

UNITED BANCORPORATION OF ALABAMA INC  
Form 10-K  
March 30, 2007

**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

**FORM 10-K**

[ X ]

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended  
December 31, 2006

Commission File No. 2-78572

**UNITED BANCORPORATION OF ALABAMA, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction organization)

**63-0833573**

(I.R.S. Employer Identification of incorporation or  
No.)

**P.O. Drawer 8, Atmore, Alabama 36504**

(Address of principal executive offices)

Registrant's telephone number, including area code: (251) 446-6000

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Class A Common Stock, Par Value \$.01 Per Share

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 of Section 15(d) of the Act. Yes  No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 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 reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

Aggregate market value of voting and nonvoting common equity held by non affiliates as of March 10, 2007 was \$42,496,616 computed by reference to the price reported to the registrant at which the common equity was last sold on or prior to that date and using beneficial ownership of stock rules adopted pursuant to Section 13 of the Securities Exchange Act of 1934 to exclude voting stock owned by directors and executive officers, some of whom might not be held to be affiliates upon judicial determination.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

Common Stock	Par Value	Outstanding at March 27, 2007
Class A	\$.01	2,236,664 Shares*
Class B	\$.01	0 Shares

\*Excludes 138,807 shares held as treasury stock.

#### DOCUMENTS INCORPORATED BY REFERENCE

The Registrant's Proxy Statement relating to the 2007 Annual Meeting of Stockholders is incorporated by reference in Part III of this report.

## PART I

### ITEM 1. BUSINESS

#### FORWARD-LOOKING STATEMENTS

When used or incorporated by reference herein, the words "anticipate", "estimate", "expect", "project", "target", "goal", and 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 risks, uncertainties and assumptions, including those set forth elsewhere herein, as well as the possibilities of (i) increases in competitive pressures in the banking industry, particularly with respect to community banks; (ii) costs or difficulties, relating to the planned increase in the number of Bank offices, which are greater than expected based on prior experience; (iii) general economic conditions, either nationally or regionally, that are less favorable than expected, resulting in deterioration in loan demand, credit quality and/or borrower liquidity, among other things; (iv) changes which may occur in the regulatory environment; and (v) large and/or rapid changes in interest rates. 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 Bank's expectations with regard to any change in events, conditions or circumstances on which any such statement is based.

#### UNITED BANCORPORATION OF ALABAMA, INC AND UNITED BANK

United Bancorporation of Alabama, Inc. (the "Corporation" or the Company ) is a one-bank financial holding company, with headquarters in Atmore, Alabama. The Corporation was incorporated under the laws of Delaware on March 8, 1982 for the purpose of acquiring all of the issued and outstanding capital stock of The Bank of Atmore, Atmore, Alabama ("Atmore") and Peoples Bank, Frisco City, Alabama ("Peoples"). Atmore was merged into United Bank of Atmore, a wholly-owned subsidiary of the Corporation, and Peoples was merged into United Bank of Frisco City ("Frisco City"), also a wholly-owned subsidiary of the Corporation, in late 1982. Effective March 30, 1984, Frisco City merged into United Bank of Atmore, which had previously changed its name to simply "United Bank."

The Corporation and its subsidiary, United Bank (herein "United Bank" or the "Bank"), operate primarily in one business segment, commercial banking. United Bank contributes substantially all of the total operating revenues and consolidated assets of the Corporation. The Bank serves its customers from fourteen full service banking offices located in Atmore (2 offices), Frisco City, Monroeville, Flomaton, Foley, Lillian, Bay Minette (2 offices), Silverhill, Magnolia Springs, and Summerdale, Alabama, a loan production office in Loxley, and offices in Jay and Milton, Florida.

United Bank offers a broad range of banking services. Services to business customers include providing checking and time deposit accounts and various types of lending services. Services provided to individual customers include checking accounts, NOW accounts, money market deposit accounts, statement savings accounts, repurchase agreements and various other time deposit savings programs and loans, including business, personal, automobile, home and home improvement loans. United Bank offers securities brokerage services, Visa multi-purpose, and nationally recognized credit card service. The Bank also offers internet banking, bill pay and access to online brokerage services at its web site, [www.ubankal.com](http://www.ubankal.com). The Bank also owns an insurance agency, United Insurance Services, Inc., which opened and began business in 2001.

## **COMPETITION**

The commercial banking business is highly competitive and United Bank competes actively with state and national banks, savings and loan associations, insurance companies, brokerage houses, and credit unions in its market areas for deposits and loans. In addition, United Bank competes with other financial institutions, including personal loan companies, leasing companies, finance companies and certain governmental agencies, all of which engage in marketing various types of loans and other services. The regulatory environment affects competition in the bank business as well.

## **EMPLOYEES**

The Corporation and its subsidiary had approximately 165 full-time equivalent employees at December 31, 2006. All of the employees are engaged in the operations of United Bank, its subsidiary, or the Corporation. The Corporation considers its employee relations good, and has not experienced and does not anticipate any work stoppage attributable to labor disputes.

## **SUPERVISION, REGULATION AND GOVERNMENT POLICY**

Bank holding companies, banks and many of their non-bank affiliates are extensively regulated under both federal and state law. The following brief summary of certain statutes, rules and regulations affecting the Corporation and the Bank is qualified in its entirety by reference to the particular statutory and regulatory provisions referred to below, and is not intended to be an exhaustive description of the statutes or regulations applicable to the Corporation's business.

Any change in applicable law or regulations could have a material effect on the business of the Corporation and its subsidiary. Supervision, regulation and examination of banks by bank regulatory agencies are intended primarily for the protection of depositors rather than holders of Corporation common stock.

The Corporation is registered as a bank holding company with the Board of Governors of the Federal Reserve System (the "Federal Reserve") under the Bank Holding Company Act of 1956, as amended (the "BHC Act"). As such, the Corporation is subject to the supervision, examination, and reporting requirements in the BHC Act and the regulations of the Federal Reserve. The Corporation is a Financial Holding Company (FHC). See discussion of the Gramm-Leach-Bliley Financial Services Modernization Act below.

The BHC Act requires every bank holding company to obtain the prior approval of the Federal Reserve before it may acquire substantially all of the assets of any bank or control of any voting shares of any bank, if, after such acquisition, it would own or control, directly or indirectly, more than 5% of the voting shares of such bank. The BHC Act requires the Federal Reserve to consider, among other things, anticompetitive effects, financial and managerial resources and community needs in reviewing such a transaction. Under the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, enacted in September 1994, bank holding companies were permitted to acquire banks located in any state without regard to whether the transaction is prohibited under any state law (except that states may establish a minimum age of not more than five years for local banks subject to interstate acquisitions by out-of-state bank holding companies), and interstate branching was permitted beginning June 1, 1997 in certain circumstances.

With the prior approval of the Superintendent of the Alabama State Department of Banking ("Superintendent") and their primary federal regulators, state banks are entitled to expand by branching.

The Corporation is a legal entity separate and distinct from the Bank. Various legal limitations restrict the Bank from lending or otherwise supplying funds to the Corporation. Such transactions, including extensions of credit, sales of securities or assets and provision of services, also must be on terms and conditions consistent with safe and sound banking practices, including credit standards, that are substantially the same or at least as favorable to the Bank as prevailing at the time for transactions with unaffiliated companies. Also, as a subsidiary of a bank holding company, the Bank is generally prohibited from conditioning the extension of credit or other services, or conditioning the lease or sale of property, on the customer's agreement to obtain or furnish some additional credit, property or service from or to such subsidiary or an affiliate.

The Bank is a state bank, subject to state banking laws and regulation, supervision and regular examination by the Alabama State Department of Banking (the "Department"), and as a member of the Bank Insurance Fund ("BIF") of the Federal Deposit Insurance Corporation (the "FDIC"), is also subject to FDIC regulation and examination. The Bank is not a member of the Federal Reserve System. Areas subject to federal and state regulation include dividend payments, reserves, investments, loans, interest rates, mergers and acquisitions, issuance of securities, borrowings, establishment of branches and other aspects of operation, including compliance with truth-in-lending and usury laws, and regulators have the right to prevent the development or continuance of unsafe or unsound banking practices regardless of whether the practice is specifically proscribed or otherwise violates law.

Dividends from United Bank constitute the major source of funds for the Corporation. United Bank is subject to state law restrictions on its ability to pay dividends, primarily that the prior written approval of the Superintendent is required if the total of all dividends declared in any calendar year exceeds the total of United Bank's net earnings of that year combined with its retained net earnings of the preceding two years, less any required transfers to surplus.

United Bank is subject to restrictions under Alabama law which also prohibits any dividends from being made from surplus without the Superintendent's prior written approval and the general restriction that dividends in excess of 90% of United Bank's net earnings (as defined by statute), may not be declared or paid unless United Bank's surplus is at least equal to 20% of its capital. United Bank's surplus is significantly in excess of 20% of its capital. Federal bank regulatory agencies also have the general authority to limit the dividends paid by insured banks and bank holding companies if such payment is deemed to constitute an unsafe and unsound practice. Federal law provides that no dividends may be paid which would render the Bank undercapitalized. United Bank's ability to make funds available to the Corporation also is subject to restrictions imposed by federal law on the ability of a bank to extend credit to its parent company, to purchase the assets thereof, to issue a guarantee, acceptance or letter of credit on behalf thereof or to invest in the stock or securities thereof or to take such stock or securities as collateral for loans to any borrower.

The Bank is also subject to the requirements of the Community Reinvestment Act of 1977 ("CRA"). The CRA and the regulations implementing the CRA are intended to encourage regulated financial institutions to help meet the credit needs of their local community, including low and moderate-income neighborhoods, consistent with the safe and sound operation of financial institutions. The regulatory agency's assessment of the Bank's CRA record is made available to the public.

The Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA") recapitalized the BIF and included numerous revised statutory provisions. FDICIA established five capital tiers for insured depository institutions: "well capitalized", "adequately capitalized", "undercapitalized", "significantly undercapitalized", and "critically undercapitalized", as defined by regulations adopted by the Federal Reserve, the FDIC and other federal depository institution regulatory agencies. At December 31, 2006, the Bank was "well capitalized" and was not subject to restrictions imposed for failure to satisfy applicable capital requirements. BIF premiums for each member financial institution depend upon the risk assessment classification assigned to the institution by the FDIC.

Banking is a business that primarily depends on interest rate differentials. In general, the difference between the interest rate paid by a bank on its deposits and other borrowings and the interest rate received by the bank on its loans and securities holdings constitutes the major portion of the bank's earnings. As a result, the earnings and business of the Corporation are and will be affected by economic conditions generally, both domestic and foreign, and also by the policies of various regulatory authorities having jurisdiction over the Corporation and the Bank, especially the Federal Reserve. The Federal Reserve, among other functions, regulates the supply of credit and deals with general economic conditions within the United States. The instruments of monetary policy employed by the Federal Reserve for those purposes influence in various ways the overall level of investments, loans and other extensions of credit and deposits and the interest rates paid on liabilities and received on assets.

The enactment of the Gramm-Leach-Bliley Financial Services Modernization Act (the GLB Act ) on November 12, 1999 represented an important development in the powers of banks and their competitors in the financial services industry by removing many of the barriers between commercial banking, investment banking, securities brokerages and insurance. Inter-affiliation of many of these formerly separated businesses is now common. The GLB Act includes significant provisions regarding the privacy of financial information. These financial privacy provisions generally require a financial institution to adopt a privacy policy regarding its practices for sharing nonpublic personal information and to disclose such policy to their customers, both at the time the customer relationship is established and at least annually during the relationship. These provisions also prohibit the Company from disclosing nonpublic personal financial information to third parties unless customers have the opportunity to opt out of the disclosure. The GLB Act gives the Federal Reserve broad authority to regulate FHCs, but provides for functional regulation of subsidiary activities by the Securities Exchange Commission, Federal Trade Commission, state insurance and securities authorities and similar regulatory agencies.

On October 26, 2001, President Bush signed into law the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the USA Patriot Act ). Among its provisions, the USA Patriot Act requires each financial institution: (i) to establish an anti-money laundering program, (ii) to establish due diligence policies, procedures and controls with respect to its private banking accounts and correspondent banking accounts involving foreign individuals and certain foreign banks and (iii) to avoid establishing, maintaining, administering, or managing correspondent accounts in the United States for, or on behalf of, a foreign



bank that does not have a physical presence in any country. In addition, the USA Patriot Act contains a provision encouraging cooperation among financial institutions, regulatory authorities and law enforcement authorities with respect to individuals, entities and organizations engaged in, or reasonably suspected of engaging in, terrorist acts or money laundering activities. The USA Patriot Act has not had a significant impact on the financial condition or results of operations of the Corporation.

In July 2002 the Sarbanes-Oxley Act of 2002 (the "SOA") was enacted. The SOA established many new operational and disclosure requirements, with the stated goals of, among other things, increasing corporate responsibility and protecting investors by improving corporate disclosures. The SOA applies generally to companies that file periodic reports with the Securities and Exchange Commission under the Securities Exchange Act of 1934 (the "Exchange Act"). As an Exchange Act reporting company, the Corporation is subject to some SOA provisions. Other SOA requirements apply only to companies which, unlike the Corporation, have stock traded on a national stock exchange or the NASDAQ.

Selected Statistical Information - The following tables set forth certain selected statistical information concerning the business and operations of the Corporation and its wholly-owned subsidiary, United Bank, as of December 31, 2006, 2005 and 2004. Averages referred to in the following statistical information are generally average daily balances.

**AVERAGE CONSOLIDATED BALANCE SHEETS**

December 31,

2006, 2005 and 2004

(Dollars In Thousands)

Assets	2006	2005	2004
Cash and due from banks	16,306	13,986	7,231
Interest - bearing deposits with other financial institutions	10,369	6,847	8,147
Federal funds sold and repurchase agreements	8,535	9,784	3,176
Taxable securities available for sale	43,275	42,604	32,878
Tax-exempt securities available for sale	31,870	26,117	23,966
Loans, net	242,431	213,311	184,634
Premises and equipment, net	9,117	8,179	7,962
Interest receivable and other assets	12,738	9,484	11,118
<b>Total Assets</b>	<b>374,641</b>	<b>330,312</b>	<b>279,112</b>
<b>Liabilities and Stockholders' Equity</b>			
Demand deposits-noninterest-bearing	63,833	63,211	48,950
Demand deposits-interest bearing	57,613	49,350	41,479
Savings deposits	21,507	25,012	21,034
Time deposits	143,241	122,387	109,333
Other borrowed funds	16,380	13,500	13,790
Repurchase agreements	41,745	27,580	17,148
Accrued expenses and other liabilities	2,026	2,789	1,697
<b>Total liabilities</b>	<b>346,345</b>	<b>303,829</b>	<b>253,431</b>
<b>Stockholders' Equity</b>			
Common stock	24	24	24
Additional Paid in Capital	5,523	5,423	5,506
Retained earnings	24,287	21,942	20,474
Accumulated other comprehensive income net of deferred taxes	(707)	(71)	533
Less: shares held in treasury, at cost	(831)	(835)	(856)
<b>Total stockholders' equity</b>	<b>28,296</b>	<b>26,483</b>	<b>25,681</b>
<b>Total liabilities and stockholders' equity</b>	<b>374,641</b>	<b>330,312</b>	<b>279,112</b>



Analysis of Net Interest Earnings: The following table sets forth interest earned and the average yield on the major categories of the Corporation's interest-earning assets and interest-bearing liabilities.

(Dollars in Thousands)			
	Average Balance	Interest Income  Expense	Average Rates  Earned Paid
2006			
Loans, net (1)	242,431	20,815	8.59%
Taxable securities available for sale	43,275	2,112	4.88%
Tax exempt sec available for sale (2)	31,870	1,912	6.00%
Federal funds sold and repurchase agreements	8,535	434	5.08%
Interest-bearing deposits with other financial institutions	10,369	427	4.12%
Total interest-earning assets	336,480	25,700	7.64%
Saving deposits and demand deposits interest-bearing	79,120	1,197	1.51%
Time deposits	143,241	5,846	4.08%
Repurchase agreements	41,745	1,661	3.98%
Other borrowed funds	16,380	1,052	6.42%
Total interest-bearing liabilities	280,486	9,756	3.48%
Net interest income/net yield on interest earning assets		15,944	4.74%
2005			
Loans, net (1)	213,311	15,786	7.40%
Taxable securities available for sale	42,604	1,822	4.28%
Tax exempt sec available for sale (2)	26,117	1,575	6.03%

Federal funds sold and repurchase agreements	9,784	243	2.48%
Interest-bearing deposits with other financial institutions	6,847	204	2.98%
Total interest-earning assets	298,663	19,630	6.57%
Saving deposits and demand deposits interest-bearing	74,362	893	1.20%
Time deposits	122,387	3,290	2.69%
Repurchase agreements	27,580	642	2.33%
Other borrowed funds	13,500	678	5.02%
Total interest-bearing liabilities	237,829	5,503	2.31%
Net interest income/net yield on interest earning assets		14,127	4.73%

2004	Average Balance	Interest Income Expense	Average Rates Earned Paid
Loans, net (1)	184,634	11,980	6.49%
Taxable securities available for sale	32,878	1,223	3.72%
Tax exempt sec available for sale (2)	23,966	1,500	6.26%
Federal funds sold and repurchase agreements	3,176	53	1.67%
Interest-bearing deposits with other financial institutions	8,147	107	1.31%
Total interest-earning assets	252,801	14,863	5.88%
Saving deposits and demand deposits interest-bearing	62,513	578	0.92%
Time deposits	109,333	2,306	2.11%
Repurchase agreements	17,148	79	0.46%
Other borrowed funds	13,790	576	4.18%
Total interest-bearing liabilities	202,784	3,539	1.75%
Net interest income/net yield on interest earning assets		11,324	4.48%

(1)

Loans on nonaccrual status have been included in the computation of average balances.

(2)

Yields on tax-exempt obligations have been computed on a full federal tax-equivalent basis using an income tax rate of 34% for 2006, 2005 and 2004

Analysis of Changes in Interest Income and Interest Expense: The following is an analysis of the dollar amounts of changes in interest income and interest expense due to changes in rates and volume for the periods indicated.

(Dollars in Thousands)						
Average Balances		Interest Income Expense		Variance	Variance As to	
2006	2005	2006	2005		Rate	Volume

\$							
242,431	213,311	Loans (Net)	20,815	15,786	5,029	2,684	2,345
		Taxable Securities					
43,275	42,604	AFS(1)	2,112	1,822	290	30	260
		Tax Exempt					
31,870	26,117	Securities AFS (2)	1,912	1,575	337	(15)	352
8,535	9,784	Fed Funds Sold	434	243	191	(52)	243
		Interest Bearing					
10,369	6,847	Deposits	427	204	223	132	91
		Total Interest					
336,480	298,663	Earning Assets	25,700	19,630	6,070	2,779	3,291
		Savings and					
		Interest Bearing					
79,120	74,362	Demand Deposits	1,197	893	304	255	49
143,241	122,387	Time Deposits	5,846	3,290	2,556	1,732	824
		Repurchase					
41,745	27,580	Agreements	1,661	642	1,019	595	424
		Other Borrowed					
16,380	13,500	Funds	1,052	678	374	130	244
		Total Int. Bearing					
280,486	237,829	Liabilities	9,756	5,503	4,253	2,712	1,541

The variance of interest due to both rate and volume has been allocated proportionately to the rate and the volume components based on the relationship of the absolute dollar amounts of the change in each.

(1)

Available for Sale (AFS)

(2)

Yields on tax-exempt obligations have been computed on a full federal tax equivalent basis using an income tax rate of 34% for 2006 and 2005.

Analysis of Changes in Interest Income and Interest Expense: The following is an analysis of the dollar amounts of changes in interest income and interest expense due to changes in rates and volume for the periods indicated.





Average Balances		(Dollars in Thousands)		Interest Income		Variance As to		
2005	2004		Expense	2005	2004	Variance	Rate	Volume
213,311	184,634	Loans (Net)		15,786	11,980	3,806	1,847	1,959
		Taxable Securities						
42,604	32,878	AFS(1)		1,822	1,223	599	207	392
		Tax Exempt						
26,117	23,966	Securities AFS (2)		1,575	1,500	75	(28)	103
9,784	3,176	Fed Funds Sold		243	53	190	150	40
		Interest Bearing						
6,847	8,147	Deposits		204	107	97	92	5
		Total Interest						
298,663	252,801	Earning Assets		19,960	14,863	4,767	2,268	2,499
		Savings and Interest						
		Bearing						
74,362	62,513	Demand Deposits		893	578	315	252	63
		Other Time						
122,387	109,333	Deposits		3,290	2,306	984	731	255
		Repurchase						
27,580	17,148	Agreements		642	79	563	350	213
		Other Borrowed						
13,500	13,790	Funds		678	576	102	62	40
		Total Int. Bearing						
237,329	202,784	Liabilities		5,503	3,539	1,964	1,395	571

The variance of interest due to both rate and volume has been allocated proportionately to the rate and the volume components based on the relationship of the absolute dollar amounts of the change in each.

(1)

Available for Sale (AFS)

(2)

Yields on tax-exempt obligations have been computed on a full federal tax equivalent basis using an income tax rate of 34% for 2005 and 2004.

## **INVESTMENTS**

The investment policy of United Bank provides that funds that are not otherwise needed to meet the loan demand of United Bank's market area can best be invested to earn maximum return for the Bank, yet still maintain sufficient liquidity to meet fluctuations in the Bank's loan demand and deposit structure. Since 2001 the Bank has moved all investments held to maturity to available for sale. The Bank's current loan policy establishes the gross optimal ratio of loans to deposits and repurchase agreements ratio as being 85%. This ratio as of December 31, 2006 was 65.35%. Growth in the loan portfolio is driven by general economic conditions and the availability of loans meeting the Bank's credit quality standards. Management expects that funding for any growth in the loan portfolio would come from deposit growth, repurchase agreement growth, reallocation of maturing investments and advances from the Federal Home Loan Bank of Atlanta (FHLB).

## **SECURITIES PORTFOLIO**

The Bank's investment policy as approved by the Board of Directors dictates approved types of securities and the conditions under which they may be held. Attention is paid to the maturity and risks associated with each investment. The distribution reflected in the tables below could vary with economic conditions, which could shorten or lengthen maturities. Management believes the level of credit and interest rate risks inherent in the securities portfolio is low.

The following table sets forth the amortized cost of the Available for Sale investment portfolio.

**INVESTMENT SECURITIES AVAILABLE FOR SALE**

December 31, 2006, 2005 and 2004

(Dollars in Thousands)

	2006		2005		2004	
	Amortized Cost	Percentage of Portfolio	Amortized Cost	Percentage of Portfolio	Amortized Cost	Percentage of Portfolio
U.S. Government sponsored agencies	55,111	50.5%	19,103	26.6%	8,082	14.8%
Mortgage Backed Sec	21,415	19.6%	23,773	33.1%	22,604	41.5%
State and Municipal	32,649	29.9%	28,894	40.3%	23,816	43.7%
Total	\$ 109,175	100.0%	\$ 71,770	100.0%	54,502	100.0%

The following table sets forth the distribution of maturities of investment securities available for sale.

**MATURITY DISTRIBUTION OF INVESTMENT SECURITIES AVAILABLE FOR SALE**

December 31, 2006, 2005 and 2004

(Dollars in Thousands)

	2006		2005		2004	
US Government Agencies excluding Mortgage Backed securities						
Within one year	29,457	5.40%	-	0.00%	-	0.00%
1-5 years	12,869	4.48%	17,103	4.06%	6,199	3.21%
5-10 years	11,785	5.48%	2,000	4.89%	1,883	4.67%
After 10 years	1,000	5.75%	-	0.00%	-	0.00%
Total	55,111	5.21%	19,103	4.15%	8,082	3.55%

Mortgage Backed Securities

Within one year	-	0.00%	-	0.00%	-	0.00%
1-5 years	3,980	4.02%	4,292	3.83%	1,914	3.61%
5-10 years	6,000	4.05%	8,358	4.06%	8,218	3.86%
After 10 years	11,435	4.66%	11,123	4.98%	12,472	4.26%
Total	21,415	4.37%	23,773	4.45%	22,604	4.06%

State & Municipal (1)

Within one year	591	2.52%	1,000	3.13%	165	11.72%
1-5 years	5,169	3.88%	4,709	3.76%	3,606	7.59%
5-10 years	12,407	4.09%	10,416	4.11%	8,654	9.24%
After 10 years	14,482	4.01%	12,769	4.01%	11,391	9.94%
Total	32,649	3.99%	28,894	3.97%	23,816	9.34%

Totals	109,175	4.68%	71,770	4.18%	54,502	6.28%
--------	---------	-------	--------	-------	--------	-------

(1)

Yields on tax-exempt obligations have been computed on a full federal tax-equivalent basis using an income tax rate of 34% for 2006, 2005 and 2004.

## **RELATIVE LENDING RISK**

United Bank serves both rural and suburban markets. The rural market is composed primarily of lower to middle income families. The rural market economy is influenced by timber and agricultural production. The suburban market is faster growing, more commercial and is composed of a higher income mix than the rural market. The Bank's loan portfolio mix is reflective of these markets. The Bank's ratio of loans to assets or deposits is comparable to its peer banks serving similar markets.

The risks associated with the Bank's lending are primarily interest rate risk and credit risks from economic conditions and concentrations and/or quality of loans.

Interest rate risk is a function of the maturity of the loan and method of pricing. The Bank's loan maturity distribution reflects 43.17% of the portfolio maturing in one year or less. In addition, 57.03% of all loans float with an interest rate index. The maturity distribution and floating rate loans help protect the Bank from unexpected interest rate changes.

Loan concentrations present different risk profiles depending on the type of loan. The majority of all types of loans offered by the Bank are collateralized. Regardless of the type of loan, repayment ability of the borrower and collateralized lending is based upon an evaluation of the collateral. Loan policy, as approved by the Board of Directors of the Bank, establishes collateral guidelines for each type of loan.

Small banks located in one community experience a much higher risk due to the dependence on the economic viability of that single community. United Bank is more geographically diverse than some of its local community banking competitors. With offices in twelve communities, risks associated with the effects of major economic disruptions in one community are somewhat mitigated. This geographic diversity affects all types of loans and plays a part in the Bank's risk management.

Each type of loan exhibits unique profiles of risk that could threaten repayment.

Commercial lending requires an understanding of the customers' business and financial performance. The Bank's commercial customers are primarily small to middle market enterprises. The larger commercial accounts are managed by Senior Commercial lenders. Risks in this category are primarily economic. Shifts in local and regional conditions could have an effect on individual borrowers; but as previously mentioned, the Bank attempts to spread this risk by serving multiple communities. As with the other categories, these loans are typically collateralized by assets of the borrower. In most situations, the personal assets of the business owners also collateralize the credit.

Agricultural lending is a specialized type of lending for the Bank. Due to the unique characteristics in this type of loan, the Bank has loan officers dedicated to this market. Collateral valuation and the experience of the borrower play heavily into the approval process. This loan category includes financing equipment, crop production, timber, dairy operations and others. Given the broad range of loans offered, it is difficult to generalize risks in agricultural lending. The area of greatest attention and risk is crop production loans. Risks associated with catastrophic crop losses are mitigated by crop insurance, government support programs, experience of the borrower, collateral other than the crop and the borrower's other financial resources. Routine visitations and contact with the borrower help inform the Bank about crop conditions.

Real estate loans, whether they are construction or mortgage, generally have lower delinquency rates than other types of loans in the portfolio. The Bank makes very few long term, fixed rate mortgage loans; however, it does offer loans with repayment terms based on amortization of up to 30 years with balloon features of shorter durations. The Bank also offers several different long-term mortgage programs provided by third party processors.

Installment loans are generally collateralized. Given the small dollar exposure on each loan, the risk of a significant loss on any one credit is limited. Pricing and close monitoring of past due loans enhance the Bank's returns from this type of loan and minimize risks.

An average loan in the loan portfolio at December 31, 2006 was approximately \$61,983, an increase of \$15,994 from 2005.

## **LOAN PORTFOLIO MATURITIES**

Maturities and loan re-pricing indices in the Corporation's loan portfolio are as follows:

**REMAINING MATURITY**

December 31, 2006

(Dollars in Thousands)

	One year or less	One - five years	After five years	Total
Commercial, financial and agricultural	\$ 46,030	67,480	12,053	\$ 125,563
Real estate - construction	52,552	12,835	1,665	\$ 67,052
Real estate - mortgage 1-4 family	8,232	23,513	6,101	\$ 37,846
Installment loans to individuals	5,259	8,683	1,236	\$ 15,178
Totals	\$ 112,073	112,511	21,055	245,639

**LOANS BY RE-PRICING INDEX**

(Dollars in Thousands)

	Index			Total
	Prime	LIBOR	Other	
Commercial, financial and agricultural	\$ 58,458	1,253	220	59,931
Real estate - construction	52,716	3,191	4,621	60,528
Real estate - mortgage 1-4 family	16,952	-	23	16,975
Installment loans to individuals	2,654	-	10	2,664
Totals	\$ 130,780	4,444	4,874	140,098

For additional information regarding interest rate sensitivity see INTEREST RATE SENSITIVITY in Item 7 below and Item 7A below.

Non-performing Assets: Management considers a loan to be impaired when it is probable that the Corporation will be unable to collect all amounts due according to the contractual terms of the loan agreement. When a loan is considered impaired, the amount of impairment is measured based on the net present value of expected future cash flows discounted at the note's effective interest rate. If the loan is collateral-dependent, the fair value of the collateral is used to determine the amount of impairment. Impaired loans are covered by the allowance for loan losses through a charge to the provision for loan losses. Subsequent recoveries are added to the allowance. Impaired loans are charged to the

allowance when such loans are deemed to be uncollectible. At December 31, 2006, the Bank had \$1,766,960 in impaired loans.

The following table sets forth the Corporation's non-performing assets at December 31, 2006, 2005, 2004, 2003 and 2002. Under the Corporation's nonaccrual policy, a loan is placed on nonaccrual status when the ability to collect the 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.



		(Dollars in Thousands)				
Descriptions	2006	2005	2004	2003	2002	
A Loans accounted for on a nonaccrual basis	\$ 1,570	\$ 1,406	\$ 1,202	\$ 2,171	\$ 1,169	
B Loans which are contractually past due ninety days or more as to interest or principal payments (excluding balances included in (A) above)	9	4	14	15	10	
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.	197	318	351	229	968	
D Other non-performing assets	621	1,131	1,384	1,108	350	
Total	\$ 2,397	\$ 2,859	\$ 2,951	\$ 3,523	\$ 2,497	

If nonaccrual loans in (A) above had been current throughout their term, interest income would have been increased by \$123,917, \$165,159, \$102,372, \$95,877 and \$29,968 for 2006, 2005, 2004, 2003, and 2002 respectively. All of the assets in (D) above at the end of 2006, 2005, 2004, 2003 and 2002 were other real estate owned (OREO).

At December 31, 2006, loans with a total outstanding balance of \$13,303,949 were considered potential problem loans compared to \$13,264,440, \$6,602,558, \$6,491,658, and \$4,127,658 as of 2005, 2004, 2003, and 2002 respectively. Potential problem loans consist of those loans for which management is monitoring performance or has concerns as to the borrower's ability to comply with present loan repayment terms.

The increase in potential problem loans in 2005 was due primarily to The Bank downgrading \$6,700,000 of agricultural loans.

There may be additional loans in the Bank's portfolio that may become classified as conditions dictate. Regulatory examiners may require the Bank to recognize additions to the allowance based upon their judgments about information available to them at the time of their examination.

## **LOAN CONCENTRATIONS**

On December 31, 2006, the Bank had \$36,937,000 of agriculture-related loans as compared to \$35,407,000, \$27,459,000, and \$26,218,000 and \$30,983,000 in 2005, 2004, 2003, and 2002 respectively. Agriculture loans accounted for \$990,143, \$424,109, \$4,980, \$2,915, and \$0 of nonaccrual loans in 2006, 2005, 2004, 2003, and 2002, respectively.

**SUMMARY OF LOAN LOSS EXPERIENCE**

(Dollars in Thousands)

	2006	2005	2004	2003	2002
Average amount of loans outstanding, net	242,431	213,311	184,634	163,897	152,869
Allowance for loan losses beginning January 1	3,028	2,562	2,117	2,117	1,993
Loans Charged off:					
Commercial, financial and agriculture	(1,062)	(365)	(155)	(451)	(563)
Real estate - mortgage	-	-	(45)	(117)	(7)
Installment loans to individuals	(95)	(108)	(158)	(238)	(195)
Total Charged off	(1,157)	(473)	(358)	(806)	(765)
Recoveries during the period					
Commercial, financial and agriculture	35	2	2	27	5
Real estate - mortgage	-	-	-	7	-
Installment loans to individuals	45	57	81	31	47
Total Recoveries	80	59	83	65	52
Loans Charged off, net	(1,077)	(414)	(275)	(741)	(713)
Other Adjustments	100	-	-	-	-
Additions to the allowance charged to operations	960	880	720	741	837
	3,011	3,028	2,562	2,117	2,117
Ratio of net charge offs during the period to average loans outstanding	0.44%	0.19%	0.15%	0.45%	0.46%

**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 the provision 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 determined based on an assessment of credit risk related to those loans. Specific loss estimate amounts are included in the allowance based on an evaluation of the individual credits. Any loan categorized loss is charged off in the period which the loan is so categorized.

The nonclassified portion of the allowance is for probable inherent losses which exist as of the evaluation date even though they may not have been identified by the more objective 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, and general economic environment in the Company's markets.

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 Company has allocated proportionately the nonclassified portion of the allowance to the individual loan categories for purposes of the loan loss allowance table below.

Management believes that the allowance for loan losses at December 31, 2006 is adequate and appropriate given past experience and the underlying strength of the loan portfolio.

The table below reflects an allocation of the allowance for the years ended December 31, 2006, 2005, 2004, 2003, and 2002. The allocation represents an estimate for each category of loans based upon historical experience and management's judgment.

(Dollars In Thousands)

	Allowance					Percentage of Loans to Total Loans				
	2006	2005	2004	2003	2002	2006	2005	2004	2003	2002
Commercial, financial and agricultural	2,173	2,271	1,942	1,505	1,453	54.2%	70.1%	76.0%	70.5%	68.6%
Real estate - construction	116	91	85	87	107	24.2%	8.5%	3.3%	4.1%	5.1%
Real estate - mortgage 1-4 family	563	454	374	379	362	15.4%	15.6%	14.4%	18.5%	17.1%

Installment loans to individuals	159	212	161	146	195	6.2%	5.8%	6.3%	6.9%	9.2%
Total	3,011	3,028	2,562	2,117	2,117	100.0%	100.0%	100.0%	100.0%	100.0%

## DELINQUENT LOAN POLICY

Installment loans are placed on nonaccrual when the loan is three payments past due. Single-date maturity notes are placed on nonaccrual status when such notes are delinquent for 90 days. Delinquent commercial loans are placed on nonaccrual status when the loan is 90 days past due. Exceptions may be made where there are extenuating circumstances, but any exception is subject to review by the Board of Directors of the Bank.

Loans are considered delinquent if payments of principal or interest have not been made by the end of periods ranging from one to ten days after the due date, depending upon the type of loan involved. Installment loans are considered delinquent if payments of principal and interest are past due for a period of ten days and commercial loans are considered delinquent if payments of principal and interest are past due for a period of one day. Single-date maturity loans are considered delinquent if payments are not made by the day following the due date of such loans.

Loans are reviewed for charge offs, as necessary, on a monthly basis. If necessary, loans can be charged off at any time with the approval of the Chief Executive Officer (CEO). The loan officer responsible for the particular loan initiates the charge off request, which then must be approved by the CEO. All charged off loans are reviewed by the Board of Directors of the Bank at the monthly board meeting.

The following table sets forth the average amount of deposits for the years 2006, 2005 and 2004 by category.

## DEPOSITS

(Dollars in Thousands)

	Average Deposits			Average Rate Paid		
	2006	2005	2004	2006	2005	2004
Noninterest-bearing demand deposits	\$ 63,833	\$ 63,211	\$ 48,950	0%	0%	0%
Interest - bearing Demand	57,613	49,350	41,479	1.98%	1.38%	1.26%

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Savings	21,507	25,012	21,034	0.25%	0.25%	0.25%
Time	143,241	122,387	109,333	4.08%	2.68%	2.11%
	\$ 222,361	\$ 196,749	\$ 171,846	3.17%	2.05%	1.68%

The following shows the amount of time deposits outstanding at December 31, 2006, classified by time remaining until maturity.

Maturity	\$100,000 or Greater	
	Certificates of Deposits	Other Time Deposits
Three months or less	\$ 16,937	20,405
Three to six months	12,076	22,229
Six to twelve months	23,694	26,643
Twelve months or more	15,937	17,190
Totals	\$ 68,644	86,467

The following table shows various amounts of repurchase agreements and other short term borrowings and their respective rates.

	(Dollars in Thousands)				Average Interest Rate at Year End
	Maximum Outstanding at any Month End	Average Balance	Average Interest Rate	Ending Balance	
2006					
Securities sold under agreements to repurchase	47,133	41,745	3.98%	44,410	4.17%
Other short term borrowings	872	362	5.25%	857	3.49%
2005					
Securities sold under agreements to repurchase	34,429	27,580	2.30%	34,429	3.14%
Other short term borrowings	1,001	346	3.45%	1,001	3.45%

2004					
Securities sold under agreements to repurchase	23,838	17,148	0.46%	18,381	1.27%
Other short term borrowings	3,250	263	1.82%	7	1.53%

Return on Equity and Assets: The following table shows the percentage return on equity and assets of the Corporation for the years ended December 31, 2006, 2005 and 2004.

	2006	2005	2004
Return on average assets	0.84%	0.88%	0.77%
Return on average equity	11.08%	10.93%	8.38%
Dividend pay-out ratio	21.43%	23.08%	30.87%
Ratio of average equity to average assets	7.55%	8.02%	9.20%



## **ITEM 1A. RISK FACTORS**

The following discusses risks that management believes could have a negative impact on the Company's financial performance. When analyzing an investment in the Company, the risks and uncertainties described below, together with all of the other information included or incorporated by reference in this report should be carefully considered.

The risk factors relate primarily to the commercial banking operations of the Bank. This list should not be viewed as comprehensive and may not include all risks that may affect the financial performance of the Company:

### **CAPITAL RISK**

The Company is required by federal and state regulatory authorities to maintain adequate levels of capital to support its operations. The Company anticipates that capital resources will satisfy these requirements in the near term.

However, the Company may need to raise additional capital to support growth or for other needs. The ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are beyond the Company's control, as well as on the Company's current and anticipated financial performance. Accordingly, there can be no assurances as to the Company's ability to raise additional capital, if needed, on favorable terms or at all. In the event the Company is unable to raise capital when needed, its ability to further expand operations through internal capital generation (net earnings) and acquisitions could be impeded.

### **INTEREST RATE RISK**

The Bank's profitability is largely a function of the spread between the interest rates earned on earning assets and the interest rates paid on deposits and other interest-bearing liabilities. Like most financial institutions, the Bank's net interest income and margin will be affected by general economic conditions, fiscal and monetary policies of the Federal government that influence market interest rates, the Bank's ability to respond to changes in such rates and other factors that determine the level and direction of movement of interest rates. At any given time, the Bank's assets and liabilities may be so positioned that they are affected differently by a change in the level or direction of interest rates. As a result, an increase or decrease in rates, loan terms, the mix of adjustable- and fixed-rate loans or investment securities in the Bank's portfolio or the shape of the yield curve could have a positive or negative effect on its net income, capital and liquidity. Although management believes it has implemented strategies and guidelines to reduce the potential effects of changes in interest rates on results of operations, any substantial and prolonged change in market interest rates could adversely affect operating results. See **INTEREST RATE SENSITIVITY** in Item 7 below and Item 7A below.

### **CREDIT RISK**

As a lender, the Bank is exposed to the risk that its borrowers may be unable to repay their loans and that any collateral securing the payment of their loans may not be sufficient to assure repayment in full. Credit losses are inherent in the lending business and could have a material adverse effect on the operating results of the Bank. Adverse changes in the economy or business conditions, either nationally or in the Bank's market areas, could increase credit related losses or related expenses and/or limit growth. Substantially all of the Bank's loans are to businesses and individuals in a limited geographic area and any economic decline in this local market could impact the Bank adversely. The Bank makes various assumptions and judgments about the collectibility of its loan portfolio and

provides an allowance for loan losses based on a number of factors. If these assumptions are incorrect, the allowance for loan losses may not be sufficient to cover losses, thereby having an adverse effect on operating results, and may cause the Bank to increase the allowance in the future by increasing the provision for loan losses. The Bank has adopted credit policies which when combined with underwriting and credit monitoring procedures produce a process that management believes is appropriate to control these risks. Such policies and procedures may not prevent unexpected losses that could have a material adverse affect on the Bank's financial condition and/or results of operations. See PROVISION FOR LOAN LOSSES in Item 7 and Summary of Loan Loss Experience and Allowance for Loan Losses in Item 1.

## COMPETITION

The financial services industry is highly competitive. Competition for attracting and retaining deposits and attracting desirable loans comes from a wide array of financial companies, such as other banks, savings institutions, credit unions, mutual fund companies, insurance companies and, increasingly, other non-bank businesses. Some of the Bank's competitors are much larger in terms of total assets and market capitalization, have a higher lending limit, and have greater access to capital and funding. The presence of one or more aggressive competitors in the Bank's market area could have an adverse affect on the Bank's financial condition and/or results of operations by increasing the cost of deposits, reducing the rates on loans or limiting access to quality borrowers. See Competition in Item 1.

## **GOVERNMENT REGULATION AND SUPERVISION**

The banking industry is heavily regulated under both Federal and state law. Banking regulations, designed primarily for the safety of depositors, may limit a financial institution's growth and the return to its investors, by restricting such activities as the payment of dividends, mergers with or acquisitions by other institutions, expansion of branch offices and the offering of securities. The Bank is also subject to capitalization guidelines established by Federal law and could be subject to enforcement actions to the extent that its subsidiary bank is found, by regulatory examiners, to be undercapitalized. It is not possible to predict what changes, if any, will be made to existing Federal and state legislation and regulations or the effect that such changes may have on the Bank's future business and earnings prospects. Any substantial changes to applicable laws or regulations could also subject the Bank to additional costs, limit the types of financial services and products it may offer, and inhibit its ability to compete with other financial service providers. See "Supervision, Regulation and Government Policy" in Item 1.

## **ATTRACTING AND RETAINING SKILLED PERSONNEL**

Attracting and retaining key personnel is critical to the Bank's success, and difficulty finding qualified personnel could have a significant impact on the Bank's business due to the lack of required skill sets and years of industry experience.

## **LOCAL ECONOMIC CONDITIONS**

The Bank's success depends primarily on the general economic conditions of the specific local markets in which the Bank operates. Unlike larger national or other regional banks that are more geographically diversified, the Bank provides banking and financial services to customers primarily in Escambia, Monroe, and Baldwin County, Alabama, and Santa Rosa County, Florida. The local economic conditions in these areas have a significant impact on the demand for the Bank's products and services as well as the ability of the Bank's customers to repay loans, the value of the collateral securing loans and the stability of the Bank's deposit funding sources. A significant decline in general economic conditions, caused by inflation, recession, acts of terrorism, outbreak of hostilities or other international or domestic occurrences, unemployment, changes in securities markets or other factors could impact those local economic conditions and, in turn, have a material adverse effect on the Bank's financial condition and results of operations. See "Relative Lending Risk" in Item 1.

## **GROWTH STRATEGY**

The Bank intends to continue pursuing a profitable growth strategy. Growth prospects must be considered in light of the risks, expenses and difficulties associated with expansion of the Bank's operation. There can be no assurance that the Bank will be able to expand its market presence in existing markets or successfully enter new markets or that any such expansion will not adversely affect the Bank's business, future prospects, financial condition or results of operations.

## **SEVERE WEATHER, NATURAL DISASTERS, ACTS OF WAR OR TERRORISM AND OTHER EXTERNAL EVENTS COULD SIGNIFICANTLY IMPACT THE CORPORATIONS BUSINESS**

Severe weather, natural disasters, acts of war or terrorism and other adverse external events could have a significant impact on the Bank's ability to conduct business. Such events could affect the stability of the Bank's deposit base, restrict the ability of borrowers to repay outstanding loans, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue and/or cause the Bank to incur additional expenses. Although management has established disaster recovery policies and procedures, the occurrence of any such event could have a material adverse effect on the Bank's business, which, in turn, could have a material adverse effect on the Bank's financial condition and results of operations.

#### **INFORMATION SYSTEMS INTEGRITY**

The Bank relies on modern data, communication, and network systems to conduct ongoing operations. These systems could be vulnerable to internal and external attacks to the physical equipment or the raw data stored within these systems. Failures to maintain the integrity of one or more of these systems could threaten the Bank's ability to serve customers in an effective and timely manner. The Bank maintains policies and procedures governing the access to and use of these systems in order to insulate the systems from any sort of security breach. However, any breach could have a material adverse effect on the financial position and future earnings of the Bank.

## **TECHNOLOGICAL ADVANCEMENT AND IMPLEMENTATION**

The future success of the Bank is directly related to the successful implementation of new technological advancements pertaining to the banking industry. Technology continues to offer the Bank new avenues to add products for customers, as well as increase the efficiency of the Bank's internal operations. Failure to effectively manage the implementation of emerging technology could result in the loss of existing customers or limit the Bank's ability to attract new customers, thus putting pressure on the Bank's financial position and future earnings.

## **INTERNAL AUDIT AND CONTROL RISK**

The Bank incorporates the use of various internal audit review and internal controls to minimize the Bank's exposure to material financial misstatement or fraudulent activity. Despite the presence of these systems, the Bank is exposed to the inherent risks that are present in any similar environment, including risks that a control, or controls, could be circumvented. The Bank attempts to revise its internal audit procedures and controls as its operations evolve. However rigorously the Bank undertakes its pursuit of internal controls, this process can only provide reasonable assurance that the Bank's financial reporting does not include material misstatement.

## **ITEM 1B. UNRESOLVED STAFF COMMENTS**

Not applicable.

## **ITEM 2. PROPERTIES**

The Corporation's bank subsidiary operates fourteen full service branches and one loan production office, which the subsidiary owns or leases. The offices are located in Escambia County, Alabama (cities of Atmore (two offices) and Flomaton); Monroe County, Alabama (cities of Monroeville and Frisco City); Baldwin County, Alabama (cities of Foley, Lillian, Bay Minette (two offices), Magnolia Springs, Silverhill, Summerdale, and a loan production office in Loxley); and Santa Rosa County, Florida (cities of Jay and Milton), with the principal office located in Atmore, Alabama. All land, buildings, and fixed assets owned by the Corporation were transferred as an investment of capital to the Bank during 2006. The office in Atmore is a modern, three story building. This building and the adjacent AgriFinance Office and the Bank's Information Systems Department facility were completely remodeled and updated following damage from Hurricanes Ivan and Dennis in 2004 and 2005. Following Hurricane Ivan in 2004, the Monroeville office received extensive remodeling and upgrades. The Bank completed construction of a full service office to replace the limited drive-thru location on the south side of Atmore during 2005. The Foley office was purchased in October of 2002. The office in Lillian is a modern two-story brick building. The Bank also owns a two story brick building in Bay Minette. The second office in Bay Minette was built in 2003 on Highway 59. The office in Silverhill is the original post office built in 1902, and is a two story wooden structure owned by the Bank. Construction was completed a new office located in Magnolia Springs on the corner of US Highway 98 and County Road 49 during the summer of 2006. The Bank has opened two new branches in Santa Rosa County, Florida.

Currently, these facilities are located in rented offices in strip shopping centers, offering limited services. The Bank is currently planning the construction or purchase of three to four branches to be placed in service during 2007 with another two to three branches to be constructed during the 2008 fiscal year.

### **ITEM 3. LEGAL PROCEEDINGS**

There are presently no pending legal proceedings to which the Corporation or its subsidiary, United Bank, is a party or to which any of their property is subject, which management of the Corporation based upon consultation with legal counsel believes are likely to have a material adverse effect upon the financial position of the Corporation.

### **ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted to a vote of the shareholders of the Corporation during the fourth quarter of the fiscal year.

## PART II

### ITEM 5. MARKET FOR THE REGISTRANT'S EQUITY AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

The Corporation's authorized common shares consist of the following:

(1)

5,000,000 shares of Class A common stock, \$.01 par value per share, of which 2,375,471 shares are issued and 2,236,664 are outstanding and held by approximately 779 shareholders of record, as of March 27, 2007.

(2)

250,000 shares of Class B common stock, \$.01 par value per share, none of which were issued, as of March 27, 2007.

The Corporation recently became aware that its common stock appears to be quoted on the Over-the-Counter-Bulleting Board, or OTCBB, a regulated quotation service that is administered and regulated by the National Association of Securities Dealers, Inc., or NASD, under the trading symbol UBAB. The Corporation has neither applied for nor had contact with NASD with respect to the OTCBB or any other quotation service. The Corporation's common stock is not listed on any exchange.

The Corporation is informed that over-the-counter market quotations reflect inter-dealer prices, without retail mark-ups, markdowns, or commissions and may not necessarily reflect actual transactions. Although bid prices have apparently been posted on the OTCBB during 2005 and 2006, the Corporation believes that no transactions occurred in 2006, and only 7 transactions occurred in 2005 at prices ranging from \$14.80 to \$15.85 per share. Because very few transactions involving the Corporation's common stock have been reported on the OTCBB, the Corporation believes that any reported bid or asked price may not reflect a fair valuation of its common stock.

The Corporation paid total cash dividends per common share of \$0.30 per common share in 2006 and 2005, and \$0.30\* per common share in 2004. The Corporation expects to continue to pay cash dividends, subject to the earnings and financial condition of the Corporation and other relevant factors; however, dividends on the Corporation's common stock are declared and paid based on a variety of considerations by the Corporation's Board of Directors and

there can be no assurance that the Corporation will continue to pay regular dividends or as to the amount of dividends if any. Payment of future dividends will depend upon business conditions, operating results, capital and reserve requirements and the Board's consideration of other relevant factors. In addition, the ability of the Corporation to pay dividends is totally dependent on dividends received from its banking subsidiary (see Note 17 to the consolidated financial statements) and is subject to statutory restrictions on dividends applicable to Delaware corporations, including the restrictions that dividends generally may be paid only from a corporation's surplus or from its net profits for the fiscal year in which the dividend is declared and the preceding year.

\*Adjusted for the two-for-one stock split in June 2004

## COMPARATIVE PERFORMANCE GRAPH

The Securities and Exchange Commission (SEC) requires the Corporation to include in this Form 10-K a graph which compares the yearly percentage change in cumulative total shareholder return on the Class A Stock with (i) the performance of a broad equity market indicator, and (ii) the performance of a published industry index or peer group. Set forth below is a graph comparing the yearly percentage change in the cumulative total stockholder return on the Class A Stock against the cumulative total return of the S&P 500 Index and the Nasdaq Bank Index for the five-year period from December 31, 2001 to December 31, 2006. The Nasdaq Bank Index is a broad-based capitalization-weighted index of domestic and foreign common stocks of banks that are traded on the Nasdaq National Market System (Nasdaq/NMS) as well as the SmallCap Market. The Class A Stock is not actively traded on a recognized market, and the price for the Class A Stock on the dates represented in the graph are based on the most recent sales prices reported to the Corporation on or prior to each such date.



	2001	2002	2003	2004	2005	2006
United Bancorporation of Alabama, Inc.	100	166.06	166.37	161.61	191.78	211.51
S & P 500	100	76.63	96.91	105.56	108.73	123.54
Nasdaq Bank Index	100	104.52	135.80	150.73	144.20	160.07

**ITEM 6. SELECTED FINANCIAL DATA**

	(Dollars in Thousands) (Except Per Share Data)				
	2006	2005	2004	2003	2002
Income statement data:					
Interest Income	\$ 25,050	\$ 19,094	\$ 14,353	\$ 13,343	\$ 14,017
Interest Expense	9,756	5,503	3,539	3,650	4,575
Net interest income	15,294	13,592	10,814	9,693	9,442
Provision for loan losses	960	880	720	741	837
Net interest income after provision for loan losses	14,334	12,712	10,094	8,952	8,605
Investment securities gains (losses), net	(5)	34	171	489	77
Noninterest income	3,912	3,136	3,045	3,467	2,726
Noninterest expense	14,089	11,913	10,374	9,614	8,693
Net earnings	3,135	2,895	2,153	2,131	2,035
Balance sheet data:					
Total assets	426,171	369,829	311,963	254,979	232,822
Total loans, net	242,627	227,282	194,617	162,031	160,319
Total deposits	326,835	291,020	250,957	199,406	182,565
Total Stockholders' equity	30,725	28,026	26,345	24,969	23,453
Per share data*:					
Basic earnings per share	1.41	1.30	0.97	0.98	0.93
Fully diluted earnings per share	1.40	1.30	0.97	0.98	0.91
Cash dividend per share*	\$ 0.30	\$ 0.30	\$ 0.30	\$ 0.28	\$ 0.28

\*Adjusted for 2-for-1 stock split  
effective June 2004

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **INTRODUCTION**

The following financial review is presented to provide an analysis of the consolidated results of operations of the Company and its subsidiary. This review should be read in conjunction with the consolidated financial statements included under Item 8.

### **OVERVIEW**

This overview is a broad, high-level discussion of various financial measures addressed in detail in the following discussion and analysis. The items addressed, as such, do not have any more or less significance than the detailed discussion to follow.

United Bancorporation of Alabama, Inc. is a one-bank holding company that competes in the commercial banking industry within the primary markets of Southwest Alabama and Northwest Florida. As a community bank, the Bank strives to serve the needs of the total market including, but not limited to, consumer and business banking needs, agricultural financing, mortgage products, and various insurance and investment needs.

At December 31, 2006 the Company had \$426,170,974 of total assets, compared to \$370,061,044 at December 31, 2005. The growth of loans and investment securities were the primary components of the increase from year to year. Total deposits increased over 12% to \$326,835,463, as compared to \$291,020,471 at the end of 2005. The growth in deposits was the primary source of funding for the growth in both loans and investments. The Company also issued Trust Preferred Securities in the amount of \$10,000,000. Of the total funds raised, \$6,000,000 was invested in United Bank as equity to provide support for the Bank's future growth. The remainder (\$4,000,000) was reserved to redeem the previous issue of Trust Preferred Securities in the third quarter of 2007 (this redemption is subject to approval by the Federal Reserve).

Net interest income after provision for loan losses was \$14,334,337 for the year ended December 31, 2006, as compared with \$12,711,510, and \$10,094,928, for the years ended December 31, 2005, and 2004 respectively. The growth in net interest income after the provision for loan losses is primarily due to the increased volume of loans and the rising rate environment during the first seven months of the year. Interest expense also increased as a function of the growth in the volume of time deposits during the year and the rise in the general level of interest rates.

Noninterest income totaled \$3,912,213 for 2006 as compared to \$3,136,151, and \$3,044,918, in 2005, and 2004, respectively. Service charges and fees, trust and brokerage revenues, income from the sale of other investments, and numerous smaller amounts were the major factors in the increase from year to year.

Noninterest expense was \$14,088,598 for the year ended December 31, 2006, as compared to \$11,912,693, and \$10,373,987 for the years ended December 31, 2005, and 2004. Noninterest expense increased in several categories including, but not limited to, salaries and benefits, occupancy, expense, professional fees, advertising, and write downs of Other Real Estate Owned.

Net Earnings for the year ended December 31, 2006 increased over 8.3% to \$3,135,070, as compared to \$2,894,784, and \$2,153,257, for the years ended December 31 2005 and 2004, respectively. The effective tax rates for 2006, 2005, and 2004 were 24.60%, 26.43%, and 22.12%. Diluted earnings per share for the same periods were \$1.40, \$1.30, and \$0.97.

### **CRITICAL ACCOUNTING ESTIMATES**

The consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States and with general practices within the banking industry, which require management to make estimates and assumptions (see Note 1 to Consolidated Financial Statements).

## **ALLOWANCE FOR LOAN LOSSES**

Management believes that its determination of the allowance for loan losses 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 credit losses is established through a provision for loan losses, which is a charge against earnings. Provisions for loan losses are made to reserve for estimated probable losses on loans.

The allowance for loan losses is a significant estimate and is regularly evaluated by management 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 borrowers' ability to pay. The use of different estimates or assumptions could produce different provisions for loan losses. Because current economic conditions can change and future events are inherently difficult to predict, the anticipated amount of estimated loan losses, and therefore the adequacy of the allowance, could change. Management believes the allowance for loan losses is adequate and properly recorded in the financial statements. For further discussion of the allowance for loan losses, see **PROVISION FOR LOAN LOSSES** below, and **Summary of Loan Loss Experience** and **Allowance for Loan Losses** under **BUSINESS** above.

## **ESTIMATES OF FAIR VALUE**

The estimation of fair value is significant to a number of the Company's assets, including, but not limited to, investment securities, derivatives, other real estate owned, intangible assets and other repossessed assets. Derivatives and investment securities are recorded at fair value while other real estate owned, intangible assets and other repossessed assets are recorded at either cost or fair value, whichever is lower. Fair values for investment securities and derivatives are based on quoted market prices, and if not available, quoted prices on similar instruments. The fair values of other real estate owned and repossessions are typically determined based on third-party appraisals less estimated costs to sell. Intangible assets, such as the charter cost, are periodically evaluated to determine if any impairment might exist.

The estimation of fair value and subsequent changes of fair value of investment securities, derivatives, other real estate owned, repossessions and intangible assets can have a significant impact on the value of the Company, as well as have an impact on the recorded values and subsequently reported net income.

Changes in interest rates is the primary determining factor in the fair value of investment securities, derivatives, and the value at which these assets are reported in the Company's financial statements. Local economic conditions are often the key factor in the valuation of other real estate owned and repossessed assets. Changes in these factors can cause assets to be written down and have an impact on the financial results. The overall financial condition and results of operations of the banking unit is the primary determinant as to the value of recorded intangible assets.

**NET INTEREST INCOME**

(Dollars in Thousands)

	2006	2005	2004
Interest income (1)	\$ 25,700	\$ 19,703	\$ 14,863
Interest expense	9,756	5,503	3,539
Net interest income	15,944	14,200	11,324
Provision for loan losses	960	880	720
Net interest income after provision for loan losses on a tax equivalent basis	14,984	13,320	10,604
Less: tax equivalent adjustment	650	609	510
Net interest income after provision for loan losses	\$ 14,334	\$ 12,711	\$ 10,094

(1)

Income on tax-exempt obligations have been computed on a full federal tax-equivalent (FTE) basis using an income tax rate of 34% for 2006, 2005, and 2004.

Total interest income (on an FTE basis) increased to \$25,700,000 in 2006, from \$19,703,000 in 2005, an increase of \$5,997,000, or 30.44%. This increase is a function of the change in average earning assets along with the rising interest rate environment that prevailed during the first seven months of 2006. The Bank expects this growth rate to lessen as the Federal Open Market Committee has held the overnight rate constant for the final five months of 2006, thus putting pressure on the interest margin and the overall demand for loans in the Bank's markets. Average loans increased \$29,120,000 while the average rate earned increased 119 basis points causing an overall increase in interest earned on loans of \$5,029,000. The average interest rate (FTE) earned on all earning assets in 2006 increased to 7.64% from 6.57% in 2005. The interest rate margin increased from 4.73% in 2005 to 4.74% in 2006, the slower increase of the net interest margin is due to the cessation of the rising rate environment, flat yield curve, and the increased volume of interest bearing demand and time deposits. Average taxable investment securities for 2006 were \$43,275,000, as compared to \$42,604,000 for 2005, an increase of \$671,000, or 1.57%. Average tax-exempt investment securities increased \$5,753,000, or 22.03%, to \$31,870,000 in 2006 from \$26,117,000 in 2005. The average volume of federal funds sold decreased to \$8,535,000 in 2006 from \$9,784,000 in 2005, a decrease of \$1,249,000 or 12.77%.

Total interest income (on an FTE basis) increased to \$19,703,000 in 2005, from \$14,863,000 in 2004, an increase of \$4,840,000, or 32.56%. This increase was a function of the change in average earning assets along with the change in interest rates. The majority of the change was due to the increase in loans. Average loans increased \$28,677,000 while the average rate earned increased 92 basis points causing an overall increase in interest earned on loans of \$3,806,000. The average interest rate (FTE) earned on all earning assets in 2005 increased to 6.60% from 5.88% in 2004. The interest rate margin increased from 4.48% in 2004 to 4.73% in 2005, as rates on interest earning assets continued to rise due to the increase in the fed funds rate and competitive conditions in many of our markets. The rise in prime rate throughout 2005 caused the variable rate loans to re-price at higher rates and time deposit rates re-priced higher as well. Average taxable investment securities for 2005 were \$42,604,000, as compared to \$32,878,000 for 2004, an increase of \$9,726,000, or 29.58%. Average tax-exempt investment securities increased \$2,151,000, or 8.98%, to \$26,117,000 in 2005 from \$23,966,000 in 2004. The average volume of federal funds sold increased to \$9,784,000 in 2005 from \$3,176,000 in 2004, an increase of \$6,608,000 or 208.06%.

Total interest expense increased \$4,253,000 or 77.28%, to \$9,756,000 in 2006, from \$5,503,000 in 2005. This increase was a function of a 16.8% increase in the volume of interest bearing deposits, the rising interest rates paid on deposits, and the interest payments related to the Company's Trust Preferred Securities. The Company expects interest expense to remain on a relatively high growth rate as the balance of time deposits continue to grow as customers move their lower interest bearing demand accounts into higher interest bearing time deposits and the Company pays interest on Trust Preferred Securities totaling \$14,000,000 during the first nine months of 2007. The average rate paid on interest-bearing liabilities in 2006 was 3.47% as compared to 2.31% in 2005. Average interest-bearing liabilities increased to \$280,486,000 in 2006, from \$237,829,000 in 2005, an increase of \$42,657,000, or 17.94%. Average savings and interest-bearing demand deposits increased \$4,758,000 or 6.40% to \$79,120,000 in 2006. Average time deposits increased to \$143,241,000 in 2006, from \$122,387,000 in 2005, an increase of \$20,854,000, or 17.04%. The average rate paid on time deposits increased to 4.08% in 2006 from 2.69% in 2005. The Corporation issued \$4,124,000 of subordinated debentures in June of 2002 at an interest rate of three month LIBOR plus 3.65%. The Corporation also issued \$10,310,000 of subordinated debentures in September of 2006 at an interest rate of LIBOR plus 1.68%. The interest expense associated with subordinated debentures in 2006 was \$557,345 or an average rate of 8.44%.



Total interest expense increased \$1,964,000 or 55.51%, to \$5,503,000 in 2005, from \$3,539,000 in 2004. This increase was a function of the increase in interest rates and a 22% increase in the volume of interest bearing liabilities. The average rate paid on interest-bearing liabilities in 2005 was 2.31% as compared to 1.75% in 2004. Average interest-bearing liabilities increased to \$237,829,000 in 2005, from \$202,784,000 in 2004, an increase of \$35,045,000, or 17.28%. Average savings and interest-bearing demand deposits increased \$11,849,000 or 18.95% to \$74,362,000 in 2005. Average time deposits increased to \$122,387,000 in 2005, from \$109,333,000 in 2004, an increase of \$13,054,000, or 11.94%. The average rate paid on time deposits increased to 2.68% in 2005 from 2.11% in 2004. The Corporation issued \$4,124,000 of subordinated debentures in June of 2002 at an interest rate of three month LIBOR plus 3.65%. The interest expense associated with subordinated debentures in 2005 was \$304,434 or an average rate of 7.14%.

## **PROVISION FOR LOAN LOSSES**

The provision for loan losses is that amount necessary to maintain the allowance for loan losses at a level appropriate for the associated credit risk, as determined by management in accordance with generally accepted accounting principles (GAAP), in the current portfolio. The provision for loan losses increased 9.09% for the year ended December 31, 2006 to \$960,000 as compared to \$880,000 and \$720,000 as of December 31, 2005 and 2004, respectively. The change in the provision maintains the allowance at a level that is determined to be appropriate by management and the board of directors of the Bank.

The allowance for loan losses at December 31, 2006 represents 1.23% of gross loans, as compared to 1.32% and 1.30% at December 31, 2005 and 2004, respectively.

While it is the Bank's policy to charge off loans when a loss is considered probable, there exists the risk of losses which cannot be quantified precisely or attributed to particular loans or classes of loans. Because this risk is continually changing in response to factors beyond the control of the Bank, management's judgment as to the appropriateness of the allowance for loan losses is approximate and imprecise. Adjustments to the allowance for loan losses may also be required by the FDIC or the Alabama Superintendent of Banks in the course of their examinations of the Bank. Accordingly, no assurances can be given that continued evaluations of the loan portfolio in light of economic conditions then prevailing, results of upcoming examinations, or other factors will not require significant changes to the allowance.

### NONINTEREST INCOME

	2006		2005		2004
Service Charge Income	\$ 907,655	\$	831,560	\$	758,307
Nonsufficient Fund Charges, net	1,833,652		1,486,699		1,500,874
Mortgage Origination Fees	261,473		241,460		196,740
Investment Securities Gains, (net)	(4,879)		33,916		170,898
Other	914,312		542,516		418,099
	\$ 3,912,213	\$	3,136,151	\$	3,044,918

Total noninterest income increased \$776,062 or 24.75%, to \$3,912,213 in 2006, as compared to \$3,136,151 in 2005.

Service charge income increased to \$907,655 in 2006, from \$831,560 in 2005, an increase of \$76,095, or 9.15%. Nonsufficient fund charges increased \$346,953 from \$1,486,699 in 2005 to \$1,833,652 in 2006. Other income increased to \$914,312 in 2006, from \$542,516 in 2005, an increase of \$371,796 or 68.53%. This increase is substantially attributable to an increase of \$20,013 in mortgage origination fees for third parties, an increase of \$124,335 in Trust and Brokerage Revenue, and the gain on a sale of a Bank investment of \$119,110. Gain on the sales of investment securities decreased \$38,795 to a loss position of \$4,879 in 2006 from a gain of \$33,916 in 2005.

Total noninterest income increased \$91,233 or 3.00%, to \$3,136,151 in 2005, as compared to \$3,044,918 in 2004.

Service charge income increased to \$831,560 in 2005, from \$758,307 in 2004, an increase of \$73,253, or 9.66%. Nonsufficient fund charges decreased \$14,175 from \$1,500,874 in 2004 to \$1,486,699 in 2005. Other income increased to \$734,781 in 2005, from \$564,823 in 2004, an increase of \$169,958 or 30.09%. This increase was attributable to an increase of \$44,720 in mortgage origination fees for third parties, while a portion of the rest of the gain was due to the gain on OREO sales in 2005 of \$45,199 and an increase of \$45,410 in Trust and Brokerage Revenue. Gain on the sales of investment securities decreased \$136,982 to \$33,916 in 2005 from \$170,898 in 2004. The Bank sold investments in 2005 to take advantage of certain market conditions that allowed for the lengthening of the duration of the investment portfolio.

**NONINTEREST EXPENSE**

	2006		2005		2004
Salaries and benefits	\$ 7,353,896	\$	6,512,743	\$	5,779,483
Net occupancy	2,368,030		2,023,492		1,988,538
Other	4,366,672		3,376,458		2,605,966
Total	\$ 14,088,598	\$	11,912,693	\$	10,373,987

Total noninterest expense increased \$2,175,905, or 18.27%, to \$14,088,598 in 2006 from \$11,912,693 in 2005. Salaries and other compensation expense increased \$841,153, or 12.92%, to \$7,353,896 in 2006 from \$6,512,743 for 2005. Occupancy expenses increased from \$2,023,492 in 2005 to \$2,368,030 in 2006, an increase of \$344,538 or 17.03%. The Bank expects its current growth strategy, which incorporates the construction or acquisition of approximately two to three locations per year, to continue to contribute to increases in noninterest expense as seen in recent years. The impact of the growth strategy is evident in increased salaries and benefits, as new officers and staff members are required to be hired and trained in order to adequately open new locations, and occupancy expense, as the depreciation expense and the costs to operate these locations are incurred. The growth model, along with the Bank's commitment to maximize current technology, also impacts other expense. Other expense increased to \$4,366,672 in 2006, from \$3,376,458 in 2005, an increase of \$990,214, or 29.33%. The major components of this increased expense include \$327,494 of increased expense in professional fees, advertising, and other expenses directly associated with opening new locations and increased competition within the Bank's existing

markets. Other expense was also impacted by an increase in write downs of OREO of \$149,899 in 2006 to \$278,100, from the 2005 total of \$128,201, as the Bank adjusted one property to its market value in preparation for its sale, and \$133,000 of expense related to overdrawn checking accounts. Income tax expense for 2006 was \$1,022,882 as compared to \$1,040,184 in 2005. The effective tax rate in 2006 was 24.60% as compared to 26.43% in 2005.

Total noninterest expense increased \$1,538,706, or 14.83%, to \$11,912,693 in 2005 from \$10,373,987 in 2004. Salaries and other compensation expense increased \$733,260, or 12.69%, to \$6,512,743 in 2005 from \$5,779,483 for 2004. This increase was due to increases in salary and benefit costs related to additions to the management team and staffing for new offices. Occupancy expenses increased from \$1,988,538 in 2004 to \$2,023,492 in 2005, an increase of \$34,954 or 1.76%. Other expense increased to \$3,376,458 in 2005, from \$2,605,966 in 2004, an increase of \$770,492, or 29.57%. This increase was caused in part by write downs of OREO of \$128,201 in 2005, an \$113,274 increase in fees largely related to the Corporation's compliance with the Sarbanes-Oxley Act of 2002, and a \$99,392 increase in miscellaneous losses. Other increases in other expense were related to the Bank's growth strategy that is focused on expansion into new markets. Income tax expense for 2005 was \$1,040,184 as compared to \$612,602 in 2004. The effective tax rate in 2005 was 26.43% as compared to 22.12% in 2004.

Basic earnings per share in 2006 were \$1.41, as compared to basic earnings per share of \$1.30 in 2005. Diluted earnings per share were \$1.40 in 2006 and \$1.30 in 2005. Return on average assets was 0.84% in 2006, as compared to 0.88% in 2005. Return on average equity was 11.08% in 2006, as compared to 10.93% in 2005. As the Bank continues to implement its growth strategy over the next few years these ratios may decline if the expenses from the growth strategy are realized prior to the realization of the expected increases in revenue.

Basic earnings per share in 2005 were \$1.30, as compared to basic earnings per share of \$0.97 in 2004. Diluted earnings per share were \$1.30 in 2005 and \$0.97 in 2004. Return on average assets was 0.88% in 2005, as compared to 0.77% in 2004. Return on average equity was 10.93% in 2005, as compared to 8.38% in 2004.

#### LOANS AT DECEMBER 31

	2006	2005	2004	2003	2002
Commercial, financial and agriculture	\$ 133,174,048	\$ 161,432,166	\$ 151,295,232	\$ 115,721,929	\$ 111,429,905
Real estate - construction	59,392,025	19,481,344	6,505,508	6,791,566	8,295,383
Real estate - mortgage	37,899,222	35,828,254	28,794,030	30,324,415	27,784,873
Installment loans to individuals	15,173,427	13,569,093	12,565,675	11,309,245	14,926,017

Totals	\$ 245,638,722	\$ 230,310,857	\$ 199,160,445	\$ 164,147,155	\$ 162,436,178
--------	----------------	----------------	----------------	----------------	----------------

Total loans increased to \$245,638,722 at December 31, 2006, from \$230,310,857 at year-end 2005, an increase of \$15,327,865, or 6.66%. Commercial, financial and agricultural loans decreased to \$133,174,048 at year end 2006, from \$161,432,166 at December 31, 2005, a decrease of 17.50%. Real estate construction loans increased \$39,910,681, or 204.87% in 2006 to \$59,392,025 from \$19,481,344 in 2005. These large changes were primarily caused by the Bank's reclassification of certain loans in accordance with general guidance provided by regulators pertaining to Commercial Real Estate loan concentrations. Real estate mortgage loans increased \$2,070,968 in 2006, or 5.78% to \$37,899,222 from \$35,828,254 in 2005. Installment loans to individuals increased to \$15,173,427 at December 31, 2006, when compared to \$13,569,093 at year end 2005. The ratio of net loans to deposits and repurchase agreements on December 31, 2006 was 65.35%, as compared to 69.84% in 2005. The decrease in net loans to deposits and repurchase agreements ratio is due to an approximately \$40,000,000 increase in repurchase agreements and interest bearing deposits in the fourth quarter of 2006 by two major depositors. Management believes that this ratio will increase as the Bank's loan portfolio expands with the additions of new markets and other cyclical fluctuations of agricultural loans and public deposits.

Total loans increased to \$230,310,857 at December 31, 2005, from \$199,160,445 at year-end 2004, an increase of \$31,150,412, or 15.64%. Commercial, financial and agricultural loans increased to \$161,432,166 at year end 2005, from \$151,295,232 at December 31, 2004. Most of the increase can be attributed to commercial loans. The Bank has experienced most of this growth in its Baldwin County markets as its newer branches begin to mature. Real estate construction loans increased by \$12,975,836, or 199.46% in 2005 to \$19,481,344 from \$6,505,508 in 2004 in part due to the Bank's expanded construction loan activity in south Baldwin County. Real estate mortgage loans increased by \$7,034,224 in 2005, or 24.43% to \$35,828,254 from \$28,794,030 in 2004. Installment loans to individuals increased to \$13,569,093 at December 31, 2005, when compared to \$12,565,675 at year end 2004. The ratio of net loans to deposits and repurchase agreements on December 31, 2005 was 69.84%, as compared to 73.21% in 2004. The decrease in loan to deposits and repurchase agreements ratio was due to the increase in repurchase agreements and interest bearing deposits in 2005.

## 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. 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. Additionally, the Company requires cash for various operating needs including dividends to shareholders, the servicing of debt and general corporate expenses. The primary source of liquidity for the Company is dividends from the Bank.

Asset and liability management functions not only serve to assure adequate liquidity in order to meet the needs of the Bank's customers, but also to maintain an appropriate balance between interest-sensitive assets and interest-sensitive liabilities so that the Company can earn a return that meets the investment requirements of its shareholders. Daily monitoring of the sources and uses of funds is necessary to maintain an acceptable cash position that meets both requirements.

The asset portion of the balance sheet provides liquidity primarily through loan principal repayments, maturities of investment securities available for sale and, to a lesser extent, sales of investment securities available for sale. Other short-term investments such as federal funds sold, and securities purchased under agreements to resell, are additional sources of liquidity funding.

The liability portion of the balance sheet provides liquidity through various customers' interest bearing and noninterest bearing deposit accounts. Federal funds purchased, securities sold under agreements to repurchase and other short-term borrowings are additional sources of liquidity. The Bank utilizes this short-term financing and maintains a borrowing relationship with the Federal Home Loan Bank to provide liquidity. These sources of liquidity are short-term in nature and are used as necessary to fund asset growth and meet short-term liquidity needs.

The Corporation's bank subsidiary has an Asset Liability Committee, which has as its primary objective the maintenance of specific funding and investment strategies to achieve short-term and long-term financial goals. See ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

The Corporation generates the majority of its cash flows from financing activities. Financing activities provided \$52,890,542 in cash in 2006, with the majority of this coming from an increase in deposits and an increase in repurchase agreements. The investing activities of the Corporation used \$56,700,821 of the cash flows, to fund the investment portfolio, loan portfolios, and the purchases of premises and equipment of the Bank. Operations provided

\$4,147,682 in cash flows with the majority of these funds coming from net income for the year ended December 31, 2006.

The following table presents information about the Company's contractual obligations and commitments at December 31, 2006.

**CONTRACTUAL OBLIGATIONS**

(Dollars in Thousands)

	Less Than 1 Year	2-3 Years	4-5 Years	More Than 5 Years
Time Deposits	\$ 121,984	\$ 25,717	\$ 7,410	\$ -
FHLB Advances	-	-	-	6,940
Long-term debt	4,124	-	-	10,310
Operating Leases	10	4	-	-
Letters of Credit	3,151	82	-	-
Commitments to extend credit	27,439	4,216	817	922

The increase in the commitments to extend credit is primarily due to the increased volume of the loan portfolio including construction loans.

## OFF-BALANCE SHEET ARRANGEMENTS

To hedge the Company's exposure to changing interest rates, management entered into an agreement known as an interest rate floor on a portion of its variable rate loan portfolio during September 2005. Interest rate floors are typically used to mitigate a loan portfolio's exposure to falling interest rates. Pursuant to the agreement, the Company's counterparty agrees to pay the Company an amount equal to the difference between the prime rate and 5.75% multiplied by a \$35,000,000 notional amount should the prime rate fall below 5.75% during the two-year term of the agreement. The Company paid its counterparty a one-time premium of \$52,500 which will be amortized over the two-year term. The interest rate floor is being marked to market and accounted for as a cash flow hedge. As of December 31, 2006, the interest rate floor contract was carried at fair value of \$2,500. The Company considers the derivative (interest rate floor contract) as highly effective in offsetting changes in cash flows of the hedged items (variable rate loans).

The Bank is currently under contract to construct, or planning to construct two to three retail banking buildings in 2007 at an estimated cost of \$3,260,000. The Bank is also in negotiation to purchase a retail banking building in the Florida market at an approximate cost of \$2,040,000.

## INTEREST RATE SENSITIVITY\*

### Interest Rate Sensitivity Analysis

Year Ended December 31, 2006

(Dollars in Thousands)

	Ending Balances as of 12/31/06	Percent Change Interest Income/Expense	
		Down 200 Basis Points	Up 200 Basis Points
<b>Earning Assets:</b>			
Cash & Short-term Investments	31,645,717	-40.77%	40.84%
Investment securities, taxable	76,526,787	-12.15%	9.45%
Investment securities, tax-exempt	32,648,697	-8.86%	0.85%
Loans**	242,626,991	-15.97%	15.55%
<b>Total Assets</b>	<b>425,872,251</b>	<b>-16.62%</b>	<b>15.60%</b>
<b>Interest Bearing Liabilities:</b>			
Interest Bearing Deposits	106,731,616	0.00%	0.00%



Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Certificates of Deposit less than \$100,000	86,467,042	-21.81%	21.77%
Certificates of Deposit greater than \$100,000	68,643,776	-15.38%	18.87%
<b>Total Interest Bearing Deposits</b>	<b>261,842,434</b>	<b>-16.33%</b>	<b>16.31%</b>
Federal funds sold & securities			
Purchased under agreement to resale	44,410,101	-39.32%	38.20%
Federal Home Loan Bank borrowings	7,796,514	-3.94%	3.94%
<b>Total Purchased Funds</b>	<b>52,206,615</b>	<b>-34.00%</b>	<b>33.05%</b>
<b>Total Liabilities</b>	<b>385,892,431</b>	<b>-20.51%</b>	<b>20.27%</b>
<b>Net Interest Income</b>		<b>-13.66%</b>	<b>12.04%</b>

\*Information pertains to the Bank only

\*\* Includes interest rate floor contract

As shown in the table above, the Company is interest rate sensitive, especially in a downward rate environment. A 200 basis point decline in interest rates would cause a 14% decline in net interest income; while a similar increase in interest rates would yield only a 5% increase in net interest income. This effect is due to the Company's mix of variable and fixed rate loans, interest bearing deposits, and borrowed funds. In September 2005, the Company purchased an interest rate floor contract to mitigate interest income losses. See OFF- BALANCE SHEET ARRANGEMENTS above.

The Corporation's sensitivity to changes in interest rates in conjunction with the structure of interest rate spreads determines the impact of change in interest rates on the Bank's performance. See ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

## **CAPITAL RESOURCES**

The Corporation has historically relied primarily on internally generated capital growth to maintain capital adequacy. The average equity to average assets ratio during 2006 was 7.55% as compared to 8.02% in 2005. Total stockholders equity on December 31, 2006 was \$30,724,720, an increase of \$2,699,075, or 9.63%, from \$28,025,645 at year end 2005. This increase is the result of the Corporation's net earnings during 2006, less dividends declared to stockholders of \$668,118, less other comprehensive gain of \$36,821 as reflected in the Consolidated Statements of Stockholders Equity and Comprehensive Income. Stockholders' equity was increased by the amount paid on the exercise of stock options of \$135,390. The Corporation's risk based capital of \$47,285,965, or 16.40%, of risk weighted assets at December 31, 2006, was well above the Corporation's minimum risk based capital requirement of \$22,975,040 or 8.0% of risk weighted assets. Based on management's projections, internally generated capital should be sufficient to satisfy capital requirements for existing operations into the foreseeable future; however, continued growth into new markets may require the Bank to access external funding sources.

In March of 2005, the Federal Reserve issued a final rule providing for the inclusion of Trust Preferred securities in Tier 1 risk weighted capital, up to a limit of 25% of total Tier 1 capital. These securities comprised 25% of the Corporation's Tier 1 Capital as of December 31, 2006.

## **ITEM 7A. 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, do not generally arise in the Bank's normal course of business activities.

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 potential. 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 strategies and tactics for managing the rate and sensitivity re-pricing 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 re-pricing 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 prime rate. The Bank uses the asset liability model developed by HNC Financial Solutions, an independent third party vendor, which takes the current rate structure of the portfolio and shocks for each rate level and calculates the new market value of equity at each rate. 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 (fair value assets less fair value liabilities) for the various rate shock levels as of December 31, 2006. All market risk sensitive instruments presented in this table are held to maturity or available for sale. The Bank has no trading securities.

### MARKET VALUE OF EQUITY SHOCK TABLE

(In thousands)

Increase (Decrease) in Interest Rates (Basis Points)	Market Value Equity	Change in Market Value Equity	Change in Market Value Equity Percent
300	\$ 55,678	(2,037)	-4%
200	56,607	(1,108)	-2%
100	57,015	(700)	-1%
0	57,715	-	0%
(100)	57,001	(714)	-1%
(200)	55,557	(2,158)	-4%
(300)	53,580	(4,135)	-7%

The preceding table indicates that at December 31, 2006, in the event of an immediate and sustained increase or decrease in prevailing market interest rates, the Bank's NPV of equity would be expected to not materially decrease.

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. For more information on forward looking statements, see FORWARD LOOKING STATEMENTS above.



**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

The Corporation's consolidated financial statements as of December 31, 2006 and 2005 and for each of the years in the three-year period ended December 31, 2006 are included in the following pages shown in the index below.

<u>Index to Financial Statements</u>	<u>Page(s)</u>
Report of Independent Registered Public Accounting Firm	F1
Consolidated Balance Sheets as of December 31, 2006 and 2005	F2
Consolidated Statements of Operations for the years ended December 31, 2006, 2005, and 2004	F4
Consolidated Statements of Stockholders' Equity and Other Comprehensive Income for the years ended December 31, 2006, 2005, and 2004	F5
Consolidated Statements of Cash Flows for the years ended December 31, 2006, 2005, and 2004	F6
Notes to Consolidated Financial Statements - December 31, 2006, 2005, and 2004	F8

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**To the Board of Directors**

**United Bancorporation of Alabama, Inc.**

**Atmore, Alabama**

We have audited the accompanying consolidated balance sheets of **United Bancorporation of Alabama, Inc. and Subsidiary** as of December 31, 2006 and 2005 and the related consolidated statements of operations, stockholders' equity and comprehensive income and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provided a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of United Bancorporation of Alabama, Inc. and Subsidiary as of December 31, 2006 and 2005 and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2006, in conformity with U.S. generally accepted accounting principles.

/s/ Mauldin & Jenkins, LLC

Birmingham, Alabama

March 27, 2007

F-1

---



**CONSOLIDATED BALANCE SHEETS**

December 31, 2006 and 2005

<b>Assets</b>	<b>2006</b>	<b>2005</b>
Cash and due from banks	\$ 19,558,529	\$ 20,876,806
Interest bearing deposits in banks	31,645,717	23,665,037
Federal funds sold	-	6,325,000
Cash and cash equivalents	51,204,246	50,866,843
Securities available for sale, at fair value (amortized cost of \$109,175,484 and \$71,770,277 at December 31, 2006 and 2005, respectively)	108,410,473	70,932,624
Loans	245,638,722	230,310,857
Less: Allowance for loan losses	3,011,731	3,028,847
Net loans	242,626,991	227,282,010
Premises and equipment, net	11,796,175	9,849,934
Interest receivable	3,579,922	3,073,531
Intangible assets	917,263	917,263
Other assets	7,635,904	7,138,839
Total assets	\$ 426,170,974	\$ 370,061,044

See accompanying notes to consolidated financial statements

**CONSOLIDATED BALANCE SHEETS**

December 31, 2006 and 2005

<b>Liabilities and Stockholders' Equity</b>	<b>2006</b>	<b>2005</b>
Deposits:		
Non-interest bearing	\$ 64,993,029	\$ 66,774,418
Interest bearing	261,842,434	224,246,053
Total deposits	326,835,463	291,020,471
Securities sold under agreements to repurchase	44,410,101	34,429,374
Advances from Federal Home Loan Bank of Atlanta	6,939,500	9,112,915
Treasury, tax, and loan account	857,015	1,001,000
Accrued expenses and other liabilities	2,081,322	2,468,890
Notes payable to Trusts, net of debt issuance costs of \$111,147 and \$121,251 in 2006 and 2005, respectively	14,322,853	4,002,749
Total liabilities	395,446,254	342,035,399
Stockholders' equity:		
Class A common stock, \$0.01 par value. Authorized 5,000,000 shares; issued and outstanding, 2,375,471 and 2,363,762 shares in 2006 and 2005, respectively	23,755	23,669
Class B common stock, \$0.01 par value. Authorized 250,000 shares; no shares issued or outstanding	-	-
Preferred stock of \$.01 par value. Authorized 250,000 shares; no shares issued or outstanding	-	-
Additional paid in capital	5,673,088	5,445,822
Accumulated other comprehensive loss, net of tax	(475,478)	(512,299)
Retained earnings	26,341,116	23,874,164
	31,562,481	28,831,356
Less: 142,789 and 143,307 treasury shares, at cost, respectively	837,761	805,711
Total stockholders' equity	30,724,720	28,025,645
Total liabilities and stockholders' equity	\$ 426,170,974	\$ 370,061,044

See accompanying notes to consolidated financial statements

F-3

---

**CONSOLIDATED STATEMENTS OF OPERATIONS**

Years ended December 31, 2006, 2005, 2004

	<b>2006</b>		<b>2005</b>		<b>2004</b>
Interest income:					
Interest and fees on loans	\$ 20,814,959		\$ 15,786,028		\$ 11,979,772
Interest on investment securities available for sale:					
Taxable	2,095,191		1,821,861		1,223,185
Nontaxable	1,261,694		1,039,290		990,195
Total investment income	3,356,885		2,861,151		2,213,380
Other interest income	878,384		446,971		159,834
Total interest income	25,050,228		19,094,150		14,352,986
Interest expense:					
Interest on deposits	7,042,421		4,182,554		2,882,638
Interest on other borrowed funds	2,713,470		1,320,086		655,420
Total interest expense	9,755,891		5,502,640		3,538,058
Net interest income	15,294,337		13,591,510		10,814,928
Provision for loan losses	960,000		880,000		720,000
Net interest income after provision for loan losses	14,334,337		12,711,510		10,094,928
Noninterest income:					
Service charge on deposits	2,741,307		2,318,259		2,259,181
Commission on credit life	45,666		49,195		50,016
Investment securities gains (losses), net	(4,879)		33,916		170,898
Mortgage fee income	261,473		241,460		196,740
Other	868,646		493,321		368,083
Total noninterest income	3,912,213		3,136,151		3,044,918
Noninterest expense:					
Salaries and benefits	7,353,896		6,512,743		5,779,483
Net occupancy expense	2,368,030		2,023,492		1,988,538

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Other	4,366,672	3,376,458	2,605,966
Total noninterest expense	14,088,598	11,912,693	10,373,987
Earnings before income tax expense	4,157,952	3,934,968	2,765,859
Income tax expense	1,022,882	1,040,184	612,602
Net earnings	\$ 3,135,070	\$ 2,894,784	\$ 2,153,257
Basic earnings per share	\$ 1.41	\$ 1.30	\$ 0.97
Basic weighted average shares outstanding	2,225,269	2,220,553	2,216,032
Diluted earnings per share	\$ 1.40	\$ 1.30	\$ 0.97
Diluted weighted average shares outstanding	2,232,279	2,227,583	2,218,381

See accompanying notes to consolidated financial statements

**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME**  
Years ended December 31, 2006, 2005, and 2004

	Shares	Common stock	Additional paid in Capital	Retained earnings	Accumulated other comprehensive income (loss)	Treasury stock	Total stockholders' equity	Comprehensive Income
Balance December 31, 2003, as originally reported	1,181,881	\$ 11,819	\$ 5,418,175	\$ 19,925,926	\$ 454,671	\$ (841,654)	\$ 24,968,937	
Prior Period Adjustment (Note 24)				231,285			231,285	
Balance December 31, 2003, as restated	1,181,881	11,819	5,418,175	20,157,211	454,671	(841,654)	25,200,222	
Net earnings				2,153,257			2,153,257	\$ 2,153,257
Other comprehensive loss (Note 18)					(153,129)		(153,129)	(153,129)
Comprehensive Income								\$ 2,000,128
Stock Split Two for One	1,181,881	11,819	(11,819)				-	
Cash dividends declared (\$.30 per share)				(664,813)			(664,813)	
Purchase of Treasury Stock						(30,366)	(30,366)	
Sale of 2,339 shares of treasury stock			38,207			33,001	71,208	
Balance December 31, 2004	2,363,762	23,638	5,444,563	21,645,655	301,542	(839,019)	26,576,379	
Net earnings				2,894,784			2,894,784	\$ 2,894,784

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Other comprehensive loss (Note 18)					(813,841)		(813,841)	(813,841)
Comprehensive income								\$ 2,080,943
Cash dividends declared (\$.30 per share)				(666,275)			(666,275)	
Exercise of stock options	2,200	22	22,214				22,236	
Sale of common stock	909	9	12,353				12,362	
Treasury shares issued to dividend reinvestment plan			(33,308)		33,308		-	
Balance December 31, 2005	2,366,871	23,669	5,445,822	23,874,164	(512,299)	(805,711)	28,025,645	
Net earnings				3,135,070			3,135,070	\$ 3,135,070
Other comprehensive income (Note 18)					36,821		36,821	36,821
Comprehensive income								\$ 3,171,891
Cash dividends declared (\$.30 per share)				(668,118)			(668,118)	
Exercise of stock options	8,600	86	135,304				135,390	
Tax benefit from exercise of stock options			8,701				8,701	
Purchase of treasury shares						(63,750)	(63,750)	
Treasury shares issued to dividend reinvestment plan			64,864			31,700	96,564	
Stock-based compensation			18,397				18,397	
Balance December 31,	2,375,471	\$ 23,755	\$ 5,673,088	\$ 26,341,116	\$ (475,478)	\$ (837,761)	\$ 30,724,720	

2006

See accompanying notes to consolidated financial statements

F-5

---



**CONSOLIDATED STATEMENTS OF CASH FLOWS**

Years ended December 31, 2006, 2005, and 2004

	<b>2006</b>		<b>2005</b>		<b>2004</b>
Cash flows from operating activities					
Net earnings	\$ 3,135,070		\$ 2,894,784		\$ 2,153,257
Adjustments to reconcile net earnings to net cash provided by operating activities					
Provision for loan losses	960,000		880,000		720,000
Depreciation of premises and equipment	1,217,193		908,320		858,498
Net amortization of premium on investment securities	72,812		185,936		168,199
(Gains) losses on sales of investment securities available for sale, net	4,879		(33,916)		(170,898)
Loss (gain) on sale of other real estate	(12,501)		2,666		(897)
Writedown of other real estate	278,100		128,201		50,000
Stock-based compensation	18,397		-		-
Gain on disposal of equipment	(3,987)		-		(4,850)
Deferred income taxes	238,646		(384,025)		(58,147)
Increase in interest receivable	(506,390)		(361,837)		(632,804)
Increase in other assets	(877,072)		(749,414)		(2,943,919)
Increase in accrued expenses and other liabilities	(377,464)		1,282,803		1,667,234
Net cash provided by operating activities	4,147,682		4,753,518		1,805,673
Cash flows from investing activities					
Proceeds from maturities, calls, and principal repayments of investment securities available for sale	8,615,708		10,080,772		10,757,098
Proceeds from sales of investment securities available for sale	1,743,150		2,827,009		4,877,992
Purchases of investment securities available for sale	(47,832,178)		(30,327,665)		(17,225,998)

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Net increase in loans	(16,544,981)	(31,663,804)	(35,588,112)
Purchases of premises and equipment, net	(3,192,253)	(3,572,323)	(469,311)
Proceeds from sale of premises and equipment	24,832	-	4,850
Proceeds from sale of other real estate	484,901	221,363	5,000
Net cash used in investing activities	\$ (56,700,821)	\$ (52,434,648)	\$ (37,638,481)
Cash flows from financing activities			
Net increase in deposits	\$ 35,814,992	\$ 38,081,804	\$ 53,533,085
Net increase in securities sold under agreements to repurchase	9,980,727	16,048,311	4,885,393
Cash dividends	(668,118)	(666,275)	(664,813)
Issuance of common stock	135,390	34,598	-
Tax benefit from exercise of stock options	8,701	-	-
Purchase of treasury stock	(63,750)	-	(30,366)
Proceeds from sale of treasury stock	-	-	71,208
Advances from FHLB Atlanta	5,000,000	9,970,000	-
Proceeds from Trust Preferred issuance	10,000,000	-	-
Repayments of advances from FHLB Atlanta	(7,173,415)	(9,149,697)	(2,617,363)
Increase (decrease) in other borrowed funds	(143,985)	288,232	149,039
Net cash provided by financing activities	52,890,542	54,606,973	55,326,183
Net increase in cash and cash equivalents	337,403	6,925,843	19,493,375
Cash and cash equivalents, beginning of year	50,866,843	43,941,000	24,447,625
Cash and cash equivalents, end of year	\$ 51,204,246	\$ 50,866,843	\$ 43,941,000
Supplemental disclosures			
Cash paid during the year for:			
Interest	\$ 9,414,207	\$ 5,276,123	\$ 3,492,119
Income taxes	1,564,073	1,250,000	650,000

Noncash transactions

Transfer of loans to other real estate through foreclosure	240,000	100,000	301,001
--	---------	---------	---------

See accompanying notes to consolidated financial statements

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

**(1)**

**Summary of Significant Accounting Policies**

*(a)*

***Principles of Consolidation***

The accompanying consolidated financial statements include the financial statements of United Bancorporation of Alabama, Inc. (the Company) and its wholly owned subsidiary United Bank (the Bank), collectively referred to as the Company. Significant inter-company balances and transactions have been eliminated in consolidation.

*(b)*

***Market Concentrations***

The Company operates primarily in one business segment, commercial banking, in Southwest Alabama and Northwest Florida.

*(c)*

***Basis of Presentation***

The consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America. In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the balance sheet and revenues and expenses for the period. Actual results could differ significantly from those estimates.

Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the allowance for loan losses. In connection with the determination of the allowance for loan losses, management obtains independent appraisals for significant properties.

Management believes the allowance for losses on loans is appropriate. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary based on changes in economic conditions, particularly in Southwest Alabama and Northwest Florida. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for losses on loans. Such

agencies may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

(d)

***Cash Equivalents***

The Company considers due from banks and federal funds sold to be cash equivalents. Federal funds are generally sold for one day periods.

(e)

***Investment Securities***

Investment securities are classified in one of three portfolios: (i) trading account securities, (ii) held to maturity securities, and (iii) securities available for sale. Trading account securities are stated at fair value. Investment securities held to maturity are stated at cost adjusted for amortization of premiums and accretion of discounts. Investment securities available for sale are stated at fair value with any unrealized gains and losses reported in a separate component of stockholders' equity, net of tax effect, until realized. Once realized, gains and losses on investment securities available for sale are reflected in current period earnings. As of December 31, 2006 and 2005, all investment securities were classified as available for sale.

Net gains and losses on the sale of investment securities available for sale, computed on the specific identification method, are shown separately in noninterest income in the consolidated statements of operations. Accretion of discounts and amortization of premiums are calculated on the effective interest method over the anticipated life of the security.

A decline in the fair value of any security below amortized cost that is deemed other than temporary is charged to income resulting in the establishment of a new cost basis for the security or the securities call date, whichever comes first.

(f)

***Loans***

Interest income on loans is credited to earnings based on the principal amount outstanding at the respective rate of interest. Accrual of interest on loans is discontinued when a loan becomes contractually past due by 90 days or more with respect to interest or principal. When a loan is placed on nonaccrual status, all interest previously accrued, but not

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

collected, is charged against current period interest income. Income on such loans is then recognized only to the extent that cash is received and where the future collection of principal is probable. Interest accruals are recorded on such loans only when they are brought fully current with respect to interest and principal and when, in the judgment of management, the loans are estimated to be fully collectible as to both principal and interest.

As of December 31, 2006 and December 31, 2005, approximately 61% and 55%, respectively, of the Company's loans were commercial loans. The Company's commercial customers are primarily small to middle market enterprises. The Company also specializes in agricultural loans, which represented approximately 15% of the Company's total loans at both December 31, 2006 and December 31, 2005, respectively.

(g)

***Allowance for Loan Losses***

Management considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. When a loan is considered impaired, the amount of impairment is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate. If the loan is collateral dependent, the fair value of the collateral is used to determine the amount of impairment. Impairment losses are included in the allowance for loan losses through a charge to the provision for loan losses. Impaired loans are charged off against the allowance when such loans are deemed to be uncollectible. Subsequent recoveries are added to the allowance.

When a loan is considered impaired, cash receipts are applied under the contractual terms of the loan agreement, first to principal and then to interest income. Once the recorded principal balance has been reduced to zero, future cash receipts are recognized as interest income, to the extent that any interest has not been recognized. Any further cash receipts are recorded as recoveries of any amount previously charged off.

A loan is also considered impaired if its terms are modified in a troubled debt restructuring. For those accruing impaired loans, cash receipts are typically applied to principal and interest receivable in accordance with the terms of the restructured loan agreement. Interest income is recognized on these loans using the accrual method of accounting.

The ultimate ability to collect a substantial portion of the Company's loan portfolio is susceptible to changes in economic and market conditions in the geographic area served by the Company and various other factors.

Additions to the allowance for loan losses are based on management's evaluation of the loan portfolio under current economic conditions, past loan loss experience and such other factors, which, in management's judgment, deserve recognition in estimating loan losses. Loans are charged off when, in the opinion of management, such loans are deemed to be uncollectible. Subsequent recoveries are added to the allowance.

*(h)*

***Premises and Equipment***

Land is carried at cost. Premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed using the straight line method over the estimated useful lives of the assets.

F-8

---

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

(i)

***Other Real Estate***

Other real estate represents property acquired through foreclosure or deeded to the Company in lieu of foreclosure on real estate mortgage loans on which borrowers have defaulted. Other real estate is carried in other assets at the lower of cost or fair value, adjusted for estimated selling costs. Reductions in the balance of other real estate at the date of foreclosure are charged to the allowance for loan losses. Subsequent valuation decreases in the carrying value of other real estate as well as costs to carry other real estate are recognized as charges to noninterest expense. As of December 31, 2006 and 2005, the Company had \$620,776 and \$1,131,276, respectively, in other real estate.

(j)

***Intangible Assets***

Intangible assets represent purchased assets that lack physical substance but can be identified because of contractual or other legal rights. Under the provisions of SFAS No. 142, intangible assets with indefinite useful lives are not amortized, but instead are tested for impairment at least annually. Intangible assets that have finite lives are amortized over their estimated useful lives and are also subject to impairment testing. The Company's intangible asset has an indefinite useful life and is not subject to amortization. Note 6 includes a summary of the Company's intangible asset.

(k)

***Income Taxes***

The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

(l)

***Stock Option Plan***

At December 31, 2006, the Company had a stock option plan, which is described more fully in Note 12 to the Consolidated Financial Statements in this annual report. Effective January 1, 2006, the Company adopted SFAS



No. 123 (revised), Share-Based Payment ( SFAS 123R ) utilizing the modified prospective approach. Prior to the adoption of SFAS 123R the Company accounted for stock option grants in accordance with the Accounting Principles Board ( APB ) Opinion No. 25, Accounting for Stock Issued to Employees (the intrinsic value method), and accordingly recognized no compensation expense for stock option grants.

Under the modified prospective approach, SFAS 123R applies to new awards and to awards that were outstanding on January 1, 2006 that are subsequently modified, repurchased or cancelled. Under the modified prospective approach, compensation cost recognized during 2006 includes compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of SFAS 123, and compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of SFAS 123R. Prior periods were not restated to reflect the impact of adopting the new standard.

As a result of adopting SFAS 123R on January 1, 2006, income before taxes and net income for the year ended December 31, 2006, were \$18,397 and \$11,610, lower than if the Company had continued to account for stock-based compensation under APB opinion No. 25 for our stock option grants. The effect of adopting this standard on our earnings per share was not significant.

The following table provides pro forma net income and earnings per share information, as if the Company had applied the fair value recognitions provisions of SFAS No. 123, Accounting for Stock Based Compensation ( SFAS 123 ) to stock-based employee compensation option plans for the two years ended December 31, 2005:

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004**

	<b>2005</b>		<b>2004</b>
Reported net earnings	\$ 2,894,784	\$	2,153,257
Deduct:			
Total stock-based compensation expense determined under fair value based method			
for all option awards, net of tax			
Pro forma net earnings	2,870,899		2,131,999
Reported basic earnings per share	1.30		0.97
Proforma basic earnings per share	1.29		0.96
Reported diluted earnings per share	1.30		0.97
Pro forma diluted earnings per share	1.29		0.96

Prior to the adoption of Statement 123(R), the Company would have presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the statement of cash flows. Statement 123(R) requires the cash flows resulting from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows.

*(m)****Earnings per Share***

Basic and diluted earnings per share are computed on the weighted average number of shares outstanding in accordance with SFAS No. 128, Earnings Per Share. Note 13 provides additional disclosure information regarding earnings per share.

*(n)****Business Segments***

SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, establishes standards for the disclosures 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 Company operates in only one segment – commercial banking.

(o)

***Derivative Financial Instruments***

The Company maintains an overall interest-rate risk management strategy that incorporates the use of derivative instruments to minimize significant unplanned fluctuations in earnings that are caused by interest-rate volatility. The Company's goal is to manage interest-rate sensitivity by modifying the repricing or maturity characteristics of certain balance sheet assets and liabilities so that the net interest margin is not, on a material basis, adversely affected by movements in interest rates. As a result of interest-rate fluctuations, hedged assets and liabilities will appreciate or depreciate in market value. The effect of this unrealized appreciation or depreciation will generally be offset by income or loss on the derivative instruments that are linked to the hedged assets and liabilities. The Company views this strategy as a prudent management of interest-rate sensitivity, such that earnings are not exposed to undue risk presented by changes in interest rates.

All derivatives are recognized on the balance sheet at their fair value. Derivative instruments that are used as part of the Company's interest-rate risk management strategy include interest rate floors. An interest rate floor will convert variable interest rates on a portion of the Company's variable rate loan portfolio to fixed interest rates should interest rates fall below a specified level. On the date the interest rate floor contract is entered into, the Company designates the derivative as a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability "cash flow" hedge. Changes in the fair value of a derivative that is highly effective as - and that is designated and qualifies as - a cash-flow hedge are recorded in other comprehensive income, until earnings are affected by the variability of cash flows (e.g., when periodic settlements on a variable-rate asset or liability are recorded in earnings).

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk-management objective and strategy for undertaking various hedged transactions. This process includes linking all derivatives that are designated as cash-flow hedges to specific assets and liabilities on the balance sheet or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

derivatives that are used in hedging transactions are highly effective in offsetting changes in cash flows of hedged items. Note 23 includes a summary of the Company's derivative instruments.

(p)

***Recent Accounting Pronouncements***

In February 2006, the FASB issued SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments* an amendment of FASB Statements No. 133 and 140. This Statement amends SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*. This Statement resolves issues addressed in SFAS No. 133 Implementation Issue No. D1, *Application of Statement 133 to Beneficial Interests in Securitized Financial Assets*. SFAS 155 permits fair value re-measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation, clarifies which interest only-strips and principal-only strips are not subject to the requirements of Statement 133, establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation, clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives, and amends SFAS No. 140 to eliminate the prohibition on a qualifying special purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006. The Corporation does not believe that the adoption of SFAS No. 155 will have a material impact on its financial position, results of operations and cash flows.

In March 2006, the FASB issued SFAS No. 156, *Accounting for Servicing of Financial Assets* an amendment of FASB Statement No. 140. This Statement amends FASB No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, with respect to the accounting for separately recognized servicing assets and servicing liabilities. SFAS No. 156 requires an entity to recognize a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract; requires all separately recognized servicing assets and servicing liabilities to be initially measured at fair value, if practicable; permits an entity to choose its subsequent measurement methods for each class of separately recognized servicing assets and servicing liabilities; at its initial adoption, permits a one-time reclassification of available-for-sale securities to trading securities by entities with recognized servicing rights, without calling into question the treatment of other available-for-sale securities under Statement 115, provided that the available-for-sale securities are identified in some manner as offsetting the entity's exposure to changes in fair value of servicing assets or servicing liabilities that a service elects to subsequently measure at fair value; and requires separate presentation of servicing assets and servicing liabilities subsequently measured at fair value in the statement of financial position and additional disclosures for all separately recognized servicing assets and servicing liabilities. An entity should adopt SFAS No. 156 as of the beginning of its first fiscal year that begins after September 15, 2006. The Corporation does not believe the adoption of SFAS No. 156 will have a material impact on its financial position, results of operations and

cash flows.

F-11

---

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

In July 2006, the FASB issued FASB Interpretation No. 48 ( FIN 48 ), Accounting for Uncertainty in Income Taxes. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in enterprises' financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement attributable for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosures and transitions. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Corporation is currently analyzing the effects of FIN 48 on its financial position, results of operations and cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This standard does not require any new fair value measurements, but rather eliminates inconsistencies found in various prior pronouncements. SFAS 157 is effective for us on January 1, 2008 and is not expected to have a significant impact on its financial statements.

In September, 2006, The FASB ratified the consensuses reached by the FASB's Emerging Issues Task Force ( EITF ) relating to EITF 06-4 Accounting for the Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements. EITF 06-4 addresses employer accounting for endorsement split-dollar life insurance arrangements that provide a benefit to an employee that extends to postretirement periods should recognize a liability for future benefits in accordance with SFAS No. 106, Employers' Accounting for Postretirement Benefits Other Than Pensions, or APB Opinion No. 12, Omnibus Opinion 1967. EITF 06-4 is effective for fiscal years beginning after December 15, 2006. Entities should recognize the effects of applying this Issue through either (a) a change in accounting principle through a cumulative-effect adjustment to retained earnings or to other components of equity or net assets in the statement of financial position as of the beginning of the year of adoption or (b) a change in accounting principle through retrospective application to all prior periods. The Corporation is currently analyzing the effect of adoption of EITF 06-4 on its financial position, results of operations and cash flows.

In September 2006, the FASB ratified the consensus reached related to EITF 06-5, Accounting for Purchases of Life Insurance Determining the Amount That Could Be Realized in Accordance with FASB Technical Bulletin No. 85-4, Accounting for Purchases of Life Insurance. EITF 06-5 states that a policyholder should consider any additional amounts included in the contractual terms of the insurance policy other than the cash surrender value in determining the amount that could be realized under the insurance contract. EITF 06-5 also states that a policyholder should determine the amount that could be realized under the life insurance contract assuming the surrender of an individual-life by individual-life policy (or certificate by certificate in a group policy). EITF 06-5 is effective for fiscal years beginning after December 15, 2006. The Corporation is currently analyzing the effect of adoption of EITF 06-5 on its financial position, results of operations and cash flows.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies are not expected to have a material impact on its financial position, results of operations and cash flows

(q)

***Reclassifications***

Certain items on the consolidated balance sheets for the year ended December 31, 2005 have been reclassified, with no effect on total assets, to be consistent with the classifications adopted for the year ended December 31, 2006.

(2)

**Cash and Due From Banks**

The Bank is required by the Federal Reserve Bank to maintain daily cash balances. These balances were \$2,984,000 and \$3,144,000 at December 31, 2006 and 2005, respectively.

(3)

**Investment Securities**

The amortized cost and fair value of investment securities available for sale at December 31, 2006 and 2005 were as follows:

**Gross                      Gross**

## UNITED BANCORPORATION OF ALABAMA, INC.

## AND SUBSIDIARY

## Notes to Consolidated Financial Statements

December 31, 2006, 2005, and 2004

	Amortized cost	unrealized gains	unrealized losses	Fair value
2006:				
U.S. government sponsored agencies, excluding mortgage backed securities	\$ 55,111,730	\$ 49,238	\$ (268,097)	\$ 54,892,871
State and political subdivisions	32,648,697	232,723	(230,686)	32,650,734
Mortgage backed securities	21,415,057	14,215	(562,404)	20,866,868
	\$ 109,175,484	\$ 296,176	\$ (1,061,187)	\$ 108,410,473
2005:				
U.S. government sponsored agencies, excluding mortgage backed securities	\$ 19,103,350	\$ 692	\$ (212,561)	\$ 18,891,481
State and political subdivisions	28,894,269	266,059	(313,135)	28,847,193
Mortgage backed securities	23,772,658	23,699	(602,407)	23,193,950
	\$ 71,770,277	\$ 290,450	\$ (1,128,103)	\$ 70,932,624

The FASB Emerging Issues Task Force Issue 03-01, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* requires disclosure of certain information about other than temporary impairments in the market value of securities. Management evaluates securities for other-than-temporary impairment at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Those investment securities which have an unrealized loss position at December 31, 2006 and 2005, are detailed below:



2006 Description of Securities	Less than 12 months		12 months or more		Total	
	Fair Value	Unrealized losses	Fair Value	Unrealized losses	Fair Value	Unrealized losses
U.S. Government sponsored agencies & mortgage-backed securities	\$ 11,416,997	\$ 100,759	\$ 32,802,651	\$ 729,742	\$ 44,219,648	\$ 830,501
State and political subdivisions	6,115,311	57,643	10,235,173	173,043	16,350,484	230,686
Total temporarily impaired securities	\$ 17,532,308	\$ 158,402	\$ 43,037,824	\$ 902,785	\$ 60,570,132	\$ 1,061,187

## 2005

## Description of Securities

U.S. Government sponsored agencies & mortgage-backed securities	\$ 25,507,595	\$ 392,119	\$ 13,068,556	\$ 422,849	\$ 38,576,151	\$ 814,968
State and political subdivisions	8,702,524	121,505	6,718,553	191,630	15,421,077	313,135
Total temporarily impaired securities	\$ 34,210,119	\$ 513,624	\$ 19,787,109	\$ 614,479	\$ 53,997,228	\$ 1,128,103

In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies has occurred, and industry analysts' reports.

As management has the ability to hold debt securities until maturity, or for the foreseeable future if classified as available for sale, no declines are deemed to be other than temporary.

The amortized cost and fair value of investment securities available for sale at December 31, 2006, categorized by contractual maturity are shown below. Expected maturities may differ from contractual maturities for mortgage-backed securities because borrowers may have the right to call or prepay obligations with or without prepayment penalties. Therefore, these securities are not presented by maturity class in the following table.



## UNITED BANCORPORATION OF ALABAMA, INC.

## AND SUBSIDIARY

## Notes to Consolidated Financial Statements

December 31, 2006, 2005, and 2004

		<b>Amortized cost</b>		<b>Fair value</b>
Investment securities available for sale:				
Due in one year or less	\$	30,048,700	\$	30,024,455
Due after one year through five years		18,037,958		17,858,237
Due after five years through ten years		24,192,084		24,226,434
Due after ten years		15,481,685		15,434,479
Subtotal		87,760,427		87,543,605
Mortgage backed securities		21,415,057		20,866,868
Total	\$	109,175,484	\$	108,410,473

Gross gains of \$3,886 and gross losses of \$8,765 were realized on sales of investment securities available for sale in 2006. Gross gains of \$49,364 and gross losses of \$15,448 were realized on sales of investment securities available for sale in 2005. Gross gains of \$170,898 were realized on sales of investment securities available for sale in 2004.

Securities with carrying values of approximately \$69,210,000 and \$55,360,000 at December 31, 2006 and 2005, respectively, were pledged to secure public and trust deposits as required by law and for other purposes.

(4)

**Loans and Allowance for Loan Losses**

At December 31, 2006 and 2005, the composition of the loan portfolio was as follows:

		<b>2006</b>		<b>2005</b>
Commercial and financial	\$	96,236,431	\$	126,024,692
Agricultural		36,937,617		35,407,474

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Real estate - construction	59,392,025	19,481,344
Real estate - 1 - 4 family residential mortgage	37,899,222	35,828,254
Installment loans to individuals	15,173,427	13,569,093
Total	\$ 245,638,722	\$ 230,310,857

A summary of the transactions in the allowance for loan losses for the years ended December 31, 2006, 2005, and 2004 follows:

	2006	2005	2004
Balance, beginning of year	\$ 3,028,847	\$ 2,562,239	\$ 2,116,060
Provision charged to earnings	960,000	880,000	720,000
Less loans charged off	(1,157,350)	(472,735)	(357,734)
Plus loan recoveries	80,185	59,343	83,913
Net charge offs	(1,077,166)	(413,392)	(273,821)
Other adjustments	100,050	-	-
Balance, end of year	\$ 3,011,731	\$ 3,028,847	\$ 2,562,239

Impaired loans, which consist of loans on which the accrual of interest had been discontinued or reduced totaled \$1,766,960 and \$1,406,422 as of December 31, 2006 and 2005, respectively. The average amount of impaired loans for the year 2006, 2005, and 2004 totaled approximately, \$2,477,000, \$1,450,000, and \$1,623,000, respectively. If these loans had been current throughout their terms, interest income would have been increased by \$123,917, \$165,159, and \$102,372, for 2006, 2005, and 2004, respectively. At December 31, 2006 and 2005, the Company had no other significant impaired loans.

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004**

During 2006, certain executive officers and directors of the Company, including their immediate families and companies with which they are associated, were loan customers of the Bank. Total loans outstanding and available lines of credit to these related parties at December 31, 2006 and 2005, totaled \$6,583,666 and \$4,923,443, respectively. Such loans are made in the ordinary course of business at normal credit terms, including interest rate and collateral requirements, and do not represent more than a normal credit risk.

**(5)****Premises and Equipment**

At December 31, 2006 and 2005, premises and equipment were as follows:

	<b>2006</b>		<b>2005</b>
Land	\$ 3,341,231	\$	2,365,033
Buildings and leasehold improvements (depreciated over 5 to 50 years)	9,341,067		6,788,752
Furniture, fixtures, and equipment (depreciated over 3 to 10 years)	6,727,116		5,234,311
Automobiles (depreciated over 3 years)	106,024		108,034
Construction in process	88,986		2,170,743
	19,604,424		16,666,873
Less accumulated depreciation	7,808,249		6,816,939
	\$ 11,796,175	\$	9,849,934

The balance of construction in process is associated with building projects that are in process, but are not complete, and are anticipated to cost approximately \$3,260,000. The Company is also in the process of negotiating the purchase of a third branch location in its Florida market for an estimated \$2,040,000.

Depreciation expense for the year ended December 31, 2006, 2005, and 2004 was \$1,217,193, \$908,320, and \$858,498, respectively.

**(6)****Intangible Assets**

On July 2, 2004, the Company acquired a State of Florida banking charter from a financial institution. Subsequent to

the purchase, the charter was terminated but the Company retained the legal right to branch into Florida through its existing Alabama bank charter. The Company accounts for the charter cost as an indefinite lived intangible asset because the legal right acquired does not have an expiration date under Florida banking laws and there is no renewal process to keep the branching rights. The Company tests the intangible asset each September 30 for impairment. At December 31, 2006, the Company operates two branch offices in Florida.

For the years ended December 31, 2006 and 2005, no impairment was recorded related to the intangible asset. As of December 31, 2006 and 2005, the Company had recorded \$917,263 in intangible assets related to the cost of the charter.

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004**

(7)

**Deposits**

At December 31, 2006 and 2005, deposits were as follows:

	<b>2006</b>		<b>2005</b>
Noninterest bearing accounts	\$ 64,993,029	\$	66,774,418
NOW accounts	68,550,299		55,954,938
Money market investment accounts	19,554,738		13,172,550
Savings account	18,626,579		22,712,909
Time deposits:			
Time deposits less than \$100,000	86,467,042		81,744,612
Time deposits greater than \$100,000	68,643,776		50,661,044
Total deposits	\$ 326,835,463	\$	291,020,471

At December 31, 2006, 2005, and 2004 interest expense on deposits was as follows:

	<b>2006</b>	<b>2005</b>	<b>2004</b>
NOW accounts	\$ 704,904	\$ 368,886	\$ 208,816
Money market investment accounts	438,237	313,329	315,353
Savings accounts	53,401	62,313	52,534
Time deposits:			
Time deposit less than \$100,000	4,104,442	2,285,009	1,718,198
Time deposit greater than \$100,000	1,741,437	1,153,017	587,738
Total interest expense on deposits	\$ 7,042,421	\$ 4,182,554	\$ 2,882,639

At December 31, 2006, the contractual maturities of time deposits are as follows:

Due in one year	\$ 121,983,918
-----------------	----------------

Due in one to two years	18,687,946
Due in two to three years	7,028,789
Due in three to four years	3,483,909
Due in four to five years	3,926,256
	\$ 155,110,818

During 2006, certain executive officers and directors of the Company were deposit customers of the Bank. Total deposits outstanding to these related parties at December 31, 2006, amounted to \$2,269,795.

**(8)**

#### **Securities Sold Under Agreements to Repurchase**

The maximum amount of outstanding securities sold under agreements to repurchase during 2006 and 2005 was \$49,918,476 and \$37,635,628, respectively. The weighted average borrowing rate at December 31, 2006 and 2005 was 4.17% and 3.14%, respectively. The average amount of outstanding securities sold under agreements to repurchase during 2006, 2005 and 2004 was \$41,745,119, \$27,580,131, and \$17,147,605 respectively. The weighted average borrowing rate during the years ended December 31, 2006, 2005, and 2004 was 3.98%, 2.30%, and 0.46% respectively. Securities underlying these agreements are under the Company's control.

F-16

---



**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004****(9)****Borrowed Funds**

The Company owed the Federal Home Loan Bank of Atlanta the following advances at December 31, 2006 and 2005.

<b>Maturity date</b>	<b>Interest rate</b>		<b>2006</b>
May 2012	7.41%	\$	64,534
April 2013	4.53%		5,000,000
July 2017	6.93%		715,000
August 2017	6.84%		117,175
June 2020	4.62%		873,000
July 2020	7.54%		169,791
Total (weighted average rate of 4.92%)		\$	6,939,500

  

<b>Maturity date</b>	<b>Interest rate</b>		<b>2005</b>
June 2006	7.19%	\$	8,615
September 2010	4.02%		5,000,000
March 2011	4.22%		2,000,000
May 2012	7.41%		76,267
July 2017	6.93%		780,000
August 2017	6.84%		128,075
June 2020	4.62%		937,667
July 2020	7.54%		182,291
Total (weighted average rate of 4.52%)		\$	9,112,915

At December 31, 2006 and 2005, the advances were collateralized by a blanket pledge of first mortgage residential loans with available collateral amounts of \$5,047,238 and \$24,667,809, respectively. At December 31, 2006 the Company's advances were also collateralized by Commercial Real Estate loans, Multi Family Real Estate loans, and Home Equity Lines of Credit with available collateral amounts of \$8,792,909, \$1,372,239, and \$3,835,868 respectively.

As of December 31, 2006, the Company had additional outstanding credit facilities with the Federal Home Loan Bank of Atlanta totaling \$20,000,000 in the form of letters of credit that mature in 2007. The letters of credit are collateralized by \$15,000,000 in deposits at the Federal Home Loan Bank of Atlanta. No amounts have been drawn on these letters of credit during 2006.

**(10)**

**Notes Payable to Trust**

*(a)*

***United Bancorp Capital Trust I***

In 2002, the Company formed a wholly-owned grantor trust to issue cumulative trust preferred securities. The grantor trust has invested the proceeds of the trust preferred securities in junior subordinated debentures of the Company. The junior subordinated debentures can be redeemed prior to maturity at the option of the Company on any interest payment date after June 30, 2007. The sole assets of the guarantor trust are the Junior Subordinated Deferrable Interest Debentures of the Company (the Debentures) held by the grantor trust. The debentures have the same interest rate (three month LIBOR plus 3.65%, floating) as the trust preferred securities. The Company has the right to defer interest payments on the Debentures at any time or from time to time for a period not exceeding 20 consecutive quarters provided that no extension period may extend beyond the stated maturity of the related Debentures. During any such extension period, distributions on the trust preferred certificates would also be deferred.

Payment of periodic cash distributions and payment upon liquidation or redemption with respect to the trust preferred securities are guaranteed by the Company to the extent of funds held by the grantor trust (the Preferred Securities Guarantee). The Preferred Securities Guarantee, when taken together with the Company's other obligations under the Debentures, constitute a full and unconditional guarantee, on a subordinated basis, by the Company of payments due on the trust preferred securities.

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

The trust preferred securities and the related debentures were issued on June 27, 2002. Distributions on the trust preferred securities are paid quarterly on March 31, June 30, September 30 and December 31 of each year. Interest on the Debentures is paid on the corresponding dates. The aggregate principal amount of Debentures outstanding at December 31, 2006 and 2005 was \$4,124,000. Certain issue costs have been deferred and netted against the outstanding debentures in the accompanying balance sheet. The issue costs are being amortized over fifteen years.

*(b)*

***United Bancorp Capital Trust II***

In 2006, the Company formed a wholly-owned grantor trust to issue cumulative trust preferred securities. The grantor trust has invested the proceeds of the trust preferred securities in junior subordinated debentures of the Company. The junior subordinated debentures can be redeemed prior to maturity at the option of the Company on or after September 30, 2011. The sole assets of the guarantor trust are the Junior Subordinated Deferrable Interest Debentures of the Company (the Debentures) held by the grantor trust. The debentures have the same interest rate (three month LIBOR plus 1.68%, floating) as the trust preferred securities. The Company has the right to defer interest payments on the Debentures at any time or from time to time for a period not exceeding 20 consecutive quarters provided that no extension period may extend beyond the stated maturity of the related Debentures. During any such extension period, distributions on the trust preferred certificates would also be deferred.

Payment of periodic cash distributions and payment upon liquidation or redemption with respect to the trust preferred securities are guaranteed by the Company to the extent of funds held by the grantor trust (the Preferred Securities Guarantee). The Preferred Securities Guarantee, when taken together with the Company's other obligations under the Debentures, constitute a full and unconditional guarantee, on a subordinated basis, by the Company of payments due on the trust preferred securities.

The trust preferred securities and the related debentures were issued on September 27, 2006. Distributions on the trust preferred securities are paid quarterly on March 31, June 30, September 30 and December 31 of each year. Interest on the Debentures is paid on the corresponding dates. The aggregate principal amount of Debentures outstanding at December 31, 2006 was \$10,310,000.

**(11)**

**Income Taxes**

The components of income tax expense for the years ended December 31, 2006, 2005, and 2004 are as follows:

<b>2006</b>	<b>2005</b>	<b>2004</b>
-------------	-------------	-------------

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Current:				
Federal	\$	736,312	1,254,044	560,929
State		47,924	170,165	109,820
Total		784,236	1,424,209	670,749
Deferred:				
Federal		174,232	(336,686)	(40,622)
State		64,414	(47,339)	(17,525)
Total		238,646	(384,025)	(58,147)
Total income tax expense	\$	1,022,882	1,040,184	612,602

F-18

---

## UNITED BANCORPORATION OF ALABAMA, INC.

## AND SUBSIDIARY

## Notes to Consolidated Financial Statements

December 31, 2006, 2005, and 2004

Total income tax expense differed from the amount computed by applying the statutory federal income tax rate of 34% to pretax earnings as follows:

	<b>2006</b>	<b>2005</b>	<b>2004</b>
Income tax at statutory rate	\$ 1,413,704	1,337,889	940,392
Increase (decrease) resulting from:			
Tax exempt interest	(471,962)	(412,592)	(377,744)
Interest disallowance	55,465	30,556	20,468
State income tax net of federal benefit	74,143	81,065	60,915
Premium amortization on tax exempt investment securities	21,892	20,928	11,910
Cash surrendered value of life insurance	(29,165)	(29,527)	(31,030)
GoZone tax credits	(30,032)	-	-
Other, net	(11,163)	11,865	(12,309)
	\$ 1,022,882	1,040,184	612,602

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at December 31, 2006 and 2005 are as follows:

	<b>2006</b>	<b>2005</b>
Deferred tax assets:		
Loans, principally due to the allowance for loan losses	\$ 809,953	831,582
Other real estate, principally due to differences in carrying value	3,874	62,796
Accrued expenses	160,604	132,054
Investment securities available for sale	306,000	335,063
Interest rate floor	13,594	8,153
Other	28,694	60,935
Total deferred tax assets	1,322,719	1,430,583
Deferred tax liabilities:		
Premises and equipment, principally due to difference in depreciation	286,794	179,736
Discount accretion	29,605	24,571
Other	83,599	41,287

Total deferred tax liabilities	399,998	245,594
Net deferred tax asset (liability)	\$ 922,721	1,184,989

In assessing the ability to realize the balance of the Company's deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies. Based upon the level of historical taxable income and projection for future taxable income over the periods which the temporary differences resulting in the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences.

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004****(12)****Stock Option Plan**

The United Bancorporation of Alabama, Inc. 1998 Stock Option Plan (the Plan) provides for the grant of options to officers, directors, and employees of the Corporation to purchase up to an aggregate of 308,000 shares of Class A Stock. As of December 31, 2006, 170,400 shares of stock could be granted in the future. The changes in outstanding options are as follows:

	<b>Shares under option</b>	<b>Weighted average exercise price per share</b>
Balance at December 31, 2003	72,400	\$ 14.70
Granted	-	-
Surrendered	-	-
Exercised	-	-
Balance at December 31, 2004	72,400	14.70
Granted	-	-
Surrendered	-	-
Exercised	(2,200)	(10.11)
Balance at December 31, 2005	70,200	14.50
Granted	6,000	16.67
Surrendered	(12,000)	(15.75)
Exercised	(8,600)	(15.75)
Balance at December 31, 2006	55,600	14.27

The following table displays information pertaining to the intrinsic value of option shares both outstanding and exercisable for the years ended December 31, 2006, 2005, and 2004 respectively.

	2006	2005	2004
Aggregate intrinsic value of outstanding options	\$ 235,437	\$ 210,207	\$ 70,901

Aggregate intrinsic value of exercisable options	\$	227,637	\$	209,691	\$	33,389
--	----	---------	----	---------	----	--------

Grant-date fair value is measured on the date of grant using an option-pricing model with market assumptions. The grant-date fair values I amortized into expense on a straight-line basis over the vesting period. The company applies the Black-Scholes-Merton option-pricing model which requires the use of highly subjective assumptions, including but not limited to, expected stock price volatility, term, dividend rates, forfeiture rates, and risk-free interest rates, which if changed can materially affect fair value estimates.

The following is a summary of our weighted average assumptions used to estimate the weighted-average per share fair value of options granted on the date of grant using the Black-Scholes-Merton option-pricing model. There were no options granted in 2005 and 2004.

	2006
Weighted-average expected life (in years)	6.67
Expected Volatility	20.00%
Risk-free interest rate	5.02%
Expected dividend yield	1.90%
Weighted-average fair value of options granted during the period	\$ 4.26

At December 31, 2006, 51,200 optioned shares were exercisable at prices between \$8.00 and \$18.00 per share. When options are exercised, par value of the shares issued is recorded as an addition to common stock, and the remainder of the proceeds (including any tax benefit, if applicable) is credited to capital surplus. The following table summarizes information about stock options outstanding at December 31, 2006 and 2005.



## UNITED BANCORPORATION OF ALABAMA, INC.

## AND SUBSIDIARY

## Notes to Consolidated Financial Statements

December 31, 2006, 2005, and 2004

Stock options outstanding and exercisable on December 31, 2006 and 2005 were as follows:

		<b>2006</b>			
<b>Exercise price per Share Outstanding:</b>	<b>Shares under option</b>	<b>Weighted average remaining contractual life in years</b>	<b>Weighted average exercise price</b>		
\$ 8.00	4,000	2.0	\$ 8.00		
11.25	8,160	2.0	11.25		
12.87	8,160	3.0	12.87		
15.65	8,960	4.0	15.65		
15.75	12,160	6.0	15.75		
16.00	4,000	9.3	16.00		
16.25	8,160	5.0	16.25		
18.00	2,000	9.7	18.00		
	55,600	4.6	\$ 14.27		
Exercisable:					
\$ 8.00	4,000	2.0	\$ 8.00		
11.25	8,160	2.0	11.25		
12.87	8,160	3.0	12.87		
15.65	8,960	4.0	15.65		
15.75	12,160	6.7	15.75		
16.00	1,200	9.2	16.00		
16.25	8,160	5.0	16.25		
18.00	400	9.7	18.00		
	51,200	4.3	\$ 14.05		



**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004**

		<b>2005</b>			
<b>Exercise price per Share Outstanding:</b>		<b>Shares under option</b>	<b>Weighted average remaining contractual life in years</b>	<b>Weighted average Exercise Price</b>	
\$	8.00	4,000	3.0	\$	8.00
	11.25	8,160	3.0		11.25
	12.87	8,160	4.0		12.87
	15.65	8,160	5.0		15.65
	15.75	33,560	7.0		15.75
	16.25	8,160	6.0		16.25
		70,200	5.6	\$	14.50
 Exercisable:					
\$	8.00	4,000	3.0	\$	8.00
	11.25	8,160	3.0		11.25
	12.87	8,160	4.0		12.87
	15.65	8,160	5.0		15.65
	15.75	26,728	7.7		15.75
	16.25	8,160	6.0		16.25
		63,368	5.8	\$	14.36

Total intrinsic value of options exercised was \$20,710, \$13,910, and \$0 for the years ended December 31, 2006, 2005, and 2004 respectively. The total fair value of options vested during the years ended December 31, 2006, 2005, and 2004 was \$21,032, \$36,189, and \$32,209, respectively.

The compensation costs related to the Company's stock option plan charged against income for the years ended December 31, 2006, 2005, and 2004 were \$18,397, \$0, and \$0, respectively. Income tax benefits recognized for the respective years were \$6,787, \$0, and \$0.

Cash received from the exercise of options was \$135,390 for the year ended December 31, 2006. The tax benefit realized for the tax deductions from options exercise of the share-based payment arrangements totaled \$8,701 for the year ended December 31, 2006.

As of December 31, 2006, there was \$19,024 of total unrecognized compensation costs related to the nonvested share based compensation arrangements granted under the plan. That cost is expected to be recognized over a period of 2 years.

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004****(13)****Net Earnings per Share**

Presented below is a summary of the components used to calculate diluted earnings per share for the years ended December 31, 2006, 2005, and 2004:

	<b>2006</b>	<b>2005</b>	<b>2004</b>
Diluted earnings per share:			
Basic weighted average common shares outstanding	2,225,269	2,220,553	2,216,032
Effect of the assumed exercise of stock options-based on the treasury stock			
method using average market price	7,010	7,030	2,349
Diluted weighted average common shares outstanding	2,232,279	2,227,583	2,218,381

**(14) Dividend Reinvestment and Share Purchase Plan**

The Company sponsors a dividend reinvestment and share purchase plan. Under the plan, all holders of record of common stock are eligible to participate in the plan. Participants in the plan may direct the plan administrator to invest cash dividends declared with respect to all or any portion of their common stock. Participants may also make optional cash payments that will be invested through the plan. All cash dividends paid to the plan administrator are invested within 30 days of cash dividend payment date. Cash dividends and optional cash payments will be used to purchase common stock of the Company in the open market, from newly-issued shares, from shares held in treasury, in negotiated transactions, or in any combination of the foregoing. The purchase price of the shares of common stock is based on the average market price. All administrative costs are borne by the Company. For the years ended December 31, 2006 and 2005, 5,518 and 4,399 shares were purchased under the plan, respectively.

**(15) Employee Benefit Plans****(a)****401(k) Savings Plan**

Prior to October 1, 2006, employees were eligible in the Company's 401(k) Employee Incentive Savings Plan after completing six months of service and attaining age 20.5. Eligible employees could contribute a minimum of 1% up to

15% of salary to the plan. The Company contributed one dollar for each dollar the employee contributed, up to 4% of the employee's salary, then the company matched fifty cents for each dollar the employee contributed up to 7% of the employee's salary.

Under a new 401(k) savings plan that became effective October 1, 2006, employees are eligible after completing ninety days of service and attaining age 20.5. Eligible employees can contribute a minimum of 1% up to 15% of salary to the plan. The Company contributes one dollar for each dollar the employee contributes, up to 5.5% of the employee's salary.

Total Company contributions to the Plan charged to expense during 2006, 2005, and 2004 were \$202,753, \$169,308, and \$160,419, respectively.

*(b)*

***Profit-Sharing Plan***

The Company also maintains a profit sharing plan for eligible employees. Eligibility requirements for this plan are the same as the 401(k) Employee Incentive Savings Plan. Annual profit sharing contributions of \$60,533, \$51,833, and \$43,858 were made in 2006, 2005, and 2004, respectively.

**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

(c)

***Salary Continuation Plan***

The Company provides a salary continuation plan providing for death and retirement benefits for certain executive officers. The present value of the estimated amounts to be paid under the plan is being accrued over the remaining service period of the executives. The expense recognized for the salary continuation plan amounted to \$77,382, \$73,007, and \$70,329 for the years ended December 31, 2006, 2005 and 2004, respectively. The balance of the liability for the salary continuation plan included in other liabilities at December 31, 2006 and 2005 totaled \$435,301 and \$357,919, respectively.

The cost of the salary continuation plan described above is being offset by earnings from, bank owned life insurance policies on the executives. The balance of the policy surrender values included in other assets totaled \$ 2,416,020 and \$2,330,246 at December 31, 2006 and 2005, respectively. Income recognized from the increase in cash surrender value on these policies totaled \$85,774, \$75,613, and \$77,092 for the years ended December 31, 2006, 2005 and 2004, respectively.

(d)

***Employee Stock Purchase Plan***

The Company sponsors an employee stock purchase plan which is available to all employees subject to certain minimum service requirements. The Plan is administered by a Board appointed committee which designates the offering period in which employees may purchase shares and the offering price. All administrative costs are borne by the Company. For the years ended December 31, 2006 and 2005, 0 and 909 shares were purchased under the plan, respectively.

(16)

**Fair Value of Financial Instruments**

The assumptions used in estimating the fair value of the Company's financial instruments are explained below. Where quoted market prices are not available, fair values are based on estimates using discounted cash flow and other valuation techniques. Discounted cash flows can be significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. The following fair value estimates cannot be substantiated by comparison to independent markets and should not be considered representative of the liquidation value of the Company's financial instruments, but rather a good faith estimate of the fair value of financial instruments held by the Company. SFAS No. 107 excludes certain financial instruments and all nonfinancial instruments from its disclosure requirements.

The following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

(a)

***Cash and Cash Equivalents***

Fair value approximates the carrying value of such assets.

(b)

***Investment Securities and Other Securities***

The fair value of investment securities is based on quoted market prices. The fair value of other securities, which includes Federal Home Loan Bank stock and other correspondent stocks, approximates their carrying value.

(c)

***Loans***

The fair value of loans is calculated using discounted cash flows and excludes lease financing arrangements. The discount rates used to determine the present value of the loan portfolio are estimated market discount rates that reflect the credit and interest rate risk inherent in the loan portfolio. The estimated maturities are based on the Company's historical experience with repayments adjusted to estimate the effect of current market conditions.

(d)

***Bank Owned Life Insurance***

The fair value of bank owned life insurance approximates its carrying value.

(e)

***Deposits***

The fair value of deposits with no stated maturity, such as non interest bearing demand deposits, NOW accounts, savings and money market deposit accounts, approximates the carrying value. Certificates of deposit have been valued using



**UNITED BANCORPORATION OF ALABAMA, INC.**

**AND SUBSIDIARY**

**Notes to Consolidated Financial Statements**

**December 31, 2006, 2005, and 2004**

discounted cash flows. The discount rates used are based on estimated market rates for deposits of similar remaining maturities.

The fair value estimates in the table below do not include the benefit that results from the low cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market.

*(f)*

***Securities Sold Under Agreements to Repurchase***

Due to their short term nature, the fair value of securities sold under agreements to repurchase approximates their carrying value.

*(g)*

***FHLB, Other Borrowed Funds and Subordinated Debt***

The fair value of the Company's other borrowed funds and subordinated debt approximates the carrying value of such liabilities. The fair value of FHLB advances have been valued using discounted cash flows. The discount rates used are based on estimated market rates for borrowings of similar remaining maturities.

*(h)*

***Accrued Interest***

The fair value of accrued interest receivable and payable approximates their carrying value.

*(i)*

***Commitments to Extend Credit and Standby Letters of Credit***

There is no market for the commitment to extend credit and standby letters of credit and they were issued without explicit cost. Therefore, it is not practical to establish their fair value.

The carrying value and estimated fair value of the Company's financial instruments at December 31, 2006 and 2005 are as follows (in thousands):

**2006**

**2005**

	<b>Carrying amount</b>	<b>Estimated fair value</b>	<b>Carrying amount</b>	<b>Estimated fair value</b>
	(Dollars in Thousands)			
Financial assets:				
Cash and short term investments	\$ 51,204	\$ 51,204	\$ 50,867	\$ 50,867
Investment securities	108,410	108,410	70,933	70,933
Other securities	1,588	1,588	1,660	1,660
Loans, net of the allowance for loan losses	242,627	241,925	227,282	231,383
Bank owned life insurance	2,416	2,416	2,330	2,330
Accrued interest receivable	3,580	3,580	3,074	3,074
Financial liabilities:				
Deposits	326,835	327,006	291,020	291,250
Securities sold under agreements to repurchase	44,410	44,410	34,429	34,429
Other borrowed funds	857	857	1,001	1,001
FHLB advances	6,939	7,054	9,113	9,205
Subordinated Debt	14,323	14,323	4,003	4,003
Accrued interest payable	937	937	596	596

(17)

**Dividends From Bank**

Dividends paid by the Bank are the primary source of funds available to the Company for payment of dividends to its stockholders and for other needs. Applicable federal and state statutes and regulations impose restrictions on the amounts of dividends that may be declared by the subsidiary bank. In addition, the subsidiary bank is also required to maintain minimum amounts of capital to total risk weighted assets, as defined by banking regulators. Capital adequacy considerations could further limit the availability of dividends from the subsidiary bank. During 2006, the Bank could have declared an additional amount of dividends of approximately \$7,500,000 without prior approval of regulatory authorities.

## UNITED BANCORPORATION OF ALABAMA, INC.

## AND SUBSIDIARY

## Notes to Consolidated Financial Statements

December 31, 2006, 2005, and 2004

(18)

## Comprehensive Income (Loss)

The following is a summary of the components of other comprehensive income (loss):

	Years ended December 31		
	2006	2005	2004
Other comprehensive income before tax:			
Unrealized holding losses arising during the period for securities, net	\$ 77,258	\$ (1,306,310)	\$ (84,317)
Less reclassification adjustment for gains on sales of securities included in net earnings	(4,879)	33,916	170,898
Unrealized holding losses arising during the period for cash flow hedges	(13,888)	(16,174)	-
Other comprehensive income (loss), before income taxes	58,491	(1,356,400)	(255,215)
Income tax expense related to other comprehensive income:			
Unrealized holding losses arising during the period for securities, net	29,063	(522,523)	(33,727)
Less reclassification adjustment for gains on sales of securities included in net earnings	(1,952)	13,566	68,359
Unrealized holding losses arising during the period for cash flow hedges	(5,441)	(6,470)	-
Total income tax expense related to other comprehensive income (loss)	21,670	(542,559)	(102,086)
Other comprehensive income (loss) after taxes	\$ 36,821	\$ (813,841)	\$ (153,129)

(19)

**Litigation**

The Company is involved in various legal proceedings arising in connection with their business. In the opinion of management, based upon consultation with legal counsel, the ultimate resolution of these proceedings is not expected to have a material adverse effect upon the financial statements of the Company.

(20)

**Commitments**

The Company leases certain property and equipment for use in its business. These leases have lease terms generally not in excess of five years. Future minimum rental payments required under operating leases, which have initial or remaining noncancelable lease terms in excess of one year as of December 31, 2006, are as follows:

Years ending December 31:	
2007	\$ 10,000
2008	4,000
Total	\$ 14,000

Rental expense for all operating leases charged to earnings aggregated \$190,036, \$191,579, and \$162,031, for the years ended December 31, 2006, 2005, and 2004, respectively.

The Company is a party to financial instruments with off balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. Such instruments involve elements of credit risk in excess of the amounts recognized in the consolidated financial statements.

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004**

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual amount of these instruments. The Company uses the same credit policies in making conditional obligations as it does for on balance sheet instruments.

The financial instruments, whose contractual amounts represent credit risk as of December 31, 2006 and 2005, are approximately as follows:

	Years Ended December 31	
	2006	2005
Commitments to extend credit	\$ 33,394,000	\$ 38,034,000
Standby letters of credit	\$ 3,233,000	\$ 5,712,000

Standby letters of credit are commitments issued by the Company to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Company holds various assets as collateral supporting those commitments for which collateral is deemed necessary.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

**(21)****Other Noninterest Expense**

Components of other noninterest expense exceeding 1% of the total of interest income and other income for any of the years ended December 31, 2006, 2005, and 2004, respectively, include the following:

	2006	2005	2004
Advertising	\$ 481,016	\$ 279,233	\$ 252,103
Accounting and audit	214,612	228,316	180,915
Supplies expenses	271,173	245,478	213,213

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

Board fees	192,327	180,095	198,024
Other real estate owned write down	278,100	128,201	50,000
Communication Expense	308,325	266,436	28,749

F-27

---

## UNITED BANCORPORATION OF ALABAMA, INC.

## AND SUBSIDIARY

## Notes to Consolidated Financial Statements

December 31, 2006, 2005, and 2004

(22)

**Regulatory Matters**

The Corporation and its subsidiary bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company. Under capital adequacy guidelines and the regulatory framework of prompt corrective action, the Corporation and its subsidiary bank must meet specific capital guidelines that involve quantitative measures of each bank's assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification of the Corporation and its subsidiary bank are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Corporation and its subsidiary bank to maintain minimum core capital (Tier I Capital) of at least 4% of risk-weighted assets, minimum total capital (Total Qualifying Capital) of at least 8% of risk-weighted assets and a minimum leverage ratio of at least 4% of average assets. Management believes, as of December 31, 2006, that the Corporation and its subsidiary bank meet all capital adequacy requirements to which they are subject.

As of December 31, 2006, the most recent notification from the appropriate regulatory agencies categorized the subsidiary bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the subsidiary banks must maintain minimum Total Qualifying Capital, Tier I Capital, and leverage ratios of at least 10%, 6%, and 5%, respectively. There are no conditions or events since that notification that management believes have changed the subsidiary bank's category.

The following table presents the actual capital amounts and ratios of the Corporation and its subsidiary bank at December 31, 2006 and 2005:

	Total Qualifying Capital		Tier I Capital		Leverage	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2006:						
United Bancorporation	\$ 47,286	16.40%	\$ 40,366	14.00%	\$ 40,366	9.47%
United Bank	42,550	14.77%	39,538	13.72%	39,538	9.88%
As of December 31, 2005:						
United Bancorporation	\$ 34,649	12.99%	\$ 31,621	11.86%	\$ 31,621	8.55%

United Bank	31,363	11.91%	28,334	10.76%	28,334	7.99%
-------------	--------	--------	--------	--------	--------	-------

(23)

**Derivative Financial Instruments**

To hedge the Company's exposure to changing interest rates, management entered into an agreement known as an interest rate floor on a portion of its variable rate loan portfolio during September 2005. Interest rate floors are typically used to mitigate a loan portfolio's exposure to falling interest rates. Pursuant to the agreement, the Company's counterparty agrees to pay the Company an amount equal to the difference between the prime rate and 5.75% multiplied by a \$35,000,000 notional amount should the prime rate fall below 5.75% during the two year term of the agreement. The Company paid its counterparty a one-time premium equal to \$52,500 which will be amortized over the 2 year term. The interest rate floor is being marked to market and accounted for as a cash flow hedge. As of December 31, 2006, the interest rate floor contract was carried at fair value which was equal to \$2,500. The Company considers the derivative (interest rate floor) as highly effective in offsetting changes in cash flows of the hedged items (variable rate loans).

(24)

**Prior Period Adjustment**

During the preparation of the Company's 2006 returns, a previously unaccounted for difference was identified between the book basis and tax basis of the cost of certain fixed assets. The range of acquisition dates for the assets was from January 1, 1960 to April 30, 2002 and resulted in income tax being overstated during these periods by a cumulative amount of \$231,285. As a result, retained earnings has been restated for prior periods.

(24)

**Parent Company Financial Information**

The condensed financial information for United Bancorporation of Alabama, Inc. (Parent Company Only) follows:



**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004****(Parent Company Only)****CONDENSED BALANCE SHEET INFORMATION**

December 31, 2006 and 2005

<b>Assets</b>	<b>2006</b>	<b>2005</b>
Cash	\$ 4,868,380	\$ 447,885
Premises and equipment	-	3,141,329
Investment in subsidiary	39,979,820	28,739,175
Other assets	580,368	124,000
Total assets	\$ 45,428,568	\$ 32,452,389
<b>Liabilities and Stockholders Equity</b>		
Other liabilities	\$ 380,995	\$ 423,995
Note payable to Trust	14,322,853	4,002,749
Total liabilities	14,703,848	4,426,744
Stockholders equity:		
Class A common stock of \$0.01 par value. Authorized 5,000,000 shares; issued 2,366,871 and 2,363,762 shares in 2005 and 2004, respectively	23,755	23,669
Class B common stock of \$0.01 par value. Authorized 250,000 shares; no shares issued	-	-
Preferred stock of \$.01 par value. Authorized 250,000 shares; no shares issued	-	-
Additional paid in capital	5,673,088	5,445,822
Retained earnings	26,341,116	23,874,164
Accumulated other comprehensive loss, net of tax	(475,478)	(512,299)
Less: 142,789 and 143,307 treasury shares at cost in 2006 and 2005, respectively	837,761	805,711
Total stockholders equity	30,724,720	28,025,645

Total liabilities and stockholders equity	\$	45,428,568	\$	32,452,389
---	----	------------	----	------------

**(Parent Company Only)****CONDENSED STATEMENTS OF OPERATIONS INFORMATION**

Years ended December 31, 2005, 2004, and 2003

	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>Income:</b>			
Dividend income	\$ 1,320,000	\$ 748,579	\$ 902,224
Other income	151,158	143,251	131,870
Total income	1,471,158	891,830	1,034,094
<b>Expense:</b>			
Interest on subordinated debentures	567,449	304,434	225,271
Other operating expense	286,216	304,801	347,087
Total expense	853,665	609,235	572,358
Income before equity in undistributed income of subsidiaries and taxes	617,493	282,595	461,736
Equity in undistributed earnings of subsidiary	2,275,608	2,612,189	1,691,521
Income before taxes	2,893,101	2,894,784	2,153,257
Income tax benefit	(241,969)	-	-
Net earnings	\$ 3,135,070	\$ 2,894,784	\$ 2,153,257

F-29

**UNITED BANCORPORATION OF ALABAMA, INC.****AND SUBSIDIARY****Notes to Consolidated Financial Statements****December 31, 2006, 2005, and 2004****(Parent Company Only)****CONDENSED STATEMENTS OF CASH FLOWS INFORMATION**

Years ended December 31, 2006, 2005, and 2004

	<b>2006</b>		<b>2005</b>		<b>2004</b>
Cash flows from operating activities:					
Net earnings	\$ 3,135,070		\$ 2,894,784		\$ 2,153,257
Adjustments to reconcile net earnings to net cash provided by operating activities:					
Equity in undistributed earnings of subsidiary	(2,275,608)		(2,612,189)		(1,691,521)
Depreciation of premises and equipment	137,151		144,648		131,148
Stock-based compensation expense	18,397		-		-
Amortization of trust preferred cost	10,104		10,104		10,104
Increase (decrease) in other liabilities	(43,000)		78,748		(5,522)
Decrease (increase) in receivables	34,859		-		332,189
Net cash provided by (used in) operating activities	1,016,973		516,095		929,655
Cash flows from investing activities:					
Investment in bank subsidiary	(6,000,000)		-		-
Purchases of premises and equipment, net	-		-		(123,421)
Net cash used in investing activities	(6,000,000)		-		(123,421)
Cash flows from financing activities:					
Cash dividends	(668,118)		(666,275)		(664,813)
Purchase of treasury stock	(63,750)		-		(30,366)
Proceeds from sale of treasury stock	-		-		71,208
Proceeds from exercise of stock options	135,390		34,598		-
Issuance of subordinated debentures					

Net cash used in financial activities	10,000,000	-	-
Net increase (decrease) in cash	9,403,522	(631,677)	(623,971)
Cash, beginning of year	4,420,495	(115,582)	182,263
Cash, end of year	447,885	563,467	381,204
	\$ 4,868,380	\$ 447,885	\$ 563,467

The table below sets forth certain quarterly supplementary financial information:

### SELECTED QUARTERLY FINANCIAL DATA 2006 - 2005

(Dollars in thousands, except for per share amounts)

	2006				2005			
	Dec. 31	Sep. 30	Jun. 30	Mar. 31	Dec. 31	Sep. 30	Jun. 30	Mar. 31
Net interest income	\$ 3,820	\$ 3,794	\$ 3,822	\$ 3,857	\$ 3,625	\$ 3,549	\$ 3,391	\$ 3,027
Provision for loan losses	240	240	240	240	195	295	195	195
Earnings before income tax expense	1,037	649	1,052	1,419	1,054	1,111	925	845
Income tax expense	189	140	316	377	301	251	295	193
Net earnings	847	510	736	1,042	753	860	630	652
Net earnings per share (basic and diluted)	\$ 0.38	\$ 0.23	\$ 0.33	\$ 0.47	\$ 0.34	\$ 0.39	\$ 0.28	\$ 0.29
Cash dividends declared per share	0.15	-	0.15	-	0.17	-	0.13	-
Total Assets	\$ 426,171	\$ 386,026	\$ 377,284	\$ 357,261	\$ 369,830	\$ 339,019	\$ 323,920	\$ 315,055



**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

Not applicable

**ITEM 9A. CONTROLS AND PROCEDURES**

(a)

Based on evaluation of the Corporation's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this annual 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.

(b)

There were no significant changes in the Corporation's internal controls or in other factors that could significantly affect these controls subsequent to the date of the evaluation referred to in (a) above.

**ITEM 9B. OTHER INFORMATION**

None



### **PART III**

#### **ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE OF THE REGISTRANT**

The Board of Directors of the Company has determined that Dale M. Ash and Michael R. Andreoli are the Audit Committee Financial Experts. Mrs. Ash and Mr. Andreoli are independent as defined in the listing standards of the National Association of Security Dealers. Additional information required by this item is incorporated herein by reference to the Company's definitive Proxy Statement relating to the Company's 2007 Annual Meeting of Stockholders to be filed not later than 120 days after the year ended December 31, 2006 pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended.

#### **ITEM 11. EXECUTIVE COMPENSATION**

The information required by this item is incorporated herein by reference to the Company's definitive Proxy Statement relating to the Company's 2007 Annual Meeting of Stockholders to be filed not later than 120 days after the year ended December 31, 2006 pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended.

#### **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by this item is incorporated herein by reference to the Company's definitive Proxy Statement relating to the Company's 2007 Annual Meeting of Stockholders to be filed not later than 120 days after the year ended December 31, 2006 pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended.

#### **ITEM 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**



The information required by this item is incorporated herein by reference to the Company's definitive Proxy Statement relating to the Company's 2007 Annual Meeting of Stockholders to be filed not later than 120 days after the year ended December 31, 2006 pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended.

**ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information required by this item is incorporated herein by reference to the Company's definitive Proxy Statement relating to the Company's 2007 Annual Meeting of Stockholders to be filed not later than 120 days after the year ended December 31, 2006 pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended.

**PART IV**

**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

- (a) (1) The financial statements listed in the Index to Financial Statements contained in Item 8 hereof are filed as part of this Annual Report on Form 10-K.
- (2) Financial statement schedules have been omitted as inapplicable.
- (3) The Exhibits listed below are filed as part of this Report. Management contracts and compensatory plans and arrangements required to be filed pursuant to Item 15(b) are identified by an asterisk (\*).
- 1.1 Purchase Agreement, dated as of September 27, 2006, among the Registrant, United Bancorp Capital Trust II and TWE, Ltd., as Purchaser (Incorporated by reference herein from Exhibit 1.1 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006).
- 3.1 Restated Certificate of Incorporation of the Registrant (Incorporated by reference herein from Exhibit 3a to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1988).
- 3.1.1 Certificate of Amendment to Restated Certificate of Incorporation Of the Registrant (Incorporated by reference herein from Exhibit 3.1.1 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 1999).
- 3.2 Amended and Restated Bylaws of the Registrant (Incorporated by reference herein from Exhibit 3.2 to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1992).
- 4.1 Junior Subordinated Indenture, dated as of September 27, 2006, by and between the Registrant and Wilmington Trust Company, as Trustee (Incorporated by reference herein from Exhibit 4.1 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006).
- 4.2 United Bancorp Capital Trust II Amended and Restated Trust Agreement, dated as of September 27, 2006, among the Registrant, as Depositor, Wilmington Trust Company, as Property Trustee, Wilmington Trust Company, as Delaware Trustee and Robert R. Jones, III and Allen O. Jones, as Administrative Trustees (Incorporated by reference herein from Exhibit 4.2 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006).
- 4.3 United Bancorp Capital Trust II Guarantee Agreement, dated as of September 27, 2006, by and between the Registrant, as Guarantor and Wilmington Trust Company, as Guarantee Trustee (Incorporated by reference herein from Exhibit 4.3 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006).
- 4.4 Common Securities Subscription Agreement, dated as of September 27, 2006, by and between United Bancorp Capital Trust II and the Registrant (Incorporated by reference herein from Exhibit 4.4 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006).
- 4.5 Junior Subordinated Note Subscription Agreement, dated as of September 27, 2006, by and between United Bancorp Capital Trust II and the Registrant (Incorporated by reference herein from Exhibit 4.5 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended September 30, 2006).

- 10.1 Form of Employment Agreement between United Bank and Robert R. Jones, III(Incorporated by reference herein from Exhibit 10.1 to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1997).\*
- 10.2 Supplemental Agreement between United Bank, the Registrant, and Robert R. Jones, III (Incorporated by reference herein from Exhibit 10.2 to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1998)\*.
- 10.3 Supplemental Agreement between United Bank, the Registrant, and Robert R. Jones, III (Incorporated by reference herein from Exhibit 10.2 to the Registrant's Annual Report on Form 10-K for the fiscal year ended December 31, 1998)\*.
- 10.4 1998 Stock Option Plan of United Bancorporation of Alabama, Inc. (Incorporated by reference herein from Exhibit 3.1.1 to Registrant's Quarterly Report on Form 10-Q for the Quarter Ended March 31, 1999).
- 10.6 1999 Employee Stock Purchase Plan of United Bancorporation of Alabama, Inc. (incorporated herein by reference from appendix A to the Registrants definitive proxy statement dated April 10, 2000)\*.
- 10.7 Supplemental Compensation Agreement and Amendment Agreement between United Bank and Robert R. Jones, III (Incorporated by reference herein from Exhibit 10.4 to the Registrant's Quarterly Report on Form 10-Q for the Quarter Ended June 30, 2001).\*
- 10.7 Placement Agreement for Floating Rate Cumulative Trust Preferred Securities of United Bancorp Capital Trust I effective as of June 27, 2002 among the Registrant, United Bancorp Capital Trust I and SAMCO Capital Markets, a division of Service Asset Management Company (Incorporated by reference herein from Exhibit 1.1 to the Registrant's report on Form 8-K dated June 27, 2002).
- 10.8 Indenture effective as of June 27, 2002, by and between the Registrant and Wells Fargo Bank, National Association, as Trustee (Incorporated by reference herein from Exhibit 4.1 to the Registrant's report on Form 8-K dated June 27, 2002).
- 10.9 United Bancorp Capital Trust I Amended and Restated Trust Agreement effective as of June 27, 2002, among the Registrant as Depositor, Wells Fargo Bank, National Association, as Property Trustee, Wells Fargo Delaware Trust Company, as Resident Trustee and Robert R. Jones, III, Mitchell D. Staples and Charles E. Karrick, as Administrative Trustees (Incorporated by reference herein from Exhibit 4.2 to the Registrant's report on Form 8-K dated June 27, 2002).
- 10.10 Trust Preferred Securities Guarantee Agreement effective as of June 27, 2002, by and between the Registrant and Wells Fargo Bank, National Association (Incorporated by reference herein from Exhibit 4.3 to the Registrant's report on Form 8-K dated June 27, 2002).

- 21 Subsidiaries of the Registrant.
- 23 Consent of Independent Registered Public Accounting Firm (Mauldin & Jenkins, LLC)
- 31.1 Certification of Chief Executive Officer under Securities Exchange Act Rules 13a-15(e) and 15d-15(e)
- 31.2 Certification of Chief Financial Officer under Securities Exchange Act Rules 13a-15(e) and 15d-15(e)
- 32.1 Certificate pursuant to 18 U.S.C Section 1350
- 32.2 Certificate pursuant to 18 U.S.C Section 1350

## SIGNATURES

Pursuant to the requirements of section 13 or 15(d) 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**  
(Registrant)

March 27, 2007

By: /s/ Robert R. Jones, III  
Robert R. Jones, III  
President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<b>SIGNATURES</b>	<b>CAPACITY IN WHICH SIGNED</b>	<b>DATE</b>
/s/ Robert R. Jones, III Robert R. Jones, III	President, Chief Executive Officer, and Director	March 27, 2007
/s/ Allen O. Jones, Jr. Allen O. Jones, Jr.	Senior Vice President Chief Financial Officer (Principal Financial and Principle Accounting Officer)	March 27, 2007
/s/ William J. Justice William J. Justice	Director	March 27, 2007
/s/ David D. Swift David D. Swift	Director	March 27, 2007

Edgar Filing: UNITED BANCORPORATION OF ALABAMA INC - Form 10-K

/s/ Dale M. Ash Dale M. Ash	Director	March 27, 2007
/s/ Michael Andreoli Michael Andreoli	Director	March 27, 2007
/s/ L. Walter Crim L. Walter Crim	Director	March 27, 2007
/s/ J. W. Trawick J. W. Trawick	Director	March 27, 2007

## **INDEX TO EXHIBITS**

### **Exhibit**

- |      |  |
|------|--|
| 21   | Subsidiaries of the Registrant.  |
| 23   | Consent of Independent Registered Public Accounting Firm (Mauldin & Jenkins, LLC)                    |
| 31.1 | Certification of Chief Executive Officer under Securities Exchange Act Rules 13a-15(e) and 15d-15(e) |
| 31.2 | Certification of Chief Financial Officer under Securities Exchange Act Rules 13a-15(e) and 15d-15(e) |
| 32.1 | Certificate pursuant to 18 U.S.C Section 1350  |
| 32.2 | Certificate pursuant to 18 U.S.C Section 1350  |