Operator

And welcome to today's third quarter earnings review program. At this time, all participants are in listen-only mode. (Operator Instructions) We'll take questions in turn during our Q&A session. And please note, today's call is being recorded.

It's now my pleasure to turn the program over to Kevin Stitt. Please begin sir.

Kevin Stitt

Good morning. Before Brian and Bruce begin their comments, let me remind you that this presentation does contain some forward-looking statements regarding both our financial condition and financial results, and that these statements involve certain risks that may cause actual results in the future to be different from our current expectations. For additional factors, please see our press release and SEC documents.

And with that, let me turn it over to Bruce.

Bruce Thompson

Thanks Kevin, and good morning, everyone. I am going to start the presentation on slide four. And as I am sure you've all seen for the third quarter of 2012 we reported net revenue of $20.6 billion. Importantly, that number was reduced by about $1.9 billion for FVO and DVA and if we adjust for that you get to a revenue net of interest expense of $22.5 billion for the quarter. Net income was $340 million or $0.00 a share after preferred dividends.

The results reflect the previously announced charges in late September that relate to $1.9 billion for the combination of FVO adjustments as well as DVA resulting from the significant tightening that we saw in our credit spreads during the quarter.

In addition, we had $1.6 billion of pre-tax of total litigation expense including the charge for the Merrill Lynch Class Action Settlement. Lastly, we had about $800 million of tax expense related to the reduction in the UK tax rate. In the aggregate, these items negatively impacted EPS by approximately $0.28.

We turn to slide five, the results in the third quarter demonstrated ongoing momentum on several fronts. Period-end deposits across the company grew $28 billion, or 2.7% versus the second quarter which is an 11% annualized rate, and we accomplished that as the rates on the deposits declined slightly from 20 basis points to 18 basis points. The net interest yield increased by 11 basis points as our liability management actions continue to benefit net interest income.

Our Mortgage business home loans had its most profitable quarter excluding asset sales since we started reporting its results separately with first-lien production up by 13%. Wealth and Investment Management showed growth in long-term assets under management, deposits and record loan levels while maintaining solid margins.

Ending loans in our Global Banking segment increased 2.5% from the second quarter or 10% on an annualized basis. Results in the capital markets area reflected strong performances both on a quarter-over-quarter as well as a year ago basis.

We continue to invest in growth areas of our company such as mortgage lending, small business banking and financial advisors. Our 60 plus day delinquent loans serviced out in a Legacy Servicing business declined 12% from second quarter levels, and we'll spend sometime later in the presentation talking about what that means going forward. And our number of full time equivalent employees declined approximately 3,000 from the end of the second quarter related to a different New BAC initiatives.

If you turn to slide six, a lot of information on the balance sheet highlight area, I just want to draw your attention to three of the line items. The first, our tangible common equity ratio improved by 12 basis points to 6.95%. If you move down the tangible book-value, it grew by $0.26 in the quarter, up to $13.48 and if you look at our adjusted loan coverage where we look at the allowance for loans over annualized charge-offs, it improved during the quarter to 2.2 times.

If you turn to slide seven; as we've seen all year, regulatory capital continued to strengthen. Our Basel 1 Tier 1 common capital ratio was up 17 basis points to 11.41%. Remember, FVO in the tax charge do not impact regulatory capital.

As we near the 2013 implementation period for Basel 3, we've estimated our Tier 1 common equity ratio and it's components to provide a better understanding of where we are relative to the expected 2019 Basel 3 requirements. Our estimate as per the final U.S. market risk rules in the U.S. Basel 3 NPRs.

As of the end of the third quarter, on a fully phased-in basis, we estimate that that Basel 3 Tier 1 capital ratio would have been 8.97%. Recall last quarter, we estimated Basel 3 under BIS Basel 3 guidelines to be approximately 8.1% and 7.95% applying the U.S. Basel 3 NPRs. If we look at the components of the ratio, our Tier 1 common equity was $134.6 billion, while our risk weighted assets would have been $1.501 trillion.

A couple points I would like to make before we leave this slide. If we look at the improvement in the numerator of roughly $8 billion, we did benefit during the quarter given the reduction that we saw in the rate environment where our OCI, which flows through the balance sheet, not the income statement, was up about $3.2 billion and contributed 21 basis points to that ratio. We also benefited on the denominator, in portion of the increase due to the tightening credit spreads that we saw across the market that did benefit the denominator.

We turn to the slide eight, and look at liquidity. Global Excess Liquidity sources increased modestly from $378 billion to $380 billion during the quarter. That was accomplished while we reduced the long-term debt footprint across the entire enterprise by about $15 billion.

A couple of actions of note during the third quarter; we had $6.2 billion of liability management actions which consisted primarily of parent redemptions of trust preferred securities as well as sub debt and in addition to that we had $12 billion of maturities that were repaid at the parent.

We took an additional action during the first quarter of October of calling $5.1 billion of additional trust preferred securities that will benefit NII by about $50 million in the fourth quarter of this year and on a go forward basis about $300 million. And as we noted before, there will be a loss upon the redemption that we'll take in the fourth quarter of about $100 million.

If we focus on the parent company for just a moment, parent company remained very strong at $102 billion. And if you look at the reduction and liquidity combined or compared to the reduction in the debt footprint, liquidity at the parent declined by $9 billion when the overall debt footprint at the parent shrink by $18 billion as we continue to move money from our bank subsidiaries up to the parent.

Time to required funding at the end of the quarter was at 35 months and as we move forward and continue to shrink the debt footprint and smooth out the maturity profile, we would expect over the next six to eight quarters that you will see that time required funding migrate down to a targeted range in the 21 to 24 month timeframe.

On slide nine, if we look at net interest income. Net interest income on a reported basis increased from $9.8 billion or a yield of 2.21% in the second quarter to $10.2 billion or 2.32% during the third quarter. If we adjust those numbers for market related hedge ineffectiveness as well as market related premium amortization or FAS 91, our net interest income increased from $10.3 billion or 2.32% up to $10.5 billion or 2.39% during the quarter.

If we look at the activity within the quarter, we benefited during the quarter from the reduction of long-term debt driven by both our liability management actions as well as debt repayment. In addition, our trading related net interest income improved during the quarter. Partially offsetting these improvements were lower consumer loan balances and yields as well as lower investment security yields.

Near-term, if we look at where we are at the end of the third quarter and given existing rate levels, we estimate that quarterly net interest income will start at the base of approximately $10.5 billion. The impact of our liability management actions in our long-term debt maturities are expected to offset any headwinds that we see from continued pressure on both consumer loan balances, as well as investment security portfolio repricing.

In general, as you consider the rate environment, if rates increased from the end of September, we would look to see benefits in our net interest income. And on the other side to the extent that the rates declined, you could see reductions.

On slide 10, we get in to the businesses. In consumer and business banking, earnings were $1.3 billion during the quarter, an increase of $130 million in the second quarter driven by lower non-interest expense in provision, which were partially offset by lower revenue.

Non-interest income decreased from the second quarter due mainly to the impact of our consumer protection products. Credit quality improved again, as net charge-offs dropped to $170 million. Average deposits increased almost $4 billion or 1% from the second quarter.

On slide 11, we give you some key indicators for our consumer and business banking area for the quarter. Compared to the second quarter, debit card purchased volumes declined seasonally, while credit card purchase volumes adjusted for our portfolio of divestitures were relatively flat. Retail credit spend per active account was up 6% from the third quarter of 2011.

If we look at the US credit card loss rate, it’s the lowest that we’ve seen since the third quarter of 2006, while the 30 plus day delinquency rate is at a historic low. Banking centers declined as we continue to optimize the delivery network around customer behaviors.

We did continue to increase our mobile banking customer base to more than 11 million people, which is an 8% increase from the prior and up 30% from the year ago quarter.

We turn to slide 12, consumer real estate services reported a loss of $877 million during the quarter, versus a loss of $766 million in the second quarter of this year. Higher revenue, which included MSR gains, net of hedge results, the sale of a business and [mobile] rep and warrant expense were more than offset by higher expenses as well as a higher provision. The provision for reps and warrants was $307 million in the quarter, a decrease from $395 million that we experienced in the second quarter.

Expenses were up $672 million, LAS drove that expense increase due to higher litigation expense, servicing cost and other mortgage related matters. Provision increased $75 million during the quarter, driven by the impact of new regulatory guidance on loans discharged at bankruptcy which I'll discuss when I get to credit quality later in this presentation, and it was partially offset by a recovery in the home equity PCI portfolio due to an improvement in the home price outlook.

The Home Loans business, which is responsible for first-lien and home equity originations within this segment, recorded a profit of $264 million for the quarter. First mortgage retail originations of $20 billion were up 13% from the prior quarter due to lower rates and up 19% compared with retail originations a year ago.

As you'll recall we exited the correspondent business late last year, so current correspondent originations are non-existent versus volumes of approximately $16 billion a year ago, even with the exist from the corresponded channel core production income is higher than the year ago, our MSR asset decreased by $621 during the quarter driven primarily by lower mortgage rates and ended the quarter at $5.1 billion.

MSR hedge results more than offset market valuation declines. And if we look at the Cap rate on the MSR at the end of the period, it was at 45 basis points versus 47 basis points in the second quarter and 52 basis points a year ago.

On slide 13, we showed some comparisons of certain matrix in our legacy asset and servicing area on a linked-quarter basis as well as compared to a year ago, as we continue to work very hard to reduce delinquent loans and find solutions for home owners.

As you'll recall, the legacy assets and servicing area reflects all of our servicing operations and the results of our MSR activities.

Our domestic FTEs excluding contractors decreased for the first time in this area in 14 quarters. The number of first-lien serviced drop 6% in the quarter, but more importantly the number of 60 plus day delinquent loans dropped by 12%.

The drop in 60 day plus delinquencies will have a positive impact on our staffing levels in the fourth quarter and beyond, as servicing cost going forward should benefit given that we were fully staffed in the third quarter to handle the various new programs and regulations.

And we've discussed previously, we'll continue hard both working through these delinquent loans internally as well as looking externally for solutions to reduce this number of delinquent loans.

On slide 14, you can see that our outstanding rep and warrant claims increased by 12% from the end of June, versus the 41% increase we experienced during the second quarter of this year.

Outstanding claims from the GSEs did increase albeit at a slower rate, as a result of ongoing disagreements with Fannie Mae about what constitutes a valid repurchase request.

Since June, given the settlement we discussed last quarter with Syncora, the backlog with Monolines has decreased. On the private label side, we had $1.9 billion increase in outstanding claims to a total of $10.5 billion at the end of the quarter. The increased on the private label side is primarily due to claims received from trustees and securitization sponsors. But keep in mind that this increase in aggregate non-GSE claims was taken in to consideration when we developed the increase in our reserves at the time of Bank of New York settlement during the second quarter of last year.

We would expect these claims to continue to grow as the process for ultimate resolution continues to evolve and remain somewhat unclear.

The other thing we ask you to keep in mind is this table reflects the unpaid principal amount of the loans, not the actual amount of losses that are incurred on the loans. Our reserve for reps and warrants at the end of the quarter increased slightly to $16.3 billion.

In the second quarter, we provided a range of possible loss over and above existing reserve levels of up to $5 billion, which only apply to non-GSE loans. At the time, a range was not provided for GSE activity as we were unable to estimate such a range.

In the third quarter as a result of ongoing dialogue and discussion with the GSEs, we have obtained additional information from which we are now able to determine a reasonable estimate of a range of possible loss in excess of our recorded reps and warrants liabilities for the GSEs.

We currently estimate that the range of possible loss for both the GSEs and the non-GSEs for rep and warrant exposures could be up to $6 billion, over our accruals of September 30th and compared to the up to $5 billion over accruals at June 30 which once again were only for non-GSE reps and warrant exposures.

The increase in the range of possible loss from our June 30 period is the net impact of among other changes updated assumptions and the inclusion of GSE rep and warrant exposure, as well as other developments.

We move to our global wealth and investment management area, on slide 15. Earnings for the quarter of $542 million or a pre-tax margin of approximately 20% were inline with the results that we saw in the second quarter.

Period end deposit growth of $6.4 billion and period end loan growth of $2.1 billion help to offset the impact of the continued low rate environment. Ending loan balances, as I mentioned earlier, were at record levels. And solid long-term AUM flows of $5.7 billion help to offset seasonal declines. This client activity along with the strong overall market performance in the third quarter should benefit our fourth quarter results.

If we move to global banking on slide 16, we had net income in the third quarter of $1.3 billion, which reflected higher net interest income and a reduction in expenses that was offset by gains in the second quarter related the certain legacy assets dispositions which did not recur in the third quarter.

Period and loans and leases increased $6.7 billion or 2.5% from the second quarter, with growth across C&I, commercial real estate, leasing as well as some quarter end findings.

Average deposit balances were up 5% from the second quarter to $252 billion as our corporate customers remain very liquid. Asset quality continued to be very strong and continued the trend from prior quarters, net charge-offs were down, NPL, NPAs dropped 20% to $2.6 billion and our reservable utilized criticized exposure declined 17%.

On slide 17, investment banking fees, investment banking fees at $1.336 billion were up nicely over both the prior quarter, up 17% as well as up 42% from the year ago period. We look at where we were relative to our competitors; we maintained a strong number two global ranking in fees to date. And as you can see below, we continue to have leading market shares globally in many of these businesses.

We switch to Global Markets on slide 18. Earnings were impacted by a DVA loss of approximately $580 million and the tax charge for changes in the UK corporate tax rate. If we back out the DVA and the charge for taxes, net income actually increased 41% from the second quarter to $789 million.

Revenue ex-DVA for the entire segment was up 5% and once again DVA losses in the quarter of $580 million last quarter losses were $156 million and those compared to gains in the year ago period to approximately $1.7 billion.

Sales and trading revenue ex-DVA was down 3% from the second quarter, but improved substantially from year ago levels. Within FICC, the core businesses of credit, mortgages and rates and currencies performed very well. Our FICC revenue ex-DVA was essentially flat with the second quarter at $2.5 billion delivering a solid performance. In equities, excluding DVA results decreased 8% from the second quarter as lower volatility and a continued lack of investor appetite for equity products depressed volumes.

On the expense side, expenses declined from both the second quarter in the prior year driven by lower personnel related expense as well as lower operational costs. Average VAR for the quarter was $55 million, down 12% from the second quarter and 67% from the prior year. And as we look at that, we continue to generate increasing levels of revenue for each dollar of risk that we take within this segment.

On slide 19, we show you the results of all other which includes our Global Principal Investments business, the non-U.S. consumer card business, our discretionary portfolio associated with interest rate risk management, insurance as well as the discontinued real estate portfolio.

The revenue decrease from the second quarter of this year was due to a negative valuation of adjustment of $1.3 billion on structured liabilities under FVO and lowered gains on debt and trust preferred repurchases partially offset by higher equity investment income during the quarter. The increase in non-interest expense was due to higher litigation expense and if we were to exclude that, non-interest expense declined compared to the second quarter.

On slide 20, non-interest expense, I would like to make a couple of comments here. Non-interest expense of $17.5 billion was down slightly from the third quarter of last year and up relative to the second quarter of this year. If we were to back out the increase in litigation expense that we incurred during the quarter, non-interest expense actually declined from Q2 to Q3.

If we look at the components of that, we saw improvements in personnel costs and other cost savings realized from our New BAC initiatives and that was partially offset by higher cost of mortgage servicing and other mortgage related matters, which as I mentioned previously, we would expect to see come down in the fourth quarter relative to the third. We also invested in selective growth areas during the quarter in our mortgage loan officers, our small business bankers and our financial solution advisors.

If we move down, and you look at the number of full-time equivalent employees, we started to implement Phase I of New BAC in the fourth quarter of 2011. Outside of LAS, which is the grey bar, you can see since we began the implementation, we have reduced the FTEs across the company outside of Legacy Assets and Servicing by almost 21,000 people or over 8% since we began that implementation. And as you can see, Legacy Assets and Servicing FTEs increased, but have now stabilized and as I said we would expect the sub start seeing come down in the fourth quarter.

If we turn to slide 21, although provision was relatively flat with the second quarter, there were two events that impacted both the net charge-offs and non-performing loans that you've heard others to speak about. The first, regulators did provide new guidance to the industry in the third quarter of this year that stated loans discharged from the courts as part of the Chapter 7 Bankruptcy should be written down the collateral value and classified as non-performing irrespective of the borrowers' payment status.

As a result, we charged-off $478 million in loans and reduced reserves by $139 million resulting in a provision increase of $339 million in the quarter as a result of this new guidance. Non-performing loans increased by $1.1 billion as a result of this change and $954 million or 91% of these borrowers are current on their contractual payments. Of these contractually performing loans more than 70% were discharged from bankruptcy more than 12 months ago and nearly 40% were discharged 24 months or more ago.

The other change, recall in March, we and other large mortgage servicers agreed in the settlement with the DOJ and 49 state attorneys to provide programs to assist home owners in modifying loans and other borrower assistant programs. We referred to that as the national mortgage settlement. As a result of these agreements, we incurred charge-offs in the third quarter of $435 million related to the extinguishment of non-purchased credit impaired loans in this home equity portfolio.

This $435 million had a corresponding decrease in non-performing loans that we reported at the end of third quarter. These loans were under water and in the later stages of delinquency or were loans that were current on their junior-lien, but severely delinquent on their underlying first.

Associated with this settlement, we also extinguished $1.7 billion of home equity loans in the PCI portfolio, resulting in a decline in both the portfolio as well as the corresponding reserve. These items had no provision impact as reserves for these loans were already established.

If we turn to slide 22, we've laid out here, the third quarter of last year, second quarter of this year and third quarter and then adjusted the numbers on the far right column for this change in regulatory guidance and the National Mortgage Settlement and what you see here are three points that we would like to make. First is net charge-offs after making these adjustments declined $417 million or 11.5% as our underlying asset quality trends continue to strengthen.

Second, 30 plus day performing consumer delinquencies, excluding fully insured consumer real estate loans declined about $200 million or 2% and our non-performers decreased $1.4 billion or 5.7% versus the second quarter, driven equally by improvements in both commercial as well as consumer loan quality. And on the commercial side, our utilized reservable criticized exposure improved by 15% or about $3 billion.

As we look at credit quality for the balance of the year, we would expect the provision as we discussed at the end of last quarter to be in the range of $1.8 billion which is what we've seen over the last two quarters and $2.4 billion which we saw during the first quarter, so that guidance is unchanged from what we have given before.

And with that, let me turn it over to Brian.

Brian Moynihan

Thank you, Bruce. I am going to cover slide 23 and add a few thoughts before we take your questions. If you think back to when we started the year, we said that we focus no a few key areas. Building the capital of the company, continue to mange risk, continue reducing the cost base of the company and driving our core business growth for the franchise.

As you look at the results Bruce covered, I think we have shown strong results and we're moving in the right direction in every area. Our industry leading Tier 1 common capital levels provided solid base to serve our customers and balance sheet that can do great customer business.

But, what I wanted to draw your attention to on this slide is the progress we made across our three groups of customers and clients, whether it's our consumers or companies or institutional investors. If you look at the business lines that Bruce described, our operational metrics are improving across the board and the cost of each of the operating businesses other than LAS were down linked quarter and year-over-year while revenues continue to be solid.

For the individual consumers we serve, our deposits continue to grow; our net account growth was solid this quarter and we regained the market share in the direct to consumer mortgage lending business. With our preferred clients in our consumer business, our growth continues as we continue to improve the offers we have for those clients with increased checking accounts and brokerage assets in our Merrill Lynch platforms.

If you think about our service network overall, we continue to optimize it, reducing branches as we meet the customer behavior changes as they move to online and mobile banking which continues to increase nicely with 11 million users in the mobile and tablet platform.

The companies we serve are also doing more business with us; small business originations are up, as Bruce stated earlier. Loans continue to expand and investment banking fees continue to grow. As we move to our institutional investor clients, we continue to add to our industry leading research capabilities and our sales and trading revenue continue to do well in an overall different environment and the markets that we had during the summer months.

So this quarter shows the progress that the company continues to make. It shows the hard work of all our teammates of streamlining and simplifying the company is paying off. It shows the strength of the integrated business model which serves customers and clients in a way that no other firm can. And it shows how that combination deepens relationships, provides the best-in-class financial capabilities and will drive growth.

With that, Bruce and I would be happy to take your questions.

Question-and-Answer Session

Operator

(Operator Instructions) And we'll go first to the site of Moshe Orenbuch with Credit Suisse. Your line is open.

Moshe Orenbuch - Credit Suisse

Just some extraordinary, I would say performance on the capital ratio; wanted to kind of talk about that a little bit, did I hear correctly that that 8.97 is inclusive of the terms of the NPR?

Bruce Thompson

That's correct.

Moshe Orenbuch - Credit Suisse

So as you think about that, I heard that some notes that there were some kind of benefits that could be somewhat temporary, but obviously over the next several quarters, one would expect that to continue to improve. Can you talk a little bit about, whether you are looking for improvement either in RWAs or your deductions, and then also how you think about that since you are likely to be more or less or either now or certainly in three months at the levels that you'd be required by the combination of Basel 3 capital requirement and (inaudible).

Bruce Thompson

When we look at the ratio, lets talk first about the numerator than we can go to the denominator. As I said, there was about $3 billion on the numerator of the $8 billion that related to things that we benefited from rates. We will obviously see how that goes going forward, but I just want to make sure that there was 3 billion there.

On the numerator side, because of where we are with respect to having NOLs as we go forward, where we are going to be different than most of our peers is on the numerator side. Our pretax income is going to tend to approximate the net income as it relates to capital build. So we've got benefits going forward relative to our peers based on using those NOLs which as you all are aware are excluded from a Basel perspective.

On the denominator side, there are three things that we would also continue to benefit from, as we look to drive this number higher. The first is on the retail credit side. We noted here during the quarter that we had about $27 billion of benefit in risk weighted assets through both the reduction in consumer exposures as well as improvement within the credit portfolio that we saw on the consumer side. And as we continue to reduce non-performing mortgages, as well as one of the consumer credit portfolios in the card business, we'd look to continue to have benefit there.

The second thing is that the structured credit in some of the legacy books will continue to run off between now and 2017, we'll benefit from that. And then, third, there obviously continues to be a lot of work that's done with respect to models in developing the systems to make sure that your measurements are appropriate here. So, we feel very good about the capital build during the quarter, and we think as we go forward that the ability to continue to optimize and drive that Basel 3 number continue to have real opportunity for us.

Moshe Orenbuch - Credit Suisse

Just a follow-up on that, that's great on the tactical side, what about strategically, now that, you are pretty much where you need to be, how do you think about that capital level differently, and do you think about it in terms of your approach towards allocating to businesses or distributions, how should we think about that?

Bruce Thompson

I wouldn't, and one other things that we highlighted, I'm going to speak first on Basel 1 to that question that, over the course of the last couple of quarters, as we've look to optimize our Basel 1 ratio, we were obviously very tight and have fairly firm limits on loan growth as we look to optimize the balance sheet, as we've gotten the balance sheet to where we wanted to be, that clearly pursuing loan growth in this rate environment is very much a priority.

And if you look at what we did during this quarter, it's the culmination of several quarters of work where we started to see good loan growth within the GWIM business.

We saw the increase in mortgage production, not all of which is loan growth, but some of it is loan growth, and then on the banking and market side where loan growth was extraordinarily strong. So we are using the strength in the balance sheet to look to drive growth in the loan side.

We are obviously doing it in a prudent way with borrowers that have the credit quality that we should be extending to, and you have seen the results of some of that.

On Basel 3, as we worked through Basel 3, a little bit of shift in mindset and that you are looking to optimize and consider both how things get measured as well as under Basel 3 as Basel 1, Basel 3 going forward is going to be the governor on capital distributions, so we are obviously very mindful to be managing the balance sheet with Basel 3 front of mind.

We are obviously at point at the end of the quarter upwards of 9% where we are very close to or in access of the stated minimums we'll need to work and see where the [safety] buffer comes out. To think we positioned ourselves very well for both growing the business as well as we look forward going through to [seek our] process.

Moshe Orenbuch - Credit Suisse

That should mean that if this process is ongoing that you would expect to see loan growth accelerate honestly from here?

Bruce Thompson

I am not going to suggest on an annualized basis that we saw commercial and corporate loan growth of 10% that you are going to see accelerate. It can bump around a little bit in any quarter, but you should expect and know that internally with those areas that have returns we are pushing and looking to drive loan growth, that's correct.

Brian Moynihan

I would add that the impact of the portfolios that we identified going back a couple a years to runoff which helps in the capital because as Bruce said earlier they actually capital is less now then it was then because A, they are smaller and the quarterly runoff is more muted which then allows a loan growth to come through the bottom line.

So think about the card business for example, we're getting in a place where we've got pretty well positioned where we want and I think with Bruce still here and 75,000 new card customers this quarter, a little bit more than we did last quarter and we're driving very high credit quality. Exactly what we want and we're driving that out.

So as you think about the ability to show loan growth through the sort of all the ins and outs of the runoff portfolios, that's where we're just starting to see to as those things are getting smaller through the [hole].

Operator

We'll take our next question from the side of John McDonald with Sanford Bernstein. Your line is open.

John McDonald - Sanford Bernstein

Yes. Bruce on the net interest income, you said that the 10.5 billion is a good starting point for the fourth quarter NII?

Bruce Thompson

That's correct John.

John McDonald - Sanford Bernstein

And what are the puts and takes from there? Did you say that you hope to get some debt reductions or the benefits of debt reductions could offset the headwinds that you expect from low rates and runoffs? Did I hear that right?

Bruce Thompson

Sure. During the third quarter, we had 6.2 billion, as I mentioned a trough that occurred during the quarter and $12 billion of stated maturities. We'll have the full benefit of those during the fourth quarter as oppose to just a partial benefit.

The second thing is the reduction of the troughs, we'll have the $50 million benefit that I mentioned in the fourth quarter and we're continuing to push deposit pricing down. So that's a benefit as well.

So as we look at the fourth quarter absent any unexpected decline in rates in any impact of negative hedging effectiveness or FAS 91. We would expect net interest income to be at least in the fourth quarter what was in the third quarter.

John McDonald - Sanford Bernstein

What about the next year NII, Bruce, do you have additional tools on the cost funding side? Do you hope to keep that $10.5 billion run rate or grow or see some pressure from that? Can you give some perspective for next year?

Bruce Thompson

We're managing the portfolio to look to be able to continue to have modest increases in NII through what we're doing on the debt footprint as well as deposit pricing. So, the goal is to continue to push that up. We think we've got a good plan in place to continue to do that. We obviously can't predict interest rates, but if they were just to stay where they are in the forward curve or to materialize, we think we'll be successful in doing that.

John McDonald - Sanford Bernstein

Okay. And then switching over to expenses, do you have any sense of where you might be on the litigation reserve bill cycle, later innings or anyway to frame that for us?

Bruce Thompson

The Merrily Lynch class action settlement was a significant litigation item to get behind us. And as you look at litigation going forward, we've narrowed that with this settlement in large part that there are cases are obviously outside of mortgage, but largely the majority of the litigation that we have now with the Merrill Lynch settlement is within the mortgage area.

And we obviously provide reserves for what we think we have and in the disclosure we give guidance on range of possible loss for what we would expect within the litigation area and we continue to work through those.

With where we've build the balance sheet, obviously getting these behind us is something that we would like to do but we're only going to do it in a way that makes sense for the shareholder.

John McDonald - Sanford Bernstein

Okay. And then, on the LAS side, you mentioned that with the 60 plus delinquents moving down, you should start to see the LAS expenses come down next quarter?

Brian Moynihan

From an operating basis John, we saw the first decline in FTE, you can see the contract is a little higher. The third quarter was a lot of work because it was a combination of Department of Justice, the timely mind work and also just the general work.

But as we look at it in even sense at the quarter end we've seen the headcounts start to come down already even further. So this thing has been - have done a lot of work on operating basis, we'd say the numbers of people and stuff like that it will be down in the fourth quarter.

The question is from the litigation perspective, you know those are things bouncing around a little bit if you look across all the last quarter. But from an operating basis, we've already reduced the headcount in the fourth quarter from what it was in the third quarter.

John McDonald - Sanford Bernstein

So I guess from a total expenses all end jumping off point for the fourth quarter, if we adjust for our own estimate a litigation reserves first [tell] what you think would be a number for the expenses to jump off from?

Bruce Thompson

I think if you just for the litigation expenses, those are going to be a good place to jump off from, and as Brian referenced we think there is the opportunity within the LAS areas to start driving those expenses down in the fourth quarter and clearly into 13.

Brian Moynihan

John, the way we think about it as we look at it year-over-year, third quarter last year, third quarter this year we had sort of flat expenses, but if you look at the impact of the increase and litigation increase in LAS, the rest the company is down $1 billion or so in operating expenses. And that will move up or down because, with a better training quarter, we could have some more compensation there but you are seeing the impacts of new BAC plus the other [nations] and the company taking the expenses down and we are just continue to work at.

That being said, we are still making investments in those company to make sure that we are doing the right thing to have a franchise and want coming of out. So more loan officers, FSAs, preferred bankers and $3 billion plus in systems development work this year, (inaudible) million of which is going to help us get the expense stay down in future years. So we're trying to balance that and that you would see expenses from the core basis what I am pointing out continuing to trend down and we're feeling better about that and the best in this quarter is we think, as you look at the LAS, you see the breakpoint here and we will see how to keep driving that down in the fourth quarter.

John McDonald - Sanford Bernstein

Okay. And the last thing from me is on the mortgage banking fee results. First, can you drill down a little bit of the drivers of the strong mortgage banking fees; you mentioned the origination volume. Just what you saw gain on sale margins and then also how did the MSR hedge gains contributed and was there a business sale as well that you mentioned?

Bruce Thompson

Sure. Within mortgage banking we did see a business sale that was about $175 million of a small ancillary business that materialized in the quarter. The second thing is, with respect to mortgage margins, they stayed relative firm in the third quarter relative to the second quarter given that the activities that the industry had industry-wide. And the third point of your question is, if you go and look at page 26 of our supplement, when you mention the MSR hedge, that relative to the last couple of quarters, we were about $350 million better in the third quarter than we had been the prior several quarters and we detailed that on slide 26.

Brian Moynihan

John, one thing I would say, tying those two questions together, on the origination side, you can see the volumes coming up, but we've added 3,000 more people during this year than we thought we have in the underwriting fulfillment side of the good mortgage side to help us get the volumes going and those people continue to come on stream. So our capacity to grow there is expanding and some of the people that were into all that account, you can see, but some of the people we were taking out LAS were converting to the first mortgage business because it needs experience to mortgage to help build our capacity, like a lot of our colleagues, the volume levels have been high and our capacity get them close with the underlying standards; it's been a lot of work and so we've added 3,000 or 4,000 people I think at this point, but then when we thought we would be this year and we'll continue to do that to capture the revenue.

Operator

We'll move next to the site of Chris Kotowski with Oppenheimer & Company. Your line is open.

Chris Kotowski - Oppenheimer & Company

Yeah. Good morning. I am looking at slide 39 and slide seven on the capital and I am sorry maybe I am a little, but the slide there and I am trying to reconcile and then slide 39 is very helpful and it's obviously nice and that the numerator is going up and the denominator is going down. But, if we're looking at slide 39 I guess, which, I am confused about, which of these movements are due to say changes in markets and rates and spreads and so on; how much of the movement is actually due to changes in the underlying assets and then, how much of the movement is due to the changes in models and assumptions, if you look at the main categories on slide 39?

Bruce Thompson

Okay. This bridge between June 30th and September 30th will be very close, recall that when we reported at June, we were using BIS as opposed to at September 30th that we're now using the U.S. NPR that had some about 15 basis points difference. But with that being said, if you look at the 126.8 to the 134.6 it's roughly $8 billion and of that $8 billion, roughly $3.2 billion was due to the impact that rates had on our securities portfolio as well as our MSR. That's the piece that was impacted by rates and there was nothing that we directly did to impact that. The rest of what you saw during the quarter had to do with pre-tax earnings before FVO which does not affect regulatory capital, it had to do with some different assets if the bank that are no longer excluded from the calculation and it had to do with a variety of other things including the fact that we no longer have any 10% threshold deductions in the number. That's the bridge on the numerator.

Chris Kotowski - Oppenheimer & Company

Okay.

Bruce Thompson

If you move to the denominator and you look at the page 39, it's about $65 billion reduction in risk weighted assets, let me give you the three biggest buckets of that. As I mentioned earlier, the first bucket is about $27 billion as it relates to retail or consumer exposures. The lion share of that $27 billion have to do with either reductions in the actual exposure or the core credit improvement that we saw within the book and a very small amount of that had to do with any model changes or model optimization.

The second big bucket that's out there is in the OTC derivatives in repo which was about $26 billion. If you look at those numbers almost all of that $26 billion had to do with either reductions in exposure, improvements with how we manage collateral or improvements in the underlying quality of the counterparty.

The third bucket and the smallest bucket of which about, is about $18 billion is a variety of things included within that $18 billion bucket, spread tightening that we saw out in the market that resulted in the ratio coming down; you can see though that the $18 billion is relatively small compared to the overall $65 billion.

Chris Kotowski - Oppenheimer & Company

Thank you for that. That's the best explanation any bankers have ever offered and I think it's a model for the rest of the industry and I appreciate that. The other thing I was just wondering on slide 21, you were the only bank that flagged the impact of the mortgage settlement. Everybody talked about the OCC guidance. But is this roughly $400 million, is this going to be a quarterly thing for a while that we're going to, you know, obviously you've made provisions for these, the impact of the NMS, but should we expect to see charge-offs at an elevated level for a year or two?

Bruce Thompson

No, as we work through the National Mortgage Settlement, we're working very hard to beat through a significant portion of the obligations that we have for modifications. The third quarter -- and I think we have a pretty good sense for this, without question will be the largest number like this that comes through, probably very small in the fourth quarter and maybe a little bit of carryover in the next year, but this is by far the most significant quarter that you will see with this. As you said, it doesn't affect the provision because you've got both a write-off as well as an allowance, but that should be a lot smaller going forward.

Operator

We'll go next to the site of Matt O'Connor with Deutsche Bank. Your line is open.

Matt O'Connor - Deutsche Bank

Good morning. A couple of follow-ups on the legacy mortgage costs and looking out beyond fourth quarter, just trying to get a sense of how quickly they may come down and I guess, how easy you think it may be to forecast, just think about modest loan price appreciation from here and nothing unusual on the regulatory side?

Bruce Thompson

Well, I think, I would say that we expect them to come down, there have been, one of the things that's been difficult about this is the third party impacts and timing of that and from what we may have thought last year at this time for example, so the Department of Justice settlement took longer to get finalized therefore it took longer to put in, so, those, yeah, so there is outside impacts going to have them.

But given everything we know, we would expect them to come down next quarter and beyond. We got to be careful because sometimes there are sort of non-operating adjustments in there. So just if you think about the headcount and the work we do, because the 60 plus day delinquencies are down as you see on the slide, that we can forecast in the work and what we're seeing as we're modifying a lot of loans and getting through those, the short sale volumes are as high as they've ever been and the liquidation volumes are high.

So everything we see says that we just have to be a little careful about how we report our quarter based on ebbs and flows and some of the legislation gets passed the state levels and things like that and they can have an impact.

I would tell you that, what we're seeing as the inventory clears very quickly, so as we get to the properties, they sell quickly within 60 days to 90 days that's been true; we're seeing by geography that areas where the process can move forward and we're seeing the outstanding 60 plus rate drop more dramatically because in the California, Arizona versus the areas which moved a little slower, New Jersey or Illinois for example. But everything we said, this is this is coming down because the works going away. You point your finger to the one key question which is if changes are made to the policies or programs that can slow it down, but I don't think there is much volume; we are seeing reduction 60 plus, that would overcome that frankly.

Matt O'Connor - Deutsche Bank

And maybe I'll just toss some numbers out there, you are at $12 billion annual run rate right now, I feel like at one point you said $2 billion could be a more sustainable level as you move through all this, so that's a $10 billion decline. Any guess on, does it take two years to get through that, is it five years to get through that?

Bruce Thompson

I think we would look at it and say '13 and into '14 it would be through that base, and I think we noted that.

Matt O'Connor - Deutsche Bank

Okay.

Bruce Thompson

But again, that's subject to caveat and something change in rules, something change in the rules, but right now as we said, we would expect that as we move through next year, the year end numbers would still be elevated, but as we move into '14, you would see them come down to more normalized levels. We are doing everything we can move to get through this as quick as possible.

Matt O'Connor - Deutsche Bank

Okay. And then just other topic here, you know as we think about maybe some of the interest rates out there outside the treasury, so like mortgage rates, the agency RMBS rates and I think a lot of other asset classes you have seen rates come down in the securities side. How you just conceptually think about managing the discretionary book from here, and I understand you are trying to grow C&I loans a little bit more, but obviously the discretionary book is still a pretty big chunk and you have a lot of deposits that you need to try and balance?

Brian Moynihan

One of the things that we are not going to do in this rate environment is stretch for yield and create an OCI problem under Basel 3 going forward. So on the securities portfolio, if you aggregate the securities portfolio as well as our whole loan portfolio, it's about a $600 billion total number that we're managing. It has an average life of about 2.5 years. And as I mentioned on the questions for net interest income, even with where we're reinvesting things that are either come due or repaid, we think the shrinkage in the long-term debt footprint will at least cover what we've got as far as repricing absent no changes and forward rates going forward.

You bring up a good point which the industry is obviously focused on is that the one area and the one area and the one asset class that doesn't have OCI risk and that's funded on the asset side the way we fund our liabilities is loan growth, and we've been pushing over the last couple of quarters for that loan growth.

As we talked about, we saw in GWIM as well as in the institutional side, we started to see that loan growth, and it's obviously as it relates to matching in the way that we manage capital where we would like to be. So it's obviously an environment that's not easy to manage in, but we think we got a variety of levers, most notably a high cost debt that we can continue to take down, so that you see some more type results to what we saw this quarter.

Operator

We'll go next to the site of Ed Najarian with ISI Group. Your line is open.

Ed Najarian - ISI Group

Two questions, the first just in terms of the GSE related mortgage repurchase claims. You know, obviously we're seeing other banks sort of move through that process, build reserves to sort of put that claim risk behind them. I know you're in a dispute with Fannie. Any sense of how you expect that dispute to get resolved, do you think that's something that you'll just sort of gradually resolve with the additional reserves and resolutions over time, do you expect to see some kind of a settlement with Fannie. Any sense of when that overhang might get sort of put in to the rearview mirror or how it will be put into the rearview mirror?

Brian Moynihan

The first point Ed, that we've made here and you see it in the numbers is that, with respect to current winnages things that have been under (inaudible) over the last couple of years, where we have an obligation to repurchase those and we have been repurchasing those. What you see when you look at the schedules, are that the increases in the unpaid or the balance of outstanding claims which as I said, are notional not losses, where you're seeing the build up is in those payments where they're greater than 24 months.

So, with respect to the piece that's greater than 24 months, I would really just repeat what we've said previously that there are two ways that this gets resolved, we have different points of view on this, we continue to have ongoing discussions, and I think the most likely outcomes are either that there is a settlement of a sort or there is some other way that we look to resolve that and that core disagreement remains. As we've said in the disclosures and how we've updated the range of possible loss, there are ongoing discussions, but there is obviously nothing done.

Ed Najarian - ISI Group

Well, that's sort of serves of my point; the two sides have this core disagreement. You know I guess you are probably unwilling to speculate how you sort of come to the middle on that core disagreement, but do you feel like its in your best interest now to sort of maybe be more proactive on that, try to meet in the middle, try to get that settle and try to get that for behind you, or do you feel pretty firm in your stance that we are right and we are going to keep digging out in our heels on this issue?

Brian Moynihan

Given the disclosure we've put out, we obviously feel pretty strongly about what our position is here. At the same time, and as we seen in Merrill Lynch, getting these legacy issues to the extent it makes any type of economic sense for the shareholder behind us is a good thing and eliminates an element of uncertainty in your mind. And the last time I just said it's going to be the right decision for the shareholders and that's what we do day in and day out as we try to put these different issues behind us.

Ed Najarian - ISI Group

The second question has to do with capital. It was only about a little over a year ago that one doctor was making an investment in your company and the chatter was all around the potential that has to build capital. Now all of a sudden we are looking at your capital ratios and thinking a lot about excess capital.

I am sure you probably don't want to give us outlook and predictions in terms of capital return in conjunction with the CCAR, but can you give us a sense, you've spend so much time in the last 18 months building capital, clearly there are shareholders that are obviously looking for dividend entries, some are looking for a stock buyback especially after looking at the capital ratios today. Can you give us any sense of how you are thinking about capital over the next 12 months above and beyond what's going to be used for internal loan growth?

Those capital ratios are going to continue to build based on some of the guidance that you just gave us over the last 45 minutes, and there is going to be a lot of people interested in thinking about what, how your thoughts are around dividend increases and stock buyback for the next 12 months as those ratios continue to build.

Brian Moynihan

We will start the work on the CCAR process in 30 days or so when we get the information, and so we won't speculate on that. But I think starting up on the broader perspective, we have made it clear that the capital we have in this company has been sufficient based on all the work that we've been doing in the last couple of years. We've been cleared that the capital is sufficient to run the company and to support the company growth, and all the capital above that.

When we have to get the approval, we'll go back to shareholders, either as dividends or share [repurchasers] till we frankly build the capital levels that we, you know, there is no reason to retain the capital at all. So it's all your capital, it's all the shareholders capital, until we get to the levels that we can return it. It's on the balance sheet, in our tangible book value per share, which we focus on and growing and see that continues to grow, and then after we hit the levels, that would be SIFI buffer plus minus whatever cushion that we feel comfortable impacts the CCAR. It's all going back in one way or the other way.

Ed Najarian - ISI Group

And then just last question related to that and Brian, in your mind, there is still are some overhanging litigation issues. There is still up to $6 billion or mortgage repurchased related cost that you outlined. Are those things that sort of, at least in the near-term will make you a little bit extra cautious on capital retention relative to where we otherwise think you might be until you sort of get those litigation and repo issues more fully resolved?

Brian Moynihan

All I have to take account in the technical rules of [QR and AS] and in things that we look. But think about this quarter, we basically had a breakeven quarter, we passed a major milestone in putting behind a major piece of litigation, and the litigation expenses were $1.6 billion or whatever they were and we still built capital.

So, it factors into it obviously, but on the other hand we have lots of ways to build capital and so, we are focused on getting the position that you suggest which is, that we start returning all the capital we've promised, we have to get to the CCAR process and until we sort of see that we can't project on that, but in those processes and in our mindset all that is factored in, but if you look at the track record, we continue to build capital even though we've been putting behind this major piece of litigation every quarter, on several quarters.

Operator

We'll go next to the site of Betsy Graseck with Morgan Stanley. Your line is open.

Betsy Graseck - Morgan Stanley

Hi, two question. One was on the hedge that you've historically had on the [AOCI] book. Have you been changing the size of that and at this stage as well.

Brian Moynihan

I'm sorry, I am cut out Betsy.

Betsy Graseck - Morgan Stanley

So, do you have a hedge on the AOCI book, and I was just wondering if you still have that in place?

Brian Moynihan

On the overall securities book?

Betsy Graseck - Morgan Stanley

Yeah.

Brian Moynihan

Yeah, as we've said a lot of the longer duration fixed rates we do swap to floating to minimize the AOCI risk.

Betsy Graseck - Morgan Stanley

Okay. And did you change the size of the hedge at all during the quarter?

Brian Moynihan

Nothing material within the securities book this quarter, no.

Betsy Graseck - Morgan Stanley

Okay. And then separately, there are some regulators who are suggesting that the debt portion of the balance sheet from senior debt through lastly (inaudible) correctly should be somewhere in the 25% to 30% range, and I am wondering, if and I just have two question and I am wondering if you've had any conversations with regulators about that, do you feel but there was anything that you would need to do in that side of the debt stack?

Brian Moynihan

It's something that's very topical. Even with the changes that we have made to our debt footprint. If you look at our debt footprint on any type of absolute and relative measure, relative to our peers we are at the high end which obviously from an expense perspective is not a good thing. So we are not going to predict what's going to happen going forward from a regulatory perspective, but I think given that we have on a relative basis more between parent and Merrill Lynch that our peers that will be able to manage that well and we look at maturities and over the course that next year we have maturities of about $30 billion of debt and we would expect to repay a large portion of that through cash that we generate and through the existing cash resources we have in the company.

Betsy Graseck - Morgan Stanley

Okay. So as we [evolve] through the next couple of years, we should see the same case of long term debt decline or in a little bit of deceleration into the next year or two?

Brian Moynihan

What I would model in is that a large portion of the maturities the way we lay those out will be taken out with existing cash not new long term debt. Periodically we will raise debt, we've said 21 to 24 months time to funding that would tend to migrate you down to a liquidity at the parent level in the zip code of $75 billion to $80 billion and as we've said, think 2013, think 2014, that the majority of that debt would be repaid with cash resources.

Betsy Graseck - Morgan Stanley

Okay. And then just lastly on capital, one of the capital rules has to do with holding a hair cutting against the CRM, I think it's an 8% hair cut or so. So when you talk about full model approvals, you are assuming that that hair cut goes away, is that correct?

Bruce Thompson

I think you are referring to -- which model -- you referring to CEM?

Betsy Graseck - Morgan Stanley

Right.

Bruce Thompson

If we look at in the capital numbers that we quote, we've assumed CEM and IMM approval. And with the different work that we've done, the spread between what our IMM numbers are versus our CMM numbers has gotten much higher. So to the extent any model where it take longer to get approved, we have reduced that risk significantly as we built capital.

Operator

We'll go next to the side of Nancy Bush with NAB Research LLC. Your line is now open.

Nancy Bush - NAB Research LLC

Two questions; on GWIM, the 20.1% pretax margin obviously depressed by the interest rate environment etcetera, etcetera. Is there a target operating margin there or is it somewhere we can sort of imagine a more normalized margin over the next years, because it seems like that business is sort of under contributing significantly at this point?

Brian Moynihan

I think that you pointed out that one of the strategies is to increase margins in wealth management businesses overall has been to drive the loans and deposits along with the strong asset management business we have. And I think as rates normalize Nancy and I guess normal is going to be hard to define here for the near term, as they normalize you'll that value has come back up and that'll increase the pre-tax margin because we don't need to do any more work to gather that in i.e. on the deposits side specially.

If you look at them, year-over-year they are down about 4% in expenses, (inaudible) banks run the two business for us, U.S. Trust and Global Merrill Lynch Global Wealth Management have been working on expenses. So revenues here will be flat and expenses are down and they're continuing to work on a non-client facing expenses especially and they'll be a beneficiary of all that work, so I think that'll help the margins.

But remember, that the core brokerage revenue which is at, and investment management revenue for the Merrill Lynch side as a group of the company is a lower margin business, our margins are better than anybody else, and so we've got to continue to improve them. But we look for that to improve, but I'd be careful about assuming, how much improvement, moving up 3%, 4% might be doable, but I wouldn't assume that it'll get back to a private banking style margin, because the dominance of the Merrill Lynch, the traditional brokerage revenue streams.

The other thing is, in overall, so remember that we're selling the international GWIM which had low margin, which will help improve the margins going forward.

Nancy Bush - NAB Research LLC

Okay. One more question on the litigation front; we've seen a couple of new lawsuits dumped on the banking industry over the past couple of weeks, you've got the [settlement to] with JPM regarding stuff required in their sterns and then you've got the Fed's of course suing Wells Fargo on FHA, way pre-crisis stuff. Are you guys vulnerable to either of those and have you already had provisions into various other settlements that you've been involved in that would address any of those issues?

Bruce Thompson

As an industry, there is no question that there has been an increase in that activity, so by virtue of being in the industry you are out there, I think the one thing that's important and if you go back to our DOJ AG settlement and when we took the hit for about $500 million when we announced that settlement, it covered a lot of the FHA activity predating I believe it was sometime in the latter half of 2009. So that piece of it relative to others we have resolved several quarters ago, it was obviously, it was a big number to resolve, so we do have that one that's out there behind us whereas some others don't and it was one of the key parts of that settlement for us. So we're little different from that perspective and we will just have to see how the balance of it unfolds and if other things come up.

Operator

We'll go next to the site of Mike Mayo with CLSA. Your line is open.

Mike Mayo - CLSA

Good morning. First a question on loan growth, what has commercial loan utilization done in this quarter versus the last quarter or two?

Bruce Thompson

It really, it's not so much that utilization of revolvers that has maintained and has remained in that loans 30s level. The loan growth that we're seeing is more actual funded loans that we're making as opposed to revolver draws.

Mike Mayo - CLSA

And I noticed that commercial loans grew 14% annualized linked quarter and that the period end loans were up a lot more than the average loans. Is anything happening in the economy to accelerate that commercial loan growth, I guess at the end of the quarter or is this just Bank of America's specific strategy?

Bruce Thompson

I think we have been pushing and looking to do more on the lending front for several quarters and we saw some of that materialize. And the one note I would Mike and we have it back in this slide, if you look at our banking segment, we did have one or two fundings at the end of the quarter that will get repaid during the fourth quarter. So it was a little bit accelerated in the fourth quarter, but even if you account to that back, we still saw very strong loan growth in the quarter.

Mike Mayo - CLSA

Alright, there will be noise when we compare fourth quarter to third quarter?

Bruce Thompson

It will be; but like I said, even without that, the growth was very strong.

Mike Mayo - CLSA

And you said loan growth is a priority. Are you willing to lower rates in order to stimulate more loan growth?

Bruce Thompson

We've been very disciplined and if you look in the supplement, and look at the average spread in our loan growth on the commercial side, that would be new originations and the spreads on that have remained at relatively flat on both on a quarter-over-quarter basis and while we want to make loans, but the loans that we make have to make economic sense and to have the returns on capital that are consistent with where we are taking the business, and the opportunities that we've seen and the ability to grow the book are generating those returns and we feel good about it.

And I think, you have to take a step back and look at the macro environment where here in the U.S. you've got banks that are competing and given the large liquidity basis that we have and capital basis looking to get invested some of the loan growth and if you look at it outside of the U.S. as we see some of the different foreign banks pull back, the opportunities for us to grow our loan base where relatively speaking were smaller internationally, we are using the opportunity with the capital and liquidity that we have to take advantage of that and you can see it in some of the trade finance and other loan areas outside the United States.

Mike Mayo - CLSA

Alright, so demand is not a whole lot better, you're not doing what's right to your gaining share from foreign banks; it might part of it anything else you want to add to that list?

Brian Moynihan

We referenced in the slide that in the real estate area, the first time in several quarters that we've seen growth in commercial real estate. We shape that business down when things got tough to a level that we thought make sense from a risk perspective and we're now in a position to be able to start growing that. And, while we're focused on doing things with our customers, we've seen one or two portfolios, not huge size that have come up that we've been able to bring in and when we do that, the first thing that we look at in those portfolios are how much of the exposure of the portfolio is the people that we do business with and we would like to do more, and we've had a couple of situations where we've been able to bring those portfolios in and become more significant with clients that we want to become more significant with.

Mike Mayo - CLSA

And then, switching gears, it was a good mortgage quarter. Are you holding any of the newly originated mortgages upon the balance sheet or are you securitizing and selling those immediately?

Brian Moynihan

A couple of points on that, the first is, we talked about loan growth within our Global Wealth and Investment Management area of a little over $2 billion on a notional amount for the quarter. A portion of that was mortgage lending that we do with that client base as well as securities base lending, so that there was some growth in mortgages within the GWIM space. Outside of the Global Wealth and Investment Management space, we are looking at starting to hold a little bit of conforming product where the product is priced and has the return that we think makes sense. So you may see in the fourth quarter and into the first quarter of next year holding a little bit more conforming product, but there was nothing material in that like during the third quarter.

Mike Mayo - CLSA

But, I mean just which spreads the way they are, why would you want to hold any mortgage loans on the balance sheet?

Bruce Thompson

Some of the mortgage loans were the mortgage loans that we make that in many cases tend to be more non-conforming, not conforming.

Mike Mayo - CLSA

Okay.

Bruce Thompson

But the non-conforming pricing can make sense and depending on the duration, some of the conforming stuff may or may not make sense. But your point is the right one and it's consistent with how we manage the different portfolios; we're not going to go out on the curve and take undue interest rate risk chasing yield in the short term.

Mike Mayo - CLSA

And then last question, there has been some articles recently about Merrill Lynch hiring brokers from other financial advisors. Are we about to see a war for financial advisor talent; are you looking to be above your number of financial advisors or just a general strategy for expanding the (inaudible)?

Brian Moynihan

We have a change our strategy, we have, Mike we have been fairly consistent in how we have worked on it, so we basically hire financial advisors and we bring advisors in the business for our PMD and our FSA programs; but no change from our standpoint.

Operator

And next to the site of Paul Miller with FBR. Your line is open.

Paul Miller - FBR

Yeah, just to piggyback Michael on the mortgage banking side. You guys used to be very a large player in the mortgage banking; we know you've exited both the wholesale and the corresponding business. But given where we are today and how profitable the mortgage banking space is, are you rethinking that a strategy, could you reenter the corresponding market or you're just planning to growth to the retail markets?

Brian Moynihan

We are not changing the strategy; we will continue to grow as we growing 14% this quarter and like the first quarter through the direct-to-retail. It's part of the focus of the strategy of the company to make mortgages to our customers and do a great job of it as oppose to buy closed loans in the secondary market.

Paul Miller - FBR

And so therefore, just the retail side, so how much market share you think you can gain on the retail side. I think you'd probably be around 4% or 5%. Can we see it materially increase that or that's probably where you are going to set?

Bruce Thompson

We are 4% or 5% of the overall mortgage market. On the direct-to-retail we are higher than that because you take out the correspondent. But if you just look at the number of customers, that have a mortgage somewhere else, there are a lot of customers in our wealth management business or in our preferred business. The amount of mortgage growth we could have to be very strong and that will continue to build as we focus the sales teams on those efforts.

If you look at the productivity of the mortgage loan officers we hired that worked with our teams and the branches and stuff, it is multiples of the productivity of people that are out working in the general fields. So as that business system continues to take hold, and even with the mortgage loan officers today, if we can get the loans process, we could close 15%, 20%, 25% more loans per day than we do today.

So we got lots of room to grow in this business, but we're going to do it in a way which is focused on our client, with high quality loans, because of the economics of business do not support anything else.

Paul Miller - FBR

Last question is your dispute with Fannie Mae, I believe you're not selling any loans of Fannie Mae, you are selling to Freddie Mac, which are both really run by the FHFA. Is the dispute with Fannie Mae at all hindering your ability to sell loans to the GSEs?

Bruce Thompson

I think we're growing faster than other people mortgage production on a quarterly basis.

Operator

We will go next to the side of Glenn Schorr with Nomura. Your line is open.

Glenn Shorr - Nomura

Thank you, just two quick follow ups, and I appreciate all the disclosure, I just want to make sure I'm trying to compare apples-to-apples. On the 8.97% that includes all model approval, when listening and looking at your disclosure it sounds like excluding model approval, it would be maybe 40 basis points lower at my end of the ballpark?

Brian Moynihan

I remember it would be slightly more of a reduction than that, but still below 100 basis points for IMM Glenn.

Glenn Shorr - Nomura

Okay, perfect. I know it's early, but in just general gut check. What should we focus on more, with or without, as we approach CCAR? In other words, again, trying to put the whole industry on an apples-to-apples basis?

Bruce Thompson

With or without?

Glenn Shorr - Nomura

IMM approval?

Bruce Thompson

We are spending an enormant amount of time, making sure through the different government channels in the like that we will be in a position as quickly as possible to be IMM compliant, obviously nobody has been declared to be IMM compliant yet, and I don't want to speculate on becoming IMM compliant.

I think the important thing is Glenn, if you look at the work that we've done with respect to Basel 3, and you look at where we are relative to our peers, we're in very good shape and I think the CCAR piece, there is two things that you have to be mindful of, the first is that last year the state of CCAR results are where your Basel 1 Tier 1 [comment] is probably gets adjusted this year to be Basel 1 and half relative to a 5% reference rate. That is the CCAR test, the way it was done last year, and our sense is probably the way that it ends up being done this year.

That's the base test. The second test is the [glide] path and do you show a path to being where you need to be from a Basel 3 perspective. And that's why when we talk about capital, we are very focused on both of those measures and we feel like, we are in very good shape under both Basel 1 and Basel 3 at this point.

Glenn Shorr - Nomura

I appreciate that. Just want to make sure, I heard what I think I heard. Some of the mortgages you are originating are putting on balance sheet now obviously good credit, the customers because its originated from your channel, but when gain on sale margins are at all time highs, it feels as an outsider that it would make sense to be selling them in to the market, but curious on how you view that in balance sheet versus selling amount?

Brian Moynihan

I think what Bruce said is in the third quarter, we sold them out. We are looking at retaining some, but it would not be material amount relative to the overall production of our mortgage business.

Glenn Shorr - Nomura

Okay, I appreciate that.

Brian Moynihan

The second things is you got to remember, we got a mortgage portfolio, runs off on the balance sheet today is $200 billion plus, so just to have that stay in place for lack of better term you have to fill it backup.

Glenn Shorr - Nomura

Unless some wants to pay you a lot of money for it, but I hear you. Finally the focus on earnings growth and loan growth, I think you talked effectively at all the price competition. I am curious if the industry has the potential to be low to sleep in this low rate environment.

So you mentioned that you are getting the same time of spread on new loan origination. It’s coming out at a lower rate, but we are in a excellent credit environment right now, but curiously if we were to see it turning the other way, if you feel like the industry might be putting on loans that were being low to sleep on spread, but the rates actually can get eaten up pretty quickly if there is a turn in credit.

Bruce Thompson

The one thing that we’ve not seen with loans coming is, historically when what you are referencing is the loans, it’s the structuring of loans and credit quality of loans that you can bring on the balance sheet starting to be impaired in this chase for yield.

The number of people globally that are looking to grow their loan books, you have to think globally is less than it's historically been, and when we're running the loan books, we're very focused on not just growing them, but making sure that the pricing returns out from a cost to capital perspective and that the structures continued to have integrity so that if what you just referenced happens, that we do not have losses that we're not comfortable living with.

And at this point, given what we're seeing in the global competitive market, the ability to put loans on that make sense for us and have the structures that protect us, we continue to feel very good about.

Brian Moynihan

And when we think about the consumer side, even the loans originated in - up to the standards were changed dramatically in ‘08 in terms of mortgage standards or even card standards in those ’07-’08, and you start to look at loans originated in the latter half of ‘08 and ‘09 and now three years plus later in an environment three years plus later where I think the core environment would have been through and [planning] to be lower than it is now and economic growth to be higher based on what people thought at that time.

We are seeing credit performance which is much better than the expected outcome. So we're always checking ourselves, and the question you raised which is how do we make sure that we drive the business and don’t have credit issues going forward.

What I’ll tell you though, is that’s where we want that we continue to frame this thing as how we run the company and focus on the core customer bases and do what they need and not just chasing growth for growth sake, and that then will keep us in things like the card business where in the past we may have drifted into credit that was more difficult from doing that, and we’re happy with our card business it’s growing strong, it’s growing with the right customers with a high credit quality, we’re not going to go reach for credit just to grow the business.

Glenn Shorr - Nomura

Perfect. I really appreciate it, thanks.

Operator

And we'll go next to the site of Vivek Juneja with JP Morgan. Your line is open.

Vivek Juneja - JPMorgan

Hi, Bruce, hi Brian. Just a couple of quick questions, HARP, how much did that account for your volume in the third quarter? And……..

Brian Moynihan

The HARP volume was about 30% of the originations.

Vivek Juneja - JPMorgan

Okay. And how long further, how far do you think you are in the process and how much longer do you expect to be able to keep doing?

Bruce Thompson

I think we'd expect that business to continue through the lion share of 2013.

Vivek Juneja - JPMorgan

Okay. Can you talk about the retail bank a little bit, it seems like, you are shutting branches but deposits continue to grow, can you talk a little bit about what's going on there, where you are getting growth from and the shutting of branches, where you are in that rationalization and despite that, it seems like you have been able to grow deposits quite a bit?

Brian Moynihan

So, let's think about it from all different points, which is, we need to bring the cost structure down so we've been on a plan to continue to close branches and you can see that we did, again,50-60 this quarter and we'll continue to do that, we're doing it carefully.

And as we close those branches the attrition we see is well within and less then we thought will be. So that's turning out to be good. So that's where the rate exposure is, so we are getting what we want. We are keeping the customers and that for less operating cost and that's a program that we'll continue carefully across and then each quarter will be a continuing progress.

When you look at the core business, the things like the Durban were in last years third quarter not this year third quarter. So you are starting to see the run rate come out of the post, of all the regulatory changes in revenue sort of linked quarter stabilizing, given the changes in fees that have been behind us now for several quarters.

Cap growth [continues] net new accounts. This mobile implementation were $11.1 million, 800,000 to subscribes this quarter, we are 1 million plus more then anybody else. But the good news is the cost impact of that or the service impact of that is, since we're allowing you to take a snap shot, you checked with almost [1.75 million] checks we've gone through in literally a couple of months of operations on that in the third quarter.

The payments made out for that platform are now running $1 billion plus a week, and we'll probably do $60 billion of payments through that platforms this year, we have already done 40 some billion or [non-30].

And then the more important part is that's all cost optimization, service optimization, and our customer scores continue to increase each month we see, our satisfaction score, we continue see an increase.

But importantly in the growth areas in the preferred segment, we continue to see strong growth there. We added about 500,000 plus clients from retail to preferred in other words upgrade and through depth of relationship which means we are bringing more than $50,000 in balances to it.

So we are quite please that business the Merrill lynch growth, and so I think its working and its working in a balance between getting the cost down on the retail side, expanding in preferred side and then also managing the customer experience in the middle.

Operator

Our next is from the side of Brennan Hawken with UBS. Your line is open.

Brennan Hawken - UBS

It's encouraging, certainly that you guys highlighted LAS expenses could come down next quarter, but is there a way to give us some magnitude so we can know how to model this.

Bruce Thompson

It's definitely no the same question, (inaudible). The best way is you are looking to model is in the third quarter, we staffed to solve or doing everything from a change in regulation, compliance as well as our own standards that we wanted to as it relates to how we both service as well as modify mortgages.

There was incremental work that was done in the third quarter to get to that point. The best way to start and to go through the analysis is to look at the number of 60 plus day delinquent loans that we have, because those without question require the most amount of work.

Given where we are now, what we would expect going forward is that you would see the expenses trend down at the same rate that you see the 60 plus day delinquencies come down, realizing it's going to be lagged by one and probably two quarters.

That’s the best way to get a proxy for the manner in which you should see those expenses come down. As Brian said, anything unexpected that comes up from an expense perspective.

Brian Moynihan

There are two things. We got to make sure we do this right and that’s why we had to build the staffing to make sure that we do the modification on a timely basis, and then secondly, getting in quarter-to-quarter, as you can see we're trying to guide you to long term, but the key thing is we are doing everything we can as the world comes down to get the resources down at the same pace.

So, it is something we’re absolutely focused on and we’ll deliver it for you, but we just have to make sure we do the work right, handle the customers right, it is a very difficult time for people to go through what’s going on, because all of these costs go to the modification, short sale, (inaudible)

Brennan Hawken - UBS

How much of that decline in 60 day delinquencies was due to modified loans and what’s the [redefault] risk there?

Brian Moynihan

Overall, we’ll get you some detail on that, but just conceptually each vintage of modifications perform better. So we’ve gone from levels of what have been after maybe year’s worth of modification back from ’08 and ’09 and ’08. We’ve been at this as long as people remember that we were running 50 and now we’re running them in the 20, low 20s or high teens.

So, the redefault rate has gone way down because the structure of the programs and frankly the duration time after the crisis.

Brennan Hawken - UBS

Okay. Just to make sure I understood, Brian I think you had said that, as far as the trajectory of the decline in expenses overall when you're looking at the entire thing at OAS taking a step back, moderate improvements in 2013, but the big lever there is 2014. Is that right or are we reading too much in to it?

Brian Moynihan

No, I think I was saying, that you'll get the improvement sort of on a quarterly basis all though '13 and in '14 you'll have the run rate of all that accumulated and for you, in year-over-year comparisons, but it's going to come all during '13.

We can debate about moderate when we are that [expense base]. The other question was discussing but it will come every single quarters, so it's not going to be held up and wait, it'll come as fast as it can.

So the word we're getting out this quarter has to do with the clients and the 60 plus day in the second quarter into the third quarter came out in the third, and the third quarter comes out in the fourth, it will take just little time, because you actually have to finish the work, reassign accounts and go on.

So it will come, it's not in quarter-by-quarter, it will come month-by-month, week-by-week all to the '13.

Bruce Thompson

And your number of modifications during the quarter was 40,000.

Kevin Stitt

Operator, one final question.

Operator

Absolutely sir, we'll take that final question from the site of Jefferson Harralson with KBW. Your line is open.

Jefferson Harralson - KBW

Okay, can you guys just remind us what your litigation cost were roughly per year recycle?

Bruce Thompson

We'll probably get back to that. I don't know (inaudible).

Jefferson Harralson - KBW

Was a long time ago.

Bruce Thompson

That seems like long time ago.

Jefferson Harralson - KBW

I just want to zero in a one line item which is on page four, the supplement (inaudible) being as other income, I heard you say something about that, they were from 600 million positive to 790 negative. Was some of that FBR or DVA or is that all in the [three account] here?

Bruce Thompson

At the FVO switch and other income was roughly, it was 1.2 billion delta during the quarter. So that's it.

Jefferson Harralson - KBW

Okay. Thank you very much guys.

Brian Moynihan

Thank you, okay. Well, thanks everyone for joining.