

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-QSB

(Mark One)

X QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE

----- ACT OF 1934

For the quarterly period ended June 30, 2004

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES

----- EXCHANGE ACT OF 1934

For the transition period from to

COMMISSION FILE NUMBER 1-5735

UNION FINANCIAL BANCSHARES, INC.

(Exact name of small business issuer as specified 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: (864) 429-1864

Check whether the issuer (1) filed all reports required 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__

The Corporation had 1,948,094 shares, \$0.01 par value, common stock issued and outstanding as of July 30, 2004.

UNION FINANCIAL BANCSHARES, INC.

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Item 1. Financial Statements**UNION FINANCIAL BANCSHARES, INC.****CONSOLIDATED BALANCE SHEETS**

June 30, 2004 and December 31, 2003 (unaudited)

December 31,	June 30,	
ASSETS	2004	2003
-----	-----	-----
	(DOLLARS IN	
	THOUSANDS)	
Cash	\$ 2,058	\$ 1,515
Short term interest-bearing deposits	5,227	27,187

Total cash and cash equivalents	7,285	28,702
Investment and mortgage-backed securities	159,419	123,789
Loans , net	161,548	153,301
Real estate acquired through foreclosure	150	374
Office properties and equipment, net	6,025	6,415
Federal Home Loan Bank Stock, at cost	3,188	3,900
Federal Reserve Stock, at cost	539	539
Accrued interest receivable	2,185	1,655
Intangible assets	4,530	4,848
Cash surrender value of life insurance	5,135	5,025
Other assets	3,120	2,117

TOTAL ASSETS	\$353,124	\$330,665
	=====	
=====		

LIABILITIES

Deposit accounts	\$226,871	\$223,131
Advances from the Federal Home Loan Bank and other borrowings	63,250	68,500
Securities sold under agreements to repurchase	29,000	5,000
Corporate obligated floating rate capital securities	8,000	8,000
Accrued interest on deposits	353	285
Advances from borrowers for taxes and insurance	202	59
Other liabilities	1,834	183

TOTAL LIABILITIES	329,510	305,158

SHAREHOLDERS' EQUITY

Serial preferred stock, no par value, authorized - 500,000 shares, issued and outstanding - None	--	--
Common stock - \$0.01 par value, authorized - 5,000,000 shares, issued and outstanding - 1,948,109 shares at 6/30/04 and 1,969,770 at 12/31/03	20	20
Additional paid-in capital	11,993	11,906
Accumulated other comprehensive gain	-2,036	99
Retained earnings, substantially restricted	14,513	13,848
Treasury stock, at cost	-876	-366

TOTAL SHAREHOLDERS' EQUITY	23,614	25,507

TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$353,124	\$330,665
	=====	

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See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

Three and Six Months Ended June 30, 2004 and 2003 (unaudited)

	Three Months Ended		Six Months Ended	
	June 30,	June 30,	June 30,	June 30,
	2004	2003	2004	2003
	-----		-----	

THOUSANDS				
	(DOLLARS IN THOUSANDS		(DOLLARS IN	
	EXCEPT PER SHARE)		EXCEPT PER SHARE)	
Interest Income:				
Loans	\$ 2,498	\$ 2,613	\$ 4,956	\$ 0
Deposits and federal funds sold	3	3	15	0
Mortgage-backed securities	509	613	979	0
Interest and dividends on investment securities	1,190	939	2,292	0
	-----	-----	-----	-----
Total Interest Income	4,200	4,168	8,242	0
	-----	-----	-----	-----
Interest Expense:				
Deposit accounts	941	1,171	1,920	0
Trust preferred corporate obligation	100	101	199	0
Advances from the FHLB and other borrowings	743	912	1,447	0
	-----	-----	-----	-----
Total Interest Expense	1,784	2,184	3,566	0
	-----	-----	-----	-----
Net Interest Income	2,416	1,984	4,676	0
Provision for loan losses	250	190	385	0
	-----	-----	-----	-----
Net Interest Income After Provision for Loan Losses	2,166	1,794	4,291	0
	-----	-----	-----	-----
Non Interest Income:				
Fees for financial services	527	468	1,021	0
Loan servicing fees(costs)	16	-55	33	0
Net gain on sale of loans	8	--	43	--

Net gain on sale of investments	--	220	--	403

Total Non Interest Income	551	633	1,097	403

Non Interest Expense:				
Compensation and employee benefits	925	839	1,901	0
Occupancy and equipment	479	445	959	0
Deposit insurance premiums	8	8	16	0
Professional services	82	61	159	0
Advertising/Public relations	46	69	82	0
Real estate operations	35	4	62	0
Deposit premium intangible	159	159	318	0
Items processing	59	53	124	0
Telephone	39	33	77	0
Other	149	125	282	0

Total Non Interest Expense	1,981	1,796	3,980	0

Income Before Income Taxes	736	631	1,408	403
Income tax expense	188	147	351	0

Net Income	\$ 548	\$ 484	\$ 1,057	\$ 403
=====				
Basic Net Income Per Common Share	\$ 0.28	\$ 0.25	\$ 0.54	\$ 0.21
=====				
Diluted Net Income Per Common Share	\$ 0.27	\$ 0.23	\$ 0.51	\$ 0.19
=====				
Weighted Average Number of Common Shares Outstanding				
Basic	1,949,950	1,966,738	1,958,255	1,965,619
Diluted	2,056,350	2,073,138	2,062,495	2,067,394

See notes to consolidated financial statements.

UNION FINANCIAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

Six Months Ended June 30, 2004 and 2003 (unaudited)

	Six Months Ended June 30, 2004	June 30, 2003
	(IN THOUSANDS)	(IN THOUSANDS)

THOUSANDS)		
OPERATING ACTIVITIES:		
Net income	\$1,057	\$0
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	385	0
Amortization of intangibles	318	0
Depreciation expense	482	0
Recognition of deferred income, net of costs	(165)	0
Deferral of fee income, net of costs	191	0
Changes in operating assets and liabilities:		
Increase in accrued interest receivable	(530)	0
Increase in other assets	(1,113)	0
Increase in other liabilities	1,794	0
Increase (decrease) in accrued interest payable	68	0

Net cash provided by operating activities	2,487	0

INVESTING ACTIVITIES:		
Purchase of investment and mortgage-backed securities:		

Available for sale	(89,114)	0
Proceeds from sale of investment and mortgage-backed securities	--	0
Proceeds from maturity of investment and mortgage-backed securities:		
Available for sale	41,359	0
Principal repayments on mortgage-backed securities:		
Available for sale	9,990	0
Net (increase) decrease in loans	(8,433)	0
Purchase of FHLB stock	--	0
Redemption of FHLB stock	712	--
Purchase of office properties and equipment	(93)	0

Net cash used by investing activities	(45,579)	0

FINANCING ACTIVITIES:		
Proceeds from the dividend reinvestment plan	57	0
Dividends paid in cash (\$0.20 per share -2004 and \$0.20 per share - 2003)	(392)	0
Proceeds from the exercise of stock options	30	0
Share repurchase program	(510)	0
Proceeds from term borrowings	18,750	0
Increase in deposit accounts	3,740	0

Net cash provided by financing activities	21,675	0

NET (DECREASE) \ INCREASE IN CASH AND CASH EQUIVALENTS	(21,417)	0
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	28,702	6,939

CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$7,285	\$6,939
	=====	

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SUPPLEMENTAL DISCLOSURES:

Cash paid for:

Income taxes	\$120	\$218
Interest	3,498	4,353

Non-cash transactions:

Loans foreclosed	\$647	\$60
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See notes to consolidated financial statements.

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UNION FINANCIAL BANCSHARES, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
SIX MONTHS ENDED JUNE 30, 2004 AND 2003 (UNAUDITED)

Shareholders'	Common Shares	Stock Amount	Additional Paid-in Capital	Retained Earnings Substantially Restricted	Accumulated Other Comprehensive Income	Treasury Stock At Cost	Total Equity
----- (In Thousands, Except Share Data)							
BALANCE AT DECEMBER 31, 2002	1,963,252	\$20	\$11,621	\$14,438	\$1,726	\$--	\$27,805
Net income				981			981
Other comprehensive income							
Unrealized losses on securities:							
Unrealized holding losses arising							
during							
period					(764)		(764)
Comprehensive income					-----	-----	217
Options exercised	7,400			74			74

Dividend reinvestment plan contributions	3,728		54				54
Share repurchase program	(5,000)					(84)	(84)
Cash dividend (\$.20 per share)				(392)			(392)

BALANCE AT JUNE 30, 2003	1,969,380	\$20	\$11,749	\$15,027	\$962	(\$84)	\$27,674
=====							
BALANCE AT DECEMBER 31, 2003	1,969,770	\$20	\$11,906	\$13,848	\$99	(\$366)	\$25,507
Net income				1,057			1,057
Other comprehensive income							
Unrealized losses on securities:							
Unrealized holding losses arising							
during							
period					(2,135)		(2,135)

Comprehensive loss							(1,078)
Options exercised	4,248		30				30
Dividend reinvestment plan contributions	3,455		57				57
Share repurchase program	(29,364)					(510)	(510)
Cash dividend (\$.20 per share)				(392)			(392)

BALANCE AT JUNE 30, 2004	1,948,109	\$20	\$11,993	\$14,513	(\$2,036)	(\$876)	\$23,614
=====							

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. Presentation of Consolidated Financial Statements

The accompanying unaudited consolidated financial statements of Union Financial Bancshares, Inc. (the "Corporation" or "Union Financial") were prepared in accordance with instructions for Form 10-QSB and, therefore, do not include all disclosures necessary for a complete presentation of consolidated financial condition, results of operations, and cash flows in conformity with generally accepted accounting principles. However, all adjustments which are, in the opinion of management, necessary for the fair presentation of the interim consolidated financial statements have been included. All such adjustments are of a normal and recurring nature. The consolidated financial statements include the Corporation's wholly owned subsidiaries, Provident Community Bank, N.A.(the "Bank"), a national bank, and Union Financial Statutory Trust I (the "Trust"), a statutory trust created under the laws of the state of Connecticut. The results of operations for the three or six months ended June 30, 2004 are not necessarily indicative of the results which may be expected for the entire calendar year. Certain amounts in the prior year's financial statements have been reclassified to conform with current year classifications.

On July 27, 2003, the Bank converted its charter to that of a national bank.

On October 21, 2003, the Board of Directors of Union Financial changed the fiscal year end of the Corporation from September 30 to December 31, effective December 31, 2003.

Recently Issued Accounting Standards

In December 2002, the Financial Accounting Standards Board ("FASB") issued Statement on Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-based Compensation--Transition and Disclosure", an amendment of FASB Statement No. 123, "Accounting for Stock-Based Compensation", to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS No. 148 also amends the disclosure provisions of SFAS No. 123 and Accounting Principles Board ("APB") Opinion No. 28, "Interim Financial Reporting", to require disclosure in the summary of significant accounting policies of the effects of an entity's accounting policy with respect to stock-based employee compensation on reported net income and earnings per share in annual and interim financial statements. While SFAS No. 148 does not amend SFAS No. 123 to require companies to account for employee stock options using the fair value method, the disclosure provisions of SFAS No. 148 are applicable to all companies with stock-based employee compensation, regardless of whether they account for that compensation using the fair value method of SFAS No. 123 or the intrinsic value method of APB Opinion No. 25. The provisions of SFAS No. 148 are

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effective for annual financial statements for fiscal years ending after December 15, 2002, and for financial reports containing condensed financial statements for interim period beginning after December 15, 2002. The Corporation has adopted the disclosure provisions of SFAS No. 148 which had no impact on the financial condition or operating results of the Corporation.

In April 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." SFAS No. 149 amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts and loan commitments that relate to the origination of mortgage loans held for sale, and for hedging activities under SFAS No. 133. SFAS No. 149 is generally effective for contracts entered into or modified after June 30, 2003. The adoption of SFAS No. 149 did not have a material impact on the financial condition or operating results of the Corporation.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." SFAS No. 150 establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. It requires that an issuer classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). Many of those instruments were previously classified as equity. SFAS No. 150 is generally effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003. The adoption of SFAS No. 150 did not have a material impact on the financial condition or operating results of the Corporation.

In November 2002, the FASB issued FASB Interpretation ("FIN") No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others". FIN No. 45 requires a company, at the time it issues a guarantee, to recognize an initial liability for the fair value of obligations assumed under the guarantee and elaborates on existing disclosure requirements related to guarantees and warranties. The initial recognition requirements of FIN No. 45 are effective for guarantees issued or modified after December 31, 2002. The disclosure requirements are effective for financial statements of periods ending after December 15, 2002. The adoption of FIN No. 45 did not have a material effect on the Company's financial position or results of operations.

In January 2003, the FASB issued FIN No. 46, "Consolidation of Variable Interest Entities." FIN No. 46 requires a variable interest entity to be consolidated by a company if that company is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns, or both. FIN No. 46 also requires disclosures about variable interest entities that a company is not required to consolidate, but in which it has a significant variable interest. FIN No. 46 provides guidance for determining whether an entity qualifies as a variable interest entity by considering, among other considerations, whether the entity lacks sufficient equity or its equity holders lack adequate decision-making

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ability. The consolidation requirements of FIN No. 46 applied immediately to variable interest entities created after January 31, 2003. The consolidation requirements applied to existing entities in the first fiscal year or interim period beginning after June 15, 2003. Certain of the disclosure requirements applied in all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The adoption of FIN No. 46 requires the Company to discontinue consolidation of the trust preferred securities. This is not expected to have a material effect on the Company's financial position or results of operations.

In March 2004, the FASB issued an exposure draft on "Share-Based Payment". The proposed statement addresses the accounting for transactions in which an enterprise receives employee services in exchange for a) equity instruments of the enterprise or b) liabilities that are based on the fair value of the enterprises's equity instruments or that may be settled by the issuance of such equity instruments. This proposed statement would eliminate the ability to account for share-based compensation transactions using APB Opinion No. 25, "Accounting for Stock Issued to Employees", and generally would require instead that such transactions be accounted for using a fair-value-based method. This statement, if approved, will be effective for awards that are granted, modified, or settled in fiscal years beginning after a) December 15, 2004 for public entities and nonpublic entities that used the fair-value-based method of accounting under the original provisions of Statement 123 for recognition or pro forma disclosure purposes and b) December 15, 2005 for all other nonpublic entities. Earlier application is encouraged provided that financial statements for those earlier years have not yet been issued. Retrospective application of this statement is not permitted. The adoption of this statement, if approved, will not have any impact on the Company's financial position or results of operations.

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

2. Income Per Share

Basic income per share amounts for the three and six months ended June 30, 2004 and 2003 were computed based on the weighted average number of common shares outstanding during the period. Diluted income per share adjusts for the dilutive effect of outstanding common stock options during the periods.

3. Assets Pledged

Approximately \$55,307,000 and \$63,692,000 of debt securities at June 30, 2004 and December 31, 2003, respectively, were pledged by the Bank as collateral to secure deposits of the State of South Carolina, and Union, Laurens and York counties. The Bank pledges as collateral for Federal Home Loan Bank advances the Bank's Federal Home Loan Bank stock

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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 Bank will also pledge securities to cover additional advances from the Federal Home Loan Bank that exceed the qualifying mortgages balance along with security repurchase lines with various brokerage houses.

4. Contingencies and Loan Commitments

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These instruments expose the Bank to credit risk in excess of the amount recognized on the balance sheet.

The Bank'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 Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments. Total credit exposure at June 30, 2004 related to these items is summarized below:

Loan Commitments:	Contract Amount
-----	-----
Approved loan commitments	\$ 3,257,000
Unadvanced portions of loans and credit lines	34,300,000

Total loan commitments	\$ 37,557,000
	=====

Loan 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. Loan commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counter party. Collateral held is primarily residential and commercial property.

Commitments outstanding at June 30, 2004 consist of fixed and adjustable rate loans at rates ranging from 5.0% to 6.5%. Commitments to originate loans generally expire within 30 to 60 days.

Commitments to fund credit lines (principally variable rate, consumer lines secured by real estate and overdraft protection) totaled approximately \$71,080,000 at June 30, 2004. Of these lines, the outstanding loan balances totaled approximately \$36,780,000. The Bank also has commitments to fund warehouse lines of credit for various mortgage banking companies totaling \$3,000,000, none of which was outstanding at June 30, 2004.

5. Corporation Obligated Floating Rate Capital Securities

On December 18, 2001, the Trust issued \$8,000,000 of floating rate capital securities through a pooled trust preferred securities offering. The proceeds from this issuance, along with the Corporation's \$248,000 capital contribution for the Trust's common securities, were used to acquire \$8,248,000 aggregate principal amount of the Corporation's floating rate junior subordinated deferrable interest debentures due December 18, 2031 (the "Debentures"), which constitute the sole asset of the Trust. The interest rate on the Debentures and the capital securities is variable and adjustable quarterly at 3.60% over the three-month LIBOR. A rate cap of 12.50% is effective through December 18, 2006. The

Corporation has, through the Trust agreement establishing the Trust, the Guarantee Agreement, the notes and the related Debenture, taken together, fully irrevocably and unconditionally guaranteed all of the Trust's obligations under the capital securities.

A summary of the Trust securities issued and outstanding follows:

Name -----	Amount Outstanding at June 30, ---			Prepayment Option Date -----	Maturity -----	Distribution Payment Frequency -----
	2004 ----	2003 ----	Rate ----			
Union Financial Statutory Trust I	\$8,000,000	\$8,000,000	5.13%	December 18, 2006 -	December 18, 2031 -	Quarterly

The stated maturity of the Debentures is December 18, 2031. In addition, the Debentures are subject to redemption at par at the option of the Corporation, 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 the Corporation 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.

The Corporation has the right, at one or more times, to defer interest payments on the Debentures for up to twenty consecutive quarterly periods. During any deferral period, each installment of interest that would otherwise have been due and payable will bear additional interest (to the extent payment of such interest would be legally enforceable) at the applicable distribution rate, compounded quarterly. Additionally, during any deferral period, the Corporation will be prohibited from declaring or paying cash dividends on its common stock.

For the purposes of these financial statements the Trust's operations have been consolidated. Beginning with the first reporting period ending after December 15, 2004, as a result of the adoption of FIN No. 46, the Corporation will no longer be allowed to consolidate the Trust's activities. The Corporation expects assets to increase by

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\$248,000 and no impact on the income statement as a result of the adoption of this standard.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward Looking Statements

Management's discussion and analysis of financial condition and results of operations and other portions of this Form 10-QSB contain certain "forward-looking statements"

concerning the future operations of the Corporation and the Bank. These forward-looking statements are generally identified by the use of the words "believe," "expect," "intend," "anticipate," "estimate," "project," or similar expressions. Management intends 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 this report 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 effect actual results include interest rate trends, the general economic climate in the Corporation's and the Bank's market area and the country as a whole, the ability of the Corporation and the Bank to control costs and expenses, 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.

Financial Condition

Assets

Total assets of the Corporation increased \$22,459,000, or 6.79%, to \$353,124,000 at June 30, 2004 from \$330,665,000 at December 31, 2003. Investments and mortgage-backed securities increased approximately \$35,630,000, or 28.78%, from December 31, 2003 to June 30, 2004, due to the purchase of shorter-term mortgage backed securities and municipal securities for tax benefits that was funded primarily with additional borrowings.

Loans increased \$8,247,000, or 5.38%, to \$161,548,000 at June 30, 2004. The Corporation continues to focus on consumer and commercial lending with reduced emphasis on residential mortgage loans. Consumer and commercial loans outstanding during this period increased \$8,866,000, or 9.78%, while outstanding residential mortgage loans decreased \$1,555,000 or 2.34%. Real estate acquired through foreclosure decreased \$224,000, or 59.89%, to \$150,000 at June 30, 2004 from \$374,000 at December 31, 2003. The decrease was due to the disposition of four real estate properties during the first six months of the year.

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Liabilities

Total liabilities increased \$24,352,000, or 7.98%, to \$329,510,000 at June 30, 2004 from \$305,158,000 at December 31, 2003. Deposits increased \$3,740,000, or 1.68%, to \$226,871,000 at June 30, 2004 from \$223,131,000 at December 31, 2003. The increase was due primarily to growth in demand accounts as a result of deposit growth from the new banking center located in York County.

Borrowings from the Federal Home Loan Bank (FHLB) decreased \$5,250,000, or 7.66%, to \$63,250,000 at June 30, 2004 from \$68,500,000 at December 31, 2003. Securities sold under agreement to repurchase increased \$24,000,000 to \$29,000,000 at June 30, 2004 from \$5,000,000 at December 31, 2003. During this period, securities sold under agreement to repurchase provided a lower cost funding alternative to Federal Home Loan Bank advances. The increase in repurchase agreements funded the additional loan growth and security purchases for the quarter. Other liabilities increased \$1,651,000 to \$1,834,000 at June 30, 2004 from \$183,000 at December 31, 2003, due primarily to an increase in loan suspense fundings.

Shareholders' Equity

Shareholders' equity decreased \$1,893,000, or 7.42%, to \$23,614,000 at June 30, 2004 from \$25,507,000 at December 31, 2003 due to a \$2,135,000 increase in unrealized losses in securities available for sale, the repurchase of 29,364 shares at a cost of \$510,000 and the payment of \$0.20 per share quarterly dividends, offset by net income.

Liquidity

Liquidity is the ability to meet demand for loan disbursements, deposit withdrawals, repayment of debt, payment of interest on deposits and other operating expenses. The primary sources of liquidity are deposits, loan repayments, borrowings, maturity of securities and interest payments.

While maturities and scheduled amortization of loans and securities are predictable sources of funds, deposit outflows and mortgage prepayments are greatly influenced by general interest rates, economic conditions and competition. The primary investing activities of the Corporation are the origination of commercial and consumer loans, and the purchase of investment, municipal and mortgage-backed securities. These activities are funded primarily by principal and interest payments on loans and investment securities, deposit growth, securities sold under agreements to repurchase and the utilization of FHLB advances.

During the six months ended June 30, 2004, the Corporation's loan originations totaled \$37,967,000. At June 30, 2004, the Corporation's investment in agency and mortgage-backed securities totaled

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\$159,419,000. Additionally, outstanding loan commitments (including commitments to fund credit lines) totaled \$37,557,000 at June 30, 2004. Management of the Corporation anticipates that it will have sufficient funds available to meet its current loan commitments.

During the six months ended June 30, 2004, total deposits increased \$3,740,000. The Corporation closely monitors its liquidity position on a daily basis. Certificates of deposit, which are scheduled to mature in one year or less from June 30, 2004, totaled \$96,114,000. The Corporation relies primarily on competitive rates, customer service, and long-standing relationships with customers to retain deposits. From time to time, the Corporation will also offer competitive special products to its customers to increase retention and to attract new deposits. Based upon the Corporation's experience with deposit retention and current retention strategies, management believes that, although it is not possible to predict future terms and conditions upon renewal, a significant portion of such deposits will remain with the Corporation. If the Corporation requires funds beyond its ability to generate them internally, additional sources of funds are available through FHLB advances and securities sold under agreements to repurchase. At June 30, 2004, the Corporation had \$63,250,000 of FHLB borrowings and \$29,000,000 of securities sold under agreements to repurchase.

Capital Management

The capital requirement of the Bank consists of three components: (1) tangible capital, (2) core capital and (3) risk based capital. Tangible capital must equal or exceed 1.5% of adjusted total assets. Core capital must be a minimum of 4% of adjusted total assets and risk based capital must be a minimum of 8% of risk weighted assets.

As of June 30, 2004, the Bank's capital position, as calculated under regulatory guidelines, exceeds these minimum requirements as follows (dollars in thousands):

	Requirement	Actual	Excess
	-----	-----	-----
Tangible capital	\$ 5,322	\$28,280	\$22,958
Tangible capital to adjusted total assets	1.50%	7.97%	6.47%
Core capital	\$14,192	\$28,280	\$14,088
Core capital to adjusted total assets	4.00%	7.97%	3.97%
Risk based capital	\$15,491	\$30,167	\$14,676
Risk based capital to risk weighted assets	8.00%	15.58%	7.58%

On January 29, 2003, the Corporation announced that the Board of Directors had approved a stock repurchase program authorizing the Corporation to repurchase up to 98,000, or

5% shares of the

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Corporation's common stock. The shares will be repurchased either through open market purchases or privately negotiated transactions and will be made from time to time depending on market conditions and other factors. Repurchased shares will be held in treasury and will be available for the Corporation's benefit plans. The repurchase program is expected to improve the Corporation's operating performance on a per share basis, enhance, in the long term, the market price per share of the Corporation's common stock and increase the liquidity of the Corporation's common stock. During the quarter ending June 30, 2004, the Corporation repurchased 15,561 shares. As of June 30, 2004, the Corporation had repurchased a total of 49,650 shares under this authorization.

Results of operations for the six months ended June 30, 2004 and 2003

General

Net income increased \$75,000, or 7.64%, to \$1,057,000 for the six months ended June 30, 2004 as compared to the same period in 2003 as an increase in net interest income was partially offset by increases in non-interest expense.

Interest Income

Interest income decreased \$223,000, or 2.63%, for the six months ended June 30, 2004 as compared to the same period in 2003. Interest income on loans decreased by 7.85%, or \$422,000, to \$4,956,000 for the six months ended June 30, 2004 from \$5,378,000 for the six months ended June 30, 2003, due primarily to declining market interest rates along with a smaller average balance of loans due to our decreased emphasis on mortgage loan originations. Interest on deposits and federal funds sold, combined with interest and dividends on investment and mortgage-backed securities increased \$199,000, or 6.45%, for the six months ended June 30, 2004 to \$3,286,000 from \$3,087,000 during the same period in 2003. The increase was due primarily to increased investments in mortgage-backed securities and government agency securities, offset by decreased yields due to the lower interest rate environment.

Interest Expense

Interest expense decreased \$787,000, or 18.08%, for the six months ended June 30, 2004 as compared to the six months ended June 30, 2003. Interest expense on deposit accounts decreased \$412,000, or 17.67%, to \$1,920,000 for the six months ended June 30, 2004 from \$2,332,000 during the same period in 2003 due to lower cost of deposits as a result of lower rates. The Corporation continues to target lower cost demand deposit accounts from traditional higher cost certificate of deposits. Interest expense on borrowings decreased \$370,000, or 20.36%, for the six months ended June 30, 2004 as compared to the same period in the previous year due to lower borrowing rates due to the use of securities sold under agreement to repurchase instead of FHLB advances and the lower interest rate environment.

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Provision for Loan Losses

During the six months ended June 30, 2004, the provision for loan losses was \$385,000 as compared to \$425,000 for the same period in the previous year, primarily due to improved asset quality, offset by increased charge-offs and a loan portfolio with greater risk. During the six months ended June 30, 2004, non-accrual loans decreased \$1,874,000 from \$2,829,000 at December 31, 2003 to \$955,000 at June 30, 2004. Loans 30-89 days past due and still accruing also decreased \$4,215,000 from \$7,636,000 at December 31, 2003 to \$3,421,000 at June 30, 2004. During the six months ended June 30, 2004, bad debt charge-offs, net of recoveries, was \$881,000 as compared to \$143,000 for the same period in the previous year. The increase in bad debt charge-offs over the previous year includes approximately \$737,000 from two commercial loans that were written down due to a reduction in the market value of the supporting loan collateral. The provision also reflects the Corporation's continued movement from longer term, fixed rate residential mortgage loans to shorter term, floating rate consumer and commercial loans. Consumer and commercial loans carry higher risk weighted rates in the reserve calculation as

compared to residential mortgage loans. Management believes the Corporation's loan loss allowance is adequate to absorb probable loan losses inherent in the portfolio. The Corporation's loan loss allowance at June 30, 2004 was approximately 1.15% of the Corporation's outstanding loan portfolio and 197.59% of non-performing loans compared to 1.51% of the Corporation's outstanding loan portfolio and 80.85% of non-performing loans at December 31, 2003.

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.

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

Balance at beginning of year	\$2,383
Provision for loan losses	385
Charge-offs, net	- 881

Balance at end of quarter	\$1,887
	=====

The following table sets forth information with respect to the Bank's non-performing assets at the dates indicated (dollars in thousands):

	June 30, 2004 -----	December 31, 2003 -----
Non-accruing loans which are contractually past due 90 days or more:		
Real Estate	\$ 412	\$ 896
Commercial	430	1,720
Consumer	113	213
	-----	-----
Total	\$ 955	\$ 2,829
	=====	=====
Percentage of loans receivable, net	0.59%	1.85 %
	=====	=====
Percentage of allowance for loan losses to total loans outstanding	1.15%	1.51 %
	=====	=====
Allowance for loan losses	\$1,887	\$2,368
	=====	=====

Real estate acquired through foreclosure and repossessed assets, net of allowances	\$ 150 =====	\$ 373 =====
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Non-Interest Income

Total non-interest income decreased \$96,000, or 8.05%, to \$1,097,000 for the six months ended June 30, 2004 from \$1,193,000 for the same period in the previous year due primarily to \$403,000 from the gain on sale of investments in 2003 compared to \$0 for the current year. Fees from financial services increased \$133,000, or 14.98%, to \$1,021,000 for the six months ended June 30, 2004 from \$888,000 for the same period in the previous year. The increase was due primarily to increases in demand deposit accounts over the previous year. Mortgage banking fees from the gain on sale of loans for the six months ended June 30, 2004 was \$43,000 compared to \$0 for the same period in the previous year as the Corporation sold \$5,221,000 in fixed rate mortgage loans during the year as part of its interest rate risk strategies. The sales represent loans funded and sold through a third party on a servicing released basis.

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Non-Interest Expense

For the six months ended June 30, 2004, total non-interest expense increased \$394,000, or 10.99%, to \$3,980,000 from \$3,586,000 for the same period in 2003. On June 16, 2003, the Corporation opened the York County regional banking center and therefore, expense categories for 2004 reflect additions for the new banking center. Compensation and employee benefits increased \$256,000, or 15.56%, to \$1,901,000 for the six month period ended June 30, 2004 from \$1,645,000 for the same period in 2003, due primarily to staff additions resulting from the new branch. Occupancy and equipment expense increased \$75,000, or 8.48%, to \$959,000 for the six months ended June 30, 2004 from \$884,000 for the same period in 2003, due to higher rent expense due to the new office. Professional services expense decreased \$19,000, or 10.67%, to \$159,000 for the six months ended June 30, 2004 from \$178,000 for the same period in 2003 due to lower legal expenses as a result of previous year costs incurred from the Corporation's conversion to a national bank charter. Advertising expense decreased \$16,000, or 16.33%, to \$82,000 for the six months ended June 30, 2004 from \$98,000 for the same period in 2003, due to the previous year promotional costs incurred related to the new banking center opening.

Real estate operations costs increased \$40,000, or 181.82%, to \$62,000 for the six months ended June 30, 2004 from \$22,000 for the same period in 2003, due to higher disposition costs associated with foreclosed real estate properties. Items processing expense increased \$13,000, or 11.71%, to \$124,000 for the six months ended June 30, 2004 from \$111,000 for the same period in 2003, due to an increase in demand accounts. Telephone expense increased \$10,000, or 14.93%, to \$77,000 for the six months ended June 30, 2004 from \$67,000 for the same period in 2003, due to additional expense from the new office. Other expense increased \$35,000, or 14.17%, to \$ 282,000 for the six months ended June 30, 2004 from \$247,000 for the same period in 2003, due primarily to higher general expenses that resulted from the new office opening in York County.

Item 3. Controls and Procedures

The Corporation's management, including the Corporation's principal executive officer and principal financial officer, have evaluated the effectiveness of the Corporation's "disclosure controls and procedures," as such term is defined in Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, (the "Exchange Act"). Based upon their evaluation, the principal executive officer and principal financial officer concluded that, as of the end of the period covered by this report, the Corporation's disclosure controls and procedures were effective for the purpose of ensuring that the information required to be disclosed in the reports that the Corporation files or submits under the Exchange Act with the Securities and Exchange Commission (the "SEC") (1) is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) is accumulated and communicated to the Corporation's management, including its principal executive and principal financial officers, as

appropriate to allow timely decisions regarding required disclosure.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

The Corporation is involved in various claims and legal actions arising in the normal course of business. Management believes that these proceedings are immaterial to the Corporation's financial condition and results of operations.

Item 2. Changes in Securities and Small Business Issuers Purchases of Equity Securities

The Corporation has the right, at one or more times, unless an event of default exists under the floating rate junior subordinated deferrable interest debentures due December 18, 2031 (the "Debentures"), to defer interest payments on the Debentures for up to 20 consecutive quarterly periods. During this time, the Corporation will be prohibited from declaring or paying cash dividends on its common stock.

The following table provides certain information with regard to shares repurchased by the Corporation during the second quarter of 2004.

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per share	(c) Total Number of Shares Purchased as part of Publicly Announced Programs	(d) Maximum Number of Shares that may be purchased under Program
April 1, 2004 through April 30, 2004	8,143	\$17.06	8,143	55,768
May 1, 2004 through May 31, 2004	5,299	\$17.45	5,299	50,469
June 1, 2004 through June 30, 2004	2,119	\$18.00	2,119	48,350

Total	15,561	\$17.32	15,561	N/A
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(1) On January 29, 2003, the Corporation announced that the Board of Directors had approved a stock repurchase program authorizing the Corporation to repurchase up to 98,000 shares of the Corporation's common stock. The repurchase program will continue until it is completed or terminated by the Board of Directors.

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Item 3. Defaults upon Senior Securities

Not applicable.

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

None

Item 5. Other Information

None

Item 6. Exhibits and Reports on Form 8-K

Exhibits

31(a) Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer

31(b) Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer

32(a) Chief Executive Officer Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32(b) Chief Financial Officer Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Reports on Form 8-K

On April 20, 2004, Union Financial Bancshares, Inc. furnished a Form 8-K announcing its financial results for the quarter ended March 31, 2004. The press release announcing financial results was attached by exhibit.

SIGNATURES

In accordance with the requirements 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.

(Registrant)

Date: August 5, 2004

Date: August 5, 2004

By: /s/ Dwight V. Neese

Dwight V. Neese, CEO

By: /s/ Richard H. Flake

Richard H. Flake, CFO

EXHIBIT 31 (a)**CERTIFICATION**

I, Dwight V. Neese, certify that:

1. I have reviewed this Form 10-QSB of Union Financial Bancshares, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;
4. The small business issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting;

and

5. The small business issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: August 5, 2004 /s/ Dwight V. Neese

President and Chief Executive Officer

EXHIBIT 31 (b)

CERTIFICATION

I, Richard H. Flake, certify that:

1. I have reviewed this Form 10-QSB of Union Financial Bancshares, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the periods presented in this report;

4. The small business issuer's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and

5. The small business issuer's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: August 5, 2004

/s/ Richard H. Flake

*Richard H. Flake
Executive Vice President and Chief
Financial Officer*

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADDED BY**

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Union Financial Bancshares, Inc. (the "Company") on Form 10-QSB for the quarter ended June 30, 2004 as filed with the Securities and Exchange Commission (the "Report"), I, Dwight V. Neese, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. ss.1350, as added by

Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the period covered by the Report.

/s/ Dwight V. Neese

Dwight V. Neese
President and Chief Executive Officer

Date: August 5, 2004

CERTIFICATION PURSUANT TO

**18 U.S.C. SECTION 1350,
AS ADDED BY**

SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Union Financial Bancshares, Inc. (the "Company") on Form 10-QSB for the quarter ended June 30, 2004 as filed with the Securities and Exchange Commission (the "Report"), I, Richard H. Flake, Executive Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. ss.1350, as added by Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the period covered by the Report.

/s/ Richard H. Flake

Richard H. Flake
Executive Vice President and Chief Financial
Officer

Date: August 5, 2004

End of Filing

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