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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-KSB

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

For the Fiscal Year Ended September 30, 2001

OR

[_] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 1-5735

Union Financial Bancshares, Inc.

(Name of small business issuer in its charter)

Delaware	57-1001177
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
203 West Main Street, Union, South Carolina	29379
(Address of principal executive offices)	(Zip Code)

Issuer's telephone number, including area code: (864) 427-9000

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

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value $.01 per share

(Title of Class)

Check whether the issuer (1) filed all reports required to be filed by
Section 13 or 15(d) of the Exchange Act during the past 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 X No___

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of the registrant's knowledge, in definitive proxy or other information statements incorporated by reference in Part III of this Form 10-KSB or any amendments to this Form 10-KSB. X

The issuer's gross revenues for the fiscal year ended September 30, 2001 were approximately $20,167,000.

As of December 1, 2001, there were 1,928,125 shares of the registrant's common stock issued and outstanding. The aggregate market value of the voting stock held by non-affiliates, computed by reference to the average bid and asked price on December 1, 2001, was approximately $18,446,771 (1,778,002 shares at $10.375 per share). Solely for the purposes of this calculation it is assumed that directors and executive officers are affiliates of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

1. Portions of the Annual Report to Shareholders for the Fiscal Year Ended September 30, 2001 (Part II).
2. Portions of the Proxy Statement for the 2002 Annual Meeting of Shareholders (Part III).

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PART I

Item 1. Business

General

Union Financial Bancshares, Inc. ("Union Financial") is the savings and loan holding company for Provident Community Bank (the "Bank"). Union Financial has no material assets or liabilities other than its investment in the Bank. Union Financial's business activity consists primarily of directing the activities of the Bank. Accordingly, the information set forth in this report, including financial statements and related data, relates primarily to the Bank. Union Financial and the Bank are collectively referred to as "the Corporation" herein.

The Bank is a federally-chartered, capital stock savings bank headquartered in Union, South Carolina. The Bank's operations are conducted through its main office and five full-service banking centers and a lending and investment center, all of which are located in the upstate area of South Carolina. The Bank is a member of the Federal Home Loan Bank ("FHLB") and its deposits are insured up to applicable limits by the Savings Association Insurance Fund ("SAIF") of the Federal Deposit Insurance Corporation ("FDIC").

The business of the Bank consists primarily of attracting deposits from the general public and originating mortgage loans on residential properties located in Laurens, Union and Fairfield counties in South Carolina. The Bank also makes commercial real estate, construction and consumer loans and invests in obligations of the federal government and its agencies and of state and local municipalities. The Bank purchases both fixed and adjustable rate mortgage-backed securities issued by Freddie Mac, Fannie Mae and Ginnie Mae. The Bank has purchased fixed and variable rate mortgages originated by other organizations. See "Lending Activities." The principal sources of funds for the Bank's lending activities include deposits received from the general public, interest and principal repayments on loans and, to a lesser extent, borrowings from the FHLB-Atlanta. The Bank's primary source of income is interest earned on loans and investments. The Bank's principal expense is interest paid on deposit accounts and borrowings and expenses incurred in operating the Bank.

This discussion and analysis contains certain "forward-looking statements" within the meaning of the federal securities laws. These forward-looking statements include, but are not limited to, estimates and expectation of future performance with respect to the financial condition and results of operations of the Corporation and other factors. These forward-looking statements are not guarantees of future performance and are subject to various factors that could cause actual results to differ materially from these forward-looking statements. These factors include, but are not limited to, changes in general economic and market conditions and the legal and regulatory environment in which Union Financial and the Bank operate and the development of an interest rate environment that adversely affects the Corporation's interest rate spread or other income anticipated from the Corporation's operations.

Competition

The Corporation faces competition in both the attraction of deposit accounts and in the origination of mortgage and consumer loans. Its most direct competition for savings deposits has historically derived from other thrift institutions and commercial banks located in and around Union, Laurens and Fairfield County, South Carolina. The Corporation faces additional significant competition for investor funds from money market instruments and mutual funds. It competes for savings by offering depositors a variety of savings accounts, convenient office locations and other services.

The Corporation competes for loans principally through the interest rates and loan fees it charges and the efficiency and quality of the services it provides borrowers, real estate brokers and home builders. The Corporation's competition for real estate loans comes principally from other thrift institutions, commercial banks and mortgage banking companies.

The Bank expects competition to increase in the future as a result of legislative, regulatory and technological changes and the continuing trend of consolidation in the financial services industry. Technological advances, for

example, have lowered barriers to market entry, allowed banks to expand their geographic reach by providing services over the Internet and made it possible for non-depositing institutions to offer products and services that traditionally have been provided by banks. The Gramm-Leach-Bliley Act, which permits affiliation among banks, securities firms and insurance companies, also has changed and may continue to change the competitive environment in which the Bank conducts business. As of September 30, 2001, a local commercial bank and an office of a regional commercial

bank were located in Union County, South Carolina. The Corporation is the largest financial institution based in Union County, South Carolina.

Recent Events

On November 14, 2001, Union Financial established Union Financial Statutory Trust I (the "Trust") as a business trust for the purpose of issuing trust preferred securities in a private placement conducted as part of a pooled offering sponsored by First Tennessee Capital Markets and Keefe Bruyette & Woods, Inc. On December 18, 2001, the Trust issued $8.0 million in trust preferred securities in the form of floating rate capital securities and issued approximately $248,000 of trust common securities to Union Financial. The Trust used the proceeds of these issuances to purchase $8.2 million of Union Financial's floating rate junior subordinated deferrable interest debentures due December 18, 2031 (the "Debentures"). The interest rate on the Debentures and the trust preferred securities is variable and adjustable quarterly at 3.60% over three-month LIBOR, with an initial rate of 5.60%. A rate cap of 12.50% is effective through December 18, 2006. The Debentures are the sole assets of the Trust and are subordinate to all of Union Financial's existing and future obligations for borrowed money, its obligations under letters of credit and certain derivative contracts, and any guarantees by Union Financial of any such obligations. The trust preferred securities generally rank equal to the trust common securities in priority of payment, but will rank prior to the trust common securities if and so long as Union Financial fails to make principal or interest payments on the Debentures. Concurrently with the issuance of the Debentures and the trust preferred and common securities, Union Financial issued a guarantee related to the trust securities for the benefit of the holders.

The Debentures, the common securities issued by the Trust, and the related income effects are eliminated within Union Financial's financial statements. Union Financial's obligations under the Debentures, the related indenture, the trust agreement relating to the trust securities, and the guarantee constitute a full and unconditional guarantee by Union Financial of the obligations of the Trust under the trust preferred securities.

The stated maturity of the Debentures is December 18, 2031. In addition, the Debentures are subject to redemption at par at the option of Union Financial, subject to prior regulatory approval, in whole or in part on any interest payment date after December 18, 2006. The Debentures are also subject to redemption prior to December 18, 2006 at 107.5% of par after the occurrence of certain events that would either have a negative tax effect on the Trust or Union Financial or would result in the Trust being treated as an investment company that is required to be registered under the Investment Company Act of 1940. Upon repayment of the Debentures at their stated maturity or following their redemption, the Trust will use the proceeds of such repayment to redeem an equivalent amount of outstanding trust preferred securities and trust common securities.

Union Financial intends to use the proceeds of the offering for general corporate purposes, to fund dividends to shareholders and for contributions to the capital of the Bank.

Average Balances, Interest and Average Yields/Cost

The following table sets forth certain information for the periods indicated regarding: (1) average balances of assets and liabilities; (2) the total dollar amounts of interest income from average interest-earning assets and interest expense on average interest-bearing liabilities; and (3) average yields and costs. Such yields and costs for the periods indicated are derived by dividing income or expense by the average monthly balance of assets or liabilities, respectively, for the periods presented. Average balances are derived from month-end balances. Management does not believe that the use of month-end balances instead of daily balances results in any material difference in the information presented.

	Year Ended September 30,					
	2001			2000		
	Average Balance	Interest	Average Yield Cost	Average Balance	Interest	Average Yield Cost
	(Dollars in thousands)					
Interest-earning assets:						
Loans receivable, net (1)	$163,665	$14,487	8.85%	$183,692	$15,272	8.31%
Mortgage-backed securities	48,721	2,894	5.94	29,157	1,711	5.87
Investment securities:						

Taxable	19,872	1,417	7.13	19,962	1,411	7.07
Nontaxable	2,276	108	4.75	1,824	84	4.60
Total investment securities	22,148	1,525	6.88	21,786	1,495	6.86
Overnight deposits	5,526	112	2.03	3,411	77	2.25
Total interest-earning assets	240,060	19,018	7.92	238,046	18,555	7.79
Non-interest-earning assets	21,998			19,794		
Total assets	$262,058			$257,840		
Interest-bearing liabilities:						
Savings accounts	$ 15,354	279	1.82	$ 16,407	319	1.94
Negotiable order of withdrawal accounts	31,779	604	1.90	28,519	474	1.66
Certificate accounts	140,576	7,939	5.65	139,621	7,574	5.42
FHLB advances and other borrowings	47,169	2,791	5.92	49,517	2,808	5.67
Total interest-bearing liabilities	234,878	11,613	4.94	234,064	11,175	4.77
Non-interest-bearing liabilities	4,907			3,657		
Total liabilities	239,785			237,721		
Shareholders' equity	22,273			20,119		
Total liabilities and shareholders' equity	262,058			257,840		
Net interest income		$ 7,405			$ 7,380	
Interest rate spread (2)			2.98%			3.02%
Net interest margin (3)		3.08%			3.10%	
Ratio of average interest-earing assets to average interest-bearing liabilities	1.02x			1.02x		

	1999		
	Average Balance	Interest	Average Yield Cost
Interest-earning assets:			
Loans receivable, net (1)	$142,020	$11,420	8.03%

Mortgage-backed securities	23,663	1,480	6.31
Investment securities:			
Taxable	14,197	1,027	7.23
Nontaxable	769	36	4.68
Total investment securities	14,966	1,063	7.10
Overnight deposits	3,079	83	2.70
Total interest-earning assets	183,728	14,046	7.65
Non-interest-earning assets	14,478		
Total assets	$198,206		
Interest-bearing liabilities:			
Savings accounts	$ 12,681	207	1.63
Negotiable order of withdrawal accounts	30,392	410	1.34
Certificate accounts	96,733	5,089	5.26
FHLB advances and other borrowings	39,452	1,992	5.04
Total interest-bearing liabilities	179,258	7,698	4.29
Non-interest-bearing liabilities	3,652		
Total liabilities	182,910		
Shareholders' equity	15,296		
Total liabilities and shareholders' equity	$198,206		
Net interest income		$ 6,348	
Interest rate spread (2)			3.36%
Net interest margin (3)		3.46%	
Ratio of average interest-earing assets to average interest-bearing liabilities	1.02x		

(1) Average loans receivable includes nonaccruing loans. Interest income does not include interest on loans 90 days or more past due.
(2) Represents difference between weighted average yield on all interest-earning assets and weighted average rate on all interest-bearing liabilities.
(3) Represents net interest income before provision for loan losses as a percentage of average interest-earning assets.

Lending Activities

General. Set forth below is selected data relating to the composition of the Corporation's loan portfolio on the dates indicated (dollars in thousands):

	At September 30,									
	2001		2000		1999		1998		1997	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
First mortgage loans:										
Conventional	$101,530	64.23%	$121,579	72.45%	$108,266	72.47%	$114,383	80.44%	$105,242	80.98%
Construction loans	12,259	7.76	12,335	7.35	17,039	11.40	12,838	9.03	13,508	10.39
Participation loans purchased	353	0.22	366	0.22	377	0.25	665	0.47	1,002	0.77
Total mortgage loans ..	114,142	72.21	134,280	80.02	125,682	84.12	127,886	89.94	119,752	92.14
Second mortgage loans	10,163	6.43	9,848	5.87	8,499	5.69	5,857	4.12	4,478	3.45
Consumer and installment loans	20,653	13.06	20,336	12.12	16,388	10.97	10,679	7.51	10,440	8.03
Commercial loans	19,955	12.63	10,719	6.39	7,748	5.19	3,539	2.49	2,550	1.97
Savings account loans	2,009	1.27	1,971	1.17	1,435	0.96	1,551	1.09	183	0.14
Total loans	166,922	105.60	177,154	105.57	159,752	106.93	149,512	105.15	137,403	105.73
Less:										
Undisbursed loans in process	(6,108)	(3.86)	(5,445)	(3.24)	(9,964)	(6.67)	(6,625)	(4.66)	(6,598)	(5.08)
Loan discount unamortized	(1,922)	(1.22)	(2,718)	(1.62)	--	--	--	--	--	--
Allowance for loan losses	(1,080)	(0.68)	(1,360)	(0.81)	(836)	(0.56)	(827)	(0.59)	(928)	(0.71)
Deferred loan fees	251	0.16	176	0.10	449	0.30	142	0.10	80	0.06
Net loans receivable....	$158,063	100.00%	$167,807	100.00%	$149,401	100.00%	$142,202	100.00%	$129,957	100.00%

The following table sets forth, at September 30, 2001, certain information regarding the dollar amount of principal repayments for loans becoming due during the periods indicated (in thousands). Demand loans (loans having no stated schedule of repayments and no stated maturity) and overdrafts are reported as due in one year or less.

	Due Within One Year	Due After 1 Year Through 5 Years	Due After 5 Years	Total
First mortgage loans:				
Conventional loans	$ 819	$ 2,785	$ 97,926	$101,530
Construction loans (1)	12,259	--	--	12,259
Participation loans purchased	--	--	353	353
Second mortgage loans	--	--	10,163	10,163
Consumer and installment loans	4,375	15,994	284	20,653
Commercial loans	7,248	11,088	1,619	19,955
Savings account loans	2,009	--	--	2,009
Total	$26,710	$29,867	$110,345	$166,922

(1) Includes construction/permanent loans.

The actual average life of mortgage loans is substantially less than their contractual term because of loan repayments and because of enforcement of due-on-sale clauses which give the Corporation the right to declare a loan immediately due and payable in the event, among other things, that the borrower sells the real property subject to the mortgage and the loan is not repaid. The average life of mortgage loans tends to increase, however, when current mortgage loan rates substantially exceed rates on existing mortgage loans.

The following table sets forth the dollar amount of loans due after September 30, 2002 which have fixed rates of interest and which have adjustable rates of interest (in thousands).

	Fixed	Adjustable	Total
Mortgage loans	$ 67,386	$ 33,325	$ 100,711
Consumer and other loans	26,720	12,781	39,501
Total	$ 94,106	$ 46,106	$ 140,212

Real Estate Loans. The primary lending activity of the Corporation is the origination of conventional mortgage loans to enable borrowers to purchase existing single family homes or to construct new homes. The Corporation's residential real estate loan portfolio also includes loans on multi-family dwellings (more than five units). At September 30, 2001, approximately $116.3 million, or 73.6% of the Corporation's total loan portfolio consisted of loans secured by residential real estate (net of undisbursed principal).

Office of Thrift Supervision regulations limit the amount which federally chartered savings institutions may lend in relationship to the appraised value of the real estate securing the loan, as determined by an appraisal at the time of loan origination. Federal regulations permit a maximum loan-to-value ratio of 100% for one- to four-family dwellings and 80% for all other real estate loans. The Corporation's lending policies, however, limit the maximum loan-to-value ratio on one- to four-family real estate mortgage loans to 80% of the lesser of the appraised value or the purchase price. Any single-family loan made in excess of an 80% loan-to-value ratio and any commercial real estate loan in excess of a 75% loan-to-value ratio is required to have private mortgage insurance or additional collateral. In the past, the Corporation has originated some commercial real estate loans in excess of a 75% loan-to-value ratio without private mortgage insurance or additional collateral.

The loan-to-value ratio, maturity and other provisions of the loans made by the Corporation have generally reflected a policy of making less than the maximum loan permissible under applicable regulations, market conditions, and underwriting standards established by the Corporation. Mortgage loans made by the Corporation are generally long-term loans (15-30 years), amortized on a monthly basis, with principal and interest due on each month. In the Corporation's experience, real estate loans remain outstanding for significantly shorter periods than their contractual terms. Borrowers may refinance or prepay loans, at their option, with no prepayment penalty.

The Corporation offers a full complement of mortgage lending products with both fixed and adjustable rates. Due to the nature of the Corporation's marketplace, only a small percentage of "local" loans are adjustable-rate loans. The majority of adjustable-rate loans in the portfolio are originated outside of Union, Fairfield, and Laurens County by third party originators. The Corporation has established a network of third party loan brokers who originate loans for the Corporation, as well as other originators, throughout the state of South Carolina. These loans are originated and underwritten using the same terms and conditions as loans originated by the Corporation. The Corporation offers ARMs tied to U.S. Treasury Bills with a maximum interest rate adjustment of 2% annually and 6% over the life of the loan. At September 30, 2001, the Corporation had approximately $37.9 million of ARMs, or 24.1% of the Corporation's total loans receivable.

At September 30, 2001, 40.4% of the Corporation's loan portfolio consisted of long-term, fixed-rate real estate loans. Because of this high concentration of fixed-rate loans, the Corporation is more vulnerable to a reduction in net interest income during periods of increasing market interest rates. Net interest income depends to a large extent on how successful the Corporation is in "matching" interest-earning assets and interest-bearing liabilities. The Corporation has taken steps to reduce its exposure to rising interest rates. For a discussion of these steps, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report.

The Corporation sells a portion of its loan production to Freddie Mac. The Corporation sells fixed-rate loans with maturities ranging from ten to 30 years. This activity is one method used by the Corporation to reduce its interest rate risk exposure. The loans are sold without recourse and the Corporation retains 25 basis points for servicing these loans. During the year ended September 30, 2001, the Corporation sold approximately $32.9 million of its fixed-rate mortgage loans. During the fourth quarter of fiscal 2000, the Corporation sold approximately $250 million or

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approximately 80% of the loan servicing portfolio. As a result of this sale, the Corporation phased its wholesale mortgage unit during the third quarter of the current fiscal year.

The Corporation purchases participation interests from other financial institutions on a selected basis. These purchased interests are on adjustable-rate loans and are collateralized by either residential or commercial real estate. At September 30, 2001, these interests totaled approximately $353,000.

Commercial real estate loans constituted approximately $1.9 million, or
1.2%, of the Corporation's loan portfolio at September 30, 2001. Commercial real estate loans consist of permanent loans secured by multi-family properties, generally apartment houses, as well as commercial and industrial properties, including office buildings, warehouses, shopping centers, hotels, motels and other special purpose properties. Commercial real estate loans have been originated and purchased for inclusion in the Corporation's portfolio. These loans generally have 20 to 30 year amortization schedules and are callable or have balloon payments after five to ten years. Typically, the loan documents provide for adjustment of the interest rate every one to three years. Fixed-rate loans secured by multi-family residential and commercial properties have terms ranging from 20 to 25 years.

Loans secured by commercial properties may involve greater risk than single-family residential loans. Such loans generally are substantially larger than single-family residential loans. The payment experience on loans secured by commercial properties typically depends on the successful operation of the properties, and thus may be subject to a greater extent to adverse conditions in the real estate market or in the economy generally.

Construction Loans. The Corporation engages in construction lending that is primarily secured by single family residential real estate and, to a much lesser extent, commercial real estate. These loans are made for a maximum 12-month construction period and require monthly interest payments. In some cases these loans automatically convert to a permanent loan requiring monthly principal and interest payments. The Corporation also grants construction loans to individuals with a takeout for permanent financing from another financial institution, and to approved builders on both

presold and unsold properties.

Loan brokers are the Corporation's primary source for construction loans. The loan broker sends the Corporation both individuals seeking construction financing for their personal dwelling or builders seeking lines of credit for the construction of single family residences on both presold and unsold properties. Construction loans to individuals are originated for a term of one year or less or are originated to convert to permanent loans at the end of the construction period. Construction loans are originated to builders for a term not to exceed 12 months. Generally, draw inspections are handled by the appraiser who initially appraised the property; however, in some instances the draw inspections are performed by the originating brokerage firm.

Construction financing affords the Corporation the opportunity to achieve higher interest rates and fees with shorter terms to maturity than do single-family permanent mortgage loans. However, construction loans are generally considered to involve a higher degree of risk than single-family permanent mortgage lending due to: (i) the concentration of principal among relatively few borrowers and development projects; (ii) the increased difficulty at the time the loan is made of estimating the building costs and selling price of the residence to be built; (iii) the increased difficulty and costs of monitoring the loan; (iv) the higher degree of sensitivity to increases in market rates of interest; and (v) the increased difficulty of working out loan problems. Speculative construction loans have the added risk associated with identifying an end-purchaser for the finished home.

At September 30, 2001, the Corporation had approximately $6.2 million outstanding in construction loans, including approximately $6.1 million in undisbursed proceeds. Of the $6.2 million in construction loans at September 30, 2001, approximately $1.2 million were "speculative," meaning that, at the time the loan was made, there was no sales contract or permanent loan in place for the finished home. Substantially all of these loans were secured by one- to four-family residences.

Consumer Loans. Federal regulations permit federally chartered thrift institutions to make secured and unsecured consumer loans up to 35% of the institution's assets. In addition, a federal thrift institution has lending authority above the 35% category for certain consumer loans, such as home equity loans, property improvement loans,

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mobile home loans and loans secured by savings accounts. The Corporation's consumer loan portfolio consists primarily of automobile loans on new and used vehicles, mobile home loans, boat loans, home equity loans, property improvement loans, loans secured by savings accounts and unsecured loans. As of September 30, 2001, consumer loans amounted to $20.6 million, or 13.1% of the Corporation's total loan portfolio. The Corporation makes consumer loans to serve the needs of its customers and as a way to improve the interest-rate sensitivity of the Corporation's loan portfolio.

Consumer loans tend to bear higher rates of interest and have shorter terms to maturity than residential mortgage loans; however, nationally, consumer loans have historically tended to have a higher rate of default than residential mortgage loans. Additionally, consumer loans entail greater risk than do residential mortgage loans, particularly in the case of loans that are unsecured or secured by rapidly depreciating assets such as automobiles. In these cases, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. The remaining deficiency often does not warrant further substantial collection efforts against the borrower beyond obtaining a deficiency judgment. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy.

Commercial Loans. The Corporation makes commercial business loans primarily in its market area to small businesses. The Corporation offers secured commercial loans with maturities of up to 20 years. The term for repayment will normally be limited to the lesser of the expected useful life of the asset being financed or a fixed amount of time, generally less than seven years. These loans have adjustable rates of interest indexed to the prime rate as reported in The Wall Street Journal and are payable on demand, subject to annual review and renewal. When making commercial loans, the Corporation considers the financial statements of the borrower, the borrower's payment history of both corporate and personal debt, the debt service capabilities of the borrower, the projected cash flows of the business, the viability of the industry in which the customer operates and the value of the collateral. Commercial loans are generally secured by a variety of collateral, primarily accounts receivable, inventory and equipment, and are generally supported by personal guarantees. Depending on the collateral used to secure the loans, commercial loans are made in amounts of up to 80% of the value of the collateral securing the loan. The Corporation's largest commercial loan relationship was a $2.5 million loan secured by assignment of real estate mortgages located in Greenville, South Carolina. This loan was performing according to its original terms at September 30, 2001.

Unlike residential mortgage loans, which generally are made on the basis of the borrower's ability to make repayment from his or her employment or other income, and which are secured by real property whose value tends to be more easily ascertainable, commercial loans are of higher risk and typically are made on the basis of the borrower's ability to make repayment from the cash flow of the borrower's business. As a result, the availability of funds for the repayment of commercial loans may depend substantially on the success of the business itself. Further, any collateral securing such loans may depreciate over time, may be difficult to appraise and may fluctuate in value.

Loan Solicitation and Processing. Loan originations come from both walk-in customers and loan brokers. The loan origination process for walk-in customers includes an initial interview with an officer of the Corporation for the purpose of obtaining a formal application. Upon receipt of a loan application from a prospective borrower, a credit report is ordered to verify specific information relating to the loan applicant's employment, income and credit standing. This information may be further verified by personal contacts with other reference sources. An appraisal of the real estate intended to secure the proposed loan is undertaken by pre-approved, independent fee appraisers. As soon as the required information has been obtained and the appraisal completed, the loan is submitted to the authorized officer, loan committees or full Board of Directors for review. The Corporation utilizes various officers and loan committees for the approval of real estate loans. The President/Chief Executive Officer has the authority to approve loan requests up to and including $500,000 in secured credit and up to and including $150,000 in unsecured credit. The Board of Directors has appointed an Executive Loan Committee comprised of four senior executive Bank officers. This Committee has the authority to approve all loan requests up to and including $500,000 in secured credit and up to and including $150,000 in unsecured credit. A quorum of two members is required for any action. The Board of Directors has also appointed a Board Loan Committee comprised of two members elected annually from the Board of Directors and four senior executive officers of the Bank. A quorum of three members, including at least one Board member, is required for any action. This Committee has the authority to approve all secured and unsecured loan requests up to the Bank's legal lending limit with the exception of a single loan request exceeding $1,000,000 in secured credit and

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exceeding $300,000 in unsecured credit. Single loan requests exceeding $1,000,000 in secured credit and $300,000 in unsecured credit require approval of the entire Board of Directors.

Loan applicants are promptly notified of the decision of the Corporation by telephone, setting forth the terms and conditions of the decision. If approved, these terms and conditions include the amount of the loan, interest rate, amortization term, and a brief description of the real estate to be mortgaged to the Corporation. The Corporation also issues a commitment letter to the potential borrower which typically remains in effect for 60 days. The Corporation's experience is that very few commitments go unfunded. See "Loan Commitments." The borrower is required to pay all costs of the Corporation's origination cost, as well as his/her own costs, incurred in connection with the particular loan closing.

The Board of Directors has appointed a second review loan committee to review all denied loan applications. This committee reviews the rationale used to deny credit and reviews denied applications for the possibility of being able to supply credit under a different loan program, or under different terms and conditions. Every attempt is made to supply credit to creditworthy applicants in a manner consistent with their needs.

Loan Originations, Purchases and Sales. The Corporation may sell a portion of its current long-term, fixed-rate loan production to Freddie Mac on a servicing-retained basis. These are cash sales with no recourse provisions. The Corporation receives 25 basis points for servicing these loans.

Mortgage operations purchases the loans from mortgage brokers primarily located in South Carolina. The loan types purchased are primarily adjustable rate residential loans. In addition, construction/permanent loans are also purchased. Mortgage operations had total purchases through the broker network of $30.8 million with loan sales of $32.8 million in fiscal 2001. The Corporation reduced broker loan purchases during fiscal 2001 in order to provide an increased capital allocation for consumer and commercial lending. At September 30, 2001 the Bank was servicing $65.9 million of loans for others.

The Corporation purchases participation interests in loans originated by other institutions. These participation interests are on both residential and commercial properties and carry either a fixed or adjustable interest rate.

The following table sets forth the Corporation's loan origination and sale activity for the periods indicated (in thousands):

	Year Ended September 30,		
	2001	2000	1999
Loans originated:			
First mortgage loans:			
Loans on existing property.....	$28,795	$34,321	$153,665
Construction loans.....	11,726	16,526	17,635
Total mortgage loans originated	40,521	50,847	171,300
Consumer and other loans.....	42,826	28,880	29,208
Total loans originated.....	$83,347	$79,727	$200,508
Loans purchased.....	30,851	44,102	108,962
Loans sold.....	$32,868	$43,508	$108,746

Loan Commitments. The Corporation's commitments to make conventional mortgage loans on existing residential dwellings are normally made for periods of up to 30 days from the date of loan approval. See "Financial Condition, Liquidity and Capital Resources" in the Annual Report.

Loan Origination and Other Fees. In addition to interest earned on loans and fees for making loan commitments, the Corporation charges origination fees or "points" for originating loans. Loan origination fees are usually a percentage of the principal amount of the mortgage loan, typically between 0.5% and 2%, depending on the

terms and conditions. The Corporation does not receive origination fees on broker loans, but does receive a $150 review fee. The Corporation also offers loan products that require no origination fees to walk-in customers. Other fees collected include late charges applied to delinquent payments and fees collected in connection with loan modifications. The Corporation charges a 5% late charge fee on payments delinquent 15 days or more on new loan originations, loan modifications, loan assumptions and loans currently in the Corporation's portfolio where applicable. The 5% late charge is calculated on the delinquent monthly principal and interest payment amount. Late charges and modification fees do not constitute a material source of income. Current accounting standards require fees received (net of certain loan origination costs) for originating loans to be deferred and amortized into interest income over the contractual life of the loan. As of September 30, 2001, the Corporation had net deferred loan fees of approximately $251,000.

Problem Assets. When a borrower fails to make a required payment on a loan, the Corporation attempts to cure the default by contacting the borrower. In general, borrowers are contacted after a payment is more than 30 days past due. In most cases, defaults are cured promptly. If the delinquency on a mortgage loan is not cured through the Corporation's normal collection procedures, or an acceptable arrangement is not worked out with the borrower, the Corporation will institute measures to remedy the default, including commencing a foreclosure action.

Loans are reviewed on a regular basis and an allowance for uncollectible interest is established against accrued interest receivable when, in the opinion of management, the collection of additional interest is doubtful. An allowance for uncollectible interest on real estate loans and consumer loans is established when either principal or interest is more than 90 days past due. Subsequent payments are either applied to the outstanding principal balance or recorded as interest income, depending on the assessment of the ultimate collectibility of the loan. See Notes 1 and 4 of Notes to Consolidated Financial Statements.

The Corporation generally determines a loan to be impaired at the time management believes that it is probable that the principal and interest may be uncollectible. Management has determined that, generally, a failure to make a payment within a 90-day period constitutes a minimum delay or shortfall and does not generally constitute an impaired loan. However, management reviews each past due loan on a loan-by-loan basis and may determine a loan to be impaired prior to the loan becoming over 90 days past due, depending upon the circumstances of that particular loan. A loan is

classified as non accrual at the time management believes that the collection of interest is improbable, generally when a loan becomes 90 days past due. The Corporation's policy for charge-off of impaired loans is on a loan-by-loan basis. At the time management believes the collection of interest and principal is remote, the loan is charged off. The Corporation's policy is to evaluate impaired loans based on the fair value of the collateral. Interest income from impaired loans is recorded using the cash method.

Real estate acquired by the Corporation as a result of foreclosure or by deed in lieu of foreclosure is classified as real estate owned below. When such property is acquired it is recorded at the lower of the unpaid principal balance of the related loan or its fair market value less selling costs. Any subsequent write-down of the property is charged to income.

The following table sets forth information with respect to the Corporation's non-performing assets for the periods indicated (dollars in thousands). It is the policy of the Corporation to cease accruing interest on loans 90 days or more past due. As of and for the years ended September 30, 2001 and 2000, loans totaled $121,075 and $55,951 respectively, that were classified within the meaning of Statement of Financial Accounting Standards ("SFAS") No.
15. Also, at the dates indicated, there were no loans which are not disclosed in the following table about which there was known information of possible credit problems of the borrowers' ability to comply with the present repayment terms:

	At September 30,				
	2001	2000	1999	1998	1997
Loans accounted for on a nonaccrual basis:					
Real estate:					
Residential	$626	$ 763	$ 43	$581	$751
Commercial	160	247	--	--	--
Consumer	9	106	141	115	27
Total	795	1,116	184	696	778
Accruing loans which are contractually past due 90 days or more	--	--	--	--	--
Real estate owned, net	77	459	241	35	1
Total non-performing assets	$872	$1,575	$425	$731	$779
Percentage of loans receivable net	0.56%	0.94%	0.28%	0.55%	0.60%

Interest income that would have been recorded for the year ended September 30, 2001 had nonaccruing loans been current in accordance with their original terms amounted to approximately $90,000. There was no interest included in interest income on such loans for the year ended September 30, 2001.

Allowance for Loan Losses. In originating loans, the Corporation recognizes that losses will be experienced and that the risk of loss will vary with, among other things, the type of loan being made, the creditworthiness of the borrower over the term of the loan, general economic conditions and, in the case of a secured loan, the quality of the security for the loan. To cover losses inherent in the portfolio of performing loans, the Corporation maintains an allowance for loan losses. Management's periodic evaluation of the adequacy of the allowance is based on a number of factors, including management's evaluation of the collectibility of the loan portfolio, the nature of the portfolio, credit concentrations, trends in historical loss experience, specific impaired loans and economic conditions. The amount of the allowance is based on the estimated value of the collateral securing the loan and other analysis pertinent to each situation.

The Corporation increases its allowance for loan losses by charging provisions for loan losses against income. The allowance for loan losses is maintained at an amount management considers adequate to absorb losses inherent in the portfolio. Although management believes that it uses the best information available to make such determinations, future adjustments to the allowance for loan losses may be necessary and results of operations could be significantly and adversely affected if circumstances differ substantially from the assumptions used in making the determinations.

The provision for loan loss calculation includes a segmentation of loan categories subdivided by residential mortgage, commercial and consumer loans. Each category is rated for all loans including performing groups. The weights assigned to each performing group is developed from previous loan loss experience and as the loss experience changes, the category weight is adjusted accordingly. In addition, as the loan categories increase and decrease in balance, the provision for loan loss calculation will adjust accordingly.

While the Corporation believes it has established its existing allowance for loan losses in accordance with generally accepted accounting principles, there can be no assurance that regulators, in reviewing the Corporation's loan portfolio, will not request the Corporation to significantly increase its allowance for loan losses. In addition, because future events affecting borrowers and collateral cannot be predicted with certainty, there can be no assurance that the existing allowance for loan losses is adequate or that substantial increases will not be necessary should the quality of any loans deteriorate as a result of the factors discussed above. Any material increase in the allowance for loan losses

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may adversely affect the Corporation's financial condition and results of operations. Management periodically evaluates the adequacy of the allowance based upon historical delinquency rates, the size of the Corporation's loan portfolio and various other factors. See Notes 1 and 4 of Notes to Consolidated Financial Statements for information concerning the Corporation's provision and allowance for possible loan losses.

The following table sets forth an analysis of the Corporation's allowance for loan losses for the periods indicated (dollars in thousands):

	At September 30,				
	2001	2000	1999	1998	1997
Balance at beginning of year	$1,360	$ 836	$ 827	$ 928	$ 799
Loans charged off:					
Real estate:					
Residential	(180)	(85)	--	--	--
Commercial	(211)	--	--	--	--
Consumer	(176)	(129)	(106)	(127)	(165)
Total charge-offs	(567)	(214)	(106)	(127)	(165)
Recoveries:					
Real estate:					
Residential	4	--	--	--	--
Commercial	8	--	--	--	--
Consumer	35	64	10	26	51
Total recoveries	47	64	10	26	51
Net charge-offs	(520)	(150)	(96)	(101)	(114)
Merger additions	--	449	--	--	--
Provision for loan losses (1)	240	225	105	--	243

Balance at end of year	$1,080	$1,360	$ 836	$ 827	$ 928
Ratio of net charge-offs to average gross loans outstanding during the period	0.32%	0.08%	0.07%	0.07%	0.09%

(1) See "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report for a discussion of the factors responsible for changes in the provision for loan losses between the periods.

The Corporation experienced bad debt charge-offs, net of recoveries, of approximately $520,000 in fiscal 2001 compared to $150,000 for fiscal 2000. The increase in bad debt charge-offs over the previous year includes approximately $210,000 from two commercial loan customers that filed for bankruptcy. The allowance for loan losses to total loans ratio at the end of fiscal 2001 was .67% compared to .80% at the end of fiscal 2000. Nonperforming assets which includes repossessed assets and loans on non accrual decreased to $872,000 at September 30, 2001 from $1,575,000 at September 30, 2000.

The following table sets forth the breakdown of the allowance for loan losses by loan category and the percentage of loans in each category to total loans for the periods indicated. Management believes that the allowance can be allocated by category only on an approximate basis. The allocation of the allowance to each category is not necessarily indicative of further losses and does not restrict the use of the allowance to absorb losses in any category (dollars in thousands):

	At September 30,									
	2001		2000		1999		1998		1997	
	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans	Amount	% of Loans in Each Category to Total Loans
Real estate:										
Residential	$ 400	73.55%	$ 600	79.76%	$400	80.77%	$400	85.90%	$400	83.49%
Commercial	100	1.23	200	2.89	75	2.12	100	2.90	162	4.88
Consumer	500	25.22	500	17.35	311	17.11	277	11.20	266	11.63
Unallocated	80	N/A	60	N/A	50	N/A	50	N/A	100	N/A
Total allowance for loan losses ..	$1,080	100.00%	$1,360	100.00%	$836	100.00%	$827	100.00%	$928	100.00%

The Corporation adjusts balances on real estate acquired in settlement of loans to the lower of cost or market based on appraised value when the property is received in settlement. These values reflect current market conditions and sales experience. See Notes 1 and 4 of Notes to Consolidated Financial Statements.

Asset Classification. The OTS requires savings institutions to classify problem assets. Under this classification system, problem assets of insured institutions are classified as "substandard," "doubtful" or "loss," depending on the presence of certain characteristics. An asset is considered "substandard" if inadequately protected by the current net worth and paying capacity of the borrower or of the collateral pledged, if any. "Substandard" assets include those characterized by the "distinct possibility" that the institution will sustain some loss if the deficiencies are not corrected. Assets classified as "doubtful" have all of the weaknesses inherent in those classified as "substandard" with the added characteristic that the weaknesses present make "collection or liquidation in full," on the basis of currently existing facts, conditions, and values, "highly questionable and improbable." Assets classified as "loss" are those considered "uncollectible" and of such little value that their continuance as assets without the establishment of a specific loss reserve is not warranted. Assets that do not currently expose the insured institution to sufficient risk to warrant classification in the above-mentioned categories but possess weaknesses are designated "special mention."

When an institution classifies problem assets as either substandard or doubtful, it is required to establish general allowances for loan losses in an amount deemed prudent by management. General allowances represent loss allowances which have been established to recognize the inherent risk associated with lending activities, but which, unlike specific allowances, have not been allocated to particular problem assets. When an institution classifies problem assets or a portion of assets as loss, it is required either to establish a specific allowance for losses equal to 100% of the amount of the asset or a portion thereof so classified or to charge-off such amount. An institution's determination as to the classification of its assets and the amount of its valuation allowances is subject to review by the OTS which can order the establishment of additional general or specific loss allowances.

The following tables set forth the number and amount of classified loans at September 30, 2001 (dollars in thousands):

	Loss		Doubtful		Substandard		Special Mention	
	Number	Amount	Number	Amount	Number	Amount	Number	Amount
Real estate:								
Residential.....	--	$ --	--	$ --	21	$ 734	61	$2,440
Commercial.....	--	--	--	--	2	1,117	3	177
Consumer.....	--	--	--	--	12	242	24	915
Total.....	--	$ --	--	$ --	35	$2,093	88	$3,532

Investment Activities

SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," requires that investments be categorized as "held to maturity," "trading securities" or "available for sale," based on management's intent as to the ultimate disposition of each security. SFAS No. 115 allows debt securities to be classified as "held to maturity" and reported in financial statements at amortized cost only if the reporting entity has the positive intent and ability to hold those securities to maturity. Securities that might be sold in response to changes in market interest rates, changes in the security's prepayment risk, increases in loan demand, or other similar factors cannot be classified as "held to maturity." Debt and equity securities held for current resale are classified as "trading securities." The Corporation currently does not use or maintain a trading account. Such securities are reported at fair value, and unrealized gains and losses on such securities would be included in earnings. Debt and equity securities not classified as either "held to maturity" or "trading securities" are classified as "available for sale." Such securities are reported at fair value, and unrealized gains and losses on such securities are excluded from earnings and reported as a net amount in a separate component of equity.

The following table sets forth the Corporation's investment and mortgage-backed securities portfolio at the dates indicated (dollars in thousands):

	At September 30,					
	2001		2000		1999	
	Carrying Value	Percent of Portfolio	Carrying Value	Percent of Portfolio	Carrying Value	Percent of Portfolio
Available for sale:						
Investment securities:						
U.S. Agency obligations.....	$13,494	17.35%	$15,286	52.28%	$13,930	50.96%
Municipal securities.....	9,726	12.50	1,669	5.71	1,576	5.76
Total investment securities.....	23,220	29.85	16,955	57.98	15,506	56.72
Mortgage-backed and related securities.....	54,582	70.15	12,285	42.02	11,829	43.28
Total available for sale.....	$77,802	100.00%	$29,240	100.00%	$27,335	100.00%
Held to Maturity:						
Investment securities:						
U.S. Agency obligations.....	$ 950	8.40%	$ 2,477	6.58%	$ -	-%
Mortgage-backed and related securities.....	10,365	91.60	35,175	93.42	5,586	100.00
Total held to maturity.....	$11,315	100.00%	$37,652	100.00%	$ 5,586	100.00%

During the quarter ended December 31, 2000 the Corporation reclassified approximately $24,000,000 in mortgage backed securities from held to maturity to available for sale as part of the adoption of FASB 133, Accounting for Derivative Instruments and Hedging Activities. The purpose of this transfer was to allow for the sale of the fixed rate securities in order to reduce interest rate risk exposure.

The Corporation purchases mortgage-backed securities, both fixed-rate and adjustable-rate, from Freddie Mac, Fannie Mae and Ginnie Mae with maturities from five to 30 years. The Corporation also purchases adjustable-rate Small Business Administration securities that are backed by the full faith and credit of the U.S. government.

The Corporation also purchases mortgage derivative securities in the form of collateralized mortgage obligations ("CMOs") and structured notes. While these securities possess minimal credit risk due to the Federal guarantee backing the U. S. government agencies, they do posses liquidity risk and interest rate risk. The amortized cost of the CMOs at September 30, 2001 was approximately $13.6 million with a fair value of $13.2 million. The Corporation has purchased structured notes for investment purposes. These include step-up bonds, single-index floaters and dual-index floaters. While all financial instruments are subject to interest rate risk and liquidity risk, structured notes are more sensitive to changes in interest rates and differing note structures (call provision, rate adjustments, etc.). The Corporation had approximately $1.1 million in structured notes as of September 30, 2001 with a fair value of approximately $1.2 million as of that date. See Note 3 of Notes to Consolidated Financial Statements for more information regarding investment and mortgage-backed securities.

The following table sets forth at amortized cost and market value the maturities and weighted average yields of the Corporation's investment and mortgage-backed securities portfolio at September 30, 2001 (dollars in thousands):

	Amount Due or Repricing within:							
	One Year or Less		Over One to Five Years		Over Five to Ten Years		Over Ten Years	
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield
Available for Sale:								
Investment securities:								
U.S. Agency obligations	$ --	--%	$ 1,826	5.96%	$ --	--%	$ 10,600	6.98%
Municipal securities (1)	--	--	201	6.03	--	--	9,687	6.28
Total investment securities	--	--	2,027	5.97	--	--	20,287	6.65
Mortgage-backed and related securities	104	6.99%	--	--	3,726	5.94%	51,658	6.04
Total available for sale	$ 104	6.99%	$ 2,027	5.97%	$ 3,726	5.94%	$ 71,945	6.21%
Held to Maturity:								
Investment securities:								
U.S. Agency obligations	$ 250	7.04%	$ 706	5.86%	$ --	--%	$ --	--%
Mortgage-backed and related securities	--	--	--	--	--	--	10,359	5.86
Total held to maturity	$ 250	7.04%	$ 706	5.86%	--	--	$ 10,359	5.86%

	Total	
	Carrying Value	Weighted Average Yield
Available for Sale:		
Investment securities:		
U.S. Agency obligations	$ 12,426	6.83%
Municipal securities (1)	9,888	6.27
Total investment securities	22,314	6.58

Mortgage-backed and related securities	55,488	6.04
Total available for sale	$ 77,802	6.19%
Held to Maturity:		
Investment securities:		
U.S. Agency obligations	$ 956	6.17%
Mortgage-backed and related securities	10,359	5.86
Total held to maturity	$ 11,315	5.89%

(1) Yields are presented on a fully taxable equivalent basis.

At September 30, 2001, approximately $8.6 million of mortgage-backed securities were adjustable-rate securities.

Deposits and Borrowings

Deposits are the major source of the Corporation's funds for lending and other investment purposes. In addition to deposits, the Corporation derives funds from principal repayments and interest payments on loans and investment and mortgage-backed securities. Principal repayments and interest payments are a relatively stable source of funds, although principal prepayments tend to slow when interest rates increase. Deposit inflows and outflows may be significantly influenced by general market interest rates and money market conditions. During fiscal year 2001, the Corporation experienced a net increase in deposits of approximately $6.1 million due to the result of various deposit promotion programs with continued emphasis on increasing core deposits. The Corporation borrowed funds to support the remaining growth experienced in fiscal 2001.

Deposits. Local deposits are, and traditionally have been, the primary source of the Corporation's funds for use in lending and for other general business purposes. The Corporation offers a number of deposit accounts including NOW accounts, money market savings accounts, passbook and statement savings accounts, individual retirement accounts and certificate of deposit accounts. Deposit accounts vary as to terms regarding withdrawal provisions, deposit provisions and interest rates.

The Corporation adjusts the interest rates offered on its deposit accounts as necessary so as to remain competitive with other financial institutions in Union, Laurens and Fairfield County.

The following table sets forth the time deposits of the Corporation classified by rates as of the dates indicated (in thousands):

	At September 30,		
	2001	2000	1999
Up to 4.0%.....	$ 18,152	$ 440	$ 558
4.01% to 6.0%.....	98,064	53,052	95,163
6.01% to 8.0%.....	24,187	88,666	5,972
Total savings certificates.....	$140,403	$142,158	$101,693

The following table sets forth the maturities of time deposits at September 30, 2001 (in thousands):

	Amount
Within three months.....	$ 48,668
After three months but within six months.....	31,756
After six months but within one year.....	36,339
After one year but within three years.....	22,313
After three years but within five years.....	1,278
After five years but within ten years.....	49
Total.....	$140,403

Certificates of deposit with maturities of less than one year decreased from $118.8 million at September 30, 2000 to $116.8 million at September 30, 2001. Historically, the Bank has been able to retain a significant amount of its deposits as they mature. In addition, management of the Bank believes that it can adjust the offering rates of savings certificates to retain deposits in changing interest rate environments.

The following table indicates the amount of the Bank's jumbo certificates of deposit by time remaining until maturity as of September 30, 2001 (in thousands). Jumbo certificates of deposit are certificates in amounts of $100,000 or more.

Maturity Period	Amount
Three months or less	$ 13,129
Over three through six months	8,627
Over six months through 12 months	9,753
Over 12 months.	6,002
Total jumbo certificates	$ 37,511

See Note 7 of Notes to Consolidated Financial Statements for additional information about deposit accounts.

Borrowings. The Corporation utilizes advances from the FHLB agreements and other borrowings (treasury, tax and loan deposits and security repurchase agreements) to supplement its supply of lendable funds for granting loans, making investments and meeting deposit withdrawal requirements. See "Regulation and Supervision -- Federal Home Loan Bank System."

The following tables set forth certain information regarding borrowings by the Bank at the dates and for the periods indicated (dollars in thousands):

	At September 30,		
	2001	2000	1999
Balance outstanding at end of period:			
FHLB advances and other borrowings	$57,007	$47,687	$46,503
Weighted average rate paid on:			
FHLB advances and other borrowings	5.92%	6.28%	5.17%

	Year Ended September 30,		
	2001	2000	1999
Maximum amount of borrowings outstanding at any month end:			
FHLB advances and other borrowings	$57,007	$55,852	$46,503
Approximate average short-term borrowings outstanding with respect to:			
FHLB advances and other borrowings	47,169	17,927	39,452
Approximate weighted average rate paid on:			
FHLB advances and other borrowings	5.41%	6.57%	5.05%

At September 30, 2001, the Corporation had unused short-term lines of credit to purchase federal funds from unrelated banks totaling $15 million. These lines of credit are available on a one-to-ten

day basis for general purposes of the Corporation. All of the lenders have reserved the right to withdraw these lines at their option. At September 30, 2001, the Corporation had unused lines of credit with the FHLB of Atlanta totaling $29 million.

Subsidiary Activities

Under OTS regulations, the Bank generally may invest up to 3% of its assets in service corporations, provided that at least one-half of the investment in excess of 1% is used primarily for community, inner-city and community development projects. In 1997, the Bank formed Provident Financial Services, Inc. for the purpose of engaging in securities brokerage activities for the benefit of the Bank's customers.

Employees

The Corporation has 70 full-time employees and 7 part-time employees. None of the employees are represented by a collective bargaining unit. The Corporation believes that relations with its employees are excellent.

REGULATION AND SUPERVISION

General

As a savings and loan holding company, Union Financial is required by federal law to file reports with, and otherwise comply with, the rules and regulations of the OTS. The Bank is subject to extensive regulation, examination and supervision by the OTS, as its primary federal regulator, and the FDIC, as the deposit insurer. The Bank is a member of the FHLB and its deposit accounts are insured up to applicable limits by the SAIF managed by the FDIC. The Bank must file reports with the OTS and the FDIC concerning its activities and financial condition in addition to obtaining regulatory approvals prior to entering into certain transactions such as mergers with, or acquisitions of, other savings institutions. The OTS and/or the FDIC conduct periodic examinations to test the Bank's safety and soundness and compliance with various regulatory requirements. This regulation and supervision establishes a comprehensive framework of activities in which an institution can engage and is intended primarily for the protection of the insurance fund and depositors. The regulatory structure also gives the regulatory authorities extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of adequate loan loss reserves for regulatory purposes. Any change in such regulatory requirements and policies, whether by the OTS, the FDIC or the Congress, could have a material adverse impact on Union Financial, the Bank and their operations. Certain of the regulatory requirements applicable to the Bank and to Union Financial are referred to below or elsewhere herein. The description of statutory provisions and regulations applicable to savings institutions and their holding companies set forth in this report does not purport to be a complete description of such statutes and regulations and their effects on Union Financial and the Bank.

Holding Company Regulation

Union Financial is a nondiversified unitary savings and loan holding company within the meaning of federal law. Under prior law, a unitary savings and loan holding company, such as the Company, was not generally restricted as to the types of business activities in which it may engage, provided that the Bank continued to be a qualified thrift lender. See "Federal Savings Institution Regulation-QTL Test." The Gramm-Leach-Bliley Act of 1999 provides that no company may acquire control of a savings association after May 4, 1999 unless it engages only in the financial activities permitted for financial holding companies under the law or for multiple savings and loan holding companies as described below. Further, the Gramm-Leach-Bliley Act specifies that existing savings and loan holding companies may only engage in such activities. The Gramm-Leach-Bliley Act, however, grandfathered the unrestricted authority for activities with respect to unitary savings and loan holding companies existing prior to May 4, 1999, so long as the Bank continues to comply with the QTL Test. The Company does qualify for the grandfathered activities. Upon any non-supervisory acquisition by Union Financial of another savings institution or savings bank that meets the qualified thrift lender test and is deemed to be a savings institution by the OTS, Union Financial would become a multiple savings and loan holding company (if the acquired institution is held as a separate subsidiary) and would generally be limited to activities permissible for bank holding companies under Section 4(c)(8) of the Bank Holding Company Act, subject to the prior approval of the OTS, and certain activities authorized by OTS regulation.

A savings and loan holding company is prohibited from, directly or indirectly, acquiring more than 5% of the voting stock of another savings institution or savings and loan holding company, without prior written approval of the OTS and from acquiring or retaining control of a depository institution that is not insured by the FDIC. In evaluating applications by holding companies to acquire savings institutions, the OTS considers the financial and managerial resources and future prospects of the company and institution involved, the effect of the acquisition on the risk to the deposit insurance funds, the convenience and needs of the community and competitive factors.

The OTS may not approve any acquisition that would result in a multiple savings and loan holding company controlling savings institutions in more than one state, subject to two exceptions: (i) the approval of interstate supervisory acquisitions by savings and loan holding companies and (ii) the acquisition of a savings institution in

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another state if the laws of the state of the target savings institution specifically permit such acquisitions. The states vary in the extent to which they permit interstate savings and loan holding company acquisitions.

Although savings and loan holding companies are not subject to specific capital requirements or specific restrictions on the payment of dividends or other capital distributions, federal regulations do prescribe such restrictions on subsidiary savings institutions as described below. The Bank must notify the OTS 30 days before declaring any dividend to Union Financial. In addition, the financial impact of a holding company on its subsidiary institution is a matter that is evaluated by the OTS and the agency has authority to order cessation of activities or divestiture of subsidiaries deemed to pose a threat to the safety and soundness of the institution.

Acquisition of the Company. Under the Federal Change in Bank Control act ("CIBCA"), a notice must be submitted to the OTS if any person (including a company), a group acting in concert, seeks to acquire 10% or more of the Company's outstanding voting stock, unless the Office of Thrift Supervision has found that the acquisition will not result in a change in control of the Company. Under the CIBCA, the OTS has 60 days from the filing of a complete notice to act, taking into consideration certain factors, including the financial and managerial resources of the acquirer and the anti-trust effects of the acquisition. Any company that so acquires control would then be subject to regulation as a savings and loan holding company.

Federal Savings Institution Regulation

Business Activities. The activities of federal savings institutions are governed by federal law and regulations. These laws and regulations delineate the nature and extent of the activities in which federal associations may engage. In particular, many types of lending authority for federal association, e.g., commercial, non-residential real property loans and consumer loans, are limited to a specified percentage of the institution's capital or assets.

Capital Requirements. The OTS capital regulations require savings institutions to meet three minimum capital standards: a 1.5% tangible capital ratio, a 4% leverage ratio (3% for institutions receiving the highest rating on the CAMELS rating system) and an 8% risk-based capital ratio. In addition, the prompt corrective action standards discussed below also establish, in effect, a minimum 2% tangible capital standard, a 4% leverage ratio (3% for institutions receiving the highest rating on the CAMELS financial institution rating system), and, together with the risk-based capital standard itself, a 4% Tier I risk-based capital standard. The OTS regulations also require that, in meeting the tangible, leverage and risk-based capital standards, institutions must generally deduct investments in and loans to subsidiaries engaged in activities as principal that are not permissible for a national bank.

The risk-based capital standard for savings institutions requires the maintenance of Tier I (core) and total capital (which is defined as core capital and supplementary capital) to risk-weighted assets of at least 4% and 8%, respectively. In determining the amount of risk-weighted assets, all assets, including certain off-balance sheet assets, are multiplied by a risk-weight factor of 0% to 100%, assigned by the OTS capital regulation based on the risks believed inherent in the type of asset. Core (Tier I) capital is defined as common stockholders' equity (including retained earnings), certain noncumulative perpetual preferred stock and related surplus, and minority interests in equity accounts of consolidated subsidiaries less intangibles other than certain mortgage servicing rights and credit card relationships. The components of supplementary capital currently include cumulative preferred stock, long-term perpetual preferred stock, mandatory convertible securities, subordinated debt and intermediate preferred stock, the allowance for loan and lease losses limited to a maximum of 1.25% of risk-weighted assets and up to 45% of unrealized gains on available-for-sale equity securities with readily determinable fair values. Overall, the amount of supplementary capital included as part of total capital cannot exceed 100% of core capital.

The capital regulations also incorporate an interest rate risk component. Savings institutions with "above normal" interest rate risk exposure are subject to a deduction from total capital for purposes of calculating their risk-based capital requirements. For the present time, the OTS has deferred implementation of the interest rate risk component. At September 30, 2001, the Bank met each of its capital requirements.

The following table presents the Bank's capital position at September 30, 2001.

				Capital	
	Actual Capital	Required Capital	Excess Amount	Actual Percent	Required Percent
	(Dollars in thousands)				
Tangible	$17,812	$ 4,086	$13,726	6.54%	1.50%
Core (Leverage)	17,812	10,896	6,916	6.54	4.00
Risk-based	18,892	11,864	7,028	12.74	8.00

Prompt Corrective Regulatory Action. The OTS is required to take certain supervisory actions against undercapitalized institutions, the severity of which depends upon the institution's degree of undercapitalization. Generally, a savings institution that has a ratio of total capital to risk weighted assets of less than 8%, a ratio of Tier I (core) capital to risk-weighted assets of less than 4% or a ratio of core capital to total assets of less than 4% (3% or less for institutions with the highest examination rating) is considered to be "undercapitalized." A savings institution that has a total risk-based capital ratio less than 6%, a Tier I capital ratio of less than 3% or a leverage ratio that is less than 3% is considered to be "significantly undercapitalized" and a savings institution that has a tangible capital to assets ratio equal to or less than 2% is deemed to be "critically undercapitalized." Subject to a narrow exception, the OTS is required to appoint a receiver or conservator for an institution that is "critically undercapitalized." The regulation also provides that a capital restoration plan must be filed with the OTS within 45 days of the date a savings institution receives notice that it is "undercapitalized," "significantly undercapitalized" or "critically undercapitalized." Compliance with the plan must be guaranteed by any parent holding company. In addition, numerous mandatory supervisory actions become immediately applicable to an undercapitalized institution, including, but not limited to, increased monitoring by regulators and restrictions on growth, capital distributions and expansion. The OTS could also take any one of a number of discretionary supervisory actions, including the issuance of a capital directive and the replacement of senior executive officers and directors.

Insurance of Deposit Accounts. Deposits of the Bank are presently insured by the SAIF. The FDIC maintains a risk-based assessment system by which institutions are assigned to one of three categories based on their capitalization and one of three subcategories based on examination ratings and other supervisory information. An institution's assessment rate depends upon the categories to which it is assigned. Assessment rates for SAIF member institutions are determined semiannually by the FDIC and currently range from zero basis points for the healthiest institutions to 27 basis points for the riskiest.

The Federal Deposit Insurance Corporation has authority to increase insurance assessments. A significant increase in Savings association Insurance Fund insurance premiums would likely have an adverse effect on the operating expenses and results of operations of the Bank. Management cannot predict what insurance assessment rates will be in the future.

In addition to the assessment for deposit insurance, institutions are required to make payments on bonds issued in the late 1980s by the Financing Corporation ("FICO") to recapitalize the predecessor to the SAIF. During 2000, FICO payments for SAIF members approximated 2.07 basis points.

Insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC or the OTS. The management of the Bank does not know of any practice, condition or violation that might lead to termination of deposit insurance.

Loans to One Borrower. Federal law provides that savings institutions are generally subject to the limits on loans to one borrower applicable to national banks. A savings institution may not make a loan or extend credit to a single or related group of borrowers in excess of 15% of its unimpaired capital and surplus. An additional amount may be lent, equal to 10% of unimpaired capital and surplus, if secured by specified readily-marketable collateral. At September 30, 2001, the Bank's limit on loans to one borrower was $2.7 million, and the Bank's largest aggregate outstanding balance of loans to one borrower was $2 million.

QTL Test. Federal law requires savings institutions to meet a qualified thrift lender test. Under the test, a savings association is required to either qualify as a "domestic building and loan association" under the Internal Revenue Code or maintain at least 65% of its "portfolio assets" (total assets less: (i) specified liquid assets up to 20% of total assets; (ii) intangibles, including goodwill; and (iii) the value of property used to conduct business) in certain "qualified thrift investments" (primarily residential mortgages and related investments, including certain mortgage-

backed securities) in at least nine months out of each 12 month period.

A savings institution that fails the qualified thrift lender test is subject to certain operating restrictions and may be required to convert to a bank charter. As of September 30, 2001, the Bank met the qualified thrift lender test. Recent legislation has expanded the extent to which education loans, credit card loans and small business loans may be considered "qualified thrift investments."

Limitation on Capital Distributions. OTS regulations impose limitations upon all capital distributions by a savings institution, including cash dividends, payments to repurchase its shares and payments to shareholders of another institution in a cash-out merger. Under the regulations, an application to and the prior approval of the OTS will be required prior to any capital distribution if the institution does not meet the criteria for "expedited treatment" of applications under OTS regulations (i.e., generally, safety and soundness, compliance and Community Reinvestment Act examination ratings in the two top categories), the total capital distributions for the calendar year exceed net income for that year plus the amount of retained net income for the preceding two years, the institution would be undercapitalized following the distribution or the distribution would otherwise be contrary to a statute, regulation or agreement with OTS. If an application is not required, the institution must still provide prior notice to OTS of the capital distribution if, like the Bank, it is a subsidiary of a holding company. If the Bank's capital fell below its regulatory requirements or the OTS notified it that it was in need of more than normal supervision, the Bank's ability to make capital distributions could be restricted. In addition, the OTS could prohibit a proposed capital distribution by any institution, which would otherwise be permitted by the regulation, if the OTS determines that such distribution would constitute an unsafe or unsound practice.

Assessments. Savings institutions are required to pay assessments to the OTS to fund the agency's operations. The general assessments, paid on a semi-annual basis, are computed upon the savings institution's total assets, including consolidated subsidiaries, as reported in the Bank's latest quarterly thrift financial report. The assessments paid by the Bank in the fiscal year ended September 30, 2001 totaled $64,343.

Transactions with Related Parties. The Bank's authority to engage in transactions with "affiliates" (e.g., any company that controls or is under common control with an institution, including the Company and its non-savings institution subsidiaries) is limited by federal law. The aggregate amount of covered transactions with any individual affiliate is limited to 10% of the capital and surplus of the savings institution. The aggregate amount of covered transactions with all affiliates is limited to 20% of the savings institution's capital and surplus. Certain transactions with affiliates are required to be secured by collateral in an amount and of a type described in federal law. The purchase of low quality assets from affiliates is generally prohibited. The transactions with affiliates must be on terms and under circumstances, that are at least as favorable to the institution as those prevailing at the time for comparable transactions with non-affiliated companies. In addition, savings institutions are prohibited from lending to any affiliate that is engaged in activities that are not permissible for bank holding companies and no savings institution may purchase the securities of any affiliate other than a subsidiary.

The Bank's authority to extend credit to executive officers, directors and 10% shareholders ("insiders"), as well as entities such persons control, is also governed by federal law. Such loans are required to be made on terms

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substantially the same as those offered to unaffiliated individuals and not involve more than the normal risk of repayment. An exception exists for loans made pursuant to a benefit or compensation program that is widely available to all employees of the institution and does not give preference to insiders over other employees. The law limits both the individual and aggregate amount of loans the Bank may make to insiders based, in part, on the Bank's capital position and requires certain board approval procedures to be followed.

Enforcement. The OTS has primary enforcement responsibility over savings institutions and has the authority to bring actions against the institution and all institution-affiliated parties, including stockholders, and any attorneys, appraisers and accountants who knowingly or recklessly participate in wrongful action likely to have an adverse effect on an insured institution. Formal enforcement action may range from the issuance of a capital directive or cease and desist order to removal of officers and/or directors to institution of receivership, conservatorship or termination of deposit insurance. Civil penalties cover a wide range of violations and can amount to $25,000 per day, or even $1 million per day in especially egregious cases. The FDIC has the authority to recommend to the Director of the OTS that enforcement action to be taken with respect to a particular savings institution. If action is not taken by the Director, the FDIC has authority to take such action under certain circumstances. Federal law also establishes criminal penalties for certain violations.

Standards for Safety and Soundness. The federal banking agencies have adopted Interagency Guidelines prescribing Standards for Safety and Soundness. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions before capital becomes impaired. If the OTS determines that a savings institution fails to meet any standard prescribed by the guidelines, the OTS may require the institution to submit an acceptable plan to achieve compliance with the standard.

Federal Home Loan Bank System

The Bank is a member of the Federal Home Loan Bank System, which consists of 12 regional Federal Home Loan Banks. The Federal Home Loan Bank provides a central credit facility primarily for member institutions. The Bank, as a member of the Federal Home Loan Bank-Atlanta, is required to acquire and hold shares of capital stock in the Federal Home Loan Bank-Atlanta in an amount at least equal to 1.0% of the aggregate principal amount of its unpaid residential mortgage loans and similar obligations at the beginning of each year, or 1/20 of its advances (borrowings) from the Federal Home Loan Bank-Atlanta, whichever is greater. The Bank was in compliance with this requirement with an investment in Federal Home Loan Bank stock at September 30, 2001, of $2.6 million.

The Federal Home Loan Banks are required to provide funds for the resolution of insolvent thrifts and to contribute funds for affordable housing programs. These requirements could reduce the amount of dividends that the Federal Home Loan Banks pay to their members and could also result in the Federal Home Loan Banks imposing a higher rate of interest on advances to their members. If dividends were reduced, or interest on future Federal Home Loan Bank advances increased, the Bank's net interest income would likely also be reduced. Recent legislation has changed the structure of the Federal Home Loan Banks' funding obligations for insolvent thrifts, revised the capital structure of the Federal Home Loan Banks and implemented entirely voluntary membership for Federal Home Loan Banks. Management cannot predict the effect that these changes may have with respect to its Federal Home Loan Bank membership.

Federal Reserve System

The Federal Reserve Board regulations require savings institutions to maintain non-interest earning reserves against their transaction accounts (primarily NOW and regular checking accounts). The regulations generally provide that reserves be maintained against aggregate transaction accounts as follows: a 3% reserve ratio is assessed on net transaction accounts over $5.7 million to and including $41.3 million and a 10% reserve ratio is applied above $41.3 million. The first $5.7 million of otherwise reservable balances are exempted from the reserve requirements. The Bank complies with the foregoing requirements.

FEDERAL AND STATE TAXATION

Federal Taxation

General. Union Financial and the Bank report their income on a fiscal year, consolidated basis and the accrual method of accounting, and are subject to federal income taxation in the same manner as other corporations with some exceptions, including particularly the Bank's reserve for bad debts discussed below. The following discussion of tax matters is intended only as a summary and does not purport to be a comprehensive description of the tax rules applicable to Union Financial or the Bank. For its 2001 taxable year, Union Financial is subject to a maximum federal income tax rate of 34%.

Bad Debt Reserves. For fiscal years beginning prior to December 31, 1995, thrift institutions which qualified under certain definitional tests and other conditions of the Internal Revenue Code were permitted to use certain favorable provisions to calculate their deductions from taxable income for annual additions to their bad debt reserve. A reserve could be established for bad debts on qualifying real property loans (generally secured by interests in real property improved or to be improved) under (i) the percentage of taxable income method or (ii) the experience method. The reserve for nonqualifying loans was computed using the experience method.

Congress repealed the reserve method of accounting for bad debts for tax years beginning after 1995 and required savings institutions to recapture (i.e., take into income) certain portions of their accumulated bad debt reserves. Thrift institutions eligible to be treated as "small banks" (assets of $500 million or less) are allowed to use the experience method applicable to such institutions, while thrift institutions that are treated as large banks (assets exceeding $500 million) are required to use only the specific charge-off method. Thus, the percentage of taxable income method of accounting for bad debts is no longer available for any financial institution.

A thrift institution required to change its method of computing reserves for bad debts will treat such change as a change in method of accounting, initiated by the taxpayer, and having been made with the consent of the Internal Revenue Service. Any Section 481(a) adjustment required to be taken into income with respect to such change generally will be taken into income ratably over a six-taxable year period, beginning with the first taxable year beginning after 1995, subject to a 2-year suspension if the "residential loan requirement" is satisfied.

Under the residential loan requirement provision, the required recapture will be suspended for each of two successive taxable years, beginning with the Bank's 1996 taxable year, in which the Bank originates a minimum of certain residential loans based upon the average of the principal amounts of such loans made by the Bank during its six taxable years preceding its current taxable year.

Distributions. If the Bank makes "non-dividend distributions" to Union Financial, such distributions will be considered to have been made from the Bank's unrecaptured tax bad debt reserves

(including the balance of its reserves as of December 31, 1987) to the extent thereof, and then from the Bank's supplemental reserve for losses on loans, to the extent thereof, and an amount based on the amount distributed (but not in excess of the amount of such reserves) will be included in the Bank's income. Non-dividend distributions include distributions in excess of the Bank's current and accumulated earnings and profits, as calculated for federal income tax purposes, distributions in redemption of stock, and distributions in partial or complete liquidation. Dividends paid out of the Bank's current or accumulated earnings and profits will not be so included in its income.

The amount of additional taxable income triggered by a non-dividend is an amount that, when reduced by the tax attributable to the income, is equal to the amount of the distribution. Thus, if the Bank makes a non-dividend distribution to Union Financial, approximately one and one-half times the amount of such distribution (but not in excess of the amount of such reserves) would be includable in income for federal income tax purposes, assuming a 35% federal corporate income tax rate. The Bank does not intend to pay dividends that would result in a recapture of any portion of its bad debt reserves.

State Taxation

South Carolina. The Bank is subject to tax under South Carolina law. South Carolina law allows a savings and loan association to use the federal bad debt deduction method for the purpose of computing net income subject to state tax, and the present South Carolina tax rate on taxable income is 6%. In order to calculate taxable income for South Carolina taxation purposes, a corporation begins with its federal taxable income and then modifies it to take into account certain adjustments. Adjustments which would be common to most financial institutions include an addition for state taxes deducted on the federal return, and a subtraction for interest on certain federal obligations and securities. South Carolina income tax is deductible for federal income tax purposes. In addition, Union Financial is subject to South Carolina taxes as a regular corporation and pays taxes based on its shareholders' equity.

Delaware. As a Delaware holding company not earning income in Delaware, Union Financial is exempted from Delaware corporate income tax, but is required to file an annual report with and pay an annual franchise tax to the State of Delaware.

Item 2. Description of Property

The Corporation owns its main office, located at 203 West Main Street in Union, South Carolina, which was opened in 1977. At September 30, 2001, the Corporation also owned a banking center which opened in April 1989, located at 508 North Duncan By-Pass, Union, South Carolina, a branch office, acquired in 1997, in Laurens, South Carolina, a lending and investment center located in Union, South Carolina and a branch office in Jonesville, South Carolina. As a result of the merger with South Carolina Community Bancshares in November 1999, the Corporation acquired two branch locations in Winnsboro, South Carolina. The net book value of the Corporation's investment in premises and equipment totaled approximately $7.2 million at September 30, 2001. See Note 5 of Notes to Consolidated Financial Statements. All property is in good condition and meets the operating needs of the Corporation.

Item 3. Legal Proceedings

Neither Union Financial nor the Bank is engaged in any legal proceedings of a material nature at the present time. From time to time, the Bank is involved in routine legal proceedings occurring in the ordinary course of business wherein it enforces the Bank's security interest in mortgage loans the Bank has made.

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

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year ended September 30, 2001.

PART II

Item 5. Market for Common Equity and Related Stockholder Matters

The information contained under the section captioned "Common Stock Market Price and Dividend Information" in the Annual Report to Shareholders (the "Annual Report") is incorporated herein by reference.

Item 6. Management's Discussion and Analysis of Financial Condition and

Results of Operations

The information contained in the section captioned "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Annual Report is incorporated herein by reference.

Item 7. Financial Statements

The financial statements contained in the Annual Report are incorporated herein by reference.

Item 8. Changes In and Disagreements With Accountants on Accounting and Financial Disclosure

No changes in or disagreements with the Corporation's independent accountants on accounting and financial disclosure has occurred during the two most recent fiscal years.

PART III

Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act

For information concerning the Board of Directors of Union Financial, the information contained under the section captioned "Proposal I -- Election of Directors" and "Directors' Compensation" in the Proxy Statement is incorporated herein by reference. Reference is made to the cover page of this Form 10-KSB and to the section captioned "Compliance with Section 16(a) of the Exchange Act" for information regarding compliance with section 16(a) of the Exchange Act.

Executive Officers of the Registrant

Certain executive officers of the Bank also serve as executive officers of Union Financial. The day-to-day management duties of the executive officers of Union Financial and the Bank relate primarily to their duties as to the Bank. The executive officers of Union Financial currently are as follows:

Name	Age(1)	Position as of September 30, 2001
Dwight V. Neese	51	President, Chief Executive Officer and Director
Richard H. Flake	53	Executive Vice President - Chief Financial Officer
Anthony E. Lawton	38	Senior Vice President - Chief Credit Officer
Wanda J. Wells	45	Vice President - Corporate Secretary

(1) At September 30, 2001.

Dwight V. Neese was appointed as President and Chief Executive Officer of the Bank effective September 5, 1995. As President and Chief Executive Officer of Provident Community Bank and the Corporation, Mr. Neese is responsible for daily operations of the Bank and implementation of the policies and procedures approved by the Board of Directors.

Richard H. Flake joined Union Financial in September 1995.

Anthony E. Lawton joined Union Financial in January 2000. Prior to joining Union Financial, Mr. Lawton was Senior Vice President for Anchor Bank in Clinton, South Carolina.

Wanda J. Wells has been employed by Union Financial since 1975.

Item 10. Executive Compensation

The information contained under the section captioned "Executive Compensation" in the Proxy Statement is incorporated herein by reference.

Item 11. Security Ownership of Certain Beneficial Owners and Management

(a) Security Ownership of Certain Beneficial Owners

Information required by this item is incorporated herein by reference to the section captioned "Stock Ownership" in the Proxy Statement.

(b) Security Ownership of Management

Information required by this item is incorporated herein by reference to the section captioned "Stock Ownership" in the Proxy Statement.

(c) Management of Union Financial knows of no arrangements, including any pledge by any person of securities of Union Financial, the operation of which may at a subsequent date result in a change in control of the registrant.

Item 12. Certain Relationships and Related Transactions

The information required by this item is incorporated herein by reference to the section captioned "Transactions with Management" in the Proxy Statement.

PART IV

Item 13. Exhibits and Reports on Form 8-K

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(a)  Exhibits
     3(a)    Certificate of Incorporation(1)
     3(b)    Bylaws(2)
     3(c)    Certificate of Amendment of Certificate of Incorporation
             dated January 22, 1997(3)
     10(a)   Employment Agreement with Dwight V. Neese(4)
     10(b)   Employment Agreement with Richard H. Flake(2)
     10(c)   Union Financial Bancshares, Inc. 1995 Stock Option Plan(5)
     10(d)   Union Financial Bancshares, Inc. 2000 Stock Option Plan(6)
     13      2001 Annual Report to Shareholders
     21      Subsidiaries of the Registrant
     23      Consent of Independent Auditor
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(b) There were no reports on Form 8-K filed during the fourth quarter of fiscal 2001.

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(1) Incorporated herein by reference to Union Financial's Registration Statement on Form S-4 (File No. 33-80808) filed with the Securities and Exchange Commission on June 29, 1994.
(2) Incorporated herein by reference to Union Financial's Form 10-KSB for the year ended September 30, 1999.
(3) Incorporated herein by reference to Exhibit 3(c) to Union Financial's Form 10-KSB for the year ended September 30, 1997.
(4) Incorporated herein by reference to Union Financial's Form 10-KSB for the year ended September 30, 1996.
(5) Incorporated herein by reference to Exhibit A to Union Financial's Proxy Statement for its 1996 Annual Meeting of Stockholders.
(6) Incorporated herein by reference to Appendix A to Union Financial's Proxy Statement for its 2000 Annual Meeting of Stockholders.

SIGNATURES

In accordance with the requirements of Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

UNION FINANCIAL BANCSHARES, INC.

Date: December 18, 2001

By: /S/ Dwight V. Neese

Dwight V. Neese
President and Chief Executive Officer
Duly Authorized Representative

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Dwight V. Neese

Dwight V. Neese
(Principal Executive Officer)

Date: December 18, 2001

By: /s/ Richard H. Flake

Richard H. Flake
(Principal Financial and Accounting Officer)

Date: December 18, 2001

By: /s/ Mason G. Alexander

Mason G. Alexander
Director

Date: December 18, 2001

By: /s/ James W. Edwards

James W. Edwards
Director

Date: December 18, 2001

By: /s/ William M. Graham

William M. Graham
Director

Date: December 18, 2001

By: /s/ Carl L. Mason

Carl L. Mason
Director

Date: December 18, 2001

By: /s/ John S. McMeekin

John S. McMeekin
Director

Date: December 18, 2001

By: /s/ Philip C. Wilkins

Philip C. Wilkins
Director

Date: December 18, 2001

By: /s/ Louis M. Jordan

Louis M. Jordan
Director

Date: December 18, 2001

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BUSINESS

Union Financial Bancshares, Inc. ("Union Financial") is the savings and loan holding company for Provident Community Bank, ("the Bank"). Union Financial engages in no significant activity other than holding the stock of the Bank and engaging in certain passive investment activities. Union Financial and the Bank are collectively referred to as "the Corporation" in this annual report.

The Bank is a federally-chartered capital stock savings bank headquartered in Union, South Carolina. The Bank, originally chartered in 1934, is a member of the Federal Home Loan Bank System ("FHLB"). Its deposits are insured to the maximum limits allowable by the Federal Deposit Insurance Corporation ("FDIC").

The business of the Bank consists primarily of attracting deposits from the general public and originating mortgage loans on residential properties located in South Carolina. The Bank also makes consumer and commercial loans, commercial real estate loans, and construction loans, invests in federal government and agency obligations and purchases fixed and variable rate mortgage participation certificates. The principal sources of funds for the Bank's lending and investing activities include deposits received from the general public and advances from the FHLB. The Bank's principal expenses are interest paid on deposit accounts and other borrowings and expenses incurred in the operation of the Bank. The Bank's operations are conducted through its main office and five full-service banking centers, all of which are located in the upstate area of South Carolina.

SELECTED FINANCIAL AND OTHER DATA

The following tables set forth selected financial data of the Corporation for the periods indicated.

Operations Data:

	Years Ended September 30,				
	2001	2000	1999	1998	1997
	Dollars In Thousands - Except Share Amounts)				
Interest income	$ 19,018	$ 18,555	$ 14,046	$ 13,405	$ 11,855
Interest expense	(11,613)	(11,175)	(7,698)	(7,549)	(6,647)
Net interest income	7,405	7,380	6,348	5,856	5,208
Provision for loan losses	(240)	(225)	(105)	--	(243)
Net interest income after provision for loan losses	7,165	7,155	6,243	5,856	4,965
Other income	1,149	2,580	1,192	1,038	953
Other expense	(6,250)	(6,352)	(4,814)	(4,447)	(3,616)
Income before income taxes	2,064	3,383	2,621	2,447	2,302
Income tax expense	(721)	(1,190)	(945)	(897)	(858)
Net income	$ 1,343	$ 2,193	$ 1,676	$ 1,550	$ 1,444
Income per common share: (1)					
Net income per common share (Basic)	$ 0.70	$ 1.18	$ 1.26	$ 1.17	$ 1.12
Net income per common share (Diluted)	$ 0.68	$ 1.16	$ 1.19	$ 1.10	$ 1.04
Weighted average number of common shares outstanding (Basic)	1,918,431	1,855,706	1,328,305	1,327,845	1,292,284
Weighted average number of common shares outstanding (Diluted)	1,971,611	1,898,494	1,414,121	1,410,158	1,391,988

(1) 1999, 1998 and 1997 share and per share amounts have been restated for the 3:2 stock split occurring in February 1998 and the 5% stock dividend occurring in February 1999.

Financial Condition:

	September 30,				
	2001	2000	1999	1998	1997
	(Dollars In Thousands)				
Total amount of:					
Assets	$277,752	$260,564	$205,294	$189,286	$171,244
Short-term interest-bearing deposits	5,694	4,500	2,781	1,124	6,213
Investment securities	24,170	19,432	15,506	9,633	16,783
Mortgage-backed securities	64,947	47,460	17,415	19,922	6,883
Loans (net)	158,063	167,807	149,401	142,202	129,957
Deposits	194,079	187,974	142,624	130,768	117,914
Shareholders' equity	24,376	21,924	14,738	15,300	13,527
Number of:					
Real estate loans outstanding	1,783	2,216	1, 411	1,651	1,706
Deposit accounts	30,240	28,526	18,865	17,686	16,443
Banking centers	6	7	5	4	4

Other Selected Data:

	Years Ended September 30,				
	2001	2000	1999	1998	1997
Interest rate spread during the year	2.98%	3.02%	3.36%	3.09%	3.16%
Net yield on average interest-earning assets	3.08%	3.10%	3.46%	3.42%	3.44%
Return on average assets	0.51%	0.85%	0.85%	0.87%	0.92%
Return on average shareholders' equity	6.03%	10.92%	10.96%	10.77%	11.21%
Dividend payout ratio	57.03%	26.13%	29.46%	30.08%	30.13%
Operating expense to average assets	2.39%	2.44%	2.43%	2.52%	2.31%
Ratio of average shareholders' equity to average assets	8.50%	7.78%	7.44%	8.12%	8.24%
Cash dividends declared and paid per share of common stock (1)	$0.40	$0.40	$0.37	$0.35	$0.34

(1) 1999, 1998 and 1997 share and per share amounts have been restated for the 3:2 stock split occurring in February 1998 and the 5% stock dividend occurring in February 1999.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Asset and Liability Management

The Corporation is committed to following a program of asset and liability management in an effort to manage the fluctuations in earnings caused by movements in interest rates. A significant portion of the Corporation's income results from the spread, or net interest income, between the yield realized on its interest-earning assets and the rate of interest paid on its deposits and other borrowings. Differences in the timing and volume of repricing assets versus the timing and volume of repricing liabilities expose the Corporation to interest rate risk. Management's policies are directed at minimizing the impact on earnings of movements in interest rates.

The Corporation continues to work to shorten the average life of its assets and to extend the term on its liabilities in an effort to help minimize the effects of rising interest rates. The Corporation enjoys an increasing net interest rate spread during periods of falling interest rates. The Corporation experiences a shrinking net interest rate spread in a rising interest rate environment.

The Corporation's Asset/Liability Committee makes weekly pricing and marketing decisions on deposit and loan products in conjunction with managing the Corporation's interest rate risk. The Asset/Liability Committee reviews the Bank's securities portfolio, FHLB advances and other borrowings as well as the Bank's asset and liability policies.

The Corporation has established policies and monitors results to control interest rate sensitivity. Although the Corporation utilizes measures such as static gap, which is simply the measurement of the difference between interest-sensitive assets and interest-sensitive liabilities repricing for a particular time period, just as important a process is the evaluation of how particular assets and liabilities are impacted by changes in interest rates or selected indices as they reprice. Asset/liability modeling techniques are utilized by the Corporation to assess varying interest rate and balance sheet mix assumptions.

At September 30, 2001 the Corporation's exposure to interest rate risk, as calculated by the Office of Thrift Supervision (OTS) and measured by the impact of changing interest rates on the Net Portfolio Value ("NPV"), was as follows:

	Rate Environment		
	Minus 200 Basis Points	Flat	Plus 200 Basis Points
		(In Thousands)	
Estimated Market Value of Assets	$293,662	$281,376	$266,191
Estimated Market Value of Liabilities	$263,067	$258,915	$254,487
NPV	$ 30,595	$ 22,461	$ 11,704
Increase/(decrease) in NPV	$ 8,134	$ -	($ 10,757)

The analysis above indicates that the Corporation would be negatively affected by an increase in interest rates and positively affected by a decrease in interest rates.

Yields Earned and Rates Paid

The Corporation's pretax earnings depend primarily on its net interest income, the difference between the income it receives on its loan portfolio and other investments and its cost of funds, consisting primarily of interest paid on savings deposits and borrowings. Net interest income is affected by the average yield on interest-earning assets, the average rate on interest-bearing liabilities, and the ratio of interest-earning assets to interest-bearing liabilities.

The following table sets forth, at or for the periods and dates indicated, the weighted average yields earned on the Corporation's interest-earning assets, the weighted average interest rates paid on the Corporation's deposit accounts and borrowings, the interest rate spread and net yield on interest-earning assets.

	At September 30,	Years Ended September 30		
	2001	2001	2000	1999
Average yield on earnings assets:				
Loans	8.37%	8.85%	8.31%	8.03%
Investments (1)	5.90%	5.92%	6.27%	6.35%
Mortgage-backed securities	5.97%	5.94%	5.84%	6.31%
Total interest-earning assets	7.50%	7.92%	7.79%	7.65%
Less:				
Average rate paid on deposits	4.11%	4.70%	4.53%	4.08%
Average rate paid on borrowings	5.41%	5.92%	5.67%	5.04%
Average Cost of Funds	4.41%	4.94%	4.77%	4.29%
Average interest rate spread	3.09%	2.98%	3.02%	3.36%
Net yield on average interest-earning assets	3.18%	3.08%	3.10%	3.46%

(1) Includes investment securities, federal funds sold, interest-bearing time deposits, overnight interest-bearing deposits and Federal Home Loan Bank stock.

Rate/Volume Analysis

The following table sets forth certain information regarding changes in interest income and interest expense of the Corporation for the periods indicated. For each category of interest-earning assets and interest-bearing liabilities, information is provided on changes attributable to (1) changes in volume (changes in volume multiplied by prior rate); (2) changes in rate (changes in rate multiplied by prior volume); and (3) the total. The net change attributable to the combined impact of rate and volume has been allocated to rate and volume variances consistently on a proportionate basis.

	Years Ended September 30,					
	2001 vs. 2000			2000 vs. 1999		
	Volume	Rate	Total	Volume	Rate	Total
	(Dollars in Thousands)					
Change in interest income:						
Loans	($1,665)	$ 880	($ 785)	$ 3,347	$ 516	$ 3,863
Mortgage-backed securities	1,143	47	1,190	347	(136)	211
Investments	155	(97)	58	454	(20)	434
Total interest income	(367)	830	463	4,148	360	4,508
Change in interest expense:						
Deposits	143	312	455	1,826	834	2,660
Borrowings and other	(133)	116	(17)	508	308	816
Total interest expense	10	428	438	2,334	1,142	3,476
Change in net interest income	($ 377)	$ 402	$ 25	$ 1,814	($ 782)	$ 1,032

RESULTS OF OPERATIONS

Comparison of Years Ended September 30, 2001 and September 30, 2000

Net income decreased $850,000 from $2,193,000 in fiscal 2000 to $1,343,000 in fiscal 2001. Earnings per share were $.70 per share (basic) and $.68 per share (diluted) for the year ended September

30, 2001 compared to $1.18 per share
(basic) and $1.16 per share (diluted) for the same period in 2000. The decrease in net income was due to reduced mortgage loan service fees and lower gain on sale of mortgage loans. A sale of the Bank's mortgage loan servicing portfolio that was completed during the fourth quarter of fiscal 2000 contributed $700,000 to non interest income in fiscal 2000. As a result of this sale, the Company phased out its wholesale mortgage unit during the third quarter of the current fiscal year.

Total interest income increased $463,000 or 2.50%, from $18,555,000 in fiscal 2000 to $19,018,000 in fiscal 2001. Interest income on loans decreased $785,000, or 5.14%, from $15,272,000 in fiscal 2000 to $14,487,000 in fiscal 2001 due primarily to the reduction of the loan portfolio as a result of lower residential mortgage loan production. The reduction in income due to lower residential loan production was somewhat offset by growth in higher yielding commercial loans. Interest income on investment and mortgage-backed securities increased $1,248,000, or 38.01%, from $3,283,000 in fiscal 2000 to $4,531,000 in fiscal 2001. The increase was due primarily to purchases of investment and mortgage-backed securities made during the current fiscal year.

Interest expense increased 3.92% to $11,613,000 for fiscal 2001 from $11,175,000 for fiscal 2000. Interest expense increased $455,000 for deposits and decreased $17,000 for other borrowings. Interest expense for deposits increased due to the growth in deposits along with higher rates on certificates of deposits at the beginning of the year. Interest expense on other borrowings decreased due to higher rates as a result of longer term maturities offset by lower average balances throughout fiscal 2001 as compared to fiscal 2000. The longer term borrowings increase will improve interest rate risk exposure.

Provisions for loan losses are charges to earnings to bring the total allowance for loan losses to a level considered by management as adequate to provide for estimated loan losses based on management's evaluation of the collectibility of the loan portfolio. The provision for loan loss calculation includes a segmentation of loan categories subdivided by residential mortgage, commercial and consumer loans. Each category is risk rated for all loans

including performing groups. The weight assigned to each performing group is developed from a threeyear historical average loan loss experience ratio and as the loss experience changes, the category weight is adjusted accordingly. In addition to loan loss experience, managements evaluation of the loan portfolio will include the market value of the underlying collateral, growth and composition of the loan portfolio, delinquency trends and economic conditions. Management evaluates the carrying value of loans periodically, and the allowance for loan losses is adjusted accordingly. The provision for loan losses increased from $225,000 in fiscal 2000 to $240,000 in fiscal 2001. See Note 4 of Consolidated Financial Statements for an analysis of loans.

The Corporation experienced bad debt charge-offs, net of recoveries, of approximately $520,000 in fiscal 2001 compared to $150,000 for fiscal 2000. The increase in bad debt charge-offs over the previous year includes approximately $210,000 from two commercial loan customers that filed for bankruptcy. The allowance for loan losses to total loans ratio at the end of fiscal 2001 was .67% compared to .80% at the end of fiscal 2000. Nonperforming assets which includes repossessed assets and loans on non accrual decreased to $915,000 at September 30, 2001 from $1,579,000 at September 30, 2000.

Non-interest income decreased 55.47% to $1,149,000 for the year ended September 30, 2001 from $2,580,000 for the year ended September 30, 2000. Service charges and fees decreased $310,000 to $928,000, primarily due to a reduction in production from Provident Financial Services, a wholly-owned subsidiary of Provident Community Bank. Provident Financial Services, which offers brokerage services, had experienced an increase in its business in 2000 which decreased in fiscal 2001 due to changing economic conditions for brokerage relationships. Loan servicing fees (net) decreased $454,000 to $(103,000) for the year ended September 30, 2001 from $351,000 for the year ended September 30, 2000. The reduction in loan servicing fees (net) was due to the sale of the loan servicing rights that was completed on September 30, 2000. In addition, higher loan prepayment speeds for the current year resulted in servicing rights amortization expense exceeding service fee income. Gain on sale of loans and investments decreased $667,000 to $324,000 during the year ended September 30, 2001 from $991,000 for the year ended September 30, 2000. During the previous fiscal year the Corporation sold approximately $250 million of servicing rights resulting in a pre-tax gain of approximately $700,000.

Non-interest expense decreased 1.61% to $6,250,000 in fiscal 2001 from $6,352,000 in fiscal 2000. The Company phased out its wholesale mortgage unit in fiscal 2001, completing the process during the third quarter. Compensation and employee benefits decreased 7.57% or $238,000 from fiscal 2000 to fiscal 2001 due primarily to the staff reductions from the phase out of the mortgage operation. Occupancy and equipment expenses decreased 6.32% or $90,000 from fiscal 2000 to fiscal 2001 due to expense reductions realized from the previous fiscal year data processing conversion. Professional services expense increased 23.76% or $72,000 from fiscal 2000 to fiscal 2001 due to higher usage of external consultants for loan operations. Other operating expenses increased 10.40% or $154,000 from fiscal 2000 to fiscal 2001 due to increases in amortization of intangibles, postage, telephone, liability insurance and expenses associated with shareholder relations.

Comparison of Years Ended September 30, 2000 and September 30, 1999

Net income increased $517,000 from $1,676,000 in fiscal 1999 to $2,193,000 in fiscal 2000. Earnings per share were $1.18 per share (basic) and $1.16 per share (diluted) for the year ended September 30, 2000 compared to $1.26 per share
(basic) and $1.19 per share (diluted) for the same period in 1999. Outstanding shares increased 41% from 1,357,214 to 1,911,005 due to shares issued for the acquisition of SCCB which was completed on November 12, 1999. See Note 2 of Consolidated Financial Statements for a discussion of the acquisition of SCCB.

Total interest income increased $4,509,000, or 32.10%, from $14,046,000 in fiscal 1999 to $18,555,000 in fiscal 2000. All interest income categories were impacted by the acquisition of South Carolina Community Bancshares. Interest income on loans increased $3,852,000, or 33.73%, from $11,420,000 in fiscal 1999 to $15,272,000 in fiscal 2000 due primarily to the growth of the loan portfolio. Interest income on investment and mortgage-backed securities increased $657,000, or 25.02%, from $2,626,000 in fiscal 1999 to $3,283,000 in fiscal 2000. The increase was due primarily to purchases in investment and mortgage-backed securities along with $2,602,000 in investments acquired from SCCB.

Interest expense increased 45.17% to $11,175,000 for fiscal 2000 from $7,698,000 for fiscal 1999. Interest expense increased $2,661,000 for deposits and increased $816,000 for other borrowings. Interest expense for deposits increased due to the growth in deposits that were acquired from SCCB along with higher rates paid on deposits for the current year. Interest expense on other borrowings increased due to higher interest rates on FHLB advances along with higher volumes throughout fiscal 2000 as compared to fiscal 1999.

Provisions for loan losses are charges to earnings to bring the total allowance for loan losses to a level considered by management as adequate to provide for estimated loan losses based on management's evaluation of the collectibility of the loan portfolio. The provision for loan losses increased from $105,000 in fiscal 1999 to $225,000 in fiscal 2000. The increase in the provision was made to provide an adequate level of reserves to be consistent with the growth in the Corporation's loan portfolio as a result of the acquisition of SCCB along with an increased level of non accrual loans from the previous year. See Note 4 of Consolidated Financial Statements for an analysis of loans.

The Corporation experienced bad debt charge-offs, net of recoveries, of approximately $150,000 in fiscal 2000 compared to $96,000 for fiscal 1999. The allowance for loan losses to total loans ratio at the end of fiscal 2000 was .80% compared to .56% at the end of fiscal 1999.

Non-interest income increased 116.44% to $2,580,000 for the year ended September 30, 2000 from $1,192,000 for the year ended September 30, 1999. Service charges and fees increased $333,000 to $1,238,000 primarily from increased deposit account fees as a result of the acquisition of SCCB. The deposit balances acquired totaled $35,688,000. Loan servicing fees (net) increased $415,000 to $351,000 for the year ended September 30, 2000 from $(64,000) for the year ended September 30, 1999. The improvement in loan servicing fees (net) was due to a reduction in loan premium amortization along with higher loan service fees as a result of the higher level of loan servicing. Gain on sale of loans increased to $991,000 during the year ended September 30, 2000 from $342,000 for the year ended September 30, 1999. During the current fiscal year the Corporation sold approximately $250 million of servicing rights resulting in a pre-tax gain of approximately $700,000.

Non-interest expense increased 31.95% to $6,352,000 in fiscal 2000 from $4,814,000 in fiscal 1999. All expenses were affected by the acquisition of SCCB. Compensation and employee benefits increased 32.73% or $775,000 from fiscal 1999 to fiscal 2000 due primarily to the additional staff assumed in the merger. Occupancy and equipment expenses increased 25.77% or $292,000 from fiscal 1999 to fiscal 2000 due to higher depreciation expense along with higher data processing expenses due to the growth of the Bank. Goodwill amortization increased 122.10% or $337,000 due to the amortization of goodwill costs assumed with the acquisition of SCCB. Other operating expenses increased 14.96% or $101,000 from fiscal 1999 to fiscal 2000 due primarily to higher costs associated with the acquisition of South Carolina Community Bancshares.

Financial Condition, Liquidity and Capital Resources

At September 30, 2001, the Corporation's assets totaled $277,752,000, an increase of $17,188,000 or 6.60% as compared to $260,564,000 at September 30, 2000. Investment and mortgage-backed securities increased $22,225,000 to $89,117,000 from $66,892,000 at September 30, 2000. The increase in securities provided additional balance sheet growth and offset the decrease in loans, which was a result of reductions in residential mortgage loans. Total loans, net, decreased $9,744,000 or 5.81% to $158,063,000 from $167,807,000 at September 30, 2000. The reduction in residential

mortgage loans reflects the Corporations movement toward higher yielding consumer and commercial loans that will provide improvements in interest rate risk exposure. The overall growth in total assets was funded by increased deposits and additional borrowings. Securities sold under agreements to repurchase was $11,000,000 at September 30, 2001 compared to $0 at September 30, 2000. The increase in securities sold under agreement to repurchase is a lower cost funding alternative to Federal Home Loan Bank advances. Total deposits increased $6,105,000 or 3.25% from $187,974,000 at September 30, 2000 to $194,079,000 on September 30, 2001. The growth was a result of various deposit promotion programs with continued emphasis on increasing core deposits.

The Bank's liquidity, as measured by the ratio of cash, cash equivalents (not committed, pledged or required to liquidate specific liabilities) and investment securities to total deposits was approximately 25.43% at September 30, 2001. Assets that qualify as eligible liquidity include cash and cash equivalents and certain types of United States

Treasury and agency obligations, and other similar investments. Liquidity management is both a short and long-term responsibility of the Bank's management. The Bank adjusts its investments in liquid assets based upon management's assessment of (i) expected loan demand, (ii) expected deposit flows, (iii) yields available on interest-bearing deposits, and (iv) liquidity of its asset/liability management program. Excess liquidity is generally invested in interest-bearing overnight deposits and other short-term government and agency obligations. The Bank has relied upon deposit growth and loan repayments as its principal sources of liquidity. If deposit growth and loan repayments do not generate sufficient liquid funds in the future, the Bank may borrow additional funds from the FHLB or liquidate short-term investments. These sources of funds are intended to provide a secondary source of relatively liquid funds upon which the Bank may rely, if necessary. See Note 14 to the financial statements for further information about commitments and contingencies.

At September 30, 2001, the Corporation's shareholder equity totaled $24,376,000, an increase of $2,452,000 or 11.18%, as compared to $21,924,000 at September 30, 2000. In addition to net income after dividends, available for sale securities valuation improved $1,868,000 from ($2,050,000) at September 30, 2000 to ($182,000) at September 30, 2001.

At September 30, 2001, the undisbursed portion of construction loans was $6.1 million and the unused portion of credit lines was $8.1 million. Funding for these commitments is expected to be provided from deposits, loan and mortgage-backed securities principal repayments, maturing investments and income generated from operations.

As of September 30, 2001, the Bank exceeded the OTS's capital requirements. See Note 16 to the Consolidated Financial Statements for further discussion of these capital requirements.

Impact of Inflation and Changing Prices

The financial statements and related data presented herein have been prepared in accordance with accounting principles generally accepted in the United States, which require the measurement of financial position and operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. Unlike industrial companies, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, interest rates have a more significant impact on a financial institution's performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. However, non-interest expenses do reflect general levels of inflation.

Forward-Looking Statements

Management's Discussion and Analysis of Financial Condition and Results of Operations and other portions of this report contain certain "forward-looking statements" concerning the future operations of the Corporation. Management desires to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995 and is including this statement for the express purpose of availing the Corporation of the protections of such safe harbor with respect to all "forward-looking statements" contained in our Annual Report. We have used "forward-looking statements" to describe future plans and strategies. Management's ability to predict results or the effect of future plans or strategies is inherently uncertain. Factors which could affect actual results include interest rate trends, the general economic climate in the Corporation's market area and the country as a whole, the ability of the Corporation to control costs and expenses, the ability of the Corporation to efficiently incorporate acquisitions into its operations, competitive products and pricing, loan delinquency rates, and changes in federal and state regulation. These factors should be considered in evaluating the "forward-looking statements", and undue reliance should not be placed on such statements.

[Letterhead of Elliott Davis, LLP]

[Elliott Davis LOGO]

REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Shareholders and Board of Directors
Union Financial Bancshares, Inc. and Subsidiaries Union, South Carolina

We have audited the accompanying consolidated balance sheets of Union Financial Bancshares, Inc. and Subsidiaries as of September 30, 2001 and 2000, and the related consolidated statements of income, shareholders' equity, and cash flows for each of the years in the three-year period ended September 30, 2001. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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 provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Union Financial Bancshares, Inc. and Subsidiaries as of September 30, 2001 and 2000 and the consolidated results of their operations and their cash flows for each of the years in the three-year period ended September 30, 2001, in conformity with accounting principles generally accepted in the United States of America.

/s/ Elliott Davis LLP

Elliott Davis LLP

Elliott Davis, LLP
Greenville, South Carolina
November 1, 2001

UNION FINANCIAL BANCSHARES, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

	September 30, 2001	September 30, 2000
	(In Thousands)	
Assets		
Cash	$ 914	$ 113
Short term interest-bearing deposits	5,694	4,500
Total cash and cash equivalents	6,608	4,613
Investment and mortgage-backed securities:		
Held to maturity	11,315	37,652
Available for sale	77,802	29,240
Total investment and mortgage-backed securities	89,117	66,892
Loans, net		
Held for sale	--	1,801
Held for investment	158,063	166,006
Total loans, net	158,063	167,807
Office properties and equipment, net	7,204	6,485
Federal Home Loan Bank Stock, at cost	2,625	2,625
Accrued interest receivable	1,629	1,629
Intangible assets	6,299	7,042
Mortgage servicing rights	842	452
Cash surrender value of life insurance	4,465	998
Other assets	900	2,021
Total assets	$ 277,752	$ 260,564
Liabilities		
Deposits	$ 194,079	$ 187,974
Advances from the Federal Home Loan Bank and other borrowings	46,007	47,687
Securities sold under agreements to repurchase	11,000	--
Accrued interest payable	404	329
Advances from borrowers for taxes and insurance	374	473
Other liabilities	1,512	2,177
Total liabilities	253,376	238,640

Commitments and contingencies - note 14

Shareholders' equity		
Serial preferred stock, no par value, authorized - 500,000 shares, issued and outstanding - None		
Common stock - $0.01 par value, authorized - 2,500,000 shares issued and outstanding - 1,924,478 shares at September 30, 2001 and 1,911,005 shares at September 30, 2000	20	20
Additional paid-in capital	11,321	11,314
Accumulated other comprehensive loss	(182)	(2,050)
Retained earnings, substantially restricted	13,217	12,640
Total shareholders' equity	24,376	21,924
Total liabilities and shareholders' equity	$ 277,752	$ 260,564

See notes to consolidated financial statements.

UNION FINANCIAL BANCSHARES, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF INCOME

	For the Years Ended September 30,		
	2001	2000	1999
	(In Thousands, Except Share Data)		
Interest Income:			
Loans	$14,487	$15,272	$11,420
Deposits and federal funds sold	112	77	83
Securities available for sale:			
State and municipal	108	84	36
Other investments	3,012	1,770	2,320
Securities held to maturity and FHLB stock dividends	1,299	1,352	187
Total interest income	19,018	18,555	14,046
Interest Expense:			
Deposit accounts	8,822	8,367	5,706

Advances from the FHLB and other	2,791	2,808	1,992
Total interest expense	11,613	11,175	7,698
Net Interest Income	7,405	7,380	6,348
Provision for loan losses	240	225	105
Net interest income after provision for loan losses	7,165	7,155	6,243
Non Interest Income:			
Fees for financial services	928	1,238	905
Loan servicing fees, net of servicing amortization	(103)	351	(64)
Net gain on sale of investments	114	--	9
Gains on sale of loans	210	991	342
Total non interest income	1,149	2,580	1,192
Non Interest Expense:			
Compensation and employee benefits	2,905	3,143	2,368
Occupancy and equipment	1,335	1,425	1,133
Deposit insurance premiums	33	54	77
Professional services	375	303	275
Intangible amortization	659	613	276
Other	943	814	685
Total non interest expense	6,250	6,352	4,814
Income before income taxes	2,064	3,383	2,621
Provision for income taxes	721	1,190	945
Net Income	$ 1,343	$ 2,193	$ 1,676
Net Income per common share (Basic)	$ 0.70	$ 1.18	$ 1.26
Net Income per common share (Diluted)	$ 0.68	$ 1.16	$ 1.19
Cash dividends per common share	$ 0.40	$ 0.40	$ 0.37
Weighted average number of common shares outstanding (Basic)	1,918,431	1,855,706	1,328,305
Weighted average number of common shares outstanding (Diluted)	1,971,611	1,898,494	1,414,121

See notes to consolidated financial statements.

UNION FINANCIAL BANCSHARES, INC. AND SUBSIDIARY CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

	Common Stock		Additional Paid-In Capital	Retained Earnings Substantially Restricted	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Shares	Amount				
	(In Thousands, Except Share Data)					
Balance at September 30, 1998	1,278,250	13	4,471	10,668	148	15,300
Net income	--	--	--	1,676	--	1,676
Other comprehensive loss, net of tax						
Unrealized holding losses arising during period	--	--	--	--	(1,927)	(1,927)
Comprehensive loss						(251)
Options exercised	315	--	1	--	--	1
Five percent stock dividend	63,818	1	830	(831)	--	--
Dividend reinvestment plan contributions	14,831	--	182	--	--	182
Cash dividend ($.37 per share)	--	--	--	(494)	--	(494)
Balance at September 30, 1999	1,357,214	14	5,484	11,019	(1,779)	14,738
Net income	--	--	--	2,193	--	2,193
Other comprehensive loss, net of tax						
Unrealized holding losses arising during period	--	--	--	--	(271)	(271)
Comprehensive income						1,922
Options exercised	2,200	--	13	--	--	13
Acquisition of SCCB	526,183	5	5,617	--	--	5,622
Dividend reinvestment plan contributions	25,408	1	200	--	--	201
Cash dividend ($.40 per share)	--	--	--	(572)	--	(572)

Balance at September 30, 2000	1,911,005	$20	$11,314	$12,640	($2,050)	$21,924
Net income	--	--	--	1,343	--	1,343
Other comprehensive income, net of tax						
Equity reclassification					113	113
Unrealized holding gains arising during period	--	--	--	--	1,869	1,869
Less investment gains included in net income	--	--	--	--	(114)	(114)
Comprehensive income						3,211
Options exercised	200	--	2	--	--	2
Equity reclassification	--	--	(113)	--	--	(113)
Dividend reinvestment plan contributions	13,273	--	118	--	--	118
Cash dividend ($.40 per share)	--	--	--	(766)	--	(766)
Balance at September 30, 2001	1,924,478	$20	$11,321	$13,217	($182)	$24,376

See notes to consolidated financial statements.

UNION FINANCIAL BANCSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

	For the Years Ended September 30,		
	2001	2000	1999
	(In Thousands)		
Operating activities:			
Net income	$1,343	$2,193	$1,676
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Provision for loan losses	240	225	105
Amortization expense	933	1,241	1,127
Depreciation expense	812	468	343
Recognition of deferred income, net of costs	(70)	(227)	(100)
Deferral of fee income, net of costs	18	471	243
Gain on investment transactions	(114)	--	(9)
Loans originated for sale	(30,851)	(44,102)	(108,962)
Proceeds from sale of loans	32,868	43,508	108,746
Gain on sale of loans held for sale	(210)	(991)	(342)
(Increase) in accrued interest receivable	--	(50)	(377)
(Increase) decrease in other assets	1,121	1,045	(1,189)
Increase(decrease) in accrued interest payable	75	103	(239)
Increase (decrease) in other liabilities	(764)	(53)	(110)
Net cash provided by (used in) operating activities	5,401	3,831	912

UNION FINANCIAL BANCSHARES, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

	For the Years Ended September 30,		
	2001	2000	1999
	(In Thousands)		
Investing activities:			
Purchase of investment and mortgage-backed securities:			
Held to maturity	$0	$(32,213)	$(4,864)
Available for sale	(46,278)	(1,575)	(16,097)
Proceeds from maturity of investment and mortgage-backed securities:			
Held to maturity	1,325	--	1,500
Available for sale	3,125	100	3,375
Proceeds from sale of investment and mortgage-backed securities:			
Available for sale	18,476	--	5,941
Principal repayments on mortgage-backed securities:			
Held to maturity	1,294	779	477
Available for sale	1,816	1,540	6,356
Net (increase) decrease in loans	7,727	23,579	(9,329)
Purchase of cash surrender value of insurance	(3,467)	--	--
Acquisition of SCCB	--	(2,436)	--
Net (increase) decrease in mortgage servicing rights	(672)	2,762	(572)
Purchase of FHLB stock	--	(575)	(27)
Purchase of office properties and equipment	(1,531)	(2,429)	(847)
Net cash used in investing activities	(18,185)	(10,468)	(14,087)
Financing activities:			
Proceeds from the exercise of stock options	2	13	1
Proceeds from dividend reinvestment plan	118	200	182
Dividends paid in cash	(766)	(572)	(494)
Proceeds from term borrowings	9,320	1,184	4,863
Acquired deposits	--	--	12,622
Increase in intangible assets	--	(4,808)	(1,256)
Increase (decrease) in deposit accounts	6,105	9,663	(766)
Net cash provided by financing activities	14,779	5,680	15,152
Net (decrease) increase in cash and cash equivalents	1,995	(957)	1,977
Cash and cash equivalents at beginning of year	4,613	5,570	3,593
Cash and cash equivalents at end of year	$6,608	$4,613	$5,570

See notes to consolidated financial statements.

UNION FINANCIAL BANCSHARES, INC. AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Organization -The Corporation is the savings and loan holding company for Provident Community Bank (formerly known as Union Federal Savings Bank), a federally chartered savings bank ("the Bank"). Provident Community Bank, founded in 1934, offers a complete array of financial services through six full service banking centers and a lending and investment center in three counties in South Carolina. The Bank offers a full range of financial services including checking, savings, time deposits, individual retirement accounts (IRAs), investment services, and secured and unsecured consumer loans. The Bank originates and services home loans and provides financing for small businesses and affordable housing. Provident Financial Services ("PFS") is a wholly-owned subsidiary of Provident Community Bank that provides investment brokerage services.

On November 12, 1999, Union Financial acquired SCCB, a thrift headquartered in Winnsboro, South Carolina (Note 2).

Accounting Principles - The accounting and reporting policies of the Corporation conform to accounting principles generally accepted in the United States of America and to general practice within the banking industry. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosure of commitments and contingencies. Actual results could differ from those estimates. The following summarizes the more significant policies.

Basis of Consolidation - The accompanying consolidated financial statements include the accounts of the Corporation and its wholly owned subsidiary, Provident Community Bank and its wholly owned subsidiary, Provident Financial Services, Inc. All intercompany amounts and balances have been eliminated in consolidation.

Cash and Cash Equivalents - Cash and cash equivalents include cash on hand and amounts due from depository institutions, federal funds sold and short term, interest-bearing deposits. From time to time, the Corporation's cash deposits with other financial institutions may exceed the FDIC insurance limits.

Investments - The Bank accounts for investment securities in accordance with **Statement of Financial Accounting Standards (SFAS) No. 115, Accounting for** Certain Investments in Debt and Equity Securities ("SFAS 115"). In accordance with SFAS 115, debt securities that the Corporation has the positive intent and ability to hold to maturity are classified as "held to maturity" securities and reported at amortized cost. Debt and equity securities that are bought and held principally for the purpose of selling in the near term are classified as "trading" securities and reported at fair value, with unrealized gains and losses included in earnings. Debt and equity securities not classified as either held to maturity or trading securities are classified as "available for sale" securities and reported at fair value with unrealized gains and losses excluded from earnings and reported as a separate component of shareholders' equity. Transfers of securities between classifications will be accounted for at fair value. No securities have been classified as trading securities.

Purchases and sales of securities are accounted for on a trade date basis. Premiums and discounts on debt securities are amortized or accreted as adjustments to income over the estimated life of the security using a method approximating the level yield method. Gains or losses on the sale of securities are based on the specific identification method. The fair value of securities is based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

Loans - Loans held for investment are recorded at cost. Mortgage loans consist principally of conventional one to four family residential loans and interim and permanent financing of non-residential loans that are secured by real estate. Commercial loans are made primarily on the strength of the borrower's general credit standing, the ability to generate repayment from income sources and the collateral securing such loans. Consumer loans generally consist of home equity loans, automobile and other personal loans.

1. Summary of Significant Accounting Policies (continued)

In many lending transactions, collateral is taken to provide an additional measure of security. Generally, the cash flow or earning power of the borrower represents the primary source of repayment, and collateral liquidation serves as a secondary source of repayment. The Corporation determines the need for collateral on a case-by-case or product-by-product basis. Factors considered include the current and prospective credit worthiness of the customer, terms of the instrument and economic conditions.

Mortgage loans held for sale are valued at the aggregate lower of cost or market as determined by outstanding commitments from investors or current investor yield requirements calculated on the aggregate loan basis.

Allowances for Estimated Losses - The Corporation maintains allowances for estimated loan losses and losses on real estate acquired in settlement of loans. Loss provisions are charged to income when, in the opinion of management, such losses for which no provision has been made are probable.

The allowance for loan losses is based upon an evaluation of the loan portfolio. The evaluation considers such factors as the delinquency status of loans, current economic conditions, the net realizable value of the underlying collateral and prior loan loss experience.

Recovery of the carrying value of loans is dependent to some extent on the future economic environment and operating and other conditions that may be beyond the Corporation's control. Unanticipated future adverse changes in such conditions could result in material adjustments to allowances (and future results of operation).

Accounting for Impaired Loans - Impaired loans are accounted for in accordance with SFAS No. 114, Accounting by Creditors for Impairment of a Loan ("SFAS 114"). SFAS 114 requires that impaired loans be measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical matter, at the loan's observable market value or fair value of the collateral if the loan is collateral dependent. If the resulting value of the impaired loan is less than the recorded balance, the impairment must be recognized by creating a valuation allowance for the difference and recognizing a corresponding bad debt expense. The risk characteristics used to aggregate loans are collateral type, borrower's financial condition and geographic location. SFAS No. 118, Accounting by Creditors for Impairment of a Loan-Income Recognition and Disclosures, amends SFAS No. 114 to allow a creditor to use existing methods for recognizing interest income on an impaired loan and requires additional disclosures about how a creditor recognizes interest income related to impaired loans. The adoption of these standards required no increase to the reserve for loan losses.

The Corporation generally determines a loan to be impaired at the time management believes that it is probable that the principal and interest may be uncollectible. Management has determined that, generally, a failure to make a payment within a 90-day period constitutes a minimum delay or shortfall and does not generally constitute an impaired loan. However, management reviews each past due loan on a loan-by-loan basis and may determine a loan to be impaired prior to the loan becoming over 90 days past due, depending upon the circumstances of that particular loan. A loan is classified as a non accrual loan at the time management believes that the collection of interest is improbable, generally when a loan becomes 90 days past due. The Corporation's policy for charge-off of impaired loans is on a loan-by-loan basis. At the time management believes the collection of interest and principal is remote, the loan is charged off. The Corporation's policy is to evaluate impaired loans based on the fair value of the collateral. Interest income from impaired loans is recorded using the cash method.

As of and for the years ended September 30, 2001 and 2000, impaired loans totaled $121,075 and $55,951 respectively, and the Corporation had recognized no interest income from impaired loans. The average balance in impaired loans was $88,513 in 2001 and $34,386 in 2000.

Office Properties and Equipment - Office properties and equipment are presented at cost less accumulated depreciation. Depreciation is provided on the straight-line basis over the estimated useful lives of the assets. Estimated useful lives are 20-50 years for buildings and improvements and generally five to ten years for furniture, fixtures and equipment.

1. Summary of Significant Accounting Policies (continued)

The cost of maintenance and repairs is charged to expense as incurred, and improvements and other expenditures, which materially increase property lives, are capitalized. The costs and accumulated depreciation applicable to office properties and equipment retired or otherwise disposed of are eliminated from the related accounts, and any resulting gains or losses are credited or charged to income.

Securities Sold Under Agreements to Repurchase - The Corporation enters into sales of securities under agreements to repurchase. Fixed-coupon reverse repurchase agreements are treated as financings, with the obligations to repurchase securities sold being reflected as a liability and the securities underlying the agreements remaining as an asset. The securities are delivered by appropriate entry by the Corporation's safekeeping agent to the counterparties' accounts. The dealers may have sold, loaned or otherwise disposed of such securities to other parties in the normal course of their operations, and have agreed to resell to the Corporation substantially identical securities at the maturities of the agreements.

Federal Home Loan Bank Stock - The Bank, as a member institution of FHLB of Atlanta, is required to own capital stock in the FHLB of Atlanta based generally upon the Bank's balances of residential mortgage loans and FHLB advances. No ready market exists for this stock and it has no quoted market value. However, redemption of this stock has historically been at par value.

Mortgage Servicing Rights - The Corporation accounts for mortgage servicing rights in accordance with SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities. Purchased mortgage servicing rights are recorded at the lower of cost or market. Originated mortgage servicing rights are capitalized based on the allocated cost which is determined when the underlying loans are sold or securitized. MSRs are amortized in proportion to and over the period of estimated net servicing income using a method that is designed to approximate a level-yield method, taking into consideration the estimated prepayment of the underlying loans. For purposes of measuring impairment, MSRs are periodically reviewed for impairment based upon quarterly valuations. Such valuations are based on projections using a discounted cash flow method that includes assumptions regarding prepayments, servicing costs and other factors. Impairment is measured on a disaggregated basis for each pool of rights.

Real Estate Acquired Through Foreclosure - Real estate acquired through foreclosure is stated at the lower of cost or estimated fair value less estimated costs to sell. Any accrued interest on the related loan at the date of acquisition is charged to operations. Costs relating to the development and improvement of property are capitalized to the extent that such costs do not exceed the estimated fair value less selling costs of the property, whereas those relating to holding the property are charged to expense. Real estate acquired through foreclosure is included in other assets on the balance sheet.

Income Taxes - The Corporation accounts for income taxes in accordance with SFAS No. 109, Accounting for Income Taxes ("SFAS 109"). Under SFAS 109, deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. A valuation allowance is established for deferred tax assets that may not be realized. Also, SFAS 109 eliminates, on a prospective basis, the exception from the requirement to record deferred taxes on tax basis bad debt reserves in excess of the base year amounts. The tax basis bad debt reserve that arose prior to the fiscal year 1988 (the base year amount) is frozen, and the book reserves at that date and all subsequent changes in book and tax basis reserves are included in the determination of deferred taxes.

Fair Values of Financial Instruments - The following methods and assumptions were used by the Corporation in estimating fair values of financial instruments as disclosed herein:

Cash and short-term instruments - The carrying amounts of cash and short-term instruments approximate their fair value.

Available for sale and held to maturity securities - Fair values for securities are based on quoted market prices. The carrying values of restricted equity securities approximate fair values.

1. Summary of Significant Accounting Policies (continued)

Loans - For variable rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values. Fair values for certain mortgage loans (for example, one-to-four-family residential), credit-card loans, and other consumer loans are based on quoted market prices of similar loans sold in conjunction with securitization transactions, adjusted for differences in loan characteristics. Fair values for commercial real estate and commercial loans are estimated using discounted cash flow analysis, using interest rates currently being offered for loans with similar terms to borrowers of similar credit quality. Fair values for impaired loans are estimated using discounted cash flow analysis or underlying collateral values, where applicable.

Deposit liabilities - The fair values disclosed for demand deposits are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). The carrying amounts of variable-rate, fixed-term money-market accounts and certificates of deposit (CD's) approximate their fair values at the reporting date. Fair values for fixed-rate CD's are estimated using a discounted cash flow calculation that applies interest rates currently being offered on certificates to a schedule of aggregated expected monthly maturities on time deposits.

Short-term borrowings - The carrying amounts of other short-term borrowings maturing within 90 days approximate their fair values. Fair values of other short-term borrowings are estimated using discounted cash flow analysis based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Long-term borrowings - The fair values of the Corporation's long-term borrowings are estimated using discounted cash flow analysis based on the Corporation's current incremental borrowing rates for similar types of borrowing arrangements.

Accrued interest - The carrying amounts of accrued interest approximate their fair values.

Off-balance-sheet instruments - Fair values for off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counter parties' credit standings.

Stock Based Compensation - The Corporation has adopted the disclosure provisions of SFAS No. 123, Accounting for Stock Based Compensation. The statement permits the Corporation to continue accounting for stock based compensation as set forth in Accounting Principles Board ("APB") Opinion 25, Accounting for Stock Issued to Employees, provided the Corporation discloses the pro forma effect on net income and earnings per share of adopting the full provisions of SFAS No. 123. Accordingly, the Corporation continues to account for stock based compensation under APB Opinion 25 and has provided the required pro forma disclosures.

Per-Share Data - SFAS 128, Earnings Per Share, issued in February 1997, simplifies the standard for computing earnings per share and makes them comparable to international earnings per share standards. It also requires the dual presentation of basic and diluted earnings per share on the face of the income statement.

Basic earnings per share is computed by dividing net income by the weighted-average number of shares outstanding for the period. Diluted earnings per share is similar to the computation of basic earnings per share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued. The dilutive effect of options outstanding under the Corporation's stock option plan is reflected in diluted earnings per share by the application of the treasury stock method.

SFAS 128 became effective for the Corporation as of September 30, 1998. As required by SFAS 128, all prior period earnings per share data presented has been restated to conform with the provisions of the statement.

Share and per-share data have been restated to reflect the 3:2 stock split which occurred in February 1998 and the 5% stock dividend which occurred in February,1999.

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1. Summary of Significant Accounting Policies (continued)

Intangible Assets - Intangible assets consist of core deposit premiums resulting from the Corporation's branch acquisitions and the excess of cost over the fair value of net assets resulting from the acquisition of SCCB. The assets are being amortized over their expected useful lives.

Interest Income - Interest on loans is accrued and credited to income monthly based on the principal balance outstanding and the contractual rate on the loan. The Corporation places loans on non-

accrual status when they become greater than ninety days delinquent or when in the opinion of management, full collection of principal or interest is unlikely. The Corporation provides an allowance for uncollectible accrued interest on loans which are ninety days delinquent for all interest accrued prior to the loan being placed on non-accrual status. The loans are returned to an accrual status when full collection of principal and interest appears likely.

Risks and Uncertainties - In the normal course of its business, the Corporation encounters two significant types of risk: economic and regulatory. There are three main components of economic risk: interest rate risk, credit risk and market risk. The Corporation is subject to interest rate risk to the degree that its interest-bearing liabilities mature or reprice at different speeds, or on different bases, than its interest earning assets.

Credit risk is the risk of default on the Corporation's loan portfolio that results from the borrowers' inability or unwillingness to make contractually required payments. Credit risk also applies to investment securities and mortgage-backed securities should the issuer of the security be unable to make principal and interest payments. Market risk reflects changes in the value of collateral underlying loans receivable, the valuation of real estate held by the Corporation and the valuation of investment securities.

The Corporation is subject to the regulations of various government agencies. These regulations can and do change significantly from period to period. The Corporation also undergoes periodic examinations by the regulatory agencies, which may subject it to further changes with respect to asset valuations, amounts of required loss allowances and operating restrictions resulting from the regulators' judgements based on information available to them at the time of their examination.

In preparing the financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the dates of the balance sheets and revenues and expenses for the periods covered. Actual results could differ from those estimates and assumptions.

Reclassifications - Certain amounts in prior years' financial statements have been reclassified to conform with current year classifications.

2. Merger

On November 12, 1999, Union Financial acquired SCCB. Union Financial issued 526,183 shares of common stock and paid $3,582,081 in cash for all of the outstanding shares of SCCB. Each shareholder received $5.25 in cash and 0.817 shares of Union Financial common stock valued at $10.68 per share that was based upon the average market price of Union Financial common stock during the 25 trading day period that ended on the trading day that immediately preceded the third day prior to the merger's closing. The transaction was accounted for under the purchase method of accounting. Accordingly, the results of operations of Union Financial included in the accompanying consolidated financial statements for the period November 12, 1999 through September 30, 2000 include income and expense associated with the net assets of the former SCCB. Assets acquired and liabilities assumed have been recorded at their estimated fair market values. The excess of cost over the estimated fair value of net assets acquired of $4,693,372 was allocated to goodwill.

3. Investment And Mortgage-backed Securities

Held to Maturity - Securities classified as held to maturity consisted of the following (in thousands):

	September 30, 2001			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Gross Unrealized				
Mortgage-backed Securities:				
FHLMC	$10,365	$--	($80)	$10,285
Investment Securities:				
U.S. Agency Obligations	950	25	--	975
Total held to maturity	$11,315	$25	($80)	$11,260

	September 30, 2000			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Mortgage-backed Securities:				
FHLMC	$34,589	$--	($1,818)	$32,771
GNMA	586	--	(2)	584
Investment Securities:				
U.S. Agency Obligations	2,477	--	(35)	2,442
Total held to maturity	$37,652	$--	($1,855)	$35,797

Available for Sale - Securities classified as available for sale consisted of the following (in thousands):

	September 30, 2001			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Investment Securities:				
U.S. Agency Obligations	$13,194	$ --	($249)	$12,945
Municipal Securities	9,765	--	(39)	9,726
Other	561	--	(12)	549
Total Investment Securities	23,520	--	(300)	23,220
Mortgage-backed Securities:				
FNMA	27,200	411	--	27,611

FHLMC	13,805	--	(14)	13,791
CMOs	13,557	--	(377)	13,180
Total Mortgage-backed Securities	54,562	411	(391)	54,582
Total available for sale	$78,082	$411	($691)	$77,802

3. Investment And Mortgage-backed Securities (continued)

	September 30, 2000			
		Gross Unrealized		
	Amortized Cost	Gains	Losses	Fair Value
Investment Securities:				
U.S. Agency Obligations	$16,264	$--	($1,414)	$14,850
Municipal Securities	1,765	--	(96)	1,669
Other	497	--	(61)	436
Total Investment Securities	18,526	--	(1,571)	16,955
Mortgage-backed Securities:				
FHLMC	7,922	--	(187)	7,735
CMOs	5,996	--	(1,446)	4,550
Total Mortgage-backed Securities	13,918	--	(1,633)	12,285
Total available for sale	$32,444	$--	($3,204)	$29,240

During the quarter ended December 31, 2000 the Corporation reclassified approximately $24,000,000 in mortgage backed securities from held to maturity to available for sale as part of the adoption of FASB 133, Accounting for Derivative Instruments and Hedging Activities. The purpose of this transfer was to allow for the possible sale of the securities in order to reduce interest rate risk exposure. For the quarter ended December 31, 2000 the unrealized loss on the above securities was $435,352. During the third and fourth quarters of fiscal 2001, approximately $14,274,000 of the securities were sold that resulted in a gain on sale of securities of $114,000.

Proceeds, gross gains and gross losses realized from the sales, calls and prepayments of available for sale securities were as follows for the years ended (in thousands):

	September 30,		
	2001	2000	1999
Proceeds	$21,601	$100	$9,316
Gross gains	$114	$--	$9
Gross losses	--	--	--
Net gain on investment transactions	$114	$--	$9

The maturities of securities at September 30, 2001 are as follows (in thousands):

	Held to Maturity		Available for Sale	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$250	$250	$101	$104
Due after one year through five years	706	731	1,986	2,027
Due after five years through ten years	--	--	3,708	3,726
Due after ten years	10,359	10,279	72,287	71,945
Total investment and mortgage-backed securities	$11,315	$11,260	$78,082	$77,802

The mortgage-backed securities held at September 30, 2001 mature between one and thirty years. The actual lives of those securities may be significantly shorter as a result of principal payments and prepayments.

At September 30, 2001 and 2000, $28,411,000 and $12,535,000, respectively, of securities were pledged as collateral for certain deposits.

3. Investment And Mortgage-backed Securities (continued)

At September 30, 2001, approximately $8,586,000 of mortgage-backed securities were adjustable rate securities. The adjustment periods range from monthly to annually and rates are adjusted based on the movement of a variety of indices.

Investments in collateralized mortgage obligations ("CMOs") represent securities issued by agencies of the federal government. At September 30, 2001 approximately $13,557,000 was invested in CMOs.

4. Loans, Net

Loans receivable consisted of the following (in thousands):

	September 30,	
	2001	2000
Conventional real estate loans:		
Fixed rate residential		
Held for sale	$ --	$1,801
Held for investment	62,262	63,776
Fixed rate commercial	1,657	4,419
Adjustable rate residential		
Held for sale	--	--
Held for investment	37,684	51,524
Adjustable rate commercial	280	425
Construction loans	12,259	12,335
Total real estate loans	114,142	134,280
Other loans:		
Consumer and installment loans	16,466	17,751
Commercial loans	19,955	10,719
Consumer lines of credit	14,350	12,433
Loans secured by deposit accounts	2,009	1,971
Total other loans	52,780	42,874
Total loans	166,922	177,154
Less:		
Undisbursed portion of interim construction loans	(6,108)	(5,445)
Loan discount unamortized	(1,922)	(2,718)
Allowance for loan losses	(1,080)	(1,360)
Net deferred loan origination costs	251	176
Total, net	$158,063	$167,807
Weighted-average interest rate of loans	8.37%	8.89%

The Corporation sells loans in the secondary market without recourse and retains servicing rights. Servicing loans for others consists of collecting mortgage payments, maintaining escrow accounts, disbursing payments to investors and foreclosure processing. Loan servicing income is recorded on the accrual basis and includes servicing fees received from the investors as well as certain charges collected from the borrowers, such as late payment fees. Loans sold and serviced by the Corporation at September 30, 2001 and 2000 were approximately $65,907,000 and $47,133,000, respectively. The Corporation sold approximately $250,000,000 in mortgage loan servicing during fiscal year 2000 resulting in a pretax gain of approximately $700,000. In connection with these loans serviced for others, the Corporation held borrowers' escrow balances of $375,000 at September 30, 2001 and $473,000 at September 30, 2000.

4. Loans, Net (continued)

Adjustable rate real estate loans (approximately $37,684,000 and $51,524,000 at September 30, 2001 and 2000, respectively) are subject to rate adjustments annually and generally are adjusted based on movement of the Federal Home Loan Bank National Monthly Median Cost of Funds rate or the Constant Maturity Treasury index. The maximum loan rates can be adjusted is 200 basis points in any one year with a lifetime cap of 600 basis points.

The Corporation made commercial real estate loans which totaled approximately $1,937,000 and $4,844,000 at September 30, 2001 and 2000, respectively. These loans are considered by management to contain a somewhat greater risk of uncollectibility due to the dependency on income production or future development and sale of the real estate. These commercial real estate loans are collateralized by housing for the aged, churches, motels, apartments and other improved real estate.

Mortgage loans held for sale are stated at the lower of aggregate cost or market, net of discounts and deferred loan fees and are included in net loans in the consolidated balance sheets. Nonrefundable deferred origination fees and cost and discount points collected at loan closing, net of commitment fees paid, are deferred and recognized at the time of sale of the mortgage loans. Gain or loss on sales of mortgage loans is recognized based upon the difference between the selling price and the carrying amount of the mortgage loans sold. Other fees earned during the loan origination process are also included in net gain or loss on sales of mortgage loans.

Mortgage servicing rights are accounted for in accordance with SFAS No. 140. SFAS No. 140 requires that an entity recognize, as separate assets, rights to service mortgage loans for others, whether purchased or originated, by allocating the total cost of loans between the loan and the mortgage servicing rights ("MSR") based on their relative fair values. Capitalized MSRs are amortized based on a method which approximates the proportion of current net servicing revenues to the total estimated net servicing revenues expected to be recognized over the average estimated remaining lives of the underlying loans. Capitalized MSRs are assessed for impairment based on their fair values.

The Bank paid $672,000 for mortgage servicing rights for approximately $30,851,000 of loans in 2001. The amortization of servicing rights and excess servicing rights included in loan servicing fees amounted to $281,729, $628,653, and $850,589 in 2001, 2000, and 1999 respectively. The fair value of mortgage servicing rights at September 30, 2001 was approximately $1,123,000.

Nonrefundable loan fees and certain direct loan origination costs are deferred and recognized over the lives of the loans using the level yield method. Amortization of these deferrals is recognized as interest income. Deferred loan origination fees are included in loans held for investment on the balance sheet.

Under OTS regulations, the Bank may not make loans to one borrower in excess of 15% of unimpaired capital. This limitation does not apply to loans made before August 9, 1989. At September 30, 2001, the Bank had loans outstanding to one borrower ranging up to $2,000,000 and was in compliance with this regulation.

Also under current regulations, the Bank's aggregate commercial real estate loans may not exceed 400% of its capital as determined under regulatory requirements. These limitations are not expected to have a material impact on the Bank's ongoing operations.

See Note 8 of Consolidated Financial Statements for an analysis of qualifying mortgages pledged for FHLB advances.

At September 30, 2001 and 2000, loans which are accounted for on a non-accrual basis or contractually past due ninety days or more totaled approximately $795,000 and $1,116,000, respectively. The amount the Corporation will ultimately realize from these loans could differ materially from their carrying value because of future developments affecting the underlying collateral or the borrower's ability to repay the loans. During the years ended September 30, 2001, 2000, and 1999, the Corporation recognized no interest income on loans past due 90 days or more, whereas, under

the original terms of these loans, the Corporation would have recognized additional interest income of approximately $90,000, $95,000, and $8,000, respectively.

4. Loans, Net (continued)

The changes in the allowance for loan losses consisted of the following (in thousands):

	Years Ended September 30,		
	2001	2000	1999
Balance at beginning of year	$1,360	$836	$827
Provision for loan losses	240	225	105
Merger additions	--	449	--
(Charge-offs) recoveries, net	(520)	(150)	(96)
Balance at end of year	$1,080	$1,360	$836

Directors and officers of the Corporation are customers of the Corporation in the ordinary course of business. Loans of directors and officers have terms consistent with those offered to other customers. Loans to officers and directors of the Corporation are summarized as follows (in thousands):

	Years Ended September 30,		
	2001	2000	1999
Balance at beginning of year	$1,545	$2,304	$1,919
Loans originated during the year	--	81	472
Loan repayments during the year	(413)	(840)	(87)
Balance at end of year	$1,132	$1,545	$2,304

5. Office Properties And Equipment

Office properties and equipment consisted of the following (in thousands):

	September 30,	
	2001	2000
Land	$884	$889
Building and improvements	4,409	3,676
Office furniture, fixtures and equipment	4,640	4,336
Total	9,933	8,901
Less accumulated depreciation	(2,729)	(2,416)
Office properties and equipment , net	$7,204	$6,485

6. Intangible Assets

The changes in intangible assets consisted of the following (in thousands):

	Years Ended September 30,		
	2001	2000	1999
Balance at beginning of year	$7,042	$2,848	$1,868
Additions	--	4,807	1,256
Amortization/other	(743)	(613)	(276)
Balance at end of year	$6,299	$7,042	$2,848

7. Deposit Accounts

Deposit accounts at September 30, were as follows (in thousands):

	2001			2000		
	Rate	Balance	%	Rate	Balance	%
Account Type						
NOW accounts:						
Commercial non interest-bearing		$10,427	5.37%		$6,904	3.67%
Noncommercial	0.87%	14,386	7.41%	1.07%	11,918	6.34%
Money market checking accounts	3.31%	10,840	5.59%	4.39%	9,404	5.00%
Regular savings	1.40%	15,309	7.88%	2.04%	15,818	8.41%
Total demand and savings deposits	1.37%	50,962	26.25%	1.69%	44,044	23.42%
Savings certificates:						
Up to 3.00%		92	0.05%		81	0.04%
3.01 %- 4.00%		18,060	9.31%		359	0.19%
4.01 %- 5.00%		63,673	32.81%		35,182	18.72%
5.01 %- 6.00%		34,391	17.72%		17,870	9.51%
6.01 %- 7.00%		19,179	9.88%		84,066	44.72%
7.01 %- 8.00%		5,008	2.58%		4,600	2.45%
Total savings certificates	5.00%	140,403	72.35%	5.51%	142,158	75.63%
Sweep accounts	3.50%	2,714	1.40%	5.00%	1,772	0.95%
Total deposit accounts	4.11%	$194,079	100.00%	4.71%	$187,974	100.00%

As of September 30, 2001 and 2000, total deposit accounts include approximately $1,533,000 and $1,921,000, respectively, of deposits from the Corporation's officers, directors, employees or parties related to them.

At September 30, 2001 and 2000, deposit accounts with balances of $100,000 and over totaled approximately $59,251,000 and $47,298,000, respectively.

Savings certificates by maturity were as follows (in thousands):

Maturity Date	September 30, 2001	September 30, 2000
Within 1 year	$116,764	$118,798
After 1 but within 2 years	17,640	22,178
After 2 but within 3 years	4,674	1,131
Thereafter	1,325	51
Total savings certificates	$140,403	$142,158

7. Deposit Accounts (continued)

Interest expense on deposits consisted of the following (in thousands):

Account Type	Years Ended September 30, 2001	2000	1999
NOW accounts and money market deposit accounts	$724	$507	$411
Passbook and statement savings accounts	279	319	207
Certificate accounts	7,842	7,577	5,107
Early withdrawal penalties	(24)	(36)	(19)
Total	$8,821	$8,367	$5,706

8. Advances From The Federal Home Loan Bank And Other Borrowings

At September 30, 2001 and 2000, the Bank had $46,007,000 and $47,687,000, respectively, of advances outstanding from the Federal Home Loan Bank and treasury, tax and loan deposits. The maturity of the advances from the Federal Home Loan Bank and treasury, tax and loan deposits is as follows (in thousands):

	September 30,	
	2001	2000
Contractual Maturity:		
Within one year - fixed rate	$ --	$5,000
Within one year - adjustable rate	2,507	20,187
After one but within three years - fixed rate	10,000	5,000
After one but within three years - adjustable rate	10,000	10,000
Greater than three years-adjustable rate	$23,500	$7,500
Total Advances	$46,007	$47,687
Weighted average rate	5.69%	5.69%

The Bank pledges as collateral to the advances their Federal Home Loan Bank Stock, and has entered into a blanket collateral agreement with the Federal Home Loan Bank whereby the Bank maintains, free of other encumbrances, qualifying mortgages (as defined) with unpaid principal balances equal to, when discounted at 75% of the unpaid principal balances, 100% of total advances. The amount of qualifying mortgages was $81,772,000 and $102,041,000, respectively, at September 30, 2001 and 2000.

9. Securities Sold Under Agreements to Repurchase

The Company had $11,000,000 and $0 borrowed under agreements to repurchase at September 30, 2001 and 2000, respectively. The amortized cost of the securities underlying the agreements to repurchase at September 30, 2001 was $12,240,000. The maximum amount outstanding at any month end during fiscal 2001 was $11,000,000. The average amount of outstanding agreements for fiscal 2001 was $917,000.

10. Income Taxes

Income tax expense (benefit) is summarized as follows (in thousands):

	For the Years Ended September 30,		
	2001	2000	1999
Current	$1,829	$1,020	($364)
Deferred	(1,108)	170	1,309
Total income taxes	$721	$1,190	$945

The provision for income taxes differed from amounts computed by applying the statutory federal rate of 34% to income before income taxes as follows (in thousands):

	For the Years Ended September 30,		
	2001	2000	1999
Tax at federal income tax rate	$702	$1,150	$891
Increase (decrease) resulting from:			
State income taxes, net of federal benefit benefit	77	109	100
Interest on municipal bonds	(20)	(23)	(9)
Non-taxable life insurance income	(23)	4	(28)
Other, net	(15)	(50)	(9)
Total	$721	$1,190	$945

The tax effects of significant items comprising the Corporation's deferred taxes as of September 30, 2001 and 2000 are as follows (in thousands):

	September 30,	
	2001	2000
Deferred tax assets:		
Book reserves in excess of tax basis bad debt reserves arising after September 30, 1988	$112	$208
Book reserves and amortization in excess of tax on mortgage servicing rights	113	58
SFAS No. 115 mark to market adjustment	167	1,337
Difference between book and tax goodwill basis	168	118
Other	104	76
Total deferred tax asset	664	1,797

Deferred tax liabilities:		
Difference between book and tax property basis	249	269
Difference between book and tax Federal Home Loan Bank stock basis	100	95
Deferred loan fees	97	72
Tax mark to market adjustment on securities	111	1,089
Other	55	276
Total deferred tax liability	612	1,801
Net deferred tax asset (liability)	$52	($4)

A deferred tax asset (liability) of $52,000 and ($4,000) at September 30, 2001 and 2000, is included in other assets in the balance sheet.

Legislation has been passed which repeals the "reserve" method of accounting for thrift bad debt reserves for the first tax year beginning after December 31, 1995 (the fiscal year ending September 30, 1999 for the Corporation which qualifies for deferral of the recapture under the "residential loan requirement"). This legislation requires all

10. Income Taxes (continued)

thrifts (including the Corporation) to account for bad debts using either the specific charge-off method (available to all thrifts) or the experience method (available only to thrifts that qualify as "small banks," i.e. under $500 million in assets). The Corporation currently uses the experience method of accounting for its tax bad debt reserves. The legislation also suspends recapture of bad debt reserves taken through 1987 (i.e., the base year reserve), but requires thrifts to recapture or repay bad debt deductions taken after 1987 over six years.

As of September 30, 2001, the bad debt reserve subject to recapture, for which deferred taxes have previously been provided, totaled approximately $138,000. As permitted under SFAS 109, no deferred tax liability is provided for approximately $1,636,000 ($621,000 approximate tax effect) of such tax bad debt reserves that arose prior to October 1, 1988.

11. Employee Benefits

The Corporation has a contributory profit-sharing plan which is available to all eligible employees. Annual employer contributions to the plan consist of an amount which matches participant contributions up to a maximum of 5% of a participant's compensation and a discretionary amount determined annually by the Corporation's Board of Directors. In addition, the Corporation implemented a money purchase pension plan, effective October 1, 1996, in which all eligible employees participate. The annual contributions to the pension plan will be 5% of a participant's compensation. Employer expensed contributions to the plans were $177,000, $209,000, and $154,000 for the years ended September 30, 2001, 2000 and 1999, respectively.

12. Financial Instruments

The Corporation 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 and to reduce its own exposure to fluctuations in interest rates. These financial instruments are commitments to extend credit. 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. The Corporation evaluates each customer's creditworthiness on a

case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Corporation upon extension of credit, is based on management's credit evaluation of the counter-party. Collateral held varies but may include accounts receivable, inventory, property, plant, and equipment and income-producing commercial properties.

Those instruments involve, to varying degrees, elements of credit and interest-rate-risk in excess of the amount recognized in the Consolidated Balance Sheets. The contract amounts of those instruments reflect the extent of the Corporation's involvement in particular classes of financial instruments.

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

The Corporation had loan commitments as follows (in thousands):

	September 30,	
	2001	2000
Fixed interest rate commitments to extend credit	$2,070	$0
Undisbursed portion of interim construction loans	6,108	5,445
Unused portion of credit lines (principally variable-rate consumer lines secured by real estate)	12,195	7,334
Total	$20,373	$12,779

The Corporation has no additional financial instruments with off-balance sheet risk.

12. Financial Instruments (continued)

The Corporation has not been required to perform on any financial guarantees during the past two years. The Corporation has not incurred any losses on its commitments in 2001, 2000 or 1999.

The estimated fair values of the Corporation's financial instruments were as follows at September 30, 2000 (in thousands):

	September 30, 2001	
	Carrying Amount	Fair Value
Financial assets		
Cash and cash equivalents	$6,608	$6,608
Securities available for sale	77,802	77,802
Securities held to maturity	11,315	11,262
FHLB Stock	2,625	2,625
Loans	158,063	163,512
Accrued interest receivable	1,629	1,629
Cash surrender value of life insurance	4,465	4,465
Financial liabilities		
Deposits	$194,079	$196,194
Advances from FHLB and other borrowings	46,007	47,723
Securities sold under agreement to repurchase	11,000	11,410
Accrued interest payable	404	404
Off-balance-sheet asset (liabilities)		
Commitments to extend credit	$20,373	$20,373

	September 30, 2000	
	Carrying Amount	Fair Value
Financial assets		
Cash and cash equivalents	$4,613	$4,613
Securities available for sale	29,240	29,240
Securities held to maturity	37,652	35,797
FHLB Stock	2,625	2,625
Loans	167,807	164,870
Accrued interest receivable	1,629	1,629
Financial liabilities		
Deposits	$187,974	$187,320
Advances from FHLB and other borrowings	47,687	46,886
Accrued interest payable	329	329
Off-balance-sheet asset (liabilities)		
Commitments to extend credit	$12,779	$12,779

13. Supplemental Cash Flow Disclosures

	For the Years Ended September 30,		
	2001	2000	1999
Cash paid for:			
Income taxes	$476	$520	$1,231
Interest	$11,613	$11,072	$7,698
Non-cash transactions:			
Loans foreclosed	$425	$387	$214
Unrealized gain (loss) on securities available for sale	$(280)	$(3,204)	$(3,119)
Exchanges of mortgage loans for securities	--	$32,300	--

14. Commitments And Contingencies

Concentrations of Credit Risk - The Corporation's business activity is principally with customers located in South Carolina. Except for residential loans in the Corporation's market area, the Corporation has no other significant concentrations of credit risk.

Litigation - The Corporation is involved in legal actions in the normal course of business. In the opinion of management, based on the advice of its general counsel, the resolution of these matters will not have a material adverse impact on future results of operations or the financial position of the Corporation.

Potential Impact of Changes in Interest Rates - The Corporation's profitability depends to a large extent on its net interest income, which is the difference between interest income from loans and investments and interest expense on deposits and borrowings. Like most financial institutions, the Corporation's interest income and interest expense are significantly affected by changes in market interest rates and other economic factors beyond its control. The Corporation's interest-earning assets consist primarily of long-term, fixed rate mortgage loans and investments which adjust more slowly to changes in interest rates than its interest-bearing liabilities which are primarily term deposits and advances. Accordingly, the Corporation's earnings would be adversely affected during periods of rising interest rates.

15. Stock Option and Ownership Plans

The Corporation has a stock option plan through which the Board of Directors may grant stock options to officers and employees to purchase common stock of the Corporation at prices not less than 100 percent of the fair market value on the date of grant. The outstanding options expire ten years from the date of grant. The Corporation has elected the disclosure-only provision of SFAS No. 123, Accounting for Stock-Based Compensation. Accordingly, no compensation cost has been charged to operations. Had compensation cost for the plan been determined based on the fair value at the grant dates for awards under the plan consistent with the accounting method available under SFAS No. 123, the Corporation's net income and net income per common share would have been

reduced to the pro forma amounts indicated below:

15. Stock Option and Ownership Plans (continued)

	Years Ended September 30,		
	2001	2000	1999
Net income (in thousands)			
As reported	$1,343	$2,193	$1,676
Pro forma	1,301	2,164	1,658
Basic net income per common share			
As reported	0.70	1.18	1.26
Pro forma	0.68	1.17	1.25
Diluted net income per common share			
As reported	0.68	1.16	1.19
Pro forma	0.66	1.14	1.17

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for grants:

Dividend yield	4%
Expected volatility	30%
Risk-free interest rate	6%
Expected lives	10 years

A summary of the status of the plan as of September 30, 2001 and 2000, and changes during the years ending on those dates is presented below (all shares have been adjusted for the 3:2 stock split in February 1998 and the 5% stock dividend in February 1999):

Grant Date	Shares Granted	Average Option Price Per Share	Expiration Date	Earliest Date Exercisable
October, 1995	32,719	5.79	October, 2005	October, 1995
January, 1996	1,890	5.79	January, 2006	January, 1996
April, 1996	6,300	6.67	April, 2006	April, 1997
March, 1997	3,939	10.00	March, 2007	March, 1997
May, 1998	8,382	15.83	May, 2008	May, 1998
October, 2000	14,000	8.75	October, 2010	October, 2000
January, 2001	39,465	9.06	January, 2011	January, 2001
Total Shares Granted	236,695			

As of September 30, 2001, the number of shares exercisable were 180,239 at an average price of $7.63 per share. Options for the three previous fiscal years were exercised as follows (adjusted for stock splits and dividends):

For the Years Ended September 30,	Shares Exercised	Average Exercise Price Per Share
2001	200	$8.75
2000	2,200	$5.79
1999	315	$5.79

Stock options for 8,518 shares at an average price of $12.46 were forfeited during the year ended September 30, 2001. Stock options for 316 shares at an average price of $15.83 were forfeited during the year ended September 30, 2000. Stock options for 5,827 shares were forfeited during the year ended September 30, 1999. At September 30, 2001, 102,400 shares were available for grant and 221,153 options at an average price of $7.95 were outstanding.

16. Shareholders' Equity, Dividend Restrictions And Regulatory Matters

On August 7, 1987, the Bank completed its conversion from a federally chartered mutual association to a federally chartered stock association. A special liquidation account was established by the Bank for the preconversion retained earnings of approximately $3,718,000. The liquidation account is maintained for the benefit of depositors who held a savings or demand account as of the March 31, 1986 eligibility or the June 30, 1987 supplemental eligibility record dates who continue to maintain their deposits at the Bank after the conversion. In the event of a future liquidation (and only in such an event), each eligible and supplemental eligible account holder who continues to maintain his or her savings account will be entitled to receive a distribution from the liquidation account. The total amount of the liquidation account will be decreased in an amount proportionately corresponding to decreases in the savings account balances of eligible and supplemental eligible account holders on each subsequent annual determination date. Except for payment of dividends by the Bank to Union Financial and repurchase of the Bank's stock, the existence of the liquidation account will not restrict the use or application of such net worth.

The Bank is prohibited from declaring cash dividends on its common stock or repurchasing its common stock if the effect thereof would cause its net worth to be reduced below either the amount

required for the liquidation account or the minimum regulatory capital requirement. In addition, the Bank is also prohibited from declaring cash dividends and repurchasing its own stock without prior regulatory approval if the total amount of all dividends and stock repurchases (including any proposed dividends and stock repurchases) for the applicable calendar year exceeds its current year's net income plus its retained net income for the preceding two years.

Under present regulations of the Office of Thrift Supervision ("OTS"), the Bank must have core capital (leverage requirement) equal to 4.0% of assets, of which 1.5% must be tangible capital, excluding intangible assets. The Bank must also maintain risk-based regulatory capital as a percent of risk weighted assets at least equal to 8.0%. In measuring compliance with capital standards, certain adjustments must be made to capital and total assets.

16. Shareholders' Equity, Dividend Restrictions And Regulatory Matters
(continued)

At September 30, 2001 and 2000, the Bank had the following actual and required capital amounts and ratios (in thousands):

	September 30, 2001		
	Tangible Capital	Core Capital	Risk-Based Capital
Actual Capital	$23,920	$23,920	$23,920
Unrealized loss on available for sale securities	192	192	192
Goodwill and other intangible assets	(6,300)	(6,300)	(6,300)
Allowances for loan losses (1)	--	--	1,080
Total Adjusted capital	17,812	17,812	18,892
Minimum Capital Requirement	4,086	10,896	11,864
Regulatory Capital Excess	$13,726	$6,916	$7,028
Regulatory Capital Ratio	6.54%	6.54%	12.74%

	September 30, 2000		
	Tangible Capital	Core Capital	Risk-Based Capital
Actual Capital	$21,827	$21,827	$21,827
Unrealized gain on available for sale securities	1,937	1,937	1,937
Goodwill and other intangible assets	(7,042)	(7,042)	(7,042)
Allowance for loan losses (1)	--	--	1,359
Total Adjusted capital	16,722	16,722	18,081
Minimum Capital Requirement	3,880	10,347	10,991
Regulatory Capital Excess	$12,842	$6,375	$7,090
Regulatory Capital Ratio	6.46%	6.46%	13.16%

(1) Limited to 1.25% of risk-weighted assets

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and discretionary actions by regulators that, if undertaken, could have a material adverse effect on the Corporation. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital amounts and classifications are also subject to qualitative judgements by the regulators about components, risk weightings and other factors. As of the most recent regulatory examination, the Bank was in compliance with the regulatory capital requirements. There are no conditions or events that management believes have changed the Bank's compliance with the guidelines since that examination.

17. Recently Issued Accounting Standards

The Financial Accounting Standards Board recently issued new accounting standards that will affect accounting, reporting, and disclosure of financial information by the Corporation. Adoption of these standards is not expected to have a material impact on financial condition or results of operations. The following is a summary of the standards and their required implementation date:

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17. Recently Issued Accounting Standards (continued)

In June 1998, the FASB issued SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. All derivatives are to be measured at fair value and recognized in the balance sheet as assets and liabilities. SFAS No. 138, Accounting for Certain Derivative Instruments and Certain Hedging
Activities was issued in June 2000 and amended the accounting and reporting standards of SFAS no. 133 for certain derivative instruments and hedging activities. The two statements were to be adopted concurrently and are effective for fiscal years and quarters beginning after June 15, 2000. Adoption of SFAS No. 133 and SFAS 138 did not have a material impact on the presentation of the Corporation's financial results or financial position.

In July 2001, the SEC issued Staff Accounting Bulletin (SAB) No. 102 - Selected Loan Loss Allowance Methodology and Documentation Issues. This staff accounting bulletin clearly defined the required development, documentation, and application of a systematic methodology for determining allowances for loan and lease losses in accordance with generally accepted accounting principles. The Corporation believes that it is in compliance with SAB 102.

In September 2000, the FASB issued SFAS No. 140, Accounting for Transfers and **Servicing of Financial Assets and Extinguishment of Liabilities. This SFAS is a** replacement of SFAS No. 125. The statement was effective for transfers and servicing of financial assets and extinguishment of debt occurring after March 31, 2001. The statement was effective for recognition and reclassification of collateral and for disclosures relating to securitization for fiscal year ending after December 15, 2000. The adoption of the standard did not have a material impact on the Corporation.

In June 2001, the FASB issued SFAS No. 141 - Business Combinatons. This FASB addresses accounting and reporting for all business combinations and defines the purchase method as the only acceptable method. This statement is effective for all business combinations initiated after June 30, 2001.

In June 2001, the FASB issued SFAS No. 142 - Goodwill and Other Intangible Assets. This SFAS addresses how goodwill and other intangible assets should be accounted for at their acquisition (except for those acquired in a business combination) and after they have been initially recognized in the financial statements. The statement is effective for all fiscal years beginning after December 15, 2001. The Company is in the process of determining the effect of this SFAS on the financial position of the Company.

Other accounting standards that have been issued or proposed by the Financial Accounting Standards Board that do not require adoption until a future date are not expected to have a material impact on the consolidated financial statements upon adoption.

18. Union Financial Bancshares, Inc. Financial Information (Parent Corporation Only)

Condensed financial information for Union Financial is presented as follows (in thousands):

Condensed Balance Sheets	September 30, 2001	September 30, 2000
Assets:		
Cash and cash equivalents	$360	$70
Investment in subsidiary	23,919	21,827
Other	97	27
Total Assets	$24,376	$21,924
Liabilities and Shareholders' Equity:		
Liabilities	$ --	$ --
Shareholders' Equity	24,376	21,924
Total Liabilities and Shareholders' Equity	$24,376	$21,924

18. Union Financial Bancshares, Inc. Financial Information (Parent Corporation Only) (continued)

Condensed Statements of Income	For Years Ended September 30, 2001	2000	1999
Equity in undistributed earnings of subsidiary	$1,440	$2,280	$1,744
Other expense, net	(97)	(87)	(68)
Net income	$1,343	$2,193	$1,676

Operating Activities:

Condensed Statements of Cash Flows

Net income	$1,343	$2,193	$1,676
Adjustments to reconcile net income to net cash used in operating activities:			
Equity in undistributed earnings of subsidiary	(1,440)	(2,280)	(1,744)
Increase in other assets	(67)	(19)	(4)
Net cash used in operating activities	(164)	(106)	(72)
Financing Activities:			
Dividends received from subsidiary	1,100	500	200
Dividend reinvestment plan contributions	118	69	182
Dividends paid	(766)	(573)	(494)
Proceeds from the exercise of stock options	2	13	1
Net cash provided by (used in) financing activities	454	9	(111)
Net increase (decrease) in cash and cash equivalents	290	(97)	(183)
Cash and cash equivalents at beginning of year	70	167	350
Cash and cash equivalents at end of year	$360	$70	$167

BOARD OF DIRECTORS
UNION FINANCIAL BANCSHARES AND SUBSIDIARIES

Mason G. Alexander
Director, Mid-South Management Company

James W. Edwards
Dean of Academics, USC-Union

William M. Graham
Owner, Graham's Flowers

Louis M. Jordan
President, Jordan's Ace Hardware, Inc.

John S. McMeekin
President, Winnsboro Furniture Company

Dwight V. Neese
President and Chief Executive Officer
Provident Community Bank

Philip C. Wilkins, DMD
Dentist

Carl L. Mason
Chairman
Retired

LEADERSHIP GROUP
PROVIDENT COMMUNITY BANK

Carolyn H. Belue
Vice President
Operational Administration Manager

Richard H. Flake
Executive Vice President
Chief Financial Officer

Anthony E. Lawton
Senior Vice President
Chief Credit Officer

Dwight V. Neese
President
Chief Executive Officer

Caroline T. Thomas
Vice President
Marketing Director

Wanda J. Wells
Vice President & Corporate Secretary
Shareholder Relations Officer

Gerald B. Wyatt
Vice President
Consumer/Commercial Lending Manager

CORPORATE INFORMATION

Common Stock Information

Union Financial Bancshares, Inc.'s common stock is quoted on the Nasdaq National Market under the symbol UFBS. As of September 30, 2001, there were 793 shareholders of record and 1,924,478 shares of common stock issued and outstanding. The following table contains the range of high and low bid information of Union Financial's common stock as reported by the Nasdaq Stock Market and per share dividend as declared during each quarter of the last two fiscal years. Share prices and dividends have been adjusted to reflect all stock splits and stock dividends. See Note 16 to the financial statements for information regarding certain limitations imposed on the Bank's ability to pay cash dividends to the holding company.

	High	Low	Dividend
Fiscal 2001			
Fourth Quarter	$11.00	$ 9.50	$.100
Third Quarte	$ 9.50	$ 9.00	$.100
Second Quarter	$ 9.87	$ 8.00	$.100
First Quarter	$ 9.94	$ 7.97	$.100

	High	Low	Dividend
Fiscal 2000			
Fourth Quarter	$ 8.75	$ 6.75	$.100
Third Quarter	$ 8.37	$ 6.25	$.100
Second Quarter	$ 9.00	$ 7.00	$.100
First Quarter	$12.50	$ 8.37	$.093

Dividend Reinvestment and Stock Purchase Plan

The Corporation has a dividend reinvestment program that allow shareholders to purchase additional shares with corporate dividends. Details of the program are outlined in the dividend reinvestment prospectus. To receive more information, please contact the Shareholder Relations Officer at the corporate address.

10-KSB Information

A copy of the Form 10-KSB filed with the Securities and Exchange Commission, will be furnished to shareholders, without charge, upon written request to the Corporate Secretary, Union Financial Bancshares, Inc., 203 West Main Street, Union, South Carolina 29379.

Annual Meeting of Shareholders

The Annual Meeting of Shareholders will convene at the Main Street Auditorium of the University of South Carolina, Union Campus, Union, South Carolina on January 30, 2002 at 2:00 p.m.

Additional Information

If you are receiving duplicate mailings of shareholder reports due to multiple accounts, we can consolidate the mailings without affecting your account registration. To do this, or for additional information, contact our Shareholder Relations Officer at the corporate address shown below.

Corporate Offices

203 West Main Street
Union, South Carolina 29379
(888) 427-9002

Transfer Agent

Registrar & Transfer Company
10 Commerce Drive
Cranford, New Jersey 07016
(800) 456-0596

Independent Certified Public Accountants

Elliott Davis, LLP
870 South Pleasantburg Drive
Greenville, SC 29607-6286
(864) 242-3370

Special Counsel

Muldoon Murphy & Faucette LLP
5101 Wisconsin Avenue, N.W.
Washington, D.C. 20016
(202) 362-0840

General Counsel

Nelson Mullins Riley & Scarborough
104 South Main Street, Suite 900
Greenville, South Carolina 29601
(864) 250-2300

Stock Information

I J L Wachovia
Interstate Tower
P. O. Box 1012
Charlotte, NC 28201-10123
(800) 929-1003

Trident Securities, Inc.
4601 Six Forks Road
Raleigh, NC 27609
(800) 222-2618

First Union Securities
P. O. Box 10586
Greenville, SC 29603
(800) 695-5104

Shareholder Relations Officer

Wanda J. Wells

Union Financial Bancshares, Inc.
203 West Main Street

Union, SC 29379
(864) 429-1861

EXHIBIT NO. 21

Subsidiaries of Registrant

Subsidiaries Owned	Percentage of	Jurisdiction or State of Incorporation
Provident Community Bank	100%	United States
Provident Financial Services, Inc. (1)	100%	South Carolina

(1) A wholly-owned subsidiary of Provident Community Bank.

Exhibit 23

[LETTERHEAD OF ELLIOTT DAVIS]

CONSENT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

We consent to the incorporation by reference in the Registration Statement on Form S-8 pertaining to the 1987 Stock Option Plan, the 1995 Stock Option Plan and the 2001 Stock Option Plan of Union Financial Bancshares, Inc. and in the Registration on Form S-3 (No. 333-35319) pertaining to the Dividend Reinvestment Plan of Union Financial Bancshares, Inc. of our report dated November 1, 2001, with respect to the consolidated financial statements of Union Financial Bancshares, Inc. and subsidiary incorporated by reference in the Annual Report of Form 10-KSB for the year ended September 30, 2001.

/s/ Elliott Davis LLP

December 19, 2001
Greenville, South Carolina

End of Filing

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