

GrandSouth BANK

February 18, 2009

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

In re: Request for information dated February 6, 2009

Dear Mr. Barofsky:

This letter is in response to your correspondence of February 6, 2009 requesting information regarding the use of Troubled Asset Relief Program (“TARP”) funds by GrandSouth Bancorporation (“GrandSouth”). GrandSouth received \$9,000,000.00 in proceeds from the sale of senior preferred stock to the U.S. Department of the Treasury on January 9, 2009. The requested information and response is as follows:

- (1) A narrative response specifically outlining
 - (a) your anticipated use of TARP funds;

RESPONSE: The proceeds of the sale of senior preferred stock to the U.S. Department of the Treasury (the TARP funds) were anticipated to be used to pay the expenses associated with the sale of the Senior Preferred Stock and warrants, which were estimated to be \$25,000 or less, with the remaining proceeds to be deposited into a non-interest bearing account with GrandSouth’s bank subsidiary (GrandSouth Bank or “Bank”), to be used for additional liquidity, and thereafter, the funds may be contributed to the bank subsidiary as capital or used for other corporate purposes; (see page 12, of the enclosed Proxy Statement For Special Meeting of Shareholders dated December 1, 2008)

- (b) whether the TARP funds were segregated from other institutional funds;

RESPONSE: The proceeds have been deposited into a non-interest bearing account in Bank;

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(c) your actual use of TARP funds to date;

RESPONSE: The funds have been used to augment the capital of GrandSouth to allow the company to continue to grow through the making of loans and holding customer deposits while maintaining capital levels within regulatory limits; the proceeds were deposited into a non-interest bearing account in Bank and the funds have been used by the Bank to increase its loan balances by approximately \$6 million as of this date;

(d) your expected use of unspent TARP funds;

RESPONSE: The remaining TARP funds will continue to be used to support the Bank's liquidity and support additional growth in loans; it is anticipated that some or all of the proceeds will ultimately be contributed to Bank as capital to meet regulatory capital guidelines and allow Bank to support future loan growth;

The annualized growth rate for the Bank's loan portfolio as of February 17, 2009 equals 15%. The availability of the capital provided by the TARP funds has allowed Bank to continue to make loans and grow the portfolio. If the Bank did not have access to this capital, loan growth would have been restricted to insure that the Bank's capital ratios were maintained within regulatory guidelines. The result would have been very little, if any growth and, if interest margins remain compressed, the balance sheet may have been managed in a manner to reduce total assets, including gross loan volumes.

- (2) Your specific plans, and the status of implementation of those plans, for addressing executive compensation requirements associated with the funding. Information provided regarding executive compensation should also include any assessments made of loan risks and their relationship to executive compensation; how limitations on executive compensation will be implemented in line with Department of Treasury guidelines; and whether any such limitations may be offset by other changes to other, longer-term or deferred forms of executive compensation.


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We have not completed the review required by 31 CFR 30.3. Otherwise, all compensation arrangements for the executive officers of GrandSouth are believed to be in compliance with Section 111 of the Emergency Economic Stabilization Act of 2008 ("EESA") but we are still evaluating the recent changes to EESA. To date no changes in existing compensation arrangements have been necessary to comply with EESA and any future modifications in compensation will comply with Section 111 of EESA.

The information provided herein is believed to be true and correct as of this date.

Sincerely,

A handwritten signature in cursive script, appearing to read "Ronald K. Earnest", with a long horizontal flourish extending to the right.

Ronald K. Earnest
President