



**NORTH DAKOTA STRONG**

**BANK OF NORTH DAKOTA 2008 ANNUAL REPORT**



**SERVING ND. SUPPORTING ND. MOVING ND.**

“Great thoughts speak only to  
the thoughtful mind, but great  
actions speak to all mankind.”

» Theodore Roosevelt

**BND**   
Bank of North Dakota

# President's Message



The beginning of 2008 started with great expectations; we moved into a new state-of-the-art facility and we were fresh off of our fifth straight year of record profits, but a few gathering clouds quickly appeared on the horizon.

The challenges that impacted much of the country's financial sector throughout the year had minimal effect on Bank of North Dakota (BND). Our earnings remained strong at \$57 million, our sixth straight year of record profits. Loan activity, quality and variety remained very good. In fact, loan growth for 2008 was a remarkable \$613 million, for a 30.6 percent increase.

As challenges mounted throughout the year, we reviewed internal procedures and best practices. We found that our straightforward approach to banking is something in which we can take pride. The instruments we use to hedge our balance sheet and manage interest rate risk are tried and true. Consequently, our exposure to the volatile derivative markets that has caused much upheaval and uncertainty in the marketplace was not a factor for us.

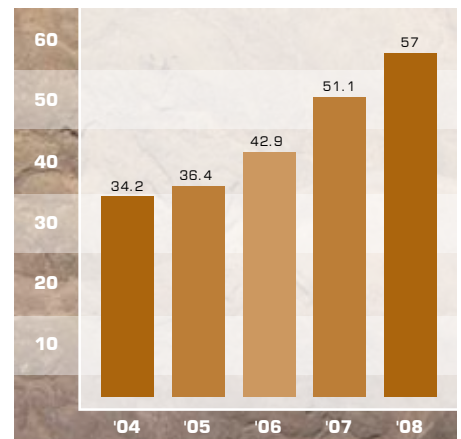
In many respects, 2008 provided more opportunities for BND to expand services than we have had in many years. As the financial crisis exploded across the country, North Dakota began to feel the effects as bank regulators called on financial institutions to increase their reserves and liquidity. Many North Dakota banks looked to BND for reassurance and used our programs including Letter of Credit for Public Deposits, loan sales, and bank stock to assist them with these issues.

The student loan industry experienced upheaval as action by the federal government eroded profit margins and the securities market for secondary loan providers dried up. Significant volume increases, attributed to 25 percent of student loan lenders leaving the industry, have not stopped earnings from falling dramatically in the student loan portfolio. Regardless, we remain deeply committed to ensuring that North Dakota students have access to financing.

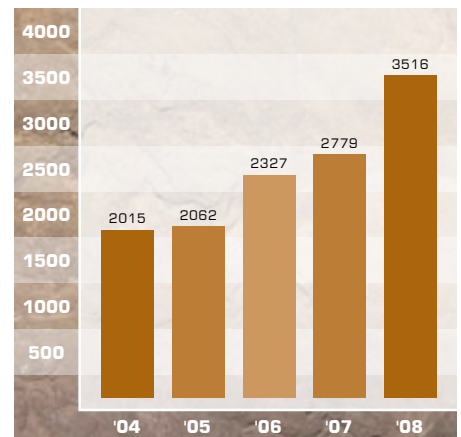
We understand 2009 will bring many more challenges to the banking industry. With this in mind, we began the process of creating a new strategic plan that will be implemented in 2009 and will take us through 2012. Our capital position and strong performing loan portfolio has positioned us as a stabilizing factor in North Dakota. We will weather this financial storm and strengthen our partnerships to ensure that we continue to meet our mission.

Eric Hardmeyer, President

**ANNUAL INCOME** (in millions)



**BND ASSETS** (in millions)







# Sinner Bros. & Bresnahan

## Meeting Global Demand for Food Grade Products

A diverse enterprise rooted in tradition and commitment to quality destined Sinner Bros. & Bresnahan (SB&B) for success. What began in 1918 as a family farm in North Dakota's Red River Valley is now a producer, processor and supplier of food grade products to customers around the world. Without assistance from American Federal Bank and BND's Business Loan Participation Program, meeting demand around the world would be difficult.

Now in its fourth generation, the family-owned, large-scale agribusiness provides consumers with traceable, pure and safe food products. In 1997, SB&B established SB&B Foods, Inc. to manage the marketing, sale and shipment of identity preserved, non-genetically modified and organic products. The company completed its final step toward vertical integration in 2004, when it constructed and opened Identity Ag Processing, LLC., a state-of-the-art processing facility.

### SB&B's spirit of entrepreneurship is exemplified in their receipt of the '09 Marketplace North Dakota Entrepreneur of the Year Award.

Todd Sinner, partner at SB&B said, "American Federal Bank and Bank of North Dakota have been supportive and accommodating to the needs of our company as we've grown. It is reassuring to know that in this difficult financial environment, both American Federal Bank and Bank of North Dakota are managed with sound principles and are there when we need them."

For the past 10 years, American Federal Bank of Fargo has provided SB&B and its companies with funding for the products they need to grow the business. As American Federal Bank needed more loan capacity for SB&B Foods, Inc., it looked to Bank of North Dakota to assist in providing operating funds to support the daily needs of the company.



*"It is reassuring to know that in this difficult financial environment, both American Federal Bank and the Bank of North Dakota are managed with sound principles and are there when we need them."*

"The participation loan program helps SB&B Foods to be successful in exporting agricultural products all over the world," said George Sinner, senior vice president of ag business banking at American Federal Bank. For SB&B, financial providers were instrumental for expanding services both domestically and internationally.

The five owners of Sinner Bros. & Bresnahan are grateful to their dedicated, loyal employees and committed regional producers who work each day with a passion for bringing economic value to the state of North Dakota and to the upper Midwest. This spirit of entrepreneurship was recognized when SB&B received the 2009 Marketplace North Dakota Entrepreneur of the Year Award, an award Todd Sinner says was "very humbling to accept and would not have been possible without the hard work and dedication of our employees."

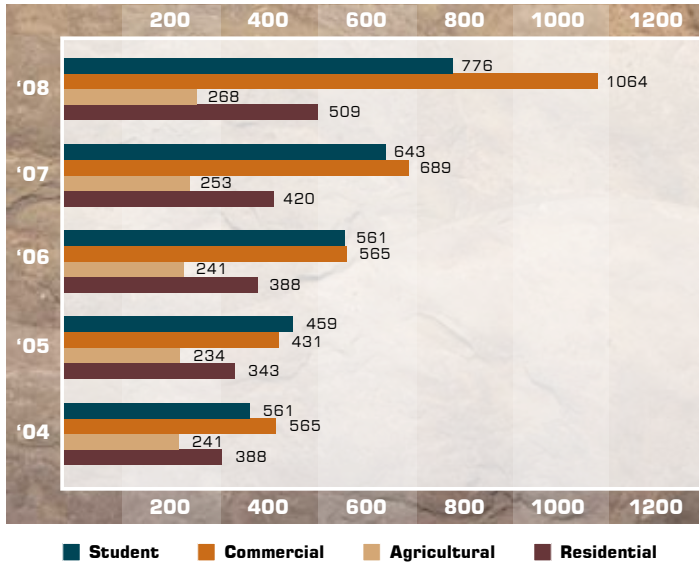
## SUCCESS STORY » SB&B • Casselton, ND



# BND: North Dakota Strong

BND moved into its new home on the shores of the Missouri River in January 2008, ending an 89-year-stay at the corner of 7th and Main in Bismarck. With an efficient use of space and the latest in technology, BND employees found themselves playing host to countless business and professional meetings including legislative gatherings, regional bank meetings and the North Dakota Banker's Association reception.

**LOAN PORTFOLIO** (balances in millions)



Dramatic growth is the underlying component of BND's 2008 loan portfolio. With a \$613 million gain, or 31 percent over 2007, the loan portfolio has doubled from \$1.3 billion to \$2.6 billion in the past five years. The portfolio's impact is felt in the furthest corners of our great state, with increases coming among four diverse loan sectors: agriculture, commercial, residential and student loans.

Despite the beginning of a nationwide economic downturn in 2008, North Dakota bucked the trend with an expanding

**Overall, the residential loan portfolio grew 21 percent to \$509 million**

economy, low unemployment and a growing energy sector. Economic development stayed at the forefront of our mission to

foster and promote agriculture, commerce and industry through a partnership approach with financial institutions and North Dakota's rural population. This is evident in our commercial loan portfolio which reached a milestone with \$1.064 billion, an increase of 54 percent. BND increased participation in business and industrial projects statewide by 66 percent, bringing the total to 328 funded projects.

As the result of an active real estate market in North Dakota, BND realized significant growth in its residential loan portfolio. Acting as a secondary market for financial institutions seeking to sell mortgages, BND booked \$148 million in new residential loans resulting in net loan growth of \$89 million. Overall, the residential loan portfolio grew 21 percent to \$509 million.

In an increasingly competitive student loan environment, many nationwide lenders chose to do business with only a select number of North Dakota's colleges in 2008. Out-of-state lenders also looked to decrease their student loan portfolios which increased demand for BND's services. Through wise business decisions and strategic purchases of loan portfolios, competitive fixed and variable interest rate options and the continued elimination of fees for North Dakota residents, the student loan portfolio grew 20 percent to \$776 million - the seventh consecutive year of growth.

January



Partnership with North Dakota Dollars for Scholars began.



BND moved to its new location.

February

BND, North Dakota University System and the ND Dept. of Corrections and Rehabilitation launched an education initiative for NDDOCR employees.

March



BND held its Grand Opening event on March 7.





# Do All Metal Fabricating

## Acquisition Results in Complete Customization

A desire to **do all** types of customized metal fabrication, large and small, shaped Kordel Korf's idea for Do All Metal Fabricating. Founded in Estevan, Saskatchewan in 2000, the company set out to meet the need for custom fabrication in the oil, gas, agricultural and mining industries. With Bank of North Dakota's Business Loan Participation Program and assistance from United Community Bank in Minot, Do All Metal Fabricating acquired a well-established machine and hydraulic shop in Glenburn, North Dakota.

Expanding operations into the United States enabled Do All Metal Fabricating to become truly capable of doing it all. The mechanical capacity inherited from the Glenburn facility complements their manufacturing expertise, and the company is now able to market and sell complete drilling rigs.

**Do All Metal Fabricating is serving a real need by providing equipment to oil and gas companies throughout the United States and Canada.**

United Community Bank in conjunction with BND's Business Loan Participation Program created funding for 60 percent of Do All Metal Fabricating's Glenburn acquisition. Ken Anderson, senior vice president of United Community Bank said, "All of the staff at BND are very responsive and great to work with. Without their experienced help, we may not have been able to provide Do All with the funding needed to expand."

"United Community Bank understands small business," Kordel reflected. "I think it's great that smaller banks can rely on Bank of North Dakota to assume some of the risk with larger loans."

What began as a one-man fabricating shop in Canada now employs 40 individuals in Glenburn and 65 employees in Estevan, most of whom are welders and machinists. Do All Metal Fabricating is serving a real need by providing equipment to oil and gas companies throughout the United States and Canada.



**“** I think it's great that smaller banks can rely on Bank of North Dakota to assume some of the risk with larger loans. ”

Kelsey Holt, vice president of United Community Bank said, "We are proud to be associated with this growing and vibrant company and look forward to a long relationship with Do All Metal Fabricating."

**SUCCESS STORY » Do All Metal Fabricating • Glenburn, ND**



BND's agriculture loan portfolio grew 6 percent to \$268 million. BND originated 448 farm loans totaling \$190 million in two direct and eight participation loan programs such as Beginning Farmer Real Estate, Farm Operating and Livestock Loan Guarantee.

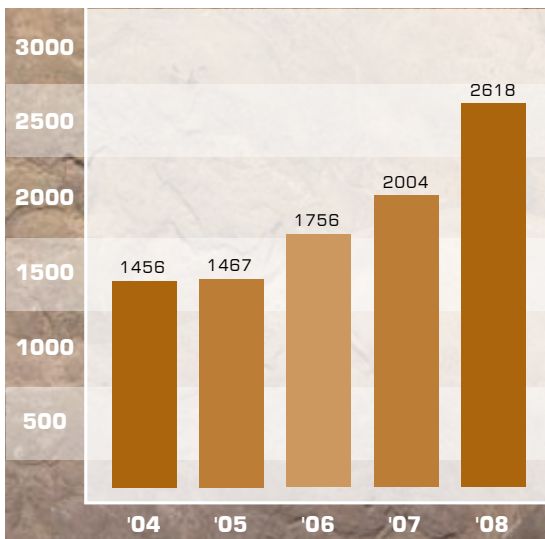
BND's overall loan portfolio remains diverse and reliably provides consistent earnings for the Bank. Commercial/business loans account for 40 percent, student loans 30 percent, residential 19 percent and agricultural loans 10 percent of the overall portfolio.

Consistent earnings coming from well-managed loan portfolios have allowed BND to contribute \$340 million to the general fund over the past 12 years (\$60 million during the 2007-2009 biennium), which makes BND the 6th largest revenue generator for the state general fund.

## Service Areas Have Strong Year

BND's service areas work with state agencies, financial institutions and many statewide organizations to successfully implement programs that have a resounding impact on our state's residents. Dedicated employees serve on committees, partake in grassroots efforts or fill administrative requirements to support organizations. The insight gained contributes to BND's professional service and willingness to adopt new technology that impacts our state from border to border.

### TOTAL LOAN PORTFOLIO (in millions)



### Treasury Services Provides Liquidity to ND Financial Institutions

Treasury Services had over \$1.8 billion of securities in safekeeping for North Dakota financial institutions at the end of 2008. The service area provided Secured and Unsecured Federal Fund Lines to 98 financial institutions with combined lines of over \$362 million which provides liquidity for increased loan demand. Sales averaged over \$49 million per day, exceeding \$110 million per day in August. The Letter of Credit for Public Deposits program provided an average of over \$197 million in additional liquidity daily. This results in the availability of additional securities in order to increase financial institutions' funding sources. Both programs provided a daily average of over \$246 million of liquidity to North Dakota financial institutions, topping out at over \$307 million in August.

**April**  
BND hosted its first Southwest Regional Meeting in the new building.

**May**



BND held its first 529 College Savings Day in the state with zoo events in Bismarck and Minot.

**June**



BND hosted the opening reception for the NDBA/SDBA Annual Convention.

JoAnn Marsh received the BND Leadership Award.

**July**

BND Image Exchange processing reached nearly 80% of all monthly item volume.





# Dwight Schilling

## A Modern Facility Increases Efficiency

The Schilling family began feeding cattle at their Venturia farm in 1984, operating with just 30 feeder cattle.

When Dwight Schilling took over the family farm, he had a vision to expand and modernize the facility. That vision became reality with help from Strasburg State Bank and Bank of North Dakota's Biofuels PACE (Partnership in Assisting Community Expansion) Program. Today he runs an operation with 3,200 head of cattle.

Just five years ago, Dwight began taking precautions to minimize runoff from the feedlot facility, thus reducing pollution of the farm's surrounding waters. Working closely with the Natural Resources Conservation Service (NRCS) of the United States Department of Agriculture, the farm received a portion of funding it needed to update the facility and comply with environmental requirements.

**The physical size of the farm's feedlot has expanded to support the larger number of cattle, which is a major income generator for Dwight's farming operation.**

The Biofuels PACE Program provided Dwight with funding to complete updates to his feedlot. The program buys down the interest rate on loans to livestock operations that agree to feed distiller grains from a biofuels facility. With Biofuels PACE, the state of North Dakota pays 5% of the loan's interest costs, not to exceed \$250,000 of total buy down costs.

"With fluctuating interest rates, farmers like me could never do something like this without having this type of program," said Dwight Schilling.

"Without Strasburg State Bank and Bank of North Dakota, we wouldn't be able to operate the feedlot size that we do."

The physical size of the farm's feedlot has expanded to support the larger number of cattle, which is a major income generator for Dwight's farming



*"Without Strasburg State Bank and Bank of North Dakota, we wouldn't be able to operate the feedlot size that we do."*

operation. Complete with lagoons, concrete feed bunks and pads, runoff from the facility has been controlled and the state's waters have been preserved. Feeding time has decreased by two hours each day, saving labor costs and increasing the operational efficiency of the farm.

Todd Lang, president of Strasburg State Bank stated, "With the expansion, Dwight has more than doubled the amount of cattle he is able to feed at any given time. The entire facility is much cleaner and more efficient."

**SUCCESS STORY » Dwight Schilling • Venturia, ND**

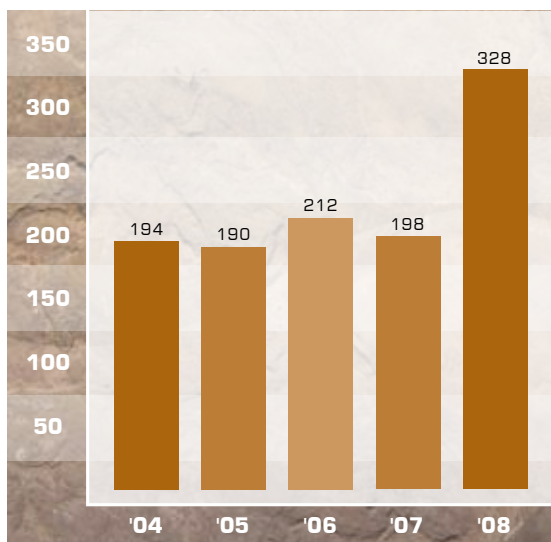




## New System Meets 21st Century Challenges

To meet the growing demand of an expanding customer base, Treasury Services converted to a new safekeeping and bond accounting system from Sungard. The new system allows customers faster access to all of their investment related information in an electronic format. Any authorized customer with Web access may securely view their information at any financial institution location. With a sophisticated set of tools and applications to help streamline back-office processes and compliance-related activities, Treasury Services is able to pass on efficiencies to these same customers.

## BUSINESS & INDUSTRIAL PROJECTS FINANCED



## Banking Services Combats Identity Theft

BND's free online account access includes safety features that help to combat identity theft. BND's new security access to online deposit account information takes every precaution so that when a customer logs on with a user code and password, an authentication image assures them they have accessed BND's Web site and no one else's.

## Electronic Processing Changes Banking

A few short years ago, all of BND's monthly item volume was processed and cleared through paper transactions. That began changing after an integrated software suite of core banking solutions was established in 2005. By the end of 2008, BND's Image Exchange product had reached high efficiency with 87 percent of all processing volume, or nearly three million monthly items, being processed electronically. With the recent implementation of Image Returns, customers may send and receive

returned items from BND in an image file. Imaging is substantially cheaper than the old paper process as 90 percent of BND's partner institutions now process items as images.

## Student Loan Services Saves Borrowers \$3.3 Million

In 2008, Student Loan Services implemented important changes based on the 2007 passage of the College Cost Reduction Access Act (CCRAA). BND no longer participates in the Federal Loan Consolidation program, however, BND continues to actively participate in the Dakota Education Alternative Loan (DEAL) Consolidation Program with loans being guaranteed by Student Loans of North Dakota. During 2008, \$6.4 million in alternative loans were consolidated by BND.

**DEAL volume on new loans increased 32 percent to \$45.5 million**

August



The original BND building was sold to IRET Properties for \$2.22 million.

The MATCH Program received a \$50 million expansion. Policy changes made to BND Loan Programs.

September



Dollars for Scholars founder speaks at NDDFS Luncheon for ND chapters.



Life 101 College Bound Family Calendars sent out.



# Ramsey National Bank & Trust Co.

## A Community Success

With help from Bank of North Dakota, a locally owned bank in Devils Lake is able to offer a competitive array of modern services.

In 1995, when the management of Ramsey National Bank & Trust Co. decided to purchase three branch locations, Bank of North Dakota provided the needed assistance with a bank stock loan to help with these transactions. Throughout the years, Ramsey has used many of the services offered through BND.

When President Scott Thompson saw other ways for Ramsey National Bank & Trust Co. to grow and expand its services to its customers, he knew he would have a willing partner in Bank of North Dakota.

"We utilize Bank of North Dakota for many purposes," stated Thompson. "BND assists us in farm lending, small business lending, and the farm real estate program, helping us extend our lending limit."

**Ramsey National Bank & Trust Co. is**

- **able to provide more money in loans to its customers, as well as enhance some of the business functions.**

With BND's assistance, Ramsey National Bank & Trust Co. is able to provide more money in loans to its customers, as well as enhance some of the business functions. Enhanced services include federal funds line, electronic image exchange, wire transfers, safekeeping service and electronic check clearing. "Having these services locally allows Ramsey National Bank & Trust Co. to provide better customer

service," said Linda Rosen in Banking Services at BND. "The easier we can make it for the bank, the easier it is for them to provide quality customer service."

Recently, Bank of North Dakota provided an additional bank stock loan, allowing the Employee Stock Ownership Plan (ESOP) to gain majority ownership. Tom



**“** BND assists us in farm lending, small business lending, and the real estate farm program, helping us extend our lending limit. **”**

Redmann in Lending Services at BND explained, "It allowed the employees to gain controlling interest in the company, which allowed the bank to continue to be community-owned."

Ramsey National Bank & Trust Co. has been providing financial services since 1892 and has always been important to the Devils Lake community where it was first established. Besides two locations in Devils Lake, they also have branches in Fargo, Cando, Cavalier, Rugby, Maddock and Esmond.

"These are exciting times at Ramsey and we look forward to the many opportunities this creates for our employees, the bank and our customers," said Thompson.

The banking partnership between Ramsey National Bank & Trust Co. and BND is a strong bond, and both look forward to working together for years to come.

## SUCCESS STORY » Ramsey NB&T • Devils Lake, ND





While many other lenders have discontinued their borrower benefit programs, BND continues to pay federal origination and default fees associated with Stafford Loans for all students attending school in North Dakota. In accordance with previous commitments, BND continues to pay the two percent administrative fee on DEAL loans for all North Dakota residents attending school across the United States. BND saved student loan borrowers \$3.3 million in 2008. In addition, BND paid \$4.4 million in fees to the U.S. Department of Education.

BND remains competitive in the student loan marketplace by offering some of the lowest fixed or variable alternative loan interest rates in the nation while working to keep defaults on existing DEAL loans at less than 1 percent. DEAL volume on new loans also increased 32 percent to \$45.5 million.

## BND Commits to Education and Students



### New Pledge Keeps Bridges Guidance Central in Schools

Providing a means for residents to continue their education remains an important component of our mission at BND. That mission goes further than only providing student loans. In 2008, Bank of North Dakota, Student Loans of North Dakota and College SAVE supported a new three-year commitment with Xap Corporation and Bridges Transitions to provide career exploration, education planning and ACT test preparation tools through Bridges Guidance Central. This is the second consecutive, three-year commitment of over \$600,000 BND has made to all North Dakota public and private middle schools and high schools. This pledge also serves as the soft match for the North Dakota Access Challenge Grant administered by the North Dakota University System.

### BND Takes on NDDFS Administrative Functions

BND broke new ground in 2008 by becoming the first state agency in the nation to partner with North Dakota Dollars for Scholars (NDDFS) and its parent organization Scholarship America. NDDFS was established in 1962, is affiliated with 80 statewide chapters and has distributed nearly \$17 million to more than 13,000 North Dakota students. To celebrate NDDFS volunteers around the state, BND and NDDFS hosted a celebratory luncheon. The inspirational Dr. Irving Fradkin, 87-year-old founder who started the organization with \$1 from Eleanor Roosevelt in 1958, delivered the keynote address. In addition to program administration, BND gave \$20,000 in matching scholarship funds to NDDFS in 2008.

**BND saved student loan borrowers \$3.3 million and paid \$4.4 million in fees to the U.S. Department of Education in 2008**



2008-09 leadership group forms

October

November



Demolition of original building began November 19

December

Senator Dorgan visited BND.



Student Loans of North Dakota unveiled its new logo.



# Kelly & Patrick Hall

## Farming Their Land with the Right Equipment

Growing up on a farm in Munich, North Dakota, taught Kelly Hall and his brother Patrick the value of having the right tools and land for running a successful farm operation. When the two brothers became primary owners of their family farm in 2004, they turned to First State Bank of Munich and Bank of North Dakota to support the purchase of necessary equipment and real estate.

BND worked alongside First State Bank of Munich to provide a Beginning Farmer Chattel Loan to the Halls, allowing them to invest in farm equipment under favorable terms. Soon after, the Halls used two Beginning Farmer Real Estate loans from BND to acquire land they had previously rented. The Beginning Farmer Loan Programs were established to assist farmers with first-time purchases of farm real estate, equipment and livestock. Qualified applicants are eligible for \$250,000 in loan assistance from each program.

**For Kelly and Patrick, maintaining a successful farm operation is the result of a combination of two things - the right equipment and assets.**

“The Beginning Farmer Loan Programs have allowed me to start and expand my farming operation with my brother,” said Kelly Hall. “We continue to work land that has been in our family over 50 years. Having the ability to purchase land when we started out has led to our success.”

Kelly also looked to the banks for assistance in funding a local project that aims to sustain and cultivate economic

activity in the community with a goal to start operations in 2009. A few years ago, Kelly became one of six individuals to invest in a canola crushing plant that produces food grade oil, with the hope of enhancing job opportunities for the community of Munich. Called Northern Prairie Specialty Oils, the project is partially funded by BND’s Ag PACE (Partnership in Assisting Community Expansion) Program in participation with First State Bank of Munich. BND’s Ag PACE Program provides interest buydown on loans to farmers investing in nontraditional activities that supplement farm income.



“The Beginning Farmer Loan Programs have allowed me to start and expand my farming operation with my brother. Having the ability to purchase land when we started out has led to our success.”

Bryan Anderson, senior vice president of First State Bank of Munich said, “The loan programs at BND offer competitive terms that work well for young farmers who are just beginning their careers, enabling them to maintain financially stable operations. The Ag PACE program is a very good program for any borrower looking to invest in North Dakota projects.”

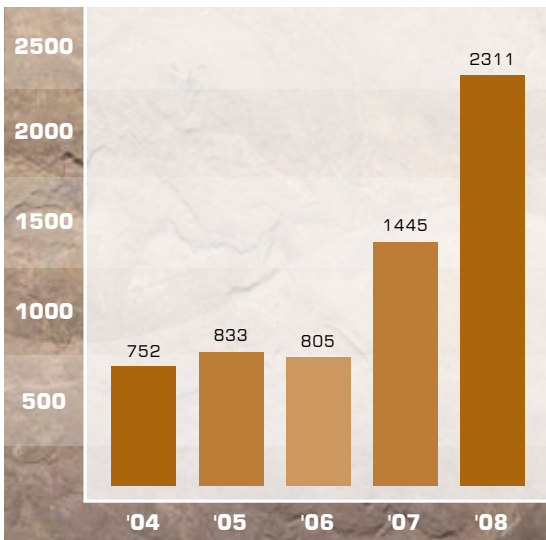
For Kelly and Patrick, maintaining a successful farm operation is the result of a combination of two things - the right equipment and assets, both made possible with the loan programs of BND and First State Bank of Munich.

**SUCCESS STORY » Kelly & Patrick Hall • Munich, ND**





## COLLEGE SAVE ND ACCTS



### College SAVE Raises In-State Profile

BND administered College SAVE has quickly become the college saving tool of choice in North Dakota. Recently enhanced features include a matching grant program, yearly state tax deduction on new contributions and federal and state tax free growth on earnings. College SAVE is being promoted across the state through affiliations with Dakota Wizards basketball, Bismarck Bobcats hockey, University of North Dakota Fighting Sioux hockey, Fargo Red Hawks baseball and Fargo Force hockey. In conjunction with grassroots efforts at the North Dakota State Fair and at Bismarck and Minot zoos on 529 College Savings Day, these marketing initiatives grew North Dakota resident participation 60 percent in 2008. Nationwide assets in 18,193 accounts totaled \$262 million.

## North Dakota Strong: Serving, Supporting, Moving ND

Year after year, BND demonstrates its strong commitment to North Dakota's economic well-being through effective participation across a range of programs and services including our popular agricultural, commercial, residential and student loan programs.

We will continue to push for economic development and competitive interest rates while assisting our financial partners with their liquidity plans. This unwavering commitment to **serve** the best interests of the state, **support** its residents and **move** North Dakota down a path to economic success is evident in our nearly 90 years of operating as the only state-owned bank in the nation. We continue to carry out our lasting mission:

***To Deliver Quality, Sound Financial Services that Promote Agriculture, Commerce and Industry in North Dakota.***

**BND**   
Bank of North Dakota



# SERVING ND. SUPPORTING ND. MOVING ND.

## ND Industrial Commission



**John Hoeven**  
Governor



**Roger Johnson**  
Agriculture Commissioner



**Wayne Stenehjem**  
Attorney General

## BND Advisory Board



Standing: Pat Mahar, Frank Larson, Karl Bollingberg  
Seated: Gary Petersen, Elaine Fremling, Pat Clement,  
John Stewart

## BND Executive Committee



L to R: Bob Humann, Kirby Martz, Julie Kubisiak,  
Eric Hardmeyer, Ed Sather, Lori Leingang, Dale Eberle





# FINANCIAL STATEMENTS

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INDEPENDENT AUDITOR’S REPORT..... PAGE 1

BALANCE SHEETS..... PAGE 2

STATEMENTS OF INCOME ..... PAGE 3

STATEMENTS OF EQUITY ..... PAGE 4

STATEMENTS OF CASH FLOWS..... PAGE 5

NOTES TO FINANCIAL STATEMENTS

    NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES ..... PAGES 6-9

    NOTE 2 - RESTRICTION ON CASH AND DUE FROM BANKS ..... PAGE 9

    NOTE 3 - DEBT AND EQUITY SECURITIES ..... PAGES 10-12

    NOTE 4 - LOANS..... PAGES 12-13

    NOTE 5 - LOAN SALES AND LOAN SERVICING ..... PAGE 13-14

    NOTE 6 - BANK PREMISES, EQUIPMENT, AND SOFTWARE..... PAGE 15

    NOTE 7 - DEPOSITS..... PAGE 16

    NOTE 8 - REPURCHASE AGREEMENTS..... PAGE 16

    NOTE 9 - SHORT AND LONG-TERM DEBT ..... PAGES 16-17

    NOTE 10 - OTHER LIABILITIES ..... PAGE 17-18

    NOTE 11 - PENSION PLAN ..... PAGE 18

    NOTE 12 - COMMITMENTS AND CONTINGENT LIABILITIES ..... PAGES 19-20

    NOTE 13 - RELATED PARTY TRANSACTIONS..... PAGE 21

    NOTE 14 - OFF-BALANCE-SHEET ACTIVITIES ..... PAGES 21

    NOTE 15 - FAIR VALUE OF FINANCIAL INSTRUMENTS ..... PAGES 22-25

    NOTE 16 - COMPREHENSIVE INCOME ..... PAGE 26

    NOTE 17 - SUPPLEMENTAL DISCLOSURES RELATED TO STATEMENTS OF CASH FLOWS ..... PAGE 26

TEN YEAR SUMMARY..... PAGES 27-28

# INDEPENDENT AUDITOR'S REPORT

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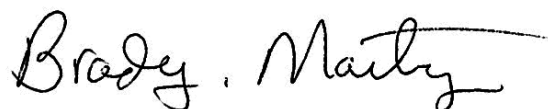
The Industrial Commission  
State of North Dakota  
Bismarck, North Dakota

We have audited the accompanying balance sheets of the Bank of North Dakota as of December 31, 2008 and 2007, and the related statements of income, equity, 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 audit.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits 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.

As described in Note 1, the Bank of North Dakota is included as part of the primary government in the State of North Dakota's reporting entity. However, the Bank of North Dakota has prepared the accompanying financial statements in accordance with Financial Accounting Standards Board pronouncements, which is accounting principles generally accepted in the United States of America for financial institutions. This basis of accounting is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America applicable to governmental units.

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, 2008 and 2007, and the results of its operations and its cash flows for the years then ended on the basis of accounting described in Note 1.



BRADY, MARTZ & ASSOCIATES, P.C.  
February 5th, 2009



**BANK OF NORTH DAKOTA**  
**BALANCE SHEETS**  
**DECEMBER 31, 2008 AND 2007**

	(In Thousands)	
	2008	2007
<b>ASSETS</b>		
Cash and due from banks	\$ 477,048	\$ 245,092
Federal funds sold	75,675	277,565
Cash and cash equivalents	552,723	522,657
Securities	331,416	235,551
Loans	2,618,402	2,004,999
Less allowance for loan losses	(36,750)	(32,863)
	2,581,652	1,972,136
Interest receivable	35,260	34,196
Bank premises, equipment, and software, net	13,581	12,328
Other assets	2,333	2,492
Total assets	\$ 3,516,965	\$ 2,779,360
<b>LIABILITIES AND EQUITY</b>		
Deposits		
Non-interest bearing	\$ 313,900	\$ 317,949
Interest bearing	2,331,456	1,553,818
	2,645,356	1,871,767
Federal funds purchased and repurchase agreements	304,020	434,061
Short and long-term debt	315,604	245,070
Other liabilities	28,063	35,991
Total liabilities	3,293,043	2,586,889
Equity		
Capital	2,000	2,000
Capital surplus	42,000	42,000
Undivided profits	182,883	145,843
Accumulated other comprehensive income (loss)	(2,961)	2,628
Total equity	223,922	192,471
Total liabilities and equity	\$ 3,516,965	\$ 2,779,360

**BANK OF NORTH DAKOTA**  
**STATEMENTS OF INCOME**  
**YEARS ENDED DECEMBER 31, 2008 AND 2007**

	(In Thousands)	
	2008	2007
INTEREST INCOME		
Federal funds sold	\$ 7,046	\$ 12,690
Securities	12,427	11,472
Loans, including fees	129,140	128,254
Total interest income	<u>148,613</u>	<u>152,416</u>
INTEREST EXPENSE		
Deposits	48,139	56,931
Federal funds purchased and repurchase agreements	9,190	15,114
Short and long-term debt	14,472	15,045
Total interest expense	<u>71,801</u>	<u>87,090</u>
NET INTEREST INCOME	76,812	65,326
PROVISION FOR LOAN LOSSES	8,900	3,100
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	<u>67,912</u>	<u>62,226</u>
NONINTEREST INCOME		
Service fees and other	7,475	6,765
Gain (loss) on available-for-sale securities	142	(92)
Total noninterest income	<u>7,617</u>	<u>6,673</u>
NONINTEREST EXPENSE		
Salaries and benefits	9,595	9,035
Data processing	3,375	3,445
Occupancy and equipment	1,194	754
Other operating expenses	4,321	4,579
Total noninterest expenses	<u>18,485</u>	<u>17,813</u>
NET INCOME	<u>\$ 57,044</u>	<u>\$ 51,086</u>



**BANK OF NORTH DAKOTA**  
**STATEMENTS OF EQUITY**  
**YEARS ENDED DECEMBER 31, 2007 AND 2006**

	(In Thousands)				
	Capital	Capital Surplus	Undivided Profits	Accumulated Other Comprehensive Income (Loss)	Total
BALANCE, DECEMBER 31, 2006	\$ 2,000	\$ 42,000	\$ 119,894	\$ (352)	\$ 163,542
Comprehensive income					
Net income			51,086		51,086
Unrealized gain on securities available for sale				2,980	2,980
Total comprehensive income					54,066
Transfer to state general fund			(25,045)		(25,045)
Transfer to Industrial Commission			(92)		(92)
BALANCE, DECEMBER 31, 2007	\$ 2,000	\$ 42,000	\$ 145,843	\$ 2,628	\$ 192,471
Comprehensive income					
Net income			57,044		57,044
Unrealized loss on securities available for sale				(5,589)	(5,589)
Total comprehensive income					51,455
Transfers to state general fund			(20,004)		(20,004)
BALANCE, DECEMBER 31, 2008	\$ 2,000	\$ 42,000	\$ 182,883	\$ (2,961)	\$ 223,922

**BANK OF NORTH DAKOTA**  
**STATEMENTS OF CASH FLOWS**  
**YEARS ENDED DECEMBER 31, 2008 AND 2007**

	(In Thousands)	
	2008	2007
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 57,044	\$ 51,086
Adjustments to reconcile net income to net cash from operating activities		
Depreciation and amortization	983	820
Provision for loan losses	8,900	3,100
Net amortization (accretion) of securities	(136)	(188)
(Gain)/loss on sale of securities	(142)	92
Gain on sale of residential loans	(1)	(20)
Gain on retirement of premises and equipment	(627)	-
(Gain)/loss on sale of foreclosed assets	28	(17)
Increase in interest receivable	(1,064)	(3,997)
Decrease in other assets	2	423
Increase in other liabilities	2,114	1,239
<b>NET CASH FROM OPERATING ACTIVITIES</b>	<b>67,101</b>	<b>52,538</b>
<b>INVESTING ACTIVITIES</b>		
Securities available for sale transactions		
Purchase of securities	(222,517)	(81,817)
Proceeds from sales, maturities, and principal repayments	125,493	68,620
Purchase of Federal Home Loan Bank stock	(8,625)	(3,605)
Sale of Federal Home Loan Bank stock	4,945	4,289
Purchase of other equity securities	(1,522)	(550)
Sale of other equity securities	1,050	-
Proceeds from sales of loans	35	2,049
Net increase in loans	(618,450)	(252,169)
Purchases of premises and equipment	(3,731)	(6,790)
Proceeds from sale of premises and equipment	2,122	-
Proceeds from sale of foreclosed assets	129	633
<b>NET CASH USED FOR INVESTING ACTIVITIES</b>	<b>(721,071)</b>	<b>(269,340)</b>
<b>FINANCING ACTIVITIES</b>		
Net increase/(decrease) in non-interest bearing deposits	(4,049)	86,956
Net increase in interest bearing deposits	777,638	167,675
Net increase/(decrease) in federal funds purchased and repurchase agreements	(130,041)	184,916
Proceeds from issuance of short and long-term debt	360,200	275,528
Payment of short and long-term debt	(289,666)	(287,667)
Payment of transfers	(30,046)	(30,046)
<b>NET CASH FROM FINANCING ACTIVITIES</b>	<b>684,036</b>	<b>397,362</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>30,066</b>	<b>180,560</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<b>522,657</b>	<b>342,097</b>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<b>\$ 552,723</b>	<b>\$ 522,657</b>



**BANK OF NORTH DAKOTA**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2008 AND 2007**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Nature of Operations*

Bank of North Dakota (BND) 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. BND is a unique institution combining elements of banking, fiduciary, investment management services, and other financial services, and state government with a primary role in financing economic development. BND is a participation lender; the vast majority of its loans are made in tandem with financial institutions throughout the State of North Dakota. BND's primary deposit products are interest-bearing accounts for state and political subdivisions.

Bank of North Dakota is included as part of the primary government in the State of North Dakota's reporting entity. As such, BND is required to follow the pronouncements of the Government Accounting Standards Board (GASB), which is the nationally accepted standard setting body for establishing generally accepted accounting principles for governmental entities. In accordance with GASB Statement No. 20, BND follows all applicable GASB pronouncements and all applicable Financial Accounting Standards Board (FASB) pronouncements issued, including those issued after November 30, 1989, unless they conflict with the GASB pronouncements.

However, the accompanying financial statements are prepared in accordance with Financial Accounting Standards Board pronouncements, which are generally accepted accounting principles for financial institutions. This basis of accounting is a comprehensive basis of accounting other than generally accepted accounting principles applicable to governmental units.

BND also prepares financial statements in accordance with GASB pronouncements.

*Use of Estimates*

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the balance sheet and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses.

*Significant Group Concentrations of Credit Risk*

Most of the Bank's lending activities are with customers within the State of North Dakota. Due to the pervasive nature of agriculture in the economy of the state, all loans, regardless of type, are impacted by agriculture. The Bank's loan portfolio is comprised of the following concentrations as of December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
Student loans, of which 98% are guaranteed	<b>30%</b>	32%
Commercial loans, of which 4% and 6% are federally guaranteed	<b>41%</b>	34%
Residential loans, of which 81% and 80% are federally guaranteed	<b>19%</b>	21%
Agricultural loans, of which 10% and 14% are federally guaranteed	<b>10%</b>	13%
	<u><b>100%</b></u>	<u>100%</u>

## NOTES TO FINANCIAL STATEMENTS

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### *Cash and Cash Equivalents*

For purposes of the statements of cash flows, cash and cash equivalents include cash and balances due from banks and federal funds sold, all with original maturities of three months or less.

### *Securities*

Securities that may be sold before maturity in response to changes in interest rates or prepayment risk, or due to liquidity needs or changes in funding sources or terms are classified as available for sale. These securities are recorded at fair value, with unrealized gains and losses, reported in equity. The change in unrealized gains and losses are excluded from earnings and reported in other comprehensive income. Securities that management has the positive intent and ability to hold to maturity are classified as held to maturity and recorded at amortized cost.

Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Declines in the fair value of securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issue for a period of time sufficient to allow for any anticipated recovery in fair value. Gains and losses on the sale of securities are recorded on the settlement date and are determined using the specific identification method.

In order to borrow from the Federal Home Loan Bank (FHLB), the Bank is required to hold FHLB stock. The amount of stock that the Bank must hold is equal to .12% of total bank assets plus 4.45% of total FHLB advances. Since ownership of this stock is restricted, these securities are carried at cost and evaluated periodically for impairment.

Nonmarketable equity securities represent venture capital equity securities that are not publicly traded. The Bank reviews these assets at least annually for possible other-than-temporary impairment. These securities do not have a readily determinable fair value and are stated at cost. The Bank reduces the asset value when it considers declines in value to be other than temporary. We recognize the estimated loss as a loss from equity securities in noninterest income.

### *Loans Held For Sale*

Mortgage loans held for sale are generally sold with the mortgage servicing rights retained by the Bank. The carrying value of the mortgage loans sold is reduced by the cost allocated to the associated mortgage servicing rights. Loans held for sale are carried at the lower of aggregate cost or market value. Gains or losses on sale of mortgage loans are recognized based on the difference between the selling price and the carrying value of the related mortgage loans sold.

### *Loans*

Loans are reported at the outstanding unpaid principal balances, adjusted for charge-offs, unamortized deferred fees and costs on originated loans and premiums or discounts on purchased loans. Interest income on loans is accrued at the specific rate on the unpaid principal balance. Unearned income, deferred fees and costs, and discounts and premiums are amortized to income over the estimated life of the loan using the interest or straight line method.

The accrual of interest is discontinued when, in management's opinion, the borrower may be unable to meet payments as they become due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on non-accrual or charged-off at an earlier date if collection of principal or interest is considered doubtful.



## NOTES TO FINANCIAL STATEMENTS

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When interest accrual is discontinued, all unpaid accrued interest is reversed against interest income. Future payments are generally applied against principal until the loan balance is at zero. Any further payments are then recorded as interest income on the cash basis. Loans can be returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

### *Allowance for Loan Losses*

The Bank uses the allowance method in providing for loan losses. Accordingly, the allowance is increased by the current year's provision for loan losses charged to operations and reduced by net charge-offs. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The adequacy of the allowance for loan losses and the provision 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. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and amount of the shortfall in relation to the principal and interest owed.

Impairment is measured on a loan-by-loan basis for commercial, agricultural, farm real estate, state institution and bank stock loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual guaranteed student and residential loans for impairment disclosures, except for such loans that are placed on nonaccrual.

### *Transfers of Financial Assets*

Transfers of financial assets are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Bank, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

## NOTES TO FINANCIAL STATEMENTS

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### *Bank Premises, Equipment, and Software*

Bank premises, equipment, hardware 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.

### *Foreclosed Assets*

Foreclosed assets, which are included in other assets, represent assets acquired through loan foreclosure or other proceedings. Foreclosed assets are recorded at the lower of the amount of the loan or fair market value of the assets. Any write-down to fair market value at the time of the transfer to foreclosed assets is charged to the allowance for loan losses. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and change in the valuation allowance are included in other operating expenses. Foreclosed assets totaled \$173,000 and \$330,000 as of December 31, 2008 and 2007, respectively.

### *Defined Benefit Plan*

The Bank funds amounts equal to pension costs accrued.

### *Income Taxes*

Bank of North Dakota is a governmental agency of the State of North Dakota and, as such, is not subject to federal or state income taxes.

### *Financial Statement Presentation*

Certain amounts in the 2007 financial statements have been reclassified to conform to the 2008 presentation.

## **NOTE 2 - RESTRICTION ON CASH AND DUE FROM BANKS**

Federal Reserve Board regulations require the Bank to maintain reserve balances with the Federal Reserve Bank. The average reserve balances maintained at the Federal Reserve Bank were approximately \$7,000,000 in 2008 and \$4,400,000 in 2007.



## NOTES TO FINANCIAL STATEMENTS

### NOTE 3 - DEBT AND EQUITY SECURITIES

Debt and equity securities have been classified in the financial statements according to management's intent. The carrying value of securities as of December 31, 2008 and 2007 consists of the following:

	(In Thousands)	
	<u>2008</u>	<u>2007</u>
Securities available for sale, at fair value	\$ 310,760	\$ 219,047
Federal Home Loan Bank stock, at cost	17,385	13,705
Other equity securities, at cost	3,271	2,799
	<u>\$ 331,416</u>	<u>\$ 235,551</u>

The amortized cost and fair value of securities with gross unrealized gains and losses follows:  
(In Thousands)

	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<b>DECEMBER 31, 2008</b>				
Securities available for sale				
Federal agency	\$ 166,881	\$ 4,047	-	\$ 170,928
Mortgage-backed	134,972	2,454	9,462	127,964
State and municipal	11,868	-	-	11,868
	<u>\$ 313,721</u>	<u>\$ 6,501</u>	<u>\$ 9,462</u>	<u>\$ 310,760</u>

	(In Thousands)			
	<u>Amortized Cost</u>	<u>Gross Unrealized Gains</u>	<u>Gross Unrealized Losses</u>	<u>Fair Value</u>
<b>DECEMBER 31, 2007</b>				
Securities available for sale				
Federal agency	\$ 87,547	\$ 2,290	\$ -	\$ 89,837
Mortgage-backed	113,405	793	455	113,743
State and municipal	15,467	-	-	15,467
	<u>\$ 216,419</u>	<u>\$ 3,083</u>	<u>\$ 455</u>	<u>\$ 219,047</u>

## NOTES TO FINANCIAL STATEMENTS

Securities carried at \$3,527,000 and \$101,285,000 at December 31, 2008 and 2007, respectively were used to secure repurchase agreements and for other required pledging purposes. FHLB stock totaling \$17,385,000 and \$13,704,500 at December 31, 2008 and 2007, respectively are pledged on the FHLB advances (Note 9).

The maturity distribution of debt securities at December 31, 2008, is shown below. The distribution of mortgage-backed securities is based on average expected maturities. Actual maturities may differ because issuers may have the right to call or prepay obligations.

	(In Thousands)	
	Available for Sale	
	Amortized Cost	Fair Value
Within one year	\$ 100,279	\$ 100,275
Over one year through five years	139,263	144,469
Over five years through ten years	22,552	17,414
Over ten years	51,627	48,602
	<u>\$ 313,721</u>	<u>\$ 310,760</u>

For the year ended December 31, 2008, proceeds from the sale of securities available for sale were \$5,835,000. Gross realized gains were \$216,000 and gross realized losses were \$75,000. For the year ended December 31, 2007, proceeds from the sale of securities available for sale were \$26,089,000. Gross realized gains were \$62,000 and gross realized losses were \$154,000.

Information pertaining to securities with gross unrealized losses at December 31, 2008, aggregated by investment category and length of time that individual securities have been in a continuous loss position, follows:

	(In Thousands)			
	Less Than Twelve Months		Over Twelve Months	
	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value
Securities available for sale				
Mortgage-backed	\$ 2,540	\$ 16,895	\$ 6,922	\$ 9,848

Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

## NOTES TO FINANCIAL STATEMENTS

At December 31, 2008, four privatized collateralized mortgage obligation securities have unrealized losses with aggregate depreciation of 36% from the amortized cost basis. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and industry analysts' reports. As management has the ability to hold these securities for the foreseeable future, the decline is not deemed to be other than temporary.

At December 31, 2007, there were no securities with aggregate depreciation of 5% from the Bank's amortized cost basis.

### NOTE 4 - LOANS

The composition of the loan portfolio at December 31, 2008 and 2007 is as follows:

	(In Thousands)	
	2008	2007
Student	\$ 776,473	\$ 643,297
Commercial	1,064,811	689,150
Residential	509,052	419,700
Agricultural	268,066	252,852
	<u>2,618,402</u>	<u>2,004,999</u>
Allowance for loan losses	36,750	32,863
	<u>\$ 2,581,652</u>	<u>\$ 1,972,136</u>

Unamortized deferred student loan costs totaled \$9,247,000 and \$6,689,000 as of December 31, 2008 and 2007, respectively. Net unamortized loan premiums and discounts, including purchased servicing rights, on residential loans totaled \$1,983,000 and \$2,004,000 as of December 31, 2008 and 2007, respectively.

The composition of the allowance for loan losses for the years ended December 31, 2008 and 2007 is as follows:

	(In Thousands)	
	2008	2007
Balance - beginning of year	\$ 32,863	\$ 30,136
Provision for loan losses	8,900	3,100
Loans charged off	(5,328)	(440)
Recoveries	315	67
Balance - end of year	<u>\$ 36,750</u>	<u>\$ 32,863</u>



## NOTES TO FINANCIAL STATEMENTS

The following is a summary of information pertaining to impaired, non-accrual and restructured loans:

	(In Thousands)	
	December 31,	
	2008	2007
Impaired loans with a valuation allowance	\$ <b>3,365</b>	\$ 2,614
Valuation allowance related to impaired loans	\$ <b>886</b>	\$ 854
Average investment in impaired loans	<b>8,310</b>	1,463
Total non-accrual loans	<b>3,365</b>	2,614
Total loans past-due ninety days or more and still accruing	<b>25,620</b>	27,909
Restructured loans	<b>10,407</b>	10,888

The interest income recorded on impaired loans is not significant.

Accruing loans 90 days or more past due include guaranteed student loans of \$23,489,000 and \$19,552,000 as of December 31, 2008 and 2007, respectively. The Bank is entitled to reimbursement from the guarantor 270 days after default in the case of a student loan payable in monthly installments and 330 days in the case of a student loan payable in less frequent installments.

There were no material commitments to lend additional funds to customers whose loans were classified as impaired or restructured at December 31, 2008 and 2007.

### NOTE 5 - LOAN SALES AND LOAN SERVICING

A summary of BND loan sales during 2008 and 2007 follows:

	(In Thousands)	
	2008	2007
Commercial loans participated	\$ <b>20,000</b>	\$ -
Residential loans sold on the secondary market	<b>34</b>	2,029

BND recognized gains on sale of loans of \$1,000 and \$20,000 in 2008 and 2007, respectively, which is included in non-interest income on the Statements of Income.

## NOTES TO FINANCIAL STATEMENTS

BND has contracts to provide servicing of loans for others. These loans are not included in the accompanying balance sheets. The unpaid principal balances of loans serviced for others as of December 31, 2008 and 2007 were as follows:

	(In Thousands)	
	<u>2008</u>	<u>2007</u>
Student loans		
North Dakota Student Loan Trust	\$ 59,920	\$ 83,927
Others	4,367	3,543
Residential loans		
Fannie Mae	18,063	21,969
Other state fund loans		
Board of University and School Lands	56,599	30,614
Community Water Facility Loan Fund	16,422	15,921
Beginning Farmer Revolving Loan Fund	8,461	8,647
Developmentally Disabled Facility Loan Program	1,153	1,544
Department of Human Services	9,110	9,520
Workforce Safety	18	15
	<u>\$ 174,113</u>	<u>\$ 175,700</u>

Under existing student loan servicing agreements, the Bank generally agrees to reimburse lenders for all principal, accrued interest and special allowance which the lender has been denied if the denial resulted from the actions or inactions of the Bank. Under the existing residential loan servicing agreement with Fannie Mae, the Bank will indemnify Fannie Mae and hold them harmless against all losses, damages, judgments or legal expenses that result from the Bank's failure in any way to perform its services and duties.

## NOTES TO FINANCIAL STATEMENTS

### NOTE 6 - BANK PREMISES, EQUIPMENT, AND SOFTWARE

A summary of changes in bank premises, equipment, furniture, and software at December 31, 2008 and 2007 is as follows:

	(In Thousands)			Balance 2008
	Balance 2007	Additions	Retirements	
Land	\$ 1,843	\$ -	\$ 672	\$ 1,171
Building	4,285	10,212	4,285	10,212
Equipment	790	301	106	985
Furniture	511	662	494	679
Hardware	925	389	26	1,288
Software	6,026	425	259	6,192
Construction in progress	8,258	1,954	10,212	-
	<u>22,638</u>	<u>13,943</u>	<u>16,054</u>	<u>20,527</u>
Less accumulated depreciation	<u>10,310</u>	<u>983</u>	<u>4,347</u>	<u>6,946</u>
	<u>\$ 12,328</u>	<u>\$ 12,960</u>	<u>\$ 11,707</u>	<u>\$ 13,581</u>

	(In Thousands)			Balance 2007
	Balance 2006	Additions	Retirements	
Land	\$ 1,843	\$ -	\$ -	\$ 1,843
Building	4,285	-	-	4,285
Equipment	737	160	107	790
Furniture	536	-	25	511
Hardware	1,039	37	151	925
Software	6,000	26	-	6,026
Construction in progress	1,691	6,567	-	8,258
	<u>16,131</u>	<u>6,790</u>	<u>283</u>	<u>22,638</u>
Less accumulated depreciation	<u>9,773</u>	<u>820</u>	<u>283</u>	<u>10,310</u>
	<u>\$ 6,358</u>	<u>\$ 5,970</u>	<u>\$ -</u>	<u>\$ 12,328</u>

Depreciation and amortization expense on the above assets amounted to \$983,000 and \$820,000 in 2008 and 2007.

The 2005 North Dakota Legislature Senate Bill 2014 provided for the construction of a new building for the Bank. In November 2005, the Bank entered into a Purchase Agreement to purchase land for the new building site. The building construction project began in the fall of 2006 and was completed in 2008. Bank personnel began occupying/utilizing the new facility in the middle of January 2008. Total costs associated with the new facility included land on which the new bank facility is constructed costing \$1,171,000. Land acquired that is not occupied by the new facility totals \$761,000 and is included in other assets. Building construction cost totaled \$10,212,000. The old bank facility was sold in 2008 at a net sales price of \$2,123,000. A gain on the sale of the old facility of \$649,000 is included in noninterest income in 2008.



## NOTES TO FINANCIAL STATEMENTS

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### NOTE 7 - DEPOSITS

The aggregate amount of locally sold certificates of deposit larger than \$100,000 was \$1,755,057,000 and \$1,116,376,000 as of December 31, 2008 and 2007, respectively.

At December 31, 2007, the scheduled maturities of certificates of deposits are as follows:

	<u>(In Thousands)</u>
One year or less	\$ 1,489,943
One to three years	147,309
Over three years	<u>141,805</u>
	<u>\$ 1,779,057</u>

### NOTE 8 - REPURCHASE AGREEMENTS

The Bank enters into agreements to repurchase the same securities that it previously sold. These agreements may have a fixed maturity or be open-ended, callable at any time. These agreements are secured by Fed book-entry securities. The aggregate amount of repurchase agreements was \$3,075,000 and \$100,630,000 as of December 31, 2008 and 2007, respectively.

### NOTE 9 - SHORT AND LONG-TERM DEBT

Short and long-term debt consists of:

	<u>(In Thousands)</u>	
	<u>2008</u>	<u>2007</u>
Federal Home Loan Bank advances - long-term	\$ 314,600	\$ 244,100
ND Public Finance Authority, 3%, matures from September 2009 through September 2017	<u>1,004</u>	<u>970</u>
	<u>\$ 315,604</u>	<u>\$ 245,070</u>

## NOTES TO FINANCIAL STATEMENTS

A summary, by years, of future minimum payments required to amortize the outstanding short and long-term debt is as follows:

	(In Thousands)		
	Principal	Interest	Total
2009	\$ 5,137	\$ 15,168	\$ 20,305
2010	122	15,022	15,144
2011	33,122	14,261	47,383
2012	122	13,086	13,208
2013	62,122	11,517	73,639
Later years	214,979	45,234	260,213
Totals	<u>\$ 315,604</u>	<u>\$ 114,288</u>	<u>\$ 429,892</u>

The FHLB long-term advances outstanding at December 31, 2008, mature from June 2009 through April 2022. The FHLB long-term advances have fixed rate interest, ranging from 3.27% to 7.35%. The advances must be secured by minimum qualifying collateral maintenance levels. Residential loans with carrying values of \$481,729,000 and \$402,539,000 at December 31, 2008 and 2007, respectively, are currently being used as security to meet these minimum levels.

The money borrowed from the ND Public Finance Authority is unsecured and is used to fund irrigation and livestock waste program loans.

### NOTE 10 - OTHER LIABILITIES

Other liabilities consist of:

	(In Thousands)	
	2008	2007
Transfers payable	\$ 15,000	\$ 25,042
Interest payable	9,190	7,316
Salary and benefits payable	911	865
Student loan related payables	544	619
Accounts payable, accrued expenses and other liabilities	2,418	2,149
	<u>\$ 28,063</u>	<u>\$ 35,991</u>

## NOTES TO FINANCIAL STATEMENTS

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The Sixtieth North Dakota Legislature passed House Bill 1014 which provides for transfers during the biennium beginning July 1, 2007 and ending June 30, 2009 totaling \$60,000,000 from the current earnings and the accumulated undivided profits of the Bank. The moneys must be transferred in the amounts and at the times requested by the director of the Office of Management and Budget. The Bank transferred \$30,000,000 to the State's General Fund in 2008.

Any transfer authorized by the sixtieth legislative assembly may only be made to the extent the transfer does not reduce the Bank's capital structure below \$175,000,000.

### **NOTE 11 - PENSION PLAN**

Bank of North Dakota participates in the North Dakota Public Employees' Retirement System (NDPERS) administered by the State of North Dakota. Following is a brief description of the plan.

NDPERS is a cost-sharing multiple-employer defined benefit pension plan covering substantially all classified employees of Bank of North Dakota. The plan provides retirement, disability, and death benefits. If an active employee dies with less than three years of credited service, a death benefit equal to the value of the employee's accumulated contributions, plus interest, is paid to the employee's beneficiary. If the employee has earned more than three years of credited service, the surviving spouse will be entitled to a single payment refund, lifetime monthly payments in an amount equal to 50% of the employee's accrued normal retirement benefit, 60 monthly payments equal to the employee's accrued normal retirement benefit calculated as if the employee were age 65 the day before death occurred, or monthly payments in an amount equal to the employee's accrued 100% joint and survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the employee's accumulated pension benefits are paid, the balance will be payable to the surviving spouse's designated beneficiary.

Eligible employees who become totally disabled after a minimum of 180 days of service receive monthly disability benefits that are equal to 25% of their final average salary with a minimum benefit of \$100. To qualify under this section, the employee must meet the criteria established by the Retirement Board for being considered totally disabled.

Employees are entitled to unreduced monthly pension benefits equal to 2.0% of their final average salary for each year of service beginning when the sum of age and years of credited service equal or exceed 85, or at normal retirement age (65). The plan permits early retirement at ages 55-64, with five or more years of service.

Benefit and contribution provisions are administered in accordance with chapter 54-52 of the North Dakota Century Code. This state statute requires that 4% of the participant's salary be contributed to the plan by either the employee or by the employer under a "salary reduction" agreement. Bank of North Dakota has implemented a salary reduction agreement and is currently contributing the employees share. Bank of North Dakota is required to contribute 4.12% of each participant's salary as the employer's share. In addition to the 4.12% employer contribution, the employer is required to contribute 1% of each participating employee's gross wage to a prefunded retiree health insurance program. The required contributions are determined using an entry age normal actuarial funding method. The North Dakota Retirement Board was created by the State Legislature and is the governing authority of NDPERS. Bank of North Dakota's required and actual contributions to NDPERS for the fiscal years ending December 31, 2008 and 2007 were approximately \$617,000 and \$591,000, respectively.

NDPERS issues a publicly available financial report that includes financial statements and the required supplementary information for NDPERS. That report may be obtained by writing to NDPERS; 400 East Broadway, Suite 505; PO Box 1657; Bismarck, ND 58502-1657.

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 12 - COMMITMENTS AND CONTINGENT LIABILITIES

*Legislative Action-* Various legislative bills provide state agencies the authority to borrow money from the Bank of North Dakota during the biennium beginning July 1, 2007 and ending June 30, 2009 and in one case provide a source of payment of principal and interest payable on bonds issued. Following is a summary of legislative action and/or North Dakota Statute in effect:

H.B. 1018, Section 15 - The Office of Management and Budget (OMB) may borrow an amount not to exceed \$5,000,000 for the purpose of providing funding to centers of excellence as directed by the centers of excellence commission. OMB shall request funding from the legislative assembly to repay any loan obtained pursuant to this bill.

H.B. 1018, Section 18 – The Secretary of State may borrow up to \$2,920,000 from the Bank for the purpose of implementing the North Dakota business development engine information technology project. The secretary of state may request budget section approval only if the revenues projected by the secretary of state and the office of management and budget to be generated as a result of provisions of H.B. 1340 over the term of the proposed loan based on the trend of actual corporate charters granted are anticipated to exceed the revenues projected by the legislative assembly related to this bill by an amount sufficient to repay the proposed loan, including interest over the term of the loan.

H.B. 1021 – The North Dakota Information Technology Department (NDITD) may borrow the necessary funds to pay the costs associated with telecommunications costs for connecting schools and libraries. No borrowing limit was established. NDITD shall request a deficiency appropriation from the legislative assembly to repay any loan made under this bill.

H.B. 1127 – The Industrial Commission may borrow an amount not to exceed \$6,000,000 for the Lignite Research Program for a period not to exceed five years on the terms and conditions as the Bank and the Industrial Commission may approve without the necessity of establishing or maintaining any reserve fund as otherwise required by section 54-17.5-05.

S.B. 2012 – The Department of Human Services (DHS) may borrow an amount not to exceed \$3,500,000 for the purpose of providing the state matching share of additional medical assistance grants for developmental disabilities services. DHS shall request funding from the legislative assembly to repay any loan obtained under this bill, including accrued interest.

S.B. 2020 – The State Water Commission is authorized a line of credit – contingent appropriation, that states, if determined necessary by the State Water Commission, Bank of North Dakota shall extend a line of credit, not to exceed \$25,000,000, for the biennium beginning July 1, 2007, and ending June 30, 2009. If the line of credit is extended to the State Water Commission by the Bank, there is appropriated out of any moneys in the water development trust fund, the resources trust fund, bond proceeds, or other sources, the sum of \$25,000,000, or so much of the sum may be necessary, to the state water commission for the purpose of repaying the line of credit. Bank of North Dakota has not funded and has not committed to fund any amount under the line of credit.

The State Water Commission is also authorized under chapter 61-02.1-04 of North Dakota Century Code, principal and interest on bonds issued are payable from transfers to be made and appropriated by the legislative assembly from the water development trust fund as provided in section 61-02.1-05, then from transfers to be made and appropriated by the legislative assembly from revenues in the resources trust fund other than revenues from state taxes, then from appropriations of other available revenues in the then current biennium, and then from any other revenues the State Water Commission makes available during the then current biennium for that purpose, including any federal moneys received by the state for the construction of flood control or reduction projects to pay bonds issued for that project. If sufficient funds from these sources are not available, then from transfers to be made and appropriated by the legislative assembly from the first available current biennial earnings of the Bank of



## NOTES TO FINANCIAL STATEMENTS

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North Dakota not to exceed \$6,500,000 per biennium prorated with any other bonds payable from transfers to be made and appropriated by the legislative assembly from the available current biennial earnings of the Bank of North Dakota, to be credited by the trustee to the fund established for paying principal and interest on the bonds under a trust indenture. If the bank has to provide a transfer to the state water commission to make principal and interest payments on these bonds, the state water commission would then have to request from the next legislative assembly funding to repay the transfer made by the bank.

S.B. 2200 – The Department of Public Instruction may borrow the necessary funds to reimburse school districts for the excess costs of serving the one percent of special education students statewide who require the greatest school district expenditures in order to be provided with special education and related services. No borrowing limit was established. The Superintendent of public instruction shall file for introduction legislation requesting the legislative assembly to return any amount transferred under this bill.

### *Farm Real Estate Loan Guarantee Program*

Chapter 6-09.7-09 provides that the Bank of North Dakota may guarantee the loan of money by banks, credit unions, lending institutions that are part of the farm credit system, and savings and loan associations in this state to eligible persons for the purchase of agricultural real estate or the restructuring of agricultural real estate loans, provided the transactions do not exceed a loan to value ratio of 80% and further provided that no single loan exceeds \$400,000. The Bank may have no more than \$8,000,000 in outstanding loan guarantees under this program. The Bank may guarantee up to 75% of the amount of principal due the lender. The guarantee term may not exceed 5 years. As of December 31, 2008 and 2007, the Bank has guarantees outstanding totaling \$1,648,000 and \$1,970,000, respectively, and had guarantee commitments outstanding of \$169,000 and \$122,000, respectively, included in commitments to extend credit.

### *Beginning Entrepreneur Loan Guarantee Program*

Chapter 6-09.15 provides that the Bank of North Dakota provide a Beginning Entrepreneur Loan Guarantee Program. The program includes an agreement with a lender that in the event of default by a beginning entrepreneur under a note and mortgage or other loan or financing agreement, the Bank shall pay the lender the amount agreed upon up to 85 percent of the amount of principal due the lender on a loan at the time the claim is approved. The total outstanding loans that the Bank may guarantee cannot exceed \$8,000,000. With an 85% guarantee maximum, the Bank may provide guarantees not exceeding \$6,800,000. A lender may apply to the Bank for a loan guarantee for a loan of up to \$100,000. The term of the guarantee may not exceed five years. As of December 31, 2008 and 2007, the Bank has guarantees outstanding totaling \$4,555,000 and \$3,758,000, respectively, and had guarantee commitments outstanding of \$66,000 and \$237,000, respectively, included in commitments to extend credit.

### *Livestock Loan Guarantee Program*

Chapter 6-09-41 of the North Dakota Century Code provides that the Bank of North Dakota establish and administer a loan guarantee program that is designed to expand livestock feeding and dairy farming in this state. This program is effective through June 30, 2009.

The Bank may guarantee loans made by the bank, credit union, a savings and loan association, or any other lending institution in this state to the owner of a commercial livestock feeding operation or to the owner of a new or expanding dairy operation. In the event of a default, the Bank shall pay to the lender the amount agreed upon, provided that the amount may not exceed 85% of the principal due the lender at the time the claim is approved.

As of December 31, 2008 and 2007, the Bank has guarantees outstanding totaling \$789,000 and \$1,416,000, respectively, and had guarantee commitments outstanding of \$850,000 and \$789,000, respectively, included in commitments to extend credit.

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 13 - 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.

See Note 5 for disclosure relating to loans sold to other state funds and/or loans serviced for other state funds, including the North Dakota Student Loan Trust.

### NOTE 14 - OFF-BALANCE-SHEET ACTIVITIES

The Bank is a party to credit related financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and financial standby letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet. The Bank's exposure to credit loss is represented by the contractual amount of these commitments. The Bank follows the same credit policies in making commitments as it does for on-balance-sheet instruments.

At December 31, 2008 and 2007, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount (In Thousands)	
	2008	2007
Commitments to extend credit	\$ 653,632	\$ 403,065
Financial standby letters of credit	295,808	238,763

Commitments to extend credit are agreements to lend to a customer as long as there is no 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 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.

Financial standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those letters of credit 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 Bank generally holds collateral supporting those commitments if deemed necessary.

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 15 - FAIR VALUE OF FINANCIAL INSTRUMENTS

We use fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. Available for sale securities are recorded at fair value on a recurring basis.

Effective January 1, 2008, the Bank adopted Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*. FAS 157 defines fair value and establishes a consistent framework for measuring fair value under generally accepted accounting principles and expands disclosure requirements for fair value measurements.

#### *Fair Value Hierarchy*

Under FAS 157, we group our assets and liabilities at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

- Level 1 – Valuation is based upon quoted prices for identical instruments traded in active markets.
- Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.
- Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect our own estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

#### *Determination of Fair Value*

Under FAS 157, we base our fair values on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It is our policy to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements, in accordance with the fair value hierarchy of FAS 157.

The following is a description of valuation methodologies used for assets and liabilities recorded at fair value and for estimating fair value for financial instruments not recorded at fair value (FAS 107 disclosures).

#### *Cash and Cash Equivalents*

Cash and cash equivalents, include cash and due from banks, items out for collection, and federal funds sold. These assets are carried at historical cost. The carrying amounts of cash and cash equivalents approximate fair value due to the relatively short period of time between the origination of the instruments and their expected realization.

#### *Securities Available for Sale*

Securities available for sale, consist primarily of Federal agencies and mortgage backed securities. Securities available for sale are recorded at fair value on a recurring basis. Fair value is based upon quoted prices, if available. If quoted market prices are not available, fair values are measured using observable market prices from independent pricing models, or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, as well as U.S. Treasury, other U.S. government and agency mortgage-backed securities that are traded by dealers or brokers in active over-the-counter markets. Level 2 securities include privatized collateralized mortgage obligations and state and political subdivision securities. Securities classified as Level 3 are FHLB stock and equity securities that are not publicly traded and do not have a readily determinable fair value.

(continued on next page)

## NOTES TO FINANCIAL STATEMENTS

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### *Loans*

The carrying value of loans is described in note 1, “Summary of Significant Accounting Policies”. We do not record loans at fair value on a recurring basis. As such, valuation techniques discussed herein for loans are primarily for estimating fair value for FAS 107 disclosure purposes. However, from time to time, we record nonrecurring fair value adjustments to loans to reflect (1) partial write-downs that are based on the observable market price or current appraised value of the collateral, or (2) the full charge-off of the loan carrying value.

The fair value estimates for FAS 107 purposes differentiates loans based on their financial characteristics, such as product classification, loan category, pricing features and remaining maturity. Prepayment and credit loss estimates are evaluated by product and loan rate.

- The fair value of student loans is based on market values as established by the secondary market.
- For real estate 1-4 family first and junior lien mortgages, fair value is calculated by discounting contractual cash flows, adjusted for prepayment and credit loss estimates, using discount rates based on current industry pricing or our own estimate of an appropriate risk-adjusted discount rate for loans of similar size, type, remaining maturity and re-pricing characteristics.
- The fair value of all other loans is calculated by discounting contractual cash flows using discount rates that reflect our current pricing for loans with similar characteristics and remaining maturity.
- Off-Balance Sheet Credit-Related Instruments include loans commitments, standby letters of credit, and guarantees. These instruments generate ongoing fees at our current pricing levels, which are recognized over the term of the commitment period. The fair value of these instruments is estimated based upon fees charged for similar agreements. The carrying value of the deferred fees is a reasonable estimate of the fair value of the commitments.

### *Interest Receivable*

The carrying amount of interest receivable approximates fair value due to the relatively short period of time between accrual and expected realization.

### *Non-Maturity Deposits*

The fair value for deposits with no stated maturity, such as demand deposits, savings, NOW, and money market accounts, are disclosed as the amount payable upon demand.

### *Deposits with Stated Maturities*

The fair value for interest bearing certificates of deposit has been estimated by discounted future cash flows using rates currently offered for deposits of similar remaining maturities.

### *Federal Funds Purchased and Repurchase Agreements*

The carrying amount of federal funds purchased and repurchase agreements approximates fair value due to the relatively short period of time between the origination of the instruments and their expected payments.

### *Interest payable*

The carrying amount of interest payable approximates fair value due to the relatively short period of time between accrual and expected payment.



## NOTES TO FINANCIAL STATEMENTS

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### *Short and Long-Term Debt*

Current market prices were used to estimate the fair value of short and long-term debt using current market rates of similar maturity debt.

### *Other Liabilities*

The carrying amount of other liabilities approximates fair value due to the short period of time until expected payment.

### *Assets and Liabilities Recorded at Fair Value on a Recurring Basis*

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis at December 31, 2008.

	(In Thousands)			
	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Securities available for sale	<u>\$ 331,416</u>	<u>\$ 282,802</u>	<u>\$ 27,958</u>	<u>\$ 20,656</u>

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis, at December 31, 2008, are summarized as follows:

	<u>Securities available for sale</u>
Balance, beginning of year	\$ 16,503
Purchases	10,149
Sales and maturities	(6,119)
Net gain on sale	123
Balance, end of year	<u>\$ 20,656</u>

## NOTES TO FINANCIAL STATEMENTS

### FAS 107, Disclosures about Fair Value of Financial Instruments

The table below is a summary of fair value estimates as of December 31, 2008 and 2007, for financial instruments, as defined by FAS 107. The carrying amounts in the following table are recorded in the balance sheet under the indicated captions. In accordance with FAS 107, we have not included assets and liabilities that are not financial instruments in our disclosure, such as our premises and equipment and other assets. Additionally, the amounts in the table have not been updated since year end, therefore the valuations may have changed significantly since that point in time. For these reasons, the total of the fair value calculations presented does not represent, and should not be construed to represent, the underlying value of the Bank.

The carrying amounts and estimated fair values of the Bank's financial instruments as of December 31, 2008 and 2007 were as follows:

	(In Thousands)			
	2008		2007	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Financial assets</b>				
Cash and cash equivalents	\$ 552,723	\$ 552,723	\$ 522,657	\$ 522,657
Securities	331,416	331,416	235,551	235,551
Interest receivable	35,260	35,260	34,196	34,196
Loans, net	2,581,652	2,758,060	1,972,136	2,010,680
Total financial assets	<u>\$ 3,501,051</u>	<u>\$ 3,677,459</u>	<u>\$ 2,764,540</u>	<u>\$ 2,803,084</u>
<b>Financial liabilities</b>				
Non-maturity deposits	\$ 866,299	\$ 866,299	\$ 732,295	\$ 732,295
Deposits with stated maturities	1,779,057	1,809,918	1,139,472	1,147,148
Federal funds purchased and repurchase agreements	304,020	304,020	434,061	434,061
Short and long-term debt	315,604	331,231	245,070	253,429
Other liabilities	28,063	28,063	35,991	35,991
Total financial liabilities	<u>\$ 3,293,043</u>	<u>\$ 3,339,531</u>	<u>\$ 2,586,889</u>	<u>\$ 2,602,924</u>

## NOTES TO FINANCIAL STATEMENTS

### NOTE 16 - COMPREHENSIVE INCOME

The Bank recognizes and includes revenue, expenses, gains and losses in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

Changes in and determination of accumulated other comprehensive income (loss) is as follows:

	(In Thousands)	
	Unrealized Gain (Loss) on Securities Available for Sale	
	2008	2007
Balance, beginning of year	\$ 2,628	\$ (352)
Unrealized holding gains (losses) arising during the period	(5,447)	2,888
Reclassification adjustment for (gains) losses realized in net income	(142)	92
Other comprehensive income	(5,589)	2,980
Balance, end of year	\$ (2,961)	\$ 2,628

### NOTE 17 - SUPPLEMENTAL DISCLOSURES RELATED TO STATEMENTS OF CASH FLOWS

	(In Thousands)	
	2008	2007
Supplemental disclosures of cash flow information		
Cash payments for:		
Interest paid to customers	\$ 46,233	\$ 55,762
Interest paid on federal funds purchased and securities sold under repurchase agreements	9,226	15,180
Interest paid on short and long-term debt	14,468	15,044
Supplemental schedule of noncash investing and financing activities		
Transfers from undivided profits to other liabilities	20,004	25,137
Net change in unrealized gain (loss) on securities available for sale	(5,589)	2,980
Other real estate and property owned acquired in exchange for loans	-	330

**BANK OF NORTH DAKOTA**  
**TEN-YEAR SUMMARY**

TEN YEAR SUMMARY	2008	2007	2006
<b>OPERATING RESULTS (in thousands)</b>			
Interest income	\$148,613	\$152,416	\$ 126,598
Interest expense	71,801	87,090	71,284
Net interest income	76,812	65,326	55,314
Provision for loan losses	8,900	3,100	3,400
Net interest income after provision for loan losses	67,912	62,226	51,914
Noninterest income	7,617	6,673	7,748
Noninterest expense	18,485	17,813	16,808
<b>Net income</b>	<b>57,044</b>	<b>51,086</b>	<b>42,854</b>
Payments to general fund	30,000	30,000	30,000
Payments to other funds	46	46	43
<b>BALANCE SHEET - YEAR END (in thousands)</b>			
<b>TOTAL ASSETS</b>	<b>3,516,965</b>	<b>2,779,360</b>	<b>2,326,693</b>
FEDERAL FUNDS SOLD AND RESELL AGREEMENTS	75,675	277,565	129,135
SECURITIES	331,416	235,551	219,412
<b>LOANS</b>	<b>2,618,402</b>	<b>2,004,999</b>	<b>1,755,562</b>
Student	776,473	643,297	561,178
Commercial	1,064,811	689,150	564,946
Residential	509,052	419,700	388,043
Agriculture	268,066	252,852	241,395
<b>DEPOSITS</b>	<b>2,645,356</b>	<b>1,871,767</b>	<b>1,617,136</b>
Non-interest bearing	313,900	317,949	230,993
Interest bearing	2,331,456	1,553,818	1,386,143
FEDERAL FUNDS PURCHASED AND REPURCHASE AGREEMENTS	304,020	434,061	249,145
SHORT AND LONG-TERM DEBT	315,604	245,070	257,209
<b>EQUITY</b>	<b>223,922</b>	<b>192,471</b>	<b>163,542</b>
Capital	2,000	2,000	2,000
Capital surplus	42,000	42,000	42,000
Undivided profits	182,883	145,843	119,894
Accumulated other comprehensive income (loss)	(2,961)	2,628	(352)



2005	2004	2003	2002	2001	2000	1999
\$ 98,086	\$ 80,133	\$ 79,463	\$ 90,315	\$ 114,490	\$ 117,163	\$ 99,350
51,623	38,392	41,755	50,666	82,840	75,774	62,487
46,463	41,741	37,708	39,649	41,650	41,389	36,863
2,400	2,400	2,000	2,200	2,700	2,700	1,600
44,063	39,341	35,708	37,449	38,950	38,689	35,263
9,332	11,248	11,474	9,764	8,646	7,224	7,838
17,038	16,373	15,488	15,022	14,537	13,331	12,642
<b>36,357</b>	<b>34,216</b>	<b>31,694</b>	<b>32,191</b>	<b>33,059</b>	<b>32,582</b>	<b>30,459</b>
30,000	30,000	34,000	30,000	50,000	-	15,000
43	37	37	36	36	35	35
<b>2,062,247</b>	<b>2,014,525</b>	<b>1,953,178</b>	<b>1,974,448</b>	<b>2,107,456</b>	<b>1,806,517</b>	<b>1,687,167</b>
195,370	122,230	89,915	209,205	257,830	271,510	249,565
157,623	253,186	284,272	235,365	329,632	192,093	235,007
<b>1,467,061</b>	<b>1,456,256</b>	<b>1,391,583</b>	<b>1,329,985</b>	<b>1,276,334</b>	<b>1,156,614</b>	<b>1,056,232</b>
459,287	417,356	372,362	364,816	399,002	376,535	335,687
431,068	480,870	469,912	432,940	392,206	362,940	342,860
342,786	322,044	318,067	309,267	271,385	213,009	188,474
233,920	235,986	231,242	222,962	213,741	204,130	189,211
<b>1,352,516</b>	<b>1,198,586</b>	<b>1,057,386</b>	<b>1,070,853</b>	<b>1,208,601</b>	<b>1,135,731</b>	<b>910,652</b>
205,854	208,277	214,275	209,112	193,354	130,470	83,798
1,146,662	990,309	843,111	861,741	1,015,247	1,005,261	826,854
248,932	201,959	190,597	296,688	315,713	215,072	250,985
275,926	436,593	525,795	421,065	399,553	254,439	363,076
<b>161,824</b>	<b>152,776</b>	<b>153,744</b>	<b>149,113</b>	<b>170,496</b>	<b>153,045</b>	<b>139,275</b>
2,000	2,000	2,000	2,000	2,000	2,000	2,000
42,000	42,000	42,000	42,000	42,000	42,000	42,000
119,894	110,947	110,947	104,237	126,237	108,707	96,703
(2,070)	(2,171)	(1,203)	876	259	338	(1,428)



Bank *of* North Dakota

**CORE VALUES:**

**SERVICE:** Excel and Deliver

**TEAMWORK:** Together We Accomplish More

**ETHICS:** Do the Right Thing

**PEOPLE:** Set Us Apart



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