NAVIGATING TODAY ANCHOR FOR TOMORROW

Annual Report 2011

Bank of North Dakota

NAVIGATING TODAY, ANCHOR FOR TOMORROW

Annual Report 2011

BND
Bank of North Dakota

MISSION

To deliver quality, sound financial services that promote agriculture, commerce, and industry in North Dakota.

VISION

Bank of North Dakota is a financial services leader in North Dakota fostering growth and economic well-being for the state and its citizens, using a partnership approach. Bank of North Dakota has knowledgeable, well-trained people delivering exceptional customer service, resulting in consistent financial returns to the state.

CORE VALUES

SERVICE: Excel and Deliver
TEAMWORK: Together We Accomplish More
ETHICS: Do the Right Thing
PEOPLE: Set Us Apart

 Photo Credit: North Dakota Tourism/ TC Worley

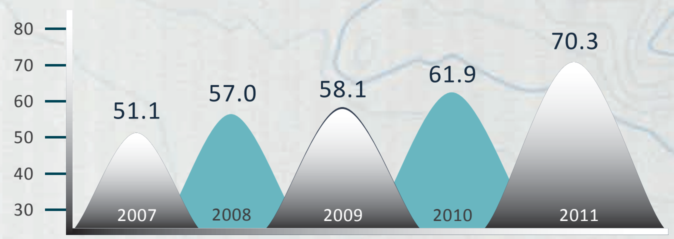
PRESIDENT'S MESSAGE

The year 2011 was extraordinary, to say the least. Oil and water, and the events they gave rise to, were forces that changed our landscape and presented challenges that required daily navigation. When extraordinary events occur, Bank of North Dakota (BND) and its resources are called upon to play a significant role.

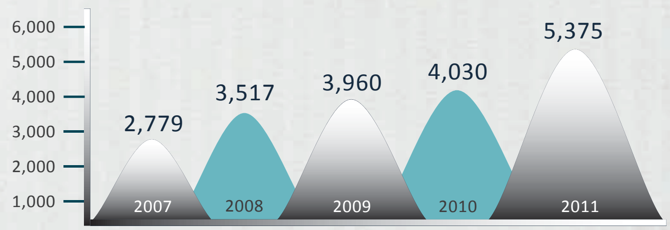
As individuals, we know that life can change quickly. However, we rarely see so many people affected simultaneously, stretching resources and testing our resolve. Ultimately, entire communities will be strengthened.

A rapidly growing oil industry helped fuel a robust economy, but also impacted the infrastructure of western and north-central North Dakota. BND responded to the needs by financing apartments, hotels, office complexes, businesses, and water systems. We also assisted state agencies like the Department of Transportation and the Department of Emergency Services with funding to improve infrastructure.

ANNUAL INCOME [IN MILLIONS]



BND ASSETS [IN MILLIONS]



Floodwater and the havoc it created was headline news. It hampered the ability of farmers to plant their fields; nearly 30 percent of the land was not farmed. Residents of nine counties fled homes because of spring and summer flooding.

BND employees were excused from work to help North Dakota communities in their valiant fight against the floods. Lending programs were designed to assist with recovery efforts: Rebuilder's Loan Program for homeowners, Business Disaster Relief Loan Program, and the Farm Disaster Relief Loan Program.

As we developed these disaster response programs, the significance of our strong relationships with local financial institutions was apparent. Their role in facilitating disaster relief loans and other BND programs for their clients has been invaluable. Our collaboration is essential to accomplishing our mission of promoting agriculture, commerce, and industry.

BND continues to be financially strong, recording its eighth consecutive year of record profits; this year's profits were over $70 million. Standard & Poors (S&P) raised BND's credit rating in December. Its long-term issuer credit rating was raised to AA- from A+ and its short-term issuer credit rating to A-1+ from A-1. This is significant when viewed in context of the ratings downgrades received by many financial institutions across the country.

Finally, we unveiled the 2012-2014 Strategic Plan. Three pillars drive our activities: Economic Development, Culture, and Finance. Imperatives were developed that will be implemented through management and staff goals to ensure completion.

The Strategic Plan remains true to BND's founding principles written in 1919. These principles serve as an anchor to provide stability for tomorrow by promoting economic growth while allowing us the flexibility to navigate today and adjust the course as needed. The future of the Bank, and North Dakota, is bright.

Eric Hardmeyer

Eric Hardmeyer

EFFERTZ OPERATION STAYS ABOVE WATER WITH HELP FROM BND

On 1,500 acres north of Bismarck lies a multi-faceted farm and ranch operation owned by Neil and Janet Effertz. The Effertz EZ Ranch is a family-run operation bordering the historic Missouri River. "We run about 200 to 250 cows depending on the year and our marketing plans," says Neil Effertz. "We sell registered breeding stock to customers all over the U.S. and abroad." The enterprise also sells frozen bovine embryos and semen collected on the ranch. Additionally, they manage a livestock sales business and several other elements complementary to the farm and ranch.

A scenic view of the Effertz EZ Ranch

The 2011 Missouri River flooding damaged a portion of the Effertz operation. "Three hundred acres of our best bottom land was under four to six feet of water from May to August," says Effertz. "The flood caused us to lose a tremendous feed source for our cattle and income to our farming operation." The Effertz's soon realized they would need more working capital to purchase hay for winter feeding and clean up the land once it dried. They contacted Brad Legreid, loan officer at American Bank Center, for assistance with a Farm Disaster Relief Loan. Legreid worked with Jim Leier at Bank of North Dakota (BND) to secure a low-interest loan for the operation. "The application and approval process was quick and efficient," said Legreid. "With BND's help, American Bank Center was able to offer Neil and Janet some relief during this difficult event."

The Farm Disaster Relief Loan provides financial relief to North Dakota farmers and ranchers impacted by the 2011 weather-related events. BND participates up to a maximum of 75 percent of the loan. "We were able to give Neil and Janet a break on interest and extend the length for repayment," said Leier. Loan proceeds are used to replace and repair equipment, improve real estate, and replenish working capital.

"We got our start farming and ranching with a BND Beginning Farmers Loan about 20 years ago. Today, with the help from the Farm Disaster Relief Loan, we were able to hang on through a very challenging summer with no crop and extensive land damage," said Effertz. "It was a positive solution to a negative situation."

The Effertz EZ Ranch borders the Missouri River.

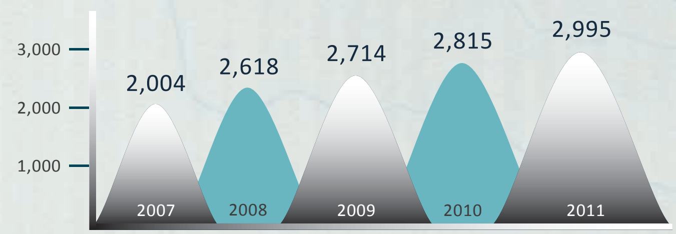
Photo Credit: North Dakota Tourism/Gerald Blank

BND: NAVIGATING TODAY, ANCHOR FOR TOMORROW

A successful day on the water requires a knowledgeable captain who makes adjustments for changes in weather and wind. Rather than working against nature, the captain monitors current conditions with the goal of providing peace of mind to the boat's passengers.

For more than 90 years, the staff of Bank of North Dakota (BND) has worked closely with government and financial institution partners to ensure a safe journey. In 2011, the Bank closely monitored global, national, and state economies while growing its diverse portfolio of agriculture, commercial, residential, and student loans. The entire loan portfolio grew steadily at 6.4 percent over 2010 to a record $3 billion. At the end of 2011, BND was a $5.37 billion institution with capital of nearly $400 million.

TOTAL LOAN PORTFOLIO [IN MILLIONS]

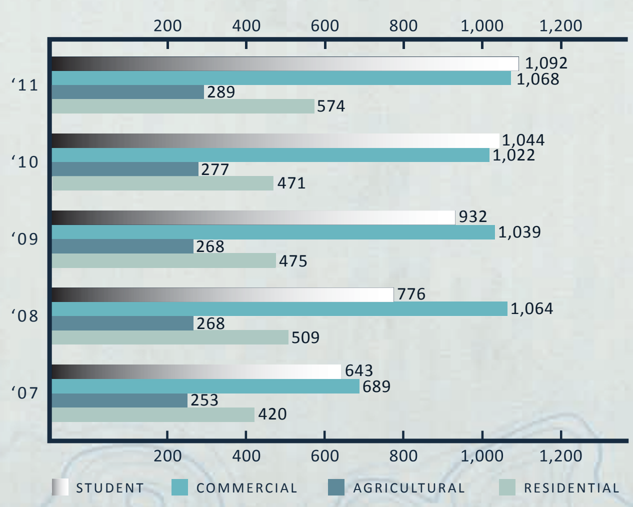


The agriculture loan portfolio grew by four percent to $289 million. The largest area of loan growth was in the financing of farm real estate loans. More than half of this portfolio is fueled by Farm and Ranch Program loans with $129 million in volume.

The commercial loan portfolio saw an increase of four percent, or $46 million. The need for Flex PACE (Partnership in Assisting Community Expansion) funding continues to be strong, growing 60 community services as energy development boomed in western North Dakota. BND also played a major role in financing development in oil-producing counties by providing $125 million in business loans and funding housing and water projects. Commercial bank participation loans grew to 64 percent of the entire $1.068 billion portfolio. BND funded 291 business and industrial projects.

Homeowners took advantage of low interest rates for purchasing and refinancing, positioning themselves to take advantage of a healthy housing market. BND acts as a secondary market for financial institutions seeking to sell FHA and VA mortgages. BND funded $100 million more in home loans in 2011. BND's loan volume has also increased because of less availability of secondary market providers. BND made 25 loans through two new rural housing programs, accounting for $3.8 million of its $574 million residential portfolio. BND also started a conventional mortgage loan origination program that was just starting to see usage at the end of 2011.

LOAN PORTFOLIO [IN MILLIONS]



The discontinuation of the Federal Family Education Loan (FFEL) Program in 2010 allowed BND the opportunity to adjust its sails and grow its exceptional state loan option, the Dakota Education Alternative Loan (DEAL). The DEAL Program saw a six percent increase in disbursements from 2010. In total, BND disbursed over $103 million in student loans and the total portfolio showed a small increase of 1.8 percent. BND continued to service its $1.092 billion student loan portfolio. While the portfolio grew, BND's student loan default rate remained low at 2.1 percent, well below the national average of 8.8 percent.

(Continued on page 6)

(Continued from page 5)

This well-diversified loan portfolio provided consistent earnings through 2011. Commercial loans accounted for 36 percent, student loans for 35 percent, agricultural loans were 10 percent, and residential loans were 19 percent of the entire portfolio. BND continued its role as an anchor for growth in a strong and healthy North Dakota economy.

BND loaned North Dakota Department of Transportation (NDDOT) interim funding to help build roads on ND Highway 22 near Killdeer. Photo courtesy of NDDOT.

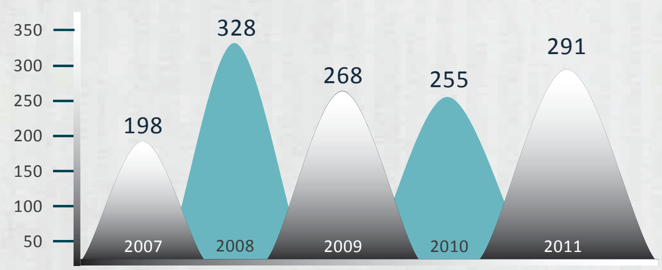
PROGRAMS AND SERVICES

Lending

Lending Navigated 2011

Bank of North Dakota (BND) played a major role in rebuilding efforts resulting from disasters statewide. Lending programs were created for homeowners, businesses, and farming operations.

BUSINESS & INDUSTRIAL PROJECTS FINANCED



Disaster Recovery Loan Programs

The Business Disaster Relief Loan Program provided financial relief to North Dakota businesses while farmers and ranchers received support through the Farm Disaster Relief Program. BND's maximum participation amount was up to $500,000, up to 75 percent of the loan; those affected by 2011 weather-related events were qualified borrowers. As of December 31, one loan was given for $86,000 to support a farm/ranch operation; 32 loans were given for a total of $4.6 million to business owners.

The 2011 Special Session of the North Dakota Legislature designated $50 million to help flood-impacted homeowners rebuild or purchase a home in the same community. The Rebuilder's Loan Program allowed homeowners to apply for up to $30,000 to cover expenses not covered by flood insurance or the Small Business Administration, or to make a downpayment on a home in the same community. Up to 20 percent of the loan can service current debt. Homeowners began making applications on December 1 with their local lenders. As of December 31, nearly $10 million in loans were closed or in process for 322 homeowners.

> "Oil and water, and the events they gave rise to, were forces that changed our landscape and presented challenges that required daily navigation."
>
> *– BND President Eric Hardmeyer*

FEMA and SBA set up their Bismarck-Mandan headquarters at BND to respond to flood victims' needs.

Supporting Residential Real Estate in Rural North Dakota

The 2011 North Dakota Legislature expanded the Residential Real Estate Loan Program by allowing BND to originate new home mortgages in rural areas when local financial institutions could not provide a home mortgage. This legislation was pursued at the request of local lenders who were struggling with new rules and regulations in the home mortgage market.

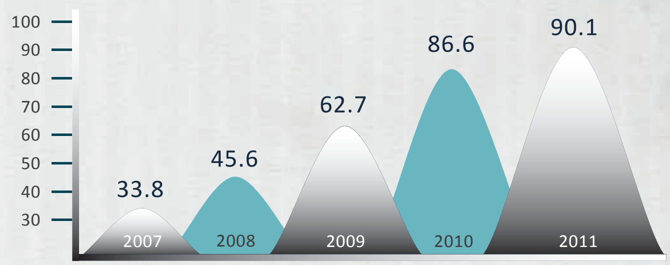
Student Loans

Student Loans successfully navigated the loss of the Federal Family Education Loan (FFEL) Program and continued their good work supporting higher education through the Dakota Education Alternative Loan (DEAL). The DEAL is available for students if the cost of education exceeds the amount a student or parent is able to borrow through federal student aid programs. There are no fees for those who are North Dakota residents or attend a North Dakota school.

BND Student Loans staff enjoy helping college students achieve their goals.

During 2011, BND disbursed more than $90.1 million in state-sponsored DEAL loans which provided loan funding for nearly 11,000 students.

DAKOTA EDUCATION ALTERNATIVE LOANS [IN MILLIONS]



In our ninth consecutive year of growth, staff continued to service 235,332 student loans totaling more than $1.092 billion. The most recent cohort default rate, as reported by the U.S. Department of Education, puts BND's default rate at 2.1%, well below the national average of 8.8%.

Agriculture Lending

This year, we saw an increase in financial institutions requesting assistance to meet customer needs in financing the high-priced cattle market. The Ag PACE (Partnership in Assisting Community Expansion) Program expanded to include sub-surface tiling on August 1; this has proved to be a popular program. With land values increasing and above-average precipitation cycles, tiling has become a more viable option for farmers.

> "The existence of BND likely enhances the viability of small banks in North Dakota."
>
> *– New England Public Policy Center Research Report 11-2, May 2011*

Ag PACE Program supports subtiling. This photo shows a tile plow working in eastern North Dakota.

WILLISTON ECONOMIC DEVELOPMENT RECEIVES ASSISTANCE FROM THE WILLISTON STAR FUND

The Ceynar Chiropractic building was made possible through the Williston Star Fund.

The city of Williston is experiencing unparalleled expansion that has produced new and difficult challenges. Rather than throw up their hands in defeat, city officials look for ways to afford the opportunities for growth.

Williston voters responded to the challenge when they approved a one percent sales tax through June 30, 2020 to create the Williston Star Fund. Seventy-five percent of the proceeds of the city sales and use tax is dedicated to property tax relief through debt reduction and to necessary infrastructure. Twenty-five percent is dedicated to economic and community development related to workforce improvement, community enhancement, and quality of life projects. The primary objective is to create jobs by applying funds for business retention, expansion, and recruitment in Williston and northwestern North Dakota.

The Williston Star Fund is a community source of buydown funds for Partnership in Assisting Community Expansion (PACE) and Flex PACE loans sponsored by Bank of North Dakota (BND) in participation with local lenders. The PACE family of programs at BND is designed to encourage specific types of economic activity within the state. The Flex PACE feature of the program is for borrowers who do not fit into the traditional definition of a PACE qualifying business. The amount of interest buydown needed is driven by the project financing and is provided by the Fund with a matching portion from BND.

The Star Fund has financed businesses that range from restaurants to laundromats to bridal stores. Tom Rolfstad, executive director of the Williston Economic Development Partnership, credits another key partner in the Fund's development. "Keith Olson, regional director of Small Business Development Center, is involved in all of the projects with BND. Keith and BND staff have always been supportive and bring creative solutions to the businesses we are assisting," said Rolfstad. "The programs fit perfectly with our fund and have allowed us to add a significant number of jobs, products, and services to our community."

All of the banks in Williston have partnered in at least one project with the Williston Star Fund and BND. Last year BND and the local banks loaned $11,988,400 in participation funding for several projects. "The beauty of these programs is that it is a win-win-win for the customer, the local banks, and our community," said Rolfstad.

The future looks bright for economic development in Williston. Chad Johnson, loan officer at BND, agrees. "Williston has been very proactive in looking for ways to make good use of the funds. As far as the future for BND's programs in Williston, the sky's the limit."

Photo Credit: North Dakota Tourism/Gerald Blank

Accounting and Treasury

Safekeeping Nearly $4.8 Billion in Treasury

Treasury Services safekept in excess of 8,000 securities totaling more than $4.7 billion at the end of 2011. The service area provided secured and unsecured federal fund lines to 113 financial institutions with combined lines of almost $400 million in 2011. Federal fund sales averaged over $10 million per day, peaking at $41 million one day in July. These reduced numbers of borrowing reflect the substantial liquidity in the marketplace.

The Letter of Credit for Public Deposits Program provided an average of nearly $220 million in additional liquidity daily. This program uses loans as collateral for the Letter of Credit which allows financial institutions to utilize investment portfolios as an additional source for other funding needs. Both programs provided a daily average of more than $230 million of liquidity to North Dakota financial institutions, topping out at more than $271 million in June.

North Dakota College Access Network (ND-CAN)

ND-CAN Programs Secure a Strong Future for Higher Education

BND's first full year administering ND-CAN successfully expanded the numbers of students it reached through education and scholarship programs.

Dual Credit Assistance

The new Dual Credit Assistance Program for high school students receiving free or reduced-price lunch allowed them to receive dual credit financial assistance for two college courses per school term. The program's popularity increased as students learned about it. By the end of the year, more than 400 students benefitted from the program.

"What [BND] does do is partner with smaller, local banks throughout the state on various loan programs… The effect is that a business loan that might otherwise not have been made – or that might have only happened at a high interest rate – can suddenly be offered at a reasonable price, prompting business growth and job creation."

Governing, January 4, 2012

Deb Gebeke, president of ND Dollars for Scholars, Ginger Strand and Paola Trottier, Rugby Dollars for Scholars, and Eric Hardmeyer, BND president, at the fall banquet

North Dakota Dollars for Scholars

This was the fourth year that BND administered North Dakota Dollars for Scholars. With the arrangement, BND supports a part-time administrator and overhead expenses. This allows for nearly 100 percent of the funds raised to be used for scholarships. In October, 59 of the 84 chapters statewide attended the annual awards luncheon in Bismarck. At the luncheon, Chapter representatives were honored with a $1,000 scholarship donation from BND President/CEO Eric Hardmeyer. The scholarship, sponsored by BND, allowed local chapters to provide a $500 scholarship to a college freshman and a $500 scholarship to a student already attending a higher education institution.

IT'S ALWAYS SUMMER AT THE BALL YARD TRAINING CENTER

Ah, summer in North Dakota, where the sounds and smells are sweet. The crack of a bat against a ball resonates with baseball and softball fans old and young, and Michael Skogen knows that better than most. Skogen has been involved in coaching baseball and softball programs for over 15 years, ranging from t-ball through the college and professional ranks at NDSU and FM RedHawks. As a coach, he realized the need for a facility to provide training all year.

A player trains in the ProBatter pitching simulator.

Skogen researched the concept of an indoor training facility in Fargo and found it to be feasible. He presented his business plan to Warren Hilde, business banker at State Bank and Trust of Fargo, to open an indoor softball and baseball training center for all ages and ability levels. "I was familiar with Michael and his passion for baseball and softball," said Hilde. "I was impressed with his business plan." Together they approached Joel Erickson at Bank of North Dakota (BND) to apply for the Beginning Entrepreneur Loan Guarantee Program. "The Ball Yard Training Center was a startup business, so we were starting from scratch," says Skogen. "Everything from batting cages and pitching simulators to office supplies and technology needed to be purchased."

The Beginning Entrepreneur Loan Guarantee Program assists in startup financing by providing a financial institution with guaranty of a loan not to exceed $200,000. The loan was a triple-play for Skogen. "Working with BND through State Bank and Trust of Fargo was great," said Skogen. "The process was easy and they were quick in their evaluation of our application. We have set up a convenient payment process that makes the program work well for everyone."

North Dakota baseball and softball enthusiasts no longer have to drive long distances to hone their skills during winter months. The Ball Yard Training Center provides an opportunity for players to become the best baseball or softball players they can be, from t-ballers through high school and college players, as well as local professionals who train on a regular basis. There may not be peanuts and Cracker Jack, but The Ball Yard Training Center in Fargo is headed for a home run.

A birthday party is hosted at The Ball Yard Training Center.

Photo Credit: North Dakota Tourism/Gerald Blank

WHY APPLY?
COLLEGE ISN'T A DREAM. IT'S YOUR OPPORTUNITY.

Why Apply Initiative

BND joined the North Dakota University System and the Indian Affairs Commission in an initiative to encourage lower income and Native American North Dakotans to attend college. Funded by a federal grant, 25 videos have been developed with written material to support the message. Videos can be viewed at kiosks located in 16 schools across the state, 13 of which are located on reservation land and on Good Health TV, a television network shown in Indian Health Service Clinics in the state. A website details the program at www.whyapplynd.com.

Crash Courses

ND-CAN partnered with the ND Center for Technology and Business to deliver eight regional Crash Courses. Crash Course is an exciting event in which students in grades 7-12 and their families learn about financial aid and Free Application for Federal Student Aid (FAFSA). Participants also receive information on job opportunities, RUReadyND.com, scholarships, and college planning.

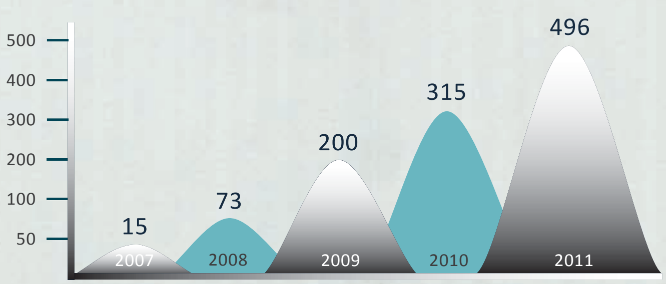
Children FIRST Launched

The College SAVE Plan launched Children FIRST in May 2011 to encourage parents of newborns to start saving for college at the earliest stage of a child's life.

Participants in Children FIRST receive a $100 grant from BND into a College SAVE account. In order to qualify a participant must open an account for a child who is born in North Dakota and is 12 months old or younger. The participant must match the $100 grant with their own $100 contribution before the child turns four years old. Funds are then comingled in the account owner's choice of investment portfolios.

This past year, 329 Children FIRST grants were distributed to participants, helping in-state College SAVE accounts grow 37 percent. Nationwide plan assets in College Save total more than $307 million.

MATCHING GRANTS



College SAVE encourages saving early for a child's education.

CROSBY COMMUNITY FULFILLS NEED FOR SENIOR HOUSING

In western North Dakota communities such as Crosby, a center for farming and oil and gas exploration, new and longtime residents share a need for reasonably priced housing. One common goal is preventing older residents from being forced to move elsewhere for assisted care.

Completed construction of Northern Lights Villa

St. Luke's Community Foundation was formed in 2008 to resolve the housing shortage in Crosby and keep people in the community. The Foundation received a Flex Partnership in Assisting Community Expansion (PACE) loan to build eight assisted living units called Northern Lights Villa on the campus of the Crosby Clinic and St. Luke's Hospital. The loan was a joint effort between Bank of North Dakota (BND) and First National Bank in Crosby, with help from Keith Olson at Small Business Development Center. After construction of Northern Lights Villa was finished in 2009 and the eight units filled successfully, the Foundation supported an addition to the Villa. In July 2011, six additional units were completed. Currently, 18 residents of Crosby are fortunate to live near their families and see their regular doctors.

The Flex PACE program provides interest buy down to borrowers who do not fit into the traditional definition of a PACE qualifying business. The buy down can reduce the borrower's interest rate by as much as five percent. Chad Johnson, loan officer at BND, said, "The interest buy down allowed the project to pay back lenders more easily as well as provide lower rent fees to residents." The program allows communities to assist borrowers with a business focus or need outside of the current requirements of PACE. "The joint effort of BND and First National Bank allowed us to establish a beautiful complex in proximity to our clinic and hospital," remarked Jean Nygaard, R.N. and manager of Northern Lights Villa. "Our rental prices are affordable, our units are full, and we have a waiting list. We are extremely proud of our facility."

Art Christianson, resident of Northern Lights Villa

No one is more thrilled about the Villas than Gwen Vassen, whose father, Art Christianson is a resident. "He was born and raised on a farm south of Crosby," said Vassen. "We were so happy that he chose to move to the Villas. He loves it, and we love it." Vassen tries to visit everyday, but when she can't, she's comfortable knowing her father is well taken care of. "I don't want to think about where he would be if the Villas hadn't been built."

Photo Credit: North Dakota Tourism/Gerald Blank

BND LEADERSHIP PROGRAM

New Leaders Graduate

The Leadership Program is a highly structured, team-focused development opportunity for BND employees that includes skills development, service area and leadership overviews from BND leaders, and a team project.

The 2011 graduates developed The Connections Program to help employees understand banking principles as they apply to BND and define the interdependencies between BND service areas. This fun learning experience "follows the money" by using a variety of learning experiences: web-based learning, service area interaction, and work studies.

The BND 2011 Leadership Class developed an employee education program.

STRATEGIC PLANNING

Strategic Planning for a Secure Tomorrow

The 2012-2014 Strategic Plan development was a four-month process that began with input from the BND Advisory Board and select community leaders. This group, which included individuals from business, higher education, and state government, identified key factors that will influence North Dakotans in the near future.

Staff members were invited to brainstorming meetings to provide a front-line assessment of the needs of their customers. BND's Executive Team and selected staff members discussed input from the groups, reviewed the current status of the banking industry, and developed the plan.

The Strategic Plan provides the foundation for the Bank's work in the next three years. Employee goals and management objectives tie into the plan, allowing it to be a document that inspires progress.

BND: NAVIGATING FINANCIAL WELLBEING FOR NORTH DAKOTA

As the only state-owned bank in the country, Bank of North Dakota garners a great deal of attention. At the end of 2011, 14 states were considering legislation for some form of a state-owned bank. Many of them look to BND as a model. We frequently receive requests from government entities, as well as national and international media.

Many of those who contact us are surprised to hear that we believe in strong partnerships with community banks and state government. This commitment extends back to the founding principles established in 1919 when the Legislature deemed that BND was "to be helpful to and to assist in the development of state and national banks and other financial institutions and public corporations within the state and not, in any manner, to destroy or to be harmful to existing financial institutions."

For 92 years, BND has weathered the storms and celebrated safe arrivals. As we navigate the challenges in the years ahead, the mission of promoting agriculture, commerce, and industry will continue to be a beacon that reminds us of this vital purpose.

2012-2014 STRATEGIC IMPERATIVES / A FRAMEWORK FOR PROGRESS

PILLAR	IMPERATIVE
ECONOMIC DEVELOPMENT Deliver quality programs and services to expand the economy of North Dakota	▪ Be proactive in our efforts to assist local financial institutions and economic entities to meet the current and future needs of ND communities. ▪ Develop the "College Planning Center" to expand its efforts in helping North Dakotans prepare and pay for college.
CULTURE Provide a culture that develops the skills of its people and is a model of efficient business and government.	▪ Generate improved processes to enhance performance, address staffing needs, and create an environment which encourages involvement in organizations and trade associations. ▪ Embrace a focused and balanced approach to improving efficiencies and processes.
FINANCIAL Generate a consistent financial return to the State of North Dakota while maintaining the strength and financial integrity of BND.	▪ Grow profits while protecting our balance sheet by following strategies that focus on income generation, risk mitigation, and expense control. ▪ Be the Correspondent Bank of Choice for financial institutions in North Dakota.

Photo Credit: North Dakota Tourism

ND INDUSTRIAL COMMISSION

Jack Dalrymple
Governor

Doug Goehring
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: Tim Porter, Joe Herslip, Eric Hardmeyer, Lori Leingang, Bob Humann

FINANCIALS
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BRADY MARTZ
CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

The Industrial Commission
State of North Dakota
Bismarck, North Dakota

We have audited the accompanying balance sheets of the Bank of North Dakota as of December 31, 2011 and 2010, 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 Accounting Standards Codification of authoritative generally accepted accounting principles to be applied by non governmental entities. 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, 2011 and 2010, 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

BRADY, MARTZ & ASSOCIATES, P.C.

February 28, 2012

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BANK OF NORTH DAKOTA
BALANCE SHEETS
DECEMBER 31, 2011 AND 2010

	(In Thousands)	
	2011	2010
ASSETS		
Cash and due from banks	**$ 1,351,055**	$ 638,100
Federal funds sold	**18,315**	33,100
Cash and cash equivalents	**1,369,370**	671,200
Securities	**1,008,051**	537,157
Loans	**2,995,154**	2,814,548
Less allowance for loan losses	**(52,883)**	(46,613)
	2,942,271	2,767,935
Interest receivable	**39,479**	39,146
Bank premises, equipment, and software, net	**12,166**	12,294
Other assets	**3,736**	2,195
Total assets	**$ 5,375,073**	$ 4,029,927
LIABILITIES AND EQUITY		
Deposits		
Non-interest bearing	**$ 649,922**	$ 387,040
Interest bearing	**3,529,915**	2,671,686
	4,179,837	3,058,726
Federal funds purchased and repurchase agreements	**318,325**	240,725
Short and long-term debt	**471,422**	397,365
Other liabilities	**5,586**	5,814
Total liabilities	**4,975,170**	3,702,630
Equity		
Capital	**2,000**	2,000
Capital surplus	**42,000**	42,000
Undivided profits	**350,249**	282,729
Accumulated other comprehensive income	**5,654**	568
Total equity	**399,903**	327,297
Total liabilities and equity	**$ 5,375,073**	$ 4,029,927

See Notes to Financial Statements

BANK OF NORTH DAKOTA
STATEMENTS OF INCOME
YEARS ENDED DECEMBER 31, 2011 AND 2010

	(In Thousands)	
	2011	2010
INTEREST INCOME		
Federal funds sold	**$ 65**	$ 96
Securities	**14,335**	11,332
Loans, including fees	**123,059**	121,972
Total interest income	**137,459**	133,400
INTEREST EXPENSE		
Deposits	**19,857**	24,443
Federal funds purchased and repurchase agreements	**337**	911
Short and long-term debt	**19,347**	19,834
Total interest expense	**39,541**	45,188
NET INTEREST INCOME	**97,918**	88,212
PROVISION FOR LOAN LOSSES	**11,000**	12,100
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	**86,918**	76,112
NONINTEREST INCOME		
Service fees and other	**6,652**	6,113
Net loss on available-for-sale securities	**(1,741)**	-
Total noninterest income	**4,911**	6,113
NONINTEREST EXPENSE		
Salaries and benefits	**11,693**	11,188
Data processing	**3,952**	4,084
Occupancy and equipment	**906**	823
Other operating expenses	**4,943**	4,279
Total noninterest expenses	**21,494**	20,374
NET INCOME	**$ 70,335**	$ 61,851

BANK OF NORTH DAKOTA
STATEMENTS OF EQUITY
YEARS ENDED DECEMBER 31, 2011 AND 2010

	(In Thousands)				
	Capital	Capital Surplus	Undivided Profits	Accumulated Other Comprehensive Income (Loss)	Total
BALANCE, DECEMBER 31, 2009	$ 2,000	$ 42,000	$ 225,966	$ 1,683	$ 271,649
Comprehensive income					
Net income			61,851		61,851
Unrealized loss on securities available for sale				(1,115)	(1,115)
Total comprehensive income					60,736
Transfer to other state funds			(5,088)		(5,088)
BALANCE, DECEMBER 31, 2010	2,000	42,000	282,729	568	327,297
Comprehensive income					
Net income			70,335		70,335
Unrealized gain on securities available for sale				3,345	3,345
Other-than-temporary impaiment losses realized in net income				1,800	1,800
Reclassification adjustment for (gains) losses realized in net income				(59)	(59)
Total comprehensive income					75,421
Transfer to other state departments			(2,815)		(2,815)
BALANCE, DECEMBER 31, 2011	$ 2,000	$ 42,000	$ 350,249	$ 5,654	$ 399,903

See Notes to Financial Statements

BANK OF NORTH DAKOTA
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011 AND 2010

	(In Thousands)	
	2011	2010
OPERATING ACTIVITIES		
Net income	**$ 70,335**	$ 61,851
Adjustments to reconcile net income to net cash from operating activities		
Depreciation and amortization	**900**	1,130
Provision for loan losses	**11,000**	12,100
Net amortization (accretion) of securities	**927**	530
Loss on available-for-sale securities	**1,741**	-
Gain on sale of residential loans	**(43)**	(13)
Loss on retirement of equipment	**8**	-
Gain on sale of foreclosed assets	**(7)**	(5)
Increase in interest receivable	**(333)**	(4,596)
Increase in other assets	**(685)**	(105)
Decrease in other liabilities	**(270)**	(559)
NET CASH FROM OPERATING ACTIVITIES	**83,573**	70,333
INVESTING ACTIVITIES		
Securities available for sale transactions		
Purchase of securities	**(589,061)**	(247,549)
Proceeds from sales, maturities, and principal repayments	**123,441**	107,491
Purchase of Federal Home Loan Bank stock	**(3,954)**	(1,179)
Sale of Federal Home Loan Bank stock	**1,510**	40
Purchase of other equity securities	**(487)**	(352)
Sale of other equity securities	**75**	117
Proceeds from sales of loans	**1,995**	1,122
Net increase in loans	**(188,641)**	(110,454)
Purchases of premises and equipment	**(780)**	(507)
Proceeds from sale of foreclosed assets	**504**	818
NET CASH USED FOR INVESTING ACTIVITIES	**(655,398)**	(250,453)
FINANCING ACTIVITIES		
Net increase/(decrease) in non-interest bearing deposits	**262,882**	(55,827)
Net increase in interest bearing deposits	**858,229**	175,494
Net increase/(decrease) in federal funds purchased and repurchase agreements	**77,600**	(96,902)
Proceeds from issuance of short and long-term debt	**90,100**	15,131
Payment of short and long-term debt	**(16,043)**	(22,771)
Payment of transfers	**(2,773)**	(5,044)
NET CASH FROM FINANCING ACTIVITIES	**1,269,995**	10,081
NET CHANGE IN CASH AND CASH EQUIVALENTS	**698,170**	(170,039)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	**671,200**	841,239
CASH AND CASH EQUIVALENTS, END OF YEAR	**$ 1,369,370**	$ 671,200

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 Accounting Standards Codification, 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, 2011 and 2010:

	2011	2010
Student loans, of which 97% and 97% are guaranteed	**35%**	37%
Commercial loans, of which 4% and 5% are federally guaranteed	**36%**	36%
Residential loans, of which 83% and 83% are federally guaranteed	**19%**	17%
Agricultural loans, of which 5% and 7% are federally guaranteed	**10%**	10%
	100%	100%

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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.

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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. 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 Credit Losses

The Bank uses the allowance method in providing for credit losses. Accordingly, the allowance is increased by the current year's provision for credit losses charged to operations and reduced by net charge-offs. Credit 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 credit losses and the provision for credit losses charged to operations are based on management's evaluation of a number of factors, including recent credit 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 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.

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Loan Charge-Offs

Loans are generally fully or partially charged down to the fair value of collateral securing the asset when:

- An unsecured loan that has principal or interest 120 or more days past due.
- A loan secured by a commercial real estate mortgage, farm real estate mortgage, conventional real estate mortgage, or by other than real property that has principal or interest 120 or more day past due.
- A loan classified as a "loss" by the North Dakota Department of Banking and Financial Institutions.
- A loan where there is a recognized loss in conjunction with the acquisition of real estate by the Bank.
- A loan where the Bank deems itself insecure due to the financial condition of the borrower.
- A loan or portion of a loan has been forgiven.

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.

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 $981,000 as of December 31, 2011. There were no foreclosed assets as of December 31, 2010.

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.

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Recent Accounting Pronouncements

In April 2011, the FASB issued amended accounting and disclosure guidance relating to a creditor's determination of whether a restructuring is a trouble debt restructuring. The amendments clarify the guidance on a creditor's evaluation of whether it has granted a concession and whether a debtor is experiencing financial difficulties. This guidance is effective for annual periods ending on or after December 15, 2012. The adoption of this guidance is not expected to have a material impact on the Bank's financial position, results of operations, or cash flows.

In May 2011, the FASB issued updated accounting guidance related to fair value measurements and disclosures that result in common fair value measurements and disclosures between U.S. GAAP and International Financial Reporting Standards. This guidance includes amendments that clarify the application of existing fair value measurement requirements, in addition to other amendments that change principles or requirements for measuring fair value and for disclosing information about fair value measurements. This guidance is effective for annual periods beginning after December 15, 2011. This guidance will primarily impact the Bank's disclosures, but otherwise is not expected to have a material impact on the Bank's financial statements.

In June 2011, the FASB issued new accounting guidance related to the presentation of comprehensive income that eliminates the option to present components of other comprehensive income as part of the statement of equity. The amendments require that all nonowner changes in equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amendments do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance is effective for fiscal years beginning after December 15, 2012. The adoption of this guidance will not impact the Bank's financial position, results of operations, or cash flows and will only impact the presentation of other comprehensive income in the financial statements.

NOTE 2 - RESTRICTION AND CONCENTRATION ON CASH AND DUE FROM BANKS

Federal Reserve Board regulations require the Bank to maintain reserve balances with the Federal Reserve Bank. The average required reserve balances maintained at the Federal Reserve Bank were approximately $56,628,000 in 2011 and $49,977,000 in 2010.

The Bank has depository relationships where it is a requirement of the other institution in order to have a business relationship. Deposits at these institutions are insured up to $250,000 with the Federal Deposit Insurance Company except for deposits with the Federal Reserve Bank and the Federal Home Loan Bank. The amount of cash deposits not covered by FDIC insurance was $1,072,703,000 and $514,771,000 as of December 31, 2011 and 2010, respectively. Of these amounts, $1,021,732,000 and $489,882,000 were deposited at the Federal Reserve Bank.

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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, 2011 and 2010 consists of the following:

	(In Thousands)	
	2011	2010
Securities available for sale, at fair value	**$ 977,833**	$ 509,794
Federal Home Loan Bank stock, at cost	**25,776**	23,333
Other equity securities, at cost	**4,442**	4,030
	$ 1,008,051	$ 537,157

The amortized cost and fair value of securities with gross unrealized gains and losses follows:

	(In Thousands)			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2011				
Securities available for sale				
Federal agency	**$ 476,946**	**$ 3,312**	**285**	**$ 479,973**
Mortgage-backed	**479,071**	**6,096**	**3,468**	**481,699**
State and municipal	**16,161**	**-**	**-**	**16,161**
	$ 972,178	**$ 9,408**	**$ 3,753**	**$ 977,833**

	(In Thousands)			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
DECEMBER 31, 2010				
Securities available for sale				
Federal agency	$ 142,647	$ 1,914	$ 800	$ 143,761
Mortgage-backed	357,711	5,233	5,779	357,165
State and municipal	8,868	-	-	8,868
	$ 509,226	$ 7,147	$ 6,579	$ 509,794

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Securities carried at $3,758,000 and $352,000 at December 31, 2011 and 2010, respectively were used to secure repurchase agreements and for other required pledging purposes. FHLB stock totaling $25,776,000 and $23,333,000 at December 31, 2011 and 2010, respectively are pledged on the FHLB advances (Note 9).

The maturity distribution of debt securities at December 31, 2011, 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	$ 187,115	$ 187,741
Over one year through five years	612,476	618,589
Over five years through ten years	135,324	134,426
Over ten years	37,263	37,076
	$ 972,178	$ 977,832

For the year ended December 31, 2011, proceeds from the sale of securities available for sale were $4,093,000. Gross realized gains were $59,000 on these sales. For the year ended December 31, 2010, proceeds from the sale of securities available for sale were $1,157,000. There were no realized gains or losses on these sales.

Information pertaining to securities with gross unrealized losses at December 31, 2011, 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	$ 1,819	$ 264,213	$ 1,934	$ 3,246

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.

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At December 31, 2011, two privatized collateralized mortgage obligation securities have unrealized losses with aggregate depreciation of 31% from the amortized cost basis. At December 31, 2010, two privatized collateralized mortgage obligation securities and one government agency collateralized mortgage obligation security have unrealized losses with aggregate depreciation of 21% from the amortized cost basis. In analyzing these obligations, management reviews payment performance, defaults, credit support and credit coverage status. As the Bank does not intend to sell these securities and it is more likely than not that management will not be required to sell prior to recovery, the decline is not deemed to be other than temporary.

At December 31, 2011, one privatized collateralized mortgage obligation security was written down as an other-than-temporary impairment. The following roll forward reflects the amount related to credit losses recognized in earnings:

	(In thousands)
	Available for Sale
Beginning balance as of December 31, 2010*	$ -
Add: Amount related to the credit loss for which an other-than-temporary impairment was not previously recognized	1,800
Add: Increases to the amount related to the credit loss for which an other-than-temporary impairment was previously recognized	-
Less: Realized losses for securities sold	-
Less: Securities for which the amount previously recognized in other comprehensive income was recognized in earnings because the Bank intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis	-
Less: Increases in cash flows expected to be collected that are recognized over the remaining life of the security	-
Ending balance as of December 31, 2011	$ 1,800

*The beginning balance represents the amount related to credit losses on debt securities held by the Bank at the beginning of the period for which a portion of an other-than-temporary impairment was recognized in other comprehensive income.

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NOTE 4 - LOANS

The composition of the loan portfolio at December 31, 2011 and 2010 is as follows:

	(In Thousands)	
	2011	2010
Commercial	**$ 1,068,598**	$ 1,022,002
Student	**1,062,534**	1,044,442
Residential	**575,020**	471,411
Agricultural	**289,002**	276,693
	2,995,154	2,814,548
Allowance for loan losses	**52,883**	46,613
	$ 2,942,271	$ 2,767,935

Unamortized deferred student loan costs totaled $11,414,000 and $12,504,000 as of December 31, 2011 and 2010, respectively. Net unamortized loan premiums and discounts, including purchased servicing rights, on residential loans totaled $4,658,000 and $3,100,000 as of December 31, 2011 and 2010, respectively.

Management has an established methodology to determine the adequacy of the allowance for credit losses that assesses the risks and losses inherent in the loan portfolio. For purposes of determining the allowance for credit losses, the Bank has segmented certain loans in the portfolio by product type. Loans are segmented into the following pools: commercial, agricultural, residential real estate, and student loans. The Bank also sub-segments the commercial and agricultural segments into classes based on the associated risks within those segments. Commercial loans are divided into three classes: commercial participations, bank stock, and all other business loans (including PACE). Agricultural loans are also divided into three classes: farm & ranch, farm real estate, and all other farm loans. Each class of loan exercises significant judgment to determine the estimation method that fits the credit risk characteristics of its portfolio segment.

The adequacy of the allowance for credit losses and the provision for credit losses charged to operations are based on management's evaluation of a number of factors, including recent credit 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. Changes in the allowance for credit loss and the related provision expense can materially affect net income.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as 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.

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The total allowance reflects management's estimate of credit losses inherent in the loan portfolio at the balance sheet date. The Bank considers the allowance for credit losses of $52,883,000 adequate to cover loan losses inherent in the loan portfolio, at December 31, 2011. The following table represents by portfolio segment, the changes in the allowance for credit losses and the recorded investment in loans.

(In Thousands)

	Commercial Loans	Farm Loans	Residential RE Loans	Student Loans	TOTAL
Beginning Balance:	$ 36,210	$ 8,803	$ 483	$ 1,117	$ 46,613
Charge-offs	(4,613)	(63)	-	(129)	(4,805)
Recoveries	42	26	-	7	75
Provision	8,479	712	1,517	292	11,000
Ending Balance	$ 40,118	$ 9,478	$ 2,000	$ 1,287	$ 52,883

The following table disaggregates our allowance for credit losses by impairment methodology.

(In Thousands)

	Commercial Loans	Farm Loans	Residential RE Loans	Student Loans	TOTAL
Collectively evaluated	$ 30,770	$ 9,081	$ 2,000	$ 1,287	$ 43,138
Individually evaluated	9,348	397	-	-	9,745
Total	$ 40,118	$ 9,478	$ 2,000	$ 1,287	$ 52,883

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The Bank's internally assigned ratings are as follows:

	Risk Code	Description
Exceptional	1	Loan considered prime on the basis of very substantial financial capacity with minimal risk of non payment
Excellent	2	Loan considered sound on the basis of strong financial capacity with little or no apparent weakness and very limited risk of non payment. The probability of serious financial deterioration is highly unlikely.
Good	3	Loan may reveal weaknesses in some areas, however, not of a serious nature and the debt remains collectible in its entirety. The collateral many be characterized as being less marketable than that of a higher rated borrower.
Acceptable	4	Bank feels that the credit risk is acceptable, but may require above average officer attention. Credit in this class exhibit the earliest signs of potential problems. A greater reliance will be placed on the quality and marketability of the underlying collateral as the cash flow may be unproven or somewhat erratic.
Special Mention	5	May be bankable based on certain types of loan programs which fall within the Bank's mission. This type of loan may be currently protected, but has potential unrealized weaknesses. The loan will require close monitoring as deterioration remains a strong possibility. The potential problems must remain manageable and must not pose a serious threat to repayment.
Substandard	6	Well defined weaknesses jeopardize orderly repayment. The loan is no longer protected by sound net worth or repayment capacity of the borrower. Even though elements of loss are present, the borrower can potentially repay if deficiencies are corrected. Close monitoring of this type of loan is extremely important to prevent loss to the Bank.
Doubtful	7	Loan had deteriorated to the point where collection or liquidation in full on the basis of current information, conditions and values is highly questionable and improbable. A doubtful classification is warranted during this period of quantifying/defining the amount of exposure or loss. A well defined corrective action or liquidation plan should be developed and implemented as soon as possible to limit further loss potential for the bank.
Loss	8	Loan is considered uncollectible and of such value that it should be charged-off. This classification does not mean that the asset has no recovery or salvage value.

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The following table represents credit exposures by internally assigned risk ratings for the year ended December 31, 2011. The rating analysis estimates the capability of the borrower to repay the contractual obligations of the loan agreements as scheduled or at all. The Bank's internal credit risk rating is based on experiences with similarly rated loans. Credit risk ratings are refreshed periodically as they become available, at which time management analyzes the resulting scores, as well as other external statistics and factors, to track loan performance.

(In Thousands)

Risk Rating	Commercial Participations	Bank Stock	All Other Business Loans (Including PACE)	Farm & Ranch	Farm Real Estate
No assigned risk rating	$ -	$ -	$ -	$ -	$ -
1	-	-	39,747	-	-
2	25,591	-	78,006	2,929	-
3	251,004	53,704	26,105	55,996	43,018
4	304,385	84,326	71,809	59,944	53,167
5	51,066	649	6,242	703	23,662
6	39,850	15,298	1,602	4,902	279
7	7,517	-	643	-	-
8	-	-	-	-	-
Loan types excluded from allowance	-	-	11,053	-	-
Total	$ 679,413	$ 153,977	$ 224,154	$ 124,474	$ 120,126

Risk Rating	All Other Farm Loans	Residential Real Estate	Student Loans	Total
No assigned risk rating	$ -	$ 574,882	$ 707,218	$ 1,282,100
1	-	-	-	39,747
2	66	-	-	106,592
3	3,208	-	-	433,035
4	20,536	-	-	594,167
5	6,478	-	-	88,800
6	-	-	-	61,931
7	-	-	-	8,160
8	-	-	-	-
Loan types excluded from allowance	14,115.00	138	355,316	380,622
Total	$ 44,403	$ 575,020	$ 1,062,534	$ 2,995,154

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Following is a table which includes an aging analysis of the recorded investment of past due financing receivables as of December 31, 2011. Also included are loans that are 90 days or more past due as to interest and principal and still accruing, because they are (1)well-secured and in the process of collection, (2) real estate loans or loans exempt under regulatory rules from being classified as nonaccrual or (3) student loans where accrued interest is guaranteed.

Loan Class	31-60 days past due	61 - 90 days past due	Greater than 90 days	Total Past Due	Current	Total Loans	Investment >90 days and accruing
	(In Thousands)						
Commercial Participations	$ 142	$ 178	$ 6,442	$ 6,762	$ 672,651	$ 679,413	$ 562
Bank Stock	-	-	-	-	153,977	153,977	-
All other Business Loans (Including PACE)	708	958	1,044	2,710	232,498	235,208	122
Farm & Ranch	1,077	1,851	952	3,880	120,594	124,474	952
Farm Real Estate	823	-	243	1,066	119,061	120,127	243
All other Farm loans	427	-	-	427	43,974	44,401	-
Residential Real Estate	10,829	2,456	5,963	19,248	555,772	575,020	5,511
Student Loans	16,648	10,835	33,076	60,559	1,001,975	1,062,534	32,861
Totals	$ 30,654	$ 16,278	$ 47,720	$ 94,652	$ 2,900,502	$ 2,995,154	$ 40,251

Management considers a loan to be impaired when, based on current information and events, it is determined that the Bank will not be able to collect all amounts due according to the loan contract, including scheduled interest payments. Determination of impairment is treated the same across all classes of loans. When management identifies a loan as impaired, the impairment is measured based on the present value of expected future cash flows, discounted at the loan’s effective interest rate, except when the sole (remaining) source of repayment for the loan is the operation or liquidation of the collateral. In these cases management uses the current fair value of the collateral, less selling costs when foreclosure is probable, instead of discounted cash flows. If management determines that the value of the impaired loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance.

When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal, under the cost recovery method. When the ultimate collectability of the total principal of an impaired loan is not in doubt and the loan is on nonaccrual status, contractual interest is credited to interest income when received, under the cash basis method.

The following table includes the recorded investment and unpaid principal balances for impaired financing receivables with the associated allowance amount, if applicable. Management determined the specific allowance based on the present value of expected future cash flows, discounted at the loan’s effective interest rate, except when the remaining source of repayment for the loan is the operation or liquidation of the collateral. In those cases, the current fair value of the collateral, less selling costs was used to determine the specific allowance recorded.

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Also presented are the average recorded investments in the impaired loans and the related amount of interest recognized during the time within the period that the impaired loans were impaired. When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal, under the cost recovery method. When the ultimate collectability of the total principal of an impaired loan is not in doubt and the loan is on nonaccrual status, contractual interest is credited to interest income when received, under the cash basis method.

	(In Thousands)			
Loan Class	Recorded Investment	Unpaid Principal Balance	Associated Allowance	Average Recorded Investment
With No Specific Allowance Recorded:				
Commercial Participations	$ -	$ -	$ -	$ -
Bank Stock	-	-	-	-
All other Business Loans (Including PACE)	61	3	-	25
Farm & Ranch	23	10	-	11
Farm Real Estate	-	-	-	-
All other Farm loans	-	-	-	-
Residential Real Estate	1,536	1,242	-	1,451
Student Loans	217	215	-	-
With an Allowance Recorded:				
Commercial Participations	$ 52,302	$ 41,287	$ 8,432	$ 42,715
Bank Stock	1,300	1,115	167	1,145
All other Business Loans (Including PACE)	4,100	2,573	749	2,842
Farm & Ranch	1,665	1,077	342	1,282
Farm Real Estate	431	383	49	389
All other Farm loans	116	81	6	89
Residential Real Estate	-	-	-	-
Student Loans	-	-	-	-
Totals:				
Commercial Participations	$ 52,302	$ 41,287	$ 8,432	$ 42,715
Bank Stock	1,300	1,115	167	1,145
All other Business Loans (Including PACE)	4,161	2,576	749	2,867
Farm & Ranch	1,688	1,087	342	1,293
Farm Real Estate	431	383	49	389
All other Farm loans	116	81	6	89
Residential Real Estate	1,536	1,242	-	1,451
Student Loans	217	215	-	-

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A loan which meets any of the following criteria must be placed in a non-accrual status:

- The following loans on which the principal and interest is 90 or more days past due: Unsecured loans, loans secured by other than real property, loans secured by a mortgage on commercial real estate, loans secured by a farm real estate mortgage, loans secured by a conventional residential real estate mortgage.
- A loan where the borrower has filed for bankruptcy or where the lead bank or the Bank deems itself insecure due to the financial condition of the borrower.
- A loan which the North Dakota Department of Financial Institutions recommends to be placed in a non-accrual status.

A loan which meets the criteria for non-accrual status may be retained in accrual status if it is (1)guaranteed or insured by the state or federal government or secured by collateral with a fair market value sufficient to discharge the outstanding principal and interest and (2)in the process of collection supported by a document source of collection.

A loan which has been placed in a non-accrual status may be returned to an accrual status only if principal and interest are no longer due and unpaid and if current principal and interest appear to be collectable. In addition, the loan must either be secured by collateral with a fair market value sufficient to discharge the outstanding principal and interest or the borrower must demonstrate through a documented repayment plan the ability to discharge the outstanding principal and interest.

On the following table are the financing receivables on nonaccrual status as of December 31, 2011. The balances are presented by class of financing receivable.

	(In Thousands)
Commercial Participations	$ 10,996
Bank Stock	-
All Other Business Loans (Including PACE)	1,100
Farm & Ranch	-
Farm Real Estate	-
All Other Farm Loans	-
Residential Real Estate	589
Student	215
TOTAL	$ 12,900

Accruing loans 90 days or more past due include guaranteed student loans of $32,861,000 and $37,600,000 as of December 31, 2011 and 2010, 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.

Residential loans of $5,511,000 and $4,433,000 as of December 31, 2011 and 2010, respectively, are also included in accruing loans 90 days or more past due. In the event of a foreclosure a residential loan guaranteed by the Federal Housing Administration will be paid in full and the property title is transferred to them with the exception of flooded properties. The Department of Veterans Affairs has the option of paying their guaranty percentage and the Bank keeps the foreclosed property as well as any gain or loss from the sale or they can pay the loan in full and title is transferred to them.

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The Bank's loan portfolio also includes certain loans that have been modified in a Trouble Debt Restructuring (TDR), where economic concessions have been granted to borrowers who have experienced or are expected to experience financial difficulties. These concessions typically result from the Bank's loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Certain TDRs are classified as nonperforming at the time of restructure and may only be returned to performing status after considering the borrower's sustained repayment performance for a reasonable period, generally six months.

When the Bank modifies a loan, management evaluates any possible impairment based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan agreement, except when the sole (remaining) source of repayment for the loan is the operation or liquidation of the collateral. In these cases management uses the current fair value of the collateral, less selling costs, instead of discounted cash flows. If management determines that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized by segment or class of loan, as applicable, through an allowance estimate or a charge-off to the allowance. Segment and class status is determined by the loan's classification at origination.

The following tables include the recorded investment and number of modifications for modified loans. The Bank reports the recorded investment in the loans prior to a modification and also the recorded investment in the loans after the loans were restructured. Management has also disclosed the recorded investment and number of modifications for troubled debt restructurings within the last year where a concession has been made, that then defaulted in the current reporting period.

		(In Thousands)	
	Number of Modifications	Recorded Investment Prior to Modification	Recorded Investment After Modification
Commercial Participations	17	$ 43,203	$ 39,533
Bank Stock	1	1,155	1,115
All Other Business Loans (Including PACE)	9	1,984	1,687
Farm & Ranch	1	1,508	1,077
Farm Real Estate	3	416	383
All Other Farm Loans	3	129	91
Residential Real Estate	6	650	655
Student Loans	0	-	-
TOTAL	40	$ 49,045	$ 44,541

There were no material commitments to lend additional funds to customers whose loans were classified as impaired or restructured at December 31, 2011 and 2010.

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NOTE 5 - LOAN SALES AND LOAN SERVICING

A summary of BND loan sales during 2011 and 2010 follows:

	(In Thousands)	
	2011	2010
Residential loans sold on the secondary market	**$ 1,952**	$ 1,109

BND recognized gains on sale of loans of $43,000 in 2011 and $13,000 in 2010 which is included in non-interest income on the Statements of Income.

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, 2011 and 2010 were as follows:

	(In Thousands)	
	2011	2010
Student loans		
North Dakota Student Loan Trust	**$ 41,233**	$ 47,160
Residential loans		
Fannie Mae	**10,250**	11,025
Other state fund loans		
Board of University and School Lands	**55,806**	43,890
Community Water Facility Loan Fund	**16,143**	17,316
Beginning Farmer Revolving Loan Fund	**-**	8,572
Developmentally Disabled Facility Loan Program	**-**	648
Rebuilders Loan Program	**2,206**	-
Department of Human Services	**7,860**	8,271
Information Technology Department	**4,404**	2,758
Workforce Safety	**152**	86
	$ 138,054	$ 139,726

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.

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NOTE 6 - BANK PREMISES, EQUIPMENT, AND SOFTWARE

A summary of changes in bank premises, equipment, furniture, and software at December 31, 2011 and 2010 is as follows:

(In Thousands)	Balance 2010	Additions	Retirements	Balance 2011
Land	$ 1,171	$ 274	$ -	$ 1,445
Building	10,212	-	-	10,212
Equipment	756	76	169	663
Furniture	679	-	-	679
Hardware	627	11	64	574
Software	5,513	419	1,019	4,913
	18,958	780	1,252	18,486
Less accumulated depreciation	6,664	900	1,244	6,320
	$ 12,294	$ (120)	$ 8	$ 12,166

(In Thousands)	Balance 2009	Additions	Retirements	Balance 2010
Land	$ 1,171	$ -	$ -	$ 1,171
Building	10,212	-	-	10,212
Equipment	987	26	257	756
Furniture	679	-	-	679
Hardware	1,267	41	681	627
Software	6,564	440	1,491	5,513
	20,880	507	2,429	18,958
Less accumulated depreciation	7,963	1,130	2,429	6,664
	$ 12,917	$ (623)	$ -	$ 12,294

Depreciation and amortization expense on the above assets amounted to $900,000 and $1,130,000 in 2011 and 2010.

NOTE 7 - DEPOSITS

The aggregate amount of locally sold certificates of deposit larger than $100,000 was $2,526,984,000 and $2,030,887,000 as of December 31, 2011 and 2010, respectively.

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At December 31, 2011, the scheduled maturities of certificates of deposits are as follows:

		(In Thousands)
One year or less	$	2,284,659
One to three years		148,410
Over three years		118,178
	$	2,551,247

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. There were no repurchase agreements as of December 31, 2011 and 2010.

NOTE 9 - SHORT AND LONG-TERM DEBT

Short and long-term debt consists of:

	(In Thousands)			
		2011		2010
Federal Home Loan Bank advances - long-term	**$**	**470,327**	$	396,200
ND Public Finance Authority, 3%, matures from September 2014 through September 2021		**1,095**		1,165
	$	**471,422**	$	397,365

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
2012	$	3,170	$	20,284	$	23,454
2013		65,291		18,584		83,875
2014		18,417		16,852		35,269
2015		13,541		16,444		29,985
2016		38,650		14,652		53,302
Later years		332,353		41,764		374,117
Totals	$	471,422	$	128,580	$	600,002

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The FHLB long-term advances outstanding at December 31, 2011, mature from January 2013 through March 2025. The FHLB long-term advances have fixed rate interest, ranging from 3.01% to 7.35%. The advances must be secured by minimum qualifying collateral maintenance levels. Residential loans and student loans with carrying values of $559,510,000 and $449,554,000 at December 31, 2011 and 2010, 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)	
	2011	2010
Interest payable	**$ 1,839**	$ 2,419
Salary and benefits payable	**999**	968
Student loan related payables	**195**	339
Transfers payable	**86**	44
Accounts payable, accrued expenses and other liabilities	**2,467**	2,044
	$ 5,586	$ 5,814

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 both 2009 and 2008 to satisfy the $60,000,000 obligation. The Bank does not have to transfer any funds to the State's General Fund for the biennium beginning July 1, 2009 and ending June 30, 2011.

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.

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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 5% 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 is required to contribute 5.12% of each participant's salary as the employer's share. In addition to the 5.12% 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, 2011 and 2010 were approximately $754,000 and $710,000, 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.

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, 2011 and ending June 30, 2013 and in one case create a loan fund to provide low cost loans to individuals to repair their flood damaged homes. Following is a summary of legislative action and/or North Dakota Statute in effect:

H.B. 1003, Section 4 – Williston State College may borrow up to $1,725,000 for the workforce training building project.

H.B. 1004, Section 5 – The Department of Health, contingent on litigation and administrative proceedings, may borrow up to $500,000, the proceeds of which is appropriated for the purpose of defraying the expenses associated with possible litigation and other administrative proceedings involving the United States Environmental Protection Agency.

H.B. 1012, Section 4 – The Department of Transportation may borrow up to $200,000,000 for the purpose of providing funding for emergency relief projects on the state highway system. Any federal funding received for projects receiving funding under this section must be used to repay the loan.

H.B. 1015, Section 3 – The Department of Corrections and Rehabilitation may borrow up to $1,100,000 for the purpose of defraying the expenses of the penitentiary expansion project.

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H.B. 1021, Sections 4 & 6 – The Health Information Technology Office Director may request the Bank of North Dakota to transfer up to $8,000,000 to the Health Information Technology Loan Fund to meet any required match for federal funds or to the Electronic Health Information Exchange Fund to meet any required match for federal funds or for ongoing operating expenditures of the Health Information Exchange or as directed, a portion to both funds to meet any required match for federal funds. The Health Information Technology Office Director shall request fund transfers from the Bank only as necessary to comply with federal requirements and to meet cash flow needs of the funds. The Health Information Technology Office Director may request the Bank of North Dakota to transfer up to $5,000,000 to the Health Information Technology Planning Loan Fund. The Health Information Technology Office Director shall request transfers from the Bank only as necessary to meet cash flow needs of the fund. For the year ended December 31, 2011, the Bank had transferred $500,000 to this fund.

H.B. 1206, Section 2 – The Bank shall provide a loan of $50,000,000 to the Western Area Water Supply Authority for construction of a large water project in the western part of the state. The terms and conditions of the loan must be negotiated between the Bank and the Western Area Water Supply Authority, however, the term of the loan may not exceed seven years after June 30, 2014.

S.B. 2150, Section1 – The Department of Public Instruction may borrow the necessary funds to reimburse school districts for the excess cost 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 Superintendant of Public Instruction shall file for introduction legislation requesting the ensuing legislative assembly to return any amount transferred under this bill.

S.B. 2308, Section 3 – A line of credit not exceeding $2,560,000 shall be extended to the Highway Patrol to establish an online electronic permit system.

S.B. 2371, Section 7 – The Bank shall transfer up to $30,000,000 from its current earnings and undivided profits to the Rebuilders Loan Program Fund. For the year ended December 31, 2011, the Bank had transferred $2,229,000 to this fund.

State Water Commission

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 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.

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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, 2011 and 2010, the Bank has guarantees outstanding totaling $273,000 and $1,116,000, respectively. The Bank had no guarantee commitments outstanding as of December 31, 2011 and December 31, 2010 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 5% of the Bank's tier one capital as defined by the Department of Financial Institutions. A lender my apply to the Bank for a loan guarantee for a loan up to $200,000. The term of the guarantee may not exceed five years. As of December 31, 2011 and 2010, the Bank has guarantees outstanding totaling $4,963,000 and $4,045,000, respectively, and had guarantee commitments outstanding of $248,000 and $38,000, 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 was 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, 2011 and 2010, the Bank has guarantees outstanding totaling $743,000 and $850,000, respectively. The Bank had no guarantee commitments outstanding as of December 31, 2011 and December 31, 2010 included in commitments to extend credit.

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.

Dakota Education Alternative Loans are fully guaranteed by the North Dakota Guaranteed Student Loan Program which is administered by the Bank.

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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, 2011 and 2010, the following financial instruments were outstanding whose contract amounts represent credit risk:

	Contract Amount (In Thousands)	
	2011	2010
Commitments to extend credit	**$ 708,282**	$ 497,044
Financial standby letters of credit	**323,703**	360,878

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 holds collateral supporting those commitments.

Financial standby letters of credit include letters of credit pledged for public deposits by North Dakota banks for $210,086,000 and $257,270,000 at December 31, 2011 and 2010, respectively. These letters of credit are an authorized form of collateral for public deposits per North Dakota Century Code 21-04-09.

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 Accounting Standards Codification (ASC) 820-10, *Fair Value* Measurements. ASC 820-10 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.

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Fair Value Hierarchy

Under ASC 820-10, 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 ASC 820-10, 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 ASC 820-10.

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 (ASC 825-10 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.

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 ASC 825-10 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.

Continued on next page

The fair value estimates for ASC 825-10 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 based on market values as established by the secondary market.
- 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 loan 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.

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.

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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, 2011.

	(In Thousands)			
	Total	Level 1	Level 2	Level 3
Available-for-sale debt securities				
Mortgage-backed securities				
Agency	$ 124,189	$ 124,189	$ -	$ -
Collateralized mortgage obligations				
Agency	235,014	235,014	-	-
Non-agency	7,891		7,891	
Agency bonds	479,973	479,973	-	-
Corporate bonds	114,605	114,605	-	-
Municipal bonds	16,161	-	16,161	-
	977,833	953,781	24,052	-
FHLB stock	25,776	-	-	25,776
Nonmarketable equity securities	4,442	-	-	4,442
Total	$ 1,008,051	$ 953,781	$ 24,052	$ 30,218

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis, at December 31, 2011, are summarized as follows:

	Securities available for sale
Balance, beginning of year	$ 27,363
Purchases	4,440
Sales and maturities	(1,585)
Balance, end of year	$ 30,218

ASC 825-10, Disclosures about Fair Value of Financial Instruments

The table below is a summary of fair value estimates as of December 31, 2011 and 2010, for financial instruments, as defined by ASC 825-10. The carrying amounts in the following table are recorded in the balance sheet under the indicated captions. In accordance with ASC 825-10, 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.

Continued on next page

The carrying amounts and estimated fair values of the Bank's financial instruments as of December 31, 2011 and 2010 were as follows:

(In Thousands)

2011

	Carrying Amount	**Fair Value**	**Level 1**	**Level 2**	**Level 3**
Financial assets					
Cash and cash equivalents	**$ 1,369,370**	**$ 1,369,370**	**$ 1,369,370**	**$ -**	**$ -**
Securities available for sale	**1,008,051**	**1,008,051**	**953,781**	**24,052**	**30,218**
Interest receivable	**39,479**	**39,479**	**-**	**39,479**	**-**
Loans, net	**2,942,271**	**3,021,256**	**-**	**3,021,256**	**-**
Financial liabilities					
Non-maturity deposits	**$ 1,539,270**	**$ 1,539,270**	**$ -**	**$ 1,539,270**	**$ -**
Deposits with stated maturities	**2,640,567**	**2,564,873**	**-**	**2,564,873**	**-**
Federal funds purchased and repurchase agreements	**318,325**	**318,325**	**-**	**318,325**	**-**
Short and long-term debt	**471,422**	**526,017**	**-**	**526,017**	**-**
Other liabilities	**5,586**	**5,586**	**-**	**5,586**	**-**

2010

	Carrying Amount	Fair Value	Level 1	Level 2	Level 3
Financial assets					
Cash and cash equivalents	$ 671,200	$ 671,200	$ 671,200	$ -	$ -
Securities available for sale	537,157	537,157	489,223	20,571	27,363
Interest receivable	39,146	39,146	-	39,146	-
Loans, net	2,767,935	2,843,766	-	2,843,766	-
Financial liabilities					
Non-maturity deposits	$ 1,003,054	$ 1,003,054	$ -	$ 1,003,054	$ -
Deposits with stated maturities	2,055,672	2,071,554	-	2,071,554	-
Federal funds purchased and repurchase agreements	240,725	240,725	-	240,725	-
Short and long-term debt	397,365	420,601	-	420,601	-
Other liabilities	5,814	5,814	-	5,814	-

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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	
	2011	2010
Balance, beginning of year	**$ 568**	$ 1,683
Unrealized holding gains (losses) arising during the period	**3,345**	(1,115)
Other-than-temporary impaiment losses realized in net income	**1,800**	-
Reclassification adjustment for (gains) losses realized in net income	**(59)**	-
Other comprehensive income	**5,086**	(1,115)
Balance, end of year	**$ 5,654**	$ 568

NOTE 17 - SUPPLEMENTAL DISCLOSURES RELATED TO STATEMENTS OF CASH FLOWS

	(In Thousands)	
	2011	2010
Supplemental disclosures of cash flow information		
Cash payments for:		
Interest paid to customers	**$ 20,436**	$ 24,567
Interest paid on federal funds purchased and securities sold under repurchase agreements	**336**	913
Interest paid on short and long-term debt	**19,349**	19,835
Supplemental schedule of noncash investing and financing activities		
Transfers from undivided profits to other liabilities	**2,815**	5,088
Net change in unrealized gain (loss) on securities available for sale	**5,086**	(1,115)
Other real estate and property owned acquired in exchange for loans	**1,353**	453

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NOTE 18- SUBSEQUENT EVENTS

No significant events occurred subsequent to the Bank's year end. Subsequent events have been evaluated through February 28, 2012, which is the date these financial statements were available to be issued.

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TEN YEAR SUMMARY	2011	2010	2009	2008
OPERATING RESULTS (in thousands)				
Interest income	$137,459	$133,400	$132,277	$148,613
Interest expense	39,541	45,188	50,994	71,801
Net interest income	97,918	88,212	81,283	76,812
Provision for loan losses	11,000	12,100	10,300	8,900
Net interest income after provision for loan losses	86,918	76,112	70,983	67,912
Non-interest income	4,911	6,113	6,206	7,617
Non-interest expense	21,494	20,374	19,106	18,485
Net income	**70,335**	**61,851**	**58,083**	**57,044**
Payments to general fund	0	0	30,000	30,000
Payments to other funds	2,815	5,044	0	46
BALANCE SHEET - YEAR END (in thousands)				
TOTAL ASSETS	**5,375,073**	**4,029,927**	**3,959,669**	**3,516,965**
FEDERAL FUNDS SOLD AND RESELL AGREEMENTS	18,315	33,100	24,190	75,675
SECURITIES	1,008,051	537,157	397,370	331,416
LOANS	**2,995,154**	**2,814,548**	**2,713,611**	**2,618,402**
Student	1,062,534	1,044,442	932,323	776,473
Commercial	1,068,598	1,022,002	1,038,589	1,064,811
Residential	575,020	471,411	475,124	509,052
Agriculture	289,002	276,693	267,575	268,066
DEPOSITS	**4,179,837**	**3,058,726**	**2,939,059**	**2,645,356**
Non-interest bearing	649,922	387,040	442,867	313,900
Interest bearing	3,529,915	2,671,686	2,496,192	2,331,456
FEDERAL FUNDS PURCHASED AND REPURCHASE AGREEMENTS	318,325	240,725	337,627	304,020
SHORT AND LONG-TERM DEBT	471,422	397,365	405,005	315,604
EQUITY	**399,903**	**327,297**	**271,649**	**223,922**
Capital	2,000	2,000	2,000	2,000
Capital surplus	42,000	42,000	42,000	42,000
Undivided profits	350,249	282,729	225,966	182,883
Accumulated other comprehensive income (loss)	5,654	568	1,683	(2,961)

Continued on next page

Bank of North Dakota
Ten Year Summary

2007	2006	2005	2004	2003	2002	2001
$152,416	$ 126,598	$ 98,086	$ 80,133	$ 79,463	$ 90,315	$ 114,490
87,090	71,284	51,623	38,392	41,755	50,666	82,840
65,326	55,314	46,463	41,741	37,708	39,649	41,650
3,100	3,400	2,400	2,400	2,000	2,200	2,700
62,226	51,914	44,063	39,341	35,708	37,449	38,950
6,673	7,748	9,332	11,248	11,474	9,764	8,646
17,813	16,808	17,038	16,373	15,488	15,022	14,537
51,086	**42,854**	**36,357**	**34,216**	**31,694**	**32,191**	**33,059**
30,000	30,000	30,000	30,000	34,000	30,000	50,000
46	43	43	37	37	36	36
2,779,360	**2,326,693**	**2,062,247**	**2,014,525**	**1,953,178**	**1,974,448**	**2,107,456**
277,565	129,135	195,370	122,230	89,915	209,205	257,830
235,551	219,412	157,623	253,186	284,272	235,365	329,632
2,004,999	**1,755,562**	**1,467,061**	**1,456,256**	**1,391,583**	**1,329,985**	**1,276,334**
643,297	561,178	459,287	417,356	372,362	364,816	399,002
689,150	564,946	431,068	480,870	469,912	432,940	392,206
419,700	388,043	342,786	322,044	318,067	309,267	271,385
252,852	241,395	233,920	235,986	231,242	222,962	213,741
1,871,767	**1,617,136**	**1,352,516**	**1,198,586**	**1,057,386**	**1,070,853**	**1,208,601**
317,949	230,993	205,854	208,277	214,275	209,112	193,354
1,553,818	1,386,143	1,146,662	990,309	843,111	861,741	1,015,247
434,061	249,145	248,932	201,959	190,597	296,688	315,713
245,070	257,209	275,926	436,593	525,795	421,065	399,553
192,471	**163,542**	**161,824**	**152,776**	**153,744**	**149,113**	**170,496**
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
145,843	119,894	119,894	110,947	110,947	104,237	126,237
2,628	(352)	(2,070)	(2,171)	(1,203)	876	259

BND

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