

FIRST INTERSTATE BANCSYSTEM INC  
Form 10-Q/A  
May 24, 2001

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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q/A

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 1997.

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the transaction period from \_\_\_\_\_ to \_\_\_\_\_

COMMISSION FILE NUMBER 333-3250  
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First Interstate BancSystem of Montana, 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.)

PO Box 30918, 401 North 31st Street, Billings, MT 59116-0918  
-----  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code 406/255-5300  
-----

N/A

-----  
(Former name, former address, and former fiscal year,  
if changed since last report)

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

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requirements for the past 90 days Yes X No

The Registrant had 1,991,274 shares of common stock and 20,000 shares of preferred stock outstanding on July 25, 1997.

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2

## FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. Quarterly Report on Form 10-Q

	Index -----	Page -----
PART I. FINANCIAL INFORMATION		
Item 1 - Financial Statements		
Restatement Explanatory Note		3
Consolidated Balance Sheets June 30, 1997 and December 31, 1996		4
Consolidated Statements of Income Three months ended June 30, 1997 and 1996, and Six months ended June 30, 1997 and 1996		5
Consolidated Statements of Cash Flows Six months ended June 30, 1997 and 1996		6
Notes to Unaudited Consolidated Financial Statements		7
As more fully described in "Notes to Unaudited Consolidated Financial Statements," the Company has restated its 1997 consolidated financial statements		
Item 2 - Managements' Discussion and Analysis of Financial Condition and Results of Operations		13
PART II. OTHER INFORMATION		
Item 1 - Legal Proceedings		17
Item 2 - Changes in Securities		17
Item 3 - Defaults upon Senior Securities		17
Item 4 - Submission of Matters to a Vote of Security Holders		17
Item 5 - Other Information		17
Item 6 - Exhibits and Reports on Form 8-K		17

2

3

## RESTATEMENT EXPLANATORY NOTE

In 2000, the Company determined it was necessary to restate the Company's 2000, 1999, 1998 and 1997 consolidated quarterly financial statements to change the accounting treatment for awards made pursuant to its Nonqualified Stock Option and Stock Appreciation Rights Plan ("Stock Option Plan") from fixed to variable plan accounting.

This Amendment No. 1 to the Company's Quarterly Report on Form 10-Q for the quarterly period ended June 30, 1997 amends and restates the previously filed Form 10-Q in its entirety. In order to preserve the nature and character of the disclosures set forth in the Form 10-Q as originally filed, no attempt has been made in this Amendment No. 1 to modify or update such disclosures except as required to reflect the effects of the restatement and make nonsubstantial revisions to the notes to the unaudited consolidated financial statements. For additional information regarding the restatement, see "Notes to Unaudited Consolidated Financial Statements - Restatement" included in Part I, Item 1.

Share and per share data presented have not been restated to give effect of a four-for-one stock split occurring during the fourth quarter of 1997.

3

4

## FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

Consolidated Balance Sheets  
(Dollars in thousands, except share data)  
(Unaudited)

Assets	June 30, 1997 (Restated)	December 31, 1996
	-----	-----
Cash and due from banks	\$ 130,362	160,962
Federal funds sold	19,275	4,945
Interest bearing deposits in banks	37	6,545
Investment securities:		
Available-for-sale	83,479	124,502
Held-to-maturity	313,452	279,069
	-----	-----
	396,931	403,571

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Loans, net	1,475,852	1,375,479
Less allowance for loan losses	28,757	27,797
	-----	-----
Net loans	1,447,095	1,347,682
Premises and equipment, net	58,976	58,183
Accrued interest receivable	21,066	19,573
Excess of purchase price over equity in net assets of subsidiaries less accumulated amortization of \$7,284 at June 30, 1997 (unaudited) and \$5,971 at December 31, 1996	34,160	39,010
Other real estate owned, net	1,098	1,546
Deferred tax asset	7,152	4,921
Other assets	15,697	16,899
	-----	-----
Total assets	\$ 2,131,849	2,063,837
	=====	=====
Liabilities and Stockholders' Equity		
Deposits:		
Noninterest bearing	\$ 353,189	385,371
Interest bearing	1,319,846	1,294,053
	-----	-----
Total deposits	1,673,035	1,679,424
Federal funds purchased	61,900	13,450
Securities sold under repurchase agreements	129,538	129,137
Accounts payable and accrued expenses	20,348	18,027
Other borrowed funds	37,272	13,071
Long-term debt	56,184	64,667
	-----	-----
Total liabilities	1,978,277	1,917,776
Stockholders' equity:		
Non-voting noncumulative 8.53% preferred stock without par value; authorized 100,000 shares; issued and outstanding 20,000 shares	20,000	20,000
Common stock without par value; authorized 5,000,000 shares; issued and outstanding 1,972,161 shares at June 30, 1997 (unaudited and 1,978,268 shares at December 31, 1996)	8,700	8,941
Retained earnings	124,502	116,613
Unrealized holding gain on investment securities available-for-sale, net	370	507
	-----	-----
Total stockholders' equity	153,572	146,061
	-----	-----
Total liabilities and stockholders' equity	\$ 2,131,849	2,063,837
	=====	=====

See accompanying notes to unaudited consolidated financial statements.

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## FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

### Consolidated Statements of Income (Dollars in thousands, except share data) (Unaudited)

	For the three months ended June 30,		For the six months ended June 30,	
	-----		-----	
	1997 (Restated)	1996	1997 (Restated)	1996
	-----	-----	-----	-----
Interest income:				
Interest and fees on loans	\$ 34,903	22,703	68,233	44,600
Interest and dividends on investment securities:				
Taxable	5,419	3,480	10,762	6,931
Exempt from Federal taxes	276	262	527	498
Interest on deposit with banks	12	21	97	225
Interest on Federal funds sold	559	117	711	600
	-----	-----	-----	-----
Total interest income	41,169	26,583	80,330	52,854
	-----	-----	-----	-----
Interest expense:				
Interest on deposits	14,083	9,648	27,470	19,456
Interest on Federal funds purchased	767	228	1,085	259
Interest on securities sold under repurchase agreements	1,486	977	2,811	2,106
Interest on other borrowed funds	446	57	519	141
Interest on long-term debt	1,199	267	2,488	589
	-----	-----	-----	-----
Total interest expense	17,981	11,177	34,373	22,551
	-----	-----	-----	-----
Net interest income	23,188	15,406	45,957	30,303
Provision for loan losses	1,058	661	2,281	1,152
	-----	-----	-----	-----
Net interest income after provision for loan losses	22,130	14,745	43,676	29,151
Other operating income:				
Income from fiduciary activities	989	661	2,022	1,523
Service charges on deposit accounts	2,531	1,803	4,910	3,518
Data processing	1,826	1,781	3,667	3,822
Other service charges, commissions, and fees	1,047	669	1,939	1,293
Net investment securities gains	15	--	73	2
Other income	452	281	874	582
	-----	-----	-----	-----
Total other operating income	6,860	5,195	13,485	10,740
	-----	-----	-----	-----
Other operating expenses:				
Salaries and wages	7,215	5,000	14,202	9,897
Employee benefits	1,832	1,293	4,991	2,663
Occupancy expense, net	1,481	1,001	3,081	2,040
Furniture and equipment expense	1,935	1,461	3,754	2,751
Other real estate expense (income), net	19	(70)	(115)	(159)
Other expenses	5,798	3,090	11,233	6,015

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Total other operating expenses	18,280	11,775	37,146	23,207
Income before income taxes	10,710	8,165	20,015	16,684
Income tax expense	4,076	3,131	7,624	6,414
Net income	\$ 6,634	5,034	12,391	10,270
Net income per common share	\$ 3.13	2.58	5.82	5.26
Dividends per common share	.98	.81	1.85	1.52
Weighted average common shares outstanding	1,984,562	1,948,672	1,984,177	1,950,723

See accompanying notes to unaudited consolidated financial statements.

5

6

FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

Consolidated Statements of Cash Flows  
(Dollars in thousands, except per share data)  
(Unaudited)

	For the six months ended June 30,	
	1997 (Restated)	1996
Cash flows from operating activities:		
Net income	\$ 12,391	\$ 10,270
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan and other real estate losses	2,277	1,152
Depreciation and amortization	4,153	2,239
Net premium amortization on investment securities	289	614
Gain on sales of investments	(73)	(2)
Gain on sales of other real estate owned	(190)	(218)
(Gain) loss on sales of property and equipment	(14)	1
Provision for deferred income taxes	(2,178)	(1,476)
Increase in interest receivable	(1,493)	(1,344)
Decrease in other assets	1,202	250
Increase (decrease) in accounts payable and accrued expenses	1,512	(501)
Net cash provided by operating activities	17,876	10,985

6

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Cash flows from investing activities:		
Purchases of investment securities:		
Held-to-maturity	(333,219)	(40,994)
Available-for-sale	(237)	(11,509)
Proceeds from maturities and paydowns of investment securities:		
Held-to-maturity	298,953	53,773
Available-for-sale	9,579	8,754
Proceeds from sales of available-for-sale investment securities	31,158	--
Decrease in interest bearing deposits in banks	6,508	22,007
Extensions of credit to customers, net of repayments	(99,191)	(71,642)
Recoveries of loans charged-off	1,652	649
Proceeds from sales of other real estate	879	482
Capital expenditures, net	(3,619)	(3,013)
	-----	-----
Net cash used in investing activities	(87,537)	(41,493)
	-----	-----
Cash flows from financing activities:		
Net decrease in deposits	(6,389)	(16,582)
Net increase in Federal funds and repurchase agreements	48,851	11,984
Net increase in other borrowed funds	24,201	3,814
Proceeds from long-term borrowings	1,750	424
Repayment of long-term borrowings	(10,233)	(6,057)
Proceeds from issuance of common stock	352	277
Payments to retire common stock	(639)	(931)
Dividends paid on common stock	(3,656)	(2,957)
Dividends paid on preferred stock	(846)	--
	-----	-----
Net cash provided by (used in) by financing activities	53,391	(10,028)
	-----	-----
Net decrease in cash and cash equivalents	(16,270)	(40,536)
Cash and cash equivalents at beginning of period	165,907	143,042
	-----	-----
Cash and cash equivalents at end of period	149,637	102,506
	=====	=====

Noncash Investing and Financing Activities:

The Company transferred loans of \$237 and \$197 to other real estate owned during the six months ended June 30, 1997 and 1996, respectively. In conjunction with stock option exercises, the Company transferred \$46 from accrued liabilities to stockholders' equity during the six months ended June 30, 1997.

See accompanying notes to unaudited consolidated financial statements.

FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands)

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In the opinion of management, the accompanying unaudited, restated consolidated financial statements contain all adjustments (all of which are of a normal recurring nature) necessary to present fairly the consolidated financial position at June 30, 1997 and December 31, 1996, and the results of consolidated operations and cash flows for each of the six month periods ended June 30, 1997 and 1996 in conformity with generally accepted accounting principles. The balance sheet information at December 31, 1996 is derived from audited consolidated financial statements, however, certain reclassifications have been made to conform to the June 30, 1997 presentation. For additional information regarding the restatement, see Note 10.

In June 1996, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 125 requires the Company to recognize as separate assets the rights to service mortgage loans for others, whether the servicing rights are acquired through purchases or loan originations. Servicing rights are initially recorded at fair value based upon the present value of estimated future cash flows. Subsequently, the servicing rights are assessed for impairment, with impairment losses recognized in the statement of income in the period the impairment occurs. For purposes of performing the impairment evaluation, the related portfolio must be stratified on the basis of certain risk characteristics including loan type and note rate. SFAS No. 125 also specifies that financial assets subject to prepayment, including loans that can be contractually prepaid or otherwise settled in such a way that the holder would not recover substantially all of its recorded investment, be measured like debt securities available-for-sale or trading securities under SFAS No. 115. The Company adopted the provisions of SFAS No. 125 as of January 1, 1997. The adoption did not have a material effect on the financial position or results of operations of the Company.

### (2) Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks and Federal funds sold for one-day-periods.

### (3) Computation of Earnings Per Share

Earnings per common share are computed by dividing net income less preferred stock dividends by the weighted average number of shares of common stock outstanding during the period presented. Stock options outstanding are considered common stock equivalents, and are included in computations of weighted average shares outstanding.

### (4) Cash Dividends

On July 21, 1997, the Company paid a cash dividend on second quarter earnings of \$1.00 per share to stockholders of record on that date. It has been the Company's practice to pay quarterly dividends based upon earnings. The July 1997 dividend represents 30% of the Company's net income for the quarter ended June 30, 1997 without taking into effect compensation expense related to stock options.



8

FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands)

(5) Allowance for Loan Losses

Transactions in the allowance for loan losses for the three month and six month periods ended June 30, 1997 and 1996 are summarized below:

	For the three months ended June 30,		For the six months ended June 30,	
	1997	1996	1997	1996
Balance at beginning of period	\$ 28,393	15,242	27,797	15,171
Provision charged to operating expense	1,058	661	2,281	1,152
Less loans charged-off	(1,612)	(903)	(2,973)	(1,566)
Add back recoveries of loans previously charged-off	918	406	1,652	649
Balance at end of period	\$ 28,757	15,406	28,757	15,406

(6) Other Real Estate Owned (OREO)

Other real estate owned consists of the following:

	June 30, 1997	December 31, 1996
Other real estate	\$ 1,560	2,057
Less allowance for OREO losses	462	511
	\$ 1,098	1,546

A summary of transactions in the allowance for OREO losses follows:

	For the three months ended June 30,	For the six months ended June 30,
--	--	--------------------------------------

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	1997	1996	1997	1996
Balance at beginning of period	\$ 466	548	511	554
Provision (reversal) during the period	(4)	--	(4)	--
Loss on dispositions	--	--	(45)	(6)
Balance at end of period	\$ 462	548	462	548

8

9

FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands)

Changes in the balance of other real estate owned for the six months ended June 30, 1997 and 1996 are summarized as follows:

	Six months ended June 30,	
	1997	1996
Balance at beginning of period	\$2,057	1,903
Add transfers from loans	237	197
Less writedowns charged to reserves	(45)	--
Cash proceeds from sales	879	482
Less gains on sales	190	218
Net basis of OREO sold	(689)	(264)
Balances, end of period	\$1,560	\$1,836

(7) Acquisitions

On February 5, 1997, First Interstate Bank of Montana, N.A. purchased the assets of Mountain Financial, a loan production office located in Eureka, Montana. The total cash purchase price of the assets acquired aggregated \$1,726, of which \$166 was for premises and equipment and the remaining \$1,560 was for loans acquired.

During June 1997, the Company finalized its allocation of purchase price related to the 1996 acquisitions of First Interstate Bank of Montana, N.A., First Interstate Bank of Wyoming, N.A. and Mountain Bank of Whitefish. Changes in preliminary estimates of the fair value of loans, other assets and other liabilities resulted in a \$3.5 million decrease in

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goodwill.

### (8) Commitments and Contingencies

In the normal course of business, the Company is named or threatened to be named as defendant in various lawsuits, some of which involve claims for substantial amounts of actual and/or punitive damages. With respect to each of these suits it is the opinion of management, following consultation with legal counsel, the suits are without merit or in the event the plaintiff prevails, the ultimate liability or disposition thereof will not have a material adverse effect on the consolidated financial condition or the results of operations. During 1985, the Company entered into a partnership agreement with two outside parties for the purpose of purchasing certain land and building with an aggregate cost of approximately \$20,000. The Company is a tenant in the building and owns a 50% undivided interest in the property. Indebtedness of the partnership in the amount of \$10,617 at June 30, 1997 is guaranteed by each of the partners.

The Company is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, in varying degrees, elements of credit and interest rate risk in excess of amounts recorded in the consolidated balance sheet.

9

10

## FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

### Notes to Unaudited Consolidated Financial Statements (Dollars in thousands)

Standby letters of credit and financial guarantees written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. Most commitments extend for no more than two years. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company holds various collateral supporting those commitments for which collateral is deemed necessary.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the commitment contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Company upon extension of credit, is based on management's credit evaluation of the customer. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, and income-producing commercial properties.

### (9) Accounting Pronouncements Not Yet Adopted

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In February 1997, the FASB issued SFAS No. 128, "Earnings per Share," which simplifies the standards for computing earnings per share ("EPS") by replacing the presentation of primary EPS with a presentation of basic EPS on the face of the income statement for all entities with complex capital structures. SFAS No. 128 also requires a reconciliation of the numerator and the denominator of the basic EPS computation to the numerator and denominator of the diluted EPS computation.

Basic EPS excludes dilution and is computed by dividing income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or resulted in the issuance of common stock that then shared in the earnings of the entity.

This statement is effective for financial statements issued for periods ending after December 15, 1997. Earlier application is not permitted. Once effective, this statement requires restatement of all prior period EPS data. Pro forma basic and diluted net income per share as determined under this statement will not differ from amounts currently reported by the Company.

In February 1997, the FASB issued SFAS No. 129, "Disclosure of Information about Capital Structure," which lists required disclosures about capital structure that had been included in a number of previously existing separate statements and opinions. SFAS No. 129 is effective for financial statements for periods ending after December 15, 1997.

In June 1997, the FASB issued SFAS No. 130, "Reporting Comprehensive Income," which establishes standards for reporting and display of comprehensive income and its components (revenues, expenses, gains, and losses) in a full set of general-purpose financial statements. This statement requires that all items required to be recognized under accounting standards as components of comprehensive income be reported in a financial statement that is displayed with the same prominence as other financial statements. This statement does not require a specific format for that financial statement but requires that an entity display an amount representing comprehensive income for the period in that financial statement.

### FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

#### Notes to Unaudited Consolidated Financial Statements (Dollars in thousands)

This statement requires that an entity (a) classify items of other comprehensive income by their nature in a financial statement and (b) display the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in-capital in the equity section of a statement of financial position.

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This statement is effective for fiscal years beginning after December 15, 1997. Reclassification of financial statements for earlier periods provided for comparative purposes is required.

(10) Restatement

In 2000, the Company determined that fixed plan accounting treatment historically afforded its Stock Option Plan was not consistent with certain elements of the Stock Option Plan's operations and accounting guidance contained in APB Opinion 25 and related interpretations. Accordingly, the Company has restated the accompanying unaudited 1997 consolidated financial statements to reflect variable plan accounting treatment for awards made pursuant to its Stock Option Plan.

The following is a summary of the effect of such restatement on the Company's consolidated financial statements:

	June 30, 1997	
	Originally Reported	Restated
 Consolidated Balance Sheets		
Deferred tax asset	\$ 6,629	7,152
Other assets	15,722	15,697
Total assets	2,131,351	2,131,849
Accounts payable and accrued expenses	19,497	20,348
Common stock	8,350	8,700
Retained earnings	125,205	124,502
	=====	=====

	For the three months ended June 30, 1997	
	Originally Reported	Restated
 Consolidated Statements of Income		
Employee benefits	\$ 1,836	1,832
	=====	=====
Income before income taxes	\$ 10,706	10,710
Income tax expense	4,074	4,076
	-----	-----
Net income	\$ 6,632	6,634
	=====	=====
Net income per common share	\$ 3.13	3.13
	=====	=====

## FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC. AND SUBSIDIARIES

Notes to Unaudited Consolidated Financial Statements  
(Dollars in thousands)

	For the six months ended June 30, 1997	
	Originally Reported	Restated
Consolidated Statements of Income		
Employee benefits	\$ 3,832 =====	4,991 =====
Income before income taxes	\$ 21,174	20,015
Income tax expense	8,080 -----	7,624 -----
Net income	\$ 13,094 =====	12,391 =====
Net income per common share	\$ 6.17 =====	5.82 =====

Included in the 1997 restated financial statement amounts for the six months ended June 30, 1997 are compensation expense of \$1,000 and a reduction in tax expense of \$394 related to periods prior to 1997. The impact on 1997 net income and earnings per share is a decrease to net income of \$606 and a decrease of \$0.32 to earnings per share.

## ITEM 2.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF  
FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(Dollars in thousands)

The following discussion focuses on significant factors affecting the financial

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condition and results of operations of First Interstate BancSystem of Montana, Inc. ("the Company") during the three and six month periods ended June 30, 1997, with comparisons to 1996 as applicable.

### ACQUISITION ACTIVITY

On October 1, 1996, the Company purchased all of the outstanding capital stock of First Interstate Bank of Wyoming, N.A. and First Interstate Bank of Montana, N.A.; and, on December 18, 1996, acquired all of the outstanding capital stock of Mountain Bank of Whitefish (collectively, "the acquired banks"). The transactions were accounted for under purchase accounting rules. Goodwill, representing the excess of cost over net assets acquired, is being amortized using the straight-line method over periods of 15 to 25 years.

### ASSET LIABILITY MANAGEMENT

The primary objective of the company's asset liability management process is to optimize net interest income while prudently managing balance sheet risks by understanding the levels of risk accompanying its decisions and monitoring and managing these risks. The ability to optimize net interest income is largely dependent on the Company's ability to manage the sensitivity of net interest income to actual or potential changes in interest rates. The Company uses interest sensitivity "gap" analysis, income simulation models, and, to a limited extent, duration analysis (including estimation of borrower prepayment options) to evaluate the potential effects of changing interest rates on its interest margin.

### EARNING ASSETS

Earning assets of \$1.9 billion at June 30, 1997 were \$96.2 million, or 5%, higher compared to December 31, 1996 primarily due to growth in loan volume. The mix of earning assets changed little from December 31, 1996 with net loans comprising approximately 77%, held-to-maturity investment securities comprising approximately 17% and interest bearing deposits, available-for-sale investment securities and federal funds sold comprising the remaining 6%.

Loans. All major categories of loans showed increases in volumes from December 31, 1996 due to continued strong economic conditions in the communities served by the Company's banking subsidiaries and some seasonal increases, particularly in agricultural lending, following traditional paydowns during the fourth quarter. Growth in net loans of 7% during the first six months of 1997 is slightly lower than the 8.1% growth rate experienced during the same period of 1996 indicating a slight slowing in the economy that has been attributed to a slowing of consumer borrowing as consumer debt rises.

Investment Securities. The Company manages its investment portfolio within established policies which provide for the management of interest rate sensitivity risks, to meet earning objectives, to provide ample liquidity and to provide adequate collateral to support deposit and repurchase agreement activities. Cash proceeds from maturities, sales and principal payments during the first six months of 1997 were generally reinvested in held-to-maturity investment securities or used to provide additional liquidity to fund increases in other earning assets.

Federal Funds Sold. Federal funds sold balances increased approximately \$14 million from December 31, 1996 as the Company's banking subsidiaries funded the cash requirements of correspondent banks. Average federal funds sold balances during the first half of 1997 of \$25,753 and during 1996 of \$25,462 showed only slight variance.

Income from Earning Assets. Income from earning assets was \$41.2 million for the three month period ended June 30, 1997, as compared to \$26.6 million for the same period in 1996. The increase of \$14.6 million or 55% resulted from increases in earning assets through internal growth and the bank acquisitions discussed previously. Exclusive of income from the acquired banks, interest income for the three months ended June 30, 1997 increased approximately 13% from the same period in 1996. Yields on average total earning assets during the second quarter of 1997 and 1996 were 8.81% and 8.90%, respectively.

For the six month periods ended June 30, 1997 and 1996, income from earning assets was \$80.3 million and \$52.9 million, respectively. Approximately 84% of the increase is due to interest income of the acquired banks. The yield on average total earning assets for the first six months of 1997 was 8.78% compared to 8.85% during 1996.

#### FUNDING SOURCES

The Company utilizes various traditional funding sources to support its earning asset portfolio including deposits, borrowings, federal funds purchased and repurchase agreements.

Deposits. Overall, total deposits decreased slightly from December 31, 1996 to June 30, 1997. Decreases in non-interest bearing deposits of \$32.0 million during the first six months of 1997, were partially offset by increases in interest-bearing deposits of \$25.8 million during the same period. The Company historically has experienced similar seasonal cycles in overall deposit growth during the first half of the year.

Federal Funds Purchased and Other Borrowed Funds. Federal funds purchased for one day periods and other borrowed funds consisting primarily of short-term borrowings from the Federal Home Loan Bank increased \$72.7 million from December 31, 1996 to June 30, 1997. The increased borrowings were the result of funding requirements related to increases in loans and Federal funds sold during the first half of 1997.

Long Term Debt. During the first half of 1997, the Company reduced its long-term indebtedness by \$8.5 million or 14%. Payments of approximately \$8.4 million on the Company's revolving term debt were funded by earnings of the Company's banking subsidiaries.

Expense of Interest Bearing Liabilities. The Company's interest expense for the three months ended June 30, 1997 was \$18.0 million, a \$ 6.8 million or 61% increase over the same period in 1996. Interest expense of the acquired banks and additional interest costs to fund the acquisitions aggregated approximately \$6 million during the second quarter and \$10.6 million year-to-date. The remaining increase was caused by higher levels of interest bearing liabilities, particularly federal funds purchased for one day periods and other borrowed funds. The cost of total average interest bearing liabilities during the first six months of 1997 of 4.4% did not change from the same period in 1996.

Provision for Loan Losses. The balance of the provision for loan losses is maintained at a level that is, in management's judgment, adequate to absorb losses inherent in the loan portfolio given past, present and expected conditions. The provision for loan losses increased \$397 and \$1,129 for the three and six month periods ended June 30, 1997, respectively, from the same periods in 1996. A significant portion of these increases relate directly to the acquired banks, \$353 for the three month period and \$919 for the six month



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period. The remaining increases are associated with growth in loan volumes and slight deteriorations in the agricultural and consumer loan portfolios. Although non-performing and problem assets have shown some increases, the fundamental economies within the Company's markets remain strong.

### LIQUIDITY

The Company actively manages its liquidity position through established policies and procedures. Management has also developed contingency plans to address potential liquidity needs. The Company's current liquidity position is supported largely through core deposits and from its investment portfolio.

The current investment portfolio contains a mix of maturities which provide a structured flow of maturing and reinvestable funds that can be converted to cash, should the need arise. Maturing balances in the loan portfolio also provide options for managing cash flows and provide an important source of intermediate and long-term liquidity.

14

15

Alternate sources of liquidity are provided by Federal funds lines carried with upstream and downstream correspondent banks. Additional liquidity could also be generated through borrowings from the Federal Reserve Bank of Minneapolis and the Federal Home Loan Bank of Seattle. At June 30, 1997, the Company had \$8.8 million available on its revolving term loan.

### OTHER OPERATING INCOME AND EXPENSE

#### OTHER OPERATING INCOME

Exclusive of income attributable to the acquired banks, other operating income increased \$261 or 5% during the second quarter of 1997 and decreased less than 1% during the six months ended June 30, 1997 compared to the same periods in the prior year. Trust and data division revenues contributed to the increase in other operating income during the second quarter, contributing an additional \$121 of income primarily due to increases in number of customers and transaction volumes. Year-to-date trust and data revenues, however, show declines from the same period last year due to non-recurring accrual adjustments made during January 1996. Service charges on deposit accounts also contributed to the overall increase in other income, up 5% for the quarter and year-to-date.

#### OTHER OPERATING EXPENSES

Overall, quarter-to-date and year-to-date other operating expense increased approximately 55% and 60%, respectively, from the same periods in the prior year. During the first quarter of 1997, the Company recorded compensation expense related to stock options of \$1.0 million for periods prior to 1997 as a result of restating the financial statements to reflect variable plan accounting for awards made pursuant to the Company's stock option plan. For additional information regarding the restatement, see "Restatement Explanatory Note" included in Part I and "Notes to Unaudited Consolidated Financial Statements-Restatement" included in Part I, Item 1. Expenses incurred directly by the acquired banks aggregated approximately \$3.6 million for the three months ended June 30, 1997 and \$8.1 million for the six months ended June 30, 1997. In

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addition to the direct other operating expenses incurred by the acquired banks, other operating expenses of the holding company and other banking subsidiaries increased, particularly in the operations and data divisions, due to the additional costs associated with providing support services to the acquired banks.

Salaries and benefits expense. Salaries and benefits expense of \$19.2 million for the six months ended June 30, 1997 increased 53% over the same period in 1996. Salaries and benefits expenses for the three month period ended June 30, 1997 increase 44% over the same period in 1996. A significant portion of the quarter-to-date and year-to-date increases are attributable to the acquisitions and increased staffing levels necessary to provide operational and other support functions to the acquired banks. In addition, \$1,000 of the increase relates to periods prior to 1997 and is the result of the restatement discussed above. The remaining increases are primarily inflationary in nature.

Furniture, equipment and occupancy expense. Exclusive of increases directly related to the acquired banks, occupancy, furniture and equipment expenses increased approximately \$255 or 10% during the three month period ended June 30, 1997 and \$654 or 14% for the six month period ended June 30, 1997. Increases are principally due to increased depreciation on data processing equipment upgrades occurring during the second half of 1996 and the first half of 1997 and the continuing upgrades and expansion of the Company's micro-computer and ATM networks.

Other expenses. Other expenses increased \$2.6 million for the three months ended June 30, 1997 compared to the same period in the prior year and \$5.1 million for the six months ended June 30, 1997 compared to the same period in the prior year. Of these increases, \$1.2 million and \$2.9 million for the three and six month periods, respectively, relate directly to the acquired banks. The remaining quarter-to-date and year-to-date increases from the previous year are principally due to increases in advertising and public relations costs, additional legal and professional costs, and increases in postage, supply and telephone expenses.

Exclusive of expenses directly related to the acquired branches, advertising and public relation expenses for the three and six month periods ending June 30, 1997 were approximately \$229 higher than the same periods in 1996. These increases are attributable to budgeted increases in advertising expense of approximately \$109 for the first half of 1997 combined with fluctuations in the timing of public relation events in the current year compared to 1996.

Legal and professional expenses increased \$367 during the three months ended June 30, 1997 compared to the same period in the previous year and \$634 during the first half of 1997 compared to the first half of 1996. Increases of \$300 and \$484, not directly related to the acquired banks, are due principally to consulting fees associated with revision of the Company's employee job evaluation system and accruals for financial planning activities.

Office supply, postage and telephone expenses increased \$273 during the second quarter and \$588 year-to-date compared to the same periods in 1996, exclusive of expenses incurred by the acquired banks. These additional expenses are primarily due to increased costs resulting from growth in the Company's customer deposit

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base.

The above increases in other expense were offset by decreases in royalty fees of \$151 during the first half of 1997 due to the termination of a franchise agreement with First Interstate Bancorp during May 1996.

Other quarter-to-date and year-to-date variances in other expenses from the previous year are not considered individually significant.

16

17

PART II. OTHER INFORMATION

- ITEM 1            LEGAL PROCEEDINGS
- None
- ITEM 2            CHANGES IN SECURITIES
- None
- ITEM 3            DEFAULTS UPON SENIOR SECURITIES
- None
- ITEM 4            SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS
- None
- ITEM 5            OTHER INFORMATION
- Not applicable or not required
- ITEM 6            EXHIBITS AND REPORTS OF FORM 8-K
- (a) Exhibits.
27. Financial Data Schedule.
- (b) No reports of Form 8-K were filed for the quarter ended June 30, 1997.

17

18

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized:

FIRST INTERSTATE BANCSYSTEM OF MONTANA, INC.

Date May 16, 2001  
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/s/ THOMAS W. SCOTT  
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Thomas W. Scott  
Chief Executive Officer

Date May 16, 2001  
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/s/ TERRILL R. MOORE  
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Terrill R. Moore  
Senior Vice President  
and Chief Financial Officer