

March 5, 2009

Via Email and First Class Mail

Neil M. Barofsky

Special Inspector General -- TARP

United States Department of the Treasury

1500 Pennsylvania Avenue, N. W., Suite 1064

Washington, D.C. 20220

Citizens Community Bank/

TARP Capital Purchase Program – UST Sequence Number: 164

Dear Mr. Barofsky,

Per your letter dated February 6, 2009, Citizens Community Bank (the “Bank”) is providing the following information in response to the audit into Troubled Asset Relief Program (“TARP”) recipients that received funds under the Emergency Economic Stabilization Act of 2008.

Use of Proceeds

Prior to Citizens Community Bank accepting funds under TARP, the Bank thoroughly considered whether to participate in the program as our community bank held capital in excess of the “well capitalized” requirement under applicable federal banking law and did not participate in the toxic mortgage lending and other transactions that were engaged in by national financial institutions which led to our country’s economic instability. After consulting with bank regulators, investment bankers and legal counsel, and considering the fact that the program was for healthy financial institutions, our Board of Directors

decided to participate in the TARP. Although a challenging decision, given the unprecedented economic times, uncertainty surrounding capital markets and our need for continued growth and a greater capital cushion, our Board believed additional capital was warranted.

Accordingly, on December 23, 2008, Citizens Community Bank accepted \$3.0 million of TARP funds from the U.S. Treasury ("Treasury") in exchange for the issuance of the Bank's Series A preferred stock along with issuing a warrant with respect to the Bank's Series B preferred stock that had a total exercise price of \$150,000 (and was immediately exercised by the Treasury). The anticipated use of the funds was to further strengthen our community bank in efforts to withstand not only the worst economic times since the Great Depression, but also to support our continued growth. With capital markets being seized up at the time of the transaction and significant uncertainty on when the capital markets would be properly functioning again, access to future capital was, and is, extremely important in continuing our growth. Citizens Community Bank had approximately \$150 million in total assets at the time of the transaction and as you may know, a certain level of scale must be generated for a financial institution to provide a meaningful return to its shareholders, customers and community.

In accepting the TARP funds, the Bank did not segregate such funds from our general operating funds, but developed a plan to prudently and efficiently deploy the proceeds. First and foremost, the Bank had to leverage the capital in a manner that would not only recoup the cost of the capital, but also allow for prudent growth and financial strength. This was accomplished by investing a portion of the proceeds into securities instruments such as mortgage-backed securities and investment grade corporate bonds. Given that it would not be prudent to immediately lend a significant amount of the TARP funds, this strategy would allow for the maturing cash flow over time to be distributed to the communities we serve through our lending operations, not to mention providing additional liquidity to the capital markets and our organization.

In regards to our lending, Citizens Community Bank fully intends to continue lending in its markets as exhibited by our loan growth since acceptance of the TARP funds. From December 23, 2008 to February 28, 2009, our community bank in rural Virginia has originated nearly \$5.7 million in loans and lines of credit, almost twice as much as received in preferred stock proceeds and has experienced \$2.4 million in outstanding net loan growth. Without the additional TARP capital, or knowing whether additional capital would be available due to the meltdown in the capital markets, our bank's growth could not continue as planned. Knowing that these uncertainties were eliminated or the associated risks were reduced with the intake of TARP funding, we are able to continue supporting our communities during this difficult economic period. Citizens Community Bank plans to continue leveraging its capital, primarily in the form of lending, in efforts to achieve the necessary scale required for its success, unless economic conditions deteriorate to a point that further lending would jeopardize the Bank or other factors lead to a prudent and significant reduction in lending. Attached is certain supporting documentation describing our use of the TARP funds: a press release dated March 5, 2009 and an unaudited balance sheet at December 23, 2008 compared to February 28, 2009.

The unleveraged portion of the capital proceeds, allows for our financial institution to maintain capital ratios well in excess of Prompt Correction Action guidelines, but allows for our bank's capital position to exceed that our peer group. As of the Bank's December 31, 2008 Uniform Bank Performance Report, Citizens Community Bank ranked in the highest quartiles among its peer group in terms of its risk-based capital ratios.

Executive Compensation

The Bank has reviewed the policies and incentive compensation programs for its senior executive officers, as required for TARP participants, and the current guidance from the Treasury. Please be advised as follows:

- As the Bank received \$3.0 million in TARP funds, the ban on any bonus, retention or incentive compensation as a result of the enactment of the American Recovery and Reinvestment Act of 2009 ("ARRA") only applies to its chief executive officer ("CEO").

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The Bank is awaiting further guidance from the Treasury regarding bonuses paid prior to the enactment of ARRA.

- Each of the five senior executive officers of the Bank has agreed to the guidelines issued by the Treasury in connection with the TARP.
- The Senior Risk Officer and the Compensation Committee are in the process of defining a Risk Assessment Checklist to be utilized on an ongoing basis whenever incentive compensation for senior executive officers is contemplated.
- There are no plans at this time to offset such limitations by offering longer-term or deferred forms of executive compensation.

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I, Tom Manson, hereby certify that I have reviewed this response and supporting documents, and, to the best of my knowledge, this response and supporting documents do not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading.

Sincerely,



Thomas C. Manson, President & CEO

Cc:S.Richter, J.Black.



FOR IMMEDIATE RELEASE
March 5, 2009

Contact: Thomas C. Manson
President and CEO
(434) 447-2265

CITIZENS COMMUNITY BANK EFFECTIVELY DEPLOYS \$3 MILLION IN "TARP" FUNDS

--New loans and secondary mortgage lending are top priority--

(South Hill, Va.) -- Since taking delivery of \$3 million as part of the Troubled Asset Relief Program (TARP) on December 23, 2008, Citizens Community Bank has experienced robust loan growth. Nearly \$5.7 million in new loans have been originated since the TARP funds were received.

"The South Hill market has been particularly responsive," commented Vin Montgomery, senior lender and executive vice president. "We have experienced strong demand across the board for all types of lending other than acquisition and development loan interest," stressed Montgomery. The South Hill office is responsible for \$4.7 million of the new loan originations.

The Bank also is investing marketing and personnel dollars to strengthen secondary mortgage lending. On January 8, 2009, Citizens Community Bank secured approval from the US Department of Housing and Urban Development to be an FHA loan originator. President and CEO Thomas C. Manson commented, "Since receiving our approval as an FHA originator, we have invested advertising and training dollars to educate our loan officers and branch managers, as well as local realtors and home builders, on the benefits derived from adding the ability to originate FHA loans as an additional product in our tool box. It is the desire of the Board of Directors for Citizens Community Bank to be a local leader in helping get the housing market in our area moving again." While initial lending efforts have been positive, Manson indicated that there are additional loans in the program's pipeline with closing dates pending.

Each of these initiatives is important both to the success of the Bank and the integrity of TARP. One of the primary goals of TARP is to encourage banks to resume lending at levels seen prior to the financial system crisis, and Citizens Community Bank is a fine example of the program's success.

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Citizens Community Bank Effectively Deploys \$3 Million in TARP Funds – page two

“We’ll continue to effectively leverage the TARP funding consistent with the initial concept of the Treasury department,” stated President Tom Manson. “The capital infusion bolsters our ability to lend within our communities and affect change within our markets and customer base.”

Citizens Community Bank is a Virginia state chartered bank headquartered in South Hill, Va. Opened in December 1999, it operates five branches, three in south central Virginia and two in northern North Carolina. For more information and additional financial data, please visit www.ccbsite.com.

This press release contains “forward-looking statements” that concern future events which are subject to risks and uncertainties. Any such statements are based on certain assumptions and analyses by the Bank and other factors it believes are appropriate in the circumstances. The Bank’s actual results, events and developments may differ materially from those contemplated by any forward-looking statement.

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CITIZENS COMMUNITY BANK
UNAUDITED BALANCE SHEET

	Unaudited February 28, 2009	Unaudited December 23, 2008	\$ Var	% Var
ASSETS:				
Cash and due from banks	\$ 3,290,098	\$ 2,678,149	\$ 611,949	22.8%
Federal funds sold	319,000	2,863,000	(2,544,000)	-88.9%
Interest bearing bank balances	2,048,478	2,085,604	(37,126)	-1.8%
Total cash and cash equivalents	<u>5,657,576</u>	<u>7,626,753</u>	<u>(1,969,177)</u>	<u>-25.8%</u>
Securities available for sale, at fair market value	26,869,263	14,098,804	12,770,459	90.6%
Restricted investments	1,212,188	951,188	261,000	27.4%
Loans:				
Loans, net of unearned income	127,946,338	125,552,045	2,394,293	1.9%
Less: allowance for loan losses	(1,567,993)	(1,499,747)	(68,246)	4.6%
Loans, net	<u>126,378,345</u>	<u>124,052,298</u>	<u>2,326,047</u>	<u>1.9%</u>
Land, premises and equipment, net	4,457,197	4,534,619	(77,422)	-1.7%
Other real estate owned	498,351	-	498,351	100.0%
Accrued interest receivable	962,804	808,515	154,289	19.1%
Bank owned life insurance	3,062,140	3,032,032	30,108	1.0%
Other assets	606,322	677,392	(71,070)	-10.5%
Total Assets	<u>\$ 169,704,186</u>	<u>\$ 155,781,601</u>	<u>\$ 13,922,585</u>	<u>8.9%</u>
LIABILITIES:				
Deposits:				
Noninterest-bearing deposits	\$ 13,671,704	\$ 14,462,587	\$ (790,883)	-5.5%
Interest bearing demand deposits	5,213,857	5,277,058	(63,201)	-1.2%
Savings	2,655,092	2,483,998	171,094	6.9%
Money markets	28,317,663	27,762,195	555,468	2.0%
Certificates of deposits	90,448,267	84,293,008	6,155,259	7.3%
Total deposits	<u>140,306,583</u>	<u>134,278,846</u>	<u>6,027,737</u>	<u>4.5%</u>
FHLB advances	8,000,000	-	8,000,000	100.0%
Accrued interest payable	39,179	235,069	(195,890)	-83.3%
Accrued expenses and other liabilities	168,508	136,135	32,373	23.8%
Total Liabilities	<u>148,514,270</u>	<u>134,650,050</u>	<u>13,864,220</u>	<u>10.3%</u>
SHAREHOLDERS' EQUITY:				
Preferred stock, Series A and Series B, \$5.00 par value; \$1,000 stated value, 1,000,000 shares authorized, 3,150 shares issued and outstanding	3,005,667	3,000,000	5,667	0.2%
Common stock, \$5.00 par value, authorized 5,000,000 shares; issued and outstanding 1,364,670 shares	6,778,920	6,756,705	22,215	0.3%
Surplus	8,589,901	8,576,350	13,551	0.2%
Retained earnings	2,575,501	2,713,617	(138,116)	-5.1%
Accumulated other comprehensive gain	239,927	84,879	155,048	182.7%
Total shareholders' equity	<u>21,189,916</u>	<u>21,131,551</u>	<u>58,365</u>	<u>0.3%</u>
Total Liabilities and Shareholders' Equity	<u>\$ 169,704,186</u>	<u>\$ 155,781,601</u>	<u>\$ 13,922,585</u>	<u>8.9%</u>

INTERNALLY PREPARED AND CONFIDENTIAL.