



Questions and Answers:

Write-down of Citizens National Bank's Investment Securities

Q. Who determines how the bank can invest money?

Citizens National Bank (CNB), like many other financial institutions, has excess funds to invest. Management works within an "Investment Policy" that allows for the investment of excess funds in a conservative manner, while providing for a diverse portfolio of highly rated investments. The investment policy is approved by the board of directors and reviewed by our external auditors and federal regulators.

Q. If the bank's investments are conservative, what happened?

In 2006 and 2007 the bank purchased auction rate securities called Money Market Preferred (MMP) securities. These securities were presented as an option by the bank's investment advisor and were highly rated at purchase by the investment rating agencies. This was a new type of investment for the bank, but not a new type of investment vehicle.

Q. What are MMPs?

MMP securities are auction rate securities that are sold at short term intervals at a dutch auction—where the price starts out high and goes down until someone agrees to purchase the securities. Interest rates are reset on each auction date. The underlying security for the investment is "preferred" stock. In essence, an auction rate security is a long-term debt issue, but it acts as if it were a shorter term issue.

Q. Why are there losses?

The value of many investment securities has been adversely affected as a result of the unprecedented financial crisis of the past months. Many auction agents suspended making a market in auction rate securities and this led to failed auctions. When the value of investment securities are deemed to be "other than temporarily impaired" (OTTI), the impairment must be reflected on the balance sheet of the company, thus the losses flow through to the income statement.

OTTI is an accounting rule under U.S. Generally Accepted Accounting Principles used to determine the value of a security, based on quantitative and qualitative analysis of the performance of the collateral supporting the security. Then an evaluation of the credit enhancement structure and determination of whether or not a principal loss is probable at any time during the life of the security are made. If a probable loss is determined, the security must be marked-to-market, even if the intent is to hold the security to maturity. OTTI losses, based on fair market values, must be recorded immediately.

Q. Are there other investments that will be affected by OTTI?

Each security is evaluated for OTTI and only those securities determined to be impaired will be marked-to-market. We believe the MMP securities are the only investments requiring the adjustment at this time.

Q. Does the bank plan to sell the investments? If not, why?

The bank does not plan to sell the investments at this time. The loss at this point is considered a non-cash loss, since we have not sold the security. When the market returns to a reasonable level, the bank will then determine when the investment is to be sold. The gain, if any, on the sale will be recorded as income.

Q. What effect will this have on CNB?

In spite of this write down CNB's strong capital position remains intact and this write down does not have an effect on the strength of the bank. The bank continues to provide a strong base of core earnings and anticipates income for 2009 will return to a positive position. However, CNB Corporation shareholders are affected because this write down adversely affected dividends for 2008.

Q. Can you provide a breakdown of how you arrived at core earnings?

Net Income (Deficit) for 2008 was	(\$5.2 million)
Add Back:	
Securities Write Downs	7.1 million
Loan Loss Provision	1.8 million
Expenses related to Bank ORE (Other Real Estate)	.6 million (includes legal fees, home maintenance, taxes and insurance)
Deduct:	
Income Tax benefit of expenses	<u>(1.5 million)</u>
Net Income from core earnings	<u>\$2.8 million</u>

Q. What are CNB's Capital Ratios compared to regulatory minimums?

	<u>CNB as of 12/31/2008</u>	<u>Regulatory Minimum</u>
Tier 1 Capital	11.03%	6.00%
Leverage Ratio	7.26%	5.00%
Total Risk Based Capital	12.20%	10.00%

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