



March 6, 2009

Mr. Neil M. Barofsky
Special Inspector General – TARP
1500 Pennsylvania Avenue, NW
Suite 1064
Washington, D.C. 20220

Dear Mr. Barofsky:

Northway Financial, Inc. (“Northway”), the parent company of Northway Bank (“Bank”), applied for and received \$10 million in TARP capital on January 30, 2009. Despite the national credit crunch, the Bank had a record year of loan growth in 2008 in all types of lending. While commercial loan demand has dropped somewhat in 2009 due to the uncertainties of the economy, the Bank has continued to call on prospective customers, and has maintained ongoing contact with existing customers regarding their financing needs. In addition, the Bank has experienced a record demand for mortgage lending fueled by current very favorable mortgage rates. We anticipate that some of the larger regional banks that are headquartered outside of New Hampshire will reduce their lending initiatives in New Hampshire, and as a result, many borrowers will look toward the Bank to address their credit needs.

1. Anticipated use of TARP funds

Even though Northway and the Bank, collectively referred to as (the “Company”) were well capitalized prior to applying for the TARP capital, the Company’s capital levels would have limited its growth capabilities. The additional \$10 million in capital allows the Bank to expand its loan portfolio beyond what would have been possible with its existing capital. We believe that by making additional credit available as described above and elsewhere herein, we will have helped accomplish the Treasury’s goal of stimulating the economy.

2. Actual use of TARP funds

In anticipation of receiving the TARP capital, we continued our aggressive loan growth strategy and in January 2009 we booked loans totaling \$13.7 million. In February 2009 we closed \$11.8 million in residential mortgages, a record month for the Bank. In addition, we closed \$16.5 million in commercial and consumer loans. We expect that we will continue to expand our loan portfolio, thereby leveraging our enhanced capital consistent with the objectives of the TARP program.

(b) (4)

3. Segregation of TARP funds

The funds we received from the Treasury are earmarked as capital. We do not anticipate segregating the TARP funds from other institutional funds. We intend to fund the new loan growth through existing loan amortization and prepayment as well as growth in deposits and borrowings.

As part of our capital structure, the TARP funds helped support our loan growth for January and February, as discussed above.

4. Unspent TARP funds (i.e. “additional” capital)

To date Northway has not determined whether there will be any “unspent” funds (i.e. “additional capital”). This additional capital will be maintained on Northway’s books and will be down-streamed to the Bank as necessary or appropriate in order to continue to leverage the Bank’s growth by expanding its lending programs and otherwise.

5. Executive compensation requirements

We have taken the following action to address executive compensation requirements associated with the TARP funding:

- Prior to the recent amendments contained in the American Recovery and Reinvestment Act of 2009 (“ARRA”), we had amended the agreements with each of the top five executives to comply with the executive compensation provisions of the Emergency Economic Stabilization Act of 2008 (“EESA”), including the limitation on “golden parachute payments” and the bonus claw-back requirement.
- Each of the top five executives has executed the waiver of claims against Treasury and the Company with respect to compensation restrictions imposed under TARP required by Treasury as a condition to TARP funding.
- Our executive compensation arrangements are quite straightforward and consist primarily of base salary and retirement benefits. We do not have any incentive compensation arrangements that involve unnecessary and excessive risks as bonus payments, if any, are determined solely at the discretion of the Compensation Committee and tend to be quite modest in nature. (b) (4)

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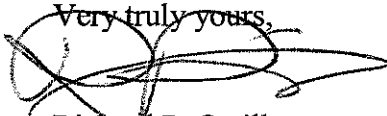
(b) (4)

- We do not own any private jets and do not provide any special perquisites to our executives. Our Chief Executive Officer is provided a leased vehicle (Toyota) for his use.
- We are reviewing the additional executive compensation restrictions imposed by ARRA. Once the Treasury provides additional guidance, we expect to ask the affected officers and employees to agree in writing to be bound by any additional restrictions.

Subject to the requirements and penalties set forth in Title 18, United States Code, Section 1001, I certify the accuracy of all statements and representations provided herein.

Should you require additional operational data in support of our response concerning use of TARP funds or other documents, please contact me at **(b) (6)** so that we may discuss the level of information which would be appropriate for your purposes.

Very truly yours,



Richard P. Orsillo

Senior Vice President and Chief Financial Officer