



TD BANK GROUP
Q3 2015 EARNINGS CONFERENCE CALL
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PRESENTATION

Rudy Sankovic – TD – Head of Investor Relations

Thank you, operator, and good afternoon, everyone. We'll begin today's presentation with remarks from Bharat Masrani, the Bank's CEO. After which, Colleen Johnston, the Bank's CFO, will present our third quarter operating results. Mark Chauvin, Chief Risk Officer, will then offer comments on credit quality. After which, we will entertain questions from pre-qualified analysts and investors on the phone. The call will last one hour and end at 4:00 PM.

Also present today to answer your questions are Tim Hockey, Group Head Canadian Banking and Wealth Management; Mike Pedersen, Group Head U.S. Banking; Bob Dorrance, Group Head Wholesale Banking; and Riaz Ahmed, Group Head Insurance, Credit Cards and Enterprise Strategy. Riaz is also responsible for the capital and treasury activities of the Bank.

Please turn to slide 2. At this time, I'd like to caution our listeners that this presentation contains forward-looking statements. There are risks that actual results could differ materially from what is discussed and that certain material factors or assumptions were applied in making these forward-looking statements.

Any forward-looking statements contained in this presentation represent the views of management and are presented for the purpose of assisting the Bank's shareholders and analysts in understanding the Bank's financial position, objectives and priorities, and anticipated financial performance. Forward-looking statements may not be appropriate for other purposes.

I'd also like to remind listeners that the Bank uses non-GAAP financial measures to arrive at adjusted results, to assess each of its businesses and to measure overall Bank performance. The Bank believes that adjusted results provide readers with a better understanding of how management views the Bank's performance. Bharat will be referring to adjusted results in his remarks. Additional information on items of note, the Bank's reported results and factors, and assumptions related to forward-looking information are all available in our Q3 2015 Report to Shareholders.

With that, let me turn the presentation over to Bharat.

Bharat Masrani – TD – Group President and CEO

Thank you for joining us today. As Rudy mentioned, Colleen will be up shortly to discuss our results in detail, but let me start by sharing my thoughts.

This was a strong quarter for TD. All our businesses performed well. The Bank generated EPS of \$1.20, an increase of 4% versus an already elevated quarter in 2014. These results were driven by solid revenue growth, good credit performance, positive operating leverage, and favorable foreign exchange.

Our Canadian Retail segment delivered very good adjusted earnings growth of 8%. We continue to take market share across a number of key categories and posted a strong quarter for new originations in our real estate secured lending business.

Wealth Management achieved double-digit earnings growth driven by strong fee-based revenues and asset growth. These results reflect the benefits of ongoing investments in this business including the addition of

new advisors. Insurance also had a very strong quarter as favorable claims performance contributed to good earnings growth.

Before I leave Canadian Retail, I'm thrilled to highlight a significant accomplishment this quarter. As you know, we pride ourselves on providing legendary service across Canada and the U.S. For the 10th year in a row, J.D. Power has recognized TD as the leader in customer satisfaction among Canadian banks. For as long as this award has existed, TD has won it. And I want to recognize the tremendous efforts of our branch, phone, digital, and ATM teams including various groups that support these businesses. I also want to thank our customers for their tremendous loyalty and for voting us the industry leader in this important category.

Turning back to the quarter, U.S. Retail results were up slightly from Q3 of last year and have increased 5% year-to-date. The business has good momentum. Loan growth is strong. We are acquiring customers significantly faster than our competitors. We are making progress on deepening relationships. Our focus on growing the U.S. wealth business is also going well as assets under management have doubled since we acquired Epoch in 2013. Margins have declined this quarter, but we are increasing our net interest income and making good strides on improving our efficiency ratio.

Wholesale Banking delivered a strong quarter with earnings of \$239 million. These results reflect higher trading revenues and investment banking fees and growth in the corporate lending portfolio. We made good progress building out our U.S. franchise, adding high-quality corporate, institutional and government clients and leveraging the deep relationships we have with customers at TD Bank, America's Most Convenient Bank.

This focus has seen strong growth in our U.S. dollar franchise in the last three to four years. Our TD Securities loan book, south of the border, has been growing at 15% annually since 2013, mainly in high-quality investment grade loans. Our government business ranks third globally in terms of raising U.S. dollar funding for its clients, and we continue to add franchise-building producers across all of our business lines.

On the capital front, our common equity Tier 1 ratio of 10.1% remains strong, and both our liquidity and leverage ratios are comfortably above our targets.

As we look ahead to Q4, we expect that credit losses will remain relatively stable with Q3 and FX will be a positive driver given the stronger U.S. dollar. On the other hand, we expect to see higher expenses and normalization of insurance earnings. Overall, 2015 is shaping up to be a good year for TD, ahead of our expectations.

Now let me talk a little about the current operating environment and what it means for us. In recent months, we've seen further weakening in economic conditions in emerging markets and downward pressure on commodity prices including oil. The Canadian economy likely contracted in the first half of the year and the Bank of Canada reduced interest rates twice.

We are living in uncertain times with increased volatility and financial market turmoil having broader and longer implications. TD is not immune to these macroeconomic forces, but with our lower risk profile and a resilient business model, I'm confident we are well-positioned to weather the storm.

We get paid to take the right risks and manage those risks, and that's exactly what we are doing. Our exposure to oil is relatively small. Underwriting standards remain strong. And to date, the oil and gas portfolio is performing within expectations, and we don't expect material losses. We continue to see originations of high-quality personal and commercial loans across our network, including Western Canada. We're standing by our customers and clients as they adapt to a new reality.

While the U.S. economy also faces uncertainty, the economic outlook is more promising. The U.S. has begun to show signs of recovery, and we will benefit from any future rate increases. The housing market, it keeps improving. Consumer spending is on the rise, in part due to falling energy prices, and labor markets are performing well. With this positive outlook, I like the way we are positioned in the U.S., with a young, high-quality franchise that's growing and taking share.

I'm proud of our performance. TD continues to grow our volumes at a healthy rate, and our focus on service and convenience is driving market share increases across our key markets. Our business model has proven to be resilient, and we are weathering these conditions well. However, we understand that we can't rely on revenue growth alone in this environment, and we continue to look for ways to make TD the Better Bank.

Last quarter, we announced a restructuring charge that reflected the first phase of a Bank-wide focus that will help make us more effective and reduce our rate of expense growth. We are well into the second and final phase and expect to complete most of the work by the end of the year.

As I look forward, our focus on permanently improving our processes will play an important role in enhancing our agility and positioning us for success, but the TD story remains one of growth. I'm equally focused on investing in opportunities that will position us for continued outperformance in our core businesses.

Our leadership team remains resolved to increase efficiency and effectiveness. I'm confident that when we are done, TD will be an easier place to work and a Better Bank for our customers to do business with. I'm excited about our prospects, and I'm proud of how we are becoming fitter and faster the TD way.

To wrap up, it was a strong quarter for TD. I'm pleased with what we have achieved, and I have full confidence that we are taking the right steps to preserve our track record of delivering good results and to invest and adapt for our customers, employees and shareholders.

With that, I'll turn it over to Colleen.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Thank you, Bharat. And good afternoon, everyone. Please turn to slide 4. This quarter, we delivered adjusted EPS of \$1.20, up 4% year-over-year. The quarter reflected strong growth from Retail and Wholesale versus last year, up 10% and 11%, respectively. The Corporate segment posted a loss of \$161 million. We continue to benefit from the favorable currency impact of stronger U.S. dollar.

Adjusted total revenue increased 10% year-over-year net of claims or 5.3% excluding FX, led by strong loan, deposit and wealth asset growth in addition to higher insurance, fee-based and trading revenue. Growth this quarter was partially offset by margin compression.

Adjusted expense growth was 9% year-over-year or 3.6% excluding FX. Expense growth was driven by increased investment in technology modernization and new capabilities and regulatory infrastructure, partly offset by productivity gains.

We were pleased to post strong operating leverage, reflecting good revenue growth, positive claims experience and prudent expense management. We remain focused on delivering sustained productivity improvement. Overall, a strong result for the Bank this quarter.

Please turn to slide 5. This slide presents our reported and adjusted earnings this quarter, with the difference due to three items of note which you have seen before. The litigation item reflects the recovery related to certain litigation matters recognized as an item of note in prior quarters.

Please turn to slide 6. Canadian Retail delivered a strong quarter with adjusted net income of \$1.6 billion, up 8% year-over-year. The increase was driven by continued good loan and deposit growth, very strong insurance earnings and wealth asset growth, partly offset by higher expenses.

Loan and deposit growth was good this quarter. Total loan growth was 5% year-over-year with real estate secured lending volume up 4%, business lending growth up 9%, and auto lending up 17%. Deposits increased by 6% due to strong growth in core checking and savings account, which were up 9%. Business deposits grew 7%.

Margin declined 1 basis point sequentially, primarily due to the impact of a credit mark release and the acquired credit card portfolio last quarter, and a low rate environment, partially offset by seasonal factors. For Q4, we expect margins to remain under pressure due to mix, seasonal factors and competitive pricing.

PCLs increased 4% year-over-year. Personal PCLs decreased \$11 million, due mainly to lower credit card, personal lending and auto provisions. Business banking PCLs increased \$20 million year-over-year.

Adjusted expenses were up 4% year-over-year, primarily due to higher employee-related costs, including higher revenue-based variable compensation in the wealth business and business growth, partially offset by productivity savings. Canadian Retail produced positive operating leverage when insurance claims are netted from revenue. Overall, a strong result from Canadian Retail.

Please turn to slide 7. U.S. Retail, excluding TD Ameritrade, posted adjusted earnings of US\$450 million, up slightly from Q3 of 2014. Results for the quarter reflected strong volume growth and disciplined expense management, largely offset by margin compression and normalizing credit losses. Revenue increased 1% year-over-year, as industry-leading volume growth and broad-based fee growth were partially offset by lower loan margins.

Loan and deposit growth remained very strong in the third quarter. Total loan growth was a strong 11% year-over-year, with a 4% increase in personal loans, and a 17% increase in business loans. Average deposits increased by 6%.

Margin declined 12 basis points quarter-over-quarter. Roughly half of the decline was attributable to our U.S. partner card programs and hedging-related items which were offset in other income. The balance of roughly 6 basis points was due to lower loan margins in commercial and auto loans and the impact of the low rate environment on deposit margins. We expect margins to remain under pressure due to continued competitive pricing and the low rate environment.

PCL increased 36% year-over-year mainly due to higher provisions for commercial loans as a result of an allowance build, partially offset by a decrease in personal banking PCL.

Expenses declined 1% year-over-year due to ongoing productivity savings, partially offset by higher expenses to support growth and higher regulatory cost. Our adjusted efficiency ratio has improved by 110 basis points year-over-year.

Earnings from our ownership stake in TD Ameritrade in U.S. dollars increased 7% year-over-year, due primarily to increased asset growth and transaction revenue, partially offset by higher operating expenses. Overall, good fundamentals from the U.S. bank which has driven 5% earnings growth in U.S. dollars on a year-to-date basis.

Please turn to slide 8. Net income for Wholesale was \$239 million, up 11% year-over-year, a very strong result. Revenue increased 13% year-over-year, due mainly to higher fixed income and equity trading, M&A fees and corporate lending, partially offset by lower equity underwriting fees compared to a strong Q3 of 2014. Non-interest expenses were up 10%, driven primarily by higher initiative spend, the impact of foreign exchange translation and higher variable compensation. ROE this quarter was 17%.

Please turn to slide 9. The Corporate segment posted an adjusted loss of \$161 million in the quarter, compared to a loss of \$53 million in the same period last year. The higher loss was the result of lower favorable tax items in the current quarter and ongoing investment in enterprise and regulatory projects and initiatives.

Please turn to slide 10. Our Basel III common equity Tier 1 ratio was 10.1% in the third quarter versus 9.9% in Q2. The increase reflects solid organic capital generation, partly offset by increased RWA, mainly due to volume growth. Both our leverage and liquidity ratios are consistent with last quarter. Overall, we continue to remain well-positioned for the evolving regulatory and capital environment.

With that, I'll turn it over to Mark.

Mark Chauvin – TD – Group Head and Chief Risk Officer

Thank you, Colleen. Good afternoon, everyone. Please turn to slide 11. While we've seen an increase in the provision for credit losses up \$47 million or 12% quarter-over-quarter and \$114 million or 35% year-over-year, the increase is attributed to the normalization of loss rates in the U.S. portfolio to a combination of increases in commercial and retail allowances to support volume growth, seasonal trends in consumer credit volumes and lower recovery levels as workout activity continue to reduce. The Bank's loss rate was flat at 33 basis points for the quarter with gross impaired loans stable at 57 basis points, up 1 basis point over the previous quarter and 2 basis points year-over-year.

The oil and gas portfolio continues to perform within expectations, and we have yet to see a meaningful deterioration in consumer credit quality in the impacted regions. Oil and gas outstanding exposure remains stable, representing less than 1% of total loans and acceptances. While we continue to maintain a cautious approach across retail and non-retail exposures impacted by low oil prices, I do not currently believe that low oil prices will result in a material increase in credit losses. In summary, credit quality remains strong across the bank as we head into the fourth quarter.

With that operator, we are ready to begin the question-and-answer session.

QUESTION AND ANSWER

Operator

Thank you. The first question is from John Aiken from Barclays Capital. Please go ahead.

John Aiken – Barclays – Analyst

Good afternoon. Bharat in his opening comments talked about TD being a growth bank, and I immediately then flipped to the indirect auto growth that you had on both sides of the border. I found that very interesting based on commentary that one of your competitors said they were actually tapping the brake in terms of that loan growth. So, Tim, can you let us know what your philosophy is in terms of this portfolio, and importantly, what you're seeing in terms of some of the longer-term lending practices that are going on in the marketplace?

Tim Hockey – TD – Group Head, Canadian Banking & Wealth Management

Sure, John. We were actually quite comfortable with this portfolio. We've had great growth through the years. The dynamic, of course, is that the auto sales continue to be strong. Just so you know, we made some investments in that particular business, and we introduced a new system this past spring and so we're seeing some of the results of that. The overall trends, if you're worried about it at this point in the cycle, we continue to see the, call it, average credit score in that business, essentially being flat through the years. We're actually a little bit below industry average when it comes to loan to value on the prime book. We're basically on market at an on-prime book, but we're still very comfortable with this particular business. We think it's an important growth area for us.

Mike Pedersen – TD – Group Head, U.S. Banking

John, it's Mike. Maybe I'll comment from a U.S. perspective. This is obviously a category where we continue to see good growth, and our new dealer strategy is paying off. We're focused mostly on super prime and prime, a little bit of near prime. And we've reduced our expense base, and both our credit and profitability metrics are improving. And as with the case of Tim's comments on Canada, all of the key and risk metrics, the stuff we're writing is better than our portfolio. So, we're improving our risk posture in this business. As things stand, I'm comfortable with it.

John Aiken – Barclays – Analyst

That's great. From a competitive standpoint though, are you guys being forced to chase the terms that are being pushed out?

Mike Pedersen – TD – Group Head, U.S. Banking

No, nor is that the case in the U.S. In fact, as I alluded to including on term, the originating terms are lower than the portfolio terms, and they're well within normal risk parameters. We're not chasing the strategy stuff.

John Aiken – Barclays – Analyst

Good. Thanks guys.

Operator

Thank you. The next question is from Meny Grauman from Cormark. Please go ahead.

Meny Grauman – Cormark Securities – Analyst

Hi good afternoon. First question, I want to follow up on the commentary you made. You talked about how you haven't seen any meaningful deterioration in consumer credit quality in affected regions, in the oil-producing regions, and I'm wondering why you think that is? Are there are some reasons that you think that's causing this?

Mark Chauvin – TD – Group Head and Chief Risk Officer

It's Mark, I'll answer that. I think that we still feel it's probably early and it's probably still to come. You can certainly see in those markets that unemployment is going up. We're just not seeing it translated to our delinquencies yet. But I still think in the next quarter or two that we will see it come in to the levels that we kind of expected when we kind of went down this road.

To put it maybe into context, we feel that at a \$35 oil price, that gradually recovers into the \$40s then into maybe \$50 over a four-year period, that you might look for an increase on the direct and indirect which would cover the consumer area of about 5% to 10% per year. So we think that that's probably likely to come. We just haven't seen yet, but we're watching it closely.

Meny Grauman – Cormark Securities – Analyst

Thanks for that. And I just wanted to switch gears, and I think this one's for Tim. I just want to ask about the Canadian mortgage market, and there are definitely headlines over the past few months about fraud. And I'm wondering from your perspective how big a problem do you think fraud is in Canada? And do you think that there is more fraud going on now in the system than, say, five years ago?

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yes. So, it's Mark again. I'll take that from maybe a risk perspective. We follow in our underwriting standards verification of income, and the down payment is very important and central to the process. So, we will do that through several means, and we will do it until we're satisfied that we have it right. So, it can be tax returns. If they're a customer of the Bank, it would be through automatic deposits to their accounts or it would be verification from employers that we would even reach out and call to them, call an employer if necessary.

But in addition to that, we do have fraud analytics that looks to assess the reasonableness of a declared income to make sure it makes sense. And my comfort that it's working effectively is that we do have a quality assurance program that follows up behind that, and we even do that for mortgages that we buy from other second-tier areas. When we buy them, we do go in and look at it. And it's effective in detecting those fraud situations and picking them up. And so, I'm quite comfortable that we're effectively managing it. We have the proper risk mitigation in place. I don't think necessarily that it's gone up over time, though, to tell you the truth.

Tim Hockey – TD – Group Head, Canadian Banking & Wealth Management

And, Meny, if I can just add, I think if you look back, to your point, five years ago, the heightened level of scrutiny on this market, both by all of us as lenders as well as the regulators – the Ministry of Finance – basically in terms of the tightening, my sense is that, if anything, it would have gone down a little bit, and there's certainly a higher degree of scrutiny on that type of activity.

Meny Grauman – Cormark Securities – Analyst

Thanks for that.

Operator

Thank you. The next question is from Stephen Theriault from Bank of America Merrill Lynch. Please go ahead.

Steve Theriault – Bank of America Merrill Lynch – Analyst

Thanks very much. I can start with a couple maybe quick questions for Mark. Mark, so I'm referring to slides 20, 21 and 22 in the deck. And maybe it's obvious but I'll ask anyway. When I look at TD versus Canadian peers versus U.S. peers, you have those three tables there. On gross impaireds, TD's screens, quite favorably, on credit provision, quite favorably as well.

But I look at the formations and may be topical given all the questions around credit these days, I noticed TD's formation in terms of basis points is higher than Canadian peers which maybe isn't too surprising but higher than U.S. peers as well. I'm wondering maybe – hopefully, my question's been long-winded enough to give you a chance to take a look at those. And if you could provide some insight as to why that is, that'd be helpful.

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yeah. I mean the increase in gross impaired loan formations really is focused in the U.S. primarily, relatively constant in Canada period-over-period. And in the U.S., what we're working through is in the HELOC portfolio, we have two legacy effectively interest-only products. One is an evergreen, so the individual in the HELOC portfolio can stay on interest-only payments for an extended period of time when the product was originally sold. And then what we refer to is a 5-5-10 product which means that it's got a 5-year interest-only period, followed by another 5-year, then amortization over 10. And these are legacy products that, over the years, with the tightening of the underwriting standards, these are products that we don't offer any longer.

And so, as we go through the portfolio, we're renewing these customers. And so if it's an interest-only or we're looking to qualify them under the current standards. And the standards are higher, and they're more rigid, appropriately so. And so if a customer does not qualify, then we are required to designate them impaired. It's a regulatory requirement – it's called TDRs – and they go into the impaired although they are still making their payments.

If you look at the formations for the quarter, 90% of those were customers that were making payments. It's just that they couldn't qualify under the current standards. And if you look at the overall impaireds for HELOC, it's about 60% that are currently making their payments themselves. So, we're about a year or so into this process. We feel that we've reserved appropriately for those based upon our experience going forward.

As the U.S. economy continues to strengthen, we think that these will get better and probably the risk of loss is not – we don't really see it as a high expected loss portfolio. But it will have an impact on our impaired formations and gross impaired loans for a period of time, I'd say, for the next three years or four years.

Steve Theriault – Bank of America Merrill Lynch – Analyst

Okay that makes sense. It's probably just a much bigger part of your mix than it would be for some of those U.S. comps in the table?

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yes, true. And I guess I don't study the others as well.

Steve Theriault – Bank of America Merrill Lynch – Analyst

And then a quick one for Colleen. Colleen, in Q2 when you announced the restructuring charge, you hinted a Q4 charge, but the work was still being done and may still very well be ongoing. But wondering if you can give us a sense for whether in terms of order of magnitude, it will be in a similar range or not when we roll around the Q4 in December.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Hi, Steve. So, the work is still ongoing, and I don't have a solid number at this point in the process. But I think we're probably looking at an order of magnitude of somewhat similar to the Q2 charge, although I would expect, at the moment, that it will be smaller than what you saw in Q2, but more to come in the fourth quarter.

Steve Theriault – Bank of America Merrill Lynch – Analyst

Okay. That's helpful. Thanks so much.

Operator

Thank you. The next question is from Robert Sedran from CIBC. Please go ahead.

Rob Sedran – CIBC World Markets – Analyst

Hi. Good afternoon. I just wanted to come back, Colleen, to your comments around the U.S. margin to make sure I understood them. So I guess half that was related to loan and deposit spreads, was any of that mix or is all that just competition?

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

So, I'll start out and then maybe hand it over to Mike to embellish a little bit. If you look at about half the margin decline, in the past, we have called out the U.S. card partner programs, and that can have an effect on the margin. And in particular, there was some accretion last quarter which didn't recur.

And also, we had – and I'm sorry to cite accounting movements, but I must do so – we did have a shift between NII and other income related to our fair value hedges. And you can see that sequentially that our other income in the in-source currency increased quite a bit. So I'd say I call about half of the margin decline was related to those two items. And then I'll turn it over to Mike to talk about the relative growth rates in our various portfolios and how that's affected the margin.

Mike Pedersen – TD – Group Head, U.S. Banking

I think the answer to the question is that it was partly mix. So, the margin did decline a bit more than we expected this quarter but mostly because we grew faster than we expected, and that was especially in larger commercial loans and in super prime auto lending. In this environment with origination margins lower than portfolio margins, if you're outgrowing the market in lending, you're subject to more margin pressure, but still good NII business.

Because we had larger-than-expected growth in larger commercial loans and in super prime, we saw a little bit of this, so you could call that mix. But I would just say that this represent good NII business with good credit quality but lower margins, but you'd want us to do this business. And you can see it in our NII. We grew our lending, and our revenues increased by US\$60 million quarter-over-quarter. So our focus is on growing our revenues and profits more than just managing to the NIM target. And in the last couple of years, we've grown our net interest income faster than both our big bank and regional bank competitors.

Rob Sedran – CIBC World Markets – Analyst

And so if I can tie that back to Colleen's comments about the pressure to be ongoing, presumably far less than what was shown this quarter.

Mike Pedersen – TD – Group Head, U.S. Banking

I think we're hesitant to put precision around this, but on balance, I would expect that it's most likely that we'll see some continued downward pressure. And that's especially if we continue to see good loan growth or better than market loan growth. I would just add that rate increases would obviously mitigate this.

Rob Sedran – CIBC World Markets – Analyst

Thank you.

Operator

Thank you. The next question is from Mario Mendonca from TD Securities. Please go ahead.

Mario Mendonca – TD Securities – Analyst

Good afternoon. Mark, first, could you just explain what you meant by the 5% to 10% increase when you were describing the expected increase and current losses? Did you mean 5% to 10%? Sorry...

Mark Chauvin – TD – Group Head and Chief Risk Officer

When we ran many stress tests and looking at the impact of low oil prices. But if you look at the one that I think is probably the most appropriate, that's the \$35 gradually increasing as I indicated earlier. And when you look at that, the incremental increase to the low oil prices in the direct, so that would be the oil and gas sector, the services sector; and the indirect would be largely consumer credit in those regions that are most impacted by low oil prices, we would expect versus current PCL levels, an increase in the 5% to 10% per year range.

Mario Mendonca – TD Securities – Analyst

Annually, so call it for the next three years if that's the way...

Mark Chauvin – TD – Group Head and Chief Risk Officer

I'm not sure I would go three years but say per year. My thinking is two, but...

Mario Mendonca – TD Securities – Analyst

Okay. That's fair. Colleen, with – the next question I'm going to ask I've had some varying degrees of success on the calls. But given what Mark's just offered about the what seems kind of like a modest increase in PCLs, the question I have is in that environment, do you think the Bank would be capable of growing earnings even just modestly year-over-year?

Mark Chauvin – TD – Group Head and Chief Risk Officer

So, Mario, maybe...

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Mario, we'll start with Mark. Mark is responsible for all of the stress testing and all of the moving parts and comments specifically on oil. And then I'll wrap it up, Mario.

Mario Mendonca – TD Securities – Analyst

Okay.

Mark Chauvin – TD – Group Head and Chief Risk Officer

In looking at the view of what is the impact of low oil prices to the Bank effectively, I mentioned the credit element. There's positives and negatives. So, the most obvious negative is the credit element, which I mentioned. But also in that scenario, we would look for reductions in interest rates. And we've seen two from the Bank of Canada already that are kind of factored into the analysis itself. And then we would also look for just revenue reductions due to the lower GDP growth.

But on the other side, looking at the positives, the reality is with low energy prices, we would expect higher consumer spending in our largest markets being Central Canada and Northeastern U.S. And we would expect those to have stronger growth. And also in that scenario, you would certainly see a low Canadian dollar which we're seeing today. And that would have a positive impact on FX translation on our U.S. earnings.

The net impact of the positives and negatives of our stress testing is kind of a neutral position. So we feel we're pretty well-positioned to weather this situation, given our relatively lower exposure to oil and gas itself, plus where our larger markets are, and coupled with the U.S. operations, to arrive at a neutral impact over that two-year period.

So I'll pass it over to Colleen.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Yeah, Mario. Just to conclude, talking about 2016, our planning process is still underway. It's probably a little early to comment on specifics. But I think if you take Mark's comments and then what I would say is that absent any other shocks, we don't necessarily see low oil prices impacting our growth trajectory. And obviously, we are working on productivity improvements which should help us in 2016. So net-net, as I say, we would still see some growth.

Mario Mendonca – TD Securities – Analyst

That's what I was looking for. Thank you.

Operator

Thank you. The next question is from Gabriel Dechaine from Canaccord Genuity. Please go ahead.

Gabriel Dechaine – Canaccord Genuity – Analyst

Hi. Good afternoon. Just the two-pronged on the expense question here. The seasonal increase, I think you guided to it last quarter that we'd still see it in Q4 this year. I'm just wondering if we're going to see a similar magnitude of quarter-over-quarter spike as we did last year which was on the high side.

And then also on the restructuring charge, help me understand the benefit for investors. If it's not a tangible EPS figure that's going to come of the cost cutting in this program, like what's – will TD be able to deliver a sub-3% growth in perpetuity, something along those lines? I think that could be helpful.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Okay. Gabriel, let me start with your first question regarding our Q4 expense increase. I'm going to give you some numbers here, and I'm going to express them in an adjusted basis and I'm going to exclude foreign exchange.

Gabriel Dechaine – Canaccord Genuity – Analyst

Sure.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Over the past couple of years, we've had an average quarter-over-quarter growth in the fourth quarter of just over 6%. This year, I do still expect an increase, but I'd be surprised if the rate of increase isn't substantially lower, again in percentage terms in the last two years. But I will caution off the top that based on where foreign exchange rates are going, I think the headline number quarter-over-quarter will look higher because of FX.

Gabriel Dechaine – Canaccord Genuity – Analyst

Yeah.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

On a Q3 year-to-date basis, our expenses again, excluding foreign exchange and M&A, increased by 3.6%. And if I'm right about Q4, this means that our full-year expense growth rate will definitely come down from the Q3 year-to-date level. So, we're definitely on the case, I can assure you.

Gabriel Dechaine – Canaccord Genuity – Analyst

Okay. That's very helpful.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

To move on to your second question. Really, the message isn't different from what we told you last quarter. If you look at our expenses this year, and I just mentioned the 3.6% growth and I'm talking on a year-to-date basis now, so I'll just give you some moving parts. Higher project and initiative spend drove about 2% growth in our total expenses, and then our base expenses are up on a year-over-year basis as well, and that always has to come in to the picture.

We are giving increases to our frontline staff. Our business volumes are growing. So that also means that our expenses will increase. And then what we're doing, we've been doing for several years and we'll continue to do at a greater rate, is then we need productivity gains to bring our rate of expense growth down. So this year, as I say 3.6%. And part of that growth, by the way, is variable comp that's linked to revenues. So that sort of gives you the picture of where we are.

When you think about as we head into next year, we expect that project and initiative spend will increase. But again, we're spending at important areas already this year. But you look at things like digital and mobile capabilities, although we're keeping our retail distribution cost in total at a very reasonable growth rate, technology modernization and transformation is really important. And that's to improve our agility and to reduce cost.

Regulatory infrastructure is an area of spend and particularly on aspects of Dodd-Frank. And also, as you look to next year, we do – the fact that we are increasing our project spend means that we will have higher depreciation cost going forward because some of our project costs are capitalized. We will continue to have base increases going forward and again for the same factors that I mentioned just a minute or so ago.

The key is what do we do in terms of productivity, and we've got to frankly increase the rate of productivity gains from what I've cited on a year-to-date basis. And that's where restructuring is going to help us. So the name of the game here is that what we want to do is make sure that we can slow down our rate of

expense growth. You're not going to see a year-over-year decline in expenses. That just isn't reasonable in this environment. But what we do want to do is reduce our rate of expense growth.

And people ask me, well, what are you doing that will fall to the bottom line? That will fall to the bottom line and assuming we obviously want to make sure that we can grow our revenues at a decent rate given the environment. So that's how we're thinking about expenses generally.

Gabriel Dechaine – Canaccord Genuity – Analyst

Okay. That's very helpful. Just a really quick one, Bharat, you mentioned the normalization of insurance earnings. It was a big spike this quarter in growth. What was the contribution from – what should I call it – the claim, positive claims development, or...

Bharat Masrani – TD – Group President and CEO

Riaz? Yeah.

Riaz Ahmed – TD – Group Head, Insurance, Credit Cards & Enterprise Strategy

It's Riaz here, Gabriel.

Gabriel Dechaine – Canaccord Genuity – Analyst

Sure.

Riaz Ahmed – TD – Group Head, Insurance, Credit Cards & Enterprise Strategy

I don't think we normally disclose that on a quarter-over-quarter basis. But I can say that if you look at the claims number on a year-over-year basis, it's down quite a bit. Half of that order of magnitude is because, as I'd mentioned in Q2 2015, that we're shedding some low value international activity, and so that brought our claims cost down a fair bit without having any meaningful impact on NIAT.

And then the other half is in Q2 and Q3, we've had terrific weather. So, our current year claims are down. We're seeing the emergence of some favorable developments, and then we didn't have any material catastrophes to speak of. I think that's what's causing us to have two very strong quarters.

Gabriel Dechaine – Canaccord Genuity – Analyst

Thank you, Riaz.

Operator

Thank you. The next question is from Sumit Malhotra from Scotia Capital. Please go ahead.

Sumit Malhotra – Scotia Capital – Analyst

Thanks. Good afternoon. Just to start with Bharat since we're there on insurance. Two years ago at this time, we had some conversations after the events in Calgary about whether the P&C insurance business was a good fit for TD's Canadian Retail operations, just given some of the consistent volatility we had seen. It's been a much better year from a claims experience perspective. Riaz has talked about some of the improvements you've made in the business. And it's also been a period where there has been M&A activity in P&C insurance domestically. Now that the business is fixed up or running better, have you given some additional thought as to whether it is a fit with what you want the brand to be in Canadian Retail?

Bharat Masrani – TD – Group President and CEO

Sumit, yes. The business continues to be core for us. Yes, we did have some issues. And as you rightly pointed out, we fixed those issues. We have adjusted our model to make sure that we take into consideration events like what happened in Calgary, so that is part of how we run the business. And frankly, we see some synergies enabling the TD brand in that business, and we can leverage that. And it is a good returning business as we saw this quarter.

Overall, we feel pretty comfortable with where we are, and we will continue to find ways to make sure that we are growing this business appropriately and in a manner that provides us with good returns. But overall, very happy with it and it continues to be core.

Sumit Malhotra – Scotia Capital – Analyst

All right. That's straightforward enough. And then one quick one hopefully for Mark since you were giving us some color on how you're thinking about the stress test process. If I look at on a year-over-year basis, we've obviously seen a significant decline in oil prices, yet unemployment in Canada as a whole basis, the unemployment rate is actually lower. When you run your stress scenario, how are you envisioning the trend in domestic unemployment? And I ask specifically due to the fact that the Bank is a bigger domestic credit card player than it was when we had the last credit cycle in Canada.

Mark Chauvin – TD – Group Head and Chief Risk Officer

Well, when we did our low oil price scenario, I mean we did look at it on a regional basis. And our scenario played out that there would be an increase in unemployment in those impacted regions in the range of from then existing levels of 40% to 50%.

And if you look at the increase in credit losses that I mentioned, the 5% to 10%, two-thirds are largely driven in the unsecured sector, which would be cards. I would include indirect auto in that as well. That's really the major driver of the increasing credit losses versus the direct exposure to the actual oil and gas producers.

Our experience in the oil and gas producers has played out very similar to how we projected last January in terms of – we have seen negative migration in the portfolio, but we've had no surprises in terms of accounts. The accounts that went down are ones we thought would go down. We've had four go into impaired status, but two of those were paid out relatively quickly. And we've only got two left in the account at above \$30 million. And actually, we've seen about \$400 million or 10% of portfolio pay out, and it was the higher risk accounts that were refinanced or taken out by acquirers. So, yes, the unemployment certainly factored into it, and it is credit cards as a driver. But we think it's well within the range of being – it's within what we would have expect our – call it, our risk appetite.

Sumit Malhotra – Scotia Capital – Analyst

And sorry, just so I have this right. I may have missed it earlier. When you say 5% to 10%, are you talking on a dollar basis on the...

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yes.

Sumit Malhotra – Scotia Capital – Analyst

...domestic provisions, a 5% to 10% lift?

Mark Chauvin – TD – Group Head and Chief Risk Officer

Correct.

Sumit Malhotra – Scotia Capital – Analyst

Thanks for your time.

Operator

Thank you. The next question is from Sohrab Movahedi from BMO Capital Markets. Please go ahead.

Sohrab Movahedi – BMO Capital Markets – Analyst

Thanks. Just quickly for Mike. Are you happy with the performance of the U.S. Retail segment in source currency?

Mike Pedersen – TD – Group Head, U.S. Banking

Sorry. I didn't catch the last bit of your question.

Sohrab Movahedi – BMO Capital Markets – Analyst

Just in source currency, so negating the FX impact, are you happy with the performance of the segment?

Mike Pedersen – TD – Group Head, U.S. Banking

I am happy with our performance in the circumstances that we're operating in. It's, as you know, difficult in terms of the low rates and the fitful economic expansion and traction, as well as the competition. As I look at the major elements of our performance, we're doing very well versus our end market competitors. We're doing well on earnings. We're doing well on revenues. We're doing well on expenses. To have 200 basis points positive operating leverage this quarter is a nice thing to have in this kind of environment. Our expenses are down for the whole year, year-to-date by 1% compared to last year.

So, I'm happy in the sense that we're outperforming our end market competitors in a very difficult environment. I'm obviously hopeful that we get some assist in terms of the economy and rates. But in the absence of that, I think we have enough levers at our disposal in terms of deepening relationships with customers and improving our distribution strategy and the productivity agenda that we can continue to generate earnings going forward no matter what the – within reason – no matter what the circumstances are. And year-to-date, our earnings are up 5%. I would have taken that at the beginning of the year if you said it was possible.

Sohrab Movahedi – BMO Capital Markets – Analyst

Okay. But just to push on that a little bit, I mean it looks like the credit environment has turned anyway for your portfolio in the U.S. You've got some incremental loan losses. Absent recoveries, that's just going to be there. And you were able to offset that with the lower expenses this quarter like year-over-year. If credit continues to not deteriorate, but at these types of levels trend higher and revenue environment stays such that the best you can do is grow lower margin but higher volume business, how much leverage do you think you have on your expense line to continue to get the bottom line in and around these types of levels?

Mike Pedersen – TD – Group Head, U.S. Banking

I'd say we understand that in this environment, for the reasons that you've articulated, that we need to be very focused on the productivity and expense management agenda. And, as I alluded to before, we are and we have been and we continue to be in terms of – it's difficult. It's a little early to look at next year. But I think we will continue to see that expense management will help us moderate that rate of expense growth. And our focus is to try to continue deliver positive operating leverage even, as we're investing for

future growth in things like our card business and our wealth business and our technology and digital platforms and so on.

Sohrab Movahedi – BMO Capital Markets – Analyst

Okay. Thank you very much.

Operator

Thank you. And the next question is from Stefan Nedialkov from Citigroup. Please go ahead.

Stefan R. Nedialkov – Citigroup – Analyst

Good afternoon and also good evening from London. Two questions. The first one on the U.S. assets, you obviously have been quite interested in buying portfolios, small books, et cetera. Could you just give us a little bit about the criteria that you have and the minimum hurdle, return, size, et cetera; and also maybe a little bit about the type of credit assets, that is cards, et cetera? And is there anything on the horizon right now that could be of interest to you?

And the second question is now that your assets are higher than RBC, or I guess some of your other competitors, I really should say, have you had any discussions with OSFI or with any other regulators in terms of the potential inclusion on the G-SIFI list? You are a significant bank in the U.S. and you are a significant bank in Canada which are obviously two quite important banking systems on a global scale. Does that potentially make you a G-SIFI down the road?

Mike Pedersen – TD – Group Head, U.S. Banking

It's Mike. I'll take the first part and then I'll let Riaz take a stab at the second. I would say that our focus on the U.S. business is on organic growth at this time. As I said before, we feel we've got lots of levers to pull, and that's our primary focus. We do, of course, look at things as they come up from time-to-time. And in that respect, I'd say we're more focused on potential asset place in the line of the Nordstrom kind of thing or similar things than we are on, for example, larger branch space acquisitions. But our focus is on organic growth.

Riaz Ahmed – TD – Group Head, Insurance, Credit Cards & Enterprise Strategy

Stefan, it's Riaz. I'd say on the question of becoming a G-SIB, as you know, both under the BCBS as well as the U.S. rules, test is a multi-factor weighted test of which the balance sheet is only one factor to be considered. So we've been, in our calculations, nowhere near being designated a G-SIB, either internationally or in the U.S.

Stefan R. Nedialkov – Citigroup – Analyst

Okay. Great. Thank you.

Operator

Thank you. The next question is from Doug Young from Desjardins Capital Markets. Please go ahead.

Doug Young – Desjardins Securities – Analyst

Good afternoon. So, most of my questions have been asked and answered. I guess the one that I was kind of just hoping you can enlighten me on is the collective IBNR did increase, I think, in U.S. dollars, \$48 million, and I think that's different than – I think the impact or what caused that was different than what caused the gross impaired loans increase, and I think you refer to it as allowance build. Can you flesh that out for me in terms of what that relates to you?

Mark Chauvin – TD – Group Head and Chief Risk Officer

It's Mark. There are two factors that are driving that. One is as you grow volumes – and the U.S. is experiencing good volume growth – you are adding to your reserves, and it's showing up in the IBNR. And the second area is there is a seasonal nature to two of the asset categories such as credit cards and indirect auto which typically, in the second quarter or the quarter ending April, tend to have improvement in quality which results in a reduction in your allowances as well as a reduction in volume through payouts.

But that naturally comes back in the third quarter, and so we've seen that swing in the third quarter in cards and indirect auto which was really totally within our forecast. But it resulted in the – those increased in the allowance as well as with the commercial side. But it was driven by effectively volume I guess is the simple answer.

Doug Young – Desjardins Securities – Analyst

Volume. And so, you would expect it to reverse in the next quarter, is that essential?

Mark Chauvin – TD – Group Head and Chief Risk Officer

Well, I think the volume will stay – well, I would expect it to stay constant...

Doug Young – Desjardins Securities – Analyst

Okay.

Mark Chauvin – TD – Group Head and Chief Risk Officer

...to increase with volume but not to the same extent because the seasonal factor won't play as much a factor in the next quarter. And everything else being equal, just so we'd be in pace with volume.

Doug Young – Desjardins Securities – Analyst

I just want to – yeah, so this has nothing to do with migration. It's more of a volume...

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yeah.

Doug Young – Desjardins Securities – Analyst

...driver.

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yes. Not credit qualities. It would be migration.

Doug Young – Desjardins Securities – Analyst

Okay.

Mark Chauvin – TD – Group Head and Chief Risk Officer

And so, we look at it. And we decomposed it, and it was driven by volume, not credit quality.

Doug Young – Desjardins Securities – Analyst

Okay. And then just second, I guess, Colleen, on the CET1 ratio – let me go back up here – do you hedge out your FX risk within the CET1 ratio or no?

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

I can turn this to Riaz but the answer is yes, we do.

Riaz Ahmed – TD – Group Head, Insurance, Credit Cards & Enterprise Strategy

Yeah.

Doug Young – Desjardins Securities – Analyst

Okay.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

So I just answered it!

Doug Young – Desjardins Securities – Analyst

Yeah, perfect. That's all I need. Thanks.

Riaz Ahmed – TD – Group Head, Insurance, Credit Cards & Enterprise Strategy

I agree.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Riaz concurs, luckily.

Doug Young – Desjardins Securities – Analyst

Thanks.

Colleen Johnston – TD – Group Head, Finance, Sourcing & Corporate Communications, and CFO

Yes, we do.

Doug Young – Desjardins Securities – Analyst

Good. Thank you.

Operator

Thank you. The next question is from Peter Routledge from National Bank Financial. Please go ahead.

Peter Routledge – National Bank Financial – Analyst

Thanks. I just want to come back to Meny's question a little earlier about the mortgage approval process. I'm kind of having a hard time reconciling the diligence you talked about, and your peers talked about as well with sort of the service aspiration of turning around approvals in 24 hours. What would you say to a skeptic who thought, well, there's no way they can hit their service goal and due diligence and there has to be corner cutting in that due diligence?

Tim Hockey – TD – Group Head, Canadian Banking & Wealth Management

Well, those are the standards that we actually have negotiated. It's Tim answering here. What we've changed in the last little while is we entered into an outsourcing relationship with First National, and they have a very dedicated senior lending team. What we do is we've basically outsourced our adjudication and our funding of the mortgages. They are writing to our specifications.

There is no auto-adjudication, which to your question, might, impact your turnaround times, but we've negotiated as part of our pricing the ability to actually get those approval rates back and quickly. And we've seen a substantial improvement in the turnaround times to the brokers which is one of the reasons why we're up strongly in real estate secured lending.

We're quite comfortable. And given this is a relatively new relationship, the oversight that we put in place with the TD folks on the ground is measuring to a brand new – newly established standard of care.

Mark Chauvin – TD – Group Head and Chief Risk Officer

I would only add, Peter, is that the verification of income or the down payment can occur after the approval. It's in the fulfillment process.

Peter Routledge – National Bank Financial – Analyst

Okay. So you have – you can still give it...

Mark Chauvin – TD – Group Head and Chief Risk Officer

So you approve it based upon...

Peter Routledge – National Bank Financial – Analyst

...conditional approval and then – yeah, okay.

Mark Chauvin – TD – Group Head and Chief Risk Officer

Yeah. Fulfillment is after that. They have to – you have to have all that documentation in order to fund, and you may identify the problem then, and not fund.

Peter Routledge – National Bank Financial – Analyst

One other question. If despite all these, at some point, it's found that a small but productive cohort of third parties have put or submitted mortgages with faulty or misrepresented underwriting data and those insured mortgages are sitting on TD's balance sheet, could your mortgage insurers deny the claims on those mortgages even if no TD employee was directly or indirectly involved in that misrepresentation?

Mark Chauvin – TD – Group Head and Chief Risk Officer

The insurer's position, they refer to it as 'fraud for shelter' and that's where – someone may overstate their income in order to get into a house. As long as there has been no employee of the organization involved in that, their position does not invalidate insurance.

Peter Routledge – National Bank Financial – Analyst

Thank you. That's very clear. Appreciate it.

Operator

Thank you. There are no further questions at this time. I will now turn it back to Bharat Masrani for closing remarks.

Bharat Masrani – TD – Group President and CEO

Thank you, operator. As you've heard with all the answers and again most importantly, the results, we're very proud of how the teams have delivered yet another strong and growing number from TD. Thank you to everybody for a terrific job well done and hopeful to seeing you in the next 90 days.