T O P R O M O T E

A G R I C U L T U R E, C O M M E R C E,

# Bank of North Dakota Annual Report 1993

A N D I N D U S T R Y

I N N O R T H D A K O T A

BND

The Mission Statement of the Bank of North Dakota featured on the cover of this year's Annual Report is as rele-

# 1993

vant today as it was when the Bank was founded in 1919. The Bank's primary mission is to promote the development and enrichment of the state's economy and spur job growth for its people. BND's secondary mission is to generate a financial return to the state while maintaining a sound balance sheet and capital structure.

The year 1993 marked a period in which BND renewed its focus and commitment to its mission in addition to adding the commitment to fully develop its people and resources in order to provide outstanding customer service. The year was one of significant accomplishments and also one during which the Bank commenced major initiatives to deal with the long term challenges it must resolve.

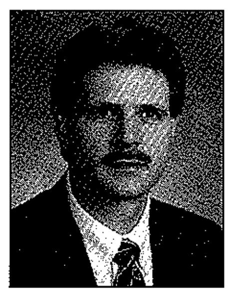
The cornerstone of BND's strategy is to build its loan portfolio. Doing so will not only increase funding for agriculture, commerce, and industry in the state—it will provide an increased return for BND. To build the loan portfolio more aggressively, but still prudently, BND has restructured its loan committees, changed its marketing approach, and worked hard to build strong ties with bankers and economic developers throughout the state. It has also worked closely with other funding sources, such as public and private venture capital funds and the guarantee agencies—particularly SBA and FmHA. By working with these other financial sources, BND can better manage risk and leverage its dollars.

Evidence that this relationship-building approach is working is demonstrated by the Bank's loan growth over the course of 1993. The commercial loan portfolio increased 23.5 percent and the agricultural loan portfolio increased 22.3 percent. After allowance for sale of $91 million in student loans to the Student Loan Trust, total loans for BND increased $82.7 million—from $222.9 million to $305.6 million—which is an overall increase of 26.3 percent. BND made a record volume of PACE loans, put funding in place for the MATCH Loan Program, and initiated a program to purchase and pool FmHA, VA, and conventional home mortgages for banks throughout the state. Since inception of the new residential mortgage program in August, BND purchased $17.7 million worth of home loans from banks throughout the state for resale into the secondary financial market.

To manage risk properly while expanding the loan portfolio, care was taken to ensure that other funding sources and the guarantee agencies participated with the Bank of North Dakota in these loans. For example, PACE loans funded or committed during the year totalled $19.4 million. Of that total, the Bank of North Dakota's share is $10.3 million, while other banks throughout the state carry $9.1 million. To date, the Bank of North Dakota has funded or committed a total of $45.2 million in PACE loans of which its share is $23.8 million and participating banks carry $21.4 million. Sharing the loans maintains prudent underwriting standards. Those underwriting standards are reflected in the program's low delinquency rate of less than one third of 1 percent with only one loan (in the amount of $6,924) charged off since inception. At the same time, a total of 2,145 jobs are in place or committed through PACE loans.



This match-funding approach to managing risk was utilized by BND with many of its programs. BND funded $126 million in loans during 1993, but that amount represents the Bank's participation interest in total loans of $245 million for a participation ratio of very close to 50 percent between BND and other financial institutions. Lending in this manner significantly leveraged BND's dollars and reduced the Bank's loan delinquency rate to 2.74 percent—



*John Hoeven, President*

one of its lowest levels ever. Further evidence that BND's approach is working was provided by the recently completed North Dakota Bankers Association Survey. Bankers throughout the state indicated their belief that BND's programs are proving

effective in helping to support economic development in North Dakota. In the region-by-region analysis provided in the survey, BND programs were consistently listed as the most helpful among programs supporting economic development.

*BND's Advisory Board members: Maren Daley, Don Porter, Frank Keogh, Curly Haugland, Todd Lang, Roger Berglumd, Bill Kingsbury*

In addition to fulfilling the Bank's primary mission, increasing loan volume is also vital to build and sustain the Bank's long-term earnings—particularly in light of the significant challenges to earnings which BND faces. Maintaining a consistent level of earnings—with growth over time—and a solid balance sheet constitute BND's secondary mission. The strong downward trend in interest rates over the last several years inflated Bank earnings in 1991 and 1992. Some of the benefit from the decline in interest rates spilled over into 1993 as well. Earnings for the year totalled $17.5 million, the second highest total in the Bank's history. A more valid comparison, however, would be to compare current earnings against the Bank's average annual earnings of $14 million over the last ten-year period. Comparison to the ten-year average is more meaningful because the Bank of North Dakota still faces significant issues which began to negatively impact earnings in 1993; the full impact will be felt in 1994 and beyond.

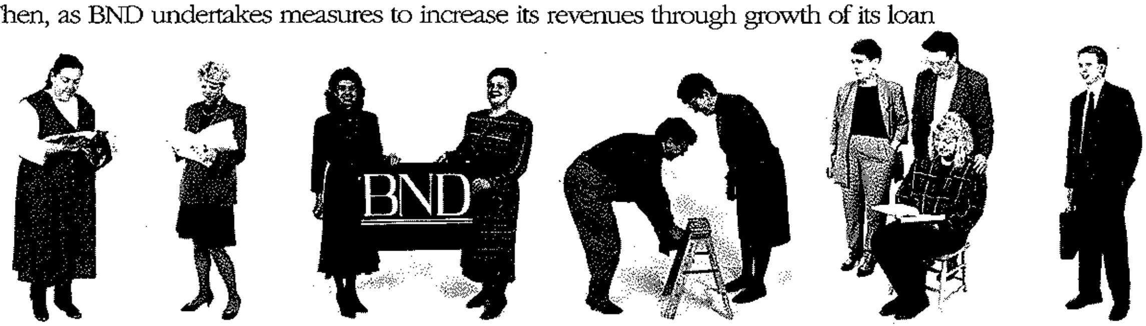
The issues which will impact earnings include a negatively gapped balance sheet. That is, the Bank has a portfolio of assets with generally longer fixed rate maturities than the maturities of the underlying deposit base utilized to fund those assets. Historically, this financial structure has enabled BND to generate strong earnings in periods of declining interest rates; but it significantly reduced Bank earnings in rising interest rate environments

such as we now face. Also, the capital base of the Bank has been reduced by approximately 20 percent through payments to the State General Fund—which is a reduction of the long term earning base. A third major concern is the Student Loan Program. Changes in federal legislation have significantly increased costs and reduced revenues from student loans, and the Federal Government is now a competitor with the state programs under the Direct Student Loan Program. A final major issue BND must resolve is absorption of the negative fund balance which has built up in the North Dakota Real Estate Trust since 1982.

The Bank of North Dakota initiated steps to manage each of these challenges during the course of 1993. The Asset/Liability Committee of the Bank worked to restructure BND's balance sheet to enable it to better perform as rates rise. A restructuring of this magnitude takes time and will not be completed until the end of 1994. One of the major steps included a program to convert the investment portfolio from fixed rate assets to variable rate assets; this will provide a higher return as interest rates rise helping to maintain BND's interest rate margin. The Bank also began close examination of the issuance of term bonds to place some term debt on the balance sheet as a means of better hedging its term assets, such as the Beginning Farmer and other loan programs that provide a fixed rate to the borrower.

*North Dakota Industrial Commission: Commissioner of Agriculture,Sarah Vogel; Governor Ed Schafer, Chairman; Attorney General Heidi Heitkamp*

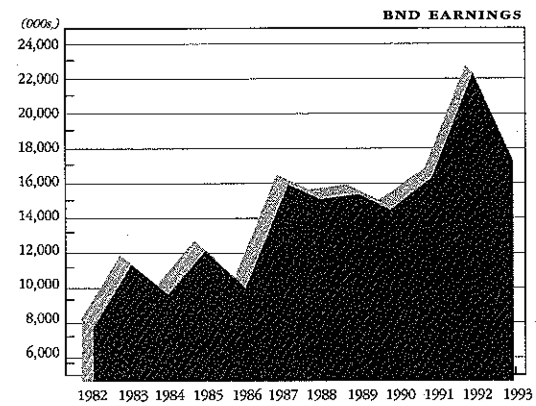
Management's objective in restructuring the balance sheet is to enable the Bank to sustain a consistent level of earnings over time regardless of interest rate fluctuations. Then, as BND undertakes measures to increase its revenues through growth of its loan

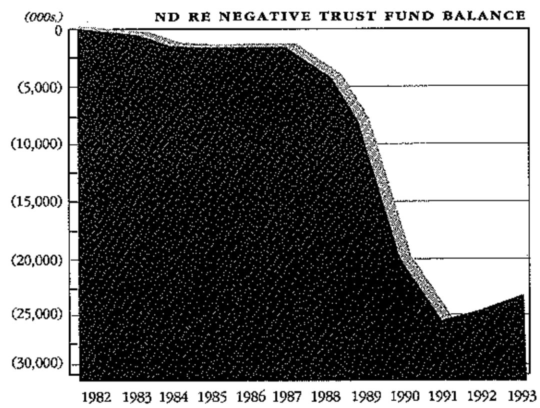


portfolio, that level of profitability can be increased and sustained at higher levels. BND finished the year with total assets of $872 million. This amount is less than 1992, however, the Bank's core deposits held steady, totalling $573 million for 1993 versus $571 million for 1992. The Bank did not experience its typical build-up of fed funds from banks throughout the state until after year end which increased total assets to well over $1 billion in early January. BND will only buy and sell funds in the secondary market to service its customer banks and generate a profit, not to maintain any specific targeted level of total assets.

To resolve the problem of the North Dakota Real Estate Trust and then restore BND's equity over time, the Bank has formulated a plan which it will bring to the Legislature for their input and concurrence by the 1995 Legislative Session. The need to implement a comprehensive plan is demonstrated by these graphs.

The graphs show Bank earnings over the last ten-year period and also the fund deficit built up in the North Dakota Real Estate Trust which the Bank of North Dakota has not yet absorbed. The North Dakota Real Estate Trust consists of a portfolio of agricultural loans made by the Bank prior to 1982. That portfolio has suffered significant losses since 1982, but those losses have not been absorbed by the Bank because the Trust was




| Year | BND Earnings | ND RE Trust Negative Fund Balance |
|---|---|---|
| 1982 | 7,824 | 0 |
| 1983 | 11,182 | (425) |
| 1984 | 9,318 | (2,277) |
| 1985 | 12,335 | (2,277) |
| 1986 | 9,997 | (2,277) |
| 1987 | 15,917 | (2,492) |
| 1988 | 15,240 | (3,927) |
| 1989 | 15,176 | (8,198) |
| 1990 | 12,547 | (19,714) |
| 1991 | 16,414 | (25,512) |
| 1992 | 22,125 | (24,126) |
| 1993 | 17,530 | (23,307) |

set up as a separate entity which issued bonds to carry the loans. BND's profits increased in the late 80s and early 90s due to the beneficial effect of falling interest rates, but the fund deficit in the North Dakota Real Estate Trust mounted significantly over the same period. Now Bank of North Dakota is faced with absorbing the existing $23 million fund deficit in the North Dakota Real Estate Trust as well as future losses of the Trust. At the same time, BND's capital has been reduced by the $20 million one-time-transfer to the State General Fund.

The Bank of North Dakota has put forward a plan and obtained Industrial Commission approval to work with the Legislature so that a resolution of the matter can be obtained by the 1995 Legislative Session. BND has already submitted the issue to Interim Legislative Committees with the recommendation that either the Bank absorb the full North Dakota Real Estate Trust liability or that the bonds be paid from property tax revenues provided by the original authorizing statute. Under this plan, BND would pay its appropriation to the State General Fund for the 1993-1995 Biennium as budgeted. It would then seek input from the 1995 Legislature: should BND absorb the Real Estate Trust?—or should outstanding bonds of the Trust be paid from the levy of property taxes? In the event the Bank absorbs the full liability, its capital will be reduced from $100 million to approximately $77 million. Therefore, the Bank must work closely with the 1995 Legislature to ensure that future earnings are utilized for rebuilding of the Bank's equity accounts over time as well as for paying a reasonable dividend to the State General Fund.

*BND's division managers: front row: Julie Kubisiak, Dale Eberle; back row: Ed Sather, Bob Gruman*

Relative to Student Loans, BND has undertaken a complete reorganization of its Student Loan Program. The purpose of this reorganization is to ensure that the Bank utilizes its people, technology, and capital efficiently in order to become a low-cost, high quality provider of student loans. Only on that basis can it compete effectively under the new Federal program. Over four years ago, the Bank began investigation and analysis of data processing systems to fully automate processing of student loans. During 1993, the Bank finally brought a new system on-line. The conversion involves over 240,000 loans totalling in excess of $300 million which BND owns or services. Consequently, the task is enormous in terms of work for our people and cost, but it is a task which must be accomplished if we are to compete successfully in the future.

The dedicated Bank of North Dakota staff has responded in positive fashion to all of these challenges. Through their efforts, much progress has been made over the course of 1993. BND is positioning itself to generate consistent earnings with growth over time. Also, the measures initiated in 1993 will strengthen the Bank's balance sheet and increase its capital base for the long term.

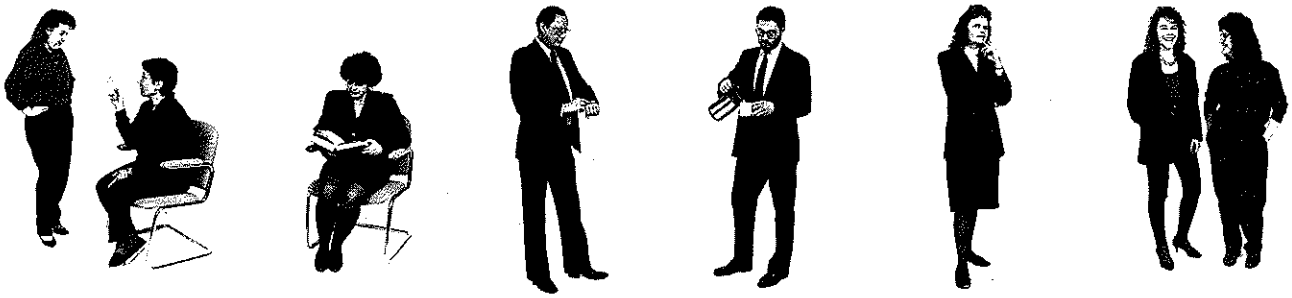
Going forward, management is committed to developing the technical resources and providing the training to ensure that BND personnel have the tools needed to maintain a high level of performance. For 1994, BND's Human Resources Department is developing a comprehensive training program to further strengthen the Bank's customer service orientation and its focus on mission. BND's role in funding economic development in North Dakota is more important than ever, and BND is working to fulfill that role.

| | 1993 | 1992 | 1991 | 1990 |
|---|---|---|---|---|
| **OPERATING RESULTS** *(in thousands)* | | | | |
| Interest income | $ 46,833 | $ 57,107 | $ 64,211 | $ 69,783 |
| Interest expense | 23,456 | 28,251 | 41,391 | 52,727 |
| Net interest income | 23,377 | 28,856 | 22,820 | 17,056 |
| Provision for loan losses | 600 | 667 | 698 | – |
| Net interst income after provision for loan losses | 22,777 | 28,189 | 22,122 | 17,056 |
| Other income | 5,388 | 5,113 | 5,083 | 4,631 |
| Other expenses | 10,635 | 10,962 | 10,791 | 9,140 |
| Net income | 17,530 | 22,340 | 16,414 | 12,547 |
| Paid to State Treasurer (Appropriation) | 11,116 | 18,596 | 4,696 | 14,000 |
| **BALANCE SHEET–YEAR END** *(in thousands)* | | | | |
| **TOTAL ASSETS** | 872,220 | 1,064,109 | 956,759 | 893,972 |
| **FEDERAL FUNDS SOLD AND SECURITIES PURCHASED UNDER REVERSE REPURCHASE AGREEMENTS** | 62,680 | 208,951 | 110,305 | 170,200 |
| **INVESTMENT SECURITIES** | 428,333 | 458,414 | 496,789 | 411,664 |
| U.S. Treasury securities | 254,792 | 316,861 | 349,028 | 230,117 |
| Obligations of other U.S. Government agencies | 10,019 | 10,030 | 55,352 | 40,484 |
| Mortgage-backed securities | 126,532 | 63,205 | 72,925 | 75,574 |
| Other money market instruments | | – | 5,000 | 50,002 |
| Obligations of states and political subdivisions | 12,989 | 11,628 | 7,942 | 7,381 |
| Commerical paper | 17,312 | 50,000 | – | – |
| Other securities | 6,689 | 6,690 | 6,542 | 8,106 |
| **LOANS** | 305,552 | 313,873 | 266,854 | 227,984 |
| Loans held for sale | 14,996 | – | – | – |
| Residential loans | 42,322 | 61,655 | 78,564 | 88,969 |
| Guaranteed student loans | 75,026 | 118,639 | 86,487 | 46,886 |
| Bank participation loans | | | | |
| Commercial | 78,697 | 63,722 | 51,269 | 43,474 |
| Agriculture | 52,567 | 43,270 | 28,636 | 22,786 |
| Farm real estate loans | 25,638 | 20,675 | 15,729 | 12,449 |
| State institutions | 12,264 | 2,965 | 3,167 | 8,441 |
| Bank stock | 3,204 | 2,795 | 2,698 | 3,892 |
| Other loans | 838 | 152 | 304 | 1,087 |
| **DEPOSITS** | 573,317 | 571,355 | 541,835 | 509,433 |
| Non-interest bearing | 87,916 | 91,158 | 80,789 | 60,794 |
| Interest bearing | 485,401 | 480,197 | 461,046 | 448,639 |
| **FEDERAL FUNDS PURCHASED AND SECURITIES SOLD UNDER REPURCHASE AGREEMENTS** | 121,112 | 322,308 | 247,664 | 227,955 |
| **CAPITAL FUNDS** | 100,000 | 114,119 | 92,917 | 96,618 |
| Capital | 22,000 | 22,000 | 22,000 | 22,000 |
| Surplus | 22,000 | 22,000 | 22,000 | 22,000 |
| Contributed capital | 1,394 | 1,394 | 1,394 | 1,394 |
| Undivided profits | 54,606 | 68,725 | 47,523 | 51,224 |

*Reclassifications: Certain amounts have been reclassified in prior years to conform to the 1993 presentation.*

## S U M M A R Y

| 1989 | 1988 | 1987 | 1986 | 1985 | 1984 |
|---|---|---|---|---|---|
| $ 74,899 | $ 68,884 | $ 68,639 | $ 75,948 | $ 75,946 | $ 77,974 |
| 55,990 | 49,489 | 48,221 | 52,680 | 55,765 | 60,296 |
| 18,909 | 19,395 | 20,418 | 23,268 | 20,181 | 17,678 |
| – | 750 | 2,000 | 10,153 | 6,893 | 8,790 |
| 18,909 | 18,645 | 18,418 | 13,115 | 13,288 | 8,888 |
| 4,485 | 3,684 | 3,484 | 3.908 | 3,704 | 2,889 |
| 8,217 | 7,089 | 5,985 | 7,026 | 4,657 | 4,128 |
| 15,176 | 15,240 | 15,917 | 9,997 | 12,335 | 9,318 |
| – | 6,000 | 7,750 | 3,500 | 3,000 | 2,500 |
| 971,866 | 900,113 | 884,569 | 944,592 | 980,348 | 829,623 |
| 388,172 | 278,875 | 198,715 | 301,575 | 255,530 | 262,355 |
| 319,773 | 368,499 | 419,323 | 345,245 | 390,914 | 235,629 |
| 86,228 | 252,057 | 270,218 | 267,828 | 300,934 | 160,028 |
| 83,065 | 48,430 | 129,658 | 67,638 | 66,400 | 63,511 |
| – | – | – | – | – | – |
| 136,250 | 56,978 | – | 2,577 | 3,228 | 3,192 |
| 5,927 | 4,971 | 14,450 | 6,987 | 20,352 | 8,898 |
| – | – | – | – | – | – |
| 8,303 | 6,063 | 4,997 | 215 | – | – |
| 203,315 | 209,225 | 207,147 | 213,674 | 243,233 | 270,490 |
| – | – | – | – | – | – |
| 99,049 | 109,445 | 117,562 | 128,627 | 144,344 | 153,978 |
| 32,744 | 29,373 | 21,204 | 23,745 | 21,336 | 27,676 |
| 32,405 | 30,077 | 34,437 | 43,000 | 62,252 | 79,023 |
| 15,495 | 12,489 | 13,172 | 4,753 | – | – |
| 10,004 | 7,745 | 6,932 | 5,773 | 4,941 | 2,186 |
| 8,590 | 13,856 | 3,102 | 1,443 | 1,665 | 289 |
| 4,398 | 5,975 | 7,093 | 5,671 | 6,478 | 5,269 |
| 631 | 265 | 3,645 | 662 | 2,217 | 2,069 |
| 545,868 | 457,485 | 559,895 | 571,545 | 628,871 | 590,800 |
| 49,133 | 48,947 | 68,563 | 82,885 | 122,722 | 104,288 |
| 496,735 | 408,538 | 491,332 | 488,600 | 506,149 | 486,512 |
| 255,952 | 274,434 | 162,500 | 217,877 | 246,585 | 140,840 |
| 84,016 | 89,472 | 74,232 | 68,921 | 58,924 | 55,589 |
| 22,000 | 22,000 | 22,000 | 22,000 | 21,750 | 18,000 |
| 22,000 | 22,000 | 22,000 | 22,000 | 21,750 | 20,000 |
| 1,394 | 1,394 | 1,394 | – | – | – |
| 38,622 | 44,078 | 28,838 | 24,921 | 15,424 | 17,589 |



## INDEPENDENT AUDITOR'S REPORT

The Industrial Commission
State of North Dakota
Bismarck, North Dakota

We have audited the accompanying balance sheets of The Bank of North Dakota as of December 31, 1993 and 1992, and the related statements of income, changes in capital funds and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Bank of North Dakota as of December 31, 1993 and 1992, and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles.

BRADY, MARTZ & ASSOCIATES, P.C.

January 14, 1994
Minot, North Dakota

THE BANK OF NORTH DAKOTA

## BALANCE SHEETS

DECEMBER 31, 1993 AND 1992

### ASSETS

| | *(in thousands)* 1993 | 1992 |
|---|---|---|
| CASH AND DUE FROM BANKS | $ 77,163 | $ 79,837 |
| FEDERAL FUNDS SOLD AND SECURITIES PURCHASED UNDER REVERSE REPURCHASE AGREEMENTS | 62,680 | 208,951 |
| Cash and cash equivalents | 139,843 | 288,788 |
| INVESTMENT SECURITIES | 428,333 | 458,414 |
| Less allowance for investment losses | (3,792) | (1,592) |
| | 424,541 | 456,822 |
| LOANS HELD FOR SALE | 14,996 | – |
| LOANS | 290,556 | 313,873 |
| Less allowance for loan losses | (12,900) | (12,664) |
| | 292,652 | 301,209 |
| BANK PREMISES, EQUIPMENT, AND SOFTWARE | 4,205 | 4,268 |
| ACCRUED INTEREST RECEIVABLE | 8,557 | 11,262 |
| OTHER ASSETS | 2,422 | 1,760 |
| | $ 872,220 | $1,064,109 |

### LIABILITIES AND CAPITAL FUNDS

| | 1993 | 1992 |
|---|---|---|
| DEPOSITS: | | |
| Non-interest bearing | $ 87,916 | $ 91,158 |
| Interest bearing | 485,401 | 480,197 |
| | 573,317 | 571,355 |
| FEDERAL FUNDS PURCHASED AND SECURITIES SOLD UNDER REPURCHASE AGREEMENTS | 121,112 | 322,308 |
| LONG-TERM DEBT | 49,908 | 49,862 |
| ACCRUED INTEREST PAYABLE | 1,752 | 1,451 |
| OTHER LIABILITIES | 4,462 | 3,878 |
| APPROPRIATIONS PAYABLE | 21,669 | 1,136 |
| TOTAL LIABILITIES | 772,220 | 949,990 |
| CAPITAL FUNDS: | | |
| Capital | 22,000 | 22,000 |
| Capital surplus | 22,000 | 22,000 |
| Contributed capital | 1,394 | 1,394 |
| Undivided profits | 54,606 | 68,725 |
| Total capital funds | 100,000 | 114,119 |
| | $ 872,220 | $1,064,109 |

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

THE BANK OF NORTH DAKOTA
## STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1993 AND 1992

| | 1993 | 1992 |
|---|---|---|
| | *(in thousands)* | |
| INTEREST INCOME | | |
| Interest and fees on loans | $ 18,853 | $ 23,054 |
| Interest on investment securities | 24,879 | 30,527 |
| Interest on federal funds sold and securities purchased under reverse repurchase agreements | 3,101 | 3,526 |
| | 46,833 | 57,107 |
| INTEREST EXPENSE | | |
| Interest on deposits | 14,542 | 17,224 |
| Interest on federal funds purchased and securities sold under repurchase agreements | 4,694 | 6,806 |
| Interest on long-term debt | 4,220 | 4,221 |
| | 23,456 | 28,251 |
| Net interest income | 23,377 | 28,856 |
| PROVISION FOR LOAN LOSSES | 600 | 667 |
| Net interest income after provision for loan losses | 22,777 | 28,189 |
| OTHER INCOME | | |
| Service fees and other | 6,636 | 4,443 |
| Securities gains and losses | 952 | 1,003 |
| Provision for investment losses | (2,200) | (333) |
| | 5,388 | 5,113 |
| OTHER EXPENSE | | |
| Salaries | 4,034 | 3,979 |
| Pensions and other employee benefits | 1,149 | 1,138 |
| Data processing | 2,199 | 1,520 |
| Other operating expenses | 2,514 | 2,083 |
| Depreciation and amortization | 739 | 742 |
| | 10,635 | 9,462 |
| INCOME BEFORE EXTRAORDINARY ITEM | 17,530 | 23,840 |
| Extraordinary item—Relief of indebtedness granted to North Dakota Real Estate Trust | – | 1,500 |
| NET INCOME | $ 17,530 | $ 22,340 |

THE BANK OF NORTH DAKOTA
## STATEMENTS OF CHANGES IN CAPITAL FUNDS
FOR THE YEARS ENDED DECEMBER 31, 1993 AND 1992

*(in thousands)*

| | Capital | Capital Surplus | Contributed Capital | Undivided Profits | Total |
|---|---|---|---|---|---|
| BALANCES, JANUARY 1, 1992 | $ 22,000 | $ 22,000 | $ 1,394 | $ 47,520 | $ 92,914 |
| Net income | – | – | – | 22,340 | 22,340 |
| Appropriations | – | – | – | (1,135) | (1,135) |
| BALANCES, DECEMBER 31, 1992 | $ 22,000 | $ 22,000 | $ 1,394 | $ 68,725 | $ 114,119 |
| Net income | – | – | – | 17,530 | 17,530 |
| Appropriations | – | – | – | (31,649) | (31,649) |
| BALANCES, DECEMBER 31, 1993 | $ 22,000 | $ 22,000 | $ 1,394 | $ 54,606 | $ 100,000 |

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

THE BANK OF NORTH DAKOTA

## STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 1993 AND 1992

| | *(in thousands)* 1993 | 1992 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | $ 17,530 | $ 22,340 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Relief of indebtedness granted to North Dakota Real Estate Trust | – | 1,500 |
| Depreciation and amortization | 847 | 850 |
| Provision for loan losses | 600 | 667 |
| Provision for investment losses | 2,200 | 333 |
| Amortization of premiums and accretion of discounts on investment securities | (2) | (101) |
| Investment securities gains, net | (863) | (1,003) |
| (Gain) loss on sale of equipment | – | (1) |
| Changes in assets and liabilities: | | |
| Increase in loans held for sale | (14,996) | – |
| Decrease in accrued interest receivable | 2,705 | 2,716 |
| (Increase) decrease in other assets | (669) | 340 |
| Increase (decrease) in accrued interest payable | 301 | (1,050) |
| Increase (decrease) in other liabilities | 584 | 330 |
| Net cash provided by operating activities | $ 8,237 | $ 26,921 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from sales and maturities of investment securities | $ 435,968 | $ 638,113 |
| Purchase of investment securities | (405,022) | (598,486) |
| Net (increase) decrease in loans | 22,898 | (47,314) |
| Purchases of equipment and software | (676) | (615) |
| Proceeds from sale of equipment | – | 1 |
| Net cash provided (used) by investing activities | $ 53,168 | $ (8,301) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Net increase (decrease) in non-interest bearing deposits | $ (3,242) | $ 10,367 |
| Net increase in interest bearing deposits | 5,204 | 18,354 |
| Net increase (decrease) in federal funds purchased and securities sold under repurchase agreements | (201,196) | 74,644 |
| Payment of appropriations due | (11,116) | (18,596) |
| Net cash provided (used) in financing activities | (210,350) | 84,769 |
| INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | $(148,945) | $ 103,389 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR | 288,788 | 185,399 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | $ 139,843 | $ 288,788 |

| | *(in thousands)* 1993 | 1992 |
|---|---|---|
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION: | | |
| Cash payments for: | | |
| Interest paid to customers | $ 14,225 | $ 18,010 |
| Interest paid on federal funds purchased and securities sold under repurchase agreements | 4,710 | 7,064 |
| Interest paid on long-term debt | 3,938 | 3,938 |
| SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES: | | |
| Other real estate acquired in settlement of loans | $ 55 | $ 130 |
| Transfer from Undivided Profits to appropriation payable to various state agencies | 31,649 | 1,135 |

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

# NOTES TO FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 1993 AND 1992

## NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Bank of North Dakota is owned and operated by the State of North Dakota under the supervision of the Industrial Commission as provided by Chapter 6-09 of the North Dakota Century Code.

**Cash and cash equivalents** - The Bank considers currency on hand, demand deposits in other financial institutions, cash items expected to be converted to cash, and federal funds sold and securities purchased under reverse repurchase agreements with original maturities of three months or less as cash and cash equivalents. The carrying amount of cash and cash equivalents is a reasonable estimate of its fair value.

**Investment securities and allowance for investment losses** - Securities are stated at cost reduced by an allowance for investment losses, and adjusted for amortization of premiums and accretion of discounts which are recognized as adjustments to interest income. Gains or losses on disposition are based on the net proceeds and the adjusted carrying amount of the securities sold, using the specific identification method. The allowance for investment losses is established through a provision for investment losses charged to expenses and is attributable to specific adverse conditions for particular securities.

**Loans held for sale** - Mortgage loans purchased and held for sale in the secondary market are carried at the lower of cost or market value determined on an aggregate basis. Net unrealized losses are recognized in a valuation allowance through charges to income. Gains and losses on the sale of loans held for sale are determined using the specific identification method. At December 31, 1993, the cost of loans held for sale exceeded market value.

**Loans** - Loans are stated at the principal balance outstanding, less an allowance for loan losses. Interest income on loans is accrued at the specific rate on the outstanding principal balance.

Interest accruals on loans are discontinued when in management's opinion the collection of the interest is doubtful. When a loan is placed on non-accrual status, accrued but uncollected interest is reversed. Interest accrued during the current year is reversed against current income, and interest accrued from prior years is charged against the allowance for loan losses.

**Allowance for loan losses** - The Bank uses the allowance method in providing for loan losses. Accordingly, the allowance is increased by the current years provision for loan losses charged to operations and reduced by net charge-offs.

The adequacy of the allowance for loan losses and the provisions for loan losses charged to operations are based on management's evaluation of a number of factors, including recent loan loss experience, continuous evaluation of the loan portfolio quality, current and anticipated economic conditions, and other pertinent factors. Loans are charged to the allowance when management believes the collection of the principal is doubtful.

**Bank premises, equipment, and software** - Bank premises, equipment, and software are stated at cost less accumulated depreciation or amortization. Depreciation and amortization are provided over the estimated useful lives of the individual assets using the straight-line method. The estimated useful lives used in the computation of depreciation or amortization are 25 years for bank premises, 5 years for equipment and software, and 10 years for furniture.

**Other real estate** - Other real estate (ORE), which is included in other assets, represents properties acquired through foreclosure or other proceedings. ORE is recorded at the lower of the amount of the loan or fair market value of the properties. Any writedown to fair market value at the time of transfer to ORE is charged to the allowance for loan losses. Property is evaluated regularly to ensure that the recorded amount is supported by the current fair market value.

**Long-term debt issue costs** - Long-term debt issue costs are being amortized over the term of the related long-term debt using the straight-line method.

**Defined benefit plan** - The Bank funds amounts equal to pension costs accrued.

**Income taxes** - The Bank of North Dakota is a governmental agency of the State of North Dakota and as such is not obligated for federal or state income taxes.

NOTE 2 - **INVESTMENT SECURITIES**

The detail of the carrying amount and approximate market value of investment securities at December 31, is as follows:

| | 1993 Carrying Amount | 1993 Approximate Market Value | 1992 Carrying Amount | 1992 Approximate Market Value |
|---|---|---|---|---|
| | *(in thousands)* December 31 | | | |
| U.S. TREASURY SECURITIES | | | | |
| Due within 1 year | $ 81,968 | $ 82,703 | $ 145,068 | $ 147,842 |
| After 1 year, within 5 years | 172,824 | 174,571 | 171,793 | 174,600 |
| Total | $ 254,792 | $ 257,274 | $ 316,861 | $ 322,442 |
| OBLIGATIONS OF OTHER U.S. GOVERNMENT AGENCIES | | | | |
| Due within 1 year | $ – | $ – | $ 5,004 | $ 5,009 |
| After 1 year, within 5 years | 10,019 | 10,508 | 5,026 | 5,452 |
| Total | $ 10,019 | $ 10,508 | $ 10,030 | $ 10,461 |
| MORTGAGE-BACKED SECURITIES | $ 126,532 | $ 126,594 | $ 63,205 | $ 64,951 |
| OBLIGATIONS OF STATES AND POLITICAL SUBDIVISIONS | | | | |
| Due within 1 year | $ 23 | $ 23 | $ 49 | $ 49 |
| After 1 year, within 5 years | 2,826 | 2,825 | 1,767 | 1,766 |
| After 5 years, within 10 years | 3,189 | 3,189 | 2,979 | 2,979 |
| After 10 years | 6,951 | 6,450 | 6,833 | 6,322 |
| Total | $ 12,989 | $ 12,487 | $ 11,628 | $ 11,116 |
| INVESTMENT IN DEBT SECURITIES | $ 404,332 | $ 406,863 | $ 401,724 | $ 408,970 |
| COMMERCIAL PAPER | | | | |
| Due within 1 year | $ 17,312 | $ 17,317 | $ 50,000 | $ 50,000 |
| OTHER SECURITIES | | | | |
| After 10 years | $ 6,689 | $ 102 | $ 6,690 | $ 1,623 |
| TOTAL INVESTMENT SECURITIES | $ 428,333 | $ 424,282 | $ 458,414 | $ 460,593 |

The market value of investment securities is based on quoted market prices bid, if available. Quoted market prices are not readily available for obligations of state and political subdivisions and certain other securities. The carrying amount of the Bank's investment in state and political subdivision debt is believed to be a conservative estimate of the market value of that debt. The market value of other securities is estimated by discounting future cash flows. The carrying amount of accrued interest receivable on investments is a reasonable estimate of its fair value.

The carrying amount, gross unrealized gains and losses, and market values of investments in debt securities are as follows:

| | (in thousands) December 31, 1993 | | | |
|---|---|---|---|---|
| | Carrying Amount | Gross Unrealized Gains | Gross Unrealized Losses | Market Value |
| U.S. TREASURY SECURITIES | $ 254,792 | $ 2,482 | $ – | $ 257,274 |
| OBLIGATION OF OTHER U.S. GOVERNMENT AGENCIES | 10,019 | 495 | 6 | 10,508 |
| MORTGAGE-BACKED SECURITIES | 126,532 | 466 | 404 | 126,594 |
| OBLIGATIONS OF STATES AND POLITICAL SUBDIVISIONS | 12,989 | – | 502 | 12,487 |
| | $ 404,332 | $ 3,443 | $ 912 | $ 406,863 |

| | (in thousands) December 31, 1992 | | | |
|---|---|---|---|---|
| | Carrying Amount | Gross Unrealized Gains | Gross Unrealized Losses | Market Value |
| U.S. TREASURY SECURITIES | $ 316,861 | $ 5,819 | $ 238 | $ 322,442 |
| OBLIGATION OF OTHER U.S. GOVERNMENT AGENCIES | 10,030 | 431 | – | 10,461 |
| MORTGAGE-BACKED SECURITIES | 63,205 | 1,748 | 2 | 64,951 |
| OBLIGATIONS OF STATES AND POLITICAL SUBDIVISIONS | 11,628 | – | 512 | 11,116 |
| | $ 401,724 | $ 7,998 | $ 752 | $ 408,970 |

Proceeds from sales of investments in debt securities for the years December 31, 1993 and 1992 were $55,884,000 and $135,225,000, respectively. Gross gains of $863,000 and $937,000 were realized on those sales in 1993 and 1992, respectively.

Securities carried at $39,044,000 at December 31, 1993 and $151,389,000 at December 31, 1992 were used for securities sold under agreements to repurchase and for other required pledged purposes. The approximate market value on the pledged securities at December 31, 1993 and 1992 was $39,967,000 and $155,283,000, respectively.

The detail of changes in the allowance for investment losses for the years ended December 31, 1993, and 1992 is as follows:

| | (in thousands) 1993 | 1992 |
|---|---|---|
| Balance, beginning of year | $ 1,592 | $ 1,259 |
| Provision for investment losses | 2,200 | 333 |
| Investments charged off | – | – |
| Balance, end of year | $ 3,792 | $ 1,592 |

NOTE 3 - **LOANS**

The fair value of residential loans has been estimated using valuation techniques which adjust mortgage values to approximate the quoted market yield for GNMA mortgage-backed securities.

The fair value of student loans is based on quoted market prices.

The fair value of all other loan categories has been estimated by discounting future cash flows to reflect management's estimate of current rates for financing borrowers under substantially similar terms and degrees of risk.

The fair value of all loans reflects the credit risk within the individual loan categories.

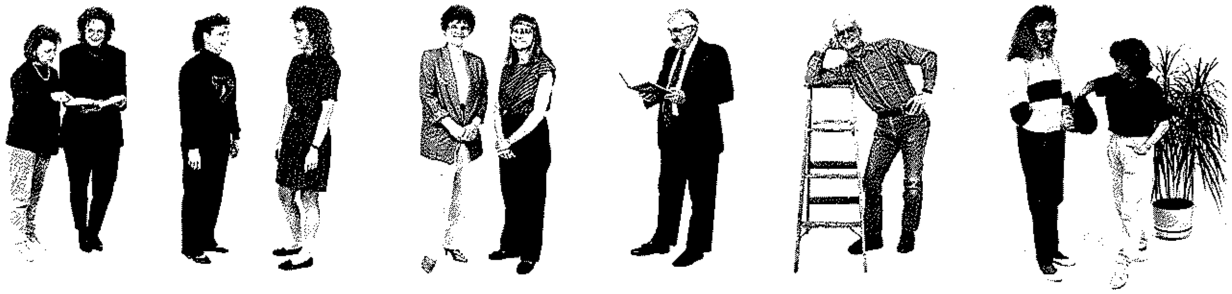
| | *(in thousands)* | | | |
|---|---|---|---|---|
| | 1993 Carrying Value | 1993 Fair Value | 1992 Carrying Value | 1992 Fair Value |
| Residential loans | $ 42,322 | $ 45,292 | $ 61,655 | $ 62,984 |
| Guaranteed student loans | 75,026 | 75,401 | 118,639 | 118,944 |
| Bank participation loans | | | | |
| Commercial | 78,697 | 72,053 | 63,722 | 57,528 |
| Agricultural | 52,567 | 49,471 | 43,270 | 41,541 |
| Farm real estate loans | 25,638 | 22,045 | 20,675 | 19,010 |
| State institutions | 12,264 | 11,334 | 2,965 | 2,689 |
| Bank stock | 3,204 | 2,127 | 2,795 | 2,502 |
| Other | 838 | 832 | 152 | 141 |
| | 290,556 | 278,555 | 313,873 | 305,339 |
| Less allowance for loan losses | (12,900) | – | (12,664) | – |
| | $ 277,656 | $ 278,555 | $ 301,209 | $ 305,339 |

The carrying amount of accrued interest receivable on loans is a reasonable estimate of fair value.

Nonaccrual and restructured loans amounted to $919,000 and $7,645,000, respectively, at December 31, 1993, and $823,000 and $5,269,000, respectively, at December 31, 1992. Additional interest income that would have been earned under original terms of the nonaccrual loans amounted to approximately $69,000 and $74,000 for 1993 and 1992, respectively.

The detail of changes in the allowance for loan losses for years ended December 31, 1993 and 1992 is as follows:

| | *(in thousands)* | |
|---|---|---|
| | 1993 | 1992 |
| Balance, beginning of year | $ 12,664 | $ 12,162 |
| Provision charged to operations | 600 | 667 |
| Loans charged off | (534) | (341) |
| Recoveries | 170 | 176 |
| Balance, end of year | $ 12,900 | $ 12,664 |



NOTE 4 - **BANK PREMISES, EQUIPMENT, AND SOFTWARE**

The following is a summary of changes in bank premises, equipment, furniture, and software at December 31, 1993 and 1992:

*(in thousands)*

| | Balance January 1, 1993 | Additions | Retirements | Balance December 31, 1993 |
|---|---|---|---|---|
| Land | $ 287 | $ – | $ – | $ 287 |
| Building | 3,687 | 172 | – | 3,859 |
| Equipment | 1,867 | 236 | – | 2,103 |
| Furniture | 562 | 130 | – | 692 |
| Software | 1,670 | 138 | – | 1,808 |
| | 8,073 | 676 | – | 8,749 |
| Less accumulated depreciation | (3,805) | (739) | – | (4,544) |
| | $ 4,268 | $ (63) | $ – | $ 4,205 |

| | Balance January 1, 1992 | Additions | Retirements | Balance December 31, 1992 |
|---|---|---|---|---|
| Land | $ 287 | $ – | $ – | $ 287 |
| Building | 3,382 | 305 | – | 3,687 |
| Equipment | 1,764 | 103 | – | 1,867 |
| Furniture | 552 | 10 | – | 562 |
| Software | 1,473 | 197 | – | 1,670 |
| | 7,458 | 615 | – | 8,073 |
| Less accumulated depreciation | (3,063) | (742) | – | (3,805) |
| | $ 4,395 | $ (127) | $ – | $ 4,268 |

Depreciation and amortization expense on the above assets amounted to $739,000 and $742,000 in 1993 and 1992, respectively.

NOTE 5 - **DEPOSITS**

The fair value of deposits with no stated maturity, such as checking, savings, money market, and NOW accounts, is equal to the amount payable on demand. The fair value of interest bearing certificates of deposit has been estimated by discounting future cash flows using rates currently offered for deposits of similar remaining maturities. The carrying amount of those certificates is $282,330,000 and $254,369,000 and the fair value is estimated to be $288,928,000 and $261,842,000 at December 31, 1993 and 1992, respectively. The carrying amount of accrued interest payable on deposits is a reasonable estimate of fair value.

NOTE 6 - **FEDERAL FUNDS PURCHASED AND SECURITIES SOLD UNDER REPURCHASE AGREEMENT**

Federal funds purchased and securities sold under repurchase agreements are short-term instruments for which carrying amounts are reasonable estimates of fair value. The carrying amount of accrued interest payable on federal funds purchased and securities sold under repurchase agreements is a reasonable estimate of fair value.

NOTE 7 - **LONG-TERM DEBT**

Long-term debt consists of:

| | *(in thousands)* 1993 | 1992 |
|---|---|---|
| Long-term notes, 7.875%, (effective interest rate 7.94%) issued December 1986, due December 1996, | $ 50,000 | $ 50,000 |
| Less unamortized discount | (92) | (138) |
| | $ 49,908 | $ 49,862 |

A summary, by years, of future minimum payments required to amortize the outstanding debt is as follows:

| | Principal | *(in thousands)* Interest | Total |
|---|---|---|---|
| 1994 | $ – | $ 3,937 | $ 3,937 |
| 1995 | – | 3,938 | 3,938 |
| 1996 | 50,000 | 3,938 | 53,938 |
| Total | $ 50,000 | $ 11,813 | $ 61,813 |

These notes may not be redeemed prior to maturity. Interest is payable semiannually on June 15 and December 15 of each year. The Bank of North Dakota entered into a letter of credit agreement dated December 1, 1986 with the Fuji Bank, Ltd. whereby the Fuji Bank has agreed to provide funds sufficient to pay the principal amount of the notes and up to 198 days' interest on the notes. Simultaneously with the letter of credit agreement, The Bank of North Dakota entered into a security agreement in which The Bank of North Dakota agreed to pledge eligible collateral. The notes are collateralized by government securities and FHA and VA guaranteed loans with balances of approximately $53,887,000 and $55,013,000 as of December 31, 1993 and 1992, respectively. The Bank is required to maintain an amount of eligible collateral such that the applicable value of the collateral is not less than 102.5% of the stated amount of the Fuji Bank letter of credit. The indenture of trust contains certain restrictive covenants, all of which the Bank is in compliance with as of December 31, 1993 and 1992, respectively.

Quoted market prices were used to estimate the fair value of long-term debt at $53,815,000 and $52,760,000 at December 31, 1993 and 1992, respectively. The carrying amount of accrued interest payable on long-term debt is a reasonable estimate of fair value.

NOTE 8 - **APPROPRIATIONS PAYABLE**

Appropriations have been transferred out of undivided profits to appropriations payable. The Bank has the following appropriations payable at December 31, 1993 and 1992:

| | *(in thousands)* 1993 | 1992 |
|---|---|---|
| State General Fund<br>To be transferred during the biennium beginning July 1, 1993, and ending June 30, 1995. | $ 21,632 | $ – |
| Industrial Commission<br>To be transferred during the biennium beginning July 1, 1993 and ending June 30, 1995. | 37 | – |
| PACE II Loan Fund<br>To be transferred during the period beginning February 7, 1992 and ending June 30, 1993. | – | 1,136 |
| | $ 21,669 | $ 1,136 |

The Industrial Commission is authorized during the biennium ending June 30, 1995, to transfer to the State General Fund $20,000,000 of accumulated and undivided profits, plus all earnings occurring during the biennium not to exceed $28,000,000. No transfers may be made which would reduce the Bank's capital structure below $100,000,000.

Appropriations payable is of a short-term nature. Its carrying amount is a reasonable estimate of fair value.



NOTE 9 - **DEFINED BENEFIT PLAN**

All eligible employees of The Bank of North Dakota participate in the North Dakota Public Employees Retirement System ("System"), a state-wide, cost-sharing multiple-employer public employee retirement system. The payroll for Bank employees covered by the System for the years ended December 31, 1993 and 1992 was approximately $3,902,000 and $3,869,000, respectively. The Bank's total payroll was approximately $4,034,000 and $3,979,000, respectively.

All employees of the Bank are eligible to participate in the System if they meet the following requirements: (1) Be at least 18 years old; (2) Position must be full-time, that is at least 20 hours per week for at least five months per year; and (3) Position must be permanent, that is regularly funded and not of limited duration. Employees are entitled to unreduced pension benefits beginning when the sum of age and years of credited service equal or exceed 90 (88 effective August 1, 1993), or at normal retirement age (65), equal to 1.69% (1.725% effective August 1, 1993) of their final average annual salary for each year of service. Benefits fully vest at age 65 or on reaching five years of service. The System permits early retirement at ages 55-64, with five or more years of service. The System also provides death and disability benefits. Benefits are established by State statute.

State statute requires that 4% of each participating employees' gross wage be contributed to the plan by either the employee or by the employer under a "salary reduction" agreement.

The same statute requires the Bank to contribute 4.12% of the employees wages. Administrative expenses and prior service costs are funded through the employer contributions. The contribution requirement for the years ended December 31, 1993 and 1992 was approximately $317,000 and $314,000, respectively.

The pension benefit obligation, which is the actuarial present value of credited projected benefits, is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and any step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure is intended to help users assess the System's funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems and employers. The System does not make separate measurements of assets and pension benefit obligations for individual employers. The pension benefit obligation at June 30, 1993 and 1992, for the System as a whole, was $413.2 million and $367.4 million, respectively. The System's net assets available for benefits (valued at market) on June 30, 1993 were $528 million and on June 30, 1992 were $454 million, leaving an over funded pension benefit obligation of $114.8 million and $86.5 million, respectively. The Bank's contribution represents approximately 1% of total contributions required of all participating entities.

Historical trend information showing the System's progress in accumulating sufficient assets to pay benefits when due, current measurements of the pension benefit obligation, and net assets available for benefits are presented in the System's June 30, 1993 and 1992 audited financial statements.

## NOTE 10 - POST-RETIREMENT BENEFITS

In addition to providing pension benefits, the state allows all PERS retirees to participate in the State Group Health Plan after retirement. The Bank's contribution requirement for the years ended December 31, 1993 and 1992, was approximately $39,000 each year.

## NOTE 11 - COMMITMENTS AND CONTINGENT LIABILITIES

**State of North Dakota long-term bonds**

The State of North Dakota, through the North Dakota Real Estate Trust (Trust), issued long-term bonds in 1982, 1984 and 1986, of which the proceeds were used to provide funds to The Bank of North Dakota. In connection with these bond issues, The Bank of North Dakota is obligated to purchase bonds and uncertificated obligations when there is insufficient cash flow in the Trust for payment of the bonds and interest as they become due. It is probable that The Bank of North Dakota will be required to make further purchases of these bonds and uncertificated obligations. An estimate of the amount cannot be made because of the inability to predict cash flows in the Trust. The Bank of North Dakota holds bonds and uncertificated obligations with a carrying value of $3,295,000 at December 31, 1993. In 1992, The Bank of North Dakota relinquished its rights to collect $1,500,000 in bonds and uncertificated obligations from the North Dakota Real Estate Trust.

**Myron G. Nelson Fund, Incorporated**

On August 5, 1992, the Industrial Commission authorized and directed the Bank to subscribe for and purchase up to $1,200,000 of common stock of Myron G. Nelson Fund, Incorporated. The purchase of shares of common stock of the Fund will be made on a matching basis for all "private capital" invested in the Fund. For each dollar of private capital invested, the Bank shall invest an equal amount through the purchase of shares.

## NOTE 12 - RELATED PARTY TRANSACTIONS

The Bank, because of its unique relationship with the State of North Dakota, is a party in many business transactions with other entities of state government. All state funds, and funds of all state penal, education, and industrial institutions must be deposited in the Bank under State law. These transactions are a normal part of bank business and, accordingly, are included in the Bank's financial statements.

NOTE 13 - **FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK**

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business. These financial instruments include commitments to extend credit, financial standby letters of credit, put and call agreements, and a guarantee agreement. Those instruments involve varying degrees of credit and interest rate risk in excess of the amount recognized in the balance sheet. The contract amounts of those instruments reflect the extent of involvement the Bank has in particular classes of off-balance-sheet financial instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit, financial standby letters of credit, and the guarantee agreement is represented by the contractual amount of those instruments. The Bank uses
the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. For the put and call agreements the actual risk of loss is less than the contract amount.

| | Contract Amount *(in thousands)* | |
|---|---|---|
| | 1993 | 1992 |
| Financial standby letters of credit | $ 24,381 | $ 25,647 |
| Commitments to extend credit | 63,285 | 29,647 |
| Put and call agreements | 890 | 890 |
| Guarantee agreement | 3,330 | 3,515 |
| | $ 91,886 | $ 59,699 |

Commitments to extend credit are agreements to lend as long as there is not violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained by the Bank upon extension of credit is based on management's credit evaluation of the customer. Collateral held may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties. Funding expectations for commercial and agricultural loan commitments vary. The fair value of these loans is not expected to have a material impact on the financial position of the Bank.

Financial standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The likelihood of funding any of these letters of credit is considered to be remote. The fair value calculation is, therefore, limited to the cash flows associated with fee revenues over the life of the individual instruments. At December 31, 1993 and 1992, the fair value of those fee revenues is estimated to be $1,154,000 and $1,235,000, respectively.

The put and call agreement are contracts which allow the purchaser to exercise an option to sell the securities at a specified price back to the Bank upon specific circumstances and the Bank has a call option to purchase the securities from the customer at a specified future date at a specified price. Risk arises from the possible movements in the value of the securities. The Bank considers the likelihood of its having to fund this agreement to be remote. The fair value of the agreement is considered to be immaterial.

*NOTE 13 - (continued)*

The guaranty agreement unconditionally guarantees that The Bank of North Dakota will make payments due for principal and interest owing on revenue bonds issued by a state agency. This guaranty expires upon the earlier to occur of (a) payment in full of all principal and interest due or to become due on the bonds or (b) the close of business on September 1, 1994. The Bank considers the likelihood of its having to fund this agreement to be remote. The fair value of the agreement is considered to be immaterial.

NOTE 14 - **SIGNIFICANT CONCENTRATIONS OF CREDIT RISK**

Most of the Bank's business is with customers within the state of North Dakota. Concentrations of credit are present in the agricultural industry. Due to the pervasive nature of agriculture in the economy of the state, all loans, regardless of type, are impacted by agriculture. Loans for agricultural purposes comprised approximately 27% and 20% of the total loans at December 31, 1993 and 1992, respectively.

NOTE 15 - **EXTRAORDINARY ITEM**

The State of North Dakota, through the North Dakota Real Estate Trust, issued long-term bonds in 1982, 1984, and 1986, of which the proceeds were used to provide funds to The Bank of North Dakota. In connection with these bond issues, The Bank of North Dakota is obligated to purchase bonds and uncertificated obligations when the trust has insufficient cash flow to pay the bonds and interest as they become due. During 1992 The Bank of North Dakota relinquished its rights to collect on $1,500,000 of bonds and uncertificated obligations from the North Dakota Real Estate Trust.



*The Executive Committee, the Advisory Board, and the Industrial Commission thank all of the employees for their fine performance. In appreciation, this annual report is dedicated to them.* *Page 1, left to right:* Debbie Reisenauer, Erna Jacobchick, Pat Magstadt, Dale Eberle, Denise Skeldum, Audree Whitmire, JoAnn Kiefer, Delores James, Glen Materi; *top to bottom:* Janis Reinowski, Mary Brandt, Pam Wagner, Tracy Zinke, Lynda Doll; *page 2:* Trudi Hogue, Melissa Banyai, Becky Hedberg, Lynette Hoffer, Maggie Spitzer, Joel Jundt, Beth Fricke, Ed Hovrud, JoAnn Marsh, Alyce Starck, Bob Gruman, Dennis Quivey; *page 3:* Stan Benson, Barbara Hoover, Tim Atkinson, Bob Humann, Linda Sitz, Mitch Auer, John Kramer, Dave Huhncke; *page 4:* Gayle Ciavarella, Sue Naumann, Janet Schwab, LaDonna Leingang, Leila Bender, Dorothy Schmitz, Leslie Schmit, Deanne Gifford, Chris Hoepfner, Randy Meissner; *page 6:* Julie Flemmer, Nancy Glass, Agnes Schirado, Loretta Riehl, Gayle Heinle, Patty Fillion, Sandy Karna, Wanda Thesing, Char Feist, Marlene Rohr, Tina Schumacher, *page 7;* Eric Hardmeyer, Al Nosbusch, Ray Zimmermann, Tim Porter, Julie Hart, Holly Schirado; *page 10, top row:* Shar Zacher, Sandy Jacobson, Donna Frey, Duane Wagner, Tom Redmann, Joyce Welder, Paula Hayward, Shirley Glass; *bottom row:* Lisa Steinolfson, Linda Rosen, Laura Miller, Helen Moch, Diane Roise, Leslie Moszer, Paul Govig, Cindy Lund, Clair Sorge, Michele Giese, Sue Davy, Mary Sundby; *page 15:* Wally Erhardt, Al Weisbeck, Sharon Hoffmann, Tam Becker, Annette Curl, Lucy Christensen, Ed Sather, Carol Perry, Roberta Mueller, Teri Riedinger, Marla Belohlavek, Kim Holden; *page 17:* Jason Coffel, Sue Mathern, Mike Fettig, Debby Barth, Evelyn Zelmer, Rod Storhaug, Dan Ruff, Cammy Lynch, Kathy Schnellbach, David Plum, Dave Osborn; *page 18, top row:* Rhonda Kambeitz, Danae Garrett, Karen Eisenbeis, Cindy Renner, Audre Goll, Rose Espeland, Terry Noelber, Ron Lyons, Elaine Gatzke, Kristy Leier; *bottom row:* Janel Bosch, Holly Nelson, Donna Groth, Cathy Jo Mindt, Deb Theisen, Kim Miller, Barry Fife, Cecilia Wanner, Darlene Nilson, Clara Dockter; *page 19:* Lori Hausauer, Jackie Nelson, Crystal Hilt, Esther Focke, Marilou Voegele, Karen Keller, Frances Vetter, Jeff Berger, Mary Frohlich, Leon Gross; *page 20:* Phyllis Lasher, Donna Roll, Kathy Knudson, Sharon Kuntz, Loretta Duma, Donna Johnson, Sue Seminary, Dan Fisher, Julie Kubisiak, Diane Walter; *page 23, top row:* Karen Strom, Becky Bosworth, Tammy Krein, Dave Falkenstein, Tammy Grabowska, Lynelle Kaseman, Betty Renz, Shelly Brown, Betty Becker, Melinda Schirado, Pam Weisenburger; *bottom row:* Karen Schadler, Dorena Blumhagen, Lois Gad, Jodi Fuchs, Evelyn Jochim, Claudine Galt, Alissa Mack, Ardean Masseth, Carl Arndt, Rod Anheluk; *page 24:* Laurie Pfliger, Lori Gabriel, Kurt Schirado, Rhonda Vetter, Marcy Ehli, Darlene Felchle, Karen Iverson, Jayden Pascua, Diane Gatzke, Shirley Wagner, Yvonne Olsrud.