UNITED BANCORPORATION OF ALABAMA INC
Form 10-Q
August 15, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2005
Commission file number 2-78572

UNITED BANCORPORATION OF ALABAMA, INC.
(Exact name of registrant as specified in its charter)

Delaware	63-0833573
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

200 East Nashville Avenue, Atmore, Alabama	36502
(Address of principal executive offices)	(Zip Code)

(251) 368-2525
(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 report(s), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes o No þ

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of July 20, 2005.

Class A Common Stock.... 2,221,440 Shares
Class B Common Stock.... -0- Shares

UNITED BANCORPORATION OF ALABAMA, INC.
FORM 10-Q
For the Quarter Ended June 30, 2005
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PART 1 FINANCIAL INFORMATION

Item 1. Financial Statements

United Bancorporation of Alabama, Inc.
and Subsidiary
Condensed Consolidated
Balance Sheets

	2005 Unaudited	2004 Audited
Assets:		
Cash and due from banks	$ 11,592,561	$ 16,446,574
Federal funds sold	7,897,849	27,494,426
Cash and cash equivalents	19,490,410	43,941,000
Securities available for sale (amortized cost of $73,289,134 and $54,502,411 respectively)	73,492,421	55,004,982
Loans	216,558,575	199,160,445
Allowance for loan losses	2,630,861	2,562,239
Net loans	213,927,714	196,598,206
Premises and equipment, net	7,068,216	7,192,202
Interest receivable and other assets	9,939,878	9,094,834
Total assets	$323,918,639	$311,831,224
Liabilities and Stockholders Equity:		
Deposits:		
Non-interest bearing	$ 59,325,961	$ 68,763,895
Interest bearing	191,127,619	184,174,772
Total deposits	250,453,580	252,938,667
Securities sold under agreements to repurchase	30,027,976	18,381,063
Other borrowed funds	9,963,544	8,292,612
Accrued expenses and other liabilities	2,311,974	1,881,143
Note payable to Trust	3,997,697	3,992,645
Total liabilities	296,754,771	285,486,130
Stockholders equity:		
Class A common stock, Authorized 5,000,000 shares of $.01 par value; 2,366,962 and 2,363,762 shares issued respectively	23,654	23,638
	0	0

Class B common stock of $.01 par value, Authorized 250,000 shares; -0- shares issued and outstanding		
Preferred stock of $.01 par value, Authorized 250,000 shares; -0- shares issued and outstanding	0	0
Additional Paid in Capital	5,435,679	5,444,563
Accumulated other comprehensive income, net of tax	121,972	301,542
Retained earnings	22,399,878	21,414,370
	27,981,183	27,184,113
Less: 145,522 and 148,966 treasury shares, at cost, respectively	817,315	839,019
Total stockholders equity	27,163,868	26,345,094
Total liabilities and stockholders equity	$323,918,639	$311,831,224

See Notes to Condensed Consolidated Financial Statements

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United Bancorporation of Alabama, Inc.
And Subsidiary
Condensed Consolidated Statements of Earnings and Comprehensive Income
(Unaudited)

	Three Months Ended June		Six Months Ended June	
	2005	2004	2005	2004
Interest income:				
Interest and fees on loans	$3,802,191	$ 2,902,448	$7,095,542	$5,590,990
Interest on investment securities available for sale:				
Taxable	480,117	299,800	862,789	602,868
Nontaxable	261,383	256,223	508,193	507,450
Total investment income	741,500	556,023	1,370,982	1,110,318
Other interest income	61,133	23,647	219,788	50,773
Total interest income	4,604,824	3,482,118	8,686,312	6,752,081
Interest expense:				
Interest on deposits	1,056,175	726,897	1,969,601	1,380,538
Interest on other borrowed funds	158,051	138,277	298,963	283,038
Total interest expense	1,214,226	865,174	2,268,564	1,663,576
Net interest income	3,390,598	2,616,944	6,417,748	5,088,505
Provision for loan losses	195,000	180,000	390,000	360,000
Net interest income after provision for loan losses	3,195,598	2,436,944	6,027,748	4,728,505
Noninterest income:				
Service charge on deposits	592,719	586,878	1,100,687	1,175,120
Commission on credit life	22,795	22,003	28,946	35,700
Investment securities gains, net		20		3,288
Other	179,782	139,142	366,980	330,645
Total noninterest income	795,296	748,043	1,496,613	1,544,753
Noninterest expense:				
Salaries and benefits	1,636,155	1,419,620	3,166,730	2,781,416
Net occupancy expense	489,717	457,020	983,093	915,418
Other	939,554	741,902	1,603,728	1,371,677

Total non-interest expense	3,065,426	2,618,542	5,753,551	5,068,511
Earnings before income tax expense	925,468	566,445	1,770,810	1,204,746
Income tax expense	295,349	79,122	488,427	256,410
Net earnings	$ 630,119	$ 487,323	$1,282,383	$ 948,336
Basic earnings per share	$ 0.28	$ 0.22	$ 0.58	$ 0.43
Diluted earnings per share	$ 0.28	$ 0.22	$ 0.58	$ 0.43
Basic weighted average shares outstanding	2,219,858	2,214,779	2,219,849	2,214,719
Diluted weighted average shares outstanding	2,220,527	2,217,128	2,220,518	2,217,068
Cash dividend per share	$ 0.15	$ 0.15	$ 0.15	$ 0.15
Statement of Comprehensive Income				
Net Income	630,119	487,323	$1,282,383	$ 948,336
Other Comprehensive (Loss) Income, net of tax:				
Unrealized holding gain (loss) arising during the period	326,920	(1,129,997)	179,570	(700,988)
Less: Reclassification adjustment for gains included in net income		12		1,961
Comprehensive (loss) income	$ 957,039	$ (642,686)	$1,461,953	$ 245,387

See Notes to Condensed Consolidated Financial Statements

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United Bancorporation of Alabama, Inc.
and Subsidiary
Condensed Consolidated Statements of Cash Flows
For The Six Months Ended June 2005 and 2004
(Unaudited)

	2005	2004
Operating Activities		
Net Income	$ 1,282,383	948,336
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities		
Provision for Loan Losses	390,000	360,000
Depreciation on Premises and Equipment	464,410	411,491
Amortizaton of Investment Securities Available for Sale	99,625	94,777
Gain on Investment Securities Available for Sale		(3,288)
Gain on Sale of Other Real Estate	(4,118)	
Gain on Disposal of Premises and Equipment		(4,850)
Writedown of Other Real Estate	103,201	
Increase in Interest Receivable and Other Assets	(944,603)	(4,880)
Increase (Decrease) in Accrued Expenses and Other Liabilities	430,831	(564,190)
Net Cash Provided by Operating Activities	1,821,729	1,237,396
Investing Activities		
Proceeds From Sales of Investment Securities Available for Sale		1,500,300
Proceeds From Maturities of Investment Securities Available for Sale	8,317,094	4,843,440
Purchases of Investment Securities Available for Sale	(27,203,399)	(11,788,315)
Net Increase in Loans	(17,769,508)	(24,329,385)
Purchases of Premises and Equipment	(340,424)	(319,521)
Proceeds From Sales of Premises and Equipment		21,104
Proceeds From Sales of Other Real Estate	170,147	
Net Cash Used in Investing Activities	(36,826,090)	(30,072,377)
Financing Activities		
Net (Decrease) Increase in Deposits	(2,485,087)	22,596,434
Net Increase in securities sold under agreement to repurchase	11,646,913	2,659,983
Cash Dividends	(288,579)	(332,215)
Net Tranactions on Treasury Stock		(2,387)
Proceeds from sale of common stock	4,540	39,581
(Increase) Decrease in Other Borrowed Funds	1,675,984	(666,848)
Net Cash Provided by Financing Activities	10,553,771	24,294,548
Decrease in Cash and Cash Equivalents	(24,450,590)	(4,540,433)
Cash and Cash Equivalents at Beginning of Period	43,941,000	24,447,625
Cash and Cash Equivalents at End of Period	$ 19,490,410	19,907,192

Supplemental disclosures

Cash paid during the year for:				
Interest	$	2,208,837	$	1,672,764
Income Taxes	$	503,000	$	230,000
Noncash transactions				
Transfer of loans to other real estate through foreclosure	$	50,000	$	230,001

See Notes to Condensed Consolidated Financial Statements

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UNITED BANCORPORATION OF ALABAMA, INC.
AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements

NOTE 1 General

This report includes interim consolidated financial statements of United Bancorporation of Alabama, Inc. (the Corporation or the Company) and its wholly-owned subsidiary, United Bank (the Bank). The interim consolidated financial statements in this report have not been audited. In the opinion of management, all adjustments necessary to present fairly the financial position and the results of operations for the interim periods have been made. All such adjustments are of a normal recurring nature. The results of operations are not necessarily indicative of the results of operations for the full year or any other interim periods. For further information, refer to the consolidated financial statements and footnotes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

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NOTE 2 Net Earnings per Share

Basic net earnings per share were computed by dividing net earnings by the weighted average number of shares of common stock outstanding during the three and six month periods ended June 30, 2005 and 2004. Common stock outstanding consists of issued shares less treasury stock. Diluted net earnings per share for the three and six month periods ended June 30, 2005 and 2004 were computed by dividing net earnings by the weighted average number of shares of common stock and the dilutive effects of the shares subject to options awarded under the Company s Stock Option Plan, based on the treasury stock method using an average fair market value of the stock during the respective periods. Presented below is a summary of the components used to calculate diluted earnings per share for the three and six months ended June 30, 2005 and 2004:

	Three Months Ended June		Six Months Ended June	
	2005	2004	2005	2004
Diluted earnings per share	$ 0.28	$ 0.22	$ 0.58	$ 0.43
Weighted average common shares outstanding	2,219,858	2,214,779	2,219,849	2,214,719
Effect of the assumed exercise of stock options based on the treasury stock method using average market price	669	2,349	669	2,349
Total weighted average common shares and potential common stock outstanding*	2,220,527	2,217,128	2,220,518	2,217,068

* 33,584 and 23,888 shares subject to outstanding options for the three and six months ended June 30, 2005 and 2004, respectively, were not included in the calculation of diluted earnings per share, as the exercise price of these options was in excess of average market price.

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NOTE 3 Allowance for Loan Losses

The following table summarizes the activity in the allowance for loan losses for the six month periods ended June 30 ($ in thousands):

	June 30	
	2005	2004
Balance at beginning of year	2,562	2,117
Provision charged to expense	390	360
Less Loans charged off	352	188
Recoveries	31	49
Balance at end of period	2,631	2,338

At June 30, 2005 and 2004, the amount of nonaccrual loans was $963,741 and $1,331,976 respectively.

NOTE 4 Operating Segments

Statement of Financial Accounting Standard 131 (SFAS 131), *Disclosures about Segments of an Enterprise and Related Information,* establishes standards for the disclosure made by public business enterprises to report information about operating segments in annual financial statements and requires those enterprises to report selected information about operating segments in interim financial reports issued to shareholders. It also establishes standards for related disclosures about products and services, geographic areas, and major customers. The Corporation operates in only one segment commercial banking.

NOTE 5 New Accounting Standards

In December 2003, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 46 (revised December 2003) (FIN 46R), *Consolidation of Variable Interest Entities*, which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. FIN 46R replaces No. 46, *Consolidation of Variable Interest Entities*, which was issued in January 2003. The Company will be required to apply FIN 46R to all entities subject to this interpretation no later than the end of the first reporting period that ends after December 15, 2004. This interpretation must be applied to those entities that are considered to be special purpose entities.

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For any variable interest entities (VIEs) that must be consolidated under FIN No. 46R that were created before January 1, 2004, the assets, liabilities, and noncontrolling interests of the VIE initially would be measured at their carrying amounts with any difference between the net amount added to the balance sheet and any previously recognized interest being recognized as the cumulative effect of an accounting change. If determining the carrying amounts is not practicable, fair value at the date FIN No. 46R first applies may be used to measure the assets, liabilities and noncontrolling interest of the VIE.

The Company has applied FIN No. 46R in accounting for United Bancorp Capital Trust I (Trust), established on June 27, 2002. Accordingly, the accompanying balance sheet includes, in other assets, the Company s investment in the Trust of $124,000 and also includes, in Note payable to Trust, the balance owed the Trust of $4,124,000. Except as related to the Trust, the application of this interpretation is not expected to have a material effect on the Company s consolidated financial statements.

In December 2004, the Financial Accounting Standards Board (FASB) published FASB Statement No. 123 (revised 2004), *Share-Based Payment* (FAS 123(R) or the Statement). FAS 123(R) requires that the compensation cost relating to share-based payment transactions, including grants of employee stock options, be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued. FAS 123(R) covers a wide range of share-based compensation arrangements including stock options, restricted share plans, performance-based awards, share appreciation rights, and employee share purchase plans. FAS 123(R) is a replacement of FASB Statement No. 123, *Accounting for Stock-Based Compensation*, and supersedes APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and its related interpretive guidance.

The effect of the Statement will be to require entities to measure the cost of employee services received in exchange for stock options based on the grant-date fair value of the award, and to recognize the cost over the period the employee is required to provide services for the award. FAS 123(R) permits entities to use any option-pricing model that meets the fair value objective in the Statement.

The Company will be required to apply FAS 123(R) as of the beginning of its first interim period that begins after December 15, 2005, which will be the quarter ending March 31, 2006.

FAS 123(R) allows two methods for determining the effects of the transition: the modified prospective transition method and the modified retrospective method of transition. Under the modified prospective transition method, an entity would use the fair value based accounting method for all employee awards granted, modified, or settled after the effective date. As of the effective date, compensation cost related to the nonvested portion of awards outstanding as of that date would be based on the grant-date fair value of those awards as calculated under the original provisions of Statement No. 123; that is, an entity would not remeasure the grant-date fair value estimate of the unvested portion of awards granted prior to the effective date of FAS 123(R). Under the modified retrospective method of transition, an entity would revise its previously issued financial statements to recognize employee compensation cost for prior periods presented in accordance with the original provisions of Statement No. 123.

Although it has not yet completed its study of the transition methods, the Company believes it will elect the modified prospective transition method. The impact of this Statement on the Company in fiscal 2006 and beyond will depend upon various factors, among them being the Company s future compensation strategy. The pro forma compensation costs presented in the table below and in prior filings for the Company have been calculated using a Black-Scholes option pricing model and may not be indicative of amounts which should be expected in future years. No decisions have been made as to which option-pricing model is most appropriate for the Company for any future awards.

NOTE 6 Stock Based Compensation

The Company applies the intrinsic value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations, in accounting for its fixed stock option plan. As such, compensation expense is recorded if the current market price on the date of grant of the underlying stock exceeds the exercise price.

Statement of Financial Accounting Standard (SFAS) No. 123 prescribes the recognition of compensation expense based on the fair value of options on the grant date and allows companies to apply APB No. 25 as long as certain pro forma disclosures are made assuming a hypothetical fair value method application.

Had compensation expense for the Company s stock options been recognized based on the fair value on the grant date under the methodology prescribed by SFAS No. 123, the Company s net earnings and earnings per share for the three and six months ended June 30, 2005 and 2004 would have been impacted as shown in the following table:

	For the three months ended June 30		For the six months ended June 30	
	2005	2004	2005	2004
Reported net earnings	$630,119	$487,323	$1,282,383	$948,336
Compensation expense, net of taxes	4,119	3,410	8,238	8,271
Pro forma net earnings	626,000	483,913	1,274,145	940,065
Reported basic earnings per share	$ 0.28	$ 0.22	$ 0.58	$ 0.43
Pro forma basic earnings per share	$ 0.28	$ 0.22	$ 0.57	$ 0.42
Reported diluted earnings per share	$ 0.28	$ 0.22	$ 0.58	$ 0.43
Pro forma diluted earnings per share	$ 0.28	$ 0.22	$ 0.57	$ 0.42

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Critical Accounting Estimates

The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require management to make estimates and assumptions. Management believes that its determination of the allowance for loan losses is a critical accounting policy and involves a higher degree of judgment and complexity than the Bank s other significant accounting policies. Further, these estimates can be materially impacted by changes in market conditions or the actual or perceived financial condition of the Bank s borrowers, subjecting the Bank to significant volatility of earnings.

The allowance for loan losses is regularly evaluated by management and reviewed by the Board of Directors for accuracy by taking into consideration factors such as changes in the nature and volume of the loan portfolio; trends in actual and forecasted portfolio credit quality, including delinquency, charge-off and bankruptcy rates; and current economic conditions that may affect a borrower s ability to pay. The use of different estimates or assumptions could produce different provisions for loan losses. The allowance for credit losses is established through the provision for loan losses, which is a charge against earnings.

Results of Operations

The following financial review is presented to provide an analysis of the results of operations of United Bancorporation of Alabama, Inc. (the Corporation) and its principal subsidiary for the three and six months ended June 30, 2005 and 2004, compared. This review should be used in conjunction with the condensed consolidated financial statements included in the Form 10-Q.

Six Months ended June 30, 2005 and 2004, Compared

Summary

Net income for the six months ended June 30, 2005, increased by $334,046, or 35.22%, as compared to the same period in 2004.

Net Interest Income

Total interest income increased $1,934,231, or 28.65%, for the first six months of 2005 as compared to the same period in 2004. Average interest-earning assets were $290,537,708 for the first six months of 2005, as compared to $246,662,920 for the same period in 2004, an increase of $43,874,788, or 17.79%. A substantial portion of the increase is due to increases in the loan portfolio as the Company continues to implement management s growth initiatives. The average rate earned on interest earning assets in 2005 was 6.14% as compared to 5.24% in 2004, reflecting

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the continuing impact of the increase in rates by the Federal Reserve Board during past and current years.

Total interest expense increased by $604,988, or 36.37%, in 2005, when compared to the same period in 2004. Average interest bearing liabilities increased to $226,183,827 in 2005 from $197,366,640 in 2004, an increase of $28,817,187, or 14.60%. The growth of the Company s interest bearing liabilities is due to a substantial increase in the funds held in Repurchase Agreements and an increase in interest bearing time deposits. The average rate paid rose to 2.02% in 2005 as compared to 1.69% in 2004.

The increase in interest expense can be attributed primarily to higher interest rates paid in 2005 on deposits, compared to lower rates paid on deposits during the same period in 2004.

Net interest margin increased to 4.45% for the first six months of 2005 as compared to 4.38% for the same period in 2004. This was due to the increase in interest rates by the Federal Reserve Board and interest rate sensitivity of the Bank s assets.

Provision for Loan Losses

The provision for loan losses totaled $390,000 for the first six months of 2005 as compared to $360,000 for the same period in 2004. This slight increase is due to the growth in the loan portfolio. See further discussion under Allowance for Loan Losses below.

Noninterest Income

Total noninterest income decreased $48,140 or 3.12% for the first six months of 2005. Service charges on deposits decreased $74,433, or 6.33%, for the first six months of 2005. This decrease is primarily due to a decrease in insufficient fund charges on checks due to a temporary increase in deposits as a result of insurance disbursements following Hurricane Ivan in September of 2004, which decreased $139,997 or 17.20%. The decrease in service charges was partially offset by an increase in ATM network fees.

Noninterest Expense

Total noninterest expense increased $685,040, or 13.52% during the first six months of 2005 as compared to 2004. Salaries and benefits increased $385,314 or 13.85% in the first six months of 2005 primarily due to the expansion of the Bank into new markets and the increased health care costs for the Bank. Occupancy expense increased $67,675 or 7.39%, also largely associated with branch expansion. Other expenses increased $232,051, or 16.92%, during the first six months of 2005. A substantial amount of this increase consists of $103,201 that was taken as a write down of several other real estate owned (OREO) properties. These properties are considered to be valued at their fair market value less any selling costs. The remaining increase in overhead expenses is attributable to the Company s expansion into new markets.

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Income Taxes

Earnings before taxes for the first six months of 2005 were $1,770,810 as compared to $1,204,746 for the first six months of 2004, an increase of $566,064, or 46.99%. Income tax expense for the first six months of 2005 increased by $232,017, to $488,427, when compared to $256,410 the same period in 2004. The effective tax rate increased to 27.58% for the first six months of 2005 when compared to 21.28% in June of 2004.

Three Months Ended June 30, 2005 and 2004, Compared

Summary

Net income for the three months ended June 30, 2005 increased $142,796, or 29.30%.

Net Interest Income

Total interest income increased $1,122,706, or 32.24%, in the second quarter of 2005 as compared to 2004. Average interest-earning assets were $293,932,785 for the second quarter of 2005, as compared to $254,255,961 for the same period in 2004, an increase of $39,676,824, or 15.61%. A substantial portion of this growth is due to the expansion of the Banks loan portfolio as the Bank expands into new markets and strengthens its position in its existing markets. The average rate earned during the second quarter of 2005 was 6.27% as compared to 5.48% in 2004, reflecting the continuing impact of increases in rates by the Federal Reserve Board during the past and current year.

Total interest expense increased by $349,052 or 40.34% in the second quarter of 2005, when compared to the same period in 2004. Average interest bearing liabilities increased to $225,255,997 in 2005 from $203,089,335 in 2004, an increase of $22,166,662, or 10.91%. The average rate paid increased to 2.16% in 2005 as compared to 1.70% in 2004. The net interest margin increased to 4.72% for the second quarter of 2005, as compared to 4.60% for the same period in 2004. This was due to the increase in interest rates by the Federal Reserve Board and the fact that the Bank s assets have repriced faster than the Bank s liabilities.

Provision for Loan Losses

The provision for loan losses totaled $195,000 for the second quarter of 2005 as compared to $180,000 for the same period in 2004. The provision reflected both the growth and improvement in credit quality in the loan portfolio. For further discussion of the provision for loan losses, see the Allowance for Loan Losses discussion below.

Noninterest Income

Total noninterest income increased $47,253 or 6.32% for the second quarter of 2005. Service charges on deposits increased $5,841, or 1.00%, for the second quarter of 2005 as compared to 2004. This increase is primarily due to a decrease in insufficient fund charges on checks and a substantial increase in ATM network fees and point of sale interchange for the period. Other income increased during the second quarter of 2005 by $40,640 or 29.21% as compared to 2004. This increase is primarily due to the net gain of $43,000 on the sale of OREO in June of 2004.

Noninterest Expense

Total noninterest expense increased $446,884, or 17.07%, during the second quarter of 2005 compared to the same quarter of 2004. Salaries and benefits increased $216,535, or 15.25%, in the second quarter of 2005 as compared to the same quarter of 2004. This increase is primarily due to the expansion of the Bank into new markets and increased health care costs for the Bank. Occupancy expense increased $32,697, or 7.15%, in the second quarter of 2005, largely associated with branch expansion. Other expenses increased $197,652 or 26.64% during the second quarter of 2005 as compared to 2004, reflecting increases in general operating expenses related to the Bank s expansion and the $103,201 of write downs that value the OREO properties at their fair market values.

Income Taxes

Earnings before taxes for the second quarter of 2005 were $925,468 as compared to $566,445 in the second quarter of 2004, an increase of $359,023 or 63.38%. Income tax expense for the second quarter increased $216,227 to $295,349, when compared to $79,122 for the same period in 2004. The effective tax rate increased to 31.92% in 2005 from 13.97% in 2004.

Financial Condition and Liquidity

Total assets on June 30, 2005 increased $12,087,415 or 3.88% from December 31, 2004. Average total assets for the first six months of 2005 were $317,534,874. The ratio of loans (net of allowance) to deposits plus repurchase agreements on June 30, 2005 was 76.27% as compared to 72.46% on December 31, 2004.

Cash and Cash Equivalents

Federal Funds Sold and interest bearing balances in other banks as of June 30, 2005 decreased by $19,596,577, or by 71.27%, from December 31, 2004. This decrease is attributed to the increase in loans, as the Bank shifts investments from lower earning assets to higher yielding investments.

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Loans

Net loans increased by $17,398,130 or 8.74% at June 30, 2005, from December 31, 2004. Agricultural lending and commercial real estate loans contributed the majority of this loan growth.

Allowance for Loan Losses

The allowance for loan losses is maintained at a level which, in management s opinion, is appropriate to provide for estimated losses in the portfolio at the balance sheet date. Factors considered in determining the adequacy of the allowance include historical loan loss experience, the amount of past due loans, loans classified from the most recent regulatory examinations and internal reviews, general economic conditions and the current portfolio mix. The amount charged to operating expenses is that amount necessary to maintain the allowance for loan losses at a level indicative of the associated risk, as determined by management, of the current portfolio.

The allowance for loan losses consists of two portions: the classified portion and the nonclassified portion. The classified portion is based on identified problem loans and is calculated based on an assessment of credit risk related to those loans. Specific loss estimate amounts are included in the allowance based on assigned loan classifications as follows: monitor (5%), substandard (15%), doubtful (50%), loss (100%) and specific reserves based on identifiable losses. Any loan categorized loss is charged off in the period in which the loan is so categorized.

The nonclassified portion of the allowance is for inherent losses which probably exist as of the evaluation date even though they may not have been identified by the more specific processes for the classified portion of the allowance. This is due to the risk of error and inherent imprecision in the process. This portion of the allowance is particularly subjective and requires judgments based upon qualitative factors which do not lend themselves to exact mathematical calculations. Some of the factors considered are changes in credit concentrations, loan mix, historical loss experience, non-accrual and delinquent loans and the general economic environment in the Corporation s markets. However, unfavorable changes in the factors used by management to determine the adequacy of the allowance, including increased loan delinquencies and subsequent charge-offs, or the availability of new information, could require additional provisions, in excess of normal provisions, to the allowance for loan losses in future periods.

While the total allowance is described as consisting of a classified and a nonclassified portion, these terms are primarily used to describe a process. Both portions are available to support inherent losses in the loan portfolio. Management realizes that general economic trends greatly affect loan losses, and no assurances can be made that future charges to the allowance for loan losses will not be significant in relation to the amount provided during a particular period, or that future evaluations of the loan portfolio based on conditions then prevailing will not require sizable charges to income. Management does, however, consider the allowance for loan losses to be appropriate for the reported periods.

The allowance for possible loan losses represents 1.21% of gross loans at June 30, 2005, as compared to 1.29% at year-end 2004. This slight decrease is acceptable to management because it is attributable to the cyclical nature of the Company s agricultural lending as seen in previous years. The bank expects a slight increase in the percentage of allowance for possible loan losses to gross loans in subsequent periods as the related agricultural loans are paid down from their current position.

The amount of loans on which the accrual of interest had been discontinued has decreased to $963,741 at June 30, 2005, as compared to $1,201,692 at December 31, 2004. Net charged-off loans for the first six months of 2005 were $321,000, as compared to $138,477 for the same period in 2004. The increase in charged-off loans is due to the Bank s decision to write off a selection of loans following a routine analysis of the loan portfolio during the second quarter of 2005.

Non-performing Assets: The following table sets forth the Corporation s non-performing assets at June 30, 2005 and December 31, 2004. Under the Corporation s nonaccrual policy, a loan is placed on nonaccrual status when collectibility of principal and interest is in doubt or when principal and interest is 90 days or more past due except for credit cards, which continue to accrue interest after ninety days.

The amount of impaired loans determined under SFAS No. 114 and 118 has been considered in the summary of non-performing assets below. These credits were considered in determining the adequacy of the allowance for loan losses and are regularly monitored for changes within a particular industry or general economic trends, which could cause the borrowers financial difficulties. At June 30, 2005 the Bank had $704,462 in impaired loans, compared to $697,017 at December 31, 2004.

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	Description	June 30, 2005	December 31, 2004
		(Dollars in Thousands)	
A	Loans accounted for on a nonaccrual basis	$ 964	$ 1,202
B	Loans which are contractually past due ninety days or more as to interest or principal payments (excluding balances included in (A) above)	$ 4	$ 14
C	Loans, the terms of which have been renegotiated to provide a reduction or deferral of interest or principal because of a deterioration in the financial position of the borrower	$ 324	$ 351
D	Other non-performing assets	$1,164	$ 1,384

Investment Securities

Total investments available for sale have increased $18,487,439 at June 30, 2005 as compared to December 31, 2004 due to the Bank investing federal funds into higher yields in the investment portfolio. As available for sale, all investments are marked-to-market on a monthly basis with unrealized gains and losses, net of tax, adjusted through a component of stockholders equity. Management considers all unrealized losses within the investment portfolio to be temporary. As of June 30, 2005, the investment portfolio had a net unrealized gain of $203,287.

Premises and Equipment

Premises and equipment decreased $123,986 during the first six months of 2005. Because renovations to the Monroeville and Atmore branch locations due to Hurricane Ivan, construction of new buildings at the existing Atmore Southside and Magnolia Springs locations, and continued expansion into the Florida Panhandle and Baldwin County, Alabama, the Company expects the amount of premises and equipment and their associated depreciation expense to increase in the near future.

Deposits

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Total deposits decreased $2,485,087, or .98%, at June 30, 2005 from December 31, 2004, including a decrease of $9,437,934 on noninterest bearing deposits. Interest bearing deposits increased $6,952,847 at June 30, 2005, from December 31, 2004. The decrease in deposits is attributable to the increased use of sweep accounts offered through the Financial Services division by the Bank s customers. The balance of funds held in sweep accounts as of June 30, 2005 was $5,328,578.

Hurricanes Ivan and Dennis

The Bank continues to repair damage caused in September 2004 by Hurricane Ivan, including at the corporate office in Atmore, Alabama. The branch in Monroeville, Alabama, which was rendered unusable, has been remodeled and reopened in the first quarter of 2005.

The Bank s market area also suffered lesser effects from Hurricane Dennis in July 2005. The Bank continues to expect no material financial impact from the hurricane damage to its various offices. Management also continues to expect that the Corporation will not experience any material adverse impact to future earning due to hurricane related damage to the local economies in the Bank s markets, and at the current time does not expect any increases in loan loss provisions because of the hurricanes.

Liquidity

One of the Bank s goals is to provide adequate funds to meet changes in loan demand or any potential increase in the normal level of deposit withdrawals. This goal is accomplished primarily by generating cash from operating activities and maintaining sufficient short-term assets. These sources, coupled with a stable deposit base, allow the Bank to fund earning assets and maintain the availability of funds. Management believes that the Bank s traditional sources of maturing loans and investment securities, cash from operating activities and a strong base of core deposits are adequate to meet the Bank s liquidity needs for normal operations. To provide additional liquidity, the Bank utilizes short-term financing through the purchase of federal funds, and maintains a borrowing relationship with the Federal Home Loan Bank to provide liquidity. Should the Bank s traditional sources of liquidity be constrained, forcing the Bank to pursue avenues of funding not typically used, the Bank s net interest margin could be impacted negatively.

The Corporation s bank subsidiary has an Asset Liability Management Committee, which has as its primary objective the maintenance of specific funding and investment strategies to achieve short-term and long-term financial goals. The Corporation s liquidity at June 30, 2005 is considered adequate by management. Also see Item 3 below.

Capital Adequacy

The Corporation has generally relied primarily on internally generated capital growth to maintain capital adequacy. Total stockholders equity on June 30, 2005, was $27,163,868, an increase of $818,774, or 3.11%, from December 31, 2004. This net increase is a combination of current period earnings, reduced by a decrease in the unrealized gains on securities available for sale and the declaration of dividends as of June 30, 2005.

Primary capital to total assets at June 30, 2005, was 9.52%, as compared to 8.44% at year-end 2004. Total capital and allowances for loan losses to total assets at June 30, 2005, was 11.16%, as compared to 9.27% at December 31, 2004. The Corporation s risk based capital was $33,124,000, or 13.44% of risk adjusted assets, at June 30, 2005, as compared to $31,827,000, or 14.12%, at year-end 2004. The minimum requirement is 8.00%. Based on management s projections, existing internally generated capital and the capital previously raised by issuance of trust preferred securities should be sufficient to satisfy capital requirements in the foreseeable future for existing operations, and for some expansion efforts. Continued growth into new markets may require the Corporation to further access external funding sources. There can be no assurance that such funding sources will be available to the Corporation.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss from adverse changes in market prices and rates. The Bank s market risk arises principally from interest rate risk inherent in its lending, deposit and borrowing activities. Management actively monitors and manages its interest rate risk exposure. Although the Bank manages other risk, such as credit quality and liquidity risk, in the normal course of business, management considers interest rate risk to be its most significant market risk. Interest rate risk could potentially have the largest material effect on the Bank s financial condition and results of operations. Other types of market risks, such as foreign currency exchange rate risk, generally do not arise in the Bank s normal course of business activities to any significant extent.

The Bank s profitability is affected by fluctuations in interest rates. Management s goal is to maintain a reasonable balance between exposure to interest rate fluctuations and earnings. A sudden and substantial increase in interest rates may adversely impact the Bank s earnings to the extent that the interest rates on interest-earning assets and interest-bearing liabilities do not change at the same speed, to the same extent or on the same basis.

The Bank s Asset Liability Management Committee (ALCO) monitors and considers methods of managing the rate and sensitivity repricing characteristics of the balance sheet components consistent with maintaining acceptable levels of changes in the net portfolio value (NPV) and net interest income. NPV represents the market values of portfolio equity and is equal to the market value of assets minus the market value of liabilities, with adjustments made for off-balance sheet items over a range of assumed changes in market interest rates. A primary purpose of the Bank s ALCO is to manage interest rate risk to effectively invest the Bank s capital and to preserve the value created by its core business operations. As such, certain management monitoring processes are designed to minimize the impact of sudden and sustained changes in interest rates on NPV and net interest income.

The Bank s exposure to interest rate risk is reviewed on a quarterly basis by the Board of Directors and the ALCO. Interest rate risk exposure is measured using interest rate sensitivity analysis to determine the Bank s change in NPV in the event of hypothetical changes in interest rates. Further, interest rate sensitivity gap analysis is used to determine the repricing characteristics of the Bank s assets and liabilities. The ALCO is charged with the responsibility to maintain the level of sensitivity of the Bank s net interest margin within Board approved limits.

Interest rate sensitivity analysis is used to measure the Bank s interest rate risk by computing estimated changes in NPV of its cash flows from assets, liabilities, and off-balance sheet items in the event of a range of assumed changes in market interest rates. This analysis assesses the risk of loss in market risk sensitive instruments in the event of a sudden and sustained 100 300 basis points increase or decrease in the market interest rates. The Bank uses the HNC Asset Liability Model, which takes the current rate structure of the portfolio and shocks for each rate level and calculates the new market value equity at each level. The Bank s Board of Directors has adopted an interest rate risk policy, which establishes maximum allowable decreases in net interest margin in the event of a sudden and sustained increase or decrease in market interest rates. The following table presents the Bank s projected change in NPV for the various rate shock levels as of December 31, 2004, the most recent date for which the Corporation has a completed analysis. Management does not expect the analysis as of June 30, 2005 to change materially from the December 31, 2004 analysis. All market risk sensitive instruments presented in this table are held to maturity or available for sale. The Bank has no trading securities.

Change in Interest Rates (Basis Points)	Market Value Equity	Change in Market Value Equity	Change in Market Value Equity %
300	62,661	7,699	25
200	59,449	5,789	19
100	55,215	5,113	10
0	50,102		
-100	44,151	(5,951)	(12)
-200	37,105	(12,997)	(26)
-300	29,308	(20,794)	(42)

The preceding table indicates that at December 31, 2004, in the event of a sudden and sustained increase in prevailing market interest rates, the Bank s NPV would be expected to increase and that in the event of a sudden decrease in prevailing market interest rates, the Bank s NPV would be expected to decrease. The growth in variable rate loans has caused the Corporation to become more asset sensitive over the period of a year, but the net interest margin remains fairly stable in all interest rate environments tested. The Bank does not foresee any material change in the above data during the first six months of 2005.

Computation of prospective effects of hypothetical interest rate changes included in these forward-looking statements are subject to certain risks, uncertainties, and assumptions including relative levels of market interest rates, loan prepayments and deposit decay rates, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions the Bank could undertake in response to changes in interest rates.

Item 4. Controls and Procedures

Based on evaluation of the Corporation s disclosure controls and procedures (as such term is defined in Rules 13a-4(c) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this quarterly report, the principal executive officer and the principal financial officer of the Corporation have concluded that as of such date the Corporation s disclosure controls and procedures were effective to ensure that information the Corporation is required to disclose in its filings under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission s rules and forms, and to ensure that information required to be disclosed by the Corporation in the reports that it files under the Exchange Act is accumulated and communicated to the Corporation s management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

The Corporation has engaged consultants to assist the Corporation in its evaluation of internal controls in anticipation of the upcoming effectiveness of regulations under Section 404 of the Sarbanes-Oxley Act of 2002. There was no change in the Corporation s internal controls over financial reporting during the period covered by this quarterly report that has materially affected, or is reasonably likely to materially affect, the Corporation s internal control over financial reporting.

Forward Looking Statements

When used or incorporated by reference herein, the words anticipate , estimate , expect , project , target , goal , a similar expressions, are intended to identify forward-looking statements within the meaning of Section 27A of the Securities Act of 1933. Such forward-looking statements are subject to certain risk, uncertainties, and assumptions including those set forth herein. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those expected or projected. These forward-looking statements speak only as of the date they are made. The Corporation expressly disclaims any obligations or undertaking to publicly release any updates or revisions to any forward-looking statement contained herein to reflect any change in the Corporation s expectations with regard to any change in events, conditions or circumstances on which any such statement is based.

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PART II OTHER INFORMATION

Item 4. Submission of Matters to a Vote of Security Holders.

(a) A description of actions taken at the annual meeting of security holders of United Bancorporation of Alabama, Inc. on May 4, 2005 was reported under Item 4 of the Corporation s Form 10-Q for the quarter ended March 31, 2005, and is incorporated by reference herein.

Item 6. Exhibits

(a) Exhibits.

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of principal accounting officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of principal accounting officer pursuant to 18 U.S.C. Section 1350, adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002

S I G N A T U R E S

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.

UNITED BANCORPORATION OF ALABAMA, INC.

Date: August 13, 2005

/s/ Robert R. Jones, III

Robert R. Jones, III
President and CEO