CITIZENS HOLDING CO /MS/
Form 10-Q
August 10, 2015
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 June 30, 2015

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 August 6, 2015:

Title	Outstanding
Common Stock, $0.20 par value	4,885,114

Table of Contents

CITIZENS HOLDING COMPANY

INTERIM FINANCIAL STATEMENTS FOR QUARTER ENDED JUNE 30, 2015

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS.

CITIZENS HOLDING COMPANY CONSOLIDATED STATEMENTS OF CONDITION

	June 30, 2015 (Unaudited)	December 31, 2014 (Audited)
ASSETS		
Cash and due from banks	$ 18,842,722	$ 22,405,730
Interest bearing deposits with other banks	11,083,914	61,481,223
Investment securities held to maturity, at amortized cost	198,298,707	206,817,169
Investment securities available for sale, at fair value	232,272,884	179,745,130
Loans, net of allowance for loan losses of $6,692,914 in 2015 and $6,542,326 in 2014	400,622,906	384,417,508
Premises and equipment, net	18,782,171	19,240,230
Other real estate owned, net	3,590,367	4,051,561
Accrued interest receivable	3,794,505	3,869,937
Cash value of life insurance	22,699,665	22,347,601
Intangible assets, net	3,149,657	3,149,657
Other assets	13,862,768	13,534,935
TOTAL ASSETS	$ 927,000,266	$ 921,060,681
LIABILITIES AND SHAREHOLDERS EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$ 141,953,804	$ 145,729,932
Interest-bearing NOW and money market accounts	296,965,294	268,567,815
Savings deposits	64,403,837	60,253,788
Certificates of deposit	217,815,290	221,542,359
Total deposits	721,138,225	696,093,894
Securities sold under agreement to repurchase	94,962,842	114,426,770
Federal Home Loan Bank advances	20,000,000	20,000,000
Accrued interest payable	56,352	190,717
Deferred compensation payable	7,419,986	7,209,694
Other liabilities	1,345,838	1,281,820
Total liabilities	844,923,243	839,202,895
SHAREHOLDERS EQUITY		
	975,054	975,482

Common stock; $.20 par value, 22,500,000 shares authorized, 4,875,270 shares outstanding at June 30, 2015 and 4,877,614 at December 31, 2014		
Additional paid-in capital	3,866,599	3,861,717
Retained earnings	87,077,889	85,901,207
Accumulated other comprehensive loss, net of tax benefit of $5,855,279 in 2015 and $5,283,048 in 2014	(9,842,519)	(8,880,620)
Total shareholders equity	82,077,023	81,857,786
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 927,000,266	$ 921,060,681

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

1

Table of Contents

CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

	For the Three Months Ended June 30, 2015	For the Three Months Ended June 30, 2014	For the Six Months Ended June 30, 2015	For the Six Months Ended June 30, 2014
INTEREST INCOME				
Loans, including fees	$ 4,988,452	$ 5,067,445	$ 9,996,012	$ 10,111,355
Investment securities	2,690,622	2,851,155	5,359,094	5,748,124
Other interest	17,245	6,913	47,284	11,962
Total interest income	7,696,319	7,925,513	15,402,390	15,871,441
INTEREST EXPENSE				
Deposits	449,772	421,870	881,925	840,166
Other borrowed funds	285,902	312,081	604,933	622,644
Total interest expense	735,674	733,951	1,486,858	1,462,810
NET INTEREST INCOME	6,960,645	7,191,562	13,915,532	14,408,631
PROVISION FOR LOAN LOSSES	81,818	211,535	265,994	572,903
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	6,878,827	6,980,027	13,649,538	13,835,728
OTHER INCOME				
Service charges on deposit accounts	954,093	963,826	1,840,877	1,893,557
Other service charges and fees	563,161	524,695	1,095,014	1,009,132
Other income	334,597	995,101	667,705	1,364,413
Total other income	1,851,851	2,483,622	3,603,596	4,267,102
OTHER EXPENSES				
Salaries and employee benefits	3,341,381	3,252,370	6,696,684	6,608,207
Occupancy expense	1,296,765	1,570,995	2,596,259	2,544,057
Other operating expense	1,683,004	2,222,630	3,515,181	4,262,594
Total other expenses	6,321,150	7,045,995	12,808,124	13,414,858
	2,409,528	2,417,654	4,445,010	4,687,972

INCOME BEFORE PROVISION FOR INCOME TAXES				
PROVISION FOR INCOME TAXES	580,941	325,135	1,022,877	798,300
NET INCOME	$ 1,828,587	$ 2,092,519	$ 3,422,133	$ 3,889,672
NET INCOME PER SHARE -Basic	$ 0.37	$ 0.43	$ 0.70	$ 0.80
-Diluted	$ 0.37	$ 0.43	$ 0.70	$ 0.80
DIVIDENDS PAID PER SHARE	$ 0.23	$ 0.22	$ 0.46	$ 0.44

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

Table of Contents

CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	For the Three Months Ended June 30, 2015	For the Three Months Ended June 30, 2014	For the Six Months Ended June 30, 2015	For the Six Months Ended June 30, 2014
Net income	$ 1,828,587	$ 2,092,519	$ 3,422,133	$ 3,889,672
Other comprehensive income				
Securities available-for-sale				
Unrealized holding gains	2,054,039	5,349,883	3,008,075	14,868,427
Income tax effect	(766,156)	(1,992,111)	(1,122,012)	(5,542,528)
	1,287,883	3,357,772	1,886,063	9,325,899
Securities transferred from available-for-sale to held-to-maturity				
Amortization of net unrealized losses during the period	529,915		1,473,944	
Income tax effect	(197,660)		(549,782)	
	332,255		924,162	
Reclassification adjustment for gains included in net income		(9,102)		(9,102)
Income tax effect		3,395		3,395
		(5,707)		(5,707)
Total other comprehensive income	955,628	3,352,065	961,901	9,320,192
Comprehensive income	$ 2,784,215	$ 5,444,584	$ 4,384,034	$ 13,209,864

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

3

Table of Contents

CITIZENS HOLDING COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the Six Months Ended June 30, 2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES		
Net cash provided by operating activities	$ 4,796,043	$ 3,850,163
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities and calls of securities available for sale	20,373,502	4,609,491
Proceeds from sales of securities available for sale		1,381,596
Proceeds from maturities and calls of securities held to maturity	10,000,000	
Purchases of investment securities available for sale	(76,439,560)	
Purchases of bank premises and equipment	(46,843)	(1,654,936)
Increase (decrease) in interest bearing deposits with other banks	50,397,309	(6,239,119)
Proceeds from sale of other real estate	1,001,949	339,934
Redemption of Federal Home Loan Bank Stock	150,700	449,700
Net (increase) decrease in loans	(17,088,940)	1,906,215
Net cash (used by) provided by investing activities	(11,651,883)	792,881
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposits	25,044,331	36,817,569
Net change in securities sold under agreement to repurchase	(19,463,928)	(5,719,172)
Decrease in federal funds purchased		(27,500,000)
Repurchase of stock	(70,122)	
Exercise of Stock Options	27,000	
Excess tax benefits on stock options	1,001	
Payment of dividends	(2,245,450)	(2,146,149)
Net cash provided by financing activities	3,292,832	1,452,248
Net (decrease) increase in cash and due from banks	(3,563,008)	6,095,292
Cash and due from banks, beginning of period	22,405,730	16,040,195
Cash and due from banks, end of period	$ 18,842,722	$ 22,135,487

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

4

CITIZENS HOLDING COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

As of and for the three and six months ended June 30, 2015

(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 June 30, 2015 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, 2014, filed with the Securities and Exchange Commission on March 13, 2015.

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 June 30, 2015, the Corporation had entered into loan commitments with certain customers with an aggregate unused balance of $53,718,491 compared to an aggregate unused balance of $50,242,705 at December 31, 2014. There was $2,666,980 of letters of credit outstanding at June 30, 2015 and $2,855,480 at December 31, 2014. 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 likely 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. Net income per share was computed as follows:

	For the Three Months Ended June 30, 2015	For the Three Months Ended June 30, 2014	For the Six Months Ended June 30, 2015	For the Six Months Ended June 30, 2014
Basic weighted average shares outstanding	4,877,614	4,870,114	4,873,097	4,870,114
Dilutive effect of granted options	1,170	704	907	535
Diluted weighted average shares outstanding	4,878,784	4,870,818	4,874,004	4,870,649
Net income	$ 1,828,587	$ 2,092,519	$ 3,422,133	$ 3,889,672
Net income per share-basic	$ 0.37	$ 0.43	$ 0.70	$ 0.80
Net income per share-diluted	$ 0.37	$ 0.43	$ 0.70	$ 0.80

Note 4. Equity Compensation Plans

Prior to the adoption of the 2013 Plan, as defined below, the Corporation utilized two stock-based compensation plans, the 1999 Directors Stock Compensation Plan (the Directors Plan) for directors, and prior to its expiration, the 1999 Employees Long-Term Incentive Plan (the Employees Plan) for employees.

The following table is a summary of the stock option activity for the six months ended June 30, 2015.

	Directors Plan Number of Shares	Directors Plan Weighted Average Exercise Price	Employees Plan Number of Shares	Employees Plan Weighted Average Exercise Price	2013 Plan Number of Shares	2013 Plan Weighted Average Exercise Price
Outstanding at December 31, 2014	96,000	$ 21.23	46,500	$ 22.14		$
Granted						
Exercised			(1,500)	18.00		
Expired	(9,000)	20.00	(22,000)	21.05		
Outstanding at June 30, 2015	87,000	$ 21.36	23,000	$ 23.46		$

The intrinsic value of options granted under the Directors Plan at June 30, 2015, was $70,980, the intrinsic value of options granted under the Employees Plan at June 30, 2015, was $0, and since there were no options granted under the 2013 Plan, the intrinsic value for the 2013 Plan is $0 for an aggregate intrinsic value at June 30, 2015, of $70,980.

The Corporation has adopted the 2013 Incentive Compensation Plan (the 2013 Plan), which the Corporation intends to use for all future equity grants to employees, directors or consultants until the termination or expiration of the 2013 Plan. During the quarter ended March 31, 2014, the Corporation s directors received restricted stock grants totaling 7,500 shares of common stock. These grants vested over a one-year period ending March 13, 2015 during which time the recipients had rights to vote the shares and to receive dividends. The grant date fair value of these shares was $138,000 and was recognized over the one year restriction period at a cost of $11,500 per month less deferred taxes of $4,290 per month.

During the quarter ended June 30, 2015, the Corporation s directors received restricted stock grants totaling 7,500 shares of common stock. These grants vest over a one-year period ending April 29, 2016 during which time the recipients has rights to vote the shares and to receive dividends. The grant date fair value of these shares was $141,450 and will be recognized over the one year restriction period at a cost of $11,788 per month less deferred taxes of $4,397 per month.

Note 5. Income Taxes

The income tax topic of the Accounting Standards Codification (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 June 30, 2015, 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 2015 relative to any tax positions taken. It is the Corporation s policy to recognize interest or penalties related to income tax matters in income tax expense.

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 2011. The Corporation s consolidated state income tax returns are also open to audit under the statute of limitations for the same period.

Table of Contents

Note 6. Securities

The amortized cost and estimated fair value of securities available-for-sale and the corresponding amounts of gross unrealized gains and losses recognized in accumulated other comprehensive income were as follows:

June 30, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities available-for-sale				
Obligations of U.S. Government agencies	$ 68,002,206	$	$ 2,366,887	$ 65,635,319
Mortgage backed securities	78,350,589	755,577	1,123,361	77,982,805
State, County, Municipals	84,618,121	2,208,522	1,051,543	85,775,100
Other investments	2,957,375		77,715	2,879,660
Total	$ 233,928,291	$ 2,964,099	$ 4,619,506	$ 232,272,884

December 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities available-for-sale				
Obligations of U.S. Government agencies	$ 77,996,980	$	$ 2,035,905	$ 75,961,075
Mortgage backed securities	12,501,990	824,844		13,326,834
State, County, Municipals	84,896,091	3,048,489	360,082	87,584,498
Other investments	2,997,401		124,678	2,872,723
Total	$ 178,392,462	$ 3,873,333	$ 2,520,665	$ 179,745,130

During the quarter ended June 30, 2014, the Corporation transferred securities with an amortized cost of $222,322,423 from available-for-sale to held-to-maturity. This transfer was completed after consideration of the Corporation s ability and intent to hold these securities to maturity.

The fair value of the securities transferred as of the date of transfer was $205,260,985 with a net unrealized loss of $17,061,438. In accordance with ASC 320-10-35-16, the discount on each security that resulted from this transfer is amortized over the remaining lives of the individual securities. Any unrealized holding losses on the date of the transfer are not recognized in net income but remain in accumulated other comprehensive loss. In accordance with ASC 320-10-15-10d, the unrealized loss amounts in accumulated other comprehensive loss are amortized simultaneously against interest income as the discount is accreted on the transferred securities. There is no effect on net income as the discount accretion offsets the accumulated other comprehensive loss amortization. The unamortized unrealized loss, before deferred taxes, was $14,042,392 and $15,516,336 at June 30, 2015 and December 31, 2014, respectively.

Table of Contents

The amortized cost and estimated fair value of securities held-to-maturity and the corresponding amounts of gross unrecognized gains and losses were as follows:

June 30, 2015	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities held-to-maturity				
Obligations of U.S. Government agencies	$ 198,298,707	$ 6,188,631	$	$ 204,487,338
Total	$ 198,298,707	$ 6,188,631	$	$ 204,487,338

December 31, 2014	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities held-to-maturity				
Obligations of U.S. Government agencies	$ 206,817,169	$ 9,928,269	$	$ 216,745,438
Total	$ 206,817,169	$ 9,928,269	$	$ 216,745,438

The amortized cost and estimated fair value of securities by contractual maturity at June 30, 2015 and December 31, 2014 are shown below. Actual maturities may differ from contractual maturities because issuers have the right to call or prepay certain obligations.

	June 30, 2015		December 31, 2014	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Available-for-sale				
Due in one year or less	$ 6,134,852	$ 6,204,469	$ 3,619,965	$ 3,644,097
Due after one year through five years	10,563,313	10,816,985	11,886,005	12,165,884
Due after five years through ten years	75,646,390	74,709,671	73,014,502	72,750,584
Due after ten years	141,583,736	140,541,759	89,871,990	91,184,565
Total	$ 233,928,291	$ 232,272,884	$ 178,392,462	$ 179,745,130
Held-to-maturity				
Due after five years through ten years	$ 36,920,537	$ 37,859,713	$ 27,599,235	$ 28,395,635
Due after ten years	161,378,170	166,627,625	179,217,934	188,349,803

Total	$ 198,298,707	$ 204,487,338	$ 206,817,169	$ 216,745,438

9

Table of Contents

The tables below show the Corporation s gross unrealized losses and fair value of available-for-sale and held-to-maturity investments, aggregated by investment category and length of time that individual investments were in a continuous loss position at June 30, 2015 and December 31, 2014.

A summary of unrealized loss information for securities available-for-sale, categorized by security type follows (in thousands):

June 30, 2015	Less than 12 months		12 months or more		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U. S. Government agencies	$ 10,295	$ 201	$ 55,340	$ 2,166	$ 65,635	$ 2,367
Mortgage backed securities	66,391	1,123			66,391	1,123
State, County, Municipal	13,285	448	12,251	604	25,536	1,052
Other investments			2,880	78	2,880	78
Total	$ 89,971	$ 1,772	$ 70,471	$ 2,848	$ 160,442	$ 4,620

December 31, 2014	Less than 12 months		12 months or more		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U. S. Government agencies	$	$	$ 75,961	$ 2,036	$ 75,961	$ 2,036
Mortgage backed securities						
State, County, Municipal	697	3	14,980	357	15,677	360
Other investments			2,873	125	2,873	125
Total	$ 697	$ 3	$ 93,814	$ 2,518	$ 94,511	$ 2,521

The Corporation s unrealized losses on its Obligations of United States Government agencies, Mortgage backed securities and State, County and Municipal bonds are the result of an upward trend in interest rates, mainly in the mid-term sector. None of the unrealized losses disclosed in the previous table are related to credit deterioration. The Corporation has determined that none of the securities in this classification are other-than-temporarily impaired at June 30, 2015 or at December 31, 2014.

The Corporation s unrealized loss on other investments relates to an investment in a pooled trust preferred security. The decline in value of the pooled trust preferred security is related to the deterioration of the markets for these types of securities brought about by the lowered credit ratings and past deferrals and defaults of the underlying issuing financial institutions. The Corporation owns a senior tranche of this security and therefore has a higher degree of which future deferrals and defaults would be required before the cash flow for the Corporation s tranche is negatively impacted. The Corporation does not intend to sell this security and it is not more likely than not that the Corporation will be required to sell at a price less than amortized cost prior to maturity. Given these factors, the Corporation does not consider the investment to be other-than-temporarily impaired at June 30, 2015 or December 31, 2014.

10

Table of Contents

Note 7. Loans

The composition of net loans (in thousands) at June 30, 2015 and December 31, 2014 is as follows:

	June 30, 2015	December 31, 2014
Real Estate:		
Land Development and Construction	$ 45,581	$ 43,233
Farmland	24,027	26,463
1-4 Family Mortgages	106,179	104,170
Commercial Real Estate	161,779	151,746
Total Real Estate Loans	337,566	325,612
Business Loans:		
Commercial and Industrial Loans	44,235	38,333
Farm Production and Other Farm Loans	1,061	1,035
Total Business Loans	45,296	39,368
Consumer Loans:		
Credit Cards	986	1,075
Other Consumer Loans	24,138	25,440
Total Consumer Loans	25,124	26,515
Total Gross Loans	407,986	391,495
Unearned income	(670)	(535)
Allowance for loan losses	(6,693)	(6,542)
Loans, net	$ 400,623	$ 384,418

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 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 (in thousands), segregated by class, were as follows:

	June 30, 2015	December 31, 2014
Real Estate:		
Land Development and Construction	$ 82	$ 92
Farmland	194	222
1-4 Family Mortgages	2,189	1,905
Commercial Real Estate	9,990	9,444
Total Real Estate Loans	12,455	11,663
Business Loans:		
Commercial and Industrial Loans	135	70
Total Business Loans	135	70
Consumer Loans:		
Other Consumer Loans	74	133
Total Consumer Loans	74	133
Total Non-Accrual Loans	$ 12,664	$ 11,854

Table of Contents

An aging analysis of past due loans (in thousands), segregated by class, as of June 30, 2015, was as follows:

	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	$ 416	$	$ 416	$ 45,165	$ 45,581	$
Farmland	251	17	268	23,759	24,027	
1-4 Family Mortgages	3,825	813	4,638	101,541	106,179	52
Commercial Real Estate	2,056	3,948	6,004	155,775	161,779	
Total Real Estate Loans	6,548	4,778	11,326	326,240	337,566	52
Business Loans:						
Commercial and Industrial Loans	138	75	213	44,022	44,235	
Farm Production and Other Farm Loans				1,061	1,061	
Total Business Loans	138	75	213	45,083	45,296	
Consumer Loans:						
Credit Cards	23		23	963	986	
Other Consumer Loans	769	37	806	23,332	24,138	17
Total Consumer Loans	792	37	829	24,295	25,124	17
Total Loans	$ 7,478	$ 4,890	$ 12,368	$ 395,618	$ 407,986	$ 69

Table of Contents

An aging analysis of past due loans (in thousands), segregated by class, as of December 31, 2014 was as follows:

	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	$ 578	$	$ 578	$ 42,655	$ 43,233	$
Farmland	889	17	906	25,557	26,463	
1-4 Family Mortgages	4,606	837	5,443	98,727	104,170	131
Commercial Real Estate	2,211	4,471	6,682	145,064	151,746	724
Total Real Estate Loans	8,284	5,325	13,609	312,003	325,612	855
Business Loans:						
Commercial and Industrial Loans	115	3	118	38,215	38,333	3
Farm Production and other Farm Loans	22		22	1,013	1,035	
Total Business Loans	137	3	140	39,228	39,368	3
Consumer Loans:						
Credit Cards	27	6	33	1,042	1,075	6
Other Consumer Loans	1,179	53	1,232	24,208	25,440	16
Total Consumer Loans	1,206	59	1,265	25,250	26,515	22
Total Loans	$ 9,627	$ 5,387	$ 15,014	$ 376,481	$ 391,495	$ 880

Loans are considered impaired when, based on current information and events, it is probable the Corporation will be unable to collect all 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 filings and any situation that might lend itself to cause a borrower to be unable to repay the loan according to the original agreement 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 (in thousands) as of June 30, 2015 and December 31, 2014, segregated by class, are as follows:

June 30, 2015	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	$ 82	$	$ 82	$ 82	$ 82	$ 332
Farmland	743	81	662	743	108	751
1-4 Family Mortgages	2,910	1,976	934	2,910	210	2,833
Commercial Real Estate	9,990	1,865	8,125	9,990	1,981	9,545
Total Real Estate Loans	13,725	3,922	9,803	13,725	2,381	13,461
Business Loans:						
Commercial and Industrial Loans	135	103	32	135	25	138
Total Business Loans	135	103	32	135	25	138
Consumer Loans:						
Other Consumer Loans	74	74		74		84
Total Consumer Loans	74	74		74		84
Total Loans	$ 14,238	$ 4,099	$ 9,835	$ 13,934	$ 2,406	$ 13,683

Table of Contents

December 31, 2014	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	$ 92	$	$ 92	$ 92	$ 92	$ 114
Farmland	798	104	694	798	108	575
1-4 Family Mortgages	2,554	1,685	869	2,554	143	2,210
Commercial Real Estate	9,444	895	8,549	9,444	1,642	9,169
Total Real Estate Loans	12,888	2,684	10,204	12,888	1,985	12,068
Business Loans:						
Commercial and Industrial Loans	70	30	40	70	40	1,147
Total Business Loans	70	30	40	70	40	1,147
Consumer Loans:						
Other Consumer Loans	121	121		121		120
Total Consumer Loans	121	121		121		120
Total Loans	$ 13,079	$ 2,835	$ 10,244	$ 13,079	$ 2,025	$ 13,335

16

Table of Contents

The following table presents troubled debt restructurings (in thousands, except for number of loans), segregated by class:

June 30, 2015	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial real estate	4	$ 6,850	$ 4,530
Total	4	$ 6,850	$ 4,530

December 31, 2014	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial real estate	4	$ 6,850	$ 4,741
Total	4	$ 6,850	$ 4,741

Changes in the Corporation s troubled debt restructurings (in thousands, except for number of loans) are set forth in the table below:

	Number of Loans	Recorded Investment
Totals at January 1, 2015	4	$ 4,741
Reductions due to:		
Principal paydowns		(211)
Total at June 30, 2015	4	$ 4,530

The allocated allowance for loan losses attributable to restructured loans was $174,274 at June 30, 2015 and December 31, 2014. The Corporation had no remaining availability under commitments to lend additional funds on these troubled debt restructuring as of June 30, 2015.

Table of Contents

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 the majority 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.

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

Table of Contents

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 june 30, 2015.

The following table details the amount of gross loans (in thousands), segregated by loan grade and class, as of June 30, 2015:

Grades	Satisfactory 1, 2, 3, 4	Special Mention 5,6	Substandard 7	Doubtful 8	Loss 9	Total Loans
Real Estate:						
Land Development and Construction	$ 43,751	$ 267	$ 1,563	$	$	$ 45,581
Farmland	21,605	841	1,581			24,027
1-4 Family Mortgages	89,269	4,556	12,354			106,179
Commercial Real Estate	134,949	13,578	13,252			161,779
Total Real Estate Loans	289,574	19,242	28,750			337,566
Business Loans:						
Commercial and Industrial Loans	43,570	430	235			44,235
Farm Production and Other Farm Loans	1,061					1,061
Total Business Loans	44,631	430	235			45,296
Consumer Loans:						
Credit Cards	986					986
Other Consumer Loans	23,708	136	262	29	3	24,138
Total Consumer Loans	24,694	136	262	29	3	25,124
Total Loans	$ 358,899	$ 19,808	$ 29,247	$ 29	$ 3	$ 407,986

Table of Contents

The following table details the amount of gross loans (in thousands) segregated by loan grade and class, as of December 31, 2014:

Grades	Satisfactory 1, 2, 3,4	Special Mention 5,6	Substandard 7	Doubtful 8	Loss 9	Total Loans
Real Estate:						
Land Development and Construction	$ 41,431	$ 424	$ 1,378	$	$	$ 43,233
Farmland	23,993	708	1,762			26,463
1-4 Family Mortgages	86,969	5,351	11,850			104,170
Commercial Real Estate	126,881	13,558	11,307			151,746
Total Real Estate Loans	279,274	20,041	26,297			325,612
Business Loans:						
Commercial and Industrial Loans	37,890	232	211			38,333
Farm Production and other Farm Loans	1,035	0				1,035
Total Business Loans	38,925	232	211			39,368
Consumer Loans:						
Credit Cards	1,069		6			1,075
Other Consumer Loans	24,889	177	358	16		25,440
Total Consumer Loans	25,958	177	364	16		26,515
Total Loans	$ 344,157	$ 20,450	$ 26,872	$ 16	$	$ 391,495

The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management s best estimate of probable losses 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 twenty quarters with the most current quarters weighted more heavily 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.

20

Table of Contents

The following table details activity in the allowance for loan losses by portfolio segment for the six months ended June 30, 2015:

June 30, 2015	Real Estate	Business Loans	Consumer	Total
Beginning Balance, January 1, 2015	$ 5,202,151	$ 873,815	$ 466,360	$ 6,542,326
Provision for possible loan losses	149,095	23,189	93,710	265,994
Chargeoffs	125,374		93,915	219,289
Recoveries	42,758	7,658	53,467	103,883
Net Chargeoffs	82,616	(7,658)	40,448	115,406
Ending Balance	$ 5,268,630	$ 904,662	$ 519,622	$ 6,692,914
Period end allowance allocated to:				
Loans individually evaluated for impairment	$ 2,381,267	$ 25,000	$	$ 2,406,267
Loans collectively evaluated for impairment	2,887,363	879,662	519,622	4,286,647
Ending Balance, March 31, 2015	$ 5,268,630	$ 904 662	$ 519,622	$ 6,692,914

The following table details activity in the allowance for loan losses by portfolio segment for the six months ended June 30, 2014:

June 30, 2014	Real Estate	Business Loans	Consumer	Total
Beginning Balance, January 1, 2014	$ 4,705,753	$ 2,767,409	$ 604,337	$ 8,077,499
Provision for possible loan losses	(172,350)	764,154	(18,902)	572,903
Chargeoffs	101,615	22,760	67,287	191,662
Recoveries	35,488	5,748	39,453	80,689
Net Chargeoffs	66,127	17,012	27,834	110,973
Ending Balance, June 30, 2014	$ 4,467,276	$ 3,514,551	$ 557,601	$ 8,539,428

Period end allowance allocated to:				
Loans individually evaluated for impairment	$ 1,067,821	$ 2,068,759	$	$ 3,136,580
Loans collectively evaluated for impairment	3,399,455	1,445,792	557,601	5,402,848
Ending Balance, March 31, 2014	$ 4,467,276	$ 3,514,551	$ 557,601	$ 8,539,428

Table of Contents

The Corporation s recorded investment in loans as of June 30, 2015 and December 31, 2014 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):

June 30, 2015	Real Estate	Business Loans	Consumer	Total
Loans individually evaluated for specific impairment	$ 13,725	$ 135	$ 74	$ 13,934
Loans collectively evaluated for general impairment	323,841	45,161	25,050	394,052
	$ 337,566	$ 45,296	$ 25,124	$ 407,986

December 31, 2014	Real Estate	Business Loans	Consumer	Total
Loans individually evaluated for specific impairment	$ 12,888	$ 70	$ 121	$ 13,079
Loans collectively evaluated for general impairment	312,724	39,298	26,394	378,416
	$ 325,612	$ 39,368	$ 26,515	$ 391,495

Table of Contents

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.

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 June 30, 2015:

	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	$	$ 65,635,319	$	$ 65,635,319
Mortgage-backed securities		77,982,805		77,982,805
State, county and municipal obligations		85,775,100		85,775,100
Other investments			2,879,660	2,879,660
Total	$	$ 229,393,224	$ 2,879,660	$ 232,272,884

Table of Contents

The following table presents assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2014:

	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	$	$ 75,961,075	$	$ 75,961,075
Mortgage-backed securities		13,326,834		13,326,834
State, county and municipal obligations		87,584,498		87,584,498
Other investments			2,872,723	2,872,723
Total	$	$ 176,872,407	$ 2,872,723	$ 179,745,130

The following table reports the activity for 2015 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, 2015	$ 2,872,723
Principal payments received	(45,411)
Unrealized gains included in other comprehensive income	52,348
Balance at June 30, 2015	$ 2,879,660

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.

Table of Contents

For assets measured at fair value on a nonrecurring basis during 2015 that were still held in the balance sheet at June 30, 2015, 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	$	$	$ 7,350,163	$ 7,350,163
Other real estate owned			437,847	$ 437,847
Total	$	$	$ 7,788,010	$ 7,788,010

For assets measured at fair value on a nonrecurring basis during 2014 that were still held in the balance sheet at December 31, 2014, 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	$	$	$ 8,782,923	$ 8,782,923
Other real estate owned			645,468	645,468
Total	$	$	$ 9,428,391	$ 9,428,391

Impaired loans with a carrying value of $9,833,430 and $10,243,082 had an allocated allowance for loan losses of $2,406,267 and $2,024,754 at June 30, 2015 and December 31, 2014, 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 six-month period ended June 30, 2015, and recorded at fair value, less costs to sell, was $617,548, of which $179,702 was acquired and sold during this period. There were no writedowns during the period on properties owned. OREO acquired during 2014 and recorded at fair value, less costs to sell, was $2,874,173. Additional writedowns during 2014 on OREO acquired in previous years was $694,207.

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.

The following represents the carrying value and estimated fair value of the Corporation s financial instruments at June 30, 2015, and December 31, 2014:

June 30, 2015	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Financial assets					
Cash and due from banks	$ 18,842,722	$ 18,842,722	$	$	$ 18,842,722
Interest bearing deposits with banks	11,083,914	11,083,914			11,083,914
Securities held-to-maturity	198,298,707		204,487,338		204,487,338
Securities available-for-sale	232,272,884		229,393,224	2,879,660	232,272,884
Net loans	400,622,906			402,890,374	402,890,374
Financial liabilities					
Deposits	$ 721,138,225	$ 503,322,935	$	$ 217,955,255	$ 721,278,190
Federal Home Loan Bank advances	20,000,000			20,770,705	20,770,705
Securities Sold under Agreement to Repurchase	94,962,842	94,962,842			94,962,842

Table of Contents

December 31, 2014	Carrying Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value
Financial assets					
Cash and due from banks	$ 22,405,730	$ 22,405,730	$	$	$ 22,405,730
Interest bearing deposits with banks	61,481,223	61,481,223			61,481,223
Securities available-for-sale	179,745,130		176,872,407	2,872,723	179,745,130
Securities held-to-maturity	206,817,168		216,745,438		216,745,438
Net loans	384,417,508			386,206,117	386,206,117
Financial liabilities					
Deposits	$ 696,093,894	$ 474,551,535	$	$ 221,685,000	$ 696,236,535
Federal Home Loan Bank advances	20,000,000			20,804,047	20,804,047
Securities Sold under Agreement to Repurchase	114,426,770	114,426,770			114,426,770

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 Held-to-Maturity

Securities held-to-maturity consists of debt securities such as obligations of states and other political subdivisions. Where quoted market prices in active markets are available, securities are classified within Level 1 of the fair value hierarchy. If quoted prices from active markets are not available, fair values are based on quoted market prices for similar instruments traded in active markets, quoted market prices for identical or similar instruments traded in markets that are not active, or model-based valuation techniques where all significant assumptions are observable in the market. Such instruments are classified within Level 2 of the fair value hierarchy. When assumptions used in model-based valuation techniques are not observable in the market, the assumptions used by management reflect estimates of assumptions used by other market participants in determining fair value. When there is limited transparency around the inputs to the valuation, the instruments are classified within Level 3 of the fair value hierarchy.

Table of Contents

Securities Available-for-Sale

Fair values for investment securities are based on quoted market prices, when available (Level 1). If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments (Level 2). 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 3).

The Corporation owns certain beneficial interests in one collateralized debt obligation secured by community bank trust preferred securities. These interests do not trade in a liquid market, and therefore, market quotes are not a reliable indicator of their ultimate realizability. The Corporation utilizes a discounted cash flow model using inputs of (1) market yields of trust-preferred securities as the discount rate and (2) expected cash flows which are estimated using assumptions related to defaults, deferrals and prepayments to determine the fair values of these beneficial interests. Many of the factors that adjust the timing and extent of cash flows are based on judgment and not directly observable in the markets. Therefore, these fair values are classified as Level 3 valuations for accounting and disclosure purposes. Since observable transactions in these securities are extremely rare, the Corporation uses assumptions that a market participant would use in valuing these instruments. These assumptions primarily include cash flow estimates and market discount rates. The cash flow estimates are sensitive to the assumptions related to the ability of the issuers to pay the underlying trust preferred securities according to their terms. The market discount rates depend on transactions, which are rare given the lack of interest of investors in these types of beneficial interests.

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.

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 a discounted cash flow analysis.

Table of Contents

Securities Sold Under Agreement to Repurchase

Due to the short term nature of these instruments, which is generally 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 Quarterly Report contains statements that 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 Quarterly Re not relate to historical facts are intended to identify forward-looking statements. These statements appear in a number of places in this Quarterly 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 Quarterly 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 June 30, 2015, was 33.11% and at December 31, 2014, was 37.72%. The decrease was due to a decrease in short term marketable assets at June 30, 2015. Management believes it maintains adequate liquidity for the Corporation s current needs.

The Corporation s primary source of liquidity is customer deposits, which were $721,138,225 at June 30, 2015, and $696,093,894 at December 31, 2014. 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 $232,272,884 invested in available-for-sale investment securities at June 30, 2015, and $179,745,130 at December 31, 2014. The Corporation also had $11,083,914 in interest bearing deposits at other banks at June 30, 2015 and $61,481,223 at December 31, 2014. The decrease in interest bearing deposits was the result of funds being invested in longer term investments, including certain mortgage backed products, which are expected to produce more interest income. The Corporation had secured and unsecured federal funds lines with correspondent banks in the amount of $45,000,000 at June 30, 2015 and December 31, 2014. In addition, the Corporation has the ability to draw on its line of credit with the FHLB. At June 30, 2015, the Corporation had unused and available $147,193,132 of its line of credit with the FHLB and at December 31, 2014, the Corporation had unused and available $142,313,563 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 2014 to June 30, 2015, was the result of an increase in the amount of loans eligible for the collateral pool. The Corporation had $0 in federal funds purchased as of June 30, 2015 and December 31, 2014. The Corporation usually purchases federal 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

Total shareholders equity was $82,077,023 at June 30, 2015, as compared to $81,857,786 at December 31, 2014. The reason for the increase in shareholders equity was the decrease in the accumulated other comprehensive loss brought about by the investment securities market value adjustment as well as the increase in the amount of earnings in excess of dividends paid. The market value increase was due to general market conditions, specifically the decrease in medium term interest rates, which caused an increase in the market price of the investment portfolio.

Aggregate cash dividends in the amount of $2,245,450, or $0.46 per share, have been paid during the six-month period ended June 30, 2015.

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 June 30, 2015, 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 June 30, 2015						
Total Capital (to Risk-Weighted Assets)	$ 95,342,314	18.14%	$ 42,053,906	>8.00%	$ 52,567,383	>10.00%
Tier 1 Capital (to Risk-Weighted Assets)	88,769,885	16.89%	21,026,953	>4.00%	31,540,430	>6.00%
Tier 1 Capital (to Average Assets)	88,769,885	9.61%	36,959,318	>4.00%	46,199,147	>5.00%

The Dodd-Frank Act requires the Federal Reserve Bank (FRB), the Office of the Comptroller of the Currency (OCC) and the FDIC to adopt regulations imposing a continuing floor on the risk based capital requirements. In December 2010, the Basel Committee released a final framework for a strengthened set of capital requirements, known as Basel III . In early July 2013, each of the U.S. federal banking agencies adopted final rules relevant to us: (1) the Basel III regulatory capital reforms; and (2) the standardized approach of Basel II for non-core banks and bank holding companies, such as the Bank and the Corporation. The capital framework under Basel III will replace the existing regulatory capital rules for all banks, savings associations and U.S. bank holding companies with greater than $500 million in total assets, and all savings and loan holding companies.

32

Table of Contents

Beginning January 1, 2015, the Bank was required to comply with the final Basel III rules, although the rules will not be fully phased-in until January 1, 2019. Among other things, the final Basel III rules will impact regulatory capital ratios of banking organizations in the following manner, when fully phased in:

- Create a new requirement to maintain a ratio of common equity Tier 1 capital to total risk-weighted assets of not less than 4.5%;

- Increase the minimum leverage capital ratio to 4% for all banking organizations (currently 3% for certain banking organizations);

- Increase the minimum Tier 1 risk-based capital ratio from 4% to 6%; and Maintain the minimum total risk-based capital ratio at 8%.

In addition, the final Basel III rules, when fully phased in, will subject a banking organization to certain limitations on capital distributions and discretionary bonus payments to executive officers if the organization did not maintain a capital conservation buffer of common equity Tier 1 capital in an amount greater than 2.5% of its total risk-weighted assets. The effect of the capital conservation buffer, when fully phased in, will be to increase the minimum common equity Tier 1 capital ratio to 7%, the minimum Tier 1 risk-based capital ratio to 8.5% and the minimum total risk-based capital ratio to 10.5% for banking organizations seeking to avoid the limitations on capital distributions and discretionary bonus payments to executive officers.

The final Basel III rules also changed the capital categories for insured depository institutions for purposes of prompt corrective action. Under the final rules, to be well capitalized, an insured depository institution must maintain a minimum common equity Tier 1 capital ratio of at least 6.5%, a Tier 1 risk-based capital ratio of at least 8%, a total risk-based capital ratio of at least 10.0%, and a leverage capital ratio of at least 5%. In addition, the final Basel III rules established more conservative standards for including an instrument in regulatory capital and imposed certain deductions from and adjustments to the measure of common equity Tier 1 capital.

Management believes that, as of June 30, 2015, the Corporation and the Bank would meet all capital adequacy requirements under Basel III and the banking agencies proposals on a fully phased-in basis if such requirements were currently effective. The changes to the calculation of risk-weighted assets did not have a material impact on the Corporation s capital ratios as presented. Management will continue to monitor these and any future proposals submitted by the Corporation s and Bank s regulators.

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 June 30, 2015	For the Three Months Ended June 30, 2014	For the Six Months Ended June 30, 2015	For the Six Months Ended June 30, 2014
Interest Income, including fees	$ 7,696,319	$ 7,925,513	$ 15,402,390	$ 15,871,441
Interest Expense	735,674	733,951	1,486,858	1,462,810
Net Interest Income	6,960,645	7,191,562	13,915,532	14,408,631
Provision for Loan Losses	81,818	211,535	265,994	572,903
Net Interest Income after Provision for Loan Losses	6,878,827	6,980,027	13,649,538	13,835,728
Other Income	1,851,851	2,483,622	3,603,596	4,267,102
Other Expense	6,321,150	7,045,995	12,808,124	13,414,858
Income Before Provision For Income Taxes	2,409,528	2,417,654	4,445,010	4,687,972
Provision for Income Taxes	580,941	325,135	1,022,877	798,300
Net Income	$ 1,828,587	$ 2,092,519	$ 3,422,133	$ 3,889,672
Net Income Per share - Basic	$ 0.37	$ 0.43	$ 0.70	$ 0.80
Net Income Per Share-Diluted	$ 0.37	$ 0.43	$ 0.70	$ 0.80

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 8.71% for the three months ended June 30, 2015, and 12.55% for the corresponding period in 2014. For the six months ended June 30, 2015, ROE was 8.20% compared to 11.50% for the six months ended June 30, 2014. In both instances, the decrease in ROE was caused by other income in the second quarter of 2014 that was the result of net proceeds from bank owned life insurance that were received after the death of an insured bank officer.

The book value per share increased to $16.80 at June 30, 2015, compared to $16.78 at December 31, 2014. The increase in book value per share reflects the amount of earnings in excess of dividends offset slightly by an increase in other comprehensive loss due to the decrease in fair value of the Corporation s investment securities. Average assets for the six months ended June 30, 2015, were $927,327,349 compared to $884,687,654 for the year ended

December 31, 2014.

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 3.39% for the quarter ended June 30, 2015 compared to 3.68% for the corresponding period of 2014. For the six months ended June 30, 2015, annualized net interest margin was 3.41% compared to 3.67% for the six months ended June 30, 2014. The decrease in net interest margin for both periods ended June 30, 2015, when compared to the same period in 2014, was the result of the decrease in yields on earning assets exceeding the decrease in rates paid on deposits and borrowed funds, as detailed below. Earning assets averaged $847,083,069 for the three months ended June 30, 2015. This represents an increase of $61,176,762, or 7.8%, over average earning assets of $785,906,307 for the three months ended June 30, 2014. The increase in average earning assets for the three months ended June 30, 2015, is the result of an increase in investment securities and loans.

Interest bearing deposits averaged $580,740,250 for the three months ended June 30, 2015. This represents an increase of $34,031,409, or 6.2%, from the average of interest bearing deposits of $546,708,481 for the three months ended June 30, 2014. This was due, in large part, to an increase in interest-bearing NOW, money market accounts and savings accounts partially offset by a decrease in certificates of deposit.

Other borrowed funds averaged $115,178,114 for the three months ended June 30, 2015. This represents a decrease of $6,017,019, or 5.0%, over the other borrowed funds of $121,195,133 for the three months ended June 30, 2014. This decrease in other borrowed funds was due to a $18,057,259 increase in the securities sold under agreement to repurchase, a $54,498 decrease in the Agribusiness Enterprise Loan Liability, a $2,607,692 decrease in Federal Funds Purchased and a decrease in the FHLB advances of $21,412,088 for the three months ended June 30, 2015, when compared to the three months ended June 30, 2014.

Interest bearing deposits averaged $570,549,460 for the six months ended June 30, 2015. This represents an increase of $26,323,986, or 4.8%, from the average of interest bearing deposits of $544,225,474 for the six months ended June 30, 2014. This was due, in large part, to an increase in interest-bearing NOW, money market accounts and savings accounts partially offset by a decrease in certificates of deposit.

Other borrowed funds averaged $125,072,207 for the six months ended June 30, 2015. This represents a decrease of $1,992,110, or 1.6%, over the other borrowed funds of $127,064,317 for the six months ended June 30, 2014. This decrease in other borrowed funds was due to a $28,681,208 increase in the securities sold under agreement to repurchase, a $56,191 decrease in the Agribusiness Enterprise Loan Liability, a $3,691,713 decrease in Federal Funds Purchased and a decrease in the FHLB advances of $26,925,414 for the six months ended June 30, 2015, when compared to the six months ended June 30, 2014.

Table of Contents

Net interest income was $6,960,645 for the three months ended June 30, 2015, a decrease of $230,917 from $7,191,562 for the three months ended June 30, 2014, primarily due to a decrease in rate partially offset by an increase in earning assets. 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 months ended June 30, 2015, the yields on earning assets decreased more than the rates paid on deposits and borrowed funds decreased from the same period in 2014. The yield on all interest bearing assets decreased 31 basis points to 3.73% in the three months ended June 30, 2015 from 4.04% for the same period in 2014. At the same time, the rate paid on all interest bearing liabilities for the three months ended June 30, 2015 dropped 1 basis point to 0.43% from 0.44% in the same period in 2014. 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 increase.

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

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2015	2014	2015	2014
Interest and Fees	$ 4,988,452	$ 5,067,445	$ 9,996,012	$ 10,111,355
Average Gross Loans	406,060,056	392,156,742	403,657,500	391,776,690
Annualized Yield	4.91%	5.17%	4.95%	5.16%

The decrease in interest rates in the three and six months ended June 30, 2015, reflects the decrease in all loan interest rates for both new and refinanced loans in the period.

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 management determines require further monitoring and supervision, are segregated and reviewed on a regular basis. Significant problem loans are reviewed monthly 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.

Table of Contents

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 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.

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

	Quarter Ended June 30, 2015	Year Ended December 31, 2014	Amount of Increase (Decrease)	Percent of Increase (Decrease)
BALANCES:				
Gross Loans	$ 407,985,639	$ 391,494,584	$ 16,491,055	4.21%
Allowance for Loan Losses	6,692,914	6,542,326	150,588	2.30%
Nonaccrual Loans	12,664,110	11,854,274	809,836	6.83%
Ratios:				
Allowance for loan losses to gross loans	1.64%	1.67%		
Net loans charged off to allowance for loan losses	1.72%	37.58%		

The provision for loan losses for the three months ended June 30, 2015, was $81,818, a decrease of $129,717 from the $211,535 provision for the same period in 2014. The provision for loan losses for the six months ended June 30, 2015, was $265,994, a decrease of $306,909 from the $572,903 provision for the same period in 2014. The change in our loan loss provisions for the three and six months is a result of management s assessment of inherent loss in the loan portfolio, including the impact caused by current local, national and international 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 exceeded payments received.

For the three months ended June 30, 2015, net loan losses charged to the allowance for loan losses totaled $14,726, a decrease of $18,953 from the $33,679 charged off in the same period in 2014. For the six months ended June 30, 2015, net loan losses charged to the allowance for loan losses totaled $115,406, an increase of $4,433 from the $110,973 charged off in the same period in 2014.

Table of Contents

Management reviews quarterly with the Corporation s Board of Directors the adequacy of the allowance for loan losses. 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 six months ended June 30, 2015 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, it remains possible that additional provisions for loan loss may be required.

Table of Contents

OTHER INCOME

Other income includes service charges on deposit accounts, wire transfer fees, safe deposit box rentals and other revenue not derived from interest on earning assets. Other income for the three months ended June 30, 2015 was $1,851,851, a decrease of $631,771, or 25.4%, from the same period in 2014. Service charges on deposit accounts decreased by $9,733, or 1.0%, to $954,093 in the three months ended June 30, 2015, compared to $963,826 for the same period in 2014. Other service charges and fees increased by $38,466, or 7.3%, to $563,161 in the three months ended June 30, 2015, compared to the same period in 2014. Other income decreased $660,504 in the three months ended June 30, 2015 from the same period in 2014 due to the net proceeds of bank owned life insurance as a result of the death of a insured bank officer. The increase in service charges on deposit accounts was the result of a increase in demand for these services and not a direct result of fee changes.

Other income for the six months ended June 30, 2015 was $3,603,596, a decrease of $663,506, or 15.5%, from the same period in 2014. Service charges on deposit accounts decreased by $52,680, or 2.8%, to $1,840,877 in the six months ended June 30, 2015, compared to $1,893,557 for the same period in 2014. Other service charges and fees increased by $85,882, or 8.5%, to $1,095,014 in the six months ended June 30, 2015, compared to the same period in 2014. Other income decreased $696,708 in the six months ended June 30, 2015 from the same period in 2014 due to the net proceeds of bank owned life insurance as a result of the death of a insured bank officer. The increase in service charges on deposit accounts was the result of a increase in demand for these services 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:

Other Income	Three months Ended June 30, 2015	Three months Ended June 30, 2014	Six months Ended June 30, 2015	Six months Ended June 30, 2014
BOLI Insurance	$ 144,000	$ 144,000	$ 288,000	$ 288,000
Mortgage Loan Origination Income	78,234	73,315	182,388	142,734
Income from security sales, net		9,102		9,102
Other Income	112,363	768,684	197,317	924,577
Total Other Income	$ 334,597	$ 995,101	$ 667,705	$ 1,364,413

OTHER EXPENSES

Other expenses include salaries and employee benefits, occupancy and equipment, and other operating expenses. Aggregate non-interest expenses for the three months ended June 30, 2015 and 2014 were $6,321,150 and $7,045,995, respectively, a decrease of $724,845, or 10.3%, from 2014 to 2015. Salaries and benefits increased slightly to $3,341,381 for the three months ended June 30, 2015, from $3,252,370 for the same period in 2014. Occupancy expense decreased by $274,230, or 17.5%, to $1,296,765 for the three months ended June 30, 2015, when compared to

Table of Contents

the same period of 2014. Other operating expenses decreased by $539,626 to $1,683,004 for the three months ended June 30, 2015, when compared to the same period of 2014. This decrease is due mainly to lower loan collection costs, supply costs and insurance costs. A detail of the major expense classifications is set forth below.

Total non-interest expenses for the six months ended June 30, 2015 and 2014 were $12,808,124 and $13,414,858, respectively, a decrease of $606,734, or 4.5%, from 2014 to 2015. Salaries and benefits increased slightly to $6,696,684 for the six months ended June 30, 2015, from $6,608,207 for the same period in 2014. Occupancy expense increased by $52,202, or 2.1%, to $2,596,259 for the six months ended June 30, 2015, when compared to the same period of 2014. Other operating expenses decreased by $747,413 to $3,515,181 for the six months ended June 30, 2015, when compared to the same period of 2014. This decrease is due mainly to lower loan collection costs, supply costs and insurance costs. A detail of the major expense classifications is set forth below.

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

	Three months ended June 30,		Six months ended June 30,	
Other Operating Expense	2015	2014	2015	2014
Advertising	179,984	212,056	389,407	364,040
Office Supplies	116,302	202,860	274,553	380,815
Legal and Audit Fees	14,173	41,657	214,060	146,311
Telephone expense	105,670	101,877	212,101	210,313
Postage and Freight	117,888	126,660	232,136	249,051
Loan Collection Expense	44,019	328,656	91,346	398,516
Other Losses	16,494	396,082	181,748	621,575
Regulatory and related expense	192,798	196,492	380,978	388,078
Debit Card/ATM expense	112,020	1,183	197,844	166,205
Travel and Convention	75,546	69,909	141,239	106,742
Other expenses	708,110	545,198	1,199,769	1,230,948
Total Other Expense	$ 1,683,004	$ 2,222,630	$ 3,515,181	$ 4,262,594

The Corporation s efficiency ratio for the three months ended June 30, 2015, was 69.80% compared to the 70.95% for the same period in 2014. For the six months ended June 30, 2015 and 2014, the Corporation s efficiency ratio was 71.15% and 69.84%, 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

	June 30, 2015	December 31, 2014	Amount of Increase (Decrease)	Percent of Increase (Decrease)
Cash and Due From Banks	$ 18,842,722	$ 22,405,730	$ (3,563,008)	-15.90%
Interest Bearing deposits with Other Banks	11,083,914	61,481,223	(50,397,309)	-81.97%
Investment Securities	430,571,591	386,562,299	44,009,292	11.38%
Loans, net	400,622,906	384,417,508	16,205,398	4.22%
Premises and Equipment	18,782,171	19,240,230	(458,059)	-2.38%
Total Assets	927,000,266	921,060,681	5,939,585	0.64%
Total Deposits	721,138,225	696,093,894	25,044,331	3.60%
Total Stockholders Equity	82,077,023	81,857,786	219,237	0.27%

CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash, balances at correspondent banks and items in process of collection. The balance at June 30, 2015 was $18,842,722, a decrease of $3,563,008 from the balance of $22,405,730 at December 31, 2014, due to a decrease in the balances at correspondent banks due to a decrease in the amount of the month ending cash letter.

INVESTMENT SECURITIES

The investment securities portfolio primarily consists of United States agency debentures, mortgage-backed securities and obligations of states, counties and municipalities. Investments at June 30, 2015, increased by $44,009,292, or 11.4%, to $430,571,591 from $386,562,299 at December 31, 2014. This increase is due to additional purchases of mortgage backed securities offset by changes in the market value of the securities portfolio.

LOANS

The loan balance increased by $16,205,398 during the six months ended June 30, 2015, to $400,622,906 from $384,417,508 at December 31, 2014. Loan demand, especially in business loan and consumer loan categories, strengthened and competition for available loans continued to be strong during the six months ended June 30, 2015. No material changes were made to the loan products offered by the Corporation during this period.

PREMISES AND EQUIPMENT

During the six months ended June 30, 2015, premises and equipment decreased by $458,059, or 2.4%, to $18,782,171 when compared to $19,240,230 at December 31, 2014. The decrease was due to depreciation expense exceeding the amount of property and equipment added for the period.

Table of Contents

DEPOSITS

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

DEPOSITS

	June 30, 2015	December 31, 2014	Amount of Increase (Decrease)	Percent of Increase (Decrease)
Noninterest-Bearing Deposits	$ 141,953,804	$ 145,729,932	$ (3,776,128)	-2.59%
Interest-Bearing Deposits	296,965,294	268,567,815	28,397,479	10.57%
Savings Deposits	64,403,837	60,253,788	4,150,049	6.89%
Certificates of Deposit	217,815,290	221,542,359	(3,727,069)	-1.68%
Total Deposits	$ 721,138,225	$ 696,093,894	$ 25,044,331	3.60%

Interest-bearing deposits and savings increased while certificates of deposit and noninterest-bearing deposits decreased during the six months ended June 30, 2015. 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 Quarterly Report for a discussion of the nature and extent of the Corporation s off-balance sheet arrangements, which consist solely 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, 2014.

Table of Contents

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

The following discussion of operations 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 condition or 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 risks below that it presently believes 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 that could affect the Corporation s financial condition or results of operation. 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 larger 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. The Corporation s ability to manage credit risk 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 June 30, 2015, the Corporation had approximately $6.6 million of available reserves to cover such losses. The models and approaches the Corporation uses to originate and manage loans are regularly reviewed, if necessary or advisable, 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.

Table of Contents

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 currency exchange, commodities or equity risk exposures.

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 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 as well as the rules and regulations promulgated by the Securities and Exchange Commission and the NASDAQ. Failure to comply with applicable regulations could result in financial or 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

Table of Contents

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 (individually 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 any certainty.

Accounting Estimate Risks

The preparation of the Corporation s consolidated financial statements in conformity with GAAP 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.

Table of Contents

ITEM 4. CONTROLS AND PROCEDURES.

The management of the Corporation, with the participation of our principal executive officer and principal financial officer, 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 officer and principal financial officer have concluded that such disclosure controls and procedures were effective as of June 30, 2015 (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 June 30, 2015, 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 is supplementing 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, 2014 filed with the Securities and Exchange Commission on March 13, 2015, 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.

Recently adopted changes to capital requirements for bank holding companies and depository institutions may negatively impact the Corporation s results of operations.

In July 2013, the Federal Reserve Board and the FDIC approved final rules that substantially amend the regulatory risk-based capital rules applicable to the Corporation. The final rules implement the Basel III regulatory capital reforms and changes required by the Dodd-Frank Act.

Under these recently adopted rules, the leverage and risk-based capital ratios of bank holding companies may not be lower than the leverage and risk-based capital ratios for insured depository institutions. The final rules implementing the Basel III regulatory capital reforms became effective as to the Corporation on January 1, 2015 and include new minimum risk-based capital and leverage ratios. Moreover, these rules refine the definition of what constitutes capital for purposes of calculating those ratios. The new minimum capital level requirements applicable to bank holding companies and banks subject to the rules are: (i) a new common equity Tier 1 capital ratio of 4.5%; (ii) a Tier 1 risk-based capital ratio of 6% (increased from 4%); (iii) a total risk-based capital ratio of 8% (unchanged from current rules); and (iv) a Tier 1 leverage ratio of 4% for all institutions. The rules also establish a capital conservation buffer of 2.5% (to be phased in over three years) above the new regulatory minimum capital ratios, and result in the following minimum ratios once the capital conservation buffer is fully phased in: (i) a common equity Tier 1 risk-based capital ratio of 7.0%; (ii) a Tier 1 risk-based capital ratio of 8.5%; and (iii) a total risk-based capital ratio of 10.5%. The capital conservation buffer requirement is to be phased in beginning in January 2016 at 0.625% of risk-weighted assets and would increase each year until fully implemented in January 2019. An institution will be subject to limitations on paying dividends, engaging in share repurchases and paying discretionary bonuses if its capital levels fall below the buffer amounts. These limitations establish a maximum percentage of eligible retained income that could be utilized for such actions.

Table of Contents

The application of these more stringent capital requirements to the Corporation could, among other things, result in lower returns on invested capital, require the raising of additional capital, and result in regulatory actions if the Corporation was to be unable to comply with such requirements. Furthermore, the imposition of liquidity requirements in connection with the implementation of the final rules regarding Basel III could result in the Corporation having to lengthen the term of their funding, restructure their business models or increase their holdings of liquid assets. Implementation of changes to asset risk weightings for risk-based capital calculations, items included or deducted in calculating regulatory capital or additional capital conservation buffers could result in management modifying its business strategy and could limit the Corporation s ability to make distributions, including paying dividends or buying back shares.

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 June 30, 2015, filed with the SEC on August 10, 2015, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Condition as of June 30, 2015 (Unaudited) and December 31, 2014 (Audited); (ii) the Consolidated Statements of Income for the three and six months ended June 30, 2015 (Unaudited) and 2014 (Unaudited); (iii) the Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2015 (Unaudited) and 2014 (Unaudited); (iv) the Consolidated Statements of Cash Flows for the six months ended June 30, 2015 (Unaudited) and 2014 (Unaudited); and (v) Notes to Consolidated Financial Statements, tagged as blocks of text (Unaudited).

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 Officer and Chief Accounting Officer)

DATE: August 6, 2015

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 June 30, 2015, filed with the SEC on August 10, 2015, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Condition as of June 30, 2015 (Unaudited) and December 31, 2014 (Audited); (ii) the Consolidated Statements of Income for the three and six months ended June 30, 2015 (Unaudited) and 2014 (Unaudited); (iii) the Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2015 (Unaudited) and 2014 (Unaudited); (iv) the Consolidated Statements of Cash Flows for the six months ended June 30, 2015 (Unaudited) and 2014 (Unaudited); and (v) Notes to Consolidated Financial Statements, tagged as blocks of text (Unaudited).