

Edgar Filing: UNIONBANCORP INC - Form 10-Q

UNIONBANCORP INC  
Form 10-Q  
November 13, 2006

=====

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

QUARTERLY REPORT  
Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the quarterly period ended September 30, 2006  
Commission File Number: 0-28846

UnionBancorp, Inc.  
(Exact name of Registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

36-3145350  
(I.R.S. Employer Identification Number)

122 West Madison Street Ottawa, Illinois 61350  
(Address of principal executive offices including zip code)

(815) 431-2720  
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer .

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

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

Class	Shares outstanding at November 13, 2006
----- Common Stock, Par Value \$1.00	----- 3,756,351

=====

UnionBancorp, Inc.  
Form 10-Q Index  
September 30, 2006

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Page

----

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

- o Unaudited Consolidated Balance Sheets.....1
- o Unaudited Consolidated Statements of Income and  
Comprehensive Income .....2
- o Unaudited Consolidated Statements of Cash Flows.....4
- o Notes to Unaudited Consolidated Financial Statements.....5

Item 2. Management's Discussion and Analysis of Financial Condition  
and Results of Operations.....15

Item 3. Quantitative and Qualitative Disclosures  
About Market Risk.....32

Item 4. Controls and Procedures .....32

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.....33

Item 1A. Risk Factors.....33

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.....33

Item 3. Defaults Upon Senior Securities.....33

Item 4. Submission of Matters to a Vote of Security Holders.....33

Item 5. Other Information.....34

Item 6. Exhibits.....34

SIGNATURES.....36

UNIONBANCORP, INC. AND SUBSIDIARIES  
UNAUDITED CONSOLIDATED BALANCE SHEETS  
September 30, 2006 and December 31, 2005 (In Thousands, Except Share Data)

	September 30 2006
-----	
ASSETS	
Cash and cash equivalents	\$ 20,051
Securities available-for-sale	182,171
Loans	407,015
Allowance for loan losses	(6,013)
-----	
Net loans	400,912
Cash surrender value of life insurance	15,928
Mortgage servicing rights	2,314

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Premises and equipment, net	13,826
Goodwill	6,310
Intangible assets, net	44
Other real estate	859
Other assets	6,436
	-----
Total assets	\$ 648,851
	=====
LIABILITIES AND STOCKHOLDERS' EQUITY	
Liabilities	
Deposits	
Non-interest-bearing	\$ 56,564
Interest-bearing	470,354
	-----
Total deposits	526,918
Federal funds purchased and securities sold under agreements to repurchase	4,116
Advances from the Federal Home Loan Bank	36,700
Notes payable	8,301
Series B mandatory redeemable preferred stock	831
Other liabilities	4,672
	-----
Total liabilities	581,538
	-----
Stockholders' equity	
Preferred stock; 200,000 shares authorized; none issued	--
Series A convertible preferred stock; 2,765 shares authorized, 2,762.24 shares outstanding (aggregate liquidation preference of \$2,762)	500
Series C preferred stock; 4,500 shares authorized; none issued	--
Common stock, \$1 par value; 10,000,000 shares authorized; 4,697,993 shares issued at September 30, 2006 and 4,684,393 shares issued at December 31, 2005	4,698
Additional paid-in capital	23,417
Retained earnings	51,510
Accumulated other comprehensive income	34
	-----
	80,159
Treasury stock, at cost; 955,142 shares at September 30, 2006 and 877,517 at December 31, 2005	(12,846)
	-----
Total stockholders' equity	67,313
	-----
Total liabilities and stockholders' equity	\$ 648,851
	=====

See Accompanying Notes to Unaudited Financial Statements

1.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 UNAUDITED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME  
 Three and Nine Months Ended September 30, 2006 and 2005 (In Thousands, Except Per Share Data)

Three Months Ended

Nine

Edgar Filing: UNIONBANCORP INC - Form 10-Q

	September 30		September 30
	2006	2005	2006
Interest income			
Loans	\$ 7,444	\$ 6,874	\$ 21,79
Securities			
Taxable	2,065	1,587	6,08
Exempt from federal income taxes	218	241	64
Federal funds sold and other	75	18	14
Total interest income	9,802	8,720	28,66
Interest expense			
Deposits	4,128	2,832	11,45
Federal funds purchased and securities sold under agreements to repurchase	69	44	19
Advances from the Federal Home Loan Bank	363	486	1,30
Series B mandatory redeemable preferred stock	12	12	3
Notes payable	156	128	46
Total interest expense	4,728	3,502	13,44
Net interest income	5,074	5,218	15,21
Provision (credit) for loan losses	(200)	50	(1,30)
Net interest income after provision for loan losses	5,274	5,168	16,51
Noninterest income			
Service charges	476	490	1,41
Trust income	202	193	62
Mortgage banking income	240	357	76
Brokerage commissions and fees	87	236	26
Banked owned life insurance	153	138	43
Securities gains, net	--	--	(8
Gain on sale of assets, net	(1)	--	(
Other income	324	288	92
Total noninterest income	1,481	1,702	4,32
Noninterest expenses			
Salaries and employee benefits	2,630	3,098	8,03
Occupancy expense, net	356	386	1,11
Furniture and equipment expense	515	497	1,50
Marketing	88	115	29
Supplies and printing	71	80	23
Telephone	104	112	33
Other real estate owned expense	2	12	1
Amortization of intangible assets	11	30	7
Other expenses	814	1,017	2,75
Total noninterest expenses	4,591	5,347	14,35
Income from continuing operations before income taxes	2,164	1,523	6,48
Income taxes	658	405	1,98
Income from continuing operations	1,506	1,118	4,50

See Accompanying Notes to Unaudited Financial Statements

Edgar Filing: UNIONBANCORP INC - Form 10-Q

UNIONBANCORP, INC. AND SUBSIDIARIES  
 UNAUDITED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME  
 Three and Nine Months Ended September 30, 2006 and 2005 (In Thousands, Except Per Share Data)

-----			
Discontinued Operations:			
Loss from operations of discontinued insurance unit (including loss on disposal of \$355 in 2006)	(440)	(93)	(53)
Income tax benefit	(170)	(36)	(20)
	-----	-----	-----
Loss on discontinued operations	(270)	(57)	(32)
	-----	-----	-----
Net Income	\$ 1,236	\$ 1,061	\$ 4,17
	=====	=====	=====
Preferred stock dividends	52	52	15
	-----	-----	-----
Net income for common stockholders	\$ 1,184	\$ 1,009	\$ 4,02
	=====	=====	=====
Basic earnings per common share from continuing operations	\$ 0.39	\$ 0.27	\$ 1.1
	=====	=====	=====
Basic earnings per common share from discontinued operations	\$ (0.07)	\$ (0.01)	\$ (0.0)
	=====	=====	=====
Basic earnings per common share	\$ 0.32	\$ 0.26	\$ 1.0
	=====	=====	=====
Diluted earnings per common share from continuing operations	\$ 0.38	\$ 0.26	\$ 1.1
	=====	=====	=====
Diluted earnings per common share From discontinued operations	\$ (0.07)	\$ (0.01)	\$ (0.0)
	=====	=====	=====
Diluted earnings per common share	\$ 0.31	\$ 0.25	\$ 1.0
	=====	=====	=====
Total comprehensive income	\$ 2,476	\$ 891	\$ 4,11
	=====	=====	=====

See Accompanying Notes to Unaudited Financial Statements

3.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 Nine Months Ended September 30, 2006 and 2005 (In Thousands)

	Nine Months Ended September 30,	
	-----	-----
	2006	2005
	-----	-----

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Cash flows from operating activities		
Net income	\$	4,176
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation		1,412
Amortization of intangible assets		71
Amortization of mortgage servicing rights		219
Amortization of bond premiums, net		328
Stock option expense		103
Federal Home Loan Bank stock dividend		(47)
Provision (credit) for loan losses		(1,300)
Provision for deferred income taxes		(310)
Net change in BOLI		(430)
Net change in OREO		2
(Gain) loss on sale of assets		7
Loss on sale of securities		88
Gain on sale of loans		(511)
Gain on sale of real estate acquired in settlement of loans		(32)
Proceeds from sales of loans held for sale		38,239
Origination of loans held for sale		(38,387)
Change in assets and liabilities		
Decrease (Increase) in other assets		439
Increase in other liabilities		(563)
		-----
Net cash provided by operating activities		3,504
Cash flows from investing activities		
Securities available-for-sale		
Proceeds from maturities and paydowns		30,634
Proceeds from sales		15,515
Purchases		(33,400)
Redemption of FHLB stock		1,079
Purchase of loans		(19,513)
Net decrease in loans		28,418
Purchase of premises and equipment		(1,169)
Cash paid to assume deposits, net of cash received on sale of branch		(6,054)
Sale of insurance unit		856
Proceeds from sale of real estate acquired in settlement of loans		681
		-----
Net cash provided by investing activities		17,047
Cash flows from financing activities		
Net increase (decrease) in deposits		(10,915)
Net increase (decrease) in federal funds purchased and securities sold under agreements to repurchase		3,504
Payments on notes payable		(2,567)
Proceeds from notes payable		1,400
Net increase in other borrowed funds		--
Net decrease in advances from the Federal Home Loan Bank		(13,300)
Dividends on common stock		(1,346)
Dividends on preferred stock		(156)
Proceeds from exercise of stock options		160
Purchase of treasury stock		(1,638)
		-----
Net cash used by financing activities		(24,858)
		-----
Net decrease in cash and cash equivalents		(4,307)
Cash and cash equivalents		
Beginning of period		24,358
		-----
End of period	\$	20,051
		=====
Supplemental disclosures of cash flow information		

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

Cash payments for			
Interest	\$	13,900	\$
Income taxes		1,372	
Transfers from loans to other real estate owned		1,307	

See Accompanying Notes to Unaudited Financial Statements

4.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

---

Note 1. Basis of Presentation and Summary of Significant Accounting Policies

The accompanying unaudited interim consolidated financial statements of UnionBancorp, Inc. (the "Company") have been prepared in accordance with U.S. generally accepted accounting principles and with the rules and regulations of the Securities and Exchange Commission for interim financial reporting. Accordingly, they do not include all of the information and footnotes required for complete financial statements. In the opinion of management, all normal and recurring adjustments which are necessary to fairly present the results for the interim periods presented have been included. The preparation of financial statements requires management to make estimates and assumptions that affect the recorded amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates. For further information with respect to significant accounting policies followed by the Company in the preparation of its consolidated financial statements, refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2005. The annualized results of operations during the three and nine months ended September 30, 2006 are not necessarily indicative of the results expected for the year ending December 31, 2006. All financial information is in thousands (000's), except per share data.

The consolidated financial statements have been restated to report the results of the Company's Insurance unit of the Wealth Management segment as a discontinued operation as described in Note 8.

Note 2. Earnings Per Share

Basic earnings per share for the three and nine months ended September 30, 2006 and 2005 were computed by dividing net income by the weighted average number of shares outstanding. Diluted earnings per share for the three and nine months ended September 30, 2006 and 2005 were computed by dividing net income by the weighted average number of shares outstanding, adjusted for the dilutive effect of the stock options. Computations for basic and diluted earnings per share are provided below:

Basic Earnings Per Common Share

Three Months Ended September 30,		Nine Month September
2006	2005	2006

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Net Income from continuing operations available to common shareholders	\$ 1,454	\$ 1,066	\$ 4,347
Net loss from discontinued operations available to common shareholders	\$ (270)	\$ (57)	\$ (327)
	-----	-----	-----
Net Income available to common shareholders	\$ 1,184	\$ 1,009	\$ 4,020
Weighted average common shares outstanding	3,743	3,895	3,757
	-----	-----	-----
Basic Earnings Per Common Share from continuing operations	\$ 0.39	\$ 0.27	\$ 1.16
	=====	=====	=====
Basic Earnings Per Common Share from discontinued operations	\$ (0.07)	\$ (0.01)	\$ (0.09)
	=====	=====	=====
Basic Earnings Per Common Share	\$ 0.32	\$ 0.26	\$ 1.07
	=====	=====	=====

5.

UNIONBANCORP, INC. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
(In Thousands, Except Per Share Data)

---

Diluted Earnings Per Common Share			
Weighted average common shares outstanding	3,743	3,895	3,757
Add: dilutive effect of assumed exercised stock options	40	64	44
	-----	-----	-----
Weighted average common and dilutive Potential shares outstanding	3,783	3,959	3,801
	=====	=====	=====
Diluted Earnings Per Common Share from continuing operations	\$ 0.38	\$ 0.26	\$ 1.14
	=====	=====	=====
Diluted Earnings Per Common Share from discontinued operations	\$ (0.07)	\$ (0.01)	\$ (0.08)
	=====	=====	=====
Diluted Earnings Per Common Share	\$ 0.31	\$ 0.25	\$ 1.06
	=====	=====	=====

There were approximately 60,000 and 40,000 options outstanding at September 30, 2006 and 2005, respectively, that were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price of the common stock and were, therefore, antidilutive.

Note 3. Securities

The Company's consolidated securities portfolio, which represented 30.8% of the Company's 2006 third quarter average earning asset base, is managed



## Edgar Filing: UNIONBANCORP INC - Form 10-Q

to minimize interest rate risk, maintain sufficient liquidity, and maximize return. The portfolio includes several callable agency debentures, adjustable rate mortgage pass-throughs, and collateralized mortgage obligations. Corporate bonds consist of investment grade obligations of public corporations. Equity securities consist of Federal Reserve stock, Federal Home Loan Bank stock, and trust preferred stock. Securities classified as available-for-sale, carried at fair value, were \$182,171 at September 30, 2006 compared to \$196,440 at December 31, 2005. The Company does not have any securities classified as trading or held-to-maturity.

The following table describes the fair value, gross unrealized gains and losses of securities available-for-sale at September 30, 2006 and December 31, 2005, respectively:

	September 30, 2006		
	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
U.S. government agencies	\$ 46,984	\$ 186	\$ (288)
States and political subdivisions	19,604	311	(24)
U.S. government mortgage-backed securities	67,575	285	(508)
Collateralized mortgage obligations	23,737	48	(97)
Equity securities	17,452	140	--
Corporate	6,819	17	(13)
	\$ 182,171	\$ 987	\$ (930)

6.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

	December 31, 2005		
	Fair Value	Gross Unrealized Gains	Gross Unrealized Losses
U.S. government agencies	30,857	8	(364)
States and political subdivisions	18,400	424	(16)
U.S. government mortgage-backed securities	101,022	854	(675)
Collateralized mortgage obligations	20,938	21	(157)
Equity securities	18,316	54	(49)
Corporate	6,907	62	(7)
	\$ 196,440	\$ 1,423	\$ (1,268)

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Note 4. Loans and Allowance for Loan Losses

The Company offers a broad range of products, including agribusiness, commercial, residential, and installment loans, designed to meet the credit needs of its borrowers. The Company concentrates its lending activity in the geographic market areas that it serves, generally lending to consumers and small to mid-sized businesses from which deposits are garnered in the same market areas. As a result, the Company strives to maintain a loan portfolio that is diverse in terms of loan type, industry, borrower and geographic concentrations. The following table describes the composition of loans by major categories outstanding as of September 30, 2006 and December 31, 2005, respectively:

	September 30, 2006		December 31, 2005	
	\$	%	\$	%
Commercial	\$ 91,921	22.58%	\$ 91,537	21.92%
Agricultural	21,718	5.34	26,694	6.39
Real estate:				
Commercial mortgages	117,602	28.89	126,503	30.31
Construction	86,085	21.15	68,508	16.41
Agricultural	25,525	6.27	33,033	7.91
1-4 family mortgages	55,761	13.70	57,920	13.87
Installment	8,090	1.99	12,747	3.05
Other	313	0.08	583	0.14
Total loans	407,015	100.00%	417,525	100.00%
Allowance for loan losses	(6,103)		(8,362)	
Loans, net	\$ 400,912		\$ 409,163	

The following table presents data on impaired loans:

	September 30, 2006	December 31, 2005
Impaired loans for which an allowance has been provided	\$ 6,034	\$ 12,585
Impaired loans for which no allowance has been provided	2,804	563
Total loans determined to be impaired	\$ 8,838	\$ 13,148
Allowance for loan loss for impaired loans included in the allowance for loan losses	\$ 1,956	\$ 3,913

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

### Note 4. Loans and Allowance For Loan Losses (Continued)

In originating loans, the Company recognizes that credit losses will be experienced and the risk of loss will vary with, among other things, current economic conditions; the type of loan being made; the creditworthiness of the borrower over the term of the loan; and in the case of a collateralized loan, the quality of the collateral for such loan. The allowance for loan losses represents the Company's estimate of the allowance necessary to provide for probable incurred losses in the loan portfolio. In making this determination, the Company analyzes the ultimate collectibility of the loans in its portfolio, incorporating feedback provided by internal loan staff, the independent loan review function and information provided by examinations performed by regulatory agencies. The Company makes an ongoing evaluation as to the adequacy of the allowance for loan losses. Transactions in the allowance for loan losses for the three and nine months ended September 30, 2006 and 2005 are summarized below:

	Three Months Ended September 30,		Nine Months September
	2006	2005	2006
Beginning balance	\$ 6,848	\$ 9,159	\$ 8,362
Charge-offs:			
Commercial	249	(208)	472
Real estate mortgages	378	1,004	860
Installment and other loans	4	15	77
Total charge-offs	631	811	1,409
Recoveries:			
Commercial	24	32	159
Real estate mortgages	46	36	255
Installment and other loans	16	27	36
Total recoveries	86	95	450
Net charge-offs	545	716	959
Provision (credit) for loan losses	(200)	50	(1,300)
Ending balance	\$ 6,103	\$ 8,493	\$ 6,103
Period end total loans, net of unearned interest	\$ 407,015	\$ 405,884	\$ 407,015
Average loans	\$ 403,049	\$ 409,545	\$ 408,175

Edgar Filing: UNIONBANCORP INC - Form 10-Q

	=====	=====	=====
Ratio of net charge-offs to average loans	0.14%	0.17%	0.23%
Ratio of provision for loan losses to average loans	(0.05)%	0.01%	(0.32)%
Ratio of allowance for loan losses to ending total loans	1.50%	2.09%	1.50%
Ratio of allowance for loan losses to total nonperforming loans	189.48%	227.94%	189.48%
Ratio of allowance at end of period to average loans	1.51%	2.07%	1.50%

8.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

---

Note 5. Stock Option Plans

In April 1993, the Company adopted the UnionBancorp 1993 Stock Option Plan ("the 1993 Option Plan"). A total of 490,206 shares were issued pursuant to stock options issued to employees and outside directors under this plan. The 1993 Stock Option Plan was terminated on April 12, 2003.

In 1999, the Company adopted the UnionBancorp, Inc. Non-qualified Stock Option Plan ("the 1999 Option Plan"). Under the 1999 Option Plan, nonqualified options may be granted to employees and eligible directors of the Company and its subsidiaries to purchase the Company's common stock at 100% of the fair market value on the date the option is granted. The Company has authorized 50,000 shares for issuance under the 1999 Option Plan. During 1999, 40,750 of these shares were granted and are 100% fully vested. The options have an exercise period of ten years from the date of grant. There are 9,250 shares available to grant under this plan.

In April 2003, the Company adopted the UnionBancorp 2003 Stock Option Plan ("the 2003 Option Plan"). Under the 2003 Option Plan, nonqualified options, incentive stock options, and/or stock appreciation rights may be granted to employees and outside directors of the Company and its subsidiaries to purchase the Company's common stock at an exercise price to be determined by the 2003 Option Plan's administrative committee. Pursuant to the 2003 Option Plan, 200,000 shares of the Company's unissued common stock have been reserved and are available for issuance upon the exercise of options and rights granted under the 2003 Option Plan. The options have an exercise period of ten years from the date of grant. There are 92,500 shares available to grant under this plan.

A summary of the status of the option plans as of September 30, 2006, and changes during the quarter ended on those dates is presented below:

	September 30, 2006	
	Shares	Weighted-Average Exercise Price
	-----	-----
Outstanding at beginning of quarter	266,364	\$ 16.11

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Granted	17,500	19.60
Exercised	100	16.07
Forfeited	--	--
	-----	-----
Outstanding at end of quarter	283,764	\$ 16.33
	=====	=====
Options exercisable at quarter end	174,133	\$ 14.07
	=====	=====
Weighted-average fair value of options granted during the quarter		\$ 19.60
		=====

9.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

Note 5. Stock Option Plans (Continued)

Options outstanding at September 30, 2006 and December 31, 2005 were as follows:

Range of Exercise Prices	September 30, 2006			
	Outstanding		Exercisable	
	Number	Weighted Average Remaining Contractual Life	Number	Weighted Average Exercise Price
-----	-----	-----	-----	-----
\$ 7.25 - \$ 9.75	9,000	0.4 years	9,000	\$ 9.75
11.25 - 13.00	59,681	3.7 years	59,681	11.64
13.88 - 18.50	112,583	4.3 years	94,452	14.92
19.60 - 23.29	102,500	8.6 years	12,000	22.78
	-----	-----	-----	-----
	283,764	5.6 years	174,133	\$ 14.07
	=====	=====	=====	=====

Range of Exercise Prices	December 31, 2005			
	Outstanding		Exercisable	
	Number	Weighted Average Remaining Contractual Life	Number	Weighted Average Exercise Price
-----	-----	-----	-----	-----
\$ 7.25 - \$ 9.75	22,300	0.7 years	22,300	\$ 8.69

Edgar Filing: UNIONBANCORP INC - Form 10-Q

11.25 - 13.00	62,681	4.5 years	54,855	11.63
13.88 - 18.50	126,694	5.0 years	98,356	15.04
20.30 - 23.29	90,000	9.2 years	12,000	22.78
	-----	-----	-----	-----
	301,675	5.8 years	187,511	\$ 13.78
	=====	=====	=====	=====

The intrinsic value for stock options is calculated based on the exercise price of the underlying awards and the market price of our common stock as of the reporting date. The intrinsic value of options exercised during the third quarter of 2006 and 2005 was \$310 and \$375. The company recorded \$103 in stock compensation expense during the nine months ended September 30, 2006 to salaries and employee benefits.

The fair value of each stock option granted is estimated using the Black-Scholes based stock option valuation model. This model requires the input of subjective assumptions that will usually have a significant impact on the fair value estimate. Expected volatilities are based on historical volatility of the Company's stock, and other factors. Expected dividends are based on dividend trends and the market price of the Company's stock price at grant. The Company uses historical data to estimate option exercises and employee terminations within the valuation model. The risk-free rate for periods within the contractual life of the options is based on the U. S. Treasury yield curves in effect at the time of grant. There were 17,500 of grants issued during the nine months ended September 30, 2006 and no grants were issued for the nine months ended September 30, 2005.

The Company elected to adopt the modified prospective application method as provided by SFAS 123R, and, accordingly the Company recorded compensation costs as the requisite service rendered for the

10.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

---

Note 5. Stock Option Plans (Continued)

unvested portion of previously issued awards that remain outstanding at the initial date of adoption and any awards issued, modified, repurchased, or cancelled after the effective date of SFAS 123R.

Prior to January 1, 2006, the Company accounted for share-based compensation to employees in accordance with Accounting Principles Board Opinion (APB) No. 25, "Accounting for Stock Issued to Employees," and related interpretations. The Company also followed the disclosure requirements of SFAS 123, "Accounting for Stock-Based Compensation". No stock-based compensation was recognized on employee stock options in the consolidated statement of income before January 1, 2006. Accordingly, financial statement amounts for the prior periods presented in this Form 10-Q have not been restated to reflect the fair value method of expensing share-based compensation.

SFAS 123R requires the recognition of stock based compensation for the number of awards that are ultimately expected to vest. As a result, recognized stock option compensation expense was reduced for estimated forfeitures prior to vesting primarily based on historical annual forfeiture rates of approximately three percent. Estimated forfeitures will be reassessed in subsequent periods

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

and may change based on new facts and circumstances. Prior to January 1, 2006, actual forfeitures were accounted for as they occurred for purposes of required pro forma stock compensation disclosures.

Unrecognized stock option compensation expense related to unvested awards (net of estimated forfeitures) for the remainder of 2006 and beyond is estimated as follows:

Year	Expense
-----	-----
October, 2006 - December, 2006	\$ 34
2007	67
2008	47
2009	28
Total	\$ 176
	=====

The following table illustrates the effect on net income and earnings per share if expense was measured using the fair value recognition provisions of SFAS 123R as of September 30, 2005:

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
	-----	-----
Net income as reported		
for common stockholders	\$ 1,009	\$ 3,251
Deduct: stock-based compensation expense		
determined under fair value based method	27	81
	-----	-----
Pro forma net income	\$ 982	\$ 3,170
	=====	=====
Basic earnings		
per common share as reported	\$ 0.26	\$ 0.82
Pro forma basic earnings		
per common share	\$ 0.25	\$ 0.80
Diluted earnings		
per common share as reported	\$ 0.25	\$ 0.80
Pro forma diluted earnings		
per common share	\$ 0.25	\$ 0.78

11.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

-----

Note 6. Contingent Liabilities And Other Matters

Neither the Company nor any of its subsidiaries are involved in any pending legal proceedings other than routine legal proceedings occurring in the normal course of business, which, in the opinion of management, in the aggregate, are not material to the Company's consolidated financial condition.

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Note 7. Segment Information

The reportable segments are determined by the products and services offered, primarily distinguished between retail, commercial, treasury, wealth management, and operations & other. Loans, and deposits generate the revenues in the commercial segments; deposits, loans, secondary mortgage sales and servicing generates the revenue in the retail segment; investment income generates the revenue in the treasury segment; brokerage and trust services generate the revenue in the wealth management segment (formerly known as the Financial Services segment); and holding company services and discontinued operations associated with the sale of the insurance segment generate the revenue in the operations & other segment. With the sale of the Insurance unit, the results for Insurance were reclassified into the Operations & Other segment from the Financial Services segment (which is now referred to as Wealth Management).

The accounting policies used with respect to segment reporting are the same as those described in the summary of significant accounting policies set forth in Note 1 on page 4. Segment performance is evaluated using net income. Information reported internally for performance assessment follows.

	Three Months Ended				
	September 30, 2006				
	Retail Segment	Commercial Segment	Treasury Segment	Wealth Management	O
Net interest income (loss)	\$ 1,909	\$ 3,217	\$ 126	\$ 50	\$
Other revenue	883	126	--	290	
Other expense	1,306	584	61	323	
Noncash items					
Depreciation	225	2	--	17	
Provision for loan losses	300	(500)	--	--	
Other intangibles	--	--	--	1	
Net allocations	740	1,193	158	214	
Income tax expense	87	641	(101)	(30)	
Segment profit (loss)	134	1,423	8	(185)	
Goodwill	2,512	2,631	--	1,167	
Segment assets	93,948	329,836	197,225	2,132	

	Three Months Ended				
	September 30, 2005				
	Retail Segment	Commercial Segment	Treasury Segment	Wealth Management	O
Net interest income (loss)	\$ 1,914	\$ 3,310	\$ 50	\$ 19	\$
Other revenue	1,024	96	--	430	
Other expense	1,675	821	57	399	
Noncash items					
Depreciation	221	2	--	1	
Provision for loan losses	40	10	--	--	
Other intangibles	--	--	--	1	
Net allocations	850	1,163	140	235	



Edgar Filing: UNIONBANCORP INC - Form 10-Q

Income tax expense	53	434	(123)	(54)
Segment profit (loss)	99	976	(24)	(133)
Goodwill	2,512	2,631	--	1,820
Segment assets	106,675	317,766	209,040	4,350

12.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

	Nine Months Ended				
	September 30, 2006				
	Retail Segment	Commercial Segment	Treasury Segment	Wealth Management	O
Net interest income (loss)	\$ 5,817	\$ 9,606	\$ 342	\$ 159	\$
Other revenue	2,641	347	(88)	876	
Other expense	4,242	1,751	192	1,057	
Noncash items					
Depreciation	668	8	--	54	
Provision for loan losses	325	(1,625)	--	--	
Other intangibles	--	--	--	4	
Net allocations	2,211	3,662	476	680	
Income tax expense	351	2,030	(353)	(208)	
Segment profit (loss)	661	4,127	(61)	(552)	
Goodwill	2,512	2,631	--	1,167	
Segment assets	93,948	329,836	197,225	2,132	

	Nine Months Ended				
	September 30, 2005				
	Retail Segment	Commercial Segment	Treasury Segment	Wealth Management	O
Net interest income (loss)	\$ 5,534	\$ 9,728	\$ 227	\$ 41	\$
Other revenue	3,000	322	--	1,030	
Other expense	4,863	2,521	174	996	
Noncash items					
Depreciation	675	8	--	61	
Provision for loan losses	330	(180)	--	--	
Other intangibles	--	--	--	45	
Net allocations	2,391	3,373	371	589	
Income tax expense	88	1,194	(318)	(172)	
Segment profit (loss)	187	3,134	--	(448)	
Goodwill	2,512	2,631	--	1,820	
Segment assets	106,675	317,766	209,040	4,350	

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Note 8. -- Discontinued Operations

The Company sold the Insurance unit of their Wealth Management segment to the Phoenix Group for \$1.2 million and the deal closed on September 29, 2006. The sale price is subject to final adjustments until December 28, 2006. The Company and Phoenix Group have until this date to evaluate any accounts receivable balances that are ninety days or more past due as of the date of the sale that is not collected in full within ninety days, at the sole discretion of the Phoenix Group, is subject to repurchase by the Company. The Company does not anticipate any significant changes at this time.

In accordance with FASB Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" ("FAS 144") the results of operations of the insurance division are reflected in the Company's statements of income for the three and nine months ended September 30, 2006 and 2005 as "discontinued operations." The loss on the sale of the insurance unit of \$355 thousand and related tax benefit of \$138 thousand are included in discontinued operations for the three and nine months ended September 30, 2006. Additionally, approximately \$1,030 of goodwill and intangibles attributed to the Insurance unit on the Company's balance sheet were written off as a result of this transaction and factored into the loss on the sale of the discontinued operations.

13.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS  
 (In Thousands, Except Per Share Data)

Note 8. -- Discontinued Operations (Continued)

	Three Months Ended September 30,		Nine Months September
	2006	2005	2006
Net Interest Income	\$ 0	\$ (0)	\$ 0
Noninterest Income	(88)	312	532
Noninterest Expense	352	405	1,066
Loss from discontinued operations before income taxes	(440)	(93)	(534)
Benefit for taxes	(170)	(36)	(207)
Net Income (loss) from discontinued operations	(270)	(57)	(327)

14.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
 OPERATIONS

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

(In Thousands, Except Per Share Data)

---

The following discussion provides an analysis of the Company's results of operations and financial condition for the three and nine months ended September 30, 2006 as compared to the same period in 2005. Management's discussion and analysis (MD&A) should be read in conjunction with the consolidated financial statements and accompanying notes presented elsewhere in this report as well as the Company's 2005 Annual Report on Form 10-K. Annualized results of operations during the three and nine months ended September 30, 2006 are not necessarily indicative of results to be expected for the full year of 2006. Unless otherwise stated, all earnings per share data included in this section and throughout the remainder of this discussion are presented on a diluted basis. All financial information is in thousands (000's), except per share data.

Safe Harbor Statement Under the Private Securities Litigation Reform Act of 1995

This report contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Act of 1934 as amended. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and is including this statement for purposes of these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations of the Company, are generally identified by the use of words such as "believe," "expect," "intend," "anticipate," "estimate," "project," "planned" or "potential" or similar expressions. The Company's ability to predict results, or the actual effect of future plans or strategies, is inherently uncertain. Factors which could have a material adverse effect on the operations and future prospects of the Company and the subsidiaries include, but are not limited to, changes in: interest rates; general economic conditions; legislative/regulatory changes; monetary and fiscal policies of the U.S. government, including policies of the U.S. Treasury and the Federal Reserve Board; the quality and composition of the loan or securities portfolios; demand for loan products; deposit flows; competition; demand for wealth management services in the Company's market areas; the Company's implementation of new technologies; the Company's ability to develop and maintain secure and reliable electronic systems; and accounting principles, policies, and guidelines. These risks and uncertainties should be considered in evaluating forward-looking statements and undue reliance should not be placed on such statements.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. By their nature, changes in these assumptions and estimates could significantly affect the Company's financial position or results of operations. Actual results could differ from those estimates. Discussed below are those critical accounting policies that are of particular significance to the Company.

**Allowance for Loan Losses:** The allowance for loan losses is a valuation allowance for probable incurred credit losses, increased by the provision for loan losses and decreased by charge-offs less recoveries. Management estimates the allowance balance required based on past loan loss experience, the nature and volume of the portfolio, information about specific borrower situations and estimated collateral values, current economic conditions, and other factors.

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

Allocations of the allowance may be made for specific loans, but the entire allowance is available for any loan that, in management's judgment, should be charged off. Loan losses are charged against the allowance when management believes that the uncollectibility of a loan balance is confirmed.

15.

### UNIONBANCORP, INC. AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

---

#### General

UnionBancorp, Inc. is a bank holding company organized under the laws of the state of Delaware. The Company derives most of its revenues and income from the operations of its bank subsidiary, UnionBank (the "Bank"). The Company provides a full range of services to individual and corporate customers located in the north central and central Illinois areas. These services include demand, time, and savings deposits; lending; mortgage banking; brokerage services; asset management; and trust services. The Company is subject to competition from other financial institutions, including banks, thrifts and credits unions, as well as nonfinancial institutions providing financial services. Additionally, the Company and the Bank are subject to regulations of certain regulatory agencies and undergo periodic examinations by those regulatory agencies.

#### Third Quarter Highlights

- o On June 30, 2006, UnionBancorp, Inc. and Centru Financial Corporation (NASDAQ: TRUE) announced that they have signed a definitive agreement to join forces in a merger of equals transaction. Under the terms of the agreement, Centru shareholders will receive shares of UnionBancorp common stock, using a fixed exchange ratio of 1.2 shares of UnionBancorp common stock for each share of Centru common stock outstanding. The combined company will adopt the Centru name and change its stock market ticker symbol to TRUE. The merger is subject to approval by UnionBancorp's and Centru's stockholders and banking regulators and other customary conditions. The transaction is expected to be completed in mid-November, 2006.
- o Diluted earnings per share increased 24.0% compared to the third quarter of 2005 and decreased 6.1% as compared to second quarter 2006 levels.
- o The Company's earnings were positively impacted by a \$200 negative provision for loan losses largely based on continued improvements in the quality of the loan portfolio.
- o During the quarter, the Company sold its Insurance unit to a third party.
- o The net interest margin decreased to 3.49% during the third quarter of 2006 as compared with 3.53% for the same period in 2005 due largely to the flat yield curve and intense competition for deposits and loans.
- o The loan portfolio decreased to \$407.0 million as compared to \$417.5 million at December 31, 2005.
- o The level of nonperforming loans to end of period loans totaled 0.79% as of September 30, 2006 compared to 0.92% at September 30, 2005 and

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

0.96% on December 31, 2005.

- o Net charge-offs for the third quarter of 2006 were 0.14% of average loans as compared to 0.17% for the same period 2005.
- o The Company's Board of Directors approved the payment of a \$0.12 quarterly cash dividend on the Company's common stock, marking the 86th consecutive quarter of dividends paid to stockholders.

16.

### UNIONBANCORP, INC. AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

-----

#### Results of Operations

##### Net Income

Income from continuing operations equaled \$1,506 or \$0.38 per diluted share for the three months ended September 30, 2006 compared to \$1,118 or \$0.26 per diluted share earned for same period in 2005. The Company recorded a net loss of (\$270) or (\$0.07) per diluted share from discontinued operations related to the recent sale of the insurance group. Net income for the period was \$1,184 or \$0.31 per diluted share as compared to \$1,009 or \$0.25 per diluted share for the same period in 2005.

For the nine months ended September 30, 2006, net income equaled \$4,020 or \$1.06 per diluted share compared to \$3,251 or \$0.80 per diluted share earned in the same period during 2005. During this period, the Company reported a net loss of (\$327) or (\$0.08) per diluted share related to the discontinued operations for the insurance group as compared to a net loss of (\$143) or (\$0.04) per diluted share for the same period in 2005. For continuing operations, the Company reported results of \$4,503 or \$1.14 per diluted share as compared with earnings of \$3,550 or \$0.84 per diluted share for the same period.

The Company's quarterly results from continuing operations were positively impacted by a negative provision of \$200 to the allowance for loan losses. This action was largely based on continued improvements in the quality of the loan portfolio, favorable loan loss experience and management's beliefs regarding the probability and estimations of future losses inherent in the loan portfolio. Additionally, quarterly earnings were assisted by continued management of noninterest expense levels which led to decreased expense levels, and fewer FTE's drove salary and benefit costs lower and lower accounting and professional fees. These items were partially offset by increased interest expense due to higher rates and an adverse shift in the deposit base from lower paying core deposit accounts to higher paying time deposit accounts. Also contributing to the change in earnings were decreases in revenue generated from the mortgage banking division and brokerage product lines due to lower production volumes.

Return on average assets was 0.76% for the third quarter of 2006 compared to 0.64% for the same period in 2005. Return on average assets was 0.85% for the nine month period ended September 30, 2006 compared to 0.69% for the same period in 2005.

Return on average stockholders' equity was 7.32% for the third quarter of 2006 compared to 6.18% for the same period in 2005. Return on average stockholder's equity was 8.43% for the nine month period ended September 30,

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

2006 compared to 6.55% for the same period in 2005.

### Net Interest Income/ Margin

Net interest income is the difference between income earned on interest-earning assets and the interest expense incurred for the funding sources used to finance these assets. Changes in net interest income generally occur due to fluctuations in the volume of earning assets and paying liabilities and the rates earned and paid, respectively, on those assets and liabilities. The net yield on total interest-earning assets, also referred to as net interest margin, represents net interest income divided by average interest-earning assets. Net interest margin measures how efficiently the Company uses its earning assets and underlying capital. The Company's long-term objective is to manage those assets and liabilities to provide the largest possible amount of income while balancing interest rate, credit, liquidity and capital risks. For purposes of this discussion, both net interest income and margin have been adjusted to a fully tax equivalent basis for certain tax-exempt securities and loans.

17.

### UNIONBANCORP, INC. AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

---

Net interest income, on a tax equivalent basis, was \$5,206 for the three months ended September 30, 2006, compared with \$5,365 earned during the same three-month period in 2005. This represented a decrease of \$159 or 3.0% from the prior year period. The change in net interest income is attributable to the increase in interest expense paid on interest bearing liabilities totaling \$1,226 partially offset by an increase in interest income earned on interest earning assets totaling \$1,067.

The \$1,067 increase in interest income resulted from an increase of \$1,218 due to rate partially offset by a decrease of \$151 due to volume. The majority of the change in interest income was related to the increases in rates experienced from the loan and investment portfolios. The volume within the security and loan portfolios were lower for the third quarter of 2006 as compared to the same period in 2005.

The \$1,226 increase in interest expense resulted from increases of \$1,213 associated with rate and \$13 associated with volume. The majority of the change was attributable to a 98 basis point increase overall in rates paid on the deposit portfolio. Specifically, the rates for time deposit products increased by 102 basis points. There was an increase in rates paid on money market accounts of 102 basis points. Also, the rates paid on NOW accounts increased by 52 basis points.

The net interest margin decreased 4 basis points to 3.49% in the third quarter 2006 as compared with 3.53% for the same period in 2005. The expectation of a flat yield curve is likely to maintain pressure on margins for the remainder of 2006.

Net interest income, on a tax equivalent basis, for the nine months ended September 30, 2006 totaled \$15,602, representing a decrease of \$447 or 2.8% compared to the \$16,049 earned during the same period in 2005. Net interest income decreased largely due to the increase in interest expense paid on interest bearing liabilities totaling \$3,628 exceeding the increase in the interest income earned on interest-earning assets totaling \$3,181. The net

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

interest margin for the first nine months of 2006 decreased 9 basis points to 3.46% compared to 3.55% for the same period in 2005.

The Company's net interest income is affected by changes in the amount and mix of interest-earning assets and interest-bearing liabilities, referred to as "volume change." It is also affected by changes in yields earned on interest-earning assets and rates paid on interest-bearing deposits and other borrowed funds referred to as "rate change." The following table details each category of average amounts outstanding for interest-earning assets and interest-bearing liabilities, average rate earned on all interest-earning assets, average rate paid on all interest-bearing liabilities, and the net yield on average interest-earning assets. In addition, the table reflects the changes in net interest income stemming from changes in interest rates and from asset and liability volume, including mix. The change in interest attributable to both rate and volume has been allocated to the changes in the rate and the volume on a pro rata basis.

18.

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

AVERAGE BALANCE SHEET  
AND ANALYSIS OF NET INTEREST INCOME

For the Three Months Ended September 30,

	2006			2005		
	Average Balance	Interest Income/Expense	Average Rate	Average Balance	Interest Income/Expense	Average Rate
<b>ASSETS</b>						
Interest-earning assets						
Interest-earning deposits	\$ 177	\$ 4	8.97%	\$ 211	\$ 2	3.7
Securities (1)						
Taxable	163,762	2,066	5.01	170,696	1,587	3.6
Non-taxable (2)	19,123	330	6.85	20,433	366	7.0
Total securities (tax equivalent)	182,885	2,396	5.20	191,129	1,953	4.0
Federal funds sold	5,678	71	4.96	1,850	16	3.4
Loans (3) (4)						
Commercial	108,754	2,067	7.54	116,435	2,018	6.7
Real estate	285,091	5,184	7.21	277,104	4,500	6.4
Installment and other	9,009	212	9.34	15,688	378	9.5
Gross loans (tax equivalent)	402,854	7,463	7.35	409,227	6,896	6.6
Total interest-						

Edgar Filing: UNIONBANCORP INC - Form 10-Q

earning assets	591,594	9,934	6.66	602,417	8,867	5.8
<hr style="border-top: 1px dashed black;"/>						
Noninterest-earning assets						
Cash and cash equivalents	17,226			20,973		
Premises and equipment, net	13,730			13,881		
Other assets	25,777			22,650		
<hr style="border-top: 1px dashed black;"/>						
Total nonearning assets	56,733			57,504		
<hr style="border-top: 1px dashed black;"/>						
Total assets	\$648,327			\$659,921		
<hr style="border-top: 1px dashed black;"/>						
LIABILITIES AND STOCKHOLDERS' EQUITY						
Interest-bearing liabilities						
NOW accounts	\$ 69,124	\$ 332	1.91%	\$ 71,893	\$ 266	1.3
Money market accounts	53,283	397	2.96	59,913	293	1.9
Savings deposits	34,657	65	0.74	41,521	48	0.4
Time deposits	307,100	3,334	4.31	283,165	2,225	3.1
Federal funds purchased and repurchase agreements	5,317	69	5.15	5,055	44	3.4
Advances from FHLB	38,820	363	3.71	49,763	486	3.8
Notes payable and other	9,489	168	7.02	10,621	140	5.2
<hr style="border-top: 1px dashed black;"/>						
Total interest-bearing liabilities	517,790	4,728	3.62	525,931	3,502	2.6
<hr style="border-top: 1px dashed black;"/>						
Noninterest-bearing liabilities						
Noninterest-bearing deposits	58,554			61,537		
Other liabilities	4,944			4,304		
<hr style="border-top: 1px dashed black;"/>						
Total noninterest-bearing liabilities	63,498			65,841		
<hr style="border-top: 1px dashed black;"/>						
Stockholders' equity	67,039			68,149		
<hr style="border-top: 1px dashed black;"/>						
Total liabilities and stockholders' equity	\$648,327			\$659,921		
<hr style="border-top: 1px dashed black;"/>						
Net interest income (tax equivalent)		\$ 5,206			\$ 5,365	
<hr style="border-top: 1px dashed black;"/>						
Net interest income (tax equivalent) to total earning assets			3.49%			3.5
<hr style="border-top: 1px dashed black;"/>						
Interest-bearing liabilities to earning assets	87.52%			87.30%		
<hr style="border-top: 1px dashed black;"/>						

- 
- (1) Average balance and average rate on securities classified as available-for-sale is based on historical amortized cost balances.
  - (2) Interest income and average rate on non-taxable securities are reflected on a tax equivalent basis based upon a statutory federal income tax rate of 34%.
  - (3) Nonaccrual loans are included in the average balances. (4) Overdraft loans are excluded in the average balances.



## Edgar Filing: UNIONBANCORP INC - Form 10-Q

UNIONBANCORP, INC. AND SUBSIDIARIES  
 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
 OPERATIONS  
 (In Thousands, Except Per Share Data)

### AVERAGE BALANCE SHEET AND ANALYSIS OF NET INTEREST INCOME

	For the Nine Months Ended September 30,					
	2006			2005		
	Average Balance	Interest Income/ Expense	Average Rate	Average Balance	Interest Income/ Expense	Average Rate
<b>ASSETS</b>						
Interest-earning assets						
Interest-earning deposits	\$ 213	\$ 11	6.90%	\$ 166	\$ 5	4.03
Securities (1)						
Taxable	173,367	6,083	4.69	165,884	4,494	3.62
Non-taxable (2)	18,493	976	7.06	21,595	1,155	7.15
Total securities (tax equivalent)	191,860	7,059	4.92	187,479	5,649	4.03
Federal funds sold	3,415	130	5.09	3,309	72	2.91
Loans (3) (4)						
Commercial	112,906	6,109	7.23	118,490	5,884	6.64
Real estate	284,636	15,004	7.05	277,172	13,017	6.28
Installment and other	10,442	738	9.45	17,996	1,243	9.23
Gross loans (tax equivalent)	407,984	21,851	7.16	413,658	20,144	6.51
Total interest- earning assets	603,472	29,051	6.44	604,612	25,870	5.72
Noninterest-earning assets						
Cash and cash equivalents	17,823			18,862		
Premises and equipment, net	13,770			13,715		
Other assets	24,350			24,114		
Total nonearning assets	55,943			56,691		
Total assets	\$659,415			\$661,303		
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>						
Interest-bearing liabilities						
NOW accounts	\$ 69,507	\$ 928	1.79%	\$ 72,827	\$ 635	1.17
Money market accounts	53,960	1,106	2.74	59,012	741	1.68
Savings deposits	36,734	187	0.68	42,940	161	0.50
Time deposits	308,021	9,231	4.01	280,501	6,186	2.95

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Federal funds purchased and repurchase agreements	5,092	192	5.04	7,002	155	2.96
Advances from FHLB	45,307	1,300	3.86	55,638	1,619	3.89
Notes payable and other	10,070	505	6.70	9,075	330	4.77
	-----	-----	-----	-----	-----	-----
Total interest-bearing liabilities	528,421	13,449	3.40	526,997	9,827	2.42
	-----	-----	-----	-----	-----	-----
Noninterest-bearing liabilities						
Noninterest-bearing deposits	59,969			60,658		
Other liabilities	4,918			4,068		
	-----			-----		
Total noninterest-bearing liabilities	64,887			64,726		
	-----			-----		
Stockholders' equity	66,107			69,580		
	-----			-----		
Total liabilities and stockholders' equity	\$659,415			\$661,303		
	=====			=====		
Net interest income (tax equivalent)		\$ 15,602			\$ 16,043	
		=====			=====	
Net interest income (tax equivalent) to total earning assets			3.46%			3.55%
			=====			=====
Interest-bearing liabilities to earning assets		87.56%			87.16%	
		=====			=====	

- 
- (1) Average balance and average rate on securities classified as available-for-sale is based on historical amortized cost balances.
- (2) Interest income and average rate on non-taxable securities are reflected on a tax equivalent basis based upon a statutory federal income tax rate of 34%.
- (3) Nonaccrual loans are included in the average balances.
- (4) Overdraft loans are excluded in the average balances.

20.

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

---

Provision for Loan Losses

The Company recorded a negative provision of \$200 to the allowance for loan losses for the third quarter of 2006 which is a decrease of \$250 from the \$50 recorded during the same period a year ago. A negative \$1,300 provision for the loan losses was charged to operation expense for the nine months ended September 30, 2006 which was a decrease of \$1,450 from \$150 recorded during the same period a year ago. The decrease in the provision was largely based on continued improvements in the quality of the loan portfolio, favorable loan loss experience and management's beliefs regarding the probability and estimations of future losses inherent in the loan portfolio. Nonperforming loans decreased \$505 from \$3,726 as of September 30, 2005 to \$3,221 as of September 30, 2006. In

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

comparison to December 31, 2005, nonperforming loans decreased \$783 from \$4,004.

Net charge-offs for the third quarter of 2006 were \$545 compared with \$716 for the comparable period in 2005. Annualized net charge-offs were 0.14% of average loans for the third quarter of 2006 compared with 0.17% of average loans for same period in 2005. Net charge-off for the nine months ended September 30, 2006 were \$959 compared with \$1,389 for the comparable period in 2005. Annualized net charge-offs also decreased to 0.23% of average loans for the nine months ended September 30, 2006 compared to 0.34% in the same period in 2005. See "Nonperforming Assets" and "Other Potential Problem Loans" for further information.

The amount of the provision for loan losses is based on management's evaluations of the loan portfolio, with particular attention directed toward nonperforming, impaired and other potential problem loans. During these evaluations, consideration is also given to such factors as management's evaluation of specific loans, the level and composition of impaired loans, other nonperforming loans, other identified potential problem loans, historical loss experience, results of examinations by regulatory agencies, results of the independent asset quality review process, the market value of collateral, the estimate of discounted cash flows, the strength and availability of guarantees, concentrations of credits, and various other factors, including concentration of credit risk in various industries and current economic conditions.

Management remains watchful of credit quality issues. Should the economic climate deteriorate from current levels, borrowers may experience difficulty, and the level of nonperforming loans, charge-offs and delinquencies could rise and require further increases in the provision.

### Noninterest Income

Noninterest income consists of a wide variety of fee-based revenues from bank-related service charges on deposits and mortgage revenues. Also included in this category are revenues generated by the Company's brokerage, trust and asset management product lines as well as increases in cash surrender value on bank-owned life insurance. The following table summarizes the Company's noninterest income:

21.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
 OPERATIONS  
 (In Thousands, Except Per Share Data)

	Three Months Ended September 30,		Nine Mont Septembe
	2006	2005	2006
Service charges	\$ 476	\$ 490	\$ 1,411
Trust income	202	193	620
Mortgage banking income	240	357	767
Brokerage commissions and fees	87	236	260
Bank owned life insurance	153	138	430
Securities gains (losses), net	--	--	(88)
Gain on the sale of assets	(1)	--	(2)

Edgar Filing: UNIONBANCORP INC - Form 10-Q

Other income	324	288	927
	-----	-----	-----
	\$ 1,481	\$ 1,702	\$ 4,325
	=====	=====	=====

Noninterest income totaled \$1,481 for the three months ended September 30, 2006, compared to \$1,702 for the same period in 2005. Exclusive of the net gains on sale of assets and net securities gains for both periods, noninterest income equaled \$1,482 for the three months ended September 30, 2006, compared to \$1,702 for the same period in 2005. This represented a decrease of \$220 or 12.9%. The quarter-over-quarter decrease was primarily attributable to a production level decrease in revenue generated from the mortgage banking division, and lower brokerage revenues.

Noninterest income totaled \$4,325 for the nine months ended September 30, 2006, compared to \$4,893 for the same time frame in 2005. Excluding all net gains on sale of assets and net securities gains for both periods, noninterest income decreased \$475 or 10.0%. The change was largely reflective of the same items discussed regarding the third quarter. Additionally, results were impacted by the impact related to losses for investment activities.

Noninterest Expense

Noninterest expense is comprised primarily of compensation and employee benefits, occupancy and other operating expense. The following table summarizes the Company's noninterest expense:

	Three Months Ended September 30,		Nine Months September
	2006	2005	2006
	-----	-----	-----
Salaries and employee benefits	\$ 2,630	\$ 3,098	\$ 8,035
Occupancy expense, net	356	386	1,110
Furniture and equipment expense	515	497	1,508
Marketing	88	115	294
Supplies and printing	71	80	230
Telephone	104	112	339
Other real estate owned expense	2	12	10
Amortization of intangible assets	11	30	71
Other expenses	814	1,017	2,754
	-----	-----	-----
	\$ 4,591	\$ 5,347	\$ 14,351
	=====	=====	=====

Noninterest expense totaled \$4,591 for the three months ended September 30, 2006, as compared to \$5,347 for the same period in 2005. This represented a decrease of \$756 or 14.2%. This improvement in noninterest expense was primarily

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

(In Thousands, Except Per Share Data)

due to the reduction of salary and benefit costs, and lower accounting and professional fees. These savings were offset by a modest increase in furniture and fixture expense.

Noninterest expense totaled \$14,351 for the nine months ended September 30, 2006, decreasing by \$1,353 or 8.7% from the same period in 2005. The change was largely reflective of the same items discussed regarding the third quarter.

### Applicable Income Taxes

Income tax expense for the periods included benefits for tax-exempt income, tax-advantaged investments, loss from discontinued operations and general business tax credits offset by the effect of nondeductible expenses. For the third quarter, the Company's effective tax rate overall was 28.3% as its total applicable taxes were \$488 on pretax earnings of \$1,724. The following table shows the Company's income from continuing operations before income taxes, as well as applicable income taxes and the effective tax rate for the three and nine months ended September 30, 2006 and 2005.

	Three Months Ended September 30,			Nine Month September
	2006	2005		2006
Income from continuing operations				
before income taxes	\$ 2,164	\$ 1,523	\$	6,436
Applicable income taxes	658	405		1,983
Effective tax rates	30.4%	26.5%		30.8%

The Company recorded an income tax expense of \$658 and of \$405 on income from continuing operations for the three months ended September 30, 2006 and 2005, respectively. Effective tax rates equaled 30.4% and 26.5% respectively, for such periods.

Income tax expense for the periods included benefits for tax-exempt income, tax-advantaged investments and general business tax credits offset by the effect of nondeductible expenses. The Company's effective tax rate was lower than statutory rates due to the Company deriving interest income from municipal securities and loans, which are exempt from federal tax and certain U. S. government agency securities, which are exempt from Illinois State tax. Additionally, the Company has reduced tax expense through various tax planning initiatives.

The Company recorded income tax expense of \$1,983 and \$1,076 on income from continuing operations for the nine months ended September 30, 2006 and 2005, respectively. Effective tax rates equaled 30.8% and 23.3% respectively, for such periods.

### Preferred Stock Dividends

The Company paid \$52 in preferred stock dividends for the three months ended September 30, 2006 and 2005, respectively. The Company paid \$156 in preferred stock dividends for the nine months ended September 30, 2006 and 2005, respectively.

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
OPERATIONS

(In Thousands, Except Per Share Data)

Interest Rate Sensitivity Management

The business of the Company and the composition of its balance sheet consist of investments in interest-earning assets (primarily loans and securities) which are primarily funded by interest-bearing liabilities (deposits and borrowings). All of the financial instruments of the Company are for other than trading purposes. Such financial instruments have varying levels of sensitivity to changes in market rates of interest. The operating income and net income of the Bank depends, to a substantial extent, on "rate differentials," i.e., the differences between the income the Bank receives from loans, securities, and other earning assets and the interest expense they pay to obtain deposits and other liabilities. These rates are highly sensitive to many factors that are beyond the control of the Bank, including general economic conditions and the policies of various governmental and regulatory authorities.

The Company measures its overall interest rate sensitivity through a net interest income analysis. The net interest income analysis measures the change in net interest income in the event of hypothetical changes in interest rates. This analysis assesses the risk of changes in net interest income in the event of a sudden and sustained 100 to 200 basis point increase or decrease in market interest rates. The interest rates scenarios are used for analytical purposes and do not necessarily represent management's view of future market movements. The tables below present the Company's projected changes in net interest income for the various rate shock levels at September 30, 2006 and December 31, 2005, respectively:

		September 30, 2006 Net Interest Income		
		Amount	Change	Change
		(Dollars in Thousands)		
+200 bp	\$	21,853	\$ 1,106	5.33%
+100 bp		21,339	592	2.85
Base		20,748	--	--
-100 bp		20,058	(690)	(3.32)
-200 bp		18,898	(1,850)	(8.92)

Based upon the Company's model at September 30, 2006, the effect of an immediate 200 basis point increase in interest rates would increase the Company's net interest income by \$1,106 or 5.33%. The effect of an immediate 200 basis point decrease in rates would decrease the Company's net interest income by \$1,850 or 8.92%.

		December 31, 2005 Net Interest Income		
		Amount	Change	Change
		(Dollars in Thousands)		
+200 bp	\$	23,043	\$ 959	4.34%

Edgar Filing: UNIONBANCORP INC - Form 10-Q

+100 bp	22,629	545	2.47
Base	22,084	--	--
-100 bp	21,314	(770)	(3.49)
-200 bp	19,744	(2,340)	(10.59)

Based upon the Company's model at December 31, 2005, the effect of an immediate 200 basis point increase in interest rates would increase the Company's net interest income by \$959 or 4.34%. The effect of an immediate 200 basis point decrease in rates would decrease the Company's net interest income by \$2,340 or 10.59%.

24.

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
OPERATIONS  
(In Thousands, Except Per Share Data)

---

Financial Condition

General

As of September 30, 2006, the Company had total assets of \$648,851, total gross loans of \$400,912, total deposits of \$526,918 and total stockholders' equity of \$67,304. Total assets decreased by \$27,371 or 4.0% from year-end 2005 related primarily to decline in the investment portfolio. Total gross loans decreased by \$10,510 or 2.5% from year-end 2005. Total deposits declined by \$16,923 or 3.1% from year-end 2005. These changes were implemented to reduce the investment portfolio as with the flat yield curve the Company was experiencing slim spreads over its cost of funds. Thus, the cost of funds which was the primarily the FHLB advances was reduced as the investments were sold.

Nonperforming Assets

The Company's financial statements are prepared on the accrual basis of accounting, including the recognition of interest income on its loan portfolio, unless a loan is placed on nonaccrual status. Loans are placed on nonaccrual status when there are serious doubts regarding the collectibility of all principal and interest due under the terms of the loans. Amounts received on nonaccrual loans generally are applied first to principal and then to interest after all principal has been collected. It is the policy of the Company not to renegotiate the terms of a loan because of a delinquent status. Rather, a loan is generally transferred to nonaccrual status if it is not in the process of collection and is delinquent in payment of either principal or interest beyond 90 days. Loans that are 90 days delinquent but are well secured and in the process of collection are not included in nonperforming assets. Other nonperforming assets consist of real estate acquired through loan foreclosures or other workout situations and other assets acquired through repossessions.

The classification of a loan as nonaccrual does not necessarily indicate that the principal is uncollectible, in whole or in part. The Bank makes a determination as to collectibility on a case-by-case basis. The Bank considers both the adequacy of the collateral and the other resources of the borrower in determining the steps to be taken to collect nonaccrual loans. The final determination as to the steps taken is made based upon the specific facts of each situation. Alternatives that are typically considered to collect nonaccrual loans are foreclosure, collection under guarantees, loan restructuring, or judicial collection actions.

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

Each of the Company's loans is assigned a rating based upon an internally developed grading system. A separate credit administration department also reviews grade assignments on an ongoing basis. Management continuously monitors nonperforming, impaired, and past due loans to prevent further deterioration of these loans. The Company has an independent loan review function which is separate from the lending function and is responsible for the review of new and existing loans.

25.

UNIONBANCORP, INC. AND SUBSIDIARIES  
 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
 OPERATIONS  
 (In Thousands, Except Per Share Data)

-----

The following table summarizes nonperforming assets and loans past due 90 days or more and still accruing for the previous five quarters.

	2006		
	Sept 30,	Jun 30,	Mar 31,
	-----	-----	-----
Non-accrual loans	\$ 3,053	\$ 2,289	\$ 2,785
Loans 90 days past due and still accruing interest	168	517	567
	-----	-----	-----
Total nonperforming loans	3,221	2,806	3,352
Other real estate owned	859	1,390	536
	-----	-----	-----
Total nonperforming assets	\$ 4,080	\$ 4,196	\$ 3,888
	=====	=====	=====
Nonperforming loans to total end of period loans	0.79%	0.70%	0.82%
Nonperforming assets to total end of period loans	1.00	1.04	0.96
Nonperforming assets to total end of period assets	0.63	0.64	0.59

The level of nonperforming loans at September 30, 2006 decreased to \$3,221 versus the \$4,004 that existed as of December 31, 2005 and from \$3,726 at September 30, 2005. The level of nonperforming loans to total end of period loans was 0.79% at September 30, 2006, as compared to 0.96% at December 31, 2005 and 0.92% at September 30, 2005. The reserve coverage ratio (allowance to nonperforming loans) was reported at 189.48% as of September 30, 2006 as compared to 208.84% as of December 31, 2005 and 227.94% as of September 30, 2005.

#### Other Potential Problem Loans

The Company has other potential problem loans that are currently performing, but where some concerns exist as to the ability of the borrower to comply with present loan repayment terms. Excluding nonperforming loans and loans that management has classified as impaired, these other potential problem loans totaled \$3,785 at September 30, 2006, as compared to \$6,339 at September 30, 2005 and \$2,879 at December 31, 2005. The classification of these loans, however, does not imply that management expects losses on each of these loans, but believes that a higher level of scrutiny and close monitoring is prudent under the circumstances. Such classifications relate to specific concerns for



## Edgar Filing: UNIONBANCORP INC - Form 10-Q

each individual borrower and do not relate to any concentration risk common to all loans in this group.

### Allowance for Loan Losses

At September 30, 2006, the allowance for loan losses was \$6,103 or 1.50% of total loans as compared to \$8,362 or 2.00% at December 31, 2005, and \$8,493 or 2.09% at September 30, 2005. The decrease in the allowance was largely based on continued improvements in the quality of the loan portfolio, favorable loan loss experience and management's beliefs regarding the probability and estimations of future losses inherent in the loan portfolio. This continued improvement in asset quality has been driven by the decrease in non-performing and watch list loans as well as resolutions, either through charge-off of non-bankable assets or through the successful workout strategies that have been executed. The Company's loans with specific reserves under FASB No. 114 assigned to them have continued to decrease throughout the year. As of September 30, 2006 the Company has approximately \$2,398 of specific reserves compared to \$4,682 as of December 31, 2005. In originating loans, the Company recognizes that credit losses will be experienced and the risk of loss will vary with, among other things, general economic conditions; the type of loan being made; the creditworthiness of the borrower over the term of the loan; and, in the case of a collateralized loan, the quality of the collateral for such a loan. The

26.

### UNIONBANCORP, INC. AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

---

allowance for loan losses represents the Company's estimate of the allowance necessary to provide for probable incurred losses in the loan portfolio. In making this determination, the Company analyzes the ultimate collectibility of the loans in its portfolio, incorporating feedback provided by internal loan staff, the independent loan review function, and information provided by examinations performed by regulatory agencies. The Company makes an ongoing evaluation as to the adequacy of the allowance for loan losses.

On a quarterly basis, management reviews the adequacy of the allowance for loan losses. Commercial credits are graded by the loan officers and the Loan Review function validates the officers' grades. In the event that the loan review function downgrades the loan, it is included in the allowance analysis at the lower grade. The grading system is in compliance with the regulatory classifications and the allowance is allocated to the loans based on the regulatory grading, except in instances where there are known differences (i.e., collateral value is nominal, etc.). To establish the appropriate level of the allowance, a sample of loans (including impaired and nonperforming loans) are reviewed and classified as to potential loss exposure.

Based on an estimation computed pursuant to the requirements of Financial Accounting Standards Board ("FASB") Statement No. 5, "Accounting for Contingencies," and FASB Statements Nos. 114 and 118, "Accounting by Creditors for Impairment of a Loan," the analysis of the allowance for loan losses consists of three components: (i) specific credit allocation established for expected losses resulting from analysis developed through specific credit allocations on individual loans for which the recorded investment in the loan exceeds its fair value; (ii) general portfolio allocation based on historical loan loss experience for each loan category; and (iii) subjective reserves based on general economic conditions as well as specific economic factors in the markets in which the Company operates.

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

The specific credit allocation component of the allowance for loan losses is based on a regular analysis of loans over a fixed-dollar amount where the internal credit rating is at or below a predetermined classification. The fair value of the loan is determined based on either the present value of expected future cash flows discounted at the loan's effective interest rate, the market price of the loan, or, if the loan is collateral dependent, the fair value of the underlying collateral less cost of sale.

The general portfolio allocation component of the allowance for loan losses is determined statistically using a loss migration analysis that examines historical loan loss experience. The loss migration analysis is performed quarterly and loss factors are updated regularly based on actual experience. The general portfolio allocation element of the allowance for loan losses also includes consideration of the amounts necessary for concentrations and changes in portfolio mix and volume.

The allowance for loan losses is based on estimates, and ultimate losses will vary from current estimates. These estimates are reviewed monthly, and as adjustments, either positive or negative, become necessary, a corresponding increase or decrease is made in the provision for loan losses. The composition of the loan portfolio has not significantly changed since year-end 2005. The methodology used to determine the adequacy of the allowance for loan losses is consistent with prior years, and there were no material reallocations.

Management remains watchful of credit quality issues. Should the economic climate deteriorate from current levels, borrowers may experience difficulty, and the level of nonperforming loans, charge-offs and delinquencies could rise and require further increases in the provision.

27.

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
OPERATIONS  
(In Thousands, Except Per Share Data)

---

### Liquidity

The Company manages its liquidity position with the objective of maintaining sufficient funds to respond to the needs of depositors and borrowers and to take advantage of earnings enhancement opportunities. In addition to the normal inflow of funds from core-deposit growth together with repayments and maturities of loans and investments, the Company utilizes other short-term funding sources such as brokered time deposits, securities sold under agreements to repurchase, overnight federal funds purchased from correspondent banks and the acceptance of short-term deposits from public entities, and Federal Home Loan Bank advances.

The Company monitors and manages its liquidity position on several bases, which vary depending upon the time period. As the time period is expanded, other data is factored in, including estimated loan funding requirements, estimated loan payoffs, investment portfolio maturities or calls, and anticipated depository buildups or runoffs.

The Company classifies all of its securities as available-for-sale, thereby maintaining significant liquidity. The Company's liquidity position is further enhanced by structuring its loan portfolio interest payments as monthly and by the significant representation of retail credit and residential mortgage loans in the Company's loan portfolio, resulting in a steady stream of loan

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

repayments. In managing its investment portfolio, the Company provides for staggered maturities so that cash flows are provided as such investments mature.

The Company's cash flows are comprised of three classifications: cash flows from operating activities, cash flows from investing activities, and cash flows from financing activities. Cash flows provided by operating activities and investing activities offset by those used in financing activities, resulted in a net decrease in cash and cash equivalents of \$4,307 from December 31, 2005 to September 30, 2006.

During the first nine months of 2006, the Company experienced net cash in flows of \$3,504 in operating activities due to negative provision and net income and \$17,047 in investing activities largely due to the decrease in net loans and securities. In contrast, net cash outflow of \$24,858 in financing activities primarily due to a decrease in deposits and borrowed funds.

### Contractual Obligations, Commitments, Contingencies, and Off-Balance Sheet Financial Instruments

The Company has entered into contractual obligations and commitments and off-balance sheet financial instruments. The following tables summarize the Company's contractual cash obligations and other commitments and off balance sheet instruments as of September 30, 2006.

	Payments Due by Period		
	Within 1 Year	1-3 Years	4-5 Years
Contractual Obligations			
Short-term debt	\$ 8,100	\$ --	\$ --
Long-term debt	--	201	--
Certificates of Deposit	244,115	64,410	1,917
Series B Mandatory redeemable			
Preferred stock	--	831	--
FHLB Advances	8,100	20,400	8,200
Total contractual cash obligations	\$ 260,315	\$ 85,842	\$ 10,117

28.

### UNIONBANCORP, INC. AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (In Thousands, Except Per Share Data)

	Amount of Commitment Expiration		
	Within 1 Year	1-3 Years	4-5 Years
Off-Balance Sheet Financial Instruments			

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

Lines of credit	\$ 57,671	\$ 5,935	\$ 1,700
Standby letters of credit	8,861	742	--
	-----	-----	-----
 Total commercial commitments	 \$ 66,532	 \$ 6,677	 \$ 1,700
	=====	=====	=====

If the announced merger between UnionBancorp, Inc. and Centru Financial Corporation (NASDAQ: TRUE) is terminated, UnionBancorp, Inc is required to fulfill the certain specified obligations to make certain payments to Centru Financial Corporation as described below:

- o If the merger agreement is terminated by Centru because UnionBancorp has not satisfied its conditions or the closing has not occurred by March 1, 2007 and UnionBancorp knowingly breached its covenants, agreements, representations or warranties under the merger agreement (unless such breach is a result of the failure by Centru to perform and comply with any of its obligations) then, provided Centru is in compliance with its obligations under the merger agreement, UnionBancorp must pay \$2,700 to Centru.
- o If the merger agreement is terminated by UnionBancorp or Centru because UnionBancorp's stockholders fail to approve the merger (a "UnionBancorp Stockholder Termination"); then, provided Centru is in compliance with its obligations under the merger agreement, UnionBancorp must pay \$500 to Centru.
- o In addition to the \$500 payment described above (if any), if there is a UnionBancorp Stockholder Termination and, within twelve months after such UnionBancorp Stockholder Termination, UnionBancorp enters into an agreement with any party other than Centru providing for the acquisition of UnionBancorp, then, provided Centru was in compliance with its obligations under the merger agreement, UnionBancorp must pay \$2,200 to Centru.
- o If UnionBancorp terminates the merger agreement as a result of a superior UnionBancorp Proposal, then UnionBancorp must pay \$2,700 to Centru.

### Capital Resources

#### Stockholders' Equity

The Company is committed to managing capital for maximum shareholder benefit and maintaining strong protection for depositors and creditors. Stockholders' equity at September 30, 2006 was \$67,313, an increase of \$1,238 or 1.8%, from December 31, 2005. The increase in stockholders' equity was the result of the net income for the period partially offset by the dividends paid to shareholders and a decrease in accumulated other comprehensive income. Average quarterly equity as a percentage of average quarterly assets was 10.34% at September 30, 2006, compared to 10.01% at December 31, 2005. Book value per common share equaled \$17.85 at September 30, 2006 compared to \$17.23 at December 31, 2005.

#### Stock Repurchase

On May 2, 2003, the Board of Directors approved a stock repurchase plan whereby the Company may repurchase from time to time up to 5% of its outstanding shares of common stock in the open market or in private transactions over an 18

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
OPERATIONS

(In Thousands, Except Per Share Data)

month period. On September 23, 2004, the Board of Directors extended the Company's stock repurchase program through May 2, 2006. On June 16, 2005, the Board of Directors amended the repurchase plan to enable the Company to acquire an additional 5% of its outstanding shares of common stock in the open market or in private transactions. On March 16, 2006, the Board of Directors approved an additional 5% stock repurchase program that begins when the existing plan is completed. Under the revised plan, the Company can repurchase approximately 188,000 shares of its outstanding shares of common stock. Under the terms of the plan, the Company is able to repurchase, from time to time, up to 5% of its outstanding shares of common stock in the open market or in private transactions. Purchases are dependent upon market conditions and the availability of shares. The extension of the repurchase program enables the Company to optimize its use of capital relative to other investment alternatives and benefits both the Company and the shareholders by enhancing earnings per share and return on equity. During the quarter ending September 30, 2006, no shares were repurchased and to date, the Company has repurchased 364,879 shares at a weighted average cost of \$21.16.

Capital Measurements

The Company is expected to meet a minimum risk-based capital to risk-weighted assets ratio of 8%, of which at least one-half (or 4%) must be in the form of Tier 1 (core) capital. The remaining one-half (or 4%) may be in the form of Tier 1 (core) or Tier 2 (supplementary) capital. The amount of loan loss allowance that may be included in capital is limited to 1.25% of risk-weighted assets. The ratio of Tier 1 (core) and the combined amount of Tier 1 (core) and Tier 2 (supplementary) capital to risk-weighted assets for the Company was 12.4% and 13.6%, respectively, at September 30, 2006. The Company is currently, and expects to continue to be, in compliance with these guidelines.

The following table sets forth an analysis of the Company's capital ratios:

	September 30, 2006	December 31,		Minimum Capital Ratios
		2005	2004	
Tier 1 risk-based capital	\$ 60,960	\$ 60,546	\$ 63,347	
Tier 2 risk-based capital	6,103	6,266	6,067	
Total capital	67,063	66,812	69,414	
Risk-weighted assets	492,984	501,342	485,325	
Capital ratios				
Tier 1 risk-based capital	12.4%	12.1%	13.0%	4.
Tier 2 risk-based capital	13.6	13.3	14.3	8.
Leverage ratio	9.5	9.0	9.5	4.

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

### Impact of Inflation, Changing Prices, and Monetary Policies

The financial statements and related financial data concerning the Company have been prepared in accordance with U.S. generally accepted accounting principles 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. The primary effect of inflation on the operations of the Company is reflected in increased operating costs. Unlike most industrial companies, virtually all of the assets and liabilities of a financial institution are monetary in nature. As a result, changes in interest rates have a more significant effect on the performance of a financial institution than do the effects of changes in the general rate of inflation and changes in prices. Interest rates do not necessarily move in the same direction or in the same magnitude as the prices of goods and services. Interest rates are highly sensitive to many factors which are beyond the control

30.

### UNIONBANCORP, INC. AND SUBSIDIARIES MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In Thousands, Except Per Share Data)

---

of the Company, including the influence of domestic and foreign economic conditions and the monetary and fiscal policies of the United States government and federal agencies, particularly the Federal Reserve Board.

### Recent Regulatory and Accounting Developments

In February, 2006, the FASB issued SFAS No. 155, "Accounting for Certain Hybrid Financial Instruments - An Amendment of FASB Statement No. 133 and 140" ("SFAS 155"). SFAS 155 simplifies the accounting for certain hybrid financial instruments that contain an embedded derivative that otherwise would have required bifurcation. SFAS 155 also eliminates the interim guidance in FASB Statement No. 133, which provides that beneficial interest in securitized financial assets are not subject to the provisions of FASB Statement No. 133. SFAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year that begins after September 15, 2006, which for the Company will be as of the beginning of fiscal 2007. The Company does not believe that the adoption of SFAS 155 will have a significant effect on its financial statements as the Company does not have any hybrid financial instruments at this time.

In March, 2006, the FASB issued SFAS No. 156, "Accounting for Servicing of Financial Assets - An Amendment of FASB Statement No. 140" ("SFAS 156"). SFAS 156 requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable. The statement permits, but does not require, the subsequent measurement of servicing assets and servicing liabilities at fair value. SFAS 156 is effective as of the beginning of the entity's first fiscal year that begins after September 15, 2006. The Company is currently evaluating any potential impact of the adoption of this SFAS.

In September, 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement does not require any new fair value measurements. It is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of the adoption of SFAS

## Edgar Filing: UNIONBANCORP INC - Form 10-Q

157, with respect to its current practice of measuring fair value and disclosure in its financial statements.

In June, 2006, the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - An Interpretation of FASB No. 109" ("FIN 48"). FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The Interpretation is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of the adoption of FIN 48, with respect to its results of operations, financial position and liquidity.

In September, 2006, the U.S. Securities and Exchange Commission ("SEC") amended Part 211 of Title 17 of the Code of Federal Regulations by adding the Staff Accounting Bulletin No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements" ("SAB 108"). SAB 108 provides guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. SAB 108 is effective for fiscal years ending after November 15, 2006. The Company is reviewing this accounting bulletin, but has not yet determined the effect of adopting the Interpretation.

31.

UNIONBANCORP, INC. AND SUBSIDIARIES  
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF  
OPERATIONS  
(In Thousands, Except Per Share Data)

---

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

The information required by this Item 3 is incorporated by reference from the discussion on page 24 of this Form 10-Q under the caption "Interest Rate Sensitivity Management" and the discussion on page 31 under the caption "Impact of Inflation, Changing Prices, and Monetary Policies."

### Item 4. Controls and Procedures

As of the end of the period covered by this report, the Company carried out an evaluation under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities and Exchange Act of 1934, as amended). Based on this evaluation, the Company's Chief Executive Officer/Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective in timely alerting them to material information relating to the Company required to be included in the Company's periodic filings with the Securities and Exchange Commission. It should be noted that in designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. The Company has designed its disclosure controls and procedures to reach a level of reasonable assurance of achieving the desired control objectives and, based on the evaluation described above, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective at reaching that level of reasonable assurance.

Edgar Filing: UNIONBANCORP INC - Form 10-Q

There was no change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended) during the Company's most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

32.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

In the normal course of business the Company may be involved in various legal proceedings from time to time. The Company does not believe it is currently involved in any claim or action the ultimate disposition of which would have a material adverse effect on the Company's financial statements.

Item 1A. Risk Factors

The Company did not experience any material changes in the Risk Factors during the Company's most recently completed fiscal quarter. For specific information about the risks facing the Company refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2005.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information about purchases of the Company's common stock by the Company during the quarter ended September 30, 2006.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased under the Plans or Programs
07/01/06 - 07/31/06	--	--	--	
08/01/06 - 08/31/06	--	--	--	
09/01/06 - 09/30/06	--	--	--	
Total (1)	--	--	--	

(1) The Company did not repurchase any stock during the quarter ended September 30, 2006. The current repurchase program approved on March 23, 2006 provides for the repurchase by us of an additional 5% of the outstanding shares of our common stock. The expiration date of this program is September 23, 2007. Unless terminated earlier by resolution of our board of directors, the program will expire on the earlier of



## Edgar Filing: UNIONBANCORP INC - Form 10-Q

such expiration date or when we have repurchased all shares authorized for repurchase under the program.

### Item 3. Defaults Upon Senior Securities

None.

33.

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

None.

### Item 5. Other Information

None.

### Item 6. Exhibits

Exhibits:

- 2.1 Agreement and Plan of Merger between UnionBancorp, Inc and Centru Financial Corporation (incorporated by reference from Current Report on Form 8-K filed on July 7, 2006).
- 2.2 First Amendment to Agreement and Plan of Merger (incorporated by reference from Current Report on Form 8-K filed on October 26, 2006).
- 3.1 Restated Certificate of Incorporation of UnionBancorp, Inc. and Amendments thereto (filed as Exhibit to UnionBancorp's Registration Statement on Form S-1 (Registration No. 33-9891) (the "S-1 Registration Statement").
- 4.1 Amendment No. 1 to Rights Agreement (incorporated by reference from Current Report on Form 8-K filed on July 7, 2006).
- 10.1 Thomas A. Daiber Employment Agreement (incorporated by reference from Exhibit 2.1 to UnionBancorp's Current Report on Form 8-K filed with the SEC on July 7, 2006 (appears as Exhibit F-1 thereto)).
- 10.2 Kurt R. Stevenson Employment Agreement (incorporated by reference from Exhibit 2.1 to UnionBancorp's Current Report on Form 8-K filed with the SEC on July 7, 2006 (appears as Exhibit F-3 thereto)).
- 10.3 UnionBancorp Voting Agreement (incorporated by reference from Current Report of Form 8-K filed on July 7, 2006).
- 10.4 Centru Voting Agreement (incorporated by reference from Current Report of Form 8-K filed on July 7, 2006).
- 31.1 Certification of Kurt R. Stevenson, Interim President and Principal Executive Officer, required by Rule 13a - 14(a).
- 31.2 Certification of Kurt R. Stevenson, Principal Financial and Accounting Officer required by Rule 13a - 14(a).

34.

Edgar Filing: UNIONBANCORP INC - Form 10-Q

32.1(1) Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, from the Company's Interim President and Principal Executive Officer.

32.2(1) Certification Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, from the Company's Principal Financial and Accounting Officer.

-----

(1) This certification is not "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.

35.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

UNIONBANCORP, INC.

Date: November 13, 2006

By: /s/ KURT R. STEVENSON

-----  
Kurt R. Stevenson  
Interim President

Date: November 13, 2006

By: /s/ KURT R. STEVENSON

-----  
Kurt R. Stevenson  
Chief Financial Officer

36.