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FIRST INTERSTATE BANCSYSTEM INC

Form 10-K405

March 29, 2002

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON D.C. 20549
FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF
1934. FOR THE FISCAL YEAR ENDED DECEMBER 31, 2001

COMMISSION FILE NUMBER: 33-64304

FIRST INTERSTATE BANCSYSTEM, INC.

(Exact name of registrant as specified in its charter)

MONTANA
(State or other jurisdiction of
incorporation or organization)

81-0331430
(IRS Employer
Identification No.)

401 NORTH 31ST STREET
BILLINGS, MONTANA
(Address of principal executive offices)

59116
(Zip Code)

(406) 255-5390
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant: (1) has filed all reports
required to be filed by Section 13 or 15(d) of the Securities Exchange Act of
1934 during the preceding 12 months (or for such shorter period that the
registrant was required to file such reports), and (2) has been subject to such
filing requirements for the past 90 days. |X| Yes | | No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405
of Regulation S-K is not contained herein, and will not be contained, to the
best of the registrant's knowledge, in definitive proxy or information
statements incorporated by reference in Part III of this Form 10-K or any
amendment to this Form 10-K. |X|

The aggregate market value (appraised minority value) of the common stock of the
registrant held by non-affiliates of the registrant as of March 1, 2002 was
\$43.00.

The number of shares outstanding of the registrant's common stock as of February
28, 2002 was 7,844,056.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the 2002 definitive Proxy Statement for the Annual Meeting of
Shareholders scheduled to be held May 17, 2002 are incorporated by reference
into Part III of this Form 10-K.

PART I

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ITEM 1. BUSINESS

THE COMPANY

First Interstate BancSystem, Inc. ("FIBS" and collectively with its subsidiaries, the "Company"), incorporated in Montana in 1971, is a financial holding company registered under the Bank Holding Company Act of 1956, as amended. FIBS is headquartered in Billings, Montana. At December 31, 2001, the Company had assets of \$3.3 billion, deposits of \$2.7 billion and total stockholders' equity of \$222 million, making it the largest banking organization in Montana.

FIBS operates a wholly-owned bank subsidiary, First Interstate Bank (the "Bank"), with 56 banking offices in 30 Montana and Wyoming communities. The Bank, a Montana corporation organized in 1916, delivers a comprehensive range of loan, deposit and investment products and, mortgage banking and trust services to meet the needs of individual customers, businesses, and municipalities.

The Company conducts various other financial-related business activities through wholly-owned non-bank subsidiaries. During 2000, the Company incorporated its technology services division into a separate subsidiary, i_Tech Corporation ("i_Tech"). i_Tech provides technology services to the Bank and to 149 non-affiliated financial institutions in Montana, Wyoming, Idaho, Washington, Oregon and Colorado. Additionally, i_Tech's ATM network provides processing support for over 2,850 ATM locations in 32 states. FIB Capital Trust ("FIB Capital"), incorporated under Delaware law in 1997, was formed for the exclusive purpose of issuing mandatorily redeemable trust preferred securities ("trust preferred securities") and using the proceeds to purchase junior subordinated debentures ("subordinated debentures") issued by FIBS. Commerce Financial, Inc. ("CFI") was incorporated in 1978. CFI's principal activity has been the liquidation of assets acquired through foreclosure actions by FIBS. FI Reinsurance, Ltd. ("FIR"), domiciled in Nevis Island, West Indies, was formed in 2001 to underwrite, as reinsurer, credit-related life and disability insurance.

The Company is the licensee under a trademark license agreement granting it an exclusive, nontransferable license to use the "First Interstate" name and logo in Montana, Wyoming and surrounding states.

COMMUNITY BANKING PHILOSOPHY

The banking industry continues to experience change with respect to regulatory matters, consolidation, consumer needs and economic and market conditions. The Company believes that it can best address this changing environment through its "Strategic Vision." The Company's Strategic Vision emphasizes providing its customers full service commercial and consumer banking at a local level using a personalized service approach, while serving and strengthening the communities in which the Bank is located through community service activities.

The Company grants significant flexibility to its banking offices in delivering and pricing products at a local level in response to market considerations and customer needs. This flexibility enables the banking offices to remain competitive and enhances the relationships between the banking offices and the customers they serve. The Company also emphasizes accountability, however, by establishing performance and incentive standards that are tied to net income and other success measures at the individual banking office and market level. The Company believes this combination of flexibility and accountability allows the banking offices to provide personalized customer service while remaining attentive to financial performance.

The Company has centralized certain products and business activities to provide consistent service levels to customers Company-wide, to gain efficiency

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in management of those products and activities and to ensure regulatory compliance. Centralized products and activities include trust, investment, wire transfer, escrow, credit card, technology and escrow services, mortgage servicing, and selected operational activities.

GROWTH STRATEGY

The Company's growth strategy includes growing internally and expanding into new and complementary markets when appropriate opportunities arise. The Company believes it has in place an infrastructure that will allow for growth and provide economies of scale into the future.

-2-

During 2000, the Company acquired Equality State Bankshares, Inc. ("ESB"), a bank holding company with three banking offices. At the date of acquisition, ESB has loans of \$64 million and deposits of \$80 million. For additional information regarding acquisitions, see "Notes to Consolidated Financial Statements - Acquisitions" included in Part IV, Item 14.

The Company has opened 18 new banking offices in Montana and Wyoming since 1998. Among these new offices are 12 full service banking offices located inside retail establishments. The Company intends to continue to expand its presence in the Montana and Wyoming markets through the opening of new banking offices. The Company currently plans to open four additional banking offices in Montana and Wyoming through 2003.

Beginning in 1999, the Company accelerated its investment in information systems and staff to support the continued growth of its technology services subsidiary, i_Tech. During 2001, i_Tech opened new item capture facilities in Idaho and Colorado. i_Tech intends to continue to expand into new market areas through aggressive sales efforts.

THE BANK

During 2001, the Company merged its two bank charters, First Interstate Bank in Montana and First Interstate Bank in Wyoming. The resulting bank, First Interstate Bank ("FIB" or the "Bank"), is headquartered in Billings, Montana.

The Company's banking offices are located in communities of approximately 700 to 90,000 people, but serve larger market areas due to the limited number of financial institutions in other nearby communities. The Company believes that the communities served provide a stable core deposit and funding base, as well as economic diversification across a number of industries, including agriculture, energy, mining, timber processing, tourism, government services, education and medical services.

CENTRALIZED SERVICES

FIBS and i_Tech provide general oversight and centralized services for the Bank to enable it to serve its markets more effectively. These services include technology services, credit administration, finance and accounting, human asset management and other support services.

Technology Services. i_Tech provides technology services to the Bank, including system support of the general ledger, investment security, loan, deposit, web banking, imaging, management reporting, cash management and e-mail systems. i_Tech also manages the Company's wide-area network and the ATM network used by the Bank and provides item proof and capture services. These technology services are performed through the use of computer hardware owned and maintained

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by the Bank and software licensed by i_Tech.

Credit Administration. FIBS monitors the lending activities of the Bank to maximize the quality and mix of loans, provides centralized loan approval for the Bank's larger loans, evaluates the risk inherent in the Bank's loan portfolio and assists in determining the loan loss reserve including specific reserve allocations.

Finance and Accounting. FIBS provides financial and accounting services for the Bank, including internal and external reporting, asset/liability management, investment portfolio analysis and capital management.

Human Asset Management. Through its human asset management group, FIBS provides the Bank with incentive and employee benefit administration and compensation, training, employee recruitment and hiring services.

Other Support Services. FIBS provides the Bank with legal, compliance, internal auditing, marketing and sales services, general administration and various other support services.

-3-

LENDING ACTIVITIES

FIBS has comprehensive credit policies establishing Company-wide underwriting and documentation standards to assist Bank management in the lending process and limit risk to the Company. The credit policies establish lending authorities based on the experience level and authority of the lending officer, the type of loan and the type of collateral. The policies also establish thresholds at which loan requests must be approved by a Bank committee and/or by FIBS.

The Bank offers short and long-term real estate, consumer, commercial, agricultural and other loans to individuals and small to medium sized businesses in its market areas. While each loan must meet minimum underwriting standards established in the Company's credit policies, lending officers are granted certain levels of flexibility in approving and pricing loans to assure that the banking offices are responsive to competitive issues and community needs in each market area.

Real Estate Loans. The Bank provides interim and permanent financing for both single-family and multi-unit properties, medium term loans for commercial, agricultural and industrial property and/or buildings, and equity lines of credit secured by real estate. The Bank originates variable and fixed rate real estate mortgages, generally in accordance with the guidelines of the Fannie Mae and the Federal Home Loan Mortgage Corporation. Loans originated in accordance with these guidelines are sold in the secondary market. Real estate loans not sold in the secondary market are typically secured by first liens on the financed property and generally mature in less than 15 years.

Consumer Loans. The Bank's consumer loans include personal loans, credit card loans and equity lines of credit. Personal loans are generally secured by automobiles, boats and other types of personal property and are made on an installment basis. Credit cards are offered to customers in the Company's market areas. Equity lines of credit are generally floating rate, reviewed annually and secured by real property. Approximately 60% of the Company's consumer loans are indirect dealer paper that is created when the Company purchases consumer loan contracts advanced for the purchase of automobiles, boats and other consumer goods from consumer products dealers.

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Commercial Loans. The Bank provides a mix of variable and fixed rate commercial loans. The loans are typically made to small and medium sized manufacturing, wholesale, retail and service businesses for working capital needs and business expansions. Commercial loans generally include lines of credit and loans with maturities of five years or less. The loans are generally made with the business operations as the primary source of repayment, but also include collateralization by inventory, accounts receivable, equipment and/or personal guarantees.

Agricultural Loans. The Bank's agricultural loans generally consist of short and medium-term loans and lines of credit that are generally used for crops, livestock, equipment and general operating purposes. Agricultural loans are generally secured by assets such as livestock or equipment and are repaid from the operations of the farm or ranch. Agricultural loans generally have maturities of five years or less, with operating lines for one production season.

For additional information about the Company's loan portfolio, see Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Loans."

FUNDING SOURCES

The Bank offers traditional depository products including checking, savings and time deposits. Additional funding sources include federal funds purchased for one day periods, repurchase agreements with primarily commercial depositors, time deposits brokered outside the Company's market areas and short-term borrowings from the Federal Home Loan Bank of Seattle. Deposits at the Bank are insured by the Federal Deposit Insurance Corporation ("FDIC") up to statutory limits.

Under repurchase agreements, the Company sells investment securities held by the Company to a customer under an agreement to repurchase the investment security at a specified time or on demand. The Company does not, however, physically transfer the investment securities. As of December 31, 2001, all outstanding repurchase agreements were due in one day.

-4-

For additional information on the Banks' funding sources, see Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Deposits" and Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Other Borrowed Funds."

COMPETITION

Competition within Montana and Wyoming for banking and related business is strong. The Bank competes with both state and nationally chartered commercial banks for deposits, loans and trust accounts, and with savings and loan associations, savings banks and credit unions for deposits and loans. In addition, there is significant competition with other financial institutions including personal loan companies, mortgage banking companies, finance companies, insurance companies, securities firms, mutual funds and certain government agencies as well as major retailers all actively engaged in providing various types of loans and other financial services.

While historically the technology services industry has been highly decentralized, there is an accelerating trend toward consolidation resulting in fewer companies competing over larger geographic regions. i_Tech's competitors

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vary in size and include national, regional and local operations.

EMPLOYEES

At December 31, 2001, the Company employed 1,494 full-time equivalent employees. None of the Company's employees are covered by a collective bargaining agreement. The Company considers its employee relations to be good.

REGULATION AND SUPERVISION

Financial holding companies and commercial banks are subject to extensive regulation under both federal and state law. Set forth below is a summary description of certain laws that relate to the regulation of FIBS and the Bank. The description does not purport to be complete and is qualified in its entirety by reference to the applicable laws and regulations.

First Interstate BancSystem, Inc.

As a financial holding company, FIBS is subject to regulation under the Bank Holding Company Act of 1956, as amended (the "BHCA"), and to supervision and regulation by the Federal Reserve.

Under Federal Reserve regulations, a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, it is the Federal Reserve's policy that in serving as a source of strength to its subsidiary banks, a bank holding company should stand ready to use available resources to provide adequate capital funds to its subsidiary banks during periods of financial stress or adversity and should maintain the financial flexibility and capital-raising capacity to obtain additional resources for assisting its subsidiary banks. A bank holding company's failure to meet its obligations to serve as a source of strength to its subsidiary banks will generally be considered by the Federal Reserve to be an unsafe and unsound banking practice or a violation of the Federal Reserve's regulations or both.

FIBS is required to obtain the prior approval of the Federal Reserve for the acquisition of 5% or more of the outstanding shares of any class of voting securities or substantially all of the assets of any bank or bank holding company. Prior approval of the Federal Reserve is also required for the merger or consolidation of FIBS and another bank holding company.

As a financial holding company, FIBS may engage in certain business activities that are financial in nature or incidental to financial activities as well as all activities authorized to bank holding companies. FIBS may engage in financial activities provided that it remains a financial holding company and meets certain regulatory standards of being well-capitalized and well-managed. FIBS must notify the Federal Reserve of its financial activities within a specified time period following its initial engagement in each business or activity.

-5-

The Bank

FIB is subject to the supervision of and regular examination by the Federal Reserve and the State of Montana. If either of the foregoing regulatory agencies determines that the financial condition, capital resources, asset quality, earning prospects, management, liquidity or other aspects of a bank's operations are unsatisfactory or that a bank or its management is violating or has violated any law or regulation, various remedies are available to such

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agencies. These remedies include the power to enjoin "unsafe or unsound" practices, to require affirmative action to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in capital, to restrict the growth of a bank, to assess civil monetary penalties, to remove officers and directors and to terminate a bank's deposit insurance, which would result in a revocation of a bank's charter. The Bank has not been the subject of any such actions by regulatory agencies.

The FDIC insures the deposits of the Bank in the manner and to the extent provided by law. For this protection, the Bank pays a semiannual statutory assessment. See "Premiums for Deposit Insurance" herein.

Restrictions on Transfers of Funds to FIBS and the Bank

A large portion of FIBS's revenues are, and will continue to be, dividends paid by the Bank. The Bank is limited, under both state and federal law, in the amount of dividends that may be paid from time to time. In general, the Bank is limited, without the prior consent of its state and federal banking regulators, to paying dividends that do not exceed the current year net profits together with retained earnings from the two preceding calendar years.

A state or federal banking regulator may impose, by regulatory order or agreement of the Bank, specific regulatory dividend limitations or prohibitions in certain circumstances. The Bank is not subject to a specific regulatory dividend limitation other than generally applicable limitations. In addition to regulatory dividend limitations, the Bank dividends are, in certain circumstances, limited by covenants in FIBS's debt instruments.

Financial transactions between the Bank and FIBS are also limited under applicable state and federal law and regulations. The Bank may not lend funds to, or otherwise extend credit to or for the benefit of, FIBS or FIBS affiliates, except on specified types and amounts of collateral and other terms.

Effect of Government Policies and Legislation

Banking depends on interest rate differentials. In general, the difference between the interest rate paid by the Bank on deposits and borrowings and the interest rate received by the Bank on loans extended to customers and on investment securities comprises a major portion of the Bank's earnings. These rates are highly sensitive to many factors that are beyond the control of the Bank. Accordingly, the earnings and potential growth of the Bank is subject to the influence of domestic and foreign economic conditions, including inflation, recession and unemployment.

The commercial banking business is not only affected by general economic conditions but is also influenced by the monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Federal Reserve. The Federal Reserve implements national monetary policies (with objectives such as curbing inflation and combating recession) by its open-market operations in United States government securities, by adjusting the required level of reserves for financial institutions subject to the Federal Reserve's reserve requirements and by varying the discount rates applicable to borrowings by depository institutions. The actions of the Federal Reserve in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. The nature and impact of any future changes in monetary policies cannot be predicted.

From time to time, legislation is enacted which has the effect of increasing the cost of doing business, limiting or expanding permissible activities or affecting the competitive balance between banks and other financial service providers. Proposals to change the laws and regulations

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governing the operations and taxation of banks, bank holding companies and other financial service providers are frequently made in Congress, in the Montana and Wyoming legislatures and before various bank regulatory and other professional agencies. The likelihood of any major legislative changes and the impact such changes might have on FIBS or the Bank are impossible to predict.

-6-

Capital Standards

The federal banking agencies have adopted minimum capital requirements for insured banks that are applicable to the Bank. In addition, the Federal Reserve has adopted minimum capital requirements that are applicable to FIBS. The capital requirements are intended to, among other things, provide a means for evaluating the capital adequacy and soundness of the institutions. The Federal banking agencies may also set higher capital requirements for particular institutions in specified circumstances under Federal laws and regulations.

At December 31, 2001, the Bank and FIBS each met the "well-capitalized" requirements applicable to the respective institution. The "well-capitalized" standard is the highest level of the minimum capital requirements established by the Federal agencies. Neither the Bank nor FIBS is subject to a minimum capital requirement other than those applicable to banks or bank holding companies generally.

For more information concerning the capital ratios of FIBS, see Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Capital Resources" and "Notes to Consolidated Financial Statements - Regulatory Capital" included in Part IV, Item 14.

Compliance and Safety and Soundness Standards

The federal banking agencies have adopted guidelines establishing standards for safety and soundness, asset quality, and earnings, as required by the Federal Deposit Insurance Corporation Improvement Act ("FDICIA"). These standards are designed to identify potential concerns and ensure that action is taken to address those concerns before they pose a risk to the deposit insurance fund. If a federal banking agency determines that an institution fails to meet any of these standards, the agency may require the institution to submit an acceptable plan to achieve compliance with the standard. If the institution fails to submit an acceptable plan within the time allowed by the agency or fails in any material respect to implement an accepted plan, the agency must, by order, require the institution to correct the deficiency.

Premiums for Deposit Insurance

Deposits in the Bank are insured by the FDIC in accordance with the Federal Deposit Insurance Act (the "FDIA"). Insurance premiums are assessed semiannually by the FDIC at a level sufficient to maintain the insurance reserves required under the FDIA and relevant regulations. The insurance premium charged to a bank is determined based upon risk assessment criteria, including relevant capital levels, results of bank examinations by state and federal regulators, and other information. The Bank currently is assessed the most favorable deposit insurance premiums under the risk-based premium system.

Community Reinvestment Act and Fair Lending Developments

The Bank is subject to certain fair lending requirements and reporting obligations involving home mortgage lending operations and Community Reinvestment Act ("CRA") activities. The CRA generally requires the federal

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banking agencies to evaluate the record of a financial institution in meeting the credit needs of its local communities, including low and moderate income neighborhoods. In addition to substantial penalties and corrective measures that may be required for a violation of certain fair lending laws, the federal banking agencies may take compliance with such laws and CRA into account when regulating and supervising other activities or in authorizing expansion activities by the Bank and FIBS.

In connection with its assessment of CRA performance, the appropriate bank regulatory agency assigns a rating of "outstanding," "satisfactory," "needs to improve" or "substantial noncompliance." FIB received an "outstanding" rating on its most recent examination.

-7-

RISK FACTORS

Asset Quality

A significant source of risk for the Company arises from the possibility that losses will be sustained by the Bank because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. The Company has adopted underwriting and credit monitoring procedures and credit policies, including the establishment and review of the allowance for loan losses, that management believes are appropriate to mitigate this risk by assessing the likelihood of nonperformance, monitoring loan performance and diversifying the Company's credit portfolio. Such policies and procedures, however, may not prevent unexpected losses that could have a material adverse effect on the Company's business, financial condition and results of operations. See "Business - Lending Activities."

Interest Rate Risk

Banking companies' earnings depend largely on the relationship between the yield on earning assets, primarily loans and investments, and the cost of funds, primarily deposits and borrowings. This relationship, known as the interest rate spread, is subject to fluctuation and is affected by economic and competitive factors which influence interest rates, the volume and mix of interest earning assets and interest bearing liabilities and the level of non-performing assets. Fluctuations in interest rates affect the demand of customers for the Company's products and services. The Company is subject to interest rate risk to the degree that its interest bearing liabilities reprice or mature more slowly or more rapidly or on a different basis than its interest earning assets. Significant fluctuations in interest rates could have a material adverse effect on the Company's business, financial condition, results of operations or liquidity.

For additional information regarding interest rate risk, see Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations - Financial Condition - Liquidity and Cash Flow."

Economic Conditions; Limited Geographic Diversification

The Company's banking operations are located in Montana and Wyoming. As a result of the geographic concentration of its operations, the Company's results depend largely upon economic conditions in these areas. Although markets served by the Company are economically diverse, a deterioration in economic conditions could adversely impact the quality of the Company's loan portfolio and the demand for its products and services, and accordingly, could have a material adverse effect on the Company's business, financial condition, results of

operations or liquidity.

Ability of the Company to Execute Its Business Strategy

The financial performance and profitability of the Company will depend on its ability to execute its business strategy and manage its future growth. Although the Company believes that it has substantially integrated recently acquired banks into the Company's operations, there can be no assurance that unforeseen issues relating to the assimilation or prior operations of these banks, including the emergence of any material undisclosed liabilities, will not materially adversely affect the Company. In addition, any future acquisitions or other future growth may present operating and other problems that could have a material adverse effect on the Company's business, financial condition, results of operations or liquidity. The Company's financial performance will also depend on the Company's ability to maintain profitable operations through implementation of its Strategic Vision. Moreover, the Company's future performance is subject to a number of factors beyond its control, including pending and future federal and state banking legislation, regulatory changes, unforeseen litigation outcomes, inflation, lending and deposit rate changes, interest rate fluctuations, increased competition and economic conditions. Accordingly, there can be no assurance that the Company will be able to continue the growth or maintain the level of profitability it has recently experienced.

-8-

Dependence on Key Personnel

The Company's success depends to a significant extent on the management skills of its existing executive officers and directors, many of whom have held officer and director positions with the Company for many years. The loss or unavailability of any of its key executives, including Thomas W. Scott, Chief Executive Officer, Lyle R. Knight, President and Chief Operating Officer, Terrill R. Moore, Senior Vice President and Chief Financial Officer, or Ed Garding, Senior Vice President and Chief Credit Officer could have a material adverse effect on the Company's business, financial condition, results of operations or liquidity. See Part III, Item 10, "Directors and Executive Officers of Registrant."

Competition

Several competitors are much larger in total assets and capitalization, have greater access to capital markets and offer a broader array of financial services than the Bank. Moreover, the Banking and Branching Act has increased competition in the Bank's markets, particularly from larger, multi-state banks. There can be no assurance that the Company will be able to compete effectively in its markets. Furthermore, developments increasing the nature or level of competition could have a material adverse effect on the Company's business, financial condition, results of operations or liquidity. See "Business - Competition" and "Business - Regulation and Supervision."

Government Regulation and Monetary Policy

The Company and the banking industry are subject to extensive regulation and supervision under federal and state laws and regulations. The restrictions imposed by such laws and regulations limit the manner in which the Company conducts its banking business, undertakes new investments and activities and obtains financing. This regulation is designed primarily for the protection of the deposit insurance funds and consumers and not to benefit holders of the Company's securities. Financial institution regulation has been the subject of significant legislation in recent years and may be the subject of further

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significant legislation in the future, none of which is in the control of the Company. Significant new laws or changes in, or repeals of, existing laws could have a material adverse effect on the Company's business, financial condition, results of operations or liquidity. Further, federal monetary policy, particularly as implemented through the Federal Reserve System, significantly affects credit conditions for the Company, and any unfavorable change in these conditions could have a material adverse effect on the Company's business, financial condition, results of operations or liquidity. See "Business-Regulation and Supervision."

Control by Affiliates

The directors and executive officers of the Company beneficially own 48.77% of the outstanding common stock of the Company. Many of these directors and executive officers are members of the Scott family, which collectively owns 80.86% of the outstanding common stock. By virtue of such ownership, these affiliates are able to control the election of directors and the determination of the Company's business, including transactions involving any merger, share exchange, sale of assets outside the ordinary course of business and dissolution.

Lack of Trading Market; Market Prices

The common stock of FIBS is not actively traded, and there is no established trading market for the stock. There is only one class of common stock, with 91.73% of the shares subject to contractual transfer restrictions set forth in shareholder agreements and 8.27% without such restrictions. FIBS has the right to acquire some or all the restricted stock at fair market value per share determined as the minority appraised value per share based upon the most recent quarterly appraisal available to FIBS. All stock not subject to such restrictions may be sold at a price per share that is acceptable to the shareholder. FIBS has no obligation to purchase unrestricted stock, but has historically purchased such stock in order to reduce the amount of its stock not subject to transfer restrictions. During 2001, the Company repurchased 20,050 shares of its unrestricted stock from participants in the Savings and Profit Sharing Plan for Employees of First Interstate BancSystem, Inc. ("Savings Plan"). All shares were repurchased at the most recent minority appraised value at the repurchase date.

The appraised minority value of the FIBS common stock represents the estimated fair market valuation of a minority block of such stock, taking into account adjustments for the lack of marketability of the stock and other factors. This value does not represent an actual trading price between a willing buyer and seller of the FIBS common stock in an informed, arm's-length transaction. As such, the appraised minority value is only an estimate as of a

-9-

specific date, and there can be no assurance that such appraisal is an indication of the actual value holders of the FIBS common stock may realize with respect to shares held by them. Moreover, the estimated fair market value of the FIBS common stock may be materially different at any date other than the valuation dates.

FIBS has no obligation, by contract, policy or otherwise to purchase stock from any shareholder desiring to sell, or to create any market for the stock. Historically, it has been the practice of FIBS to repurchase common stock to maintain a shareholder base with restrictions on sale or transfer of the stock. In the last three calendar years (1999-2001), FIBS has repurchased a total of 382,573 shares of common stock, 362,523 of which were restricted by the

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shareholder agreements. FIBS repurchased the stock at the price determined in accordance with the shareholder agreements. FIBS's repurchases of stock are subject to corporate law and regulatory restrictions that could prevent stock repurchases. See also Part II, Item 5, "Market for Registrant's Common Equity and Related Stockholder Matters."

There is a limited public market for the trust preferred securities. Future trading prices of the trust preferred securities depend on many factors including, among other things, prevailing interest rates, the operating results and financial condition of the Company and the market for similar securities. As a result of the existence of FIBS's right to defer interest payments on or, subject to prior approval of the Federal Reserve if then required under applicable capital guidelines or policies of the Federal Reserve, shorten the stated maturity of the subordinated debentures, the market price of the trust preferred securities may be more volatile than the market prices of subordinated debentures that are not subject to such optional deferrals or reduction in maturity. There can be no assurance as to the market prices for the trust preferred securities or the subordinated debentures that may be distributed in exchange for the trust preferred securities if the Company exercises its right to dissolve FIB Capital.

Forward-Looking Statements

Certain statements contained in this document including, without limitation, statements containing the words "believes," "anticipates," "expects," and words of similar import, constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include, among others, the following: general economic and business conditions in those areas in which the Company operates; demographic changes; competition; fluctuations in interest rates; changes in business strategy or development plans; changes in governmental regulation; credit quality; the availability of capital to fund the expected expansion of the Company's business; and other factors referenced in this document, including, without limitation, information under the captions "Risk Factors" and Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations." Given these uncertainties, shareholders, trust preferred security holders and prospective investors are cautioned not to place undue reliance on such forward-looking statements. The Company disclaims any obligation to update any such factors or to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

ITEM 2. PROPERTIES

The Company is the anchor tenant in a commercial building in which the Company's principal executive offices are located in Billings, Montana. The building is owned by a joint venture partnership in which FIB is one of the two partners, owning a 50% interest in the partnership. As of December 31, 2001, the Company leases approximately 68,087 square feet of space for operations in the building. The Company also leases space for operations, technology services, and 21 banking offices in 27 buildings. All other banking offices are located in Company-owned facilities.

ITEM 3. LEGAL PROCEEDINGS

In the normal course of business, the Company is named or threatened to be named as a defendant in various lawsuits. In the opinion of management, following consultation with legal counsel, the pending lawsuits are without

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merit or, in the event the plaintiff prevails, the ultimate liability or disposition thereof will not have a material adverse effect on the Company's business, financial condition, results of operations or liquidity.

-10-

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

DESCRIPTION OF FIBS CAPITAL STOCK

The authorized capital stock of FIBS consists of 20,000,000 shares of common stock without par value, of which 7,848,704 shares were outstanding as of December 31, 2001, and 100,000 shares of preferred stock without par value, none of which were outstanding as of December 31, 2001.

Common Stock

Each share of the common stock is entitled to one vote in the election of directors and in all other matters submitted to a vote of stockholders. Accordingly, holders of a majority of the shares of common stock entitled to vote in any election of directors may elect all of the directors standing for election if they choose to do so, subject to the rights of the holders of the preferred stock. Voting for directors is noncumulative.

Subject to the preferential rights of any preferred stock that may at the time be outstanding, each share of common stock has an equal and ratable right to receive dividends when, if and as declared by the Board of Directors out of assets legally available therefore. In the event of a liquidation, dissolution or winding up of the Company, the holders of common stock will be entitled to share equally and ratably in the assets available for distribution after payments to creditors and to the holders of any preferred stock that may at the time be outstanding. Holders of common stock have no conversion rights or preemptive or other rights to subscribe for any additional shares of common stock or for other securities. All outstanding common stock is fully paid and non-assessable.

The common stock of FIBS is not actively traded, and there is no established trading market for the stock. There is only one class of common stock, with 91.73% of the shares subject to contractual transfer restrictions set forth in shareholder agreements and 8.27% held by 16 shareholders without such restrictions, including the Company's 401(k) plan which holds 76.51% of the unrestricted shares. See also Part I, Item 1, "Risk Factors - Lack of Trading Market; Market Prices."

Quarter-end minority appraisal values for the past two years, determined by Alex Sheshunoff & Co. Investment Banking are as follows:

Valuation As Of -----	Appraised Minority Value -----
December 31, 1999	\$ 40.00

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March 31, 2000	39.00
June 30, 2000	38.00
September 30, 2000	38.00
December 31, 2000	39.00
March 31, 2001	39.00
June 30, 2001	40.00
September 30, 2001	42.00
December 31, 2001	43.00

As of December 31, 2001, options for 24,170 shares of the FIBS common stock were outstanding at various exercise prices, ranging from \$7.61 to \$42.00. The aggregate cash proceeds to be received by FIBS upon exercise of all options outstanding at December 31, 2001 would be \$638,334, or a weighted average exercise price of \$26.41 per share.

The appraised minority value as of December 31, 2001 was \$43.00. See also Part I, Item 1, "Risk Factors - Lack of Trading Market; Market Prices."

-11-

Resale of FIBS stock may be restricted pursuant to the Securities Act of 1933 and applicable state securities laws. In addition, most shares of FIBS stock are subject to shareholder's agreements:

- Members of the Scott family, as majority shareholders of FIBS, are subject to a shareholder's agreement ("Scott Agreement"). The Scott family, under the Scott Agreement, has agreed to limit the transfer of shares owned by members of the Scott family to family members or charities, or with FIBS's approval, to the Company's officers, directors, advisory directors, or to the Company's Savings Plan.
- Shareholders of the Company who are not Scott family members, with the exception of 16 shareholders who own an aggregate of 648,799 shares of unrestricted stock, are subject to shareholder's agreements ("Shareholder's Agreement"). Stock subject to the Shareholder's Agreement may not be sold or transferred without triggering the Company's option to acquire the stock in accordance with the terms of the Shareholder's Agreement. In addition, the Shareholder's Agreement grants the Company the right to repurchase all or some of the stock at any time.

Purchases of FIBS common stock made through the Company's Savings Plan are not restricted by the Shareholder's Agreement, due to requirements of Employee Retirement Income Security Act ("ERISA") and the Internal Revenue Code. However, since the Savings Plan does not allow distributions "in kind," any distributions from an employee's account in the Savings Plan will allow, and may require, the Trust Department of FIB (the "Plan Trustee"), to sell the FIBS stock. While FIBS has no obligation to repurchase the stock, it is possible that FIBS will repurchase FIBS stock sold by the Savings Plan. Any such repurchases would be upon terms set by the Plan Trustee and accepted by FIBS.

There are 531 record shareholders of FIBS as of December 31, 2001, including the Company's Savings Plan as trustee for 496,407 shares held on behalf of 876 individual participants in the plan. 246 individuals in the Savings Plan also own shares of FIBS stock outside of the Plan. The Plan Trustee votes the shares based on the instructions of each participant. In the event the participant does not provide the Plan Trustee with instructions, the Plan

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Trustee votes those shares in accordance with voting instructions received from a majority of the participants in the Plan.

Dividends

It is the policy of FIBS to pay a dividend to all common shareholders quarterly. Dividends are declared and paid in the month following the calendar quarter and the amount has historically been determined based upon a percentage of net income for the calendar quarter immediately preceding the dividend payment date. Since 1996, the Company has paid dividends of approximately 30% of quarterly net income without taking into effect compensation expense or benefit related to stock options. The Board of Directors of FIBS has no current intention to change its dividend policy, but no assurance can be given that the Board may not, in the future, change or eliminate the payment of dividends.

Historical quarterly dividends for 2000 and 2001 are as follows:

Quarter	Month Declared and Paid	Amount Per Share	Total Cash Dividend
-----	-----	-----	-----
1st quarter 2000	April 2000	\$.27	\$ 2,142,112
2nd quarter 2000	July 2000	.28	2,216,554
3rd quarter 2000	October 2000	.30	2,373,769
4th quarter 2000	January 2001	.28	2,209,055
1st quarter 2001	April 2001	.25	1,966,110
2nd quarter 2001	July 2001	.31	2,427,846
3rd quarter 2001	October 2001	.34	2,676,300
4th quarter 2001	January 2002	.30	2,352,927

-12-

Dividend Restrictions

For a description of restrictions on the payment of dividends, see "Regulation and Supervision - Restrictions on Transfers of Funds to FIBS and the Bank."

Preferred Stock

The authorized capital stock of FIBS includes 100,000 shares of preferred stock. The FIBS Board of Directors is authorized, without approval of the holders of common stock, to provide for the issuance of preferred stock from time to time in one or more series in such number and with such designations, preferences, powers and other special rights as may be stated in the resolution or resolutions providing for such preferred stock. FIBS Board of Directors may cause FIBS to issue preferred stock with voting, conversion and other rights that could adversely affect the holders of the common stock or make it more difficult to effect a change of control of the Company.

Sales of Unregistered Securities

During 2001, the Company issued 1,400 shares of its common stock to one of its former executive officers exercising stock options. The weighted average exercise price of the options was \$15.80 per share. The shares were immediately redeemed by the Company at the minority appraised value of \$40.00 per share.

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During 2001, the Company issued 3,613 unregistered shares of its common stock to 53 senior officers valued at an aggregate of \$137,294 as part of the incentive bonuses paid to them. These issuances were made in reliance upon the exemption from registration under Section 4(2) of the Securities Act of 1933.

ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following selected consolidated financial data with respect to the Company's consolidated financial position as of December 31, 2001 and 2000 and its results of operations for the fiscal years ended December 31, 2001, 2000 and 1999, has been derived from the consolidated financial statements of the Company included in Part IV, Item 14. This data should be read in conjunction with Part II, Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" and such consolidated financial statements, including the notes thereto.

FIVE YEAR SUMMARY

(Dollars in thousands except share and per share data)

Years ended December 31,	2001	2000	1999
<hr/>			
Operating Data:			
Interest income	\$ 219,126	211,797	183,362
Interest expense	93,984	101,789	83,015
<hr/>			
Net interest income	125,142	110,008	100,347
Provision for loan losses	7,843	5,280	3,563
<hr/>			
Net interest income after provision for loan losses	117,299	104,728	96,784
Noninterest income	52,034	44,151	37,676
Noninterest expense	120,249	101,323	91,503
<hr/>			
Income before income taxes	49,084	47,556	42,957
Income tax expense	17,901	17,176	15,229
<hr/>			
Net income	\$ 31,183	30,380	27,728
<hr/>			
Net income applicable to common stock	\$ 31,183	30,380	27,728
Basic earnings per common share	3.97	3.83	3.48
Diluted earnings per common share	3.94	3.78	3.42
Dividends per common share	1.18	1.11	1.07
Weighted average common shares outstanding - diluted	7,921,694	8,044,531	8,111,316
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-13-

FIVE YEAR SUMMARY, CONTINUED

(Dollars in thousands except share and per share data)

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Years ended December 31,	2001	2000	1999

Operating Ratios:			
Return on average assets	1.01%	1.10	1.09
Return on average common stockholders' equity	14.89	16.81	16.60
Average stockholders' equity to average assets	6.80	6.52	6.58
Net interest margin	4.66	4.59	4.54
Net interest spread	4.11	4.00	3.97
Common stock dividend payout ratio(1)	29.72	28.98	30.75
Ratio of earnings to fixed charges(2):			
Excluding interest on deposits	7.76x	5.23x	5.78x
Including interest on deposits	1.52x	1.46x	1.51x
=====			
Balance Sheet Data at Year End:			
Total assets	\$3,314,716	2,933,262	2,612,663
Loans	2,157,968	1,972,323	1,722,961
Allowance for loan losses	34,091	32,820	29,599
Investment securities	693,178	613,708	578,647
Deposits	2,708,613	2,365,225	2,118,183
Other borrowed funds	8,095	11,138	41,875
Long-term debt	34,331	37,000	23,394
Trust preferred securities	40,000	40,000	40,000
Stockholders' equity	222,069	197,986	173,638
=====			
Asset Quality Ratios at Year End:			
Nonperforming assets to total loans			
and other real estate owned ("OREO") (3)	1.24%	1.54	1.89
Allowance for loan losses to total loans	1.58	1.66	1.72
Allowance for loan losses to			
nonperforming loans(4)	129.16	119.73	94.84
Net charge-offs to average loans	0.32	0.17	0.27
=====			
Regulatory Capital Ratios at Year End:			
Tier 1 risk-based capital	8.73%	8.55	9.62
Total risk-based capital	10.33	10.36	11.69
Leverage ratio	6.77	6.78	7.15
=====			

(1) Dividends per common share divided by basic earnings per common share.

(2) For purposes of computing the ratio of earnings to fixed charges, earnings represents income before income taxes and fixed charges. Fixed charges represent interest expense and preferred stock dividends, which dividends commenced in October 1996 and concluded in October 1997. Deposits include interest bearing deposits and repurchase agreements. Without including preferred stock dividends in fixed charges and excluding interest on deposits, the ratio of earnings to fixed charges for the year ended December 31, 1997 was 5.76x. Without including preferred stock dividends in fixed charges and including interest on deposits, the ratio of earnings to fixed charges for the year ended December 31, 1997 was 1.55x.

(3) For purposes of computing the ratio of non-performing assets to total loans and OREO, non-performing assets include non-accrual

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loans, loans past due 90 days or more and still accruing interest, restructured loans and OREO.

- (4) For purposes of computing the ratio of allowance for loan losses to non-performing loans, non-performing loans include non-accrual loans, loans past due 90 days or more and still accruing interest and restructured loans.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

The following discussion and analysis is intended to provide greater details of the results of operations and financial condition of the Company. The following discussion should be read in conjunction with the information under Part II, Item 6, "Selected Consolidated Financial Data" and the Company's consolidated financial statements,

-14-

including the notes thereto, and other financial data appearing elsewhere in this document. Certain statements included in the following discussion constitute "forward-looking statements" which involve various risks and uncertainties. The Company's actual results may differ significantly from those anticipated in such forward-looking statements. Factors that might cause such a difference include, without limitation, the ability of the Company to execute its business strategy, interest rate risk, economic conditions, government regulation, competition and asset quality. For additional information concerning these and other factors, see Part I, Item 1, "Business - Risk Factors."

RESULTS OF OPERATIONS

Increases in the Company's earnings during recent years have been effected through a successful combination of acquisitions and internal growth. Internal growth experienced by the Company is reflected by an increased volume of customer loans and deposits, without giving effect to acquisitions. The Company's internal growth has largely been accomplished through a combination of effective offering and promotion of competitively priced products and services and the opening of several de novo banking offices. Net income was \$31.2 million, or \$3.94 per diluted share, in 2001 as compared to \$30.4 million, or \$3.78 per diluted share, in 2000 and \$27.7 million, or \$3.42 per diluted share, in 1999.

Net Interest Income

Net interest income, the largest source of the Company's operating income, is derived from interest, dividends and fees received on interest earning assets, less interest expense incurred on interest bearing liabilities. Interest earning assets primarily include loans and investment securities. Interest bearing liabilities primarily include deposits and various forms of indebtedness.

The following table presents, for the periods indicated, condensed average balance sheet information for the Company, together with interest income and yields earned on average interest earning assets, and interest expense and rates paid on average interest bearing liabilities.

AVERAGE BALANCE SHEETS, YIELDS AND RATES

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	Years Ended December 31,		
	2001		
(Dollars in thousands)	Average Balance	Interest	Average Rate
Interest earning assets:			
Loans(1) (2)	\$2,056,179	181,845	8.84
U.S. and agency securities	444,462	27,067	6.09
Federal funds sold	72,368	2,709	3.74
Other securities	75,983	4,343	5.72
Tax exempt securities(2)	79,380	5,747	7.24
Interest bearing deposits in banks	20,014	466	2.33
Total interest earning assets	2,748,386	222,177	8.08
Noninterest earning assets	331,719		
Total assets	\$3,080,105		
Interest bearing liabilities and trust preferred securities:			
Demand deposits	\$ 403,285	5,421	1.34
Savings deposits	640,101	18,654	2.91
Time deposits	990,616	55,567	5.61
Borrowings(3)	250,306	7,969	3.18
Long-term debt	41,032	2,844	6.93
Trust preferred securities	40,000	3,529	8.82
Total interest bearing liabilities and trust preferred securities	2,365,340	93,984	3.97
Noninterest bearing deposits	471,798		
Other noninterest bearing liabilities	33,551		
Stockholders' equity	209,416		
Total liabilities and stockholders' equity	\$3,080,105		

	Years Ended December 31,		
	2000		
(Dollars in thousands)	Average Balance	Interest	Average Rate
Interest earning assets:			

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Loans(1) (2)	\$1,865,125	176,742	9.48
U.S. and agency securities	414,274	25,809	6.23
Federal funds sold	21,167	1,400	6.61
Other securities	77,872	4,914	6.31
Tax exempt securities(2)	77,784	5,617	7.22
Interest bearing deposits in banks	1,641	112	6.83

Total interest earning assets	2,457,863	214,594	8.73
Noninterest earning assets	313,193		

Total assets	\$2,771,056		
=====			
Interest bearing liabilities and trust preferred securities:			
Demand deposits	\$ 368,710	6,961	1.89
Savings deposits	556,930	22,470	4.03
Time deposits	876,350	50,774	5.79
Borrowings(3)	278,721	15,525	5.57
Long-term debt	31,293	2,530	8.08
Trust preferred securities	40,000	3,529	8.82

Total interest bearing liabilities and trust preferred securities	2,152,004	101,789	4.73

Noninterest bearing deposits	407,241		
Other noninterest bearing liabilities	31,036		
Stockholders' equity	180,775		

Total liabilities and stockholders' equity	\$2,771,056		

	Years Ended December 31,		
	1999		
(Dollars in thousands)	Average Balance	Interest	Average Rate
Interest earning assets:			
Loans(1) (2)	\$1,598,594	145,164	9.33
U.S. and agency securities	464,954	27,777	5.97
Federal funds sold	24,854	1,304	5.25
Other securities	91,606	5,680	6.20
Tax exempt securities(2)	72,755	5,250	7.22
Interest bearing deposits in banks	7,071	353	4.99
Total interest earning assets	2,259,834	185,528	8.21
Noninterest earning assets	279,945		

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Total assets	\$2,539,779		
=====			
Interest bearing liabilities and trust preferred securities:			
Demand deposits	\$ 346,711	6,084	1.75
Savings deposits	539,513	19,482	3.61
Time deposits	785,307	41,959	5.34
Borrowings(3)	221,037	9,998	4.52
Long-term debt	24,556	1,963	7.99
Trust preferred securities	40,000	3,529	8.82

Total interest bearing liabilities and trust preferred securities	1,957,124	83,015	4.24

Noninterest bearing deposits	387,969		
Other noninterest bearing liabilities	27,675		
Stockholders' equity	167,011		

Total liabilities and stockholders' equity	\$2,539,779		
=====			

-15-

AVERAGE BALANCE SHEETS, YIELDS AND RATES, CONTINUED

(Dollars in thousands)	Years Ended December 31					
	2001			2000		
	Average Balance	Interest	Average Rate	Average Balance	Interest	Average Rate
Net FTE interest income		\$128,193			\$112,805	
Less FTE adjustments(2)		(3,051)			(2,797)	

Net interest income per consolidated statements of income		\$125,142			\$110,008	
=====						
Interest rate spread			4.11%			4.11%
=====						
Net yield on interest earning assets(4)			4.66%			4.66%
=====						

(1) Average loan balances include nonaccrual loans. Loan fees included in interest income were \$7.2 million, \$5.2 million and \$4.8 million

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for the years ended December 31, 2001, 2000 and 1999, respectively.

- (2) Interest income and average rates for tax exempt loans and securities are presented on a fully-taxable equivalent (FTE) basis.
- (3) Includes interest on Federal funds purchased, securities sold under repurchase agreements and other borrowed funds. Excludes long-term debt.
- (4) Net yield on interest earning assets during the period equals (i) the difference between interest income on interest earning assets and the interest expense on interest bearing liabilities and trust preferred securities, divided by (ii) average interest earning assets for the period.

Net interest income on a fully-taxable equivalent basis ("FTE") increased 13.6% to \$128.2 million in 2001 from \$112.8 in 2000 primarily due to a more rapid decline in the cost of funds than the decline in the yield on interest earning assets in combination with strong growth in loans and deposits. A higher mix of loans in earning assets allowed the net yield on earning assets to increase 11 basis points to 4.11% in 2001 from 4.00% in 2000. Net FTE interest income increased 10.0% to \$112.8 million in 2000 from \$102.5 million in 1999 primarily due to increases in the prime lending rate and continued strong loan demand, principally in commercial and commercial real estate loans. Approximately 31% of this increase is directly attributable to new banking offices opened or acquired in 2000 and 1999.

Customer loan fees, included in net interest income, increased 38.4% to \$7.2 million in 2001 from \$5.2 million in 2000. All major categories of loan fees increased with the most significant increases occurring in commercial and consumer loan fees. Customer loan fees increased 8.3% to \$5.2 million in 2000 from \$4.8 million in 1999 primarily due to increases in consumer, real estate and commercial loan business.

The most significant impact on the Company's net interest income between periods is derived from the interaction of changes in the volume of and rates earned or paid on interest earning assets and interest bearing liabilities. The volume of loans, investment securities and other interest earning assets, compared to the volume of interest bearing deposits and indebtedness, combined with the spread, produces changes in the net interest income between periods.

The table below sets forth, for the periods indicated, a summary of the changes in interest income and interest expense resulting from estimated changes in average asset and liability balances (volume) and estimated changes in average interest rates (rate). Changes which are not due solely to volume or rate have been allocated to these categories based on the respective percent changes in average volume and average rate as they compare to each other.

ANALYSIS OF INTEREST CHANGES DUE TO VOLUME AND RATES (Dollars in thousands)

Year ended	December 31, 2001 compared with December 31, 2000 favorable (unfavorable)			December 31, 2000 compared with December 31, 1999 favorable (unfavorable)			
	-----			-----			
	Volume	Rate	Net	Volume	Rate	Net	
	-----			-----			

Interest earning assets:

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Loans(1)	\$18,105	(13,002)	5,103	24,203	7,375	31,578	1
U.S. and agency securities	1,881	(623)	1,258	(3,028)	1,060	(1,968)	
Federal funds sold	3,386	(2,077)	1,309	(193)	289	96	(
Other securities	(119)	(452)	(571)	(852)	86	(766)	
Tax exempt securities(1)	115	15	130	363	4	367	
Interest bearing deposits in banks	1,254	(900)	354	(271)	30	(241)	
<hr/>							
Total change	24,622	(17,039)	7,583	20,222	8,844	29,066	1
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-16-

ANALYSIS OF INTEREST CHANGES DUE TO VOLUME AND RATES, CONTINUED (Dollars in thousands)

Year ended	December 31, 2001 compared with December 31, 2000 favorable (unfavorable)			December 31, 2000 compared with December 31, 1999 favorable (unfavorable)		
	Volume	Rate	Net	Volume	Rate	Net
<hr/>						
Interest bearing liabilities and trust preferred securities:						
Demand deposits	653	(2,193)	(1,540)	386	491	877
Savings deposits	3,356	(7,172)	(3,816)	629	2,359	2,988
Time deposits	6,620	(1,827)	4,793	4,864	3,951	8,815
Borrowings(2)	(1,583)	(5,973)	(7,556)	2,609	2,918	5,527
Long-term debt	787	(473)	314	539	28	567
Trust preferred securities	--	--	--	--	--	--
<hr/>						
Total change	9,833	(17,638)	(7,805)	9,027	9,747	18,774
<hr/>						
Increase (decrease) in FTE net interest income (1)	\$14,789	599	15,388	11,195	(903)	10,292
<hr/>						

(1) Interest income and average rates for tax exempt loans and securities are presented on a fully-taxable equivalent (FTE) basis.

(2) Includes interest on Federal funds purchased, securities sold under repurchase agreements and other borrowed funds.

Provision for Loan Losses

The provision for loan losses creates an allowance for loan losses known and inherent in the loan portfolio at each balance sheet date. The Company performs a quarterly assessment of the risks inherent in its loan portfolio, as well as a detailed review of each significant asset with identified weaknesses. Based on this analysis, the Company records a provision for loan losses in order to maintain the allowance for loan losses at assessed levels. Periodically,

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provisions are made for loans where the probable loss can be individually identified and reasonably determined, while the balance of the provisions for loan losses are based on internally assigned risk classifications of loans, historical loan loss rates, changes in the nature of the loan portfolio, overall portfolio quality, industry concentrations, delinquency trends, current economic factors and the estimated impact of current economic conditions on certain historical loan loss rates. Annual fluctuations in the provision for loan losses result from management's assessment of the adequacy of the allowance for loan losses. Ultimate loan losses may vary from current estimates. See additional information concerning the provision for loan losses, see "Critical Accounting Policies" included herein.

The provision for loan losses increased 48.5% to \$7.8 million in 2001 from \$5.3 million in 2000 and 48.2% to \$5.3 million in 2000 from \$3.6 million in 1999. These increases are primarily the result of increases in problem loans, softening economic conditions in the Company's market areas, particularly in agriculture, health care, transportation and hotel/motel market sectors, and slowing regional and national economies.

Noninterest Income

The principal sources of noninterest income include service charges on deposit accounts; technology services revenues; other service charges, commissions and fees; and, income from fiduciary activities, comprised principally of fees earned on trust assets. Noninterest income increased 17.9% to \$52.0 million in 2001 from \$44.2 million in 2000, and 17.2% to \$44.2 million in 2000 from \$37.7 million in 1999. These increases in noninterest income were a function of changes in each of the principal categories, as discussed below.

Service charges on deposit accounts increased 16.2% to \$14.6 million in 2001 from \$12.6 million in 2000. Approximately 38% of this increase is directly attributable to new banking offices opened or acquired since June 2000. The remaining increase occurred primarily in overdraft fees. Service charges on deposit accounts increased 10.7% to \$12.6 million in 2000 from \$11.4 million in 1999 primarily due to new banking offices opened or acquired during 1999 and 2000 and increases in volume of overdraft fees.

Technology services revenues were flat in 2001 as compared to the prior year. Increases in core data processing revenues were largely offset by decreases in item processing revenues. Technology services revenues increased 22.9% to \$10.2 million in 2000 from \$8.3 million in 1999. Approximately 29% of this increase resulted from the addition of one new customer during the fourth quarter of 1999. The remaining increase is primarily due to increases in the number of customers using the Company's back-room processing services and higher ATM transaction volumes combined with greater numbers of ATMs supported by the Company's ATM network.

-17-

Other service charges, commission and fees primarily include origination and processing fees on real estate loans held for resale, loan servicing fee income, credit card fees, brokerage revenues, debit card interchange fees and ATM service charge revenue. Other service charges, commissions and fees increased 43.9% to \$16.7 million in 2001 from \$11.6 million in 2000. Origination and processing fees on real estate loans sold in the secondary market increased \$4.0 million in 2001 as compared to the prior year principally due to increased refinancing activity resulting from decreases in residential lending rates. The remaining increase is primarily attributable to loan servicing fee income generated through internal growth and the acquisition of loan servicing rights in December 2000 and increases in debit card interchange fees resulting from

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higher transaction volumes. Other service charges, commissions and fees increased 9.1% to \$11.6 million in 2000 from \$10.6 million in 1999 primarily due to loan servicing income generated through internal growth and increases in ATM fee income resulting from higher debit card and foreign ATM transaction volumes combined with increases in fees for foreign ATM transactions.

Revenues from fiduciary activities are largely dependent on the fair value of assets under trust management. As a result of stock market value declines in 2001, revenues from fiduciary activities decreased 4.2% to \$4.7 million in 2001 from \$4.9 million in 2000. Revenues from fiduciary activities increased 9.2% to \$4.9 million in 2000 from \$4.5 million in 1999 primarily due to growth in customer assets, including mineral rights, under trust management and increases in fees charged for trust services.

The Company recorded net OREO expense of \$130,000 in 2001 as compared to net OREO income of \$689,000 in 2000 and \$366,000 in 1999. Variations in net OREO income or expense during the periods is primarily the result of fluctuations in gains and losses on sales of OREO. OREO income or expense is directly related to prevailing economic conditions, and such income could decrease significantly should an unfavorable shift occur in the economic conditions of the Company's markets.

Other income increased 41.6% to \$5.7 million in 2001 from \$4.0 million in 2000 primarily due to premium revenues of \$1.3 million related to reinsurance of credit-related life and disability insurance (see discussion of increases in other operating expenses herein). In addition, during 2001, the Company recorded non-recurring revenue related to the demutualization of life insurance company stock and the partial recovery of three previously recorded non-credit losses. Other income increased 61.3% to \$4.0 million in 2000 from \$2.5 million in 1999 principally due to non-recurring fourth quarter adjustments to record life insurance company demutualization stocks and the recognition of the Company's share of undistributed earnings in an unconsolidated joint venture partnership. The remaining increase was primarily due to the gain recognized on the sale of an aircraft and the partial recovery of a prior year non-credit loss.

Noninterest Expense

Noninterest expense increased 18.7% to \$120.2 million in 2001 from \$101.3 million in 2000 and increased 10.7% to \$101.3 million in 2000 from \$91.5 million in 1999. Significant components of these increases are discussed below.

Salaries, wages and employee benefits expense increased 18.9% to \$61.6 million in 2001 from \$51.8 million in 2000. Approximately 28% of the increase is directly attributable to new banking offices opened or acquired since June 2000. In addition, \$1.1 million of the increase is due to compensation expense related to outstanding stock options. The remaining increase is primarily due to increases in administrative staffing levels to support the Company's expanding number of banking offices, increases in group health insurance premiums and inflationary wage increases. Salaries, wages and employee benefits expense increased 7.9% to \$51.8 million in 2000 from \$48.0 million in 1999. Approximately \$2.1 million of the increase is directly attributable to new banking offices opened or acquired in 2000 and 1999. The remaining increase is primarily due to inflationary wage increases, increases in administrative staffing levels to support the Company's expanding number of banking offices and growth in the brokerage services division. Increases in salaries, wages and employee benefits expense in 2000 were partially offset by a \$3.1 million decrease resulting from the remeasurement of compensation expense related to outstanding stock options. For additional information relating to the Company's Stock Option Plan, see "Notes to Consolidated Financial Statements - Employee Benefit Plans" included in Part IV, Item 14.

Occupancy expense increased 18.6% to \$9.6 million in 2001 from \$8.1

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million in 2000 and 13.8% to \$8.1 million in 2000 from \$7.1 million in 1999. These increases are primarily due to additional rent and depreciation expenses associated with internal growth, bank acquisitions and the remodeling of existing facilities.

-18-

Furniture and equipment expenses increased 14.7% to \$12.3 million in 2001 from \$10.7 million in 2000. Approximately 26% of this increase is directly attributable to new banking offices opened or acquired since June 2000. The remaining increase is largely due to maintenance and depreciation expenses associated with the Company's continued upgrade of facilities and depreciation expense associated with furnishing the Company's new item proof and capture facilities in Colorado and Idaho. Furniture and equipment expense increased 4.6% to \$10.7 million in 2000 from \$10.2 million in 1999 primarily due to new banking offices opened or acquired in 2000 and 1999 and increased depreciation expense associated technology upgrades.

FDIC insurance premiums of \$442,000 remained stable in 2001 compared to \$438,000 in 2000. FDIC insurance premiums of \$438,000 in 2000 increased 88.0% from \$233,000 in 1999 due to an increase in the FDIC FICO bond assessment effective January 1, 2000. FDIC insurance rates in 2001, 2000 and 1999 reflect the Company's well-capitalized rating by the FDIC.

Goodwill amortization expense increased 9.0% to \$2.2 million in 2001 from \$2.0 million in 2000 and 20.0% to \$2.0 million in 2000 from \$1.7 million in 1999 due to acquisitions during the third quarters of 2000 and 1999. For additional information regarding goodwill, see "Critical Accounting Policies" included herein and "Notes to Consolidated Financial Statements - Summary of Significant Accounting Policies" included in Part IV, Item 14.

Core deposit intangibles amortization expense of \$1.4 million in 2001 and 2000 increased 32.2% from \$1.1 million in 1999 primarily due to acquisitions in 1999 and 2000.

Other expenses primarily include advertising and public relations costs; legal, audit and other professional fees; office supply, postage, freight and telephone expenses; and loan servicing rights amortization and impairment charges. Other expenses increased 21.8% to \$32.7 million in 2001 from \$26.9 million in 2000. Approximately 22% of this increase is attributable to new banking offices opened or acquired since June 2000. In addition, the Company recorded insurance reserves and claims of \$1.1 million related to its reinsurance of credit-related life and disability insurance and impairment of capitalized loan servicing rights of \$1.1 million. The remaining increase is primarily due to employee education, professional fees related to regulatory reporting and increases in ATM, postage, express mail, supply and telephone expenses. Other expenses increased 16.0% to \$26.9 million in 2000 from \$23.2 million in 1999 principally due to new banking offices opened or acquired in 2000 and 1999, two non-credit losses aggregating \$863,000, net of recoveries, and increases in advertising, public relations, ATM and loan servicing intangible amortization expenses.

Income Tax Expense

The Company's effective federal tax rate was 30.7%, 31.3% and 31.3% for the years ended December 31, 2001, 2000 and 1999, respectively. State income tax applies only to pretax earnings of entities operating within Montana, Colorado and Idaho. The Company's effective state tax rate was 4.8%, 4.2% and 5.3% for years ended December 31, 2001, 2000 and 1999, respectively.

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Lines of Business

The Company is managed along two primary business lines, community banking and technology services. The community banking line encompasses commercial and consumer banking services provided to individual customers, businesses and municipalities. These services primarily include the acceptance of deposits, extension of credit, fee-based investment services and mortgage servicing.

The technology services line encompasses technology services provided by i_Tech to affiliated and non-affiliated financial institutions including ATM processing support, item proof and capture, wide area network services and system support.

Additional information regarding the Company's business segments, see "Notes to Consolidated Financial Statements - Business Line Reporting" included in Part IV, Item 14.

-19-

The following table summarizes the Company's business line results, for the years indicated:

BUSINESS LINE RESULTS

Year ended December 31,	Net Income (Loss)		
	2001	2000	1999
Community Banking	37,673	34,125	33,297
Technology Services	3,050	2,954	1,999
Other	(9,540)	(6,699)	(7,568)
Consolidated	31,183	30,380	27,728

Community banking net income increased 10.4% to \$37.7 million in 2001 from \$34.1 million in 2000. This increase is primarily due to internally generated growth in net interest income and increases in processing and origination fees on residential real estate loans resold in the secondary market. These increases were partially offset by net losses incurred by new banking offices opened or acquired since June, 2000 and increases in administrative staffing levels to support the Company's expanding number of banking offices. Community banking net income increased 2.5% to \$34.1 million in 2000 from \$33.3 million in 1999 primarily due to growth in net interest income resulting from a combination of acquisitions and internal growth. In addition, the Company experienced growth in investment services revenues and earnings in unconsolidated joint ventures. These increases were partially offset by net losses incurred by new banking offices opened or acquired since 1999 and increases in administrative staffing levels to support the Company's expanding number of banking offices.

Technology services revenues increased 3.2% to \$3.1 million in 2001 from \$3.0 million in 2000 primarily due to increases in core data processing revenues from affiliates. Technology services revenues increased 47.8% to \$3.0 million in 2000 from \$2.0 million in 1999 primarily due to the addition of one new customer during the fourth quarter of 1999 and higher ATM transaction volumes combined

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with increases in the number of ATMs supported by the Company's ATM network.

Other includes the net funding cost of the Parent Company, compensation expense or benefit related to outstanding stock options, the operating results of non-bank subsidiaries except i_Tech and intercompany eliminations. Other net losses increased 42.4% to \$9.5 million in 2001 from \$6.7 million in 2000 primarily due to increases in compensation expense related to outstanding stock options, increases in interest expense primarily due to borrowings used to fund acquisitions in 2000, increases in salaries, wages and employee benefits expenses and the establishment of an allowance for loan losses by the Parent Company. Other net losses decreased 11.5% to \$6.7 million in 2000 from \$7.6 million in 1999 primarily due to compensation benefit related to outstanding stock options.

FINANCIAL CONDITION

Total assets increased 13.0% to \$3,315 million as of December 31, 2001 from \$2,933 million as of December 31, 2000. This increase was due to internal growth in loans and increases in investment securities and cash equivalents funded primarily by customer deposits.

Loans

Total loans increased 9.4% to \$2,158 million as of December 31, 2001 from \$1,973 million as of December 31, 2000. All major categories of loans increased from December 31, 2000 with the exception of consumer loans, which decreased slightly. The most significant growth occurred in loans secured by residential real estate. During 2001, the Company continued to expand its market presence through a combination of marketing activities and opening new banking offices. Total loans increased 14.5% to \$1,973 million as of December 31, 2000 from \$1,723 million as of December 31, 1999 primarily due to acquisitions and the opening of new banking offices combined with generally strong loan demand in the Company's market areas.

The Company's loan portfolio consists of a mix of real estate, consumer, commercial, agricultural and other loans, including fixed and variable rate loans. Fluctuations in the loan portfolio are directly related to the economies of the communities served by the Company. Thus, the Company's borrowers could be adversely impacted by a downturn in these sectors of the economy that could have a material adverse effect on the borrowers' abilities to repay their loans.

-20-

The following tables present the composition of the Company's loan portfolio as of the dates indicated:

LOANS OUTSTANDING

(Dollars in thousands)	As of December 31,					
	2001	Percent	2000	Percent	1999	Percent
Loans						
Real estate	\$1,137,160	52.8%	\$ 954,933	48.5%	\$ 806,320	46.2%
Consumer	483,636	22.4	495,445	25.1	463,414	26.3
Commercial	434,330	20.1	420,706	21.3	344,371	20.0
Agricultural	95,513	4.4	95,387	4.8	106,887	6.5

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Other loans	7,329	0.3	5,852	0.3	1,969	0
<hr/>						
Total loans	2,157,968	100.0%	1,972,323	100.0%	1,722,961	100
<hr/>						
Less allowance for loan losses	34,091		32,820		29,599	
<hr/>						
Net loans	\$2,123,877		\$1,939,503		\$1,693,362	
<hr/>						
Ratio of allowance to total loans	1.58%		1.66%		1.72%	
<hr/>						

As of December 31,					
(Dollars in thousands)	1998	Percent	1997	Percent	
<hr/>					
Loans					
Real estate	\$ 681,670	45.9%	\$ 683,212	46.5%	
Consumer	379,197	25.5	412,231	28.0	
Commercial	311,040	21.0	261,513	17.8	
Agricultural	106,707	7.2	107,649	7.3	
Other loans	5,845	0.4	5,809	0.4	
<hr/>					
Total loans	1,484,459	100.0%	1,470,414	100.0%	
<hr/>					
Less allowance for loan losses	28,803		28,180		
<hr/>					
Net loans	\$1,455,656		\$1,442,234		
<hr/>					
Ratio of allowance to total loans	1.94%		1.92%		
<hr/>					

The following table presents the maturity distribution of the Company's loan portfolio and the sensitivity of the loans to changes in interest rates as of December 31, 2001:

MATURITIES AND INTEREST RATE SENSITIVITIES

(Dollars in thousands)	Within One Year	One Year to Five Years	After Five Years	Total
<hr/>				
Real estate	\$ 515,729	500,386	121,045	1,137,160
Consumer	239,290	235,346	9,000	483,636

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Commercial	244,116	155,974	34,240	434,330
Agriculture	78,927	15,447	1,139	95,513
Other loans	7,329	--	--	7,329

	\$1,085,391	907,153	165,424	2,157,968
=====				
Loans at fixed interest rates	\$ 670,420	654,158	18,384	1,342,962
Loans at variable interest rates	396,698	252,995	147,040	796,733
Nonaccrual loans	18,273	--	--	18,273

	\$1,085,391	907,153	165,424	2,157,968
=====				

For additional information concerning the Company's loan portfolio and its credit administration policies, see Part I, Item 1, "Business-Lending Activities."

Investment Securities

The Company's investment portfolio is managed to attempt to obtain the highest yield while meeting the Company's risk tolerance and liquidity needs and to satisfy pledging requirements for deposits of state and political subdivisions and securities sold under repurchase agreements. The portfolio is comprised of U.S. Treasury securities, U.S. government agency securities, tax exempt securities, corporate securities, other mortgage-backed securities and other equity securities. Federal funds sold are additional investments that are classified as cash equivalents rather than as investment securities. Investment securities classified as available-for-sale are recorded at fair value, while investment securities classified as held-to-maturity are recorded at amortized cost. Unrealized gains or losses, net of the deferred tax effect, on available-for-sale securities are reported as increases or decreases in accumulated other comprehensive income or loss, a component of stockholders' equity.

-21-

Investment securities increased 12.9% to \$693 million as of December 31, 2001 from \$614 million as of December 31, 2000 primarily due to investment of funds generated through internal deposit growth. Mortgage backed securities comprised 51.1% of the total investment portfolio as of December 31, 2001 as compared to 30.2% in 2000. In attempting to obtain the Company's investment portfolio objectives, mortgage backed securities are currently the primary reinvestment selection for maturing and prepaying investments. Investment securities increased 6.1% to \$614 million as of December 31, 2000 from \$578 million as of December 31, 1999. The majority of this increase occurred in U.S. Government agencies and corporate securities.

On January 1, 2001, the Company adopted the provision of SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." In conjunction with the initial application of SFAS No. 133, the Company transferred held-to-maturity investment securities with amortized costs and fair values of \$104 million and \$103 million, respectively, to available-for-sale investment securities to better conform to the Company's investment objectives. Upon adoption of SFAS No. 133, the Company recorded net unrealized holding losses of \$569,000, net of tax, related to the transferred securities.

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The following table sets forth the book value, percentage of total investment securities and average yield for the Company's investment securities as of December 31, 2001:

SECURITIES MATURITIES AND YIELD

(Dollars in thousands)	Book Value	% of Total Investment Securities

U.S. Treasury securities		
Maturing within one year	\$ 21,499	3.1%
Maturing after ten years	517	0.1

Mark-to-market adjustments on securities available-for-sale	548	

Total	22,564	3.3

U.S. Government agency securities		
Maturing within one year	\$ 19,920	2.9
Maturing in one to five years	145,107	20.9

Mark-to-market adjustments on securities available-for-sale	4,898	

Total	169,925	24.5

Tax exempt securities		
Maturing within one year	2,292	0.3
Maturing in one to five years	18,518	2.7
Maturing in five to ten years	53,798	7.8
Maturing after ten years	8,719	1.3

Mark-to-market adjustments on securities available-for-sale	--	

Total	83,327	12.0

Corporate securities		
Maturing within one year	16,690	2.4
Maturing in one to five years	57	0.0

Mark-to-market adjustments on securities available-for-sale	--	

Total	16,747	2.4

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SECURITIES MATURITIES AND YIELD, CONTINUED

(Dollars in thousands)	Book Value	% of Total Investment Securities
Mortgage-backed securities		
Maturing within one year	130,312	18.8
Maturing in one to five years	147,938	21.3
Maturing in five to ten years	24,655	3.6
Maturing after ten years	49,314	7.1
Mark-to-market adjustments on securities available-for-sale	2,091	
Total	354,310	51.1
Other securities		
Maturing after ten years	175	0.0
Mark-to-market adjustments on securities available-for-sale	--	
Total	175	0.0
Mutual funds with no stated maturity	46,130	6.7
Mark-to-market adjustments on securities available-for-sale	--	
Total	46,130	6.7
Total	\$693,178	100.0%

(1) Average yields have been calculated on a fully-taxable basis.

The maturities noted above reflect \$89,045 of investment securities at their final maturities although they have call provisions within the next year. Mortgage backed securities, and to a limited extent, other securities have uncertain cash flow characteristics that present additional risk to the Company in the form of prepayment or extension risk primarily caused by changes in market interest rates. This additional risk is generally rewarded in the form of higher yields. Mortgage backed securities presented above are based on current prepayment assumptions.

As of December 31, 2000, the Company had U.S. Treasury securities, U.S. Government agency securities, tax exempt securities, corporate securities, other mortgage-backed securities and equity securities with carrying values of \$66,377, \$240,972, \$78,640, \$41,970, \$185,549 and \$200, respectively.

As of December 31, 1999, the Company had U.S. Treasury securities, U.S. Government agency securities, tax exempt securities, corporate securities, other mortgage-backed securities and equity securities with carrying values of \$121,051, \$172,234, \$76,835, \$30,564, \$177,713 and \$12,112, respectively.

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For additional information concerning investment securities, see "Notes to Consolidated Financial Statements - Investment Securities" included in Part IV, Item 14.

Deposits

The Company emphasizes developing total client relationships with its customers in order to increase its core deposit base, which is the Company's primary funding source. The Company's deposits consist primarily of noninterest bearing demand and interest bearing demand, saving, IRA and time deposit accounts. For additional information concerning the Company's deposits, including its use of repurchase agreements, as discussed below, see Part I, Item 1, "Business - Funding Sources."

Deposits increased 14.5% to \$2,709 million as of December 31, 2001 from \$2,365 million as of December 31, 2000 due to internal growth. The most significant growth occurred in noninterest bearing demand and savings deposits. Deposits increased 11.7% to \$2,365 million as of December 31, 2000 as compared to \$2,118 million as of December 31, 1999. Approximately \$80 million of this increase is attributable to acquisitions in 2000. The remaining increase is the result of internal growth. For additional information concerning customer deposits as of December 31, 2000 and 1999, see "Notes to Consolidated Financial Statements - Deposits" included in Part IV, Item 14.

-23-

Other Borrowed Funds

In addition to deposits, the Company also uses other traditional funding sources to support its earning asset portfolio including other borrowed funds consisting primarily of short-term borrowings from the Federal Home Loan Bank of Seattle; repurchase agreements with commercial depositors; and, on a seasonal basis, Federal funds purchased.

Other borrowed funds decreased 27.3% to \$8 million as of December 31, 2001 from \$11 million as of December 31, 2000 primarily due to timing of tax deposits made by customers and the subsequent withdrawal of funds by the Federal government. Other borrowed funds decreased 73.8% to \$11 million as of December 31, 2000 from \$42 million as of December 31, 1999 primarily due to a \$30 million, 90 day note payable to the Federal Home Loan Bank of Seattle obtained in 1999 and repaid in 2000.

For additional information on other borrowed funds as of December 31, 2001 and 2000, see "Notes to Consolidated Financial Statements - Long-Term Debt and Other Borrowed Funds" included in Part IV, Item 14.

Federal Funds Purchased and Securities Sold Under Repurchase Agreements

The following table sets forth certain information regarding Federal funds purchased and repurchase agreements as of the dates indicated:

FEDERAL FUNDS PURCHASED AND SECURITIES SOLD UNDER REPURCHASE AGREEMENTS

As of and for the years ended December 31,	2001	2000	1999

(Dollars in thousands)			

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Federal funds purchased:

Balance at period end	\$ 625	19,535	900
Average balance	2,116	25,735	32,405
Maximum amount outstanding at any month-end	13,765	48,110	69,260
Average interest rate:			
During the year	3.78%	6.24%	5.06%
At period end	1.42%	5.35%	4.74%

Securities sold under repurchase agreements:

Balance at period end	\$271,952	229,078	188,024
Average balance	240,069	206,595	163,974
Maximum amount outstanding at any month-end	271,952	240,751	209,464
Average interest rate:			
During the year	3.15%	5.24%	4.29%
At period end	1.41%	5.17%	4.80%

Long-Term Debt

The Company's long-term debt is comprised principally of an unsecured revolving term loan and unsecured subordinated notes. Long-term debt decreased 7.2% to \$34 million as of December 31, 2001 from \$37 million as of December 31, 2000 primarily due to paydowns. Long-term debt increased 60.9% to \$37 million as of December 31, 2000 from \$23 million as of December 31, 1999. Additional borrowings in 2000 were used to fund acquisitions.

For additional information on long-term debt as of December 31, 2001 and 2000, see "Notes to Consolidated Financial Statements - Long-Term Debt and Other Borrowed Funds" included in Part IV, Item 14.

Trust Preferred Securities

The Company had trust preferred securities of \$40 million at December 31, 2001 and 2000. For additional information on trust preferred securities, see "Notes to Consolidated Financial Statements - Trust Preferred Securities" included in Part IV, Item 14.

-24-

Non-Performing Assets

Non-performing assets include loans past due 90 days or more and still accruing interest, non-accrual loans, restructured loans and OREO. Management generally places loans on non-accrual when they become 90 days past due, unless they are well secured and in the process of collection. When a loan is placed on non-accrual status, any interest previously accrued but not collected is reversed from income. Approximately \$1,688,000, \$1,943,000 and \$1,424,000, \$1,062,000 and \$763,000 of gross interest income would have been accrued if all loans on non-accrual had been current in accordance with their original terms for the years ended December 31, 2001, 2000, 1999, 1998 and 1997, respectively.

Restructured loans are those where the Company has granted a concession on the interest rate or original repayment terms due to financial difficulties of the borrower.

OREO consists of real property acquired through foreclosure on the related collateral underlying defaulted loans. The Company initially records OREO at the lower of carrying value or fair value less estimated costs to sell by a charge against the allowance for loan losses, if necessary. Estimated losses that result from the ongoing periodic valuation of these properties are charged to

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earnings with a provision for losses on foreclosed property in the period in which they are identified.

The following table sets forth information regarding non-performing assets as of the dates indicated:

NON-PERFORMING ASSETS

As of December 31,	2001	2000	1999	1998

(Dollars in thousands)				
Non-performing loans:				
Nonaccrual loans	\$18,273	19,619	22,854	10,414
Accruing loans past due 90 days or more	7,200	5,158	4,695	4,695
Restructured loans	921	2,635	3,660	3,660

Total non-performing loans	26,394	27,412	31,209	18,769
OREO	414	3,028	1,445	1,445

Total non-performing assets	\$26,808	30,440	32,654	19,214
=====				
Non-performing assets to total loans and OREO	1.24%	1.54%	1.89%	1.89%
=====				

Non-performing assets decreased 11.9% to \$27 million as of December 31, 2001 compared to \$30 million as of December 31, 2000 primarily due to decreases in nonaccrual loans and sales of OREO. Loans past due 90 days or more and still accruing interest as of December 31, 2001 includes one matured commercial loan of \$2 million in the process of being renewed. Non-performing assets decreased 6.8% to \$30 million as of December 31, 2000, compared to \$33 million as of December 31, 1999 primarily due to loan paydowns by one commercial borrower.

In addition to the non-performing loans included in the table above, management has identified certain performing loans for which management has serious doubts as to the ability of the borrowers to comply with the present loan repayment terms and which may result in future non-performing loans. There can be no assurance that the Company has identified all of its potential non-performing loans. Furthermore, management cannot predict the extent to which economic conditions in the Company's market areas may worsen or the full impact such conditions may have on the Company's loan portfolio. Accordingly, there can be no assurances that other loans will not become 90 days or more past due, be placed on non-accrual or become restructured loans or OREO in the future.

Allowance for Loan Losses

The allowance for loan losses is established through a provision for loan losses based on management's evaluation of known and inherent risk in its loan portfolio. See "Provision for Loan Losses" herein. The allowance for loan losses is increased by provisions charged against earnings and reduced by net loan charge-offs. Loans are charged-off when management determines that collection has become unlikely. Consumer loans are generally charged off when they become 120 days past due. Other loans, or portions thereof, are charged off when they become 180 days past due unless they are well-secured and in the process of collection. Recoveries are recorded only when cash payments are received.

-25-

The allowance for loan losses is maintained at an amount to sufficiently provide for estimated losses based on management's evaluation of known and inherent risks in its loan portfolio at each balance sheet date. The allowance for loan losses is determined by applying estimated loss factors to the credit exposures from outstanding loans. For commercial, agriculture and real estate loans, loss factors are applied based on internal risk classifications of these loans. For certain consumer loans, loss factors are applied on a portfolio basis. Loss factors are based on peer and industry loss data which are comparable to the Company's historical loss experience, and are reviewed on a quarterly basis, along with other factors affecting the collectibility of the loan portfolio such as changes in the size and composition of the loan portfolio, delinquency levels, actual loan loss experience, current economic conditions and detailed analyses of individual loans for which full collectibility may not be assured.

Specific allowances are established for loans where management