values of the assets acquired and the liabilities assumed at the dates of acquisition are as follows:

(Canadian \$ in millions)	2005			2004
	MBI	NLSB	LCB	Other
Cash resources	\$ 111	\$ 111	\$ 13	\$ -
Securities	166	393	31	-
Loans	620	774	181	-
Premises and equipment	18	32	3	-
Goodwill	91	193	28	14
Core deposit intangible asset	15	30	2	-
Other intangible assets	-	-	-	8
Other assets	25	48	2	-
<b>Total assets</b>	<b>1,046</b>	<b>1,581</b>	<b>260</b>	<b>22</b>
Deposits	752	1,225	209	-
Other liabilities	100	42	2	-
<b>Total liabilities</b>	<b>852</b>	<b>1,267</b>	<b>211</b>	<b>-</b>
<b>Purchase price</b>	<b>\$ 194</b>	<b>\$ 314</b>	<b>\$ 49</b>	<b>\$ 22</b>

**Future Acquisition***Villa Park Trust and Savings Bank*

On July 7, 2005, we announced the acquisition of Chicago-based Villa Park Trust and Savings Bank ("Villa Park"), a community bank, for total cash consideration of approximately \$81 million.

The acquisition of Villa Park is expected to close in December 2005. The acquisition of Villa Park will provide us with the opportunity to expand our banking services in the Chicago, Illinois market. The results of Villa Park's operations will be included in our consolidated financial statements as of the date of acquisition.

## Note 12 ▶ Sale of Harrisdirect LLC

On October 6, 2005, we sold our interest in our U.S. direct investing operations Harrisdirect LLC to E\*Trade Financial Corporation for cash proceeds of \$827 million (US\$700 million). The gain of \$49 million was recorded in non-interest revenue – other in our Consolidated Statement of Income (\$18 million, after tax). Included in the gain is \$29 million (US\$25 million) representing the estimated reimbursement by Harrisdirect LLC of mutual fund program fees related to our Harris Insight Funds. Certain costs associated with the transaction have not been finalized; if actual costs differ from the estimates, the impact would be recorded in future periods.

We have provided the purchaser standard indemnifications as part of the purchase and sale agreement.

Our Consolidated Statement of Income includes the results of Harrisdirect LLC, including the gain on sale in 2005, as follows:

(Canadian \$ in millions)	2005	2004	2003
Net Interest Income	\$ 68	\$ 66	\$ 67
Non-Interest Revenue	184	179	191
	252	245	258
Non-Interest Expense	243	271	297
Income taxes	14	(11)	(12)
Net Loss	\$ (5)	\$ (15)	\$ (27)

## Note 13 ▶ Goodwill and Intangible Assets

### Goodwill

When we acquire a subsidiary, joint venture or investment securities where we exert significant influence, we allocate the purchase price paid to the assets acquired, including identifiable intangible assets, and the liabilities assumed. Any excess of the amount paid over the fair value of those net assets is considered to be goodwill.

Goodwill is not amortized; however, it is tested at least annually for impairment. The impairment test consists of allocating goodwill to our reporting units (groups of businesses with similar

characteristics) and then comparing the book value of the reporting units, including goodwill, to their fair values. We determine fair value using discounted cash flows or price-to-earnings or other multiples, whichever is most appropriate under the circumstances. The excess of carrying value of goodwill over fair value of goodwill, if any, is recorded as an impairment charge in the period in which impairment is determined.

There were no write-downs of goodwill due to impairment during the years ended October 31, 2005, 2004 and 2003.

A continuity of our goodwill by reporting unit, within our operating groups, for the years ended October 31, 2005 and 2004 is as follows:

(Canadian \$ in millions)	Personal and Commercial Client Group	Retail and Commercial Banking		Client Investing	Retail Investment Products	Private Banking	Private Client Group Total	Investment Banking Group	Other	Total
Goodwill as at October 31, 2003	\$ 404	\$ 593	\$ 187	\$ 74	\$ 854	\$ 73	\$ 3	\$ 1,334		
Acquisitions during the year	233	–	–	–	–	2	–	235		
Other (1)	(49)	(40)	–	–	(40)	27	–	(62)		
Goodwill as at October 31, 2004	588	553	187	74	814	102	3	1,507		
Acquisitions during the year	91	–	–	–	–	–	–	91		
Sale of Harrisdirect LLC	–	(471)	–	–	(471)	–	–	(471)		
Other (1)	(18)	(14)	–	(2)	(16)	(2)	–	(36)		
Goodwill as at October 31, 2005	\$ 661 <sup>(2)</sup>	\$ 68 <sup>(3)</sup>	\$ 187 <sup>(4)</sup>	\$ 72 <sup>(5)</sup>	\$ 327	\$ 100 <sup>(6)</sup>	\$ 3	\$ 1,091		

(1) Other changes in goodwill include the effects of translating goodwill denominated in foreign currencies into Canadian dollars, purchase accounting adjustments related to prior year purchases and certain other reclassifications.

(2) Relates primarily to New Lenox State Bank, First National Bank of Joliet, Household Bank branches, Moneris Solutions Corporation and Mercantile Bancorp, Inc.

(3) Relates to BMO Nesbitt Burns Corporation Limited.

(4) Relates to Guardian Group of Funds Ltd.

(5) Relates primarily to myCFO, Inc.

(6) Relates to Gerard Klauer Mattison & Co., Inc. and BMO Nesbitt Burns Corporation Limited.

### Intangible Assets

Intangible assets related to our acquisitions are recorded at their fair value at the acquisition date. Intangible assets by category are as follows:

(Canadian \$ in millions)	2005			2004
	Cost	Accumulated amortization	Carrying value	Carrying value
Customer relationships	\$ 76	\$ 42	\$ 34	\$ 287
Core deposits	202	116	86	95
Branch distribution networks	174	108	66	81
Other	24	14	10	17
Total	\$ 476	\$ 280	\$ 196	\$ 480

As a result of the sale of Harrisdirect LLC, intangible assets were reduced by \$194 million.

Intangible assets with a finite life are amortized to income over the period during which we believe the assets will benefit us on either a straight-line or an accelerated basis, depending on the specific asset, over a period not to exceed 15 years.

We test intangible assets with a finite life for impairment when events or changes in circumstances indicate that their carrying value may not be recoverable. We write them down to fair value when the related undiscounted cash flows are not expected to allow for recovery of the carrying value. There were no write-downs of intangible assets due to impairment during the years ended October 31, 2005, 2004 and 2003.

The total estimated amortization expense relating to intangible assets for each of the next five years is \$44 million for 2006, \$42 million for 2007, \$35 million for 2008, \$30 million for 2009 and \$18 million for 2010.

**Note 14 ▶ Other Assets**

(Canadian \$ in millions)	2005	2004
Accounts receivable, prepaid expenses and other items	\$ 4,973	\$ 5,405
Accrued interest receivable	896	666
Due from clients, dealers and brokers	3,521	3,748
Pension asset (Note 22)	1,177	1,155
<b>Total</b>	<b>\$ 10,567</b>	<b>\$ 10,974</b>

**Note 15 ▶ Deposits**

(Canadian \$ in millions)	Demand deposits				Payable after notice		Payable on a fixed date		Total	
	Interest bearing		Non-interest bearing		2005	2004	2005	2004	2005	2004
	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004
Deposits by:										
Banks	\$ 368	\$ 356	\$ 352	\$ 408	\$ 670	\$ 329	\$ 24,083	\$ 19,561	\$ 25,473	\$ 20,654
Businesses and governments	5,499	5,570	11,284	10,380	15,521	18,621	60,133	45,043	92,437	79,614
Individuals	3,459	3,495	4,740	4,189	34,669	33,797	33,015	33,441	75,883	74,922
<b>Total</b>	<b>\$ 9,326</b>	<b>\$ 9,421</b>	<b>\$ 16,376</b>	<b>\$ 14,977</b>	<b>\$ 50,860</b>	<b>\$ 52,747</b>	<b>\$ 117,231</b>	<b>\$ 98,045</b>	<b>\$ 193,793</b>	<b>\$ 175,190</b>
Booked in:										
Canada	\$ 8,079	\$ 7,947	\$ 12,001	\$ 10,894	\$ 35,691	\$ 37,182	\$ 71,211	\$ 63,876	\$ 126,982	\$ 119,899
United States	1,128	1,408	4,168	4,072	14,631	14,798	25,026	18,039	44,953	38,317
Other countries	119	66	207	11	538	767	20,994	16,130	21,858	16,974
<b>Total</b>	<b>\$ 9,326</b>	<b>\$ 9,421</b>	<b>\$ 16,376</b>	<b>\$ 14,977</b>	<b>\$ 50,860</b>	<b>\$ 52,747</b>	<b>\$ 117,231</b>	<b>\$ 98,045</b>	<b>\$ 193,793</b>	<b>\$ 175,190</b>

Included in deposits as at October 31, 2005 and 2004 are \$74,038 million and \$61,982 million of deposits denominated in U.S. dollars, and \$6,297 million and \$6,761 million of deposits denominated in other foreign currencies.

Demand deposits are comprised primarily of our customers' chequing accounts, some of which we pay interest on. Our customers need not notify us prior to withdrawing money from their chequing accounts.

Deposits payable after notice are comprised primarily of our customers' savings accounts, on which we pay interest.

Deposits payable on a fixed date are comprised primarily of various investment instruments purchased by our customers to earn interest over a fixed period, such as term deposits and guaranteed investment certificates. The terms of these deposits can vary from one day to 10 years.

Deposits payable on a fixed date include federal funds purchased, which are overnight borrowings of other banks' excess reserve funds at a United States Federal Reserve Bank. As at October 31, 2005, we had purchased \$4,396 million of federal funds (\$3,165 million in 2004).

Deposits payable on a fixed date include commercial paper totalling \$604 million as at October 31, 2005 (\$335 million in 2004).

Included in our deposits payable on a fixed date as at October 31, 2005 were \$94,840 million of individual deposits greater than one hundred thousand dollars, of which \$49,912 million were booked in Canada, \$23,933 million were booked in the United States and \$20,995 million were booked in other countries. We had \$73,273 million of such deposits as at October 31, 2004, of which \$41,453 million were booked in Canada, \$15,689 million were booked in the United States and \$16,131 million were booked in other countries. Of these deposits booked in Canada as at October 31, 2005, the amount maturing within three months was \$31,541 million, between three and six months was \$1,767 million, between six and 12 months was \$5,341 million and over 12 months was \$11,263 million. As at October 31, 2004, the amount maturing within three months was \$26,592 million, between three and six months was \$1,309 million, between six and 12 months was \$2,491 million and over 12 months was \$11,061 million.

**Note 16 ▶ Other Liabilities**

(Canadian \$ in millions)	2005	2004
Acceptances	\$ 5,934	\$ 5,355
Securities sold but not yet purchased	16,142	10,441
Securities lent or sold under repurchase agreements	22,657	21,345
<b>Total</b>	<b>\$ 44,733</b>	<b>\$ 37,141</b>

**Acceptances**

Acceptances represent a form of negotiable short-term debt that is issued by our customers and which we guarantee for a fee. We have an offsetting claim, equal to the amount of the acceptances, against our customers when the instruments mature. The amount due under acceptances is recorded as a liability and our corresponding claim is recorded as a loan in our Consolidated Balance Sheet.

### Securities Sold but not yet Purchased

Securities sold but not yet purchased represent our obligation to deliver securities which we do not own at the time of sale. These obligations are recorded at their market value. Adjustments to the market value as at the balance sheet date and gains and losses on the settlement of these obligations are recorded in trading revenues in our Consolidated Statement of Income.

### Securities Lent or Sold under Repurchase Agreements

Securities lent or sold under repurchase agreements represent short-term funding transactions where we sell securities that we already own and simultaneously commit to repurchase the same securities at a specified price on a specified date in the future. The obligation to repurchase these securities is recorded at the amount owing. The interest expense related to these liabilities is recorded on an accrual basis.

(Canadian \$ in millions)	2005	2004
<b>Other</b>		
Accounts payable, accrued expenses and other items	\$ 8,812	\$ 9,161
Accrued interest payable	1,146	991
Non-controlling interest in subsidiaries	1,374	944
Liabilities of subsidiaries, other than deposits	271	502
Pension liability (Note 22)	18	18
Other employee future benefits liability (Note 22)	582	540
<b>Total</b>	<b>\$ 12,203</b>	<b>\$ 12,156</b>

Included in non-controlling interest in subsidiaries as at October 31, 2005 were capital trust securities totalling \$1,042 million (\$595 million in 2004) that form part of our Tier 1 regulatory capital (see Note 18).

## Note 17 ▶ Subordinated Debt

Subordinated debt represents our direct unsecured obligations, in the form of notes and debentures, to our debt holders and forms part of our regulatory capital. The rights of the holders of our notes and debentures are subordinate to the claims of depositors and certain other creditors. We require approval from the Superintendent of Financial Institutions Canada before we can redeem any part of our subordinated debt.

### Change in Accounting Policy

See Note 20 for discussion of a change in accounting policy affecting our capital trust securities included in non-controlling interest in subsidiaries, which was effective November 1, 2004.

### Customer Loyalty Program

We record the liability associated with our credit card customer loyalty program rewards in the period in which our customers become entitled to redeem the rewards. We estimate the liability using the expected future redemption rate and apply the cost of expected redemptions. Our estimate of the expected redemption rate is based on statistical analysis of past customer behaviour. The costs of our loyalty program are recorded as a reduction in non-interest revenue – card fees in the Consolidated Statement of Income. The liability is included in other liabilities in the Consolidated Balance Sheet.

### Change in Accounting Estimate

During the years ended October 31, 2005 and 2004, we increased the estimate of the liability associated with our credit card customer loyalty program. The change in estimate during fiscal 2005 was due to further refinements made to the methodology used to determine the liability. The change in estimate during 2004 was due to rising reward redemption rates. The impact of this change on our Consolidated Statement of Income for the year ended October 31, 2005 was a reduction in non-interest revenue – card fees of \$40 million, a decrease in income taxes of \$14 million and a decrease in net income of \$26 million (\$65 million, \$23 million and \$42 million, respectively, for the year ended October 31, 2004).

The term to maturity and repayments of our subordinated debt required over the next five years and thereafter are as follows:

(Canadian \$ in millions, except as noted)	Face value	Maturity date	Interest rate (%)	Redeemable at our option beginning in	1 year	2 years	3 years	4 years	5 years	Over 5 years	2005 Total	2004 Total
					\$	\$	\$	\$	\$	\$	\$	
Debentures Series 12	\$ 140	December 2008	10.85	December 1998	\$ –	\$ –	\$ –	\$ 140	\$ –	\$ –	\$ 140	\$ 140
Debentures Series 16	\$ 100	February 2017	10.00	February 2012	–	–	–	–	–	100	100	100
Debentures Series 18	\$ 250	September 2010	8.80	redeemed	–	–	–	–	–	–	–	250
Debentures Series 19	\$ 125	March 2011	7.40	March 2006	–	–	–	–	–	125	125	125
Debentures Series 20	\$ 150	December 2025 to 2040	8.25	not redeemable	–	–	–	–	–	150	150	150
Debentures Series 21	\$ 300	May 2011	8.15	May 2006	–	–	–	–	–	300	300	300
Debentures Series 22	\$ 150	July 2012	7.92	July 2007	–	–	–	–	–	150	150	150
6.10% Notes	US\$ 300	September 2005	6.10	September 1998 (1)	–	–	–	–	–	–	–	365
7.80% Notes	US\$ 300	April 2007	7.80	April 2000 (1)	–	354	–	–	–	–	354	365
Series A Medium-Term Notes												
2nd Tranche	\$ 150	February 2013	5.75	February 2008	–	–	–	–	–	150	150	150
Series B Medium-Term Notes	\$ 300	June 2010	6.60	redeemed	–	–	–	–	–	–	–	300
Series C Medium-Term Notes												
1st Tranche	\$ 500	January 2015	4.00	January 2010 (2)	–	–	–	–	–	500	500	–
2nd Tranche	\$ 500	April 2020	4.87	April 2015 (3)	–	–	–	–	–	500	500	–
<b>Total</b>					<b>\$ –</b>	<b>\$ 354</b>	<b>\$ –</b>	<b>\$ 140</b>	<b>\$ –</b>	<b>\$ 1,975</b>	<b>\$ 2,469</b>	<b>\$ 2,395</b>

(1) Redeemable at our option only if certain tax events occur.

(2) Redeemable at the greater of par and the Canada Yield Price prior to January 21, 2010, and redeemable at par commencing January 21, 2010.

(3) Redeemable at the greater of par and the Canada Yield Price prior to April 22, 2015, and redeemable at par commencing April 22, 2015.

## Note 18 ▶ Capital Trust Securities

We issue BMO Capital Trust Securities (“BOaTS”) through our consolidated subsidiary BMO Capital Trust (the “Trust”). The proceeds of the BOaTS are used to purchase mortgages. Upon consolidation, the BOaTS are reported in our Consolidated Balance Sheet either as non-controlling interest in subsidiaries or as other liabilities, depending on the terms of the BOaTS. Holders of the

BOaTS are entitled to receive semi-annual non-cumulative fixed cash distributions as long as the Bank declares dividends on its preferred shares, or if no such shares are outstanding, on its common shares in accordance with ordinary Bank dividend practice. The terms of the BOaTS are as follows:

(Canadian \$ in millions, except Distribution)	Distribution dates	Distribution per BMO BOaTS	Redemption date	Conversion date	Principal amount	
			At the option of the Trust	At the option of the holder	2005	2004
<b>Other Liabilities</b>						
Series A	June 30, December 31	\$ 34.52	December 31, 2005	December 31, 2010	\$ 350	\$ 350
Series B	June 30, December 31	33.24	June 30, 2006	June 30, 2011	400	400
Series C	June 30, December 31	33.43	December 31, 2006	June 30, 2012	400	400
					<b>1,150</b>	1,150
<b>Non-Controlling Interest</b>						
Series D	June 30, December 31	\$ 27.37 <sup>(1)</sup>	December 31, 2009		600	600
Series E	June 30, December 31	23.17 <sup>(2)</sup>	December 31, 2010		450	—
					<b>1,050</b>	600
<b>Total Capital Trust Securities</b>					<b>\$ 2,200</b>	\$ 1,750

(1) After December 31, 2014, the distribution will be at the Bankers' Acceptance Rate plus 1.5%.

(2) After December 31, 2015, the distribution will be at the Bankers' Acceptance Rate plus 1.5%.

### Redemption by the Trust

On or after the redemption dates indicated above, and subject to the prior approval of the Superintendent of Financial Institutions Canada, the Trust may redeem the BOaTS in whole without the consent of the holders.

### Conversion by the Holder

On or after the conversion dates indicated above, the BOaTS Series A, B and C may be exchanged for the Bank's Class B Preferred shares Series 7, 8 and 9, respectively, at the option of the holder.

### Automatic Exchange

The BOaTS Series A, B, C, D and E will be automatically exchanged for 40 of the Bank's Class B Preferred shares Series 7, 8, 9, 11 and 12, respectively, without the consent of the holder on the occurrence of specific events such as a wind-up of Bank of Montreal, a regulatory requirement to increase capital and violations of regulatory capital requirements.

### Change in Accounting Policy

On November 1, 2004, we adopted the CICA's new accounting requirements on the classification of financial instruments as liabilities or equity. The new rules require that our capital trust securities, which are ultimately convertible into a variable number of our common shares at the holders' option, be classified as liabilities. We reclassified \$1,150 million of our capital trust securities, Series A, B and C, previously recorded as non-controlling interest in subsidiaries in other liabilities, to capital trust securities. The distributions made on those capital trust securities are now recorded as interest expense.

We have restated prior years' consolidated financial statements to be consistent with the new presentation. See Note 20 for the impact of this change in accounting policy on our consolidated financial statements.

## Note 19 ▶ Interest Rate Risk

We earn interest on interest bearing assets and we pay interest on interest bearing liabilities. We also have off-balance sheet financial instruments whose values are sensitive to changes in interest rates. To the extent that we have assets, liabilities and financial instruments maturing or repricing at different points in time, we are exposed to interest rate risk.

### Interest Rate Gap Position

The determination of the interest rate sensitivity or gap position by necessity encompasses numerous assumptions. It is based on the earlier of the repricing or maturity date of assets, liabilities and derivatives used to manage interest rate risk.

The gap position presented is as at October 31 of each year. It represents the position outstanding at the close of the business day and may change significantly in subsequent periods based on customer behaviours and the application of our asset and liability management policies.

The assumptions for 2005 were as follows:

#### Assets

Fixed term assets, such as residential mortgage loans and consumer loans, are reported based upon the scheduled repayments and estimated prepayments that reflect expected borrower behaviour.

Trading and underwriting (mark-to-market) assets and interest bearing assets on which the customer interest rate changes with the prime rate or other short-term market rates are reported in the zero to three months category.

Fixed rate and non-interest bearing assets with no defined maturity are reported based upon expected account balance behaviour.

#### Deposits/Liabilities

Fixed rate liabilities, such as investment certificates, are reported at scheduled maturity with estimated redemptions that reflect expected depositor behaviour.

Interest bearing deposits on which the customer interest rate changes with the prime rate or other short-term market rates are reported in the zero to three months category.

Fixed rate and non-interest bearing liabilities with no defined maturity are reported based upon expected account balance behaviour.

#### Capital

Common shareholders' equity is reported as non-interest sensitive.

#### Yields

Yields are based upon the contractual interest rates in effect for the assets or liabilities on October 31, 2005.

#### Interest Rate Gap Position

(Canadian \$ in millions)

As at October 31	0 to 3 months	4 to 6 months	7 to 12 months	Total within 1 year	Effective interest rate (%)	1 to 5 years	Effective interest rate (%)	Over 5 years	Effective interest rate (%)	Non-interest sensitive	Total
<b>Canadian Dollar</b>											
<b>Assets</b>											
Cash resources	\$ 2,238	\$ 292	\$ –	\$ 2,530	3.09	\$ 294	–	\$ –	–	\$ (154)	\$ 2,670
Securities	27,599	72	252	27,923	3.07	785	6.82	68	5.10	169	28,945
Securities borrowed or purchased under resale agreements	16,084	78	–	16,162	2.96	–	–	–	–	–	16,162
Loans	59,317	3,461	5,962	68,740	5.00	32,580	5.60	2,731	5.45	5,891	109,942
Other assets	34,277	253	507	35,037	na	4,056	na	–	na	–	39,093
<b>Total assets</b>	<b>139,515</b>	<b>4,156</b>	<b>6,721</b>	<b>150,392</b>		<b>37,715</b>		<b>2,799</b>		<b>5,906</b>	<b>196,812</b>
<b>Liabilities and Shareholders' Equity</b>											
Deposits	59,794	4,744	8,278	72,816	2.18	38,658	2.24	1,985	4.65	–	113,459
Securities sold but not yet purchased	15,323	–	–	15,323	3.00	–	–	–	–	–	15,323
Securities lent or sold under repurchase agreements	8,877	–	–	8,877	2.93	–	–	–	–	–	8,877
Other liabilities	32,828	114	227	33,169	na	1,817	na	1,050	na	5,891	41,927
Subordinated debt	–	125	300	425	7.93	1,740	5.70	1,550	6.46	–	3,715
Shareholders' equity	26	–	–	26	na	–	na	200	na	13,285	13,511
<b>Total liabilities and shareholders' equity</b>	<b>116,848</b>	<b>4,983</b>	<b>8,805</b>	<b>130,636</b>		<b>42,215</b>		<b>4,785</b>		<b>19,176</b>	<b>196,812</b>
On-balance sheet gap position	22,667	(827)	(2,084)	19,756		(4,500)		(1,986)		(13,270)	–
Off-balance sheet gap position	(18,731)	1,728	1,705	(15,298)		11,523		3,775		–	–
<b>Total Canadian dollar interest rate gap position</b>											
<b>2005</b>	<b>\$ 3,936</b>	<b>\$ 901</b>	<b>\$ (379)</b>	<b>\$ 4,458</b>		<b>\$ 7,023</b>		<b>\$ 1,789</b>		<b>\$(13,270)</b>	<b>\$ –</b>
2004	2,379	990	772	4,141		7,030		972		(12,143)	–

#### U.S. Dollar and Other Currencies

##### Assets

Cash resources	\$ 9,898	\$ 4,618	\$ 3,292	\$ 17,808	1.38	\$ (122)	3.55	\$ –	–	\$ 365	\$ 18,051
Securities	20,400	1,195	1,785	23,380	0.37	4,582	0.28	298	0.98	51	28,311
Securities borrowed or purchased under resale agreements	11,446	–	672	12,118	0.61	–	–	–	–	–	12,118
Loans	22,635	1,016	1,725	25,376	0.94	8,812	0.70	1,329	0.07	598	36,115
Other assets	1,514	236	413	2,163	na	3,959	na	–	na	3	6,125
<b>Total assets</b>	<b>65,893</b>	<b>7,065</b>	<b>7,887</b>	<b>80,845</b>		<b>17,231</b>		<b>1,627</b>		<b>1,017</b>	<b>100,720</b>
<b>Liabilities and Shareholders' Equity</b>											
Deposits	60,564	3,308	2,526	66,398	2.69	13,733	0.33	170	0.16	33	80,334
Securities sold but not yet purchased	819	–	–	819	3.61	–	–	–	–	–	819
Securities lent or sold under repurchase agreements	13,778	1	1	13,780	0.53	–	–	–	–	–	13,780
Other liabilities	3,795	(101)	44	3,738	na	742	na	–	na	598	5,078
Subordinated debt	–	–	–	–	–	354	7.80	–	–	–	354
Shareholders' equity	–	–	–	–	na	–	na	355	na	–	355
<b>Total liabilities and shareholders' equity</b>	<b>78,956</b>	<b>3,208</b>	<b>2,571</b>	<b>84,735</b>		<b>14,829</b>		<b>525</b>		<b>631</b>	<b>100,720</b>
On-balance sheet gap position	(13,063)	3,857	5,316	(3,890)		2,402		1,102		386	–
Off-balance sheet gap position	1,177	(109)	(260)	808		(99)		(709)		–	–
<b>Total U.S. dollar and other currencies interest rate gap position</b>											
<b>2005</b>	<b>\$ (11,886)</b>	<b>\$ 3,748</b>	<b>\$ 5,056</b>	<b>\$ (3,082)</b>		<b>\$ 2,303</b>		<b>\$ 393</b>		<b>\$ 386</b>	<b>\$ –</b>
2004	(13,227)	3,526	4,650	(5,051)		2,082		2,802		167	–

na – not applicable

## Note 20 ▶ Share Capital

### Outstanding

(Canadian \$ in millions, except as noted)

	2005			2004			2003		
	Number of shares	Amount	Dividends declared per share	Number of shares	Amount	Dividends declared per share	Number of shares	Amount	Dividends declared per share
<b>Preferred Shares – Classified as Liabilities</b>									
Class B – Series 3	–	\$ –	\$ –	–	\$ –	\$ 1.18	16,000,000	\$ 400	\$ 1.39
Class B – Series 4	8,000,000	200	1.20	8,000,000	200	1.20	8,000,000	200	1.20
Class B – Series 6	10,000,000	250	1.19	10,000,000	250	1.19	10,000,000	250	1.19
<b>Preferred Shares – Classified as Liabilities</b>		<b>450</b>			<b>450</b>			<b>850</b>	
<b>Preferred Shares – Classified as Equity</b>									
Class B – Series 5	8,000,000	\$ 200	\$ 1.33	8,000,000	\$ 200	\$ 1.33	8,000,000	\$ 200	\$ 1.33
Class B – Series 10	12,000,000	396	US\$ 1.49	12,000,000	396	US\$ 1.49	12,000,000	396	US\$ 1.49
<b>Preferred Shares – Classified as Equity</b>		<b>596</b>			<b>596</b>			<b>596</b>	
<b>Common Shares</b>	<b>500,219,068</b>	<b>4,022</b>	<b>\$ 1.85</b>	500,896,857	3,857	\$ 1.59	499,632,368	3,662	\$ 1.34
Share Capital		<b>\$ 4,618</b>			\$ 4,453			\$ 4,258	

### Preferred Shares

We are authorized by our shareholders to issue an unlimited number of Class A Preferred shares and Class B Preferred shares without par value, in series, for unlimited consideration. Class B Preferred shares may be issued in a foreign currency.

During the year ended October 31, 2004, we redeemed all of our Class B Preferred shares, Series 3, at a price of \$25.50 per share plus any declared and unpaid dividends. The excess of the redemption price over carrying value of \$8 million was charged to retained earnings in preferred share dividends.

### Preferred Share Rights and Privileges

Class B – Series 4 shares are redeemable at our option starting August 25, 2005 for \$25.00 cash per share, plus a premium if we redeem the shares before August 25, 2007, or an equivalent value of our common shares. They are convertible at the shareholder's option starting May 25, 2008 into our common shares; however, we have the right to pay \$25.00 cash per share instead. The shares carry a non-cumulative quarterly dividend of \$0.30 per share.

Class B – Series 5 shares are redeemable at our option starting February 25, 2013 for \$25.00 cash per share, and are not convertible. The shares carry a non-cumulative quarterly dividend of \$0.33125 per share.

Class B – Series 6 shares are redeemable at our option starting November 25, 2005 for \$25.00 cash per share, plus a premium if we redeem the shares before November 25, 2007, or an equivalent value of our common shares. They are convertible at the shareholder's option starting November 25, 2008 into our common shares; however, we have the right to pay \$25.00 cash per share instead. The shares carry a non-cumulative quarterly dividend of \$0.296875 per share.

Class B – Series 10 shares are redeemable at our option starting February 25, 2012 for US\$25.00 cash per share, and are convertible at our option starting February 25, 2012 into our common shares. The shares carry a non-cumulative quarterly dividend of US\$0.371875 per share.

### Common Shares

We are authorized by our shareholders to issue an unlimited number of our common shares, without par value, for unlimited consideration. Our common shares are not redeemable or convertible. Dividends are declared by us on a quarterly basis and the amount can vary from quarter to quarter.

### Normal Course Issuer Bid

On September 7, 2005, we commenced a normal course issuer bid, effective for one year. Under this bid, we may repurchase up to 15,000,000 common shares, approximately 3% of our outstanding common shares.

We participated in a normal course issuer bid during the period from August 10, 2004 to August 6, 2005, under which we were able to repurchase up to 15,000,000 common shares, approximately 3% of our then outstanding common shares.

During the year ended October 31, 2005, we repurchased 6,957,800 shares at an average cost of \$56.04 per share, totalling \$390 million. During the year ended October 31, 2004, we repurchased 6,220,500 shares at an average cost of \$53.63 per share, totalling \$333 million.

### Issuances Exchangeable into Common Shares

One of our subsidiaries, Bank of Montreal Securities Canada Limited ("BMSCL"), has issued various classes of non-voting shares that can be exchanged at the option of the holder for our common shares, based on a formula. If all of these BMSCL shares had been converted into our common shares, up to 361,397, 646,383 and 771,212 of our common shares would have been needed to complete the exchange as at October 31, 2005, 2004 and 2003, respectively.

### Share Redemption and Dividend Restrictions

The Superintendent of Financial Institutions Canada must approve any plan to redeem any of our preferred share issues for cash.

We are prohibited from declaring dividends on our preferred or common shares when we would be, as a result of paying such a dividend, in contravention of the capital adequacy, liquidity or any other regulatory directives issued under the *Bank Act*. In addition, common share dividends cannot be paid unless all dividends declared and payable on our preferred shares have been paid or sufficient funds have been set aside to do so.

In addition, we have agreed that if BMO Capital Trust, one of our subsidiaries, fails to pay any required distribution on its capital trust securities, we will not declare dividends of any kind on any of our preferred or common shares for a period of time following the Trust's failure to pay the required distribution (as defined in the capital trust securities' prospectuses) unless the Trust first pays such distribution to the holders of capital trust securities (see Note 18).

### Shareholder Dividend Reinvestment and Share Purchase Plan

We offer a dividend reinvestment and share purchase plan for our shareholders. Participation in the plan is optional. Under the terms of the plan, cash dividends on common shares are reinvested to purchase additional common shares. Shareholders also have the

opportunity to make optional cash payments to acquire additional common shares. We may issue these common shares at an average of the closing prices of the Bank's common shares on the Toronto Stock Exchange based on the five trading days prior to the last business day of the month or we may purchase them on the open market at market price. During the year, we issued a total of 1,258,463 common shares (1,120,931 in 2004) under the plan.

#### Potential Share Issuances

As at October 31, 2005, we had reserved 4,646,625 common shares for potential issuance in respect of our Shareholder Dividend Reinvestment and Share Purchase Plan and 5,081,508 common shares in respect of the exchange of certain shares of BMSCL. We also have reserved 30,169,925 common shares for the potential exercise of stock options, as further described in Note 21.

#### Issued on the Acquisition of a Business

In 2003, 634,551 common shares at a value of \$27 million were issued in connection with the acquisition of Gerard Klauer Mattison & Co., Inc.

#### Change in Accounting Policy

On November 1, 2004, we adopted the CICA's new accounting requirements on the classification of financial instruments as liabilities or equity. The new rules require that our preferred shares and capital trust securities, which are ultimately convertible into a variable number of our common shares at the holders' option, be classified as liabilities. We reclassified \$450 million of our Class B Preferred shares Series 4 and 6 from share capital to preferred share liability. In addition, we also reclassified \$1,150 million of our capital trust securities, Series A, B and C, previously recorded as

non-controlling interest in subsidiaries in other liabilities, to capital trust securities. The dividends declared on those preferred shares as well as the distributions made on those capital trust securities are now recorded as interest expense. This change did not impact earnings per share or net income available to common shareholders since preferred share dividends are deducted from net income in determining those measures.

We have restated prior years' consolidated financial statements to be consistent with the new presentation. The impact of this change in accounting policy on our consolidated financial statements for the current and prior years is as follows:

(Canadian \$ in millions)	2005	2004	2003
Increase (decrease)			
<b>Consolidated Statement of Income</b>			
Interest Expense – Preferred shares and capital trust securities	\$ (97)	\$ (124)	\$ (122)
Non-controlling interest in subsidiaries	42	43	42
Income taxes	37	36	36
Net Income	(18)	(45)	(44)
Preferred share dividends	18	45	44
Net income available to common shareholders	\$ –	\$ –	\$ –
Increase (decrease)			
<b>Consolidated Balance Sheet</b>			
Preferred Share Liability	\$ 450	\$ 450	\$ 850
Capital Trust Securities	1,150	1,150	1,150
Other Liabilities	(1,150)	(1,150)	(1,150)
Share capital	(450)	(450)	(850)

## Note 21 ▶ Employee Compensation – Stock-Based Compensation

#### Stock Option Plan

We maintain a Stock Option Plan for designated officers, employees and directors. The options granted under the plan from 1995 to 1999 all vest five fiscal years from November 1 of the year in which the options were granted to the officer or employee, if we have met

certain performance targets. The options granted since 1999 vest 25% per year over a four-year period starting from their grant date. A portion of the options granted since 1999 can only be exercised once certain performance targets are met. All options expire 10 years from the date they are granted.

The following table summarizes information about our Stock Option Plan:

(Canadian \$, except as noted)	2005		2004		2003	
	Number of stock options	Weighted-average exercise price	Number of stock options	Weighted-average exercise price	Number of stock options	Weighted-average exercise price
Outstanding at beginning of year	30,442,060	\$ 33.87	35,212,440	\$ 31.89	38,374,627	\$ 30.21
Granted	1,471,764	56.60	1,645,900	53.93	2,244,800	40.90
Exercised	4,736,826	29.30	6,239,301	27.77	5,325,916	23.45
Forfeited/cancelled	257,649	36.77	176,979	35.22	81,071	34.00
Outstanding at end of year	26,919,349	35.86	30,442,060	33.87	35,212,440	31.89
Exercisable at end of year	20,016,144	32.68	21,102,433	30.94	13,337,147	28.29
Available for grant	3,397,576		4,611,691		6,080,612	
Outstanding stock options as a % of outstanding shares	5.38%		6.08%		7.05%	

No stock options expired during the years ended October 31, 2005, 2004 and 2003.

Options outstanding and options exercisable as at October 31, 2005 by range of exercise price are as follows:

(Canadian \$, except as noted)	Options outstanding			Options exercisable		
Range of exercise prices	Number of stock options	Weighted-average remaining contractual life (years)	Weighted-average exercise price	Number of stock options	Weighted-average exercise price	
\$15.50 to \$20.00	690,304	0.8	\$ 19.18	690,304	\$ 19.18	
\$20.01 to \$30.00	4,280,516	4.0	\$ 25.60	4,280,516	\$ 25.60	
\$30.01 to \$40.00	16,665,861	4.7	\$ 34.99	14,182,457	\$ 34.78	
\$40.01 to \$56.60	5,282,668	7.7	\$ 49.10	862,867	\$ 44.03	

**Change in Accounting Policy**

On November 1, 2002, we changed our accounting policy for stock options granted on or after that date. Under the new policy, we determine the fair value of stock options on their grant date and record this amount as compensation expense over the period that the stock options vest, with a corresponding increase to contributed surplus. When these stock options are exercised, we record the amount of proceeds, together with the amount recorded in contributed surplus, in share capital.

We determine the fair value of options granted using a trinomial option pricing model. The weighted-average fair value of options granted during the years ended October 31, 2005, 2004 and 2003 was \$10.34, \$10.63 and \$7.85, respectively. The following weighted-average assumptions were used to determine the fair value of options on the date of grant:

	2005	2004	2003
Expected dividend yield	3.1%	2.6%	3.2%
Expected share price volatility	22.8%	23.2%	23.4%
Risk-free rate of return	4.2%	4.8%	4.8%
Expected period until exercise	7.1 years	7.1 years	7.1 years

Changes to the input assumptions can result in materially different fair value estimates.

We do not record any compensation expense for stock options granted in prior years. When these stock options are exercised, we include the amount of proceeds in share capital. The impact on our net income and earnings per share if we had always recorded stock option expense based on the fair value of all of our outstanding stock options on their grant date is as follows:

(Canadian \$ in millions, except as noted)	2005	2004	2003
Stock option expense included in employee compensation expense	\$ 10	\$ 7	\$ 3
Net income, as reported	\$ 2,400	\$ 2,306	\$ 1,781
Additional expense that would have been recorded if we had expensed the fair value of all outstanding stock options granted before November 1, 2002	11	29	43
Net income, pro forma	\$ 2,389	\$ 2,277	\$ 1,738
Earnings per share (Canadian \$)			
Basic, as reported	\$ 4.74	\$ 4.53	\$ 3.51
Basic, pro forma	4.72	4.48	3.43
Diluted, as reported	4.64	4.42	3.44
Diluted, pro forma	4.62	4.36	3.35

**Other Stock-Based Compensation Plans***Share Purchase Plan*

We offer our employees the option of contributing a portion of their gross salary toward the purchase of our common shares. For employee contributions up to 6% of their individual gross salaries, we match 50% of their contributions. The shares in the employee share purchase plan are purchased on the open market and are considered outstanding for purposes of computing earnings per share. The dividends earned on Bank common shares held by the employee share purchase plan are used to purchase additional common shares on the open market.

We account for our contribution as employee compensation expense when it is contributed to the plan.

Employee compensation expense related to this plan for the years ended October 31, 2005, 2004 and 2003 was \$33 million, \$32 million and \$29 million, respectively. There were 12,184,377, 11,445,595 and 10,676,918 common shares outstanding held in this plan for the years ended October 31, 2005, 2004 and 2003, respectively.

*Mid-Term Incentive Plans*

We offer mid-term incentive plans for executives and certain senior employees. Depending on the plan, these pay either a single cash payment at the end of the three-year period of the plan, or three annual cash payments in each of the three years of the plan. The amount of the incentive payment is adjusted to reflect dividends and changes in the market value of our common shares. For the majority of executives and some senior employee grants, a portion of the incentive payment also varies based on performance targets driven by annualized total shareholder return compared with that of our competitors.

We entered into agreements with third parties to assume most of our obligations related to these plans in exchange for cash payments of \$187 million, \$173 million and \$105 million in the years ended October 31, 2005, 2004 and 2003, respectively. Amounts paid under these agreements were recorded in the Consolidated Balance Sheet in other assets and are recorded as employee compensation expense evenly over the period until payment to employees. We no longer have any liability related to these plans because any future payments required will be the responsibility of the third parties. The amount deferred and recorded in other assets in our Consolidated Balance Sheet totalled \$142 million and \$133 million as at October 31, 2005 and 2004, respectively.

For the remaining obligations relating to plans for which we have not entered into agreements with third parties, the amount of compensation expense is amortized over the period until payment to employees to reflect the current market value of our common shares and our total shareholder return compared with that of our competitors.

Employee compensation expense related to these plans for the years ended October 31, 2005, 2004 and 2003 was \$169 million, \$143 million and \$97 million, respectively.

*Deferred Bonus Plans*

We offer deferred bonus plans for certain senior executives and certain key employees in our Investment Banking and Private Client Groups. Under these plans, payment of annual incentive payments and/or commissions can be deferred as stock units of our common shares. The amount of deferred incentive payments and/or commissions is adjusted to reflect dividends and changes in the market value of our common shares.

Depending on the plan, deferred incentive payments can be paid either upon retirement/resignation, over the three-year period of the plan or at the end of the three-year period of the plan. The deferred incentive payments can be paid in cash, shares or a combination of both.

Employee compensation expense for these plans is recorded in the year the incentive payment and/or commission is earned. Changes in the amount of the incentive payment payable as a result of dividends and share price movements are recorded as employee compensation expense in the period of the change.

We have entered into derivative instruments in order to hedge our exposure to these plans. Changes in the fair value of these derivatives are recorded as employee compensation expense in the period in which they arise.

Liabilities related to these plans were recorded in other liabilities in our Consolidated Balance Sheet and totalled \$177 million and \$218 million as at October 31, 2005 and 2004, respectively.

Employee compensation expense related to these plans for the years ended October 31, 2005, 2004 and 2003 was \$4 million, \$4 million and \$26 million, respectively, net of the impact of hedging.

**Pension and Other Employee Future Benefit Plans**

We have a number of arrangements in Canada, the United States and the United Kingdom that provide pension and other employee future benefits to our retired and current employees.

Pension arrangements include defined benefit statutory pension plans as well as supplemental arrangements, which provide pension benefits in excess of statutory limits. Generally, under these plans we provide retirement benefits based on an employee’s years of service and average annual earnings over a period of time prior to retirement. We are responsible for ensuring that the statutory pension plans have sufficient assets to pay the pension benefits upon retirement of employees. Voluntary contributions can be made by employees but are not required.

We also provide defined contribution pension plans to employees in some of our subsidiaries. Under these plans, we are responsible for contributing a predetermined amount to a participant’s retirement savings, based on a percentage of that employee’s salary. We recognize the cost of our defined contribution pension plans in employee compensation expense as the employees work for us.

We also provide other employee future benefits, including health and dental care benefits and life insurance for current and retired employees.

**Pension and Other Employee Future Benefit Liabilities**

We have two types of benefit liabilities: our defined benefit pension liabilities and our other employee future benefit liabilities. These benefit liabilities represent the amount of pension and other employee future benefits that our employees and retirees have earned as at year end.

Our actuaries perform valuations of our benefit liabilities for pension and other employee future benefits as at October 31 of each year for our Canadian plans (September 30 for our U.S. plans), using the projected benefit method prorated on service, based on management’s assumptions about discount rates, salary growth, retirement age, mortality and health care cost trend rates. The discount rate is determined by management with reference to market conditions at year end. Other assumptions are determined with reference to long-term expectations.

Components of the change in our benefit liabilities year over year and our pension and other employee future benefit expense are as follows:

**Benefits earned by employees** represent benefits earned in the current year. They are determined with reference to the current workforce and the amount of benefits to which they will be entitled upon retirement, based on the provisions of our benefit plans.

**Interest cost on the benefit liabilities** represents the increase in the liability that results from the passage of time.

**Actuarial gains or losses** may arise in two ways. First, each year our actuaries recalculate the benefit liabilities and compare them to those estimated as at the prior year end. Any differences that result from changes in assumptions or from plan experience being different from what was expected by management at the previous year end are considered actuarial gains or losses.

Secondly, actuarial gains and losses arise when there are differences between expected and actual returns on plan assets.

At the beginning of each year, we determine whether the unrecognized actuarial gain or loss is more than 10% of the greater of our plan asset or benefit liability balances. Any unrecognized actuarial gain or loss in excess of this 10% threshold is recognized in expense over the remaining service period of active employees. Amounts below the 10% threshold are not recognized in income.

**Plan amendments** are changes in our benefit liabilities as a result of changes to provisions of the plans. These amounts are recognized in expense over the remaining service period of active employees.

**Expected return on assets** represents management’s best estimate of the long-term rate of return on plan assets applied to the fair value of plan assets. We establish our estimate of the expected rate of return on plan assets based on the fund’s target asset allocation and estimated rates of return for each asset class. Estimated rates of return are based on expected returns from fixed income securities, which take into consideration bond yields. An equity risk premium is then applied to estimate equity returns. Returns from other asset classes are set to reflect the relative risks of these classes as compared to fixed income and equity assets. Differences between expected and actual return on assets are included in our actuarial gain or loss balance, as described above.

**Settlements** occur when benefit liabilities for plan participants are settled, usually through lump sum cash payments, and as a result we no longer have a liability to provide them with benefit payments in the future.

**Funding of Pension and Other Employee Future Benefit Plans**

We make cash contributions to our statutory pension plans. The actual and target asset allocations are set out on the following page. The investment policy for the main Canadian pension plan assets is to have a diversified mix of quality investments that is expected to provide a superior real rate of return over the long term, while limiting performance volatility. We also have a retirement compensation arrangement that partially funds supplemental pension benefits in Canada. However, pension payments related to this plan are paid directly by the Bank. Retirement benefits for our supplemental plans in the United States are also paid directly by the Bank. Our other employee future benefit liability in the United States is partially funded; and our other employee future benefit liability in Canada is unfunded. Benefits in connection with our other employee future benefit plans are paid directly by the Bank.

We measure the fair value of plan assets as at October 31 for our Canadian plans (September 30 for our U.S. plans). In addition to actuarial valuations for accounting purposes, we are required to prepare valuations for determining our pension contributions (our “funding valuation”). The most recent funding valuation for our main Canadian plan was performed as at October 31, 2005. We are required to file funding valuations for that plan with the Office of the Superintendent of Financial Institutions Canada at least every three years. An annual funding valuation is required for our U.S. statutory plan. The most recent valuation was performed as at January 1, 2005.

The benefit liability and the fair value of plan assets in respect of plans that are not fully funded are as follows:

(Canadian \$ in millions)	Pension benefit plans			Other employee future benefit plans		
	2005	2004	2003	2005	2004	2003
Accrued benefit liability	\$ 959	\$ 865	\$ 883	\$ 852	\$ 741	\$ 711
Fair value of plan assets	693	607	544	66	58	55
Unfunded benefit liability	\$ 266	\$ 258	\$ 339	\$ 786	\$ 683	\$ 656

**Asset Allocations**

Plan assets are rebalanced within ranges around target allocations. Allocations as at the end of each year and the target allocations for October 31 are as follows:

	Funded pension benefit plans (1)				Funded other employee future benefit plans			
	Target 2005	Actual 2005	Actual 2004	Actual 2003	Target 2005	Actual 2005	Actual 2004	Actual 2003
Equities	51%	<b>50%</b>	47%	45%	65%	<b>67%</b>	70%	61%
Fixed income investments	35%	<b>38%</b>	40%	42%	35%	<b>33%</b>	30%	30%
Other	14%	<b>12%</b>	13%	13%	–	–	–	9%

(1) Excludes the Canadian supplementary plan whose assets are fully invested in fixed income investments.

**Pension and Other Employee Future Benefit Expenses**

Pension and other employee future benefit expenses are determined as follows:

(Canadian \$ in millions, except as noted)	Pension benefit plans			Other employee future benefit plans		
	2005	2004	2003	2005	2004	2003
<b>Annual Benefits Expense</b>						
Benefits earned by employees	<b>\$ 127</b>	\$ 120	\$ 111	<b>\$ 17</b>	\$ 16	\$ 17
Interest cost on accrued benefit liability	<b>205</b>	201	196	<b>46</b>	44	38
Actuarial loss recognized in expense	<b>69</b>	77	62	<b>10</b>	10	–
Amortization of plan amendment costs	<b>4</b>	2	3	<b>(7)</b>	(7)	–
Loss realized on settlement of a portion of the benefit liability	<b>–</b>	–	4	<b>–</b>	–	–
Expected return on plan assets	<b>(230)</b>	(213)	(217)	<b>(5)</b>	(4)	(4)
Annual benefits expense	<b>175</b>	187	159	<b>61</b>	59	51
Canada and Quebec pension plan expense	<b>45</b>	45	44	<b>–</b>	–	–
Defined contribution expense	<b>11</b>	11	10	<b>–</b>	–	–
Total annual pension and other employee future benefit expenses recognized in the Consolidated Statement of Income	<b>\$ 231</b>	\$ 243	\$ 213	<b>\$ 61</b>	\$ 59	\$ 51

**The impact on annual benefits expense if we had recognized all costs and expenses as they arose**

Total annual pension and other employee future benefit expenses recognized in the Consolidated Statement of Income	<b>\$ 231</b>	\$ 243	\$ 213	<b>\$ 61</b>	\$ 59	\$ 51
(Excess) of actual returns over expected returns on plan assets	<b>(141)</b>	(118)	(6)	<b>(5)</b>	(4)	(6)
(Excess) shortfall of actuarial (gains) losses amortized over actuarial (gains) losses arising	<b>320</b>	1	97	<b>59</b>	(10)	170
(Excess) shortfall of plan amendment costs amortized over plan amendment costs arising	<b>11</b>	17	(3)	<b>7</b>	7	(66)
Total pro forma annual pension and other employee future benefit costs if we had recognized all costs and benefits during the year	<b>\$ 421</b>	\$ 143	\$ 301	<b>\$ 122</b>	\$ 52	\$ 149

**Weighted-average assumptions used to determine benefit expenses**

Estimated average service period of active employees (in years)	<b>10</b>	10	11	<b>12</b>	13	14
Discount rate at beginning of year	<b>6.0%</b>	6.2%	6.5%	<b>6.2%</b>	6.4%	6.7%
Expected long-term rate of return on plan assets	<b>6.7%</b>	6.7%	6.9%	<b>8.0%</b>	8.0%	8.0%
Rate of compensation increase	<b>3.9%</b>	4.0%	4.2%	<b>3.9%</b>	4.1%	3.7%
Assumed overall health care cost trend rate	<b>na</b>	na	na	<b>8.0%</b> (1)	8.4%(1)	5.3%(2)

(1) Trending to 4.5% in 2013 and remaining at that level thereafter.

(2) Trending to 4.4% in 2013 and remaining at that level thereafter.

na – not applicable

Changes in the estimated financial positions of our pension benefit plans and other employee future benefit plans are as follows:

(Canadian \$ in millions, except as noted)	Pension benefit plans			Other employee future benefit plans		
	2005	2004	2003	2005	2004	2003
<b>Benefit liability</b>						
Benefit liability at beginning of year	\$ 3,479	\$ 3,300	\$ 3,157	\$ 741	\$ 711	\$ 595
Benefits earned by employees	127	120	111	17	16	17
Interest cost on benefit liability	205	201	196	46	44	38
Benefits paid to pensioners and employees	(185)	(190)	(195)	(19)	(23)	(25)
Voluntary employee contributions	6	5	5	—	—	—
Loss on the benefit liability arising from changes in assumptions (a)	389	78	159	69	—	170
Plan amendments	15	19	—	—	—	(66)
Reduction in liability due to partial settlement	—	—	(15)	—	—	—
Other, primarily foreign exchange	(23)	(54)	(118)	(2)	(7)	(18)
Benefit liability at end of year	\$ 4,013	\$ 3,479	\$ 3,300	\$ 852	\$ 741	\$ 711
<b>Weighted-average assumptions used to determine the benefit liability</b>						
Discount rate at end of year	5.3%	6.0%	6.2%	5.5%	6.2%	6.4%
Rate of compensation increase	3.8%	3.9%	4.2%	3.8%	3.9%	4.1%
Assumed overall health care cost trend rate	na	na	na	7.7%(1)	8.2%(2)	8.4%(1)
<b>Fair value of plan assets</b>						
Fair value of plan assets at beginning of year	\$ 3,511	\$ 3,191	\$ 2,912	\$ 58	\$ 55	\$ 55
Actual return on plan assets	371	331	223	10	8	10
Bank contributions	192	208	333	19	23	25
Voluntary employee contributions	6	5	5	—	—	—
Benefits paid to pensioners and employees	(185)	(190)	(195)	(19)	(23)	(25)
Amounts paid to participants to settle their pension	—	—	(17)	—	—	—
Other, primarily foreign exchange	(14)	(34)	(70)	(2)	(5)	(10)
Fair value of plan assets at end of year	\$ 3,881	\$ 3,511	\$ 3,191	\$ 66	\$ 58	\$ 55
<b>Plan funded status</b>						
Unrecognized actuarial loss (a)	\$ (132)	\$ 32	\$ (109)	\$ (786)	\$ (683)	\$ (656)
Unrecognized cost (benefit) of plan amendments (b)	1,234	1,059	1,192	256	202	219
	57	46	29	(52)	(59)	(66)
<b>Net benefit asset (liability) at end of year</b>	<b>\$ 1,159</b>	<b>\$ 1,137</b>	<b>\$ 1,112</b>	<b>\$ (582)</b>	<b>\$ (540)</b>	<b>\$ (503)</b>
<b>Recorded in:</b>						
Other assets	\$ 1,177	\$ 1,155	\$ 1,171	\$ —	\$ —	\$ —
Other liabilities	(18)	(18)	(59)	(582)	(540)	(503)
Net benefit asset (liability) at end of year	\$ 1,159	\$ 1,137	\$ 1,112	\$ (582)	\$ (540)	\$ (503)

The plans paid \$3 million for the year ended October 31, 2005 (\$4 million in 2004; \$4 million in 2003) to us and certain of our subsidiaries for investment management, record-keeping, custodial and administrative services rendered on the same terms that we offer these services to our customers. The plans did not hold any of our shares directly as at October 31, 2005, 2004 and 2003.

(1) Trending to 4.5% in 2013 and remaining at that level thereafter.  
(2) Trending to 4.4% in 2013 and remaining at that level thereafter.  
na - not applicable

(a) A continuity of our actuarial (gains) losses is as follows:

(Canadian \$ in millions)	Pension benefit plans			Other employee future benefit plans		
	2005	2004	2003	2005	2004	2003
Unrecognized actuarial loss at beginning of year	\$ 1,059	\$ 1,192	\$ 1,148	\$ 202	\$ 219	\$ 63
Loss on the benefit liability arising from changes in assumptions	389	78	159	69	—	170
(Excess) shortfall of actual returns over expected returns on plan assets	(141)	(118)	(6)	(5)	4	(6)
Recognition in expense of a portion of the unrecognized actuarial loss	(69)	(77)	(62)	(10)	(10)	—
Impact of foreign exchange and other	(4)	(16)	(47)	—	(11)	(8)
Unrecognized actuarial loss at end of year	\$ 1,234	\$ 1,059	\$ 1,192	\$ 256	\$ 202	\$ 219

(b) A continuity of the unrecognized cost (benefit) of plan amendments is as follows:

(Canadian \$ in millions)	Pension benefit plans			Other employee future benefit plans		
	2005	2004	2003	2005	2004	2003
Unrecognized cost (benefit) of plan amendments at beginning of year	\$ 46	\$ 29	\$ 33	\$ (59)	\$ (66)	\$ —
Cost (benefit) of plan amendments initiated during the year	15	19	—	—	—	(66)
Recognition in expense of a portion of the unrecognized cost (benefit) of plan amendments	(4)	(2)	(3)	7	7	—
Impact of foreign exchange	—	—	(1)	—	—	—
Unrecognized cost (benefit) of plan amendments at end of year	\$ 57	\$ 46	\$ 29	\$ (52)	\$ (59)	\$ (66)

**Sensitivity of Assumptions**

Key weighted-average economic assumptions used in measuring the pension benefit liability, the other employee future benefit liability and related expenses are outlined in the adjoining table. The sensitivity analysis provided in the table should be used with caution as it is hypothetical and changes in each key assumption may not be linear. The sensitivities in each key variable have been calculated independently of changes in other key variables.

Actual experience may result in changes in a number of key assumptions simultaneously. Changes in one factor may result in changes in another, which could amplify or reduce certain sensitivities.

(Canadian \$ in millions, except as noted)	Pension		Other employee future benefits	
	Benefit liability	Benefit expense	Benefit liability	Benefit expense
Discount rate (%)	5.3	6.0	5.5	6.2
Impact of: 1% increase (\$)	(501)	(13)	(117)	(3)
1% decrease (\$)	625	16	150	3
Rate of compensation increase (%)	3.8	3.9	3.8	3.9
Impact of: 0.25% increase (\$)	24	2	1	–
0.25% decrease (\$)	(26)	(2)	(1)	–
Expected rate of return on assets (%)	na	6.7	na	8.0
Impact of: 1% increase (\$)	na	(33)	na	(1)
1% decrease (\$)	na	33	na	1
Assumed overall health care cost trend (%)	na	na	7.7 <sup>(1)</sup>	8.0 <sup>(2)</sup>
Impact of: 1% increase (\$)	na	na	129	10
1% decrease (\$)	na	na	(104)	(9)

(1) Trending to 4.5% in 2013 and remaining at that level thereafter.

(2) Trending to 4.4% in 2013 and remaining at that level thereafter.

na – not applicable

**Cash Flows**

Cash payments made by the Bank during the year in connection with our employee future benefit plans are as follows:

(Canadian \$ in millions)	Pension benefit plans			Other employee future benefit plans		
	2005	2004	2003	2005	2004	2003
Contributions to defined benefit plans	\$ 177	\$ 189	\$ 325	\$ –	\$ –	\$ –
Contributions to defined contribution plans	11	11	10	–	–	–
Benefits paid directly to pensioners by the Bank	15	19	8	19	23	25
Total	\$ 203	\$ 219	\$ 343	\$ 19	\$ 23	\$ 25

Our best estimate of the amounts we expect to contribute for the year ending October 31, 2006 is \$182 million to our pension plans and \$37 million to our other employee future benefit plans.

**Estimated Future Benefit Payments**

Estimated future benefit payments in the next five years and thereafter are as follows:

(Canadian \$ in millions)	Pension benefit plans	Other employee future benefit plans
2006	\$ 195	\$ 37
2007	206	35
2008	218	39
2009	232	39
2010	244	41
2011–2015	1,426	255

**Note 23 ▶ Income Taxes**

We report our provision for income taxes in our Consolidated Statement of Income based upon transactions recorded in our consolidated financial statements regardless of when they are recognized for income tax purposes, with the exception noted below for repatriation of retained earnings from our foreign subsidiaries.

In addition, we record income tax expense or benefit directly in shareholders' equity when the taxes relate to amounts recorded in shareholders' equity. For example, income tax expense on hedging gains related to our net investment in foreign operations is recorded in shareholders' equity as part of net unrealized foreign exchange gain (loss).

The future income tax balances included in our Consolidated Balance Sheet in other assets of \$24 million and other liabilities of \$126 million are the cumulative amount of tax applicable to temporary differences between the accounting and tax values of our assets and liabilities. Future income tax assets and liabilities are measured at the tax rates expected to apply when these differences reverse. Changes in future income tax assets and liabilities related to a change in tax rates are recorded in income in the period of the tax rate change.

We expect that we will realize our future income tax assets in the normal course of our operations.

<b>Components of Future Income Tax Balances</b>		
(Canadian \$ in millions)	2005	2004
<b>Future Income Tax Assets</b>		
Allowance for credit losses	\$ 427	\$ 431
Employee future benefits	198	184
Deferred compensation benefits	175	148
Other	18	111
<b>Total future income tax assets</b>	<b>\$ 818</b>	<b>\$ 874</b>
<b>Future Income Tax Liabilities</b>		
Premises and equipment	\$ (342)	\$ (316)
Pension	(414)	(410)
Intangible assets	(104)	(112)
Other	(60)	(47)
<b>Total future income tax liabilities</b>	<b>\$ (920)</b>	<b>\$ (885)</b>

Income which we earn in foreign countries through our branches or subsidiaries is generally subject to tax in those countries. We are also subject to Canadian taxation on the income earned in our foreign branches. Canada allows a credit for foreign taxes paid on this income. Upon repatriation of earnings from certain foreign subsidiaries, we would be required to pay tax on certain of these earnings. As repatriation of such earnings is not planned in the foreseeable future, we have not recorded the related future income tax liability. Canadian and foreign taxes that would be payable, at existing tax rates, if all of our foreign subsidiaries' earnings were repatriated as at October 31, 2005, 2004 and 2003 are estimated to be \$532 million, \$495 million and \$490 million, respectively.

<b>Provision for Income Taxes</b>			
(Canadian \$ in millions)	2005	2004	2003
<b>Consolidated Statement of Income</b>			
Provision for income taxes – Current	\$ 784	\$ 823	\$ 689
– Future	91	149	(37)
	<b>875</b>	972	652
<b>Shareholders' Equity</b>			
Income tax expense related to:			
Foreign currency gains on translation of net investments in foreign operations	101	254	601
Other	–	9	–
<b>Total</b>	<b>\$ 976</b>	<b>\$ 1,235</b>	<b>\$ 1,253</b>

<b>Components of Total Provision for Income Taxes</b>			
Canada: Current income taxes			
Federal	\$ 430	\$ 578	\$ 725
Provincial	227	264	285
	<b>657</b>	842	1,010
Canada: Future income taxes			
Federal	35	88	7
Provincial	9	39	2
	<b>44</b>	127	9
<b>Total Canadian</b>	<b>701</b>	969	1,019
Foreign: Current income taxes			
Future income taxes	228	236	280
	<b>47</b>	30	(46)
<b>Total foreign</b>	<b>275</b>	266	234
<b>Total</b>	<b>\$ 976</b>	<b>\$ 1,235</b>	<b>\$ 1,253</b>

Set out below is a reconciliation of our statutory tax rates and income tax that would be payable at these rates to the effective income tax rates and provision for income taxes that we have recorded in our Consolidated Statement of Income:

(Canadian \$ in millions, except as noted)	2005		2004		2003	
Combined Canadian federal and provincial income taxes at the statutory tax rate	\$ 1,160	34.8%	\$ 1,152	35.0%	\$ 890	36.2%
Increase (decrease) resulting from:						
Tax-exempt income	(88)	(2.7)	(95)	(2.9)	(112)	(4.6)
Foreign operations subject to different tax rates	(211)	(6.3)	(96)	(3.0)	(153)	(6.2)
Large corporations tax	4	0.1	5	0.1	7	0.3
Change in tax rate for future income taxes	–	–	(11)	(0.2)	10	0.4
Intangible assets not deductible for tax purposes	13	0.5	14	0.4	14	0.6
Other	(3)	(0.1)	3	0.1	(4)	(0.1)
<b>Provision for income taxes and effective tax rate</b>	<b>\$ 875</b>	<b>26.3%</b>	<b>\$ 972</b>	<b>29.5%</b>	<b>\$ 652</b>	<b>26.6%</b>

## Note 24 ▶ Earnings Per Share

### Basic Earnings per Share

Our basic earnings per share is calculated by dividing our net income, after deducting total preferred share dividends, by the daily average number of fully paid common shares outstanding throughout the year.

<b>Basic earnings per share</b>			
(Canadian \$ in millions, except as noted)	2005	2004	2003
Net income	\$ 2,400	\$ 2,306	\$ 1,781
Dividends on preferred shares	(30)	(31)	(38)
<b>Net income available to common shareholders</b>	<b>\$ 2,370</b>	<b>\$ 2,275</b>	<b>\$ 1,743</b>
Average number of common shares outstanding (in thousands)	500,060	501,656	496,208
(Canadian \$)			
<b>Basic earnings per share</b>	<b>\$ 4.74</b>	\$ 4.53	\$ 3.51

### Diluted Earnings per Share

Diluted earnings per share represents what our earnings per share would have been if instruments convertible into common shares that had the impact of reducing our earnings per share had been converted either at the beginning of the year for instruments that were outstanding all year or from the date of issue for instruments issued during the year.

#### Convertible Shares

In determining diluted earnings per share, we increase net income available to common shareholders by dividends paid on convertible shares as these dividends would not have been paid if the shares had been converted at the beginning of the year. Similarly, we increase the average number of common shares outstanding by the number of shares that would have been issued had the conversion taken place at the beginning of the year.

Our Series 4, 6 and 10 Class B Preferred shares, in certain circumstances, are convertible into common shares. These conversions are not included in the calculation of diluted earnings per share as we have the option to settle the conversion in cash instead of common shares.

#### Employee Stock Options

In determining diluted earnings per share, we increase the average number of common shares outstanding by the number of shares that would have been issued if all stock options with a strike price below the average share price for the year had been exercised. When performance targets have not been met, those are excluded from the calculation. We also decrease the average number of common shares outstanding by the number of our common shares that we could have repurchased if we had used the proceeds from the exercise of stock options to repurchase them on the open market at the average share price for the year. We do not adjust for stock options with a strike price above the average share price for the year because including them would increase our earnings per share, not dilute it.

#### Diluted earnings per share

(Canadian \$ in millions, except as noted)	2005	2004	2003
Net income available to common shareholders	\$ 2,370	\$ 2,275	\$ 1,743
Dividends on convertible shares	–	1	1
Net income adjusted for dilution effect	\$ 2,370	\$ 2,276	\$ 1,744
Average number of common shares outstanding (in thousands)	500,060	501,656	496,208
Convertible shares	361	683	996
Stock options potentially exercisable (1)	25,424	32,057	36,608
Common shares potentially repurchased (2)	(15,109)	(19,351)	(26,803)
Average diluted number of common shares outstanding (in thousands)	510,736	515,045	507,009
(Canadian \$)			
Diluted earnings per share	\$ 4.64	\$ 4.42	\$ 3.44

(1) In computing diluted earnings per share we excluded average stock options outstanding of 410,265, 679,510 and 455,282 with weighted-average exercise prices of \$56.60, \$53.93 and \$41.21 for the years ended October 31, 2005, 2004 and 2003, respectively.

(2) The number of shares potentially repurchased is determined by computing a weighted average of the number of shares potentially repurchased.

#### Future Change in Accounting Policy

The CICA has issued new rules that will require us to include the potential conversion of certain of our preferred shares and capital trust securities to common shares in the calculation of diluted earnings per share. The effective date has not been finalized; however, we expect to adopt these new rules in the year ended October 31, 2006. Diluted earnings per share of prior periods will be restated upon adoption. Under the new standard our diluted earnings per share for the years ended October 31, 2005, 2004 and 2003 would be reduced by approximately \$0.06, \$0.09 and \$0.11, respectively.

## Note 25 ▶ Operating and Geographic Segmentation

### Operating Groups

We conduct our business through operating groups, each of which has a distinct mandate. We determine operating groups based on our management structure and therefore our groups and results attributed to our groups may not be comparable with those of other financial services companies. We evaluate the performance of our groups using measures such as net income, return on equity, net economic profit and non-interest expense-to-revenue (productivity) ratio.

### Personal and Commercial Client Group

Personal and Commercial Client Group (“P&C”) offers a full range of products and services to personal and business clients in Canada and the United States through branches and direct banking channels such as telephone banking, online banking and a network of automated banking machines.

### Private Client Group

Private Client Group (“PCG”) brings together all of our wealth management businesses. Operating primarily in Canada and the United States, PCG serves a full range of North American client segments, from mainstream to ultra-high net worth, as well as select institutional market segments. PCG offers its clients a broad range of wealth management products and services, including full-service and direct investing, private banking and investment products, providing the tools they need to accumulate, protect and grow their financial assets.

### Investment Banking Group

Investment Banking Group (“IBG”) combines all of our businesses serving corporate, institutional and government clients. In Canada, its client base comprises large corporations and institutions across a broad range of industry sectors. In the United States, it serves middle-market and institutional clients in selected sectors. IBG also serves institutional and government clients in the United Kingdom, Europe and Asia. It offers clients complete financial solutions across the entire balance sheet, including public and private debt

and equity underwriting, cash management, corporate lending, securitization, foreign exchange and trade finance. The group also offers financial advisory services in mergers and acquisitions and restructurings, while providing investing clients with research, sales and trading services.

### Corporate Support

Corporate Support includes Technology and Solutions (“T&S”) and the Corporate units that provide expertise and governance support in areas such as strategic planning, law, finance, internal audit, risk management, corporate communications, economics, corporate marketing, human resources and learning. Operating results for Corporate Support include revenues and expenses associated with certain securitization activities, the hedging of foreign-source earnings and activities related to the management of certain balance sheet positions and our overall asset liability structure.

T&S manages, maintains and provides governance over information technology, real estate, operations services and sourcing for the Bank. The unit focuses on enterprise-wide priorities that improve quality and efficiency.

Operating results for T&S are included with Corporate Support for reporting purposes. However, costs of T&S services are transferred to P&C, PCG and IBG and only minor amounts are retained in T&S’s results. As such, results for Corporate Support largely reflect operating results of Corporate units.

Corporate Support also includes residual revenues and expenses representing the differences between actual amounts earned or incurred and the amounts allocated to operating groups.

### Basis of Presentation

The results of these operating groups are based on our internal financial reporting systems. The accounting policies used in these groups are generally consistent with those followed in the preparation of the consolidated financial statements as disclosed in Note 1 and throughout the consolidated financial statements. Notable

accounting measurement differences are the taxable equivalent basis adjustment and the provision for credit losses, as described below.

### Taxable Equivalent Basis

We analyze net interest income on a taxable equivalent basis ("teb"). This basis includes an adjustment which increases GAAP revenues and the GAAP provision for income taxes by an amount that would raise revenues on certain tax-exempt securities to a level that would incur tax at the statutory rate.

Analysis on a teb basis neutralizes the impact of investing in tax-exempt or tax-advantaged securities rather than fully taxable securities with higher yields. It reduces distortions in net interest income related to the choice of tax-advantaged and taxable investments.

### Provisions for Credit Losses

Provisions for credit losses are generally allocated to each group based on expected losses for that group over an economic cycle. Differences between expected loss provisions and provisions required under GAAP are included in Corporate Support.

### Inter-Group Allocations

Various estimates and allocation methodologies are used in the preparation of the operating groups' financial information. We allocate expenses directly related to earning revenue to the groups that earned the related revenue. Expenses not directly related to earning revenue, such as overhead expenses, are allocated to operating groups using allocation formulas applied on a consistent basis. Operating group net interest income reflects internal funding charges and credits on the groups' assets, liabilities and capital, at market rates, taking into account relevant terms and currency considerations. The offset of the net impact of these charges and credits is reflected in Corporate Support.

### Geographic Information

We operate primarily in Canada and the United States but also have operations in the United Kingdom, Europe, the Caribbean and Asia, which are grouped in Other Countries. We allocate our results by geographic region based on the location of the unit responsible for managing the related assets, liabilities, revenues and expenses, except for the consolidated provision for credit losses, which is allocated based upon the country of ultimate risk.

Our results and average assets, allocated by operating group and geographic region, are as follows:

(Canadian \$ in millions)	P&C	PCG	IBG	Corporate Support <sup>(1)</sup>	Total (teb basis)	Teb adjustments	Total (GAAP basis)	Canada	United States	Other Countries
<b>2005</b>										
Net interest income	\$ 3,561	\$ 577	\$ 965	\$ (197)	\$ 4,906	\$ (119)	\$ 4,787	\$ 3,504	\$ 1,266	\$ 136
Non-interest revenue	1,655	1,459	1,776	162	5,052	–	5,052	3,544	1,345	163
Total Revenue	5,216	2,036	2,741	(35)	9,958	(119)	9,839	7,048	2,611	299
Provision for credit losses	299	4	98	(222)	179	–	179	192	14	(27)
Non-interest expense	3,142	1,520	1,477	188	6,327	–	6,327	4,344	1,855	128
Income before taxes and non-controlling interest in subsidiaries	1,775	512	1,166	(1)	3,452	(119)	3,333	2,512	742	198
Income taxes	576	192	314	(88)	994	(119)	875	798	248	(52)
Non-controlling interest in subsidiaries	–	–	–	58	58	–	58	36	22	–
Net Income	\$ 1,199	\$ 320	\$ 852	\$ 29	\$ 2,400	\$ –	\$ 2,400	\$ 1,678	\$ 472	\$ 250
Average Assets	\$ 127,018	\$ 7,061	\$ 163,848	\$ 5,233	\$ 303,160	\$ –	\$ 303,160	\$ 201,950	\$ 75,621	\$ 25,589
<b>2004 (Restated)</b>										
Net interest income	\$ 3,352	\$ 533	\$ 1,260	\$ (208)	\$ 4,937	\$ (139)	\$ 4,798	\$ 3,331	\$ 1,438	\$ 168
Non-interest revenue	1,525	1,318	1,508	200	4,551	–	4,551	3,200	1,200	151
Total Revenue	4,877	1,851	2,768	(8)	9,488	(139)	9,349	6,531	2,638	319
Provision for credit losses	299	5	138	(545)	(103)	–	(103)	(1)	(46)	(56)
Non-interest expense	3,077	1,504	1,405	171	6,157	–	6,157	4,062	1,960	135
Income before taxes and non-controlling interest in subsidiaries	1,501	342	1,225	366	3,434	(139)	3,295	2,470	724	240
Income taxes	518	115	393	85	1,111	(139)	972	795	279	37
Non-controlling interest in subsidiaries	1	–	–	16	17	–	17	2	15	–
Net Income	\$ 982	\$ 227	\$ 832	\$ 265	\$ 2,306	\$ –	\$ 2,306	\$ 1,673	\$ 430	\$ 203
Average Assets	\$ 117,126	\$ 7,145	\$ 141,691	\$ 3,830	\$ 269,792	\$ –	\$ 269,792	\$ 177,410	\$ 68,743	\$ 23,639
<b>2003 (Restated)</b>										
Net interest income	\$ 3,230	\$ 559	\$ 1,344	\$ (204)	\$ 4,929	\$ (152)	\$ 4,777	\$ 3,168	\$ 1,612	\$ 149
Non-interest revenue	1,549	1,175	1,244	252	4,220	–	4,220	2,914	1,184	122
Total Revenue	4,779	1,734	2,588	48	9,149	(152)	8,997	6,082	2,796	271
Provision for credit losses	298	6	231	(80)	455	–	455	211	211	33
Non-interest expense	3,070	1,510	1,345	162	6,087	–	6,087	3,993	1,989	105
Income before taxes and non-controlling interest in subsidiaries	1,411	218	1,012	(34)	2,607	(152)	2,455	1,878	596	133
Income taxes	493	81	321	(91)	804	(152)	652	598	222	(16)
Non-controlling interest in subsidiaries	4	–	–	18	22	–	22	6	16	–
Net Income	\$ 914	\$ 137	\$ 691	\$ 39	\$ 1,781	\$ –	\$ 1,781	\$ 1,274	\$ 358	\$ 149
Average Assets	\$ 108,046	\$ 7,015	\$ 144,418	\$ 4,487	\$ 263,966	\$ –	\$ 263,966	\$ 167,427	\$ 76,622	\$ 19,917

(1) Corporate Support includes Technology and Solutions.

Prior years have been restated to give effect to the current year's organization structure and presentation changes.

## Note 26 ▶ Related Party Transactions

We provide banking services to our joint ventures and equity-accounted investees on the same terms that we offer to our customers.

Effective September 1, 1999, new loans and mortgages to executive officers were no longer available at preferred rates, other than mortgages related to transfers we initiate. A select suite of customer loan and mortgage products is now offered to employees at rates normally accorded to preferred customers. We also offer employees a fee-based subsidy on annual credit card fees.

Prior to September 1, 1999, loans to executive officers for personal purposes, principally for consumer purchases, home improvements and sundry investments, were made available at an interest rate of one-half of our prime rate and up to a maximum loan amount of \$25,000. Loans in excess of this amount were available at prime rate.

The amounts outstanding under these preferred rate loan agreements are as follows:

(Canadian \$ in millions)	2005	2004
Mortgage loans	\$ 82	\$ 80
Personal loans	—	66
<b>Total</b>	<b>\$ 82</b>	<b>\$ 146</b>

The interest earned on these loans is recorded in interest, dividend and fee income in our Consolidated Statement of Income.

### Board of Directors Compensation

#### Stock Option Plan

In fiscal 2002, we introduced a stock option plan for non-officer directors, the terms of which are the same as the plan for designated

officers and employees described in Note 21. During the fiscal year 2003, we granted 42,000 stock options at an exercise price of \$43.25 per share. The granting of options under the Non-Officer Director Stock Option Plan was discontinued effective November 1, 2003.

Stock option expense for this plan is calculated in the same manner as employee stock option expense. It was included in other expenses in our Consolidated Statement of Income and was less than \$1 million for the years ended October 31, 2005, 2004 and 2003, respectively.

#### Deferred Share Units

Our Board of Directors is required to take 100% of their annual retainers and other fees in the form of either our common shares (purchased on the open market) or deferred share units until such time as the directors' shareholdings are greater than six times their annual retainers as directors. After this threshold is reached, the directors are required to take at least 50% of their annual retainers in this form.

Deferred share units allocated under this deferred share unit plan are adjusted to reflect dividends and changes in the market value of our common shares. The value of these deferred share units will be paid upon termination of service as a director. The expense for this plan was included in other expenses in our Consolidated Statement of Income and totalled \$3 million, \$3 million and \$2 million for the years ended October 31, 2005, 2004 and 2003, respectively.

We provide certain banking services to entities which are affiliated with our directors. These services are on the same terms as we offer to our customers.

## Note 27 ▶ Contingent Liabilities

### (a) Legal Proceedings

In the bankruptcy of Adelphia Communications Corporation ("Adelphia"), the Official Committees of Unsecured Creditors and Equity Security Holders have been given leave to pursue claims against Bank of Montreal, its indirect subsidiary Harris Nesbitt Corp., and approximately 380 other financial institutions. The Complaints allege various federal statutory and common law claims and seek an unspecified amount of damages and punitive damages and equitable relief. Also in the bankruptcy proceeding, Adelphia and Bank of Montreal have entered into a tolling agreement with respect to the time within which Adelphia may bring an adversary proceeding against Bank of Montreal seeking return of certain payments received by Bank of Montreal, claiming that such payments were voidable preferences.

In addition, Harris Nesbitt Corp. is one of many underwriters named, in addition to the Bank and other financial institutions, in several civil actions, including a class action, brought by investors in Adelphia securities. All seek unspecified damages. The court in the class action recently dismissed without prejudice all federal securities law claims against Bank of Montreal and Harris Nesbitt Corp. but a common law claim against Bank of Montreal and a securities law claim against the lead underwriters remain. The parties in the class action presently are engaged in mediation to try to resolve these matters.

In addition, Bank of Montreal and Harris Nesbitt Corp. have been named as defendants in actions brought by an individual and certain trusts in which that individual, directly or indirectly, maintains an interest, and by a corporation and certain of its affiliates, all of whom or which acquired Adelphia common stock in exchange for certain of their businesses. The complaints assert claims under various state statutes and the common law and claim unspecified actual and punitive damages.

There remains the possibility that other or additional claims related to Adelphia's bankruptcy might be asserted by one or more interested parties.

As these matters are all in the early stages, we are unable to determine the eventual outcome of these matters but management believes that the Bank and Harris Nesbitt Corp. have strong defences to these claims and will vigorously defend against all such actions.

BMO Nesbitt Burns Inc., an indirect subsidiary of Bank of Montreal, has been named as a defendant in several class and individual actions in Canada and a class action in the United States brought on behalf of shareholders of Bre-X Minerals Ltd. ("Bre-X"). Other defendants named in one or more of these actions include Bre-X, officers and directors of Bre-X, a mining consulting firm retained by Bre-X, Bre-X's financial advisor, brokerage firms which sold Bre-X common stock, and a major gold production company. These actions are largely based on allegations of negligence, negligent or fraudulent misrepresentation and a breach of the *U.S. Securities Exchange Act of 1934* (United States only), in connection with the sale of Bre-X securities. Two of the proposed class actions in Canada have been dismissed as to BMO Nesbitt Burns Inc. The proposed U.S. class action was dismissed in October 2005.

During 2004, claims were made against us in relation to the termination of certain derivative positions. These claims were settled in 2005.

The Bank and its subsidiaries are party to other legal proceedings in the ordinary course of their businesses. Management does not expect the outcome of any of these other proceedings, individually or in the aggregate, to have a material adverse effect on the consolidated financial position or results of the Bank's operations.

## (b) Pledged Assets

In the normal course of our business, we pledge assets as security for various liabilities that we incur. The following tables summarize our pledged assets, to whom they are pledged and in relation to what activity:

(Canadian \$ in millions)	2005	2004
Cash resources	\$ 9	\$ 2
Securities		
Issued or guaranteed by Canada	8,734	5,227
Issued or guaranteed by a Canadian province, municipality or school corporation	1,779	1,668
Other securities	16,789	11,421
Other assets	16,764	21,559
<b>Total assets pledged</b>	<b>\$ 44,075</b>	<b>\$ 39,877</b>

Excludes restricted cash resources disclosed in Note 2.

(Canadian \$ in millions)

2005

2004

### Assets pledged to:

Clearing systems, payment systems and depositories \$ 1,735 \$ 1,253

### Assets pledged in relation to:

Obligations related to securities lent or sold under repurchase agreements 20,275 20,865  
Securities borrowing and lending 12,472 11,229  
Derivatives transactions 2,209 1,121  
Other 7,384 5,409

**Total \$ 44,075 \$ 39,877**

Excludes cash pledged with central banks disclosed as restricted cash in Note 2.

## Note 28 ▶ Fair Value of Financial Instruments

We record trading assets and liabilities at market values and non-trading assets and liabilities at their original amortized cost less allowances or write-downs for impairment. Fair value is subjective in nature, requiring a variety of valuation techniques and assumptions. The values are based upon the estimated amounts for individual assets and liabilities and do not include an estimate of the fair value of any of the legal entities or underlying operations that comprise our business.

Fair value amounts disclosed represent point-in-time estimates that may change in subsequent reporting periods due to market conditions or other factors. Fair value represents our estimate of the amounts for which we could exchange the financial instruments with willing third parties who were interested in acquiring the instruments. In most cases, however, the financial instruments are not typically exchangeable or exchanged and therefore it is difficult to determine their fair value. In those cases, we have estimated fair value taking into account only changes in interest rates and credit risk that have occurred since we acquired them or entered into the underlying contract. These calculations represent management's best estimates based on a range of methodologies and assumptions; since they involve uncertainties, the fair values may not be realized in an actual sale or immediate settlement of the instruments.

Interest rate changes are the main cause of changes in the fair value of our financial instruments.

Items that are not financial instruments, such as premises and equipment, goodwill and intangible assets, have been excluded from our estimate of fair value. The assets excluded totalled \$3,134 million as at October 31, 2005 (\$4,007 million in 2004).

### Financial Instruments Whose Book Value Approximates Fair Value

Fair value is assumed to equal book value for acceptance-related assets and liabilities, securities sold but not yet purchased and securities lent or sold under repurchase agreements, due to the short-term nature of these assets and liabilities. Fair value is also assumed to equal book value for our cash resources, certain other assets and certain other liabilities.

### Loans

In determining the fair value of our loans, we incorporate the following assumptions:

- For fixed rate performing loans, we discount the remaining contractual cash flows, adjusted for estimated prepayment, at market interest rates currently offered for loans with similar terms.
- For floating rate performing loans, changes in interest rates have minimal impact on fair value since loans reprice to market frequently. On that basis, fair value is assumed to equal carrying value.

The value of our loan balances determined based on the above assumptions is further reduced by the allowance for credit losses to determine the fair value of our loan portfolio.

### Securities

The fair value of our securities, both trading and investment, by instrument type and the methods used to determine fair value are provided in Note 3.

### Derivative Financial Instruments

The methods used to determine the fair value of derivative financial instruments are provided in Note 9.

### Deposits

In determining the fair value of our deposits, we incorporate the following assumptions:

- For fixed rate, fixed maturity deposits, we discount the remaining contractual cash flows for these deposits, adjusted for expected redemptions, at market interest rates currently offered for deposits with similar terms and risks.
- For floating rate, fixed maturity deposits, changes in interest rates have minimal impact on fair value since deposits reprice to market frequently. On that basis, fair value is assumed to equal book value.
- For deposits with no defined maturities, we consider fair value to equal book value based on book value being equivalent to the amount payable on the reporting date.

### Subordinated Debt

The fair value of our subordinated debt is determined by referring to current market prices for similar debt instruments.

Set out in the following table are the amounts which would be reported if all of our financial instrument assets and liabilities were reported at their fair values, adjusted for the impact of derivatives that hedge changes in fair value.

(Canadian \$ in millions)

	2005				2004			
	Book value	Fair value	Fair value of hedging derivatives <sup>(1)</sup>	Fair value over (under) book value	Book value	Fair value	Fair value of hedging derivatives <sup>(1)</sup>	Fair value over (under) book value
<b>Assets</b>								
Cash resources	\$ 20,721	\$ 20,721	\$ –	\$ –	\$ 18,045	\$ 18,045	\$ –	\$ –
Securities	57,256	57,253	15	12	50,472	50,558	(48)	38
Loans and customers' liability under acceptances, net of the allowance for credit losses	174,337	174,838	(31)	470	156,248	156,407	(37)	122
Derivative financial instruments – trading	30,851	30,851	–	–	24,914	24,914	–	–
Other assets	10,567	10,567	–	–	10,974	10,974	–	–
	<b>\$ 293,732</b>	<b>\$ 294,230</b>	<b>\$ (16)</b>	<b>\$ 482</b>	<b>\$ 260,653</b>	<b>\$ 260,898</b>	<b>\$ (85)</b>	<b>\$ 160</b>
<b>Liabilities</b>								
Deposits	\$ 193,793	\$ 194,288	\$ (122)	\$ 373	\$ 175,190	\$ 175,710	\$ (196)	\$ 324
Derivative financial instruments – trading	28,829	28,829	–	–	23,741	23,741	–	–
Acceptances	5,934	5,934	–	–	5,355	5,355	–	–
Securities sold but not yet purchased	16,142	16,142	–	–	10,441	10,441	–	–
Securities lent or sold under repurchase agreements	22,657	22,657	–	–	20,865	20,865	–	–
Other liabilities	12,203	12,203	–	–	12,636	12,636	–	–
Subordinated debt	2,469	2,637	(3)	165	2,395	2,630	8	243
Preferred share liability	450	465	–	15	450	475	–	25
Capital trust securities	1,150	1,240	–	90	1,150	1,269	–	119
	<b>\$ 283,627</b>	<b>\$ 284,395</b>	<b>\$ (125)</b>	<b>\$ 643</b>	<b>\$ 252,223</b>	<b>\$ 253,122</b>	<b>\$ (188)</b>	<b>\$ 711</b>
Total				<b>\$ (161)</b>				<b>\$ (551)</b>

(1) Refer to Note 9.

## Note 29 ▶ Reconciliation of Canadian and United States Generally Accepted Accounting Principles

We prepare our consolidated financial statements in accordance with GAAP in Canada, including interpretations of GAAP by our regulator, the Superintendent of Financial Institutions Canada.

We have included the significant differences which would result if United States GAAP were applied in the preparation of

our Consolidated Statement of Income, Consolidated Balance Sheet and Consolidated Statement of Comprehensive Income. We have not included our Consolidated Statement of Cash Flows as the differences are immaterial.

### Condensed Consolidated Statement of Income

For the Year Ended October 31 (Canadian \$ in millions, except per share amounts)

	2005	2004	2003
Net income, as reported under Canadian GAAP	\$ 2,400	\$ 2,306	\$ 1,781
Adjustments to arrive at United States GAAP:			
Net Interest Income			
Liabilities and equity (k)	97	124	123
Variable interest entities (a)	–	38	–
Mortgage prepayment fees (b)	–	(42)	–
Non-Interest Revenue			
Merchant banking (l)	(83)	–	–
Variable interest entities (a)	(13)	104	–
Securitizations (c)	–	(3)	(44)
Derivatives (d)	(66)	(5)	(3)
Non-Interest Expense			
Variable interest entities (a)	–	(7)	–
Stock options (e)	(11)	(29)	(43)
Software development costs (f)	(42)	(42)	39
Pension and related benefits (g)	2	5	(2)
Goodwill and other assets (h)	5	6	7
Income taxes and net change in income taxes (i) (including adjustments due to items listed above)	66	(60)	(34)
Non-controlling interest in subsidiaries	(79)	(43)	(42)
Cumulative impact of an accounting change (a)	–	(111)	–
Net income based on United States GAAP	<b>\$ 2,276</b>	<b>\$ 2,241</b>	<b>\$ 1,782</b>
Earnings per share: basic			
– Canadian GAAP net income	\$ 4.74	\$ 4.53	\$ 3.51
– United States GAAP net income before cumulative impact of an accounting change	4.49	4.54	3.43
– Cumulative impact of an accounting change	–	(0.23)	–
– United States GAAP net income	4.49	4.31	3.43
Earnings per share: diluted			
– Canadian GAAP net income	\$ 4.64	\$ 4.42	\$ 3.44
– United States GAAP net income before cumulative impact of an accounting change	4.40	4.42	3.35
– Cumulative impact of an accounting change	–	(0.22)	–
– United States GAAP net income	4.40	4.20	3.35

Certain comparative figures have been reclassified to conform with the current year's presentation.

## Condensed Consolidated Balance Sheet

As at October 31 (Canadian \$ in millions)

	2005			2004		
	Canadian GAAP	Increase (Decrease)	United States GAAP	Canadian GAAP	Increase (Decrease)	United States GAAP
<b>Assets</b>						
Cash resources (a)	\$ 20,721	\$ –	\$ 20,721	\$ 18,045	\$ 28	\$ 18,073
Securities						
Investment and loan substitutes (n)	12,947	(12,947)	–	15,028	(15,028)	–
Trading	44,309	–	44,309	35,444	–	35,444
Available for sale (d,j,n)	–	14,102	14,102	–	15,873	15,873
Loans and customers' liability under acceptances, net of the allowance for credit losses (a,d)	174,337	(15)	174,322	156,248	20,796	177,044
Derivative financial instruments (a,d)	31,517	391	31,908	25,448	327	25,775
Premises and equipment (f)	1,847	79	1,926	2,020	127	2,147
Goodwill (h)	1,091	(41)	1,050	1,507	(43)	1,464
Intangible assets (h)	196	(21)	175	480	(26)	454
Other assets (a,d,g,n)	10,567	658	11,225	10,974	163	11,137
<b>Total Assets</b>	<b>\$ 297,532</b>	<b>\$ 2,206</b>	<b>\$ 299,738</b>	<b>\$ 265,194</b>	<b>\$ 22,217</b>	<b>\$ 287,411</b>
<b>Liabilities and Shareholders' Equity</b>						
Deposits	\$ 193,793	\$ 53	\$ 193,846	\$ 175,190	\$ 4	\$ 175,194
Derivative financial instruments (a,d)	28,868	62	28,930	23,973	(13)	23,960
Acceptances	5,934	–	5,934	5,355	–	5,355
Securities sold but not yet purchased	16,142	–	16,142	10,441	–	10,441
Securities lent or sold under repurchase agreements	22,657	–	22,657	21,345	–	21,345
Other liabilities (d,j,k)	12,203	3,220	15,423	12,156	23,179	35,335
Subordinated debt (d)	2,469	(40)	2,429	2,395	9	2,404
Preferred share liability (k)	450	(450)	–	450	(450)	–
Capital trust securities (k)	1,150	(1,150)	–	1,150	(1,150)	–
Shareholders' equity (d,m)	13,866	511	14,377	12,739	638 <sup>(1)</sup>	13,377
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 297,532</b>	<b>\$ 2,206</b>	<b>\$ 299,738</b>	<b>\$ 265,194</b>	<b>\$ 22,217</b>	<b>\$ 287,411</b>

(1) Includes cumulative adjustment to shareholders' equity arising from current and prior years' GAAP differences. Certain comparative figures have been reclassified to conform with the current year's presentation.

## Consolidated Statement of Comprehensive Income

For the Year Ended October 31 (Canadian \$ in millions)

	2005	2004	2003
Net income (under United States GAAP)	\$ 2,276	\$ 2,241	\$ 1,782
Other Comprehensive Income, net of income taxes:			
Unrealized loss on translation of net investments in foreign operations, net of hedging activities (1)	(114)	(295)	(597)
Unrealized holding gains (losses) on available-for-sale securities, net of hedging activities (2)	99	(4)	76
Realized (gains) and write-downs on available-for-sale securities recognized in net income (3)	(107)	(114)	(25)
Unrealized losses on derivatives designated as cash flow hedges (4)	(49)	(205)	(37)
Net gains on derivatives designated as cash flow hedges recognized in net income (5)	5	253	21
Minimum pension liability (6)	12	(5)	(45)
<b>Total Other Comprehensive Loss</b>	<b>(154)</b>	<b>(370)</b>	<b>(607)</b>
<b>Comprehensive Income</b>	<b>\$ 2,122</b>	<b>\$ 1,871</b>	<b>\$ 1,175</b>

(1) Net of income taxes of \$102 million (\$254 million in 2004; \$601 million in 2003).

(2) Net of income taxes of \$53 million (\$2 million in 2004; \$37 million in 2003).

(3) Net of income taxes of \$58 million (\$64 million in 2004; \$14 million in 2003).

(4) Net of income taxes of \$26 million (\$110 million in 2004; \$19 million in 2003).

(5) Net of income taxes of \$41 million (\$209 million in 2004; \$12 million in 2003).

(6) Net of income taxes of \$26 million (\$3 million in 2004; \$30 million in 2003).

### (a) Variable Interest Entities

Under United States GAAP, we adopted a new accounting standard on the consolidation of variable interest entities ("VIEs") effective January 31, 2004. Under this new standard, we consolidate the financial results of VIEs if the investments we hold in these entities and/or the relationships we have with them result in us being exposed to a majority of their expected losses, being able to benefit from a majority of their expected residual returns, or both, based on a calculation determined by the standard setters.

When we adopted this new U.S. accounting standard on January 31, 2004, it resulted in the consolidation of our multi-seller conduits. We recorded a one-time transition adjustment of \$111 million related to unrealized losses on interest rate swaps held by our VIEs to hedge their exposure to interest rate risk in the Consolidated Statement of Income, as the cumulative effect

of an accounting change. These derivative instruments had been accounted for as hedging derivatives under Canadian GAAP but did not meet the detailed hedge accounting requirements under United States GAAP in prior periods. As a result, although they are effective as economic hedges, they are required to be marked to market under United States GAAP. The liability associated with these unrealized losses will reverse, with a corresponding increase in net income, over the remaining terms of the swaps for United States GAAP reporting.

The impact of the new standard on our Consolidated Balance Sheet as at October 31, 2004 was an increase in cash resources of \$28 million, an increase in loans of \$20,805 million, a decrease in derivative assets of \$51 million, an increase in other assets of \$25 million, a decrease in derivative liabilities of \$13 million, an increase in other liabilities of \$20,849 million and a decrease in shareholders' equity of \$29 million.

On April 29, 2005, we restructured our multi-seller conduits by either terminating or changing the terms of our swaps with the VIEs and amending some of the rights of note holders in the VIEs. As a result, they no longer meet the criteria for consolidation. The impact of deconsolidating these VIEs was an increase in non-interest revenue of \$13 million representing the reversal of unamortized mark-to-market losses on swaps.

*(b) Mortgage Prepayment Fees*

Under United States GAAP, mortgage prepayment fees are recognized in income when the related mortgage is prepaid or renegotiated at market rates. Prior to November 1, 2003 these fees were deferred and amortized to income over the average remaining term of the related mortgages under Canadian GAAP.

Effective November 1, 2003, we adopted a new Canadian accounting standard on sources of GAAP that eliminated this difference and resulted in recording in income, for Canadian GAAP purposes, the balance of deferred mortgage prepayment fees as at November 1, 2003 of \$42 million before income taxes. This amount was already recognized in net income under United States GAAP.

*(c) Securitizations*

Under United States GAAP, gains on all of our securitizations are recorded at the date of the securitization. Under Canadian GAAP, prior to July 1, 2001, gains on sales of NHA-insured mortgages were recorded at the date of the securitization and gains on sales of other loans securitized were deferred and recorded over the life of the loans securitized. Effective July 1, 2001, we adopted a new Canadian accounting standard on securitizations that eliminated this difference for securitizations that took place after July 1, 2001. There was an adjustment to our Consolidated Statement of Income until the deferred gains related to loans securitized prior to July 1, 2001 were recorded in income.

*(d) Derivatives*

Under United States GAAP, hedging derivatives are recorded at fair value in our Consolidated Balance Sheet. Changes in the fair value of hedging derivatives are either offset in our Consolidated Statement of Income against the change in the fair value of the hedged asset, liability or firm commitment, or are recorded in other comprehensive income until the hedged item is recorded in our Consolidated Statement of Income. If the change in the fair value of the derivative is not completely offset by the change in the fair value of the item it is hedging, the difference is recorded immediately in our Consolidated Statement of Income.

Under Canadian GAAP, hedging derivatives are accounted for on an accrual basis, with gains or losses deferred and recorded in income on the same basis as the underlying hedged item.

*(e) Stock Options*

Under United States GAAP, the fair value of stock options on their grant date is recorded as compensation expense over the period that the options vest. Under Canadian GAAP, prior to November 1, 2002, we included the amount of proceeds in shareholders' equity when the options were exercised and did not recognize any compensation expense. Effective November 1, 2002, we adopted a new Canadian accounting standard on stock-based compensation that eliminated this difference for stock options granted on or after November 1, 2002. As a result, there will continue to be an adjustment to our Consolidated Statement of Income until stock option expense has been fully recognized for stock options granted prior to November 1, 2002 under United States GAAP.

*(f) Software Development Costs*

Under United States GAAP, costs of internally developed software are required to be capitalized and amortized over the

expected useful life of the software. Under Canadian GAAP, prior to November 1, 2003, only costs paid to third parties related to internally developed software were capitalized and amortized over the expected useful life of the software. Effective November 1, 2003, we adopted a new Canadian accounting standard on sources of GAAP that eliminated this difference for software development costs incurred after October 31, 2003. There will continue to be an adjustment to our Consolidated Statement of Income until software development costs capitalized prior to fiscal 2004 are fully amortized.

*(g) Pension and Related Benefits*

Under United States GAAP, both pension and other employee future benefits are recorded in our Consolidated Statement of Income in the period services are provided by our employees. The related obligations are valued using current market rates. Under Canadian GAAP, prior to November 1, 2000, pension benefits were recorded in our Consolidated Statement of Income in the period services were provided by our employees, with the corresponding obligation valued using management's best estimate of the long-term rate of return on assets, while other employee future benefits were expensed as incurred. Effective November 1, 2000, we adopted a new Canadian accounting standard on pension and other employee future benefits that eliminated the difference between Canadian and United States GAAP. When we adopted this new standard, we accounted for the change in accounting as a charge to retained earnings. As a result, there will continue to be an adjustment to our Consolidated Statement of Income until amounts previously deferred under United States GAAP have been fully amortized to income.

*(h) Goodwill and Other Assets*

Under United States GAAP, our acquisition of Suburban Bancorp, Inc. in 1994 would have been accounted for using the pooling of interests method. Under Canadian GAAP, we accounted for this acquisition using the purchase method, which resulted in the recognition and amortization of goodwill and other intangible assets associated with the acquisition. Effective November 1, 2001, goodwill is no longer amortized to income under either United States or Canadian GAAP. The remaining difference relates to the amortization of intangible assets under Canadian GAAP.

*(i) Income Taxes*

In addition to the tax impact of differences outlined above, under United States GAAP, tax rate changes do not impact the measurement of our future income tax balances until they are passed into law. Under Canadian GAAP, tax rate changes are recorded in income in the period of change.

*(j) Non-Cash Collateral*

Under United States GAAP, non-cash collateral received in security lending transactions that we are permitted by contract to sell or re-pledge is recorded as an asset in our Consolidated Balance Sheet and a corresponding liability is recorded for the obligation to return the collateral. Under Canadian GAAP, such collateral and the related obligation are not recorded in our Consolidated Balance Sheet. As a result of this difference, available for sale securities and other liabilities have been increased by \$2,191 million and \$1,289 million for the years ended October 31, 2005 and 2004, respectively.

*(k) Liabilities and Equity*

Under United States GAAP, certain of our preferred shares and capital trust securities are classified as equity and non-controlling interest, respectively. Under Canadian GAAP, as both instruments are ultimately convertible into a variable number of our common shares at the holders' option, they are classified as liabilities. Prior year Canadian GAAP financial statements have been restated.

*(l) Merchant Banking Investments*

Under United States GAAP, our merchant banking subsidiaries account for their investments at cost or under the equity method. Under Canadian GAAP, these subsidiaries account for their investments at fair value with changes in fair value recorded in income as they occur.

*(m) Shareholders' Equity*

Accumulated other comprehensive income is recorded as a separate component of shareholders' equity under United States GAAP. Canadian GAAP does not permit presentation of other comprehensive income.

The accumulated balances related to each component of other comprehensive income, net of income taxes, are as follows:

(Canadian \$ in millions)	2005	2004
Unrealized loss on translation of net investments in foreign operations, net of hedging activities	\$ (585)	\$ (471)
Net unrealized gains on available-for-sale securities (n)	3	11
Unrealized gains on derivatives designated as cash flow hedges (d)	230	274
Minimum pension liability (o)	(38)	(50)
<b>Total Accumulated Other Comprehensive Loss</b>	<b>\$ (390)</b>	<b>\$ (236)</b>

*(n) Available-for-Sale Securities*

Under United States GAAP, we have designated as available-for-sale all of our investment securities and loan substitute securities, other than investments in corporate equity where we exert significant influence but not control. Available-for-sale securities are carried at fair value, with any unrealized gains or losses recorded in other comprehensive income. Under Canadian GAAP, investment securities are carried at cost, amortized cost or adjusted cost. Investments in corporate equity where we exert significant influence but not control are classified in other assets under United States GAAP.

*(o) Minimum Pension Liability*

Under United States GAAP, we must recognize an additional pension liability in cases where the pension obligation, calculated without taking salary increases into account, exceeds the fair value of pension assets at year end. The amount of the minimum pension liability is recognized in other comprehensive income. The pension obligation, calculated without taking salary increases into account, was \$3,582 million and \$3,087 million as at October 31, 2005 and 2004, respectively. Under Canadian GAAP, there is no similar requirement.