BMO Financial Group
Accounting for Purchased loans

How do BMO Harris Bank, N.A. and BMO Financial Corp. (BMO U.S. subsidiaries) account for the purchased loan portfolio?

As a result of the acquisition of Marshall & Ilsley Corporation, we have established an accounting policy for purchased loans. We record loans that we purchase at fair value on the day that we acquire the loans, which includes an interest rate mark for interest rate differentials as well as a credit mark representing an estimate of expected credit losses as of the acquisition date. As a result, no allowance for credit losses is recorded in our Consolidated Balance Sheet on the acquisition date.

For performing loans, the entire credit mark will be amortized to net interest income over the term of the portfolio using the effective interest method. Specific PCLs will be recorded as required when currently performing loans become impaired and require a specific provision. An appropriate general allowance will be built over time as the credit mark amortizes.

Purchased credit-impaired loans are regularly re-evaluated. Increases in the credit mark result in a charge to the provision for credit losses and an increase to the allowance for credit losses. Decreases in the credit mark result in a recovery of any previously recorded allowance for credit losses or an increase in the effective interest rate on a prospective basis.

Does the accounting described above also apply to the Bank of Montreal consolidated results as at October 31, 2011?

The accounting approach will be similar; however, BMO Harris Bank, N.A. and BMO Financial Corp. financial statements are prepared on a US GAAP basis and Bank of Montreal consolidated results are reported under Canadian GAAP. Under Canadian GAAP and IFRS only a portion of the expected credit losses will be amortized and a lower level of general allowance will be built. The accounting for purchased credit-impaired loans will be similar under Canadian and US GAAP, except that decreases in the credit mark will be immediately recognized in income under Canadian GAAP, rather than resulting in a revised effective interest rate as done under US GAAP.

What was the accounting used for the Bank of Montreal financial results in Q3, 2011?

While a different approach was taken in Q3, the impact of loan accounting was not material to the Q3 results. We note that there is no change in our view of the underlying economic performance of the portfolio.