CITIZENS HOLDING CO /MS/
Form 10-Q
August 08, 2013
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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, 2013

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 incorporation or organization)	**(IRS Employer 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, 2013:

Title	Outstanding
Common Stock, $0.20 par value	4,870,114

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CITIZENS HOLDING COMPANY

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PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS.

CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF CONDITION

	June 30, 2013	December 31, 2012
ASSETS		
Cash and due from banks	$ 19,572,317	$ 21,561,288
Interest bearing deposits with other banks	3,538,237	16,228,747
Investment securities available for sale, at fair value	418,552,716	420,907,815
Loans, net of allowance for loan losses of $6,803,043 in 2013 and $6,954,269 in 2012	356,224,900	361,936,495
Premises and equipment, net	18,965,981	19,425,292
Other real estate owned, net	4,588,832	4,682,255
Accrued interest receivable	3,963,496	4,665,868
Cash value of life insurance	21,525,566	21,191,930
Intangible assets, net	3,149,657	3,149,657
Other assets	16,580,769	7,090,551
TOTAL ASSETS	$ 866,662,471	$ 880,839,898
LIABILITIES AND STOCKHOLDERS EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$ 120,057,734	$ 119,946,574
Interest-bearing NOW and money market accounts	243,924,050	228,111,275
Savings deposits	51,054,475	46,240,652
Certificates of deposit	238,118,973	248,250,837
Total deposits	653,155,232	642,549,338
Securities sold under agreement to repurchase	64,444,099	73,306,765
Federal funds purchased	23,500,000	
Federal Home Loan Bank advances	43,500,000	68,500,000
Accrued interest payable	235,850	321,472
Deferred compensation payable	6,307,090	5,917,662
Other liabilities	2,069,490	1,375,831
Total liabilities	793,211,761	791,971,068
STOCKHOLDERS EQUITY		
Common stock; $.20 par value, 22,500,000 shares authorized, 4,870,114 shares outstanding at June 30, 2013 and 4,861,411 shares outstanding at December 31, 2012	973,982	972,282
Additional paid-in capital	3,748,217	3,620,967
Retained earnings	80,803,705	79,928,035
Accumulated other comprehensive income (loss), net of applicable taxes of $7,183,489 in 2013 and ($2,586,340) in 2012	(12,075,194)	4,347,546
Total stockholders equity	73,450,710	88,868,830
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 866,662,471	$ 880,839,898

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

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CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
INTEREST INCOME				
Loans, including fees	$ 5,120,642	$ 6,038,190	$ 10,319,823	$ 12,010,427
Investment securities	2,850,563	2,956,655	5,621,329	5,874,050
Other interest	19,714	8,323	37,414	17,681
Total interest income	7,990,919	9,003,168	15,978,566	17,902,158
INTEREST EXPENSE				
Deposits	494,614	703,728	1,014,757	1,428,434
Other borrowed funds	690,468	753,525	1,402,551	1,539,408
Total interest expense	1,185,082	1,457,253	2,417,308	2,967,842
NET INTEREST INCOME	6,805,837	7,545,915	13,561,258	14,934,316
PROVISION FOR LOAN LOSSES	574,595	330,097	749,104	865,777
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	6,231,242	7,215,818	12,812,154	14,068,539
OTHER INCOME				
Service charges on deposit accounts	913,942	897,920	1,804,799	1,745,570
Other service charges and fees	473,586	437,473	926,513	866,069
Other income	541,342	301,763	878,549	635,116
Total other income	1,928,870	1,637,156	3,609,861	3,246,755
OTHER EXPENSES				
Salaries and employee benefits	3,336,317	3,473,956	6,642,487	7,033,660
Occupancy expense	1,111,195	1,097,856	2,223,706	2,129,165
Other operating expense	1,699,519	2,102,189	3,838,002	3,921,443
Total other expenses	6,147,031	6,674,001	12,704,195	13,084,268
INCOME BEFORE PROVISION FOR INCOME TAXES	2,013,081	2,178,973	3,717,820	4,231,026
PROVISION FOR INCOME TAXES	409,337	427,375	699,630	816,262
NET INCOME	$ 1,603,744	$ 1,751,598	$ 3,018,190	$ 3,414,764
NET INCOME PER SHARE				
-Basic	$ 0.33	$ 0.36	$ 0.62	$ 0.70
-Diluted	$ 0.33	$ 0.36	$ 0.62	$ 0.70
DIVIDENDS PAID PER SHARE	$ 0.22	$ 0.22	$ 0.44	$ 0.44

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

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CITIZENS HOLDING COMPANY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Net income	$ 1,603,744	$ 1,751,598	$ 3,018,190	$ 3,414,764
Other comprehensive (loss) income				
Unrealized holding (losses) gains	(28,291,193)	4,631,065	(26,037,912)	1,190,231
Income tax effect	8,871,667	(1,727,387)	9,712,141	(443,956)
	(19,419,526)	2,903,678	(16,325,771)	746,275
Reclassification adjustment for gains included in net income	(154,655)	(9,061)	(154,655)	(37,753)
Income tax effect	57,686	3,380	57,686	14,082
	(96,969)	(5,681)	(96,969)	(23,671)
Total other comprehensive (loss) income	(19,516,495)	2,897,997	(16,422,740)	722,604
Comprehensive (loss) income	$ (17,912,751)	$ 4,649,595	$ (13,404,550)	$ 4,137,368

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

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CITIZENS HOLDING COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the Six Months Ended June 30, 2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net cash provided by operating activities	$ 6,335,193	$ 6,065,086
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from maturities and calls of securities available for sale	74,355,294	190,899,754
Purchases of investment securities available for sale	(135,615,144)	(115,075,780)
Proceeds from sales of investment securities	37,061,134	
Purchases of bank premises and equipment	(101,530)	(30,889)
Decrease (increase) in interest bearing deposits with other banks	12,690,510	(63,966,812)
Purchase of Federal Home Loan Bank Stock		(282,700)
Proceeds from sale of other real estate	1,032,649	1,235,367
Net decrease in loans	4,023,265	3,874,402
Net cash (used by) provided by investing activities	(6,553,822)	16,653,342
CASH FLOWS FROM FINANCING ACTIVITIES		
Net increase in deposits	10,605,894	19,233,750
Net change in securities sold under agreement to repurchase	(8,862,666)	(41,116,643)
Proceeds from exercising stock options	128,950	257,425
(Decrease) increase in Federal Home Loan Bank advances	(25,000,000)	10,000,000
Increase in federal funds purchased	23,500,000	
Payment of dividends	(2,142,520)	(2,137,261)
Net cash used by financing activities	(1,770,342)	(13,762,729)
Net decrease in cash and due from banks	(1,988,971)	8,955,699
Cash and due from banks, beginning of period	21,561,288	35,407,715
Cash and due from banks, end of period	$ 19,572,317	$ 44,363,414

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

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CITIZENS HOLDING COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

As of and for the three and six months ended June 30, 2013

(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, 2013, 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, 2012, filed with the Securities and Exchange Commission on March 15, 2013.

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, 2013, the Corporation had entered into loan commitments with certain customers with an aggregate unused balance of $43,211,976 compared to an aggregate unused balance of $37,703,387 at December 31, 2012. There were $3,082,530 of letters of credit outstanding at June 30, 2013 and $3,113,225 at December 31, 2012. The fair value of such contracts is not considered material because letters of credit and loan commitments often are not used in their entirety, if at all, before they expire. The balances of such letters and commitments should not be used to project actual future liquidity requirements. However, the Corporation does incorporate expectations about the level of draws under its credit-related commitments into its asset and liability management program.

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

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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,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Basic weighted average shares outstanding	4,868,977	4,859,125	4,866,237	4,854,145
Dilutive effect of granted options	588	6,881	3,363	8,654
Diluted weighted average shares outstanding	4,869,565	4,866,006	4,869,600	4,862,799
Net income	$ 1,603,744	$ 1,751,598	$ 3,018,190	$ 3,414,764
Net income per share-basic	$ 0.33	$ 0.36	$ 0.62	$ 0.70
Net income per share-diluted	$ 0.33	$ 0.36	$ 0.62	$ 0.70

Note 4. Stock Option Plan

For the quarter ended June 30, 2013, the Corporation utilized one stock-based compensation plan, which is the 1999 Directors Stock Compensation Plan (the Directors Plan). Prior to its expiration, the Corporation also had the 1999 Employees Long-Term Incentive Plan, or the Employees Plan.

The Corporation has adopted the 2013 Incentive Compensation Plan (the 2013 Plan), which the Corporation intends to use for all future equity grants until the termination or expiration of the 2013 Plan.

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The following table below is a summary of the stock option activity for the three months ended June 30, 2013.

	Directors Plan		Employees Plan	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Outstanding at December 31, 2012	111,000	$ 20.97	108,000	$ 20.90
Granted				
Exercised	(3,000)	16.40	(7,000)	14.91
Expired	(4,500)	16.40	(16,000)	17.36
Outstanding at June 30, 2013	103,500	$ 21.30	85,000	$ 22.06

The intrinsic value of options granted under the Directors Plan at June 30, 2013, was $33,405 and the intrinsic value of options granted under the Employees Plan at June 30, 2013, was $2,565 for a total intrinsic value at June 30, 2013, of $35,970. No awards have been granted under the 2013 Plan.

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, 2013, 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 2013 relative to any tax positions taken. It is the Corporation s policy to recognize interest and/or penalties related to income tax matters in income tax expense.

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 2009. The Corporation s consolidated state income tax returns are also open to audit under the statute of limitations for the same period.

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Note 6. Loans

The composition of net loans at June 30, 2013 and December 31, 2012 is as follows:

	June 30, 2013	December 31, 2012
	(In Thousands)	
Real Estate:		
Land Development and Construction	$ 17,840	$ 12,755
Farmland	30,896	31,663
1-4 Family Mortgages	107,981	115,837
Commercial Real Estate	135,850	132,495
Total Real Estate Loans	292,567	292,750
Business Loans:		
Commercial and Industrial Loans	42,783	45,564
Farm Production and Other Farm Loans	1,507	1,433
Total Business Loans	44,290	46,997
Consumer Loans:		
Credit Cards	1,038	1,050
Other Consumer Loans	25,573	28,341
Total Consumer Loans	26,611	29,391
Total Gross Loans	363,468	369,138
Unearned income	(440)	(248)
Allowance for loan losses	(6,803)	(6,954)
Loans, net	$ 356,225	$ 361,936

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.

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

	June 30, 2013	December 31, 2012
	(in thousands)	
Real Estate:		
Land Development and Construction	$ 150	$ 142
Farmland	438	1,087
1-4 Family Mortgages	1,833	2,356
Commercial Real Estate	8,890	10,175
Total Real Estate Loans	11,311	13,760
Business Loans:		
Commercial and Industrial Loans	2,178	167
Farm Production and Other Farm Loans	2	3
Total Business Loans	2,180	170
Consumer Loans:		
Other Consumer Loans	200	212
Total Consumer Loans	200	212
Total Non-Accrual Loans	$ 13,691	$ 14,142

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An aging analysis of past due loans, segregated by class of loans, as of June 30, 2013, was as follows (in thousands):

	Loans 30-89 Days Past Due	Loans 90 or more Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or more Days Past Due
Real Estate:						
Land Development and Construction	$ 10	$ 406	$ 416	$ 17,424	$ 17,840	$ 406
Farmland	455	69	524	30,596	30,896	
1-4 Family Mortgages	3,830	177	4,007	104,666	107,981	
Commercial Real Estate	6,396	4,055	10,451	130,127	135,850	
Total Real Estate Loans	10,691	4,707	15,398	282,813	292,567	406
Business Loans:						
Commercial and Industrial Loans	239	25	264	42,589	42,783	
Farm Production and Other Farm Loans	46		46	1,461	1,507	
Total Business Loans	285	25	310	44,050	44,290	
Consumer Loans:						
Credit Cards	29	15	44	994	1,038	15
Other Consumer Loans	916	80	996	24,635	25,573	47
Total Consumer Loans	945	95	1,040	25,629	26,611	62
Total Loans	$ 11,921	$ 4,827	$ 16,748	$ 352,492	$ 363,468	$ 468

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An aging analysis of past due loans, segregated by class of loans, as of December 31, 2012 was as follows (in thousands):

	Loans 30-89 Days Past Due	Loans 90 or more Days Past Due	Total Past Due Loans	Current Loans	Total Loans	Accruing Loans 90 or more Days Past Due
Real Estate:						
Land Development and Construction	$ 2,588	$	$ 2,588	$ 10,167	$ 12,755	$
Farmland	786	589	1,375	30,288	31,663	
1-4 Family Mortgages	8,139	623	8,762	107,075	115,837	32
Commercial Real Estate	3,033	5,013	8,046	124,449	132,495	544
Total Real Estate Loans	14,546	6,225	20,771	271,979	292,750	576
Business Loans:						
Commercial and Industrial Loans	3,070	9	3,079	42,485	45,564	
Farm Production and other Farm Loans	2		2	1,431	1,433	
Total Business Loans	3,072	9	3,081	43,916	46,997	
Consumer Loans:						
Credit Cards	40	30	70	980	1,050	30
Other Consumer Loans	1,711	57	1,768	26,573	28,341	3
Total Consumer Loans	1,751	87	1,838	27,553	29,391	33
Total Loans	$ 19,369	$ 6,321	$ 25,690	$ 343,448	$ 369,138	$ 609

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 contract terms. If a loan is determined to be impaired and the collateral is deemed to be insufficient to fully repay the loan, a specific reserve will be established. Interest payments on impaired loans are typically applied to principal unless collectability of the principal amount is reasonably assured, in which case interest is recognized on a cash basis. Impaired loans or portions thereof, are charged-off when deemed uncollectible.

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Impaired loans as of June 30, 2013 and December 31, 2012, by class of loans, are as follows (in thousands):

June 30, 2013	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	$ 150	$ 33	$ 117	$ 150	$ 117	$ 172
Farmland	438	303	135	438	24	594
1-4 Family Mortgages	1,833	1,484	349	1,833	95	2,055
Commercial Real Estate	8,890	706	8,184	8,890	1,009	9,172
Total Real Estate Loans	11,311	2,526	8,785	11,311	1,245	11,993
Business Loans:						
Commercial and Industrial Loans	2,178	2,099	79	2,178	55	2,375
Farm Production and Other Farm Loans	2	2		2		2
Total Business Loans	2,180	2,101	79	2,180	55	2,377
Consumer Loans:						
Other Consumer Loans	200	200		200		190
Total Consumer Loans	200	200		200		190
Total Loans	$ 13,691	$ 4,827	$ 8,864	$ 13,691	$ 1,300	$ 13,419

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December 31, 2012	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	$ 142	$ 18	$ 124	$ 142	$ 117	$ 638
Farmland	1,087	947	140	1,087	24	864
1-4 Family Mortgages	2,356	1,740	616	2,356	186	2,211
Commercial Real Estate	10,175	5,954	4,221	10,175	711	8,496
Total Real Estate Loans	13,760	8,659	5,101	13,760	1,038	12,209
Business Loans:						
Commercial and Industrial Loans	167	76	91	167	55	226
Farm Production and other Farm Loans	3	3		3		12
Total Business Loans	170	79	91	170	55	238
Consumer Loans:						
Other Consumer Loans	212	212		212		323
Total Consumer Loans	212	212		212		323
Total Loans	$ 14,142	$ 8,950	$ 5,192	$ 14,142	$ 1,093	$ 12,770

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

June 30, 2013	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial real estate	4	$ 6,850	$ 5,213
Total	4	$ 6,850	$ 5,213

December 31, 2012	Number of Loans	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial real estate	4	$ 6,850	$ 5,602
Total	4	$ 6,850	$ 5,602

Changes in the Company s troubled debt restructurings are set forth in the table below:

	Number of Loans	Recorded Investment
Totals at January 1, 2013	4	$ 5,602
Reductions due to:		
Principal paydowns		(389)
Total at June 30, 2013	4	$ 5,213

The allocated allowance for loan losses attributable to restructured loans was $194 thousand at June 30, 2013 and $43 thousand at December 31, 2012. The Corporation had no remaining availability under commitments to lend additional funds on these troubled debt restructuring as of June 30, 2013.

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

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

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

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

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.

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

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

These internally assigned grades are updated on a continual basis throughout the course of the year and represent management s most updated judgment regarding grades at June 30, 2013.

The following table details the amount of gross loans by loan grade and class as of June 30, 2013 (in thousands):

Grades	Satisfactory 1, 2, 3, 4	Special Mention 5, 6	Substandard 7	Doubtful 8	Loss 9	Total Loans
Real Estate:						
Land Development and Construction	$ 15,704	$ 1,855	$ 281	$	$	$ 17,840
Farmland	26,560	2,705	1,631			30,896
1-4 Family Mortgages	90,311	5,837	11,833			107,981
Commercial Real Estate	113,753	6,274	15,823			135,850
Total Real Estate Loans	246,328	16,671	29,568			292,567
Business Loans:						
Commercial and Industrial Loans	39,795	451	2,512	25		42,783
Farm Production and Other Farm Loans	1,491	12	4			1,507
Total Business Loans	41,286	463	2,516	25		44,290
Consumer Loans:						
Credit Cards	1,023		15			1,038
Other Consumer Loans	24,502	265	756	49	1	25,573
Total Consumer Loans	25,525	265	771	49	1	26,611
Total Loans	$ 313,139	$ 17,399	$ 32,855	$ 74	$ 1	$ 363,468

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The following table details the amount of gross loans by loan grade and class as of December 31, 2012 (in thousands):

Grades	Satisfactory 1, 2, 3, 4	Special Mention 5, 6	Substandard 7	Doubtful 8	Loss 9	Total Loans
Real Estate:						
Land Development and Construction	$ 10,596	$ 1,890	$ 269	$	$	$ 12,755
Farmland	27,069	2,701	1,893			31,663
1-4 Family Mortgages	97,630	6,177	12,030			115,837
Commercial Real Estate	108,914	6,728	16,853			132,495
Total Real Estate Loans	244,209	17,496	31,045			292,750
Business Loans:						
Commercial and Industrial Loans	41,449	3,486	601	28		45,564
Farm Production and other Farm Loans	1,358	26	49			1,433
Total Business Loans	42,807	3,512	650	28		46,997
Consumer Loans:						
Credit Cards	1,020		30			1,050
Other Consumer Loans	26,995	287	1,029	28	2	28,341
Total Consumer Loans	28,015	287	1,059	28	2	29,391
Total Loans	$ 315,031	$ 21,295	$ 32,754	$ 56	$ 2	$ 369,138

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 5 years with the most current years weighted to show the effect of the most recent chargeoff activity. This percentage is also adjusted for economic factors such as local unemployment and general business conditions, both local and nationwide.

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

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The following table details activity in the allowance for possible loan losses by portfolio segment for the six months ended June 30, 2013:

June 30, 2013	Real Estate	Business Loans	Consumer	Total
Beginning Balance, January 1, 2013	$ 4,629,559	$ 1,554,698	$ 770,012	$ 6,954,269
Provision for possible loan losses	640,104	262,487	(153,487)	749,104
Chargeoffs	606,296	345,651	75,725	1,027,672
Recoveries	72,133	13,311	41,898	127,342
Net Chargeoffs	534,163	332,340	33,827	900,330
Ending Balance	$ 4,735,500	$ 1,484,845	$ 582,698	$ 6,803,043
Period end allowance allocated to:				
Loans individually evaluated for impairment	$ 1,244,809	$ 54,706	$	$ 1,299,515
Loans collectively evaluated for impairment	3,490,691	1,430,139	582,698	5,503,528
Ending Balance, June 30, 2013	$ 4,735,500	$ 1,484,845	$ 582,698	$ 6,803,043

The following table details activity in the allowance for possible loan losses by portfolio segment for the six months ended June 30, 2012:

June 30, 2012	Real Estate	Business Loans	Consumer	Total
Beginning Balance, January 1, 2012	$ 4,176,475	$ 1,672,467	$ 832,470	$ 6,681,412
Provision for possible loan losses	817,494	(160,894)	209,177	865,777
Chargeoffs	280,703	28,759	158,865	468,327
Recoveries	28,459	39,553	63,843	131,855
Net Chargeoffs	252,244	(10,794)	95,022	336,472
Ending Balance, June 30, 2012	$ 4,741,725	$ 1,522,367	$ 946,625	$ 7,210,717
Period end allowance allocated to:				
Loans individually evaluated for impairment	$ 1,548,065	$ 57,325	$	$ 1,605,390
Loans collectively evaluated for impairment	3,193,660	1,465,042	946,625	5,605,327
Ending Balance, June 30, 2012	$ 4,741,725	$ 1,522,367	$ 946,625	$ 7,210,717

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The Corporation s recorded investment in loans as of June 30, 2013 and December 31, 2012 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, 2013	Real Estate	Business Loans	Consumer	Total
Loans individually evaluated for specific impairment	$ 11,311	$ 2,180	$ 200	$ 13,691
Loans collectively evaluated for general impairment	281,256	42,110	26,411	349,777
	$ 292,567	$ 44,290	$ 26,611	$ 363,468

December 31, 2012	Real Estate	Business Loans	Consumer	Total
Loans individually evaluated for specific impairment	$ 13,760	$ 170	$ 212	$ 14,142
Loans collectively evaluated for general impairment	278,990	46,827	29,179	354,996
	$ 292,750	$ 46,997	$ 29,391	$ 369,138

Note 7. Recent Accounting Pronouncements

In February 2013, Financial Accounting Standards Board (FASB) issued an update to ASC 220, Comprehensive Income, (ASC 220) that requires a reporting entity to disclose information about reclassification adjustments from accumulated other comprehensive income in their financial statements on the face of the financial statement that presents comprehensive income or as a separate disclosure in the footnotes of the financial statements. This update to ASC 220 is effective prospectively for interim and annual reporting periods beginning after December 15, 2012, with early adoption permitted. The adoption of the update will impact disclosures only and has not had a material impact on the financial position or results of operations of the Company.

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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, 2013:

	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	$	$ 296,762,855	$	$ 296,762,855
Mortgage-backed Securities		19,574,602		19,574,602
State, county and municipal obligations		99,564,767		99,564,767
Other investments			2,650,492	2,650,492
Total	$	$ 415,902,224	$ 2,650,492	$ 418,552,716

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The following table presents assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2012:

	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	$	$ 269,110,901	$	$ 269,110,901
Mortgage-backed Securities		38,421,301		38,421,301
State, county and municipal obligations		110,569,360		110,569,360
Other investments			2,806,253	2,806,253
Total	$	$ 418,101,562	$ 2,806,253	$ 420,907,815

The following table reports the activity for 2013 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, 2013	$ 2,806,253
Unrealized losses included in other comprehensive income	(155,761)
Balance at June 30, 2013	$ 2,650,492

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.

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For assets measured at fair value on a nonrecurring basis during 2013 that were still held in the balance sheet at June 30, 2013, 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	$	$	$ 7,564,919	$ 7,564,919
Other real estate owned			759,357	759,357
Total	$	$	$ 8,324,276	$ 8,324,276

For assets measured at fair value on a nonrecurring basis during 2012 that were still held in the balance sheet at December 31, 2012, 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	$	$	$ 4,099,031	$ 4,099,031
Other real estate owned			2,469,110	2,469,110
Total	$	$	$ 6,568,141	$ 6,568,141

Impaired loans with a carrying value of $8,864,434 and $5,192,258 had an allocated allowance for loan losses of $1,299,515 and $1,093,227 at June 30, 2013 and December 31, 2012, 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, 2013, and recorded at fair value, less costs to sell, was $939,226, of which $179,869 was acquired and sold during this period. There have been no writedowns during the period on OREO previously acquired and still held. OREO acquired during 2012 and recorded at fair value, less costs to sell, was $1,697,450. Additional writedowns during 2012 on OREO acquired in previous years was $309,797 on 5 properties valued at $1,081,457.

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, 2013, and December 31, 2012:

June 30, 2013	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	$ 19,572,317	$ 19,572,317	$	$	$ 19,572,317
Interest bearing deposits with banks	3,538,237	3,538,237			3,538,237
Securities available-for-sale	418,552,716		415,902,224	2,650,492	418,552,716
Net loans	356,224,900			358,627,387	358,627,387
Financial liabilities					
Deposits	$ 653,155,232	$ 415,036,259	$	$ 238,306,117	$ 653,342,376
Federal Home Loan Bank advances	43,500,000			44,723,137	44,723,137
Securities Sold under Agreement to Repurchase	64,444,099	64,444,099			64,444,099

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December 31, 2012	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	$ 21,561,288	$ 21,561,288	$	$	$ 21,561,288
Interest bearing deposits with banks	16,228,747	16,228,747			16,228,747
Securities available-for-sale	420,907,815		418,101,562	2,806,253	420,907,815
Net loans	361,936,495			362,114,991	362,114,991
Financial liabilities					
Deposits	$ 642,549,338	$ 394,298,501	$	$ 248,464,899	$ 642,763,400
Federal Home Loan Bank advances	68,500,000			70,844,530	70,844,530
Securities Sold under Agreement to Repurchase	73,306,765	73,306,765			73,306,765

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

Cash and Due from Banks and Interest Bearing Deposits with Banks

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

Securities Available-for-Sale

Fair values for investment securities are based on quoted market prices, when available (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.

Securities Sold Under Agreement to Repurchase

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

Off-Balance Sheet Instruments

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

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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 Qua do 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.

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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, 2013, was 40.53% and at December 31, 2012, was 44.74%. Liquidity decreased due to a decrease in short term marketable assets and an increase in core deposits at June 30, 2013. Management believes it maintains adequate liquidity for the Corporation s current needs.

The Corporation s primary source of liquidity is customer deposits, which were $653,155,232 at June 30, 2013, and $642,549,338 at December 31, 2012. 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 $418,552,716 invested in investment securities at June 30, 2013, and $420,907,815 at December 31, 2012. The Corporation also had $3,538,237 in interest bearing deposits at other banks at June 30, 2013 and $16,228,747 at December 31, 2012. The Corporation had secured and unsecured federal funds lines with correspondent banks in the amount of $37,500,000 at June 30, 2013 and December 31, 2012. In addition, the Corporation has the ability to draw on its line of credit with the FHLB. At June 30, 2013, the Corporation had unused and available $101,141,372 of its line of credit with the FHLB and at December 31, 2012, the Corporation had unused and available $96,139,520 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 2012 to June 30, 2013, was the result of a reduction in the amount of advances outstanding partially offset by a reduction in the amount of loans eligible for the collateral pool. The Corporation had $23,500,000 in federal funds purchased as of June 30, 2013 and none at December 31, 2012. The Corporation usually purchases funds from correspondent banks on a temporary basis to meet short term funding needs.

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

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CAPITAL RESOURCES

The total stockholders equity was $73,450,710 at June 30, 2013, as compared to $88,868,830 at December 31, 2012. The reason for the decrease in stockholders equity was the decrease in the investment securities market value adjustment due to a decrease in the market value of the Corporation s investment portfolio and the decrease in the amount of earnings in excess of dividends paid. This market value decrease was due to general market conditions, specifically the increase in medium term interest rates, which caused a decrease in the market price of the investment portfolio.

Cash dividends in the amount of $2,142,520, or $0.44 per share, have been paid as of the end of the quarter ended June 30, 2013.

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, 2013, 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, 2013						
Total Capital (to Risk-Weighted Assets)	$ 88,448,392	18.24%	$ 38,803,259	>8.00%	$ 48,504,074	>10.00%
Tier 1 Capital (to Risk-Weighted Assets)	82,376,247	16.98%	19,401,630	>4.00%	29,102,444	>6.00%
Tier 1 Capital (to Average Assets)	82,376,247	9.29%	35,466,413	>4.00%	44,333,016	>5.00%

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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,		For the Six Months Ended June 30,	
	2013	2012	2013	2012
Interest Income, including fees	$ 7,990,919	$ 9,003,168	$ 15,978,566	$ 17,902,158
Interest Expense	1,185,082	1,457,253	2,417,308	2,967,842
Net Interest Income	6,805,837	7,545,915	13,561,258	14,934,316
Provision for Loan Losses	574,595	330,097	749,104	865,777
Net Interest Income after Provision for Loan Losses	6,231,242	7,215,818	12,812,154	14,068,539
Other Income	1,928,870	1,637,156	3,609,861	3,246,755
Other Expense	6,147,031	6,674,001	12,704,195	13,084,268
Income Before Provision For Income Taxes	2,013,081	2,178,973	3,717,820	4,231,026
Provision for Income Taxes	409,337	427,375	699,630	816,262
Net Income	$ 1,603,744	$ 1,751,598	$ 3,018,190	$ 3,414,764
Net Income Per share - Basic	$ 0.33	$ 0.36	$ 0.62	$ 0.70
Net Income Per Share-Diluted	$ 0.33	$ 0.36	$ 0.62	$ 0.70

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

Annualized return on average equity (ROE) was 7.30% for the three months ended June 30, 2013, and 7.79% for the corresponding period in 2012. For the six months ended June 30, 2013, ROE was 6.95% compared to 7.74% for the six months ended June 30, 2012. In both instances, the decrease in ROE was caused by a lower net interest income.

The book value per share decreased to $15.08 at June 30, 2013, compared to $18.28 at December 31, 2012. The decrease in book value per share reflects the decrease in other comprehensive income due to the decrease in fair value of the Corporation s investment securities offset by the amount of earnings in excess of dividends. Average assets for the six months ended June 30, 2013, were $890,437,264 compared to $842,455,950 for the year ended December 31, 2012.

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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 3.48% for the second quarter of 2013 compared to 4.16% for the corresponding period of 2012. For the six months ended June 30, 2013, annualized net interest margin was 3.50% compared to 4.13% for the six months ended June 30, 2012. The decrease in net interest margin from 2012 to 2013 is the result of a decrease in yields on earning assets exceeding the decrease in rates paid on deposits and borrowed funds, offset partially by an increase in average earning assets, as detailed below. Earning assets averaged $808,655,185 for the three months ended June 30, 2013. This represents an increase of $34,559,986, or 4.5%, over average earning assets of $774,095,199 for the three-month period ended June 30, 2012. Earning assets averaged $809,715,877 for the six months ended June 30, 2013. This represents an increase of $43,914,419, or 5.7% over average earning assets of $765,801,458 for the six months ended June 30, 2012. The increase in earning assets for the three and six months ended June 30, 2013, is the result of an increase in investment securities offset partially by a decrease in loans due to the declining loan demand due to current local, national and international economic conditions.

Interest bearing deposits averaged $535,671,123 for the three months ended June 30, 2013. This represents an increase of $65,175,106, or 13.9%, from the average of interest bearing deposits of $470,496,017 for the three-month period ended June 30, 2012. This was due, in large part, to an increase in interest-bearing NOW and money market accounts partially offset by a decrease in certificates of deposit.

Other borrowed funds averaged $144,225,051 for the three months ended June 30, 2013. This represents a decrease of $19,763,150, or 12.1%, over the other borrowed funds of $163,988,201 for the three-month period ended June 30, 2012. This decrease in other borrowed funds was due to a $4,312,761 decrease in the securities sold under agreement to repurchase, a $66,597 decrease in the Agribusiness Enterprise Loan Liability, a $2,680,495 decrease in Federal Funds Purchased and a decrease in the FHLB advances of $12,703,297 for the three-month period ended June 30, 2012, when compared to the three-month period ended June 30, 2012.

Interest bearing deposits averaged $537,157,304 for the six months ended June 30, 2013. This represents an increase of $70,113,540, or 15.0%, from the average of interest bearing deposits of $467,043,764 for the six-month period ended June 30, 2012. This was due, in large part, to an increase in interest-bearing NOW and money market accounts partially offset by a decrease in certificates of deposit.

Other borrowed funds averaged $141,771,476 for the six months ended June 30, 2013. This represents a decrease of $27,069,357, or 16.0%, over the other borrowed funds of $168,840,833 for the six-month period ended June 30, 2012. This decrease in other borrowed funds was due to a $15,265,349 decrease in the securities sold under agreement to repurchase, a $48,798 decrease in the Agribusiness Enterprise Loan Liability, a $2,923,597 decrease in Federal Funds Purchased and a decrease in the FHLB advances of $8,831,613 for the six-month period ended June 30, 2013, when compared to the six-month period ended June 30, 2012.

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Net interest income was $6,805,837 for the three-month period ended June 30, 2013, a decrease of $740,077 from $7,545,915 for the three-month period ended June 30, 2012, primarily due to a decrease in rate. The changes in volume in earning assets and in deposits and in borrowed funds are discussed above. As to changes in rate in the three-month period ended June 30, 2013, the yield on earning assets decreased more than the rates paid on deposits and borrowed funds decreased from the same period in 2012. The yield on all interest bearing assets decreased 87 basis points to 4.06% in the second quarter of 2013 from 4.93% for the same period in 2012. At the same time, the rate paid on all interest bearing liabilities for the second quarter of 2013 decreased by 22 basis points to 0.70% from 0.92% in the same period of 2012. 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.

Net interest income was $13,561,258 for the six months ended June 30, 2013, a decrease of $1,373,057 from the $14,934,316 for the six months ended June 30, 2012, primarily due to changes in both rate and volume. The changes in volume in earning assets and in deposits and in borrowed funds are discussed above. As to changes in rate in the six-month period ended June 30, 2013, the yield on earning assets decreased more than the rates paid on deposits and borrowed funds as compared to the changes in rates and yields in the same period of 2012. The yield on all interest bearing assets decreased 82 basis points to 4.10% in the first six months of 2013 from 4.92% for the same period in 2012. At the same time, the rate paid on all interest bearing liabilities for the first six months of 2013 decreased 22 basis points to 0.71% from 0.93% in the same period in 2012. 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.

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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,	
	2013	2012	2013	2012
Interest and Fees	$ 5,120,642	$ 6,038,190	$ 10,319,823	$ 12,010,427
Average Loans	365,045,290	386,667,016	367,932,362	387,733,738
Annualized Yield	5.61%	6.25%	5.61%	6.20%

The decrease in interest rates in the three-month period ended June 30, 2013, 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.

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.

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

	Quarter Ended June 30, 2013	Year Ended December 31, 2012	Amount of Increase (Decrease)	Percent of Increase (Decrease)
BALANCES:				
Gross Loans	$ 363,468,787	$ 369,138,109	$ (5,669,322)	-1.54%
Allowance for Loan Losses	6,803,043	6,954,269	(151,226)	-2.17%
Nonaccrual Loans	13,691,330	14,141,887	(450,557)	-3.19%
Ratios:				
Allowance for loan losses to gross loans	1.87%	1.88%		
Net loans charged off to allowance for loan losses	13.23%	18.30%		

The provision for loan losses for the three months ended June 30, 2013, was $574,595, an increase of $244,498 from the $330,097 provision for the same period in 2012. The provision for loan losses was $749,104 for the six-month period ended June 30, 2013, compared to a provision of $865,777 for the six months ended June 30, 2012. The change in our loan loss provisions for the three- and six-month periods is a result of a decrease in loan losses recorded for the respective periods and management s assessment of inherent loss in the loan portfolio, including the impact caused by current local, national and global economic conditions. The Corporation s model used to calculate the provision is based on the percentage of historical charge-offs applied to the current loan balances by loan segment and specific reserves applied to certain impaired loans. Nonaccrual loans decreased during this period due to payments received in excess of the amount of new loans being added to the list.

For the three months ended June 30, 2013, net loan losses charged to the allowance for loan losses totaled $606,127, an increase of $414,797 from the $191,330 charged off in the same period in 2012. For the six months ended June 30, 2013, net loan losses charged to the allowance for loan losses totaled $900,330, an increase of $563,858 from the $336,472 charged off in the same period in 2012. This increase was due to an overall increase in the number of charge offs in 2013 when compared to the same period in 2012 and not the result of any one loan segment.

Management reviews quarterly with the 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 first six months of 2013 that have not been charged off. Management also believes that the Corporation s allowance will be adequate to absorb probable losses inherent in the Corporation s loan portfolio. However, in light of overall economic conditions in the Corporation s geographic area, the nation and internationally, as a whole, it is possible that additional provisions for loan loss may be required.

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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, 2013, was $1,928,870, an increase of $291,715, or 17.8%, from the same period in 2012. Service charges on deposit accounts increased by $16,023, or 1.8%, to $913,942 in the three months ended June 30, 2013, compared to $897,920 for the same period in 2012. Other service charges and fees increased by $36,113, or 8.3%, in the three months ended June 30, 2013, compared to the same period in 2012. The increase in fee income was the result of an increase in demand for these services and not a direct result of fee changes.

Other income for the six months ended June 30, 2012, was $3,609,861, an increase of $363,107, or 11.2%, from the same period in 2012. Service charges on deposit accounts increased by $59,230, or 3.4%, to $1,804,799 in the six months ended June 30, 2013, compared to $1,745,570 for the same period in 2012. Other service charges and fees increased by $60,444, or 7.0%, in the six months ended June 30, 2013, compared to the same period in 2012. The increase in fee income was the result of an increase in the demand for these services and a small increase in certain fees.

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

	Three months ended June 30,		Six months ended June30,	
Other Income	2013	2012	2013	2012
BOLI Insurance	$ 120,000	$ 120,000	$ 240,000	$ 240,000
Mortgage Loan Origination Income	110,593	100,783	230,837	217,012
Income from Security Sales, net	154,655	9,061	154,655	37,753
Other Income	156,094	71,919	253,057	140,351
Total Other Income	$ 541,342	$ 301,763	$ 878,549	$ 635,116

OTHER EXPENSES

Other expenses include salaries and employee benefits, occupancy and equipment, and other operating expenses. Aggregate non-interest expenses for the three-month period ended June 30, 2013 and 2012 were $6,147,031 and $6,674,001, respectively, a decrease of $526,970, or 7.9%, from 2012 to 2013. Salaries and benefits decreased to $3,336,317 for the three months ended June 30, 2013, from $3,473,956 for the same period in 2012. This represents a decrease of $137,639, or 4.0%. This decrease was the result of decreases in the cost of employee benefits paid by the Corporation and a reduction in the number of employees. Occupancy expense increased by $13,339, or 1.2%, to $1,111,195 for the three months ended June 30, 2013, when compared to the same period of 2012. This increase is due in part to an increase in office and equipment rental, property taxes and service costs. Other operating expenses decreased by $402,670 from 2013 to 2012. This decrease is due mainly to lower regulatory and related costs. A detail of the major expense classifications is set forth below.

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Total non-interest expenses for the six-month period ended June 30, 2013 and 2012 were $12,704,195 and $13,084,268, respectively, a decrease of $380,073, or 2.9%, from 2012 to 2013. Salaries and benefits decreased to $6,642,487 for the six months ended June 30, 2013, from $7,033,660 for the same period in 2012. This represents a decrease of $391,173, or 5.6%. This decrease was the result of a reduction in the number of employees and a reduction in employee benefits. Occupancy expense increased $94,541, or 4.4%, to $2,223,706 in the six months ended June 30, 2013 when compared to the same period in 2012. This increase is due in part to an increase in office and equipment rental, property taxes and service costs. Other operating expenses decreased by $83,441 from 2012 to 2013. This decrease is due mainly to lower regulatory and related 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	2013	2012	2013	2012
Intangible Amortization	$	$ 30,782	$	$ 76,955
Advertising	151,188	171,044	297,356	333,654
Office Supplies	99,891	94,650	234,362	208,708
Legal and Audit Fees	104,885	121,954	204,135	226,779
Telephone expense	129,755	92,626	240,522	211,666
Postage and Freight	104,508	93,350	222,151	230,033
Loan Collection Expense	89,621	126,323	310,232	229,498
Other Losses	24,486	16,675	178,518	29,398
Regulatory and related expense	10,703	316,966	342,098	628,416
Debit Card/ATM expense	184,107	205,522	353,658	397,584
Travel and Convention	69,212	52,648	114,607	105,211
Other expenses	731,163	779,649	1,340,363	1,243,541
Total Other Expense	$ 1,699,519	$ 2,102,189	$ 3,838,002	$ 3,921,443

The Corporation s efficiency ratio for the three months ended June 30, 2013, was 68.02% compared to the 69.54% for the same period in 2012. For the six months ended June 30, 2013 and 2012, the Corporation s efficiency ratio was 71.43% and 69.54%, 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.

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BALANCE SHEET ANALYSIS

	June 30, 2013	December 31, 2012	Amount of Increase (Decrease)	Percent of Increase (Decrease)
Cash and Due From Banks	$ 19,572,317	$ 21,561,288	$ (1,988,971)	-9.22%
Interest Bearing deposits with Other Banks	3,538,237	16,228,747	(12,690,510)	-78.20%
Investment Securities	418,552,716	420,907,815	(2,355,099)	-0.56%
Loans, net	356,224,900	361,936,495	(5,711,595)	-1.58%
Total Assets	866,662,471	880,839,898	(14,177,427)	-1.61%
Total Deposits	653,155,232	642,549,338	10,605,894	1.65%
Total Stockholders Equity	73,450,710	88,868,830	(15,418,120)	-17.35%

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, 2013 was $19,572,317, a decrease of $1,988,971 from the balance of $21,561,288 at December 31, 2012, due to a decrease in the balances at correspondent banks due to an increase in the amount of the month ending cash letter.

PREMISES AND EQUIPMENT

During the period ended June 30, 2013, premises and equipment decreased by $459,311, or 2.4%, to $18,965,981 when compared to $19,425,292 at December 31, 2012. The decrease was due to the amount of depreciation exceeding the addition of property and equipment in the normal course of business.

INVESTMENT SECURITIES

The investment securities portfolio primarily consists of United States agency debentures, mortgage-backed securities and obligations of states, counties and municipal. Investments at June 30, 2013, decreased $2,355,099, or 0.6%, to $418,552,716 from $420,907,815 at December 31, 2012. This decrease is due to changes in the market value of the securities portfolio offset by purchases of investment securities.

LOANS

The loan balance decreased by $5,711,595 during the six months ended June 30, 2013, to $356,224,900 from $361,936,495 at December 31, 2012. Loan demand, especially in business loan and consumer loan categories, remained weak and competition for available loans was great during the first six months of 2013. No material changes were made to the loan products offered by the Corporation during this period.

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DEPOSITS

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

	June 30, 2013	December 31, 2012	Amount of Increase (Decrease)	Percent of Increase (Decrease)
Noninterest-Bearing Deposits	$ 120,057,734	$ 119,946,574	$ 111,160	0.09%
Interest-Bearing Deposits	243,924,050	228,111,275	15,812,775	6.93%
Savings Deposits	51,054,475	46,240,652	4,813,823	10.41%
Certificates of Deposit	238,118,973	248,250,837	(10,131,864)	-4.08%
Total Deposits	$ 653,155,232	$ 642,549,338	$ 10,605,894	1.65%

Interest-bearing deposits, noninterest-bearing deposits and savings increased while certificates of deposit decreased during the six months ended June 30, 2013. 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 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, 2012.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

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

The Corporation s strategies and its management s ability to react to changing competitive and economic environments have historically enabled the Corporation to compete effectively and manage risks to acceptable levels. The Corporation has outlined potential risk factors below that it presently believe could be important; however, other risks may prove to be important in the future. New risks may emerge at any time and the Corporation cannot predict with certainty all potential developments that could affect the Corporation s financial performance. The following discussion highlights potential risks, which could intensify over time or shift dynamically in a way that might change the Corporation s risk profile.

Competition Risks

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

Credit Risks

Like all lenders, the Corporation faces the risk that the Corporation s customers may not repay their loans and that the realizable value of collateral may be insufficient to avoid a loss of principal. In the Corporation s business, some level of credit loss is unavoidable and overall levels of credit loss can vary over time. The Corporation s ability to manage credit risks depends primarily upon the Corporation s ability to assess the creditworthiness of customers and the value of collateral, including real estate. The Corporation controls credit risk by diversifying the Corporation s loan portfolio and managing its composition, and by recording and managing an allowance for expected loan losses in accordance with applicable accounting rules. At the end of June 30, 2013, the Corporation had approximately $6.8 million of available reserves to cover such losses. The models and approaches the Corporation uses to originate and manage loans are regularly updated to take into account changes in the competitive environment, in real estate prices and other collateral values, and in the economy, among other things based on the Corporation s experience originating loans and servicing loan portfolios.

Financing, Funding and Liquidity Risks

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

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

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Interest Rate and Yield Curve Risks

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

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

Regulatory and Legal Risks

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

The Corporation also faces litigation risks from customers (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 certainty.

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Accounting Estimate Risks

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

Expense Control

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

ITEM 4. CONTROLS AND PROCEDURES.

The management of the Corporation, with the participation of our principal executive 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, 2013 (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, 2013, that have materially affected, or are reasonably likely to materially affect, the Corporation s internal control over financial reporting.

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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, 2012, to include the following:

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

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

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 will become 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.

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 and/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 and/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.

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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, 2013, filed with the SEC on August 8, 2013, formatted in Extensible Business Reporting Language (XBRL): (i) the Consolidated Statements of Condition as of June 30, 2013 (Unaudited) and December 31, 2012; (ii) the Consolidated Statements of Income for the three and six months ended June 30, 2013 (Unaudited) and 2012 (Unaudited); (iii) the Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2013 (Unaudited) and 2012 (Unaudited); (iv) the Consolidated Statements of Cash Flows for the six months ended June 30, 2013 (Unaudited) and 2012 (Unaudited); and (v) Notes to Consolidated Financial Statements, tagged as blocks of text (Unaudited).*

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

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SIGNATURES

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

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, 2013

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EXHIBIT INDEX

Exhibit Number	Description of Exhibit
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