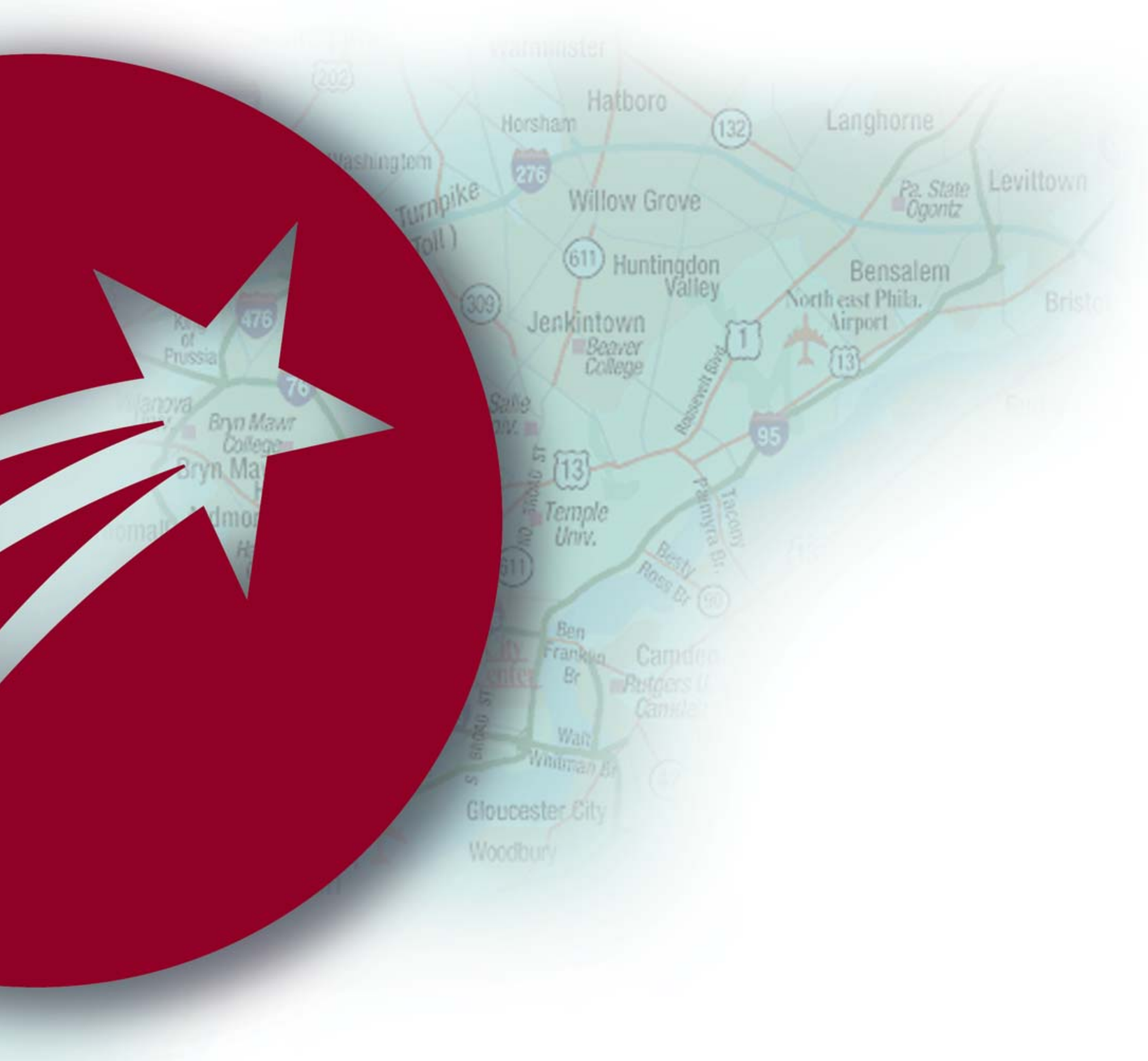
Allegiance Bank
OF NORTH AMERICA

ANNUAL REPORT 2005



President's Letter

March 24, 2006

Dear Shareholder:

Many thanks to all of our shareholders for your continued support of the growth and vitality of Allegiance Bank of North America – Your Bank.

2005 was a banner year for Allegiance Bank reflecting net income of $1,017,000 versus $474,000 in 2004 – a 115% increase from year to year. It should be noted that while we had start-up loss carry-forwards to offset income taxes in 2004 & 2005, we will begin to pay income taxes in 2006. Earnings per share increased to $0.22 in 2005 from $0.20 in 2004. This increase took place even though we more then doubled the number of shares outstanding in early 2005.

Total Assets at year end 2005 were $122.6 million versus $87.6 million at year end 2004. Stockholders' Equity grew to $22.8 million in 2005 from $9.2 million in 2004 as a result of the 2005 net income and the $12.7 million stock offering at the beginning of 2005.

On a more somber note, we have to report to you that our Founder, Chairman Emeritus and the guiding light for the formation of Allegiance Bank, Larry Isdaner, died December 26, 2005 at his home in Bala Cynwyd.

Earlier in 2005, Larry was elected Chairman Emeritus, Ed Landis was elected Chairman, and Bob Kramer replaced Ed as Vice Chairman.

May we once again thank you for your support.

Sincerely,

C. Andrew Cook

C. Andrew Cook
President/CEO

Looking Ahead

We believe that 2006 should be an exciting and pivotal year for your Bank. We are planning to open three more branches this year to complement our existing offices in Bala Cynwyd and Old City Philadelphia. These branches will be in King of Prussia, Worcester and Berwyn.

Allegiance Bank is making a transition from a commercial bank focused primarily on meeting the needs of the small business community to an institution with much greater emphasis on branch and retail banking; a step we feel is necessary to not only procure lower-cost deposits to fund our lending activity, but to add franchise value for our shareholders.

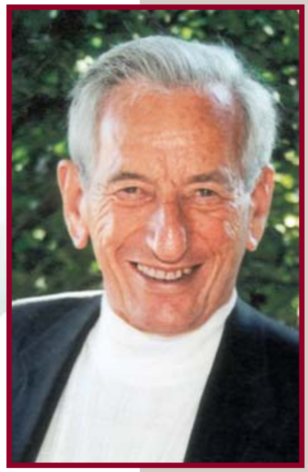
Branching is only one part of this transition. Working with experts in branding, we have developed our brand for Allegiance Bank centered around the concept of acting as “champions” for our clients. The brand will be developed over time in our advertising, community affairs, branch style and in everything we do. In fact, we are planning a proactive campaign for name recognition through advertising and public relations now.

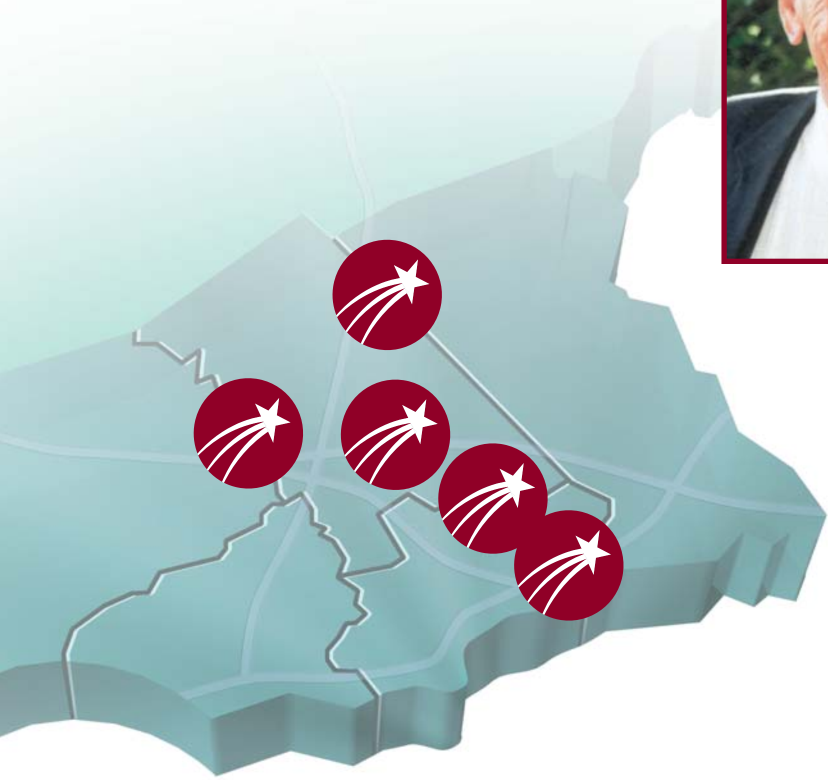
With the addition of new branch sites we expect to do more business through one of our subsidiaries, Allegiance Financial Services, Inc., which provides non-deposit products such as insurance, retirement plans, financial planning, etc. We recently joined forces with a local organization to help us provide these vital services to our clients.

While all of this is truly exciting, and is necessary to grow your Bank in an intelligent manner, please be aware that the cost for developing a branch system will impede profit growth for a while until each branch is able to stand on its own.

Overall, we are very enthusiastic about our plans for your Bank. We appreciate your encouragement and support in this effort.

Isdaner Leaves Legacy of Solid Future for Allegiance Bank





Allegiance Bank, which Larry Isdaner founded and chaired until recently, is well positioned for success in 2006 and beyond because of his stewardship. The Allegiance Bank family is very sad that he will not be on hand to share in it further. Larry Isdaner passed away on December 26, 2005 after a half-century career in financial services, most of it centered in the Philadelphia market.

Larry founded Allegiance in 1999 to fill a void for small-to-midsized business owners who were finding themselves neglected amid all the mergers and consolidations in the financial services industry. He helped shape the strong customer service philosophy of the Bank. He advised the design of branches that would be warmer, friendlier places to do business. And has always abided by the credo that the customer comes first.

The Allegiance Bank family will miss Larry deeply, and we will be forever grateful for the legacy he has left to us and to the financial services industry.

Consolidated Balance Sheets

ALLEGIANCE BANK OF NORTH AMERICA

	December 31, 2005	December 31, 2004
	(In Thousands, Except Share Data)	
Assets		
Cash and due from banks	**$ 1,142**	$ 1,097
Interest-bearing demand deposits	**974**	524
Federal funds sold	**284**	1,142
Cash and Cash Equivalents	**2,400**	2,763
Securities available for sale	**20,337**	2,586
Loans receivable, net of allowance for loan losses 2005 $1,464; 2004 $931	**96,901**	80,273
Bank premises and equipment, net	**1,220**	627
Federal Home Loan Bank stock	**887**	669
Accrued interest receivable	**608**	343
Other assets	**243**	348
Total Assets	**$ 122,596**	$ 87,609
Liabilities and Stockholders' Equity		
Liabilities		
Deposits:		
Demand, non-interest bearing	**$ 5,362**	$ 4,439
Demand, interest bearing	**27,696**	24,868
Savings	**903**	786
Time, $100,000 and over	**29,303**	23,873
Time, other	**20,381**	14,552
Total Deposits	**83,645**	68,518
Short-term debt	**14,307**	8,250
Long-term debt	**719**	736
Accrued interest payable	**92**	115
Other liabilities	**1,005**	791
Total Liabilities	**99,768**	78,410
Stockholders' Equity		
Preferred stock, par value $1.00 per share; authorized 2,000,000 shares; issued none	**–**	–
Common stock, par value $1.00 per share; authorized 20,000,000 shares; issued and outstanding 2005 4,780,758 shares; 2004 2,362,302 shares	**4,781**	2,362
Surplus	**19,595**	9,304
Accumulated deficit	**(1,438)**	(2,455)
Accumulated other comprehensive loss	**(110)**	(12)
Total Stockholders' Equity	**22,828**	9,199
Total Liabilities and Stockholders' Equity	**$ 122,596**	$ 87,609

See notes to consolidated financial statements.

Consolidated Statements of Income

ALLEGIANCE BANK OF NORTH AMERICA

	Years Ended December 31,		
	2005	2004	2003
	(In Thousands, Except Per Share Amounts)		
Interest Income			
Loans receivable, including fees	**$ 7,579**	$ 5,222	$ 4,135
Securities, taxable	**282**	86	75
Other	**121**	8	28
Total Interest Income	**7,982**	5,316	4,238
Interest Expense			
Deposits	**2,275**	1,474	1,341
Short-term debt	**52**	66	5
Long-term debt	**41**	41	41
Total Interest Expense	**2,368**	1,581	1,387
Net Interest Income	**5,614**	3,735	2,851
Provision for Loan Losses	**518**	529	288
Net Interest Income after Provision for Loan Losses	**5,096**	3,206	2,563
Other Income			
Customer service fees	**89**	76	67
Mortgage banking fees	**306**	68	–
Other	**29**	40	19
Total Other Income	**424**	184	86
Other Expenses			
Salaries and employee benefits	**2,520**	1,647	1,233
Occupancy	**403**	252	227
Equipment and data processing	**479**	409	364
Advertising, marketing and business development	**220**	147	77
Professional fees	**395**	211	202
Bank shares tax	**66**	56	49
Other	**420**	204	193
Total Other Expenses	**4,503**	2,926	2,345
Income before Minority Interest	**1,017**	464	304
Minority Interest in Net Loss of Subsidiary	**–**	10	–
Net Income	**$ 1,017**	$ 474	$ 304
Earnings Per Share			
Basic	**$0.22**	$0.20	$0.16
Diluted	**$0.22**	$0.20	$0.16

See notes to consolidated financial statements.

Consolidated Statements of Stockholders' Equity

ALLEGIANCE BANK OF NORTH AMERICA

Years Ended December 31, 2005, 2004 and 2003

	Common Stock	Surplus	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
			(Dollars In Thousands)		
Balance - December 31, 2002	$ 1,472	$ 7,594	$ (3,233)	$ 33	$ 5,866
Comprehensive income:					
Net income	–	–	304	–	304
Net change in unrealized losses on securities available for sale	–	–	–	(16)	(16)
Total Comprehensive Income					288
Sale of 496,350 shares of common stock	497	2,103	–	–	2,600
Balance - December 31, 2003	1,969	9,697	(2,929)	17	8,754
Comprehensive income:					
Net income	–	–	474	–	474
Net change in unrealized losses on securities available for sale	–	–	–	(29)	(29)
Total Comprehensive Income					445
20% stock dividend, 393,713 shares	393	(393)	–	–	–
Balance - December 31, 2004	2,362	9,304	(2,455)	(12)	9,199
Comprehensive income:					
Net income	–	–	**1,017**	–	**1,017**
Net change in unrealized losses on securities available for sale	–	–	–	**(98)**	**(98)**
Total Comprehensive Income					919
Exercise of 3,456 stock options	**4**	**13**	–	–	**17**
Sale of 2,415,000 shares of common stock	**2,415**	**10,278**	–	–	**12,693**
Balance - December 31, 2005	**$ 4,781**	**$19,595**	**$ (1,438)**	**$ (110)**	**$ 22,828**

See notes to consolidated financial statements.

Consolidated Statements of Cash Flows

ALLEGIANCE BANK OF NORTH AMERICA

	Years Ended December 31, 2005	2004	2003
	(In Thousands)		
Cash Flows from Operating Activities			
Net income	**$ 1,017**	$ 474	$ 304
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan losses	**518**	529	288
Provision for depreciation and amortization	**250**	205	194
Net amortization of securities premiums	**1**	9	7
Amortization of purchased loan premiums	**–**	8	27
Deferred income taxes	**(40)**	–	–
Increase in accrued interest receivable	**(265)**	(23)	(45)
(Increase) decrease in other assets	**5**	(62)	13
Increase (decrease) in accrued interest payable	**(23)**	20	2
Increase in other liabilities	**214**	239	201
Net Cash Provided Operating Activities	**1,677**	1,399	991
Cash Flows from Investing Activities			
Decrease in interest-bearing deposit	**–**	–	88
Purchases of securities available for sale	**(27,553)**	(3,000)	(13,848)
Proceeds from maturities of and principal repayments on securities available for sale	**9,703**	14,319	1,729
Net increase in loans	**(17,146)**	(16,305)	(13,664)
Purchases of bank premises and equipment	**(843)**	(208)	(127)
Net increase in Federal Home Loan Bank stock	**(218)**	(348)	(154)
Net Cash Used in Investing Activities	**(36,057)**	(5,542)	(25,976)
Cash Flows from Financing Activities			
Net increase (decrease) in deposits	**15,127**	(4,047)	21,481
Net increase in short-term borrowings	**6,057**	8,250	–
Repayment of long-term borrowings	**(17)**	(17)	(15)
Proceeds from sale of common stock, net	**13,859**	–	2,600
Stock offering costs	**(1,026)**	(140)	–
Proceeds from exercise of stock options	**17**	–	–
Net Cash Provided by Financing Activities	**34,017**	4,046	24,066
Net Decrease in Cash and Cash Equivalents	**(363)**	(97)	(919)
Cash and Cash Equivalents - Beginning	**2,763**	2,860	3,779
Cash and Cash Equivalents - Ending	**$ 2,400**	$ 2,763	$ 2,860
Supplementary Cash Flows Information			
Interest paid	**$ 2,391**	$ 1,561	$ 1,385

See notes to consolidated financial statements.

Note 1 – Summary of Significant Accounting Policies

Organization and Nature of Operations
Allegiance Bank of North America was incorporated on December 24, 1998 under the laws of the Commonwealth of Pennsylvania and is a Pennsylvania state chartered bank. The Bank commenced operations on July 6, 1999 and is a full service bank providing personal and business lending and deposit services. As a state chartered, non-Federal Reserve member bank, the Bank is subject to regulation of the Pennsylvania Department of Banking and the Federal Deposit Insurance Corporation. The area served by the Bank is southeastern Pennsylvania.

The consolidated financial statements include the accounts of Allegiance Bank of North America and its wholly-owned subsidiary, Allegiance Financial Services, Inc., and its 51% owned subsidiary, Paramount Mortgage and Capital, LLC. Allegiance Financial Services, Inc. provides investment and insurance products and generates related fee income through a strategic alliance with the Financial Partners Program of Mass Mutual Financial Group. Paramount was formed on December 18, 2003 to broker and originate residential real estate loans and secured commercial loans. All intercompany transactions and balances have been eliminated in consolidation.

Estimates
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of the allowance for loan losses and the valuation of deferred tax assets.

Significant Group Concentrations of Credit Risk
Most of the Bank's activities are with customers located within southeastern Pennsylvania. Note 2 discusses the types of securities that the Bank invests in. Note 3 discusses the types of lending that the Bank engages in. The Bank does not have any significant loan concentrations to any one industry or customer. Although the Bank has a diversified loan portfolio, its debtors' ability to honor their contracts is influenced by the region's economy.

Presentation of Cash Flows
For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold and interest-bearing demand deposits. Generally, federal funds are purchased and sold for one day periods.

Securities
Securities classified as available for sale are those securities that the Bank intends to hold for an indefinite period of time but not necessarily to maturity. Securities available for sale are carried at fair value. Any decision to sell a security classified as available for sale would be based on various factors, including significant movement in interest rates, changes in maturity mix of the Bank's assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors. Unrealized gains and losses are reported as increases or decreases in other comprehensive income. Realized gains or losses, determined on the basis of the cost of the specific securities sold, are included in earnings. Premiums and discounts are recognized in interest income using the interest method over the terms of the securities.

Declines in the fair value of available for sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Bank to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value.

Federal law requires a member institution of the Federal Home Loan Bank system to hold stock of its district FHLB according to a predetermined formula. This restricted stock is recorded at cost.

Note 1 – Summary of Significant Accounting Policies (Continued)

Loans Receivable
Loans receivable that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Discounts and premiums on purchased loans are amortized to income using the interest method over the expected lives of the loans. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield (interest income) of the related loans. The Bank is generally amortizing these amounts over the contractual life of the loan.

The accrual of interest is discontinued when the contractual payment of principal or interest has become 90 days past due or management has serious doubts about further collectibility of principal or interest, even though the loan is currently performing. A loan may remain on accrual status if it is in the process of collection and is either guaranteed or well secured. When a loan is placed on nonaccrual status, unpaid interest credited to income in the current year is reversed and unpaid interest accrued in prior years is charged against the allowance for loan losses. Interest received on nonaccrual loans generally is either applied against principal or reported as interest income, according to management's judgment as to the collectibility of principal. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time and the ultimate collectibility of the total contractual principal and interest is no longer in doubt.

Allowance for Loan Losses
The allowance for loan losses is established through provisions for loan losses charged against income. Loans deemed to be uncollectible are charged against the allowance for loan losses, and subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the allowance is based on known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant factors. This evaluation is inherently subjective as it requires material estimates that may be susceptible to significant revision as more information becomes available.

The allowance consists of specific, general and unallocated components. The specific component relates to loans that are classified as either doubtful, substandard or special mention. For such loans that are also classified as impaired, an allowance is established when the discounted cash flows (or collateral value or observable market price) of the impaired loan is lower than the carrying value of that loan. The general component covers non-classified loans and is based on historical loss experience adjusted for qualitative factors. An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating specific and general losses in the portfolio.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial loans by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and home equity loans for impairment disclosures, unless such loans are subject to a restructuring agreement.

Note 1 – Summary of Significant Accounting Policies (Continued)

Transfers of Financial Assets
Transfers of financial assets, including loan participation sales, are accounted for as sales, when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Bank, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets and (3) the Bank does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Bank Premises and Equipment
Bank premises and equipment are stated at cost less accumulated depreciation. Depreciation is computed on the straight-line method over the estimated useful lives of the related assets.

Advertising Costs
The Bank follows the policy of charging the costs of advertising to expense as incurred.

Income Taxes
Deferred income taxes are provided on the liability method whereby deferred tax assets are recognized for deductible temporary differences and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and net operating loss carryforwards and their tax basis. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Off-Balance Sheet Financial Instruments
In the ordinary course of business, the Bank has entered into off-balance sheet financial instruments consisting of commitments to extend credit and letters of credit. Such financial instruments are recorded in the balance sheet when they are funded.

Earnings per Common Share
Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares included in the computations relate solely to outstanding stock options and warrants, and are determined using the treasury stock method.

Note 1 – Summary of Significant Accounting Policies (Continued)

Earnings per Common Share (Continued)

The following table shows the amounts used in computing earnings per share for the years ended December 31, 2005, 2004 and 2003 (as adjusted for the 20% stock dividend issued in 2004):

	Net Income	Weighted Average Common Shares Outstanding	Earnings Per Share
	(Dollars In Thousands, Except Per Share Amounts)		
2005:			
Basic	**$ 1,017**	**4,642,653**	**$0.22**
Dilutive effect of potential common stock, stock options	**–**	**32,134**	**–**
Diluted	**$ 1,017**	**4,674,787**	**$0.22**
2004:			
Basic	$ 474	2,362,302	$0.20
Dilutive effect of potential common stock, stock options and warrants	–	8,498	–
Diluted	$ 474	2,370,800	$0.20
2003:			
Basic	$ 304	1,915,489	$0.16
Dilutive effect of potential common stock, stock options and warrants	–	7,932	–
Diluted	$ 304	1,923,421	$0.16

Stock-Based Compensation

The Bank accounts for its stock option plan under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under the plan had an exercise price equal to the market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Bank had applied the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation," to stock-based compensation for the years ended December 31, 2005, 2004 and 2003:

	2005	2004	2003
	(In Thousands, Except Per Share Data)		
Net income, as reported	**$ 1,017**	$ 474	$ 304
Deduct total stock-based employee compensation expense determined under fair value based method for all awards	**(32)**	(21)	(28)
Pro Forma Net Income	**$ 985**	$ 453	$ 276
Basic earnings per share:			
As reported	**$0.22**	$0.20	$0.16
Pro forma	**$0.21**	$0.19	$0.14
Diluted earnings per share:			
As reported	**$0.22**	$0.20	$0.16
Pro forma	**$0.21**	$0.19	$0.14

Note 1 – Summary of Significant Accounting Policies (Continued)

Stock-Based Compensation (Continued)
The fair value of each option grant using the fair value method in 2005 and the minimum value method for 2004 and 2003 is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions for 2005, 2004 and 2003: risk-free interest rate of 4.4%, 3.3%, and 3.6%, respectively; dividend yield of 0%; expected volatility of 18%, -0-%, and -0-%, and an expected life of 7.5 years. The weighted average fair value of options granted was $1.95 per share in 2005, $0.96 per share in 2004, and $1.01 per share in 2003, as adjusted for the 20% stock dividend issued in 2004.

Comprehensive Income
Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income.

The components of other comprehensive income (loss) are as follows:

	Years Ended December 31, 2005	2004	2003
	(In Thousands)		
Unrealized holding losses on securities available for sale	**$ (98)**	$ (29)	$ (16)
Less reclassification adjustment for gains included in net income	-	-	-
Net Unrealized Losses	**$ (98)**	$ (29)	$ (16)

New Accounting Standards
In December 2004, the Financial Accounting Standards Board (FASB) issued Statement No. 123(R), "Share-Based Payment." Statement No. 123(R) replaces Statement No. 123, "Accounting for Stock-Based Compensation," and supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees." Statement No. 123(R) requires compensation costs related to share-based payment transactions to be recognized in the financial statements over the period that an employee provides service in exchange for the award. Public companies are required to adopt the new standard using a modified prospective method and may elect to restate prior periods using the modified retrospective method. Under the modified prospective method, companies are required to record compensation cost for new and modified awards over the related vesting period of such awards prospectively and record compensation cost prospectively for the unvested portion, at the date of adoption, of previously issued and outstanding awards over the remaining vesting period of such awards. No change to prior periods presented is permitted under the modified prospective method. Under the modified retrospective method, companies record compensation costs for prior periods retroactively through restatement of such period using the exact pro forma amounts disclosed in the companies' footnotes. Also, in the period of adoption and after, companies record compensation cost based on the modified prospective method. Statement No. 123(R) is effective for periods beginning after December 15, 2005. Early application of Statement No. 123(R) is encouraged, but not required.

The Bank will adopt the modified prospective method. Using the modified prospective method, the Bank will record stock-based compensation expense, net of related tax effects, of approximately $25,000 in 2006 and $17,000 in 2007 for unvested stock options outstanding at December 31, 2005. Any additional impact that the adoption of this Statement will have on our consolidated financial position and results of operations will be determined by share-based payments granted in future periods. There is no impact on cash flows.

In October 2005, the FASB issued FSP FAS 123(R)-2, "Practical Accommodation to the Application of Grant Date as Defined in FAS 123(R)" ("FSP 123(R)-2"). FSP 123(R)-2 provides guidance on the application of grant date as defined in SFAS No. 123(R). In accordance with this standard a grant date of an award exists if a) the award is a unilateral grant and b) the key terms and conditions of the award are expected to be communicated to an individual recipient within a relatively short time period from the date of approval. We will adopt this standard when we adopt SFAS No. 123(R), and it will not have a material impact on our consolidated financial position, results of operations or cash flows.

Note 1 – Summary of Significant Accounting Policies (Continued)

New Accounting Standards (Continued)
In November 2005, the FASB issued final FASB Staff Position (FSP) FAS No. 123R-3, “Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards.” The FSP provides an alternative method of calculating excess tax benefits (the APIC pool) from the method defined in FAS 123R for share-based payments. A one-time election to adopt the transition method in this FSP is available to those entities adopting FAS 123R using either the modified retrospective or modified prospective method. Up to one year from the initial adoption of FAS 123R or effective date of the FSP is provided to make this one-time election. However, until an entity makes its election, it must follow the guidance in FAS 123R. FSP 123R-3 is effective upon initial adoption of FAS 123R and will become effective for the Bank the first quarter of fiscal 2006. We are currently evaluating the potential impact of calculating the APIC pool with this alternative method and have not determined which method we will adopt, nor the expected impact on our financial position or results of operations.

In March 2004, the FASB’s Emerging Issues Task Force (EITF) reached a consensus on Issue No. 03-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.” EITF 03-1 provides guidance on other-than-temporary impairment models for marketable debt and equity securities accounted for under SFAS 115 and non-marketable equity securities accounted for under the cost method. The EITF developed a basic three-step model to evaluate whether an investment is other-than-temporarily impaired. In November 2005, the FASB approved the issuance of FASB Staff Position FAS No. 115-1 and FAS 124-1, “The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments.” The FSP addresses when an investment is considered impaired, whether the impairment is other-than-temporary and the measurement of an impairment loss. The FSP also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary. The FSP is effective for reporting periods beginning after December 15, 2005 with earlier application permitted. For the Bank, the effective date will be the year ending December 31, 2006. The adoption of this accounting principle is not expected to have a significant impact on our consolidated financial position or results of operations.

In July 2005, the FASB issued a proposed interpretation of FAS 109, “Accounting for Income Taxes,” to clarify certain aspects of accounting for uncertain tax positions, including issues related to the recognition and measurement of those tax positions. If adopted as proposed, any adjustments required to be recorded as a result of adopting the interpretation would be reflected as a cumulative effect from a change in accounting principle. We are currently in the process of determining the impact of adoption of the interpretation as proposed on our consolidated financial position or results of operations.

In June 2005, the FASB’s Emerging Issues Task Force (EITF) reached a consensus on Issue No. 05-6, “Determining the Amortization Period for Leasehold Improvements Purchased after Lease Inception or Acquired in a Business Combination” (“EITF 05-6”). This guidance requires that leasehold improvements acquired in a business combination or purchased subsequent to the inception of a lease be amortized over the shorter of the useful life of the assets or a term that includes required lease periods and renewals that are reasonably assured at the date of the business combination or purchase. This guidance is applicable only to leasehold improvements that are purchased or acquired in reporting periods beginning after June 29, 2005. The adoption of this pronouncement did not have an impact on the Bank’s consolidated financial statements.

In October 2005, the FASB issued FASB Staff Position FAS 13-1 (“FSP FAS 13-1”), which requires companies to expense rental costs associated with ground or building operating leases that are incurred during a construction period. As a result, companies that are currently capitalizing these rental costs are required to expense them beginning in its first reporting period beginning after December 15, 2005. FSP FAS 13-1 is effective for our Bank as of the year ending December 31, 2006. We evaluated the provisions of FSP FAS 131 and do not believe that its adoption will have a material impact on our Bank’s consolidated financial condition or results of operations.

Note 1 – Summary of Significant Accounting Policies (Continued)

New Accounting Standards (Continued)
In May 2005, FASB issued SFAS 154, “Accounting Changes and Error Corrections.” The Statement requires retroactive application of a voluntary change in accounting principle to prior period financial statements unless it is impracticable. Statement No. 154 also requires that a change in method of depreciation, amortization, or depletion for long-lived, non-financial assets be accounted for as a change in accounting estimate that is affected by a change in accounting principle. Statement No. 154 replaces APB Opinion 20, “Accounting Changes,” and Statement No. 3, “Reporting Accounting Changes in Interim Financial Statements.” Statement No. 154 will be effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. Management currently believes that adoption of the provisions of SFAS 154 will not have a material impact on the Bank’s consolidated financial statements.

Note 2 – Securities Available for Sale

The amortized cost and approximate fair value of securities at December 31, 2005 and 2004 are summarized as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
		(In Thousands)		
December 31, 2005:				
U.S. Government agencies	**$ 14,994**	**$ –**	**$ 110**	**$ 14,884**
Mortgage-backed securities	**5,423**	**–**	**–**	**5,423**
Equity securities	**30**	**–**	**–**	**30**
	$ 20,447	**$ –**	**$ 110**	**$ 20,337**
December 31, 2004:				
U.S. Government agencies	$ 2,000	$ –	$ 14	$ 1,986
Mortgage-backed securities	568	3	1	570
Equity securities	30	–	–	30
	$ 2,598	$ 3	$ 15	$ 2,586

The amortized cost and fair value of securities as of December 31, 2005, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because the borrowers may have the right to prepay obligations with or without any penalties.

	Amortized Cost	Fair Value
	(In Thousands)	
Due in one year or less	**$ 9,993**	$ 9,958
Due after one year through five years	**5,001**	4,926
Mortgage-backed securities	**5,423**	5,423
Equity securities	**30**	30
	$ 20,447	$ 20,337

There were no sales of securities during the years ended December 31, 2005, 2004 and 2003.

Securities with a carrying value of $14,884,000 and $1,986,000 at December 31, 2005 and 2004, respectively, were pledged to secure public deposits as required or permitted by law.

Note 2 – Securities Available for Sale (Continued)

The following table shows the Bank's investments' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2005 and 2004:

	Less Than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(In Thousands)			
December 31, 2005:						
U.S. Government agencies	**$8,053**	**$ 55**	**$1,946**	**$ 55**	**$9,999**	**$110**
Total Temporarily Impaired Securities	**$8,053**	**$55**	**$1,946**	**$55**	**$9,999**	**$110**
December 31, 2004:						
U.S. Government agencies	$1,986	$ 14	$ –	$ –	$1,986	$ 14
Mortgage-backed securities	–	–	397	1	397	1
Total Temporarily Impaired Securities	$1,986	$14	$397	$ 1	$2,383	$15

In management's opinion, the unrealized losses primarily reflect changes in interest rates subsequent to the acquisition of specific securities. At December 31, 2005 and 2004, the Bank had six and three securities, respectively, in an unrealized loss position. The Bank has the intent and the ability to hold such securities until maturity or market price recovery. Management believes that the unrealized losses represent temporary impairment of the securities.

Note 3 – Loans Receivable and Allowance for Loan Losses

The composition of net loans receivable at December 31, 2005 and 2004 is as follows:

	2005	2004
	(In Thousands)	
Commercial real estate	**$ 44,477**	$ 37,915
Commercial construction	**28,798**	16,331
Commercial	**20,184**	19,826
Home equity	**5,581**	7,580
Consumer	**37**	102
Total Loans	**99,077**	81,754
Unearned net loan origination fees	**(712)**	(550)
Allowance for loan losses	**(1,464)**	(931)
Net Loans	**$ 96,901**	$ 80,273

Note 3 – Loans Receivable and Allowance for Loan Losses (Continued)

The changes in the allowance for loan losses for the years ended December 31, 2005, 2004, and 2003 are as follows:

	2005	2004	2003
		(In Thousands)	
Balance, beginning	**$ 931**	$ 796	$ 505
Provision for loan losses	**518**	529	288
Loans charged off	**–**	(404)	–
Recoveries	**15**	10	3
Balance, ending	**$ 1,464**	$ 931	$ 796

There were no recorded investments in impaired loans requiring an allowance for loan losses as of December 31, 2005 or 2004. The recorded investment in impaired loans not requiring an allowance for loan losses at December 31, 2005 and 2004 was $425,000 and $165,000, respectively. For the years ended December 31, 2005, 2004, and 2003, the average recorded investment in impaired loans was $151,000, $136,000, and $43,000 respectively, and the interest income recognized on these impaired loans using the cash basis method was $17,000, $33,000, and $-0-, respectively. Nonaccrual loans at December 31, 2005 and 2004 were $425,000 and $165,000, respectively. In addition, the Bank had no loans greater than 90 days delinquent and still accruing interest as of December 31, 2005 and 2004.

Note 4 – Bank Premises and Equipment

The components of bank premises and equipment at December 31, 2005 and 2004 are as follows:

	2005	2004
	(In Thousands)	
Leasehold improvements	**$ 807**	$ 486
Furniture, fixtures and equipment	**500**	222
Computer equipment and data processing software	**919**	856
Automobiles	**54**	50
Construction in progress	**139**	109
	2,419	1,723
Accumulated depreciation	**(1,199)**	(1,096)
	$ 1,220	$ 627

Depreciation expense for the years ended December 31, 2005, 2004 and 2003 amounted to $250,000, $205,000, and $194,000, respectively.

In 2005, the Bank entered into leases for three new branches to open in 2006. The construction in progress above relates to leasehold improvements, furniture, fixtures, and equipment for the new facilities. The Bank also has outstanding commitments for premises and equipment of approximately $84,000 as of December 31, 2005 related to these branches.

Note 5 – Deposits

Included in time deposits at December 31, 2005 and 2004 are brokered deposits of $20,432,000 and $16,004,000, respectively.

At December 31, 2005, the scheduled maturities of time deposits are as follows (in thousands):

2006	**$ 30,332**
2007	**11,723**
2008	**686**
2009	**5,115**
2010	**1,828**
	$ 49,684

Note 6 – Borrowings

The Bank has a line of credit commitment from the Federal Home Loan Bank for borrowings up to $20,000,000 expiring January 24, 2006. Borrowings under this line of credit at December 31, 2005 were $14,307,000 with interest at 4.26%. The Bank had borrowings of $8,250,000 with interest at 2.24% as of December 31, 2004.

The Bank also has a line of credit commitment with Atlantic Central Bankers Bank for unsecured borrowings up to $1,000,000, which is renewable annually. There were no borrowings under this line of credit at December 31, 2005 and 2004.

Long-term debt at December 31, 2005 and 2004 consisted of a fixed rate note with the Federal Home Loan Bank, due in monthly installments with interest at 5.45% through May 2027.

Maturities of long-term debt in years subsequent to December 31, 2005 are as follows (in thousands):

2006	**$ 18**
2007	**19**
2008	**20**
2009	**21**
2010	**23**
Thereafter	**618**
	$ 719

Advances from the Federal Home Loan Bank are secured by certain qualifying assets of the Bank. The Bank has a maximum borrowing capacity with the Federal Home Loan Bank of approximately $66,430,000 at December 31, 2005, of which $15,026,000 was outstanding.

Note 7 – Lease Commitments and Total Rental Expense

The Bank leases the premises for its main banking office under a seven-year operating lease agreement expiring July 2010. The Bank has the option to extend the lease agreement for one additional five year period. The Bank may be required to pay additional rent for its portion of certain increases in operating costs over the base year costs, as determined by the landlord.

The Bank also leases the premises for a new branch that opened in 2005 under a ten-year operating lease agreement expiring October 2014. The Bank has the option to extend this lease agreement for two additional five-year periods.

Note 7 – Lease Commitments and Total Rental Expense (Continued)

The Bank also leases the premises for two new branches scheduled to open in 2006. The first lease is under a five-year operating lease agreement expiring August 2010. The Bank has the option to extend this lease agreement for three additional five-year periods. The second lease is under a ten-year operating lease agreement expiring November 2015. The Bank has the option to extend this lease agreement for three additional five-year periods.

The Bank is responsible for paying all real estate taxes and utilities pertaining to these premises.

Future minimum lease payments by year are as follows (in thousands):

2006	$ **378**
2007	**363**
2008	**353**
2009	**351**
2010	**273**
Thereafter	**754**
	$ **2,472**

Total rent expense was $290,000, $161,000, and $139,000 for the years ended December 31, 2005, 2004 and 2003, respectively.

Note 8 – Employment Agreement

The Bank entered into a three year employment agreement in July 1999 with its chief executive officer which includes minimum annual salary commitments and change of control provisions. Upon resignation after a change in the control of the Bank, as defined in the agreement, the individual will receive monetary compensation in the amount set forth in the agreement. The term of the agreement shall be extended by one calendar day for each expired calendar day, maintaining a three year term unless written notice electing not to renew is given by the Bank or individual.

Note 9 – Employee Benefit Plan

The Bank has a 401(k) profit sharing plan for its employees. Employees may contribute an elective deferral percentage of their salary to the Plan each year, subject to limitations which are set by law. The Bank provides a matching contribution equal to 50% of the amount the employee elects to defer limited to 6% of each employees annual compensation. The Bank may also make discretionary contributions. The employer contribution charged to expense for the years ended December 31, 2005, 2004 and 2003 was $38,000, $29,000, and $23,000, respectively.

Note 10 – Stockholders' Equity

On February 2, 2005, the Bank completed its offering of 2,415,000 shares of common stock at a price of $5.75 per share. The underwriter's option to acquire 315,000 shares to cover over-allotments was fully exercised, and is included in the 2,415,000 shares. Proceeds of the offering were $12,693,000, net of offering costs of $1,193,000. As of December 31, 2004, the Bank had incurred offering costs of $140,000, which are included in other assets on the balance sheet.

On June 18, 2003, the Bank commenced a sale of its common stock at a price of $5.25 per share to existing stockholders and to a limited number of accredited investors pursuant to a Stock Purchase and Voting Agreement dated June 6, 2003 (the "Investor Group Agreement"). Shares were offered to other accredited investors at $6.00 per share until the offering expiration date of December 31, 2003. Under this offering, 483,350 shares were sold in 2003 resulting in net proceeds of $2,535,000 after stock issuance costs of $9,500.

Under a 2002 offering which expired in February 2003, the Bank sold 13,000 shares of common stock in 2003 resulting in net proceeds of $65,000.

Note 11 – Stock Option Plans

The Bank has a 2000 Stock Option Plan to provide for the granting of stock options to employees, outside directors, certain consultants and organizers of the Bank. Under the Plan, the Board may grant "incentive stock options" and "non-qualified stock options", provided that only employees of the Bank will be eligible to receive incentive stock options. A total of 293,760 shares of common stock have been reserved for issuance under the Plan, as adjusted for the 20% stock dividend issued in 2004. As of December 31, 2005, there are 19,289 options available for grant under this Plan.

On May 21, 2003, the Bank adopted the 2003 Stock Option Plan to provide for the granting of stock options to employees and outside directors of the Bank. Under the plan, the Board may grant "incentive stock options" and "non-qualified stock options" provided that only employees of the Bank will be eligible to receive incentive stock options. A total of 120,000 shares have been reserved for issuance under the Plan, including 84,000 shares specifically reserved for grants to employees, as adjusted for the 20% stock dividend in 2004. As of December 31, 2005, there are 58,250 options available for grant under this Plan.

In September 2005, the Board of Directors approved the 2005 Stock Option Plan to provide for the granting of stock options to employees and outside directors of the Bank. Under the Plan, the Board may grant "incentive stock options" and "non-qualified stock options" provided that only employees of the Bank will be eligible to receive incentive stock options. A total of 700,000 shares have been reserved for the issuance under the Plan. The 2005 Stock Option Plan is pending shareholder approval in 2006.

The option price of options granted under the Plans cannot be less than the fair market value of the common stock at the date of grant. The vesting of employee stock options under the Plans is at the discretion of the committee awarding the options.

The following summarizes changes in stock options outstanding for the years ended December 31, 2005, 2004 and 2003 (as adjusted for 20% stock dividend in 2004).

	Number of Options	Weighted Average Exercise Price
Outstanding, December 31, 2002	267,624	$ 5.16
Granted	23,220	4.30
Forfeited	(14,640)	4.10
Outstanding, December 31, 2003	276,204	5.14
Granted	37,200	4.38
Forfeited	(4,440)	4.37
Outstanding, December 31, 2004	308,964	5.06
Granted	**31,750**	**5.75**
Exercised	**(3,456)**	**4.79**
Forfeited	**(4,493)**	**4.28**
Outstanding, December 31, 2005	**332,765**	**$ 5.14**
Exercisable, December 31, 2005	**274,475**	**$ 5.14**

The weighted-average remaining contractual life of the above options is approximately 5.0 years.

Note 11 – Stock Option Plans (Continued)

The following table summarizes information about stock options outstanding at December 31, 2005:

Range of Exercise Price	Weighted Average Exercised Price	Number Outstanding	Weighted Average Remaining Contractual Life	Number Exercisable
$3.34 to 3.93	$3.59	44,553	5.5	44,553
4.30 to 4.79	4.56	94,894	6.1	68,354
5.75 to 5.79	5.78	193,318	5.0	161,568
		332,765		274,475

In September 2005, the Board of Directors approved the granting of 60,000 stock options to outside directors of the Bank under the 2005 Stock Option Plan. These options will be issued and deemed granted upon shareholder approval of the Plan.

Note 12 – Federal Income Taxes

The components of income tax expense for the years ended December 31, 2005, 2004, and 2003 are as follows:

	2005	2004	2003
		(In Thousands)	
Current	**$ 598**	$ 191	$ 212
Deferred	**(40)**	–	–
Benefit from the utilization of net operating loss carryforwards	**(558)**	(191)	(212)
	$ –	$ –	$ –

The components of the net deferred tax asset at December 31, 2005 and 2004 are as follows:

	2005	2004
	(In Thousands)	
Deferred tax assets:		
Allowance for loan losses	**$ 438**	$ 292
Net operating loss carryforwards	**47**	605
AMT credit carryforwards	**50**	10
Bank premises and equipment	**22**	-
Total Deferred Tax Assets	**557**	907
Valuation allowance	**(383)**	(774)
Total Deferred Tax Assets, Net of Valuation Allowance	**174**	133
Deferred tax liabilities:		
Bank premises and equipment	–	(1)
Cash basis conversion	**(118)**	(116)
Other	**(16)**	(16)
Total Deferred Tax Liabilities	**(134)**	(133)
Net Deferred Tax Asset	**$ 40**	$ -

The Bank has net operating loss carryforwards available for federal income tax purposes of approximately $109,000 expiring in the years 2019 through 2022.

Note 13 – Transactions with Executive Officers, Directors and Principal Stockholders

The Bank has had, and may be expected to have in the future, banking transactions in the ordinary course of business with its executive officers, directors, principal stockholders, their immediate families and affiliated companies (commonly referred to as related parties), on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others. At December 31, 2005 and 2004, these persons were indebted to the Bank for loans totaling $874,000 and $665,000, respectively. During the year ended December 31, 2005, $562,000 of new loans were made and repayments totaled $353,000. Deposits of related parties totaled $1,170,000 and $2,970,000 at December 31, 2005 and 2004, respectively.

Note 14 – Financial Instruments with Off-Balance Sheet Risk

The Bank is a party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and letters of credit. Such commitments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the balance sheet.

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

A summary of the Bank's financial instrument commitments at December 31, 2005 and 2004 is as follows:

	2005	2004
	(In Thousands)	
Commitments to grant loans	**$ 6,483**	$ 1,383
Unfunded commitments under lines of credit	**27,622**	24,806
Outstanding letters of credit	**501**	96

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation. Collateral held varies but may include personal or commercial real estate, accounts receivable, inventory and equipment.

Outstanding letters of credit written are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The majority of these standby letters of credit expire within the next twelve months. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank requires collateral supporting these letters of credit as deemed necessary. Management believes that the proceeds through liquidation of such collateral would be sufficient to cover the maximum potential amount of future payments required under the corresponding guarantees. The amount of the liability as of December 31, 2005 and 2004 for guarantees under standby letters of credit is not material.

Note 15 – Regulatory Matters

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets, and of Tier 1 capital to average assets. Management believes, as of December 31, 2005 and 2004, that the Bank meets all capital adequacy requirements to which it is subject.

As of December 31, 2005, the most recent notification from the Federal Deposit Insurance Corporation categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank's category.

The Bank's actual capital amounts and ratios at December 31, 2005 and 2004 are presented below:

	Actual		**For Capital Adequacy Purposes**		**To be Well Capitalized under Prompt Corrective Action Provisions**	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
	(Dollar Amounts in Thousands)					
As of December 31, 2005:						
Total capital (to risk-weighted assets)	**$ 24,029**	**27.65%**	**$ ≥6,952**	**≥8.00%**	**$ ≥8,690**	**≥ 10.00%**
Tier 1 capital (to risk-weighted assets)	**22,938**	**26.40**	**≥3,476**	**≥4.00**	**≥5,214**	**≥ 6.00**
Tier 1 capital (to average assets)	**22,938**	**20.43**	**≥4,492**	**≥4.00**	**≥5,614**	**≥ 5.00**
As of December 31, 2004:						
Total capital (to risk-weighted assets)	$ 10,110	14.07%	$ ≥5,748	≥8.00%	$ ≥7,185	≥ 10.00%
Tier 1 capital (to risk-weighted assets)	9,211	12.82	≥2,874	≥4.00	≥4,311	≥ 6.00
Tier 1 capital (to average assets)	9,211	11.18	≥3,296	≥4.00	≥4,120	≥ 5.00

The Bank is subject to certain restrictions on the amount of dividends that it may declare due to regulatory considerations. The Pennsylvania Banking Code provides that cash dividends may be declared and paid only out of accumulated net earnings.

Note 16 – Formation of Mortgage Company

On December 18, 2003, the Bank entered into an operating agreement with Paramount Capital Mortgage Corp. to form Paramount Mortgage and Capital, LLC (the "Company"). The Company was formed primarily to broker or originate residential real estate loans and secured commercial loans. Residential mortgage loans are generally funded by or sold to third parties to generate mortgage banking income. Secured commercial loans are held by the Company and funded by loans to the Company from the Bank. Operations of the Company began in 2004. The Bank contributed $10,200 in capital to the Company in 2004 for a 51% ownership interest.

Note 17 – Fair Value of Financial Instruments

Management uses its best judgment in estimating the fair value of the Bank's financial instruments; however, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts the Bank could have realized in a sales transaction on the dates indicated. The estimated fair value amounts have been measured as of their respective year-ends, and have not been re-evaluated or updated for purposes of these financial statements subsequent to those respective dates. As such, the estimated fair values of these financial instruments subsequent to the respective reporting dates may be different than the amounts reported at each year-end.

The following information should not be interpreted as an estimate of the fair value of the entire Bank since a fair value calculation is only provided for a limited portion of the Bank's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Bank's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair value of the Bank's financial instruments at December 31, 2005:

Note 17 – Fair Value of Financial Instruments (Continued)

Cash and Cash Equivalents
The carrying amounts for cash and cash equivalents approximate fair value.

Securities
The fair values for securities are based on quoted market prices or dealer prices, if available. If quoted market prices or dealers prices are not available, fair value is estimated using quoted market prices or dealer prices for similar securities.

Loans
The fair value of loans is estimated by discounting the future cash flows, using the current rates at which similar loans with similar remaining maturities would be made to borrowers with similar credit ratings.

Federal Home Loan Bank Stock
The Federal Home Loan Bank stock is restricted; accordingly, its carrying amount approximates its fair value.

Deposits
For demand and savings accounts, fair value is the carrying amount reported in the consolidated financial statements. For fixed-maturity certificates of deposit, fair value is estimated by discounting the future cash flows, using the rates currently offered for deposits of similar remaining maturities.

Short-Term and Long-Term Debt
The fair values of these borrowings are estimated by discounting future cash flows, using rates currently available on borrowings with similar remaining maturities.

Accrued Interest Receivable and Accrued Interest Payable
The carrying amounts of accrued interest receivable and payable approximate fair value.

Off-Balance Sheet Instruments
The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of guarantees and letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

The estimated fair values of the Bank's financial instruments at December 31, 2005 were as follows:

	Carrying Amount	Fair Value
	(In Thousands)	
Financial assets:		
Cash and cash equivalents	$ 2,400	$ 2,400
Securities available for sale	20,337	20,337
Loans receivable, net	96,901	96,264
Federal Home Loan Bank stock	887	887
Accrued interest receivable	608	608
Financial liabilities:		
Deposits	83,645	83,517
Short-term debt	14,307	14,307
Long-term debt	719	693
Accrued interest payable	92	92
Off-balance sheet financial instruments:		
Commitments to extend credit	–	–
Outstanding letters of credit	–	–

Independant Auditor's Report

bmc

To the Board of Directors
Allegiance Bank of North America
Bala Cynwyd, Pennsylvania

We have audited the accompanying consolidated balance sheets of Allegiance Bank of North America and its subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2005. These consolidated financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Allegiance Bank of North America and its subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America.

Beard Miller Company LLP

Beard Miller Company LLP
Allentown, Pennsylvania
January 13, 2006

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OF NORTH AMERICA

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