CITIZENS HOLDING CO /MS/
Form 10-Q
November 08, 2011
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended September 30, 2011

OR

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

For the transition period from to

Commission File Number: 001-15375

CITIZENS HOLDING COMPANY

(Exact name of registrant as specified in its charter)

MISSISSIPPI	**64-0666512**
(State or other jurisdiction of	**(IRS Employer**
incorporation or organization)	**Identification No.)**
521 Main Street, Philadelphia, MS	**39350**
(Address of principal executive offices)	**(Zip Code)**

601-656-4692

(Registrant s telephone number, including area code)

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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). x Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller Reporting Company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes x No

Number of shares outstanding of each of the issuer s classes of common stock, as of November 4, 2011:

Title	**Outstanding**
Common Stock, $0.20 par value	4,843,911

Table of Contents

CITIZENS HOLDING COMPANY

INTERIM FINANCIAL STATEMENTS FOR QUARTER ENDED SEPTEMBER 30, 2011

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS (Unaudited).

CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF CONDITION (Unaudited)

	September 30, 2011	December 31, 2010
ASSETS		
Cash and due from banks	$ 19,537,859	$ 16,963,393
Interest bearing deposits with other banks	34,864,177	1,155,588
Investment securities available for sale, at fair value	316,094,724	324,730,301
Loans, net of allowance for loan losses of $7,404,418 in 2011 and $6,379,070 in 2010	398,595,158	415,496,720
Premises and equipment, net	20,828,016	20,751,478
Other real estate owned, net	4,557,194	3,068,209
Accrued interest receivable	4,736,881	4,823,227
Cash value of life insurance	20,060,314	19,535,300
Intangible assets, net	3,272,785	3,411,303
Other assets	4,060,157	8,297,213
TOTAL ASSETS	$ 826,607,265	$ 818,232,732
LIABILITIES AND STOCKHOLDERS EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$ 106,033,042	$ 95,324,759
Interest-bearing NOW and money market accounts	182,853,067	164,325,092
Savings deposits	41,367,112	37,778,537
Certificates of deposit	236,996,244	240,001,335
Total deposits	567,249,465	537,429,723
Federal Funds Purchased		2,500,000
Securities sold under agreement to repurchase	97,492,973	110,483,437
Federal Home Loan Bank advances	68,500,000	84,400,000
Accrued interest payable	367,628	538,881
Deferred compensation payable	4,914,455	4,330,069
Other liabilities	2,298,906	2,255,526
Total liabilities	740,823,427	741,937,636
STOCKHOLDERS EQUITY		
Common stock; $.20 par value, 22,500,000 shares authorized, 4,843,911 shares outstanding at September 30, 2011 and 4,838,411 shares outstanding at December 31, 2010	968,782	967,682
Additional paid-in capital	3,247,208	3,061,221
Retained earnings	76,699,648	74,464,123
Accumulated other comprehensive income (loss), net of tax expense of ($2,896,074) in 2011 and tax benefit of $1,307,540 in 2010	4,868,200	(2,197,930)

Total stockholders equity	85,783,838	76,295,096
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 826,607,265	$ 818,232,732

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

Table of Contents

CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	For the Three Months Ended September 30, 2011	2010	For the Nine Months Ended September 30, 2011	2010
INTEREST INCOME				
Loan income, including fees	$ 6,306,980	$ 6,982,131	$ 19,254,589	$ 21,247,055
Investment securities	3,101,121	2,459,128	8,924,368	7,487,294
Other interest	14,967	20,962	33,234	54,924
Total interest income	9,423,068	9,462,221	28,212,191	28,789,273
INTEREST EXPENSE				
Deposits	757,177	1,274,676	2,446,794	4,061,406
Other borrowed funds	833,020	906,420	2,592,724	2,670,169
Total interest expense	1,590,197	2,181,096	5,039,518	6,731,575
NET INTEREST INCOME	7,832,871	7,281,125	23,172,673	22,057,698
PROVISION FOR LOAN LOSSES	1,659,873	397,200	2,586,707	1,717,411
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	6,172,998	6,883,925	20,585,966	20,340,287
OTHER INCOME				
Service charges on deposit accounts	999,478	991,121	2,729,861	2,976,894
Other service charges and fees	474,171	400,299	1,303,304	1,146,696
Other income	973,163	343,500	1,514,508	1,405,245
Total other income	2,446,812	1,734,920	5,547,673	5,528,835
OTHER EXPENSES				
Salaries and employee benefits	3,518,464	3,465,713	10,562,176	10,314,413
Occupancy expense	1,081,113	1,017,538	3,188,602	2,955,888
Other operating expense	2,100,350	1,900,782	5,595,469	5,711,185
Total other expenses	6,699,927	6,384,033	19,346,247	18,981,486
INCOME BEFORE PROVISION FOR INCOME TAXES	1,919,883	2,234,812	6,787,392	6,887,636
PROVISION FOR INCOME TAXES	297,525	453,263	1,355,876	1,434,426
NET INCOME	$ 1,622,358	$ 1,781,549	$ 5,431,516	$ 5,453,210
NET INCOME PER SHARE				

-Basic	$	0.33	$	0.37	$	1.12	$	1.13
-Diluted	$	0.33	$	0.37	$	1.12	$	1.12
DIVIDENDS PAID PER SHARE	$	0.22	$	0.21	$	0.66	$	0.63

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

2

Table of Contents

CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2011	2010	2011	2010
Net income	$ 1,622,358	$ 1,781,549	$ 5,431,516	$ 5,453,210
Other comprehensive income, net of tax				
Unrealized holding gains (losses)	1,185,505	1,864,923	6,423,799	3,770,253
Reclassification adjustment for gains included in net income	636,542	17,446	642,331	635,459
Total other comprehensive income (loss)	1,822,047	1,882,369	7,066,130	4,405,712
Comprehensive income	$ 3,444,405	$ 3,663,918	$ 12,497,646	$ 9,858,922

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

Table of Contents

CITIZENS HOLDING COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the Nine Months Ended September 30, 2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net cash provided by operating activities	$ 9,650,546	$ 11,672,663
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities of securities available for sale	138,683,906	156,278,394
Proceeds from sales of securities available for sale	19,791,797	30,089,646
Purchases of investment securities available for sale	(138,881,327)	(180,842,931)
Net change in securities sold under agreement to repurchase	(12,990,464)	(3,260,447)
Purchases of bank premises and equipment	(967,408)	(2,363,088)
Increase in interest bearing deposits with other banks	(33,708,589)	(16,936,046)
Purchase of Federal Home Loan Bank Stock	(108,000)	(529,300)
Proceeds from sale of other real estate acquired by foreclosure	466,095	1,096,609
Net decrease in loans	12,350,775	15,334,054
Net cash used by investing activities	(15,363,215)	(1,133,109)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase (decrease) in deposits	29,819,741	(11,334,755)
Proceeds from exercising stock options	63,385	189,161
(Decrease) increase in Federal Home Loan Bank advances	(15,900,000)	10,000,000
Repurchase of stock		(366,381)
Decrease in federal funds purchased	(2,500,000)	
Payment of dividends	(3,195,991)	(3,046,341)
Net cash provided by (used by) financing activities	8,287,135	(4,558,316)
Net increase in cash and due from banks	2,574,466	5,981,238
Cash and due from banks, beginning of period	16,963,393	15,365,612
Cash and due from banks, end of period	$ 19,537,859	$ 21,346,850

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

Table of Contents

CITIZENS HOLDING COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

As of and for the three and nine months ended September 30, 2011

(Unaudited)

Note 1. Basis of Presentation

These interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). However, these financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. The interim consolidated financial statements are unaudited and reflect all adjustments and reclassifications, which, in the opinion of management, are necessary for a fair presentation of the results of operations and financial condition as of and for the interim periods presented. All adjustments and reclassifications are of a normal and recurring nature. Results for the period ended September 30, 2011, are not necessarily indicative of the results that may be expected for any other interim periods or for the year as a whole.

The interim consolidated financial statements of Citizens Holding Company include the accounts of its wholly-owned subsidiary, The Citizens Bank of Philadelphia (the Bank and collectively with Citizens Holding Company, the Corporation). All significant intercompany transactions have been eliminated in consolidation.

For further information and significant accounting policies of the Corporation, see the Notes to Consolidated Financial Statements of Citizens Holding Company included in the Corporation s Annual Report on Form 10-K for the year ended December 31, 2010, filed with the Securities and Exchange Commission on March 15, 2011.

Note 2. Commitments and Contingent Liabilities

In the ordinary course of business, the Corporation enters into commitments to extend credit to its customers. The unused portion of these commitments is not reflected in the accompanying financial statements. As of September 30, 2011, the Corporation had entered into loan commitments with certain customers with an aggregate unused balance of $33,120,963 compared to an aggregate unused balance of $36,011,792 at December 31, 2010. There were $3,209,825 of letters of credit outstanding at September 30, 2011 and $3,141,959 at December 31, 2010. The fair value of such contracts is not considered material because letters of credit and loan commitments often are not used in their entirety, if at all, before they expire. The balances of such letters and commitments should not be used to project actual future liquidity requirements. However, the Corporation does incorporate expectations about the level of draws under its credit-related commitments into its asset and liability management program.

The Corporation is a party to lawsuits and other claims that arise in the ordinary course of business, all of which are being vigorously contested. In the regular course of business, management evaluates estimated losses or costs related to litigation, and provisions are made for anticipated losses whenever management believes that such losses are probable and can be reasonably estimated. At the present time, management believes, based on the advice of legal counsel, that the final resolution of pending legal proceedings will not have a material impact on the Corporation s consolidated financial condition or results of operations.

Table of Contents

Note 3. Net Income per Share

Net income per share - basic has been computed based on the weighted average number of shares outstanding during each period. Net income per share - diluted has been computed based on the weighted average number of shares outstanding during each period plus the dilutive effect of outstanding stock options using the treasury stock method. Earnings per share was computed as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2011	2010	2011	2010
Basic weighted average shares outstanding	4,843,911	4,838,411	4,841,829	4,834,657
Dilutive effect of granted options	10,364	12,633	7,683	27,903
Diluted weighted average shares outstanding	4,854,275	4,851,044	4,849,512	4,862,560
Net income	$ 1,622,358	$ 1,781,549	$ 5,431,516	$ 5,453,210
Net income per share-basic	$ 0.33	$ 0.37	$ 1.12	$ 1.13
Net income per share-diluted	$ 0.33	$ 0.37	$ 1.12	$ 1.12

Note 4. Stock Option Plan

At September 30, 2011, the Corporation had one stock-based compensation plan, which is the 1999 Directors Stock Compensation Plan (the Directors Plan). Prior to its expiration, the Corporation also had the 1999 Employees Long-Term Incentive Plan, or the Employees Plan. The Corporation accounts for these plans under the stock compensation topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC). This topic provides guidance related to share-based payment transactions, including valuation methods (including assumptions such as expected volatility and expected term), the classification of compensation expense, non-GAAP financial measures, first-time adoption in an interim period and disclosure in Management s Discussion and Analysis subsequent to adoption.

On April 27, 2011, the members of the Board of Directors were granted a total of 13,500 options as specified in the Directors Plan. These options were granted at an exercise price of $20.02 per option, which was the closing price of Citizens Holding Company stock on that day. These options are first exercisable on October 28, 2011, and must be exercised no later than April 27, 2021.

The fair value of each option granted is estimated on the date of the grant using the Black-Scholes option-pricing model. The following assumptions were used in estimating the fair value of the options granted to the directors in the second quarter of 2011.

Table of Contents

Assumption	Directors
Dividend Yield	4.90%
Risk-Free Interest Rate	2.24%
Expected Life	8.1 years
Expected Volatility	74.47%
Calculated Value per Option	$ 9.16
Forfeitures	0.00%

Using the Black-Scholes option-pricing model with the foregoing assumptions, it was determined that the cost of options granted under the Directors Plan on April 27, 2011 was $123,702 and should be recognized as an expense of $20,617 per month over the six-month requisite service period, beginning on April 27, 2011. This was recorded as salary expense with a credit to paid-in capital. A deferred tax on these options was recorded in the aggregate amount of $46,140, or $7,690 per month, over the six-month requisite service period, beginning on April 27, 2011.

The following table below is a summary of the stock option activity for the three months ended September 30, 2011.

	Directors Plan		Employees Plan	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding at December 31, 2010	93,000	$ 20.65	136,500	$ 19.92
Granted	13,500	20.02		
Exercised	(4,500)	10.83	(1,000)	14.65
Expired				
Outstanding at September 30, 2011	102,000	$ 21.00	135,500	$ 19.96

The intrinsic value of options granted under the Directors Plan at September 30, 2011, was $37,200 and the intrinsic value of options granted under the Employees Plan at September 30, 2011, was $148,400 for a total intrinsic value at September 30, 2011, of $185,600.

Note 5. Income Taxes

The income tax topic of the ASC defines the threshold for recognizing the benefits of tax return positions in the financial statements as more-likely-than-not to be sustained by the taxing authority. This topic also provides guidance on the derecognition, measurement and classification of income tax uncertainties, along with any related interest and penalties, and includes guidance concerning accounting for income tax uncertainties in interim periods. As of September 30, 2011, the Corporation had no unrecognized tax benefits related to federal and state income tax matters. Therefore, the Corporation does not anticipate any material increase or decrease in the effective tax rate during 2011 relative to any tax positions taken. It is the Corporation s policy to recognize interest and/or penalties related to income tax matters in income tax expense.

Table of Contents

The Corporation files a consolidated United States federal income tax return. The Corporation is currently open to audit under the statute of limitations by the Internal Revenue Service for all tax years after 2007. The Corporation consolidated state income tax returns are also open to audit under the statute of limitations for the same period.

Note 6. Loans

The composition of net loans at September 30, 2011 and December 31, 2010 is as follows:

	September 30, 2011	December 31, 2010
	(In Thousands)	
Real Estate:		
Land Development and Construction	$ 12,422	$ 21,838
Farmland	37,081	44,734
1-4 Family Mortgages	137,876	143,627
Commercial Real Estate	134,211	139,760
Total Real Estate Loans	321,590	349,959
Business Loans:		
Commercial and Industrial Loans	43,457	28,429
Farm Production and other Farm Loans	1,799	2,429
Total Business Loans	45,256	30,858
Consumer Loans:		
Credit Cards	956	990
Other Consumer Loans	38,425	40,292
Total Consumer Loans	39,381	41,282
Total Gross Loans	406,227	422,099
Unearned income	(228)	(223)
Allowance for loan losses	(7,404)	(6,379)
Loans, net	$ 398,595	$ 415,497

Loans are considered to be past due if the required principal and interest payments have not been received as of the date such payments were due. Loans are placed on non-accrual status, when, in management s opinion, the borrower may be unable to meet payment obligations as they become due, as well as when required by regulatory provisions. Loans may be placed on non-accrual status regardless of whether or not such loans are considered past due. When interest accruals are discontinued, all unpaid accrued interest is reversed. Interest income is subsequently recognized only to the extent cash payments are received in excess of principal due. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Table of Contents

Period-end non-accrual loans, segregated by class of loans, were as follows:

	September 30, 2011	December 31, 2010
	(in thousands)	
Real Estate:		
Land Development and Construction	$ 697	$ 553
Farmland	896	581
1-4 Family Mortgages	2,030	1,741
Commercial Real Estate	6,600	6,590
Total Real Estate Loans	10,223	9,465
Business Loans:		
Commercial and Industrial Loans	1,132	1,250
Farm Production and other Farm Loans	18	8
Total Business Loans	1,150	1,258
Consumer Loans:		
Credit Cards		
Other Consumer Loans	333	209
Total Consumer Loans	333	209
Total Non-Accrual Loans	$ 11,706	$ 10,932

Table of Contents

An age analysis of past due loans, segregated by class of loans, as of September 30, 2011, was as follows (in thousands):

	Loans 30-89 Days Past Due	Loans 90 or more Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or more Days Past Due
Real Estate:						
Land Development and Construction	$ 556	$ 696	$ 1,252	$ 11,170	$ 12,422	$
Farmland	658	896	1,554	35,527	37,081	
1-4 Family Mortgages	3,868	2,078	5,946	131,930	137,876	35
Commercial Real Estate	6,789	6,601	13,390	120,821	134,211	
Total Real Estate Loans	11,871	10,271	22,142	299,448	321,590	35
Business Loans:						
Commercial and Industrial Loans	199	1,119	1,318	42,139	43,457	
Farm Production and other Farm Loans	26	28	54	1,745	1,799	10
Total Business Loans	225	1,147	1,372	43,884	45,256	10
Consumer Loans:						
Credit Cards	29	14	43	913	956	14
Other Consumer Loans	1,791	1,482	3,273	35,152	38,425	2
Total Consumer Loans	1,820	1,496	3,316	36,065	39,381	16
Total Loans	$ 13,916	$ 12,914	$ 26,830	$ 379,397	$ 406,227	$ 61

Table of Contents

An age analysis of past due loans, segregated by class of loans, as of December 31, 2010 was as follows (in thousands):

	Loans 30-89 Days Past Due	Loans 90 or more Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or more Days Past Due
Real Estate:						
Land Development and Construction	$ 312	$ 808	$ 1,120	$ 20,718	$ 21,838	$ 447
Farmland	1,675	417	2,092	42,642	44,734	115
1-4 Family Mortgages	5,231	808	6,039	137,588	143,627	63
Commercial Real Estate	1,564	95	1,659	138,101	139,760	
Total Real Estate Loans	8,782	2,128	10,910	339,049	349,959	625
Business Loans:						
Commercial and Industrial Loans	1,763	502	2,265	26,164	28,429	300
Farm Production and other Farm Loans	39	5	44	2,385	2,429	5
Total Business Loans	1,802	507	2,309	28,549	30,858	305
Consumer Loans:						
Credit Cards	21	70	91	899	990	70
Other Consumer Loans	2,268	139	2,407	37,885	40,292	23
Total Consumer Loans	2,289	209	2,498	38,784	41,282	93
Total Loans	$ 12,873	$ 2,844	$ 15,717	$ 406,382	$ 422,099	$ 1,023

Loans are considered impaired when, based on current information and events, it is probable the Corporation will be unable to collect all the amounts due in accordance with the original contractual terms of the loan agreement, including scheduled principal and interest payments. In determining which loans to evaluate for impairment, management looks at past due loans, bankruptcy filing and any situation that might lend itself to cause a borrower to be unable to repay the loan according to the original contract terms. If a loan is determined to be impaired and the collateral is deemed to be insufficient to fully repay the loan, a specific reserve will be established. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans or portions thereof, are charged-off when deemed uncollectible.

Table of Contents

Impaired loans as of September 30, 2011 and December 31, 2010, by class of loans, are as follows (in thousands):

September 30, 2011	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Real Estate:						
Land Development and Construction	$ 697	$ 550	$ 147	$ 697	$ 133	$ 714
Farmland	896	829	67	896	25	645
1-4 Family Mortgages	2,129	1,170	959	2,129	231	2,014
Commercial Real Estate	6,988	4,654	2,334	6,988	832	7,047
Total Real Estate Loans	10,710	7,203	3,505	10,710	1,221	10,420
Business Loans:						
Commercial and Industrial Loans	1,131	195	936	1,131	868	790
Farm Production and other Farm Loans	18	18		18		12
Total Business Loans	1,149	213	936	1,149	868	802
Consumer Loans:						
Credit Cards						
Other Consumer Loans	333	328	5	333		313
Total Consumer Loans	333	328	5	333		313
Total Loans	$ 12,192	$ 7,744	$ 4,448	$ 12,192	$ 2,089	$ 11,535

December 31, 2010	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Real Estate:						
Land Development and Construction	$ 553	$ 391	$ 162	$ 553	$ 156	$ 630
Farmland	581	394	187	581	79	534
1-4 Family Mortgages	1,840	967	873	1,840	196	1,801
Commercial Real Estate	6,981	4,443	2,538	6,981	832	6,975
Total Real Estate Loans	9,955	6,195	3,760	9,955	1,263	9,940
Business Loans:						
Commercial and Industrial Loans	1,342	1,017	325	1,342	194	1,436
Farm Production and other Farm Loans	7	7		7		17
Total Business Loans	1,349	1,024	325	1,349	194	1,453
Consumer Loans:						
Credit Cards						
Other Consumer Loans	209	135	74	209	21	206
Total Consumer Loans	209	135	74	209	21	206
Total Loans	$ 11,513	$ 7,354	$ 4,159	$ 11,513	$ 1,478	$ 11,599

The Corporation utilizes a risk grading matrix to assign a risk grade to each of its loans when originated and is updated as factors related to the strength of the loan changes. Loans are graded on a scale of 1 to 9. A description of the general characteristics of the 9 risk grades is as follows.

Grade 1. MINIMAL RISK - These loans are without loss exposure to the Corporation. This classification is reserved for only the best, well secured loans to borrowers with significant capital strength, low leverage, stable earnings and growth and other readily available financing alternatives. This type of loan would also include loans secured by a program of the government.

Grade 2. MODEST RISK - These loans include borrowers with solid credit quality and moderate risk of loss. These loans may be fully secured by certificates of deposit with another reputable financial institution, or secured by readily marketable securities with acceptable margins.

Grade 3. AVERAGE RISK - This is the rating assigned to most of the loans held by the Corporation. This includes loans with average loss exposure and average overall quality. These loans should liquidate through possessing adequate collateral and adequate earnings of the borrower. In addition, these loans are properly documented and are in accordance with all aspects of the current loan policy.

Table of Contents

Grade 4. ACCEPTABLE RISK-Borrower generates sufficient cash flow to fund debt service but most working asset and capital expansion needs are provided from external sources. Profitability and key balance sheet ratios are usually close to peers but one or more may be higher than peers.

Grade 5. MANAGEMENT ATTENTION- Borrower has significant weaknesses resulting from performance trends or management concerns. The financial condition of the borrower has taken a negative turn and may be temporarily strained. Cash flow is weak but cash reserves remain adequate to meet debt service. Management weakness is evident.

Grade 6. OTHER LOANS ESPECIALLY MENTIONED (OLEM) - Loans in this category are fundamentally sound but possess some weaknesses. OLEM loans have potential weaknesses which may, if not checked or corrected, weaken the asset or inadequately protect the bank s credit position at some future date. These loans have an identifiable weakness in credit, collateral, or repayment ability but there is no expectation of loss.

Grade 7. SUBSTANDARD ASSETS - Assets classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Assets classified as substandard must have a well-defined weakness based upon objective evidence. Assets classified as substandard are characterized by the distinct possibility that the insured institution will sustain some loss if the deficiencies are not corrected. The possibility that liquidation would not be timely requires a substandard classification even if there is little likelihood of total loss.

Grade 8. DOUBTFUL - A loan classified as doubtful has all the weaknesses of a substandard classification and the added characteristic that the weakness makes collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable or improbable. The possibility of loss is extremely high, but because of certain important and reasonable specific pending factors which may work to the advantage and strengthening of the asset, its classification as an estimated loss is deferred until its more exact status may be determined. A doubtful classification could reflect the fact that the primary source of repayment is gone and serious doubt exists as to the quality of a secondary source of repayment.

Grade 9. LOSS - Loans classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may occur in the future. Also included in this classification is the defined loss portion of loans rated substandard assets and doubtful assets.

These internally assigned grades are updated on a continual basis throughout the course of the year and represent management s most updated judgment regarding grades at September 30, 2011.

Table of Contents

The following table details the amount of gross loans by loan grade and class as of September 30, 2011 (in thousands):

Grades	Satisfactory 1, 2, 3, 4	Special Mention 5,6	Substandard 7	Doubtful 8	Loss 9	Total Loans
Real Estate:						
Land Development and Construction	$ 8,571	$ 2,326	$ 1,525	$	$	$ 12,422
Farmland	32,236	3,050	1,758	37		37,081
1-4 Family Mortgages	118,680	6,162	13,007	27		137,876
Commercial Real Estate	110,532	9,506	14,173			134,211
Total Real Estate Loans	270,019	21,044	30,463	64		321,590
Business Loans:						
Commercial and Industrial Loans	40,382	1,301	927	36	811	43,457
Farm Production and other Farm Loans	1,696	8	95			1,799
Total Business Loans	42,078	1,309	1,022	36	811	45,256
Consumer Loans:						
Credit Cards	886		70			956
Other Consumer Loans	36,742	310	1,355	14	4	38,425
Total Consumer Loans	37,628	310	1,425	14	4	39,381
Total Loans	$ 349,725	$ 22,663	$ 32,910	$ 114	$ 815	$ 406,227

15

Table of Contents

The following table details the amount of gross loans by loan grade and class as of December 31, 2010:

Grades	Satisfactory 1, 2, 3,4	Mention 5,6	Substandard 7	Doubtful 8	Loss 9	Total Loans
Real Estate:						
Land Development and Construction	$ 20,165	$ 65	$ 1,608	$	$	$ 21,838
Farmland	40,462	2,210	2,062			44,734
1-4 Family Mortgages	128,505	1,966	13,130	26		143,627
Commercial Real Estate	127,851	542	11,367			139,760
Total Real Estate Loans	316,983	4,783	28,167	26		349,959
Business Loans:						
Commercial and Industrial Loans	26,062	608	1,739	16	4	28,429
Farm Production and other Farm Loans	2,363	14	52			2,429
Total Business Loans	28,425	622	1,791	16	4	30,858
Consumer Loans:						
Credit Cards	920		70			990
Other Consumer Loans	38,674	34	1,571	10	3	40,292
Total Consumer Loans	39,594	34	1,641	10	3	41,282
Total Loans	$ 385,002	$ 5,439	$ 31,599	$ 52	$ 7	$ 422,099

The allowance for loan losses is a reserve established through a provision for possible loan losses charged to expense, which represents management s best estimate of probable losses that will occur within the existing portfolio of loans. The allowance, in the judgment of management, is necessary to reserve for estimated loan losses and risks inherent in the loan portfolio.

The allowance on the majority of the loan portfolio is calculated using a historical chargeoff percentage applied to the current loan balances by loan segment. This historical period is the average of the previous 5 years with the most current years weighted to show the effect of the most recent chargeoff activity. This percentage is also adjusted for economic factors such as local unemployment and general business conditions, both local and nationwide.

The group of loans that are considered to be impaired are individually evaluated for possible loss and a specific reserve is established to cover any loss contingency. Loans that are determined to be a loss with no benefit of remaining in the portfolio are charged off to the allowance. These specific reserves are reviewed periodically for continued impairment and adequacy of the specific reserve and adjusted when necessary.

Table of Contents

The following table details activity in the allowance for possible loan losses by portfolio segment for the nine months ended September 30, 2011:

September 30, 2011	Real Estate	Business Loans	Consumer	Total
Beginning Balance, January 1, 2011	$ 4,306,691	$ 1,104,706	$ 967,673	$ 6,379,070
Provision for possible loan losses	1,526,083	1,079,771	(19,147)	2,586,707
Chargeoffs	1,273,951	182,092	202,037	1,658,080
Recoveries	17,551	8,752	70,418	96,721
Net Chargeoffs	1,256,400	173,340	131,619	1,561,359
Ending Balance	$ 4,576,374	$ 2,011,137	$ 816,907	$ 7,404,418
Period end allowance allocated to:				
Loans individually evaluated for impairment	1,220,686	868,355	62	2,089,103
Loans collectively evaluated for impairment	3,355,688	1,142,782	816,845	5,315,315
Ending Balance, September 30, 2011	$ 4,576,374	$ 2,011,137	$ 816,907	$ 7,404,418

Activity in the allowance for possible loan losses for the nine months ended September 30, 2010 was as follows:

	September 30, 2010
Balance, beginning of period	$ 5,525,927
Provision for loan losses	1,717,411
Loans charged off	(1,135,887)
Recoveries of loans previously charged off	188,128
Balance, end of period	$ 6,295,579

Table of Contents

The Corporation s recorded investment in loans as of September 30, 2011 and December 31, 2010 related to each balance in the allowance for possible loan losses by portfolio segment and disaggregated on the basis of the Corporation s impairment methodology was as follows (in thousands):

September 30, 2011	Real Estate	Business Loans	Consumer	Total
Loans individually evaluated for impairment	$ 10,710	$ 1,149	$ 333	$ 12,192
Loans collectively evaluated for impairment	310,880	44,107	39,048	394,035
	$ 321,590	$ 45,256	$ 39,381	$ 406,227

December 31, 2010	Real Estate	Business Loans	Consumer	Total
Loans individually evaluated for impairment	$ 9,955	$ 1,349	$ 209	$ 11,513
Loans collectively evaluated for impairment	340,004	29,509	41,073	410,586
	$ 349,959	$ 30,858	$ 41,282	$ 422,099

Note 7. Recent Accounting Pronouncements

In April 2011, FASB issued an update to ASC Topic 310. The update clarifies which loan modifications constitute troubled debt restructurings and is intended to assist creditors in determining whether a modification of the terms of a receivable meets the criteria to be considered a troubled debt restructuring, both for purposes of recording an impairment loss and for disclosure of troubled debt restructurings. In evaluating whether a restructuring constitutes a troubled debt restructuring, a creditor must separately conclude that both of the following exist: (a) the restructuring constitutes a concession; and (b) the debtor is experiencing financial difficulties. This update became effective for the Corporation on July 1, 2011, and applies retrospectively to restructurings occurring on or after January 1, 2011. This update has not had a significant impact on the Corporation s financial position, results of operations or stockholders equity.

In April 2011, FASB issued an update to ASC Topic 860 which is intended to improve financial reporting of repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. This update removes from the assessment of effective control (i) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (ii) the collateral maintenance guidance related to that criterion. This update will be effective for the Corporation on January 1, 2012 and is not expected to have a significant impact on the Corporation s consolidated financial statements.

Table of Contents

In May 2011, FASB issued an update to ASC Topic to converge the fair value measurement guidance in U.S. generally accepted accounting principles and International Financial Reporting Standards. This update clarifies the application of existing fair value measurement requirements, changes certain principles in Topic 820 and requires additional fair value disclosures. This update will be effective for annual and interim reporting periods beginning after December 15, 2011, and is not expected to have a significant impact on the Corporation s financial statements.

In June 2011, FASB issued an update to ASC Topic 220 to require that all non-owner changes in stockholders equity be presented in either a single continuous statement of comprehensive income or in two separate but consecutive statements. Additionally, the update requires entities to present, on the face of the financial statements, reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement or statements where the components of net income and the components of other comprehensive income are presented. The option to present components of other comprehensive income as part of the statement of changes in stockholders equity was eliminated. This update is effective for annual periods beginning after December 15, 2011, and is not expected to have an impact on the Corporation s financial statements.

In September 2011, FASB issued an update to ASC Topic 350 to give entities the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test is unnecessary. However, if an entity concludes otherwise, then it is required to perform the first step of the two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit. This update is effective for annual and interim impairment tests beginning after December 15, 2011, and is not expected to have a significant impact on the Corporation s financial statements.

Note 8. Fair Value of Financial Instruments

The fair value topic of the ASC establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. This topic clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. This topic also requires disclosure about how fair value was determined for assets and liabilities and establishes a hierarchy for which these assets and liabilities must be grouped, based on significant levels of inputs as follows:

Level 1	Quoted prices in active markets for identical assets or liabilities;
Level 2	Quoted prices in active markets for similar assets and liabilities and inputs that are observable for the asset or liability; or
Level 3	Unobservable inputs, such as discounted cash flow models or valuations.

Table of Contents

The determination of where assets and liabilities fall within this hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

The following table presents assets and liabilities that are measured at fair value on a recurring basis as of September 30, 2011:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Securities available for sale				
Obligations of U. S. Government Agencies	$	$ 173,717,732	$	$ 173,717,732
Mortgage-backed Securities		37,726,324		37,726,324
Other investments		102,544,907	2,105,761	104,650,668
Total	$	$ 313,988,963	$ 2,105,761	$ 316,094,724

The following table presents assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2010:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Securities available for sale				
Obligations of U. S. Government Agencies	$	$ 186,157,928	$	$ 186,157,928
Mortgage-backed Securities		37,759,943		37,759,943
Other investments		98,927,753	1,884,677	100,812,430
Total	$	$ 322,845,624	$ 1,884,677	$ 324,730,301

Table of Contents

The following table reports the activity for 2011 in assets measured at fair value on a recurring basis using significant unobservable inputs.

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Structured Financial Product	
Balance at January 1, 2011	$	1,884,677
Unrealized gains included in other comprehensive income		221,084
Balance at September 30, 2011	$	2,105,761

As of September 30, 2011, management determined, based on the current credit ratings, known defaults and deferrals by the underlying banks and the degree to which future defaults and deferrals would be required to occur before the cash flow for the Corporation s tranche is negatively impacted, that no other-than-temporary impairment exists.

The Corporation recorded no gains or losses in earnings for the period that were attributable to the change in unrealized gains or losses relating to assets still held at the reporting date.

For assets measured at fair value on a nonrecurring basis during 2011 that were still held in the balance sheet at September 30, 2011, the following table provides the hierarchy level and the fair value of the related assets:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Impaired loans	$	$	$ 3,598,611	$ 3,598,611
Other real estate owned			1,868,000	1,868,000
Total	$	$	$ 5,466,611	$ 5,466,611

Table of Contents

For assets measured at fair value on a nonrecurring basis during 2010 that were still held in the balance sheet at December 31, 2010, the following table provides the hierarchy level and the fair value of the related assets:

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Impaired loans	$	$	$ 2,680,775	$ 2,680,775
Other real estate owned			2,172,198	2,172,198
Total	$	$	$ 4,852,973	$ 4,852,973

Impaired loans with a carrying value of $4,447,562 and $4,159,181 had an allocated allowance for loan losses of $2,089,103 and $1,478,406 at September 30, 2011 and December 31, 2010, respectively. The allocated allowance is based on the carrying value of the impaired loan and the fair value of the underlying collateral less estimated costs to sell.

Other real estate owned (OREO) acquired during the nine-month period ended September 30, 2011, and recorded at fair value, less costs to sell, was $1,868,000. There have been no writedowns during the period on OREO previously acquired and still held. OREO acquired during 2010 and recorded at fair value, less costs to sell, was $973,758. Additional writedowns during 2010 on OREO previously acquired was $112,060 on five properties valued at $1,198,440.

The financial instruments topic of the ASC requires disclosure of financial instruments fair values, as well as the methodology and significant assumptions used in estimating fair values. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. The financial instruments topic of the ASC excludes certain financial instruments from its disclosure requirements. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Corporation and may not be indicative of amounts that might ultimately be realized upon disposition or settlement of those assets and liabilities.

Table of Contents

The following represents the carrying value and estimated fair value of the Corporation s financial instruments at September 30, 2011, and December 31, 2010:

	September 30, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and due from banks	$ 19,537,859	$ 19,537,859	$ 16,963,393	$ 16,963,393
Interest bearing deposits with banks	34,864,177	34,864,177	1,155,588	1,155,588
Securities available-for-sale	316,094,724	316,094,724	324,730,301	324,730,301
Net loans	398,595,158	398,174,752	415,496,720	415,605,513
Financial liabilities				
Deposits	$ 567,249,465	$ 567,525,720	$ 537,429,723	$ 537,751,275
Federal Home Loan Bank advances	68,500,000	72,181,021	84,400,000	88,038,797
Federal funds purchased			2,500,000	2,500,000
Securities Sold under agreement to repurchase	97,492,973	97,492,973	110,483,437	110,483,437

The fair value estimates, methods and assumptions used by the Corporation in estimating its fair value disclosures for financial statements were as follows:

Cash and Due from Banks and Interest Bearing Deposits with Banks

The carrying amounts reported in the balance sheet for these instruments approximate fair value because of their immediate and shorter-term maturities, which are considered to be three months or less when purchased.

Securities Available-for-Sale

Fair values for investment securities are based on quoted market prices, when available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. When neither quoted prices nor comparable instruments are available, unobservable inputs are needed to form an expected future cash flow analysis to establish fair values. Level 2 securities include debt securities such as obligations of United States government agencies and corporations, mortgage-backed securities and state, county and municipal bonds. Level 3 securities consist of a pooled trust preferred security.

Net Loans

For variable-rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values for other loans (i.e., commercial real estate and rental property mortgage loans, commercial and industrial loans, financial institution loans, and agricultural loans) are estimated using discounted cash flow analyses, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. The carrying amount of accrued interest receivable approximates its fair value.

Table of Contents

Impaired Loans

Loans considered impaired are reserved for at the time the loan is identified as impaired taking into account the fair value of the collateral less estimated selling costs. Collateral may be real estate and/or business assets including but not limited to, equipment, inventory and accounts receivable. The fair value of real estate is determined based on appraisals by qualified licensed appraisers. The fair value of the business assets is generally based on amounts reported on the business financial statements. Appraised and reported values may be adjusted based on management s historical knowledge, changes in market conditions from the time of valuation and management s knowledge of the client and the client s business. Since not all valuation inputs are observable, these nonrecurring fair value determinations are classified Level 3. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly, based on the same factors previously identified.

Other real estate owned

OREO is comprised of commercial and residential real estate obtained in partial or total satisfaction of loan obligations. OREO acquired in settlement of indebtedness is recorded at fair value of the real estate, less costs to sell. Subsequently, it may be necessary to record nonrecurring fair value adjustments for decline in fair value. Fair value, when recorded, is determined based on appraisals by qualified licensed appraisers and adjusted for management s estimates of costs to sell. As such, values for OREO are classified as Level 3.

Deposits

The fair values for demand deposits, NOW and money market accounts and savings accounts are, by definition, equal to the amount payable on demand at the reporting date (i.e., their carrying amounts). The carrying amounts for variable-rate, fixed-term money market accounts and time deposits approximate their fair values at the reporting date. Fair values for fixed-rate time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Federal Home Loan Bank (FHLB) Borrowings

The fair value of FHLB advances is based on discounted cash flow analysis.

Federal Funds Sold and Purchased and Commercial Repurchase Agreements

Due to the short term nature of these instruments, which is considered to be three months or less, the carrying amount is equal to the fair value.

Off-Balance Sheet Instruments

The fair value of commitments to extend credit and letters of credit are estimated using fees currently charged to enter into similar agreements. The fees associated with these financial instruments are not material.

Table of Contents

CITIZENS HOLDING COMPANY

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

FORWARD LOOKING STATEMENTS

In addition to historical information, this report contains statements which constitute forward-looking statements and information within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, which are based on management s beliefs, plans, expectations and assumptions and on information currently available to management. The words may, should, expect, anticipate, intend, plan, continue, believe, seek, estimate and similar expressions used in this report that do not re facts are intended to identify forward-looking statements. These statements appear in a number of places in this report, including, but not limited to, statements found in Item 1, Notes to Consolidated Financial Statements and in Item 2, Management s Discussion and Analysis of Financial Condition and Results of Operations. The Corporation notes that a variety of factors could cause the actual results or experience to differ materially from the anticipated results or other expectations described or implied by such forward-looking statements. The risks and uncertainties that may affect the operation, performance, development and results of the Corporation s business include, but are not limited to, the following: (a) the risk of adverse changes in business conditions in the banking industry generally and in the specific markets in which the Corporation operates; (b) changes in the legislative and regulatory environment that negatively impact the Corporation through increased operating expenses; (c) increased competition from other financial institutions; (d) the impact of technological advances; (e) expectations about the movement of interest rates, including actions that may be taken by the Federal Reserve Board in response to changing economic conditions; (f) changes in asset quality and loan demand; (g) expectations about overall economic strength and the performance of the economies in the Corporation s market area; and (h) other risks detailed from time to time in the Corporation s filings with the Securities and Exchange Commission. The Corporation does not undertake any obligation to update or revise any forward-looking statements subsequent to the date on which they are made.

Table of Contents

Management s discussion and analysis is intended to provide greater insight into the results of operations and the financial condition of Citizens Holding Company and its wholly owned subsidiary, The Citizens Bank of Philadelphia (the Bank, and collectively with Citizens Holding Company, the Corporation). The following discussion should be read in conjunction with the consolidated financial statements and notes appearing elsewhere in this report.

LIQUIDITY

The Corporation has an asset and liability management program that assists management in maintaining net interest margins during times of both rising and falling interest rates and in maintaining sufficient liquidity. A measurement of liquidity is the ratio of net deposits and short-term liabilities divided by the sum of net cash, short-term investments and marketable assets. This measurement for liquidity of the Corporation at September 30, 2011, was 25.26% and at December 31, 2010, was 19.98%. Liquidity increased due to the amount of investment securities that were called and not reinvested at September 30, 2011. Management believes it maintains adequate liquidity for the Corporation s current needs.

The Corporation s primary source of liquidity is customer deposits, which were $567,249,565 at September 30, 2011, and $537,429,723 at December 31, 2010. Other sources of liquidity include investment securities, the Corporation s line of credit with the Federal Home Loan Bank (FHLB) and federal funds lines with correspondent banks. The Corporation had $316,094,724 invested in investment securities at September 30, 2011, and $324,730,301 at December 31, 2010. The Corporation had secured and unsecured federal funds lines with correspondent banks in the amount of $37,500,000 at September 30, 2011 and $46,400,000 at December 31, 2010. The Corporation lowered its available federal funds lines with correspondent banks after an assessment of prior use and the need for this line in the future. In addition, the Corporation has the ability to draw on its line of credit with the FHLB. At September 30, 2011, the Corporation had unused and available $129,644,221 of its line of credit with the FHLB and at December 31, 2010, the Corporation had unused and available $119,501,966 of its line of credit with the FHLB. The increase in the amount available under the Corporation s line of credit with the FHLB from the end of 2010 to September 30, 2011, was mostly the result of a decrease in advances outstanding.

The Corporation had no federal funds purchased as of September 30, 2011. As of December 31, 2010, the Corporation had federal funds purchased in the amounts of $2,500,000. The Corporation usually purchases funds from correspondent banks on a temporary basis to meet short term funding needs.

When the Corporation has more funds than it needs for its reserve requirements or short-term liquidity needs, the Corporation increases its investment portfolio, increases the balances in interest bearing due from accounts or sells federal funds. It is management s policy to maintain an adequate portion of its portfolio of assets and liabilities on a short-term basis to insure rate flexibility and to meet loan funding and liquidity needs. When deposits decline or do not grow sufficiently to fund loan demand, management will seek funding either through federal funds purchased or advances from the FHLB.

Table of Contents

CAPITAL RESOURCES

The Corporation s equity capital was $85,783,838 at September 30, 2011, as compared to $76,295,096 at December 31, 2010. One of the reasons for the increase in equity capital was net earnings in excess of dividends paid. Equity capital was also positively impacted by the investment securities market value adjustment due to an increase in the market value of the Corporation s investment portfolio. This market value increase was due to general market conditions, specifically the decrease in short term interest rates, which caused an increase in the market price of the investment portfolio.

Cash dividends in the amount of $3,195,991, or $0.66 per share, have been paid in 2011 as of the end of the third quarter.

Quantitative measures established by federal regulations to ensure capital adequacy require the Corporation to maintain minimum amounts and ratios of Total and Tier 1 capital (primarily common stock and retained earnings, less goodwill) to risk weighted assets, and of Tier 1 capital to average assets. Management believes that as of September 30, 2011, the Corporation meets all capital adequacy requirements to which it is subject.

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Actions Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of September 30, 2011						
Total Capital (to Risk-Weighted Assets)	$ 83,756,263	17.17%	$ 39,022,541	>8.00%	$ 48,778,176	>10.00%
Tier 1 Capital (to Risk-Weighted Assets)	77,642,853	15.92%	19,511,270	>4.00%	29,266,906	>6.00%
Tier 1 Capital (to Average Assets)	77,642,853	9.32%	33,315,533	>4.00%	41,644,416	>5.00%

27

Table of Contents

RESULTS OF OPERATIONS

The following table sets forth for the periods indicated, certain items in the consolidated statements of income of the Corporation and the related changes between those periods:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2011	2010	2011	2010
Interest Income, including fees	$ 9,423,068	$ 9,462,221	$ 28,212,191	$ 28,789,273
Interest Expense	1,590,197	2,181,096	5,039,518	6,731,575
Net Interest Income	7,832,871	7,281,125	23,172,673	22,057,698
Provision for Loan Losses	1,659,873	397,200	2,586,707	1,717,411
Net Interest Income after Provision for Loan Losses	6,172,998	6,883,925	20,585,966	20,340,287
Other Income	2,446,812	1,734,920	5,547,673	5,528,835
Other Expense	6,699,927	6,384,033	19,346,247	18,981,486
Income before Provision For Income Taxes	1,919,883	2,234,812	6,787,392	6,887,636
Provision for Income Taxes	297,525	453,263	1,355,876	1,434,426
Net Income	$ 1,622,358	$ 1,781,549	$ 5,431,516	$ 5,453,210
Net Income Per share - Basic	$ 0.33	$ 0.37	$ 1.12	$ 1.13
Net Income Per Share-Diluted	$ 0.33	$ 0.37	$ 1.12	$ 1.12

See Note 3 to the Corporation s Consolidated Financial Statements for an explanation regarding the Corporation s calculation of Net Income Per Share - basic and - diluted.

Annualized return on average equity (ROE) was 7.68% for the three months ended September 30, 2011, and 8.89% for the corresponding period in 2010. For the nine months ended September 30, 2011, ROE was 8.93% compared to 9.29% for the nine months ended September 30, 2010. In both instances, the decrease in ROE was caused by a slight increase in average equity along with an decrease in net income for the three and nine months of 2011.

The book value per share increased to $17.73 at September 30, 2011, compared to $15.77 at December 31, 2010. The increase in book value per share reflects the increase in equity due to the amount of earnings in excess of dividends and the increase in other comprehensive income due to the increase in market value of the Corporation s investment securities. Average assets for the nine months ended September 30, 2011, were $828,386,995 compared to $839,212,189 for the year ended December 31, 2010.

Table of Contents

NET INTEREST INCOME / NET INTEREST MARGIN

One component of the Corporation s earnings is net interest income, which is the difference between the interest and fees earned on loans and investments and the interest paid for deposits and borrowed funds. The net interest margin is net interest income expressed as a percentage of average earning assets.

The annualized net interest margin was 4.31% for the third quarter of 2011 compared to 3.96% for the corresponding period of 2010. For the nine months ended September 30, 2011, annualized net interest margin was 4.28% compared to 4.04% for the nine months ended September 30, 2010. The increase in net interest margin from 2010 to 2011 is the result of an increase in yields on earning assets compared to the decrease in rates paid on deposits and borrowed funds, along with a decrease in average earning assets, as detailed below. Earning assets averaged $760,797,459 for the three months ended September 30, 2011. This represents a decrease of $9,116,654, or 1.2%, over average earning assets of $769,914,113 for the three month period ended September 30, 2010. Earning assets averaged $752,606,627 for the nine months ended September 30, 2011. This represents a decrease of $11,527,279, or 1.5% over average earning assets of $764,133,906 for the nine months ended September 30, 2010. The decrease in earning assets for the three and nine months ended September 30, 2011, is the result of the declining loan demand and decline in deposits due to current local, national and international economic conditions.

Interest bearing deposits averaged $455,677,955 for the three months ended September 30, 2011. This represents a decrease of $17,010,258, or 3.6%, from the average of interest bearing deposits of $472,688,213 for the three-month period ended September 30, 2010. This was due, in large part, to a decrease in certificates of deposit.

Other borrowed funds averaged $190,689,061 for the three months ended September 30, 2011. This represents a decrease of $6,978,174, or 3.5%, over the other borrowed funds of $197,667,235 for the three-month period ended September 30, 2010. This decrease in other borrowed funds was due to a $7,969,551 decrease in the Commercial Repo Liability, a $215,145 decrease in the ABE Loan Liability, a $56,522 decrease in Federal Funds Purchased and an increase in the FHLB advances of $1,263,044 for the three-month period ended September 30, 2011, when compared to the three-month period ended September 30, 2010.

Interest bearing deposits averaged $444,477,323 for the nine-month period ended September 30, 2011. This represents a decrease of $26,706,962, or 5.7% from the average of interest bearing deposits of $471,184,285 for the nine-month period ended September 30, 2010. This was due, in large part, to a decrease in certificates of deposit and interest bearing transaction accounts.

Other borrowed funds averaged $200,600,755 for the nine months ended September 30, 2011. This represents an increase of $5,384,359, or 2.8% over the other borrowed funds of $195,216,396 for the nine-month period ended September 30, 2010. This increase in other borrowed funds was due to a $4,448,233 increase in the Commercial Repo Liability, a $210,028

Table of Contents

decrease in the ABE Loan Liability, a $595,971 increase in Federal Funds Purchased and an increase in the Federal Home Loan Bank advances of $550,183 for the nine-month period ended September 30, 2011, when compared to the nine-month period ended September 30, 2010.

Net interest income was $7,832,871 for the three-month period ended September 30, 2011, an increase of $551,746 from $7,281,125 for the three-month period ended September 30, 2010, primarily due to changes in rate. The changes in volume in earning assets and in deposits and in borrowed funds are discussed above. As to changes in rate in the three-month period ended September 30, 2011, the yield on earning assets increased while the rates paid on deposits and borrowed funds decreased from the same period in 2010. The yield on all interest bearing assets increased 5 basis points to 5.15% in the third quarter of 2011 from 5.10% for the same period in 2010. At the same time, the rate paid on all interest bearing liabilities for the third quarter of 2011 decreased by 23 basis points to 0.99% from 1.22% in the same period of 2010. As longer term interest bearing assets and liabilities mature and reprice, management believes that the yields on interest bearing assets and rates on interest bearing liabilities will both decrease.

Net interest income was $23,172,673 for the nine months ended September 30, 2011, an increase of $563,229 from the $22,057,698 for the nine-months ended September 30, 2010, primarily due to changes in both rate and volume. The changes in volume in earning assets and in deposits and in borrowed funds are discussed above. As to changes in rate, in the nine-month period ended September 30, 2011, the rates paid on deposits and borrowed funds decreased more than the yield on earning assets as compared to the changes in rates and yields in the same period of 2010. The yield on all interest bearing assets decreased 4 basis points to 5.17% in the first nine months of 2011 from 5.21% for the same period in 2010. At the same time, the rate paid on all interest bearing liabilities for the first nine months of 2011 decreased 31 basis points to 1.04% from 1.35% in the same period in 2010. As longer term interest bearing assets and liabilities mature and reprice, management believes that the yields on interest bearing assets and rates on interest bearing liabilities will both decrease.

The following table shows the interest and fees and corresponding yields for loans only.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2011	2010	2011	2010
Interest and Fees	$ 6,306,980	$ 6,982,131	$ 19,254,589	$ 21,247,055
Average Gross Loans	406,037,412	432,742,314	412,278,737	441,440,344
Annualized Yield	6.21%	6.45%	6.23%	6.42%

The decrease in interest rates in the three-month period ended September 30, 2011, reflects the decrease in all loan interest rates for both new and refinanced loans in the period.

Table of Contents

CREDIT LOSS EXPERIENCE

As a natural corollary to the Corporation s lending activities, some loan losses are to be expected. The risk of loss varies with the type of loan being made and the overall creditworthiness of the borrower over the term of the loan. The degree of perceived risk is taken into account in establishing the structure of, and interest rates and security for, specific loans and for various types of loans. The Corporation attempts to minimize its credit risk exposure by use of thorough loan application and approval procedures.

The Corporation maintains a program of systematic review of its existing loans. Loans are graded for their overall quality. Those loans, which the Corporation s management determines require further monitoring and supervision, are segregated and reviewed on a regular basis. Significant problem loans are reviewed on a monthly basis by the Corporation s Board of Directors.

The Corporation charges off that portion of any loan that management has determined to be a loss. A loan is generally considered by management to represent a loss in whole or in part when exposure beyond the collateral value is apparent, servicing of the unsecured portion has been discontinued or collection is not anticipated based on the borrower's financial condition. The general economic conditions in the borrower s industry influence this determination. The principal amount of any loan that is declared a loss is charged against the Corporation s allowance for loan losses.

The Corporation s allowance for loan losses is designed to provide for loan losses that can be reasonably anticipated. The allowance for loan losses is established through charges to operating expenses in the form of provisions for loan losses. Actual loan losses or recoveries are charged or credited to the allowance for loan losses. Management of the Corporation determines the amount of the allowance. Among the factors considered in determining the allowance for loan losses are the current financial condition of the Corporation s borrowers and the value of security, if any, for their loans. Estimates of future economic conditions and their impact on various industries and individual borrowers are also taken into consideration, as are the Corporation s historical loan loss experience and reports of banking regulatory authorities. As these estimates, factors and evaluations are primarily judgmental, no assurance can be given as to whether the Corporation will sustain loan losses in excess or below its allowance or that subsequent evaluation of the loan portfolio may not require material increases or decreases in such allowance.

Table of Contents

The following table summarizes the Corporation s allowance for loan losses for the dates indicated:

	Nine Months Ended September 30, 2011	Year Ended December 31, 2010	Amount of Increase (Decrease)	Percent of Increase (Decrease)
BALANCES:				
Gross Loans	$ 406,227,196	$ 422,098,362	$ (15,871,166)	-3.76%
Allowance for Loan Losses	7,404,418	6,379,070	1,025,348	16.07%
Nonaccrual Loans	11,705,595	10,931,670	773,925	7.08%
Ratios:				
Allowance for loan losses to gross loans	1.82%	1.51%		
Net loans charged off to allowance for loan losses	21.09%	25.12%		

The provision for loan losses for the three months ended September 30, 2011, was $1,659,873, an increase of $1,262,673 from the $397,200 provision for the same period in 2010. The provision for loan losses was $2,586,707 for the nine month period ended September 30, 2011, compared to a provision of $1,717,411 for the nine months ended September 30, 2010. The increase in our loan loss provisions for the three and nine-month periods is a result of an increase in loan losses recorded for the respective periods and management s assessment of inherent loss in the loan portfolio, including the impact caused by current local, national and global economic conditions. The Corporation s model used to calculate the provision is based on the percentage of historical charge-offs applied to the current loan balances by loan segment and specific reserves applied to certain impaired loans. Nonaccrual loans increased during this period due to the amount of new loans being added to the list in excess of payments received.

For the three months ended September 30, 2011, net loan losses charged to the allowance for loan losses totaled $615,057, an increase of $499,088 from the $115,969 charged off in the same period in 2010. For the nine months ended September 30, 2011, net loan losses charged to the allowance for loan losses totaled $1,561,359 an increase of $613,599 from the $947,760 charged off in the same period in 2010. This increase was due to an overall increase in the number of charge offs in 2011 when compared to the same period in 2010 and not the result of any one loan segment.

Management reviews with the Board of Directors the adequacy of the allowance for loan losses on a quarterly basis. The loan loss provision is adjusted when specific items reflect a need for such an adjustment. Management believes that there were no material loan losses during the first nine months of 2011 that have not been charged off. Management also believes that the Corporation s allowance will be adequate to absorb probable losses inherent in the Corporation s loan portfolio. However, in light of overall economic conditions in the Corporation s geographic area, the nation and internationally, as a whole, it is possible that additional provisions for loan loss may be required.

Table of Contents

NON-INTEREST INCOME

Non-interest income includes service charges on deposit accounts, wire transfer fees, safe deposit box rentals and other revenue not derived from interest on earning assets. Non-interest income for the three months ended September 30, 2011, was $2,446,812, an increase of $711,892, or 41.0%, from the same period in 2010. The increase in non-interest income is the result of investment security gains realized in 2011 that did not occur in 2010. Service charges on deposit accounts increased by $8,357, or 0.8%, to $999,478 in the three months ended September 30, 2011, compared to $991,121 for the same period in 2010. Other service charges and fees increased by $73,872, or 18.5%, in the three months ended September 30, 2011, compared to the same period in 2010. The difference in fee income was the result of fluctuations in volume and not a direct result of fee changes.

Non-interest income for the nine months ended September 30, 2011, was $5,547,673, an increase of $18,838, or 0.3%, compared to $5,528,835 for the same period in 2010. Service charges on deposit accounts decreased $274,033, or 8.3%, to $2,729,861 in the nine months ended September 30, 2011, as compared to the same period in 2010. Other service charges and fees increased $156,608, or 13.7%, in the nine months ended September 30, 2011, as compared to the same period in 2010. The difference in fee income was the result of fluctuations in volume and not a direct result of fee changes.

The following is a detail of the other major income classifications that are included in Other Income on the income statement:

	Three months ended September 30,		Nine months ended September 30,	
Other Income	2011	2010	2011	2010
BOLI Insurance	$ 135,544	$ 108,225	$ 372,853	$ 328,540
Mortgage Loan Origination Income	89,232	167,757	257,725	271,369
Income from Security Sales, net	636,542	17,446	642,331	635,459
Other Income	111,845	50,072	241,599	169,877
Total Other Income	$ 973,163	$ 343,500	$ 1,514,508	$ 1,405,245

NON-INTEREST EXPENSE

Non-interest expenses include salaries and employee benefits, occupancy and equipment, and other operating expenses. Aggregate non-interest expenses for the three-month period ended September 30, 2011 and 2010 were $6,699,927 and $6,384,033, respectively, an increase of $315,894, or 4.9%, from 2010 to 2011. Salaries and benefits increased to $3,518,464 for the three months ended September 30, 2011, from $3,465,713 for the same period in 2010. This represents an increase of $52,751, or 1.5%. This increase was the result of normal yearly salary increases. Occupancy expense increased by $63,575, or 6.2%, to $1,081,113 for the three months ended September 30, 2011, when compared to the same period of 2010. This increase is due in part to the expenses related to the new branch located in Hattiesburg, Mississippi.

Table of Contents

Total non-interest expenses for the nine-month period ended September 30, 2011 and 2010 were $19,346,247 and $18,981,486, respectively, an increase of $364,761, or 1.9%, from 2010 to 2011. Salaries and benefits increased to $10,562,176 for the nine months ended September 30, 2011, from $10,314,413 for the same period in 2010. This represents an increase of $247,763, or 2.4%. This increase was the result of normal yearly salaries increases. Occupancy expense increased $232,714, or 7.9%, to $3,188,602 in the nine months ended September 2011 when compared to the same period in 2010. This increase is due in part to the expenses related to the new branch located in Hattiesburg, Mississippi.

The following is a detail of the major expense classifications that make up the other operating expense line item in the income statement:

Other Operating Expense	Three months ended September 30, 2011	Three months ended September 30, 2010	Nine months ended September 30, 2011	Nine months ended September 30, 2010
Intangible Amortization	$ 46,173	$ 46,173	$ 138,518	$ 138,518
Advertising	212,313	201,519	563,975	490,867
Office Supplies	100,325	107,812	403,575	333,921
Legal and Audit Fees	105,956	110,950	343,116	348,726
Telephone expense	103,245	131,937	317,397	409,287
Postage and Freight	82,618	109,220	275,492	296,949
Loan Collection Expense	247,794	170,903	289,845	412,722
Other Losses	10,126	55,994	21,628	477,459
FDIC and State Assessment	310,458	257,348	843,328	765,388
Debit Card/ATM expense	166,747	148,126	552,108	423,982
Travel and Convention	57,870	45,564	196,649	183,884
Other expenses	656,725	515,236	1,649,838	1,429,482
Total Other Expense	$ 2,100,350	$ 1,900,782	$ 5,595,469	$ 5,711,185

The Corporation s efficiency ratio for the three months ended September 30, 2011, was 63.22% compared to the 68.30% for the same period in 2010. For the nine months ended September 30, 2011 and 2010, the Corporation s efficiency ratio was 65.20% and 65.95%, respectively. The efficiency ratio is the ratio of non-interest expenses divided by the sum of net interest income (on a fully tax equivalent basis) and non-interest income.

Table of Contents

BALANCE SHEET ANALYSIS

	September 30, 2011	December 31, 2010	Amount of Increase (Decrease)	Percent of Increase (Decrease)
Cash and Due From Banks	$ 19,537,859	$ 16,963,393	$ 2,574,466	15.18%
Interest Bearing deposits with Other Banks	34,864,177	1,155,588	33,708,589	2917.01%
Investment Securities	316,094,724	324,730,301	(8,635,577)	-2.66%
Loans, net	398,595,158	415,496,720	(16,901,562)	-4.07%
Total Assets	826,607,265	818,232,732	8,374,533	1.02%
Total Deposits	567,249,464	537,429,723	29,819,741	5.55%
Total Stockholders Equity	85,783,838	76,295,096	9,488,742	12.44%

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash, balances at correspondent banks, interest bearing deposits with other banks and items in process of collection. The balance at September 30, 2011, was $54,402,036, an increase of $36,283,055 from the balance of $18,118,981 at December 31, 2010, due to an increase in the availability of cash letters sent for collection on the last day of the period and an increase in the balances of interest bearing deposits with other banks.

PREMISES AND EQUIPMENT

During the nine-month period ended September 30, 2011, premises and equipment increased by $76,538, or 0.4%, to $20,828,016 when compared to $20,751,478 at December 31, 2010. The increase was due to the addition of property and equipment exceeding the amount of depreciation in the normal course of business.

INVESTMENT SECURITIES

The investment securities portfolio consists of United States agency debentures, mortgage-backed securities, obligations of states, counties and municipal governments and FHLB stock. Investments at September 30, 2011, decreased $8,635,577, or 2.7%, to $316,094,724 from the balance at December 31, 2010. This decrease is due to the maturities and calls that were not reinvested.

LOANS

The loan balance decreased by $16,901,562 during the nine months ended September 30, 2011, to $398,595,158 from $415,496,720 at December 31, 2010. Loan demand, especially in the commercial and industrial loan and consumer categories, was weak during the first nine months of 2011. No material changes were made to the loan products offered by the Corporation during this period.

Table of Contents

DEPOSITS

The following table shows the balance and percentage change in the various deposits:

	September 30, 2011	December 31, 2010	Amount of Increase (Decrease)	Percent of Increase (Decrease)
Noninterest-Bearing Deposits	$ 106,033,042	$ 95,324,759	$ 10,708,283	11.23%
Interest-Bearing Deposits	182,853,067	164,325,092	18,527,975	11.28%
Savings Deposits	41,367,112	37,778,537	3,588,575	9.50%
Certificates of Deposit	236,996,244	240,001,335	(3,005,091)	-1.25%
Total Deposits	$ 567,249,465	$ 537,429,723	$ 29,819,742	5.55%

Interest-bearing deposits, noninterest-bearing deposits and savings increased while certificates of deposit decreased during the nine months ended September 30, 2011. Management continually monitors the interest rates on loan and deposit products to ensure that the Corporation is in line with the rates dictated by the market and our asset and liability management. These rate adjustments impact deposit balances.

OFF-BALANCE SHEET ARRANGEMENTS

Refer to Note 2 to the consolidated financial statements included in this report for a discussion of the nature and extent of the Corporation s off-balance sheet arrangements, which consist of commitments to fund loans and letters of credit.

CONTRACTUAL OBLIGATIONS

There have been no material changes outside of the ordinary course of the Corporation s business to the contractual obligations set forth in Note 12 to the Corporation s financial statements contained in the Corporation s Annual Report on Form 10-K for the year ended December 31, 2010.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

The following discussion outlines specific risks that could affect the Corporation s ability to compete, change the Corporation s risk profile or eventually impact the Corporation s financial results. The risks the Corporation faces generally are similar to those experienced, to varying degrees, by all financial services companies.

The Corporation s strategies and its management s ability to react to changing competitive and economic environments have historically enabled the Corporation to compete effectively and manage risks to acceptable levels. The Corporation has outlined potential risk factors below that

Table of Contents

it presently believe could be important; however, other risks may prove to be important in the future. New risks may emerge at any time and the Corporation cannot predict with certainty all potential developments which could affect the Corporation s financial performance. The following discussion highlights potential risks, which could intensify over time or shift dynamically in a way that might change the Corporation s risk profile.

Competition Risks

The market in which the Corporation competes is saturated with community banks seeking to provide a service oriented banking experience to individuals and businesses compared with what the Corporation believes is the more rigid and less friendly environment found in large banks. This requires the Corporation to offer most, if not all, of the products and conveniences that are offered by the larger banks with a service differentiation. In doing so, it is imperative that the Corporation identify the lines of business that the Corporation can excel in, prudently utilize the Corporation s available capital to acquire the people and platforms required thereof and execute on the strategy.

Credit Risks

Like all lenders, the Corporation faces the risk that the Corporation s customers may not repay their loans and that the realizable value of collateral may be insufficient to avoid a loss of principal. In the Corporation s business, some level of credit loss is unavoidable and overall levels of credit loss can vary over time. Our ability to manage credit risks depends primarily upon the Corporation s ability to assess the creditworthiness of customers and the value of collateral, including real estate. The Corporation controls credit risk by diversifying the Corporation s loan portfolio and managing its composition, and by recording and managing an allowance for expected loan losses in accordance with applicable accounting rules. At the end of September 30, 2011, the Corporation had $7.404 million of available reserves to cover such losses. The models and approaches the Corporation uses to originate and manage loans are regularly updated to take into account changes in the competitive environment, in real estate prices and other collateral values, and in the economy, among other things based on the Corporation s experience originating loans and servicing loan portfolios.

Financing, Funding and Liquidity Risks

One of the most important aspects of management s efforts to sustain long-term profitability for the Corporation is the management of interest rate risk. Management s goal is to maximize net interest income within acceptable levels of interest-rate risk and liquidity.

The Corporation s assets and liabilities are principally financial in nature and the resulting earnings thereon are subject to significant variability due to the timing and extent to which the Corporation can reprice the yields on interest-earning assets and the costs of interest bearing liabilities as a result of changes in market interest rates. Interest rates in the financial markets affect the Corporation s decisions on pricing its assets and liabilities which impacts net interest income, an important cash flow stream for the Corporation. As a result, a substantial part of the Corporation s risk-management activities are devoted to managing interest-rate risk. Currently, the Corporation does not have any significant risks related to foreign exchange, commodities or equity risk exposures.

Table of Contents

Interest Rate and Yield Curve Risks

A significant portion of the Corporation s business involves borrowing and lending money. Accordingly, changes in interest rates directly impact the Corporation s revenues and expenses, and potentially could compress the Corporation s net interest margin. The Corporation actively manages its balance sheet to control the risks of a reduction in net interest margin brought about by ordinary fluctuations in rates.

Like all financial services companies, the Corporation faces the risks of abnormalities in the yield curve. The yield curve simply shows the interest rates applicable to short and long term debt. The curve is steep when short-term rates are much lower than long-term rates: it is flat when short-term rates are equal, or nearly equal, to long-term rates: and it is inverted when short-term rates exceed long-term rates. Historically, the yield curve is positively sloped. A flat or inverted yield curve tends to decrease net interest margin, as funding costs increase relative to the yield on assets. Currently, the yield curve is positively sloped.

Regulatory and Legal Risks

The Corporation operates in a heavily regulated industry and therefore is subject to many banking, deposit, and consumer lending regulations in addition to the rules applicable to all companies publicly traded in the U.S. securities markets. Failure to comply with applicable regulations could result in financial, structural, and operational penalties. In addition, efforts to comply with applicable regulations may increase the Corporation s costs and, or limit the Corporation s ability to pursue certain business opportunities. Federal and state regulations significantly limit the types of activities in which the Corporation, as a financial institution, may engage. In addition, the Corporation is subject to a wide array of other regulations that govern other aspects of how the Corporation conducts business, such as in the areas of employment and intellectual property. Federal and state legislative and regulatory authorities occasionally consider changing these regulations or adopting new ones. Such actions could limit the amount of interest or fees the Corporation can charge, could restrict the Corporation s ability to collect loans or realize on collateral or could materially affect us in other ways. Additional federal and state consumer protection regulations also could expand the privacy protections afforded to customers of financial institutions, restricting the Corporation s ability to share or receive customer information and increasing the Corporation s costs. In addition, changes in accounting rules can significantly affect how the Corporation records and reports assets, liabilities, revenues, expenses and earnings.

The Corporation also faces litigation risks from customers (singly or in class actions) and from federal or state regulators. Litigation is an unavoidable part of doing business, and the Corporation manages those risks through internal controls, personnel training, insurance, litigation management, the Corporation s compliance and ethics processes and other means. However, the commencement, outcome and magnitude of litigation cannot be predicted or controlled with certainty.

Table of Contents

Accounting Estimate Risks

The preparation of the Corporation s consolidated financial statements in conformity with United States generally accepted accounting principles requires management to make significant estimates that affect the financial statements. The Corporation s most critical estimate is the level of the allowance for credit losses. However, other estimates occasionally become highly significant, especially in volatile situations such as litigation and other loss contingency matters. Estimates are made at specific points in time; as actual events unfold, estimates are adjusted accordingly. Due to the inherent nature of these estimates, it is possible that, at some time in the future, the Corporation may significantly increase the allowance for credit losses or sustain credit losses that are significantly higher than the provided allowance, or the Corporation may make some other adjustment that will differ materially from the estimates that the Corporation makes today.

Expense Control

Expenses and other costs directly affect the Corporation s earnings. The Corporation s ability to successfully manage expenses is important to its long-term profitability. Many factors can influence the amount of the Corporation s expenses, as well as how quickly they grow. As the Corporation s businesses change or expand, additional expenses can arise from asset purchases, structural reorganization evolving business strategies, and changing regulations, among other things. The Corporation manages expense growth and risk through a variety of means, including actual versus budget management, imposition of expense authorization, and procurement coordination and processes.

ITEM 4. CONTROLS AND PROCEDURES.

The management of the Corporation, with the participation of our principal executive and financial officers, has evaluated the effectiveness of our disclosure controls and procedures in ensuring that the information required to be disclosed in our filings under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, including ensuring that such information is accumulated and communicated to the Corporation s management as appropriate to allow timely decision regarding required disclosure. Based on such evaluation, our principal executive and financial officers have concluded that such disclosure controls and procedures were effective as of September 30, 2011 (the end of the period covered by this Quarterly Report on Form 10-Q).

There were no changes to the Corporation s internal control over financial reporting that occurred in the three months ended September 30, 2011, that have materially affected, or are reasonably likely to materially affect, the Corporation s internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

ITEM 1A. RISK FACTORS.

The Corporation has updated the risk factors that appear in Part I, Item 1A., Risk Factors, of the Corporation s Annual Report on Form 10-K for the year ended December 31, 2010, to include the following.

Changes in interest rates could make it difficult to maintain our current interest income spread and could result in reduced earnings.

Our earnings are largely derived from net interest income, which is interest income and fees earned on loans and investments, less interest paid on deposits and other borrowings. Interest rates are highly sensitive to many factors that are beyond the control of our management, such as general economic conditions and the policies of various governmental and regulatory authorities. An unanticipated rapid decrease or increase in interest rates could have an adverse effect on the spreads between the interest rates earned on assets and the rates of interest paid on liabilities, and therefore on the level of net interest income. Further, substantially higher interest rates generally reduce loan demand and may result in slower loan growth than previously experienced. Due to concerns regarding the federal debt ceiling, one credit rating agency has downgraded the credit rating of the federal government, and others may as well, which could result in increased interest rates generally. For the reasons set forth above, an increase in interest rates generally as a result of such a credit rating downgrade could adversely affect our net interest income levels, thereby resulting in reduced earnings, and reduce loan demand.

Table of Contents

ITEM 6. EXHIBITS.
Exhibits

31(a)	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a).
31(b)	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a).
32(a)	Certification of the Chief Executive Officer pursuant to 18 U.S.C. § 1350.
32(b)	Certification of the Chief Financial Officer pursuant to 18 U.S.C. § 1350.
101	The following financial information from Citizens Holding Company s Quarterly Report on Form 10-Q for the period ended September 30, 2011, filed with the SEC on November 8, 2011, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Condition as of September 30, 2011 (Unaudited) and December 31, 2010; (ii) the Consolidated Statements of Income for the three and nine months ended September 30, 2011 (Unaudited) and 2010 (Unaudited); (iii) the Consolidated Statements of Comprehensive Income for the three months and nine months ended September 30, 2011 (Unaudited) and 2010 (Unaudited); (iv) the Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 (Unaudited) and 2010 (Unaudited); and (v) Notes to Consolidated Financial Statements, tagged as blocks of text (Unaudited).*

* Pursuant to Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be filed for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be deemed part of a registration statement, prospectus or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filings.

Table of Contents

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.

CITIZENS HOLDING COMPANY

BY: /s/ Greg L. McKee
Greg L. McKee
President and Chief Executive Officer
(Principal Executive Officer)

BY: /s/ Robert T. Smith
Robert T. Smith
Treasurer and Chief Financial Officer
(Principal Financial and Accounting Officer)

DATE: November 4, 2011

Table of Contents

EXHIBIT INDEX

Exhibit Number	Description of Exhibit
31(a)	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a)
31(b)	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a)
32(a)	Certification of the Chief Executive Officer pursuant to 18 U.S.C. §1350.
32(b)	Certification of the Chief Financial Officer pursuant to 18 U.S.C. §1350.
101	The following financial information from Citizens Holding Company s Quarterly Report on Form 10-Q for the period ended September 30, 2011, filed with the SEC on November 8, 2011, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Condition as of September 30, 2011 (Unaudited) and December 31, 2010; (ii) the Consolidated Statements of Income for the three and nine months ended September 30, 2011 (Unaudited) and 2010 (Unaudited); (iii) the Consolidated Statements of Comprehensive Income for the three months and nine months ended September 30, 2011 (Unaudited) and 2010 (Unaudited); (iv) the Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 (Unaudited) and 2010 (Unaudited); and (v) Notes to Consolidated Financial Statements, tagged as blocks of text (Unaudited).*

* Pursuant to Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be filed for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be deemed part of a registration statement, prospectus or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filings.