

Home City Financial Corporation

Accountants' Report and Consolidated Financial Statements

December 31, 2005 and 2004

Home City Financial Corporation
December 31, 2005 and 2004

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Independent Accountants' Report

Board of Directors
Home City Financial Corporation
Springfield, Ohio

Cincinnati, Ohio

Home City Financial Corporation
Consolidated Balance Sheets
December 31, 2005 and 2004
(Dollars in thousands)

Assets

	2005	2004
Cash and due from banks	\$ 2,397	\$ 859
Interest-bearing demand deposits	4,006	6,529
Federal funds sold	443	2,207
Cash and cash equivalents	6,846	9,595
Available-for-sale securities	5,261	6,432
Loans, net of allowance for loan losses of \$1,377 and \$760 at December 31, 2005 and 2004	127,409	130,067
Premises and equipment	3,398	3,602
Federal Home Loan Bank stock	2,480	2,360
Interest receivable	559	544
Cash surrender value of life insurance	3,197	3,067
Other	403	557
Total assets	\$ 149,553	\$ 156,224

Liabilities and Shareholders' Equity

Liabilities

Deposits		
Demand	\$ 5,763	\$ 5,235
Savings, NOW and money market	32,980	51,173
Time	59,712	50,796
Total deposits	98,455	107,204
Federal Home Loan Bank advances	36,337	35,120
Interest payable and other liabilities	1,355	1,165
Total liabilities	136,147	143,489

Shareholders' Equity

Preferred stock, no par value, authorized 1,000,000 shares; none issued		
Common stock, no par value; authorized 5,000,000 shares; issued – 981,913 shares		
Additional paid-in capital	6,366	6,325
Retained earnings	9,337	8,868
Unearned recognition and retention plan (RRP) shares	(41)	(69)
Unearned employee stock ownership plan (ESOP) shares	(111)	(221)
Accumulated other comprehensive loss	(155)	(178)
Treasury stock, at cost, 146,223 shares	(1,990)	(1,990)
Total shareholders' equity	13,406	12,735
Total liabilities and shareholders' equity	\$ 149,553	\$ 156,224

Home City Financial Corporation
Consolidated Statements of Income
Years Ended December 31, 2005 and 2004
(Dollars in thousands, except per share amounts)

	2005	2004
Interest and Dividend Income		
Loans	\$ 8,725	\$ 8,426
Securities	103	178
Federal funds sold	18	47
Dividends on Federal Home Loan Bank stock	120	95
Deposits with financial institutions	145	26
Total interest and dividend income	9,111	8,772
Interest Expense		
Deposits	2,470	2,435
Borrowings	1,937	1,935
Total interest expense	4,407	4,370
Net Interest Income	4,704	4,402
Provision for Loan Losses	705	200
Net Interest Income After Provision for Loan Losses	3,999	4,202
Noninterest Income		
Service charges on deposits	41	39
Net realized gains on sales of available-for-sale securities	0	6
Gain on redemption of Intrieve Incorporated stock	345	0
Life insurance	162	142
Other	87	52
Total noninterest income	635	239
Noninterest Expense		
Salaries and employee benefits	1,788	1,868
Net occupancy expense	267	282
Equipment expense	215	222
Data processing fees	244	232
Professional fees	344	252
Franchise taxes	162	150
Other	396	446
Total noninterest expense	3,416	3,452

	<u>2005</u>	<u>2004</u>
Income Before Income Tax	\$ 1,218	\$ 989
Provision for Income Taxes	<u>381</u>	<u>307</u>
Net Income	\$ <u>837</u>	\$ <u>682</u>
Earnings Per Share		
Basic	\$ 1.02	\$ 0.86
Diluted	\$ 1.01	\$ 0.84

Home City Financial Corporation
Consolidated Statements of Shareholders' Equity
Years Ended December 31, 2005 and 2004
(Dollars in thousands)

	<u>Shares</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Unearned Compensation</u>	<u>Unearned ESOP Shares</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Treasury Shares</u>	<u>Total</u>
Balance, January 1, 2004	962,200	\$ 6,130	\$ 8,549	\$ (185)	\$ (229)	\$ (92)	\$ (2,266)	\$ 11,907
Comprehensive income								
Net income			682					682
Change in unrealized gain (loss) on securities available for sale, net of reclassification adjustment and tax effect						(86)		<u>(86)</u>
Total comprehensive income								<u>596</u>
Purchase of treasury shares (24,420)							(411)	(411)
Stock options exercised:								
From treasury (45,997)		(149)					687	538
New issue	19,713	231						231
Dividends on common stock, \$.44 per share			(363)					(363)
Amortization of unearned compensation expense		(101)		116				15
ESOP shares earned		<u>214</u>			<u>8</u>			<u>222</u>
Balance, December 31, 2004	981,913	6,325	8,868	(69)	(221)	(178)	(1,990)	12,735
Comprehensive income								
Net income			837					837
Change in unrealized gain (loss) on securities available for sale, net of reclassification adjustment and tax effect						23		<u>23</u>
Total comprehensive income								<u>860</u>
Dividends on common stock, \$.44 per share			(368)					(368)
Amortization of unearned compensation expense				28				28
ESOP shares earned		<u>41</u>			<u>110</u>			<u>151</u>
Balance, December 31, 2005	<u>981,913</u>	<u>\$ 6,366</u>	<u>\$ 9,337</u>	<u>\$ (41)</u>	<u>\$ (111)</u>	<u>\$ (155)</u>	<u>\$ (1,990)</u>	<u>\$ 13,406</u>

Home City Financial Corporation
Consolidated Statements of Cash Flows
Years Ended December 31, 2005 and 2004
(Dollars in thousands)

	2005	2004
Operating Activities		
Net income	\$ 837	\$ 682
Items not requiring (providing) cash		
Depreciation and amortization	231	237
Provision for loan losses	705	200
Amortization of premiums and discounts on securities	28	4
Deferred income taxes	(214)	95
Increase in cash surrender balance of life insurance	(130)	(115)
Employee Stock Ownership Plan compensation expense	151	222
Recognition and Retention Plan compensation expense	28	15
Net realized gains on available-for-sale securities	0	(6)
Gain on redemption of Intrieve Incorporated stock	(345)	0
Gain on sale of real estate owned	(73)	(58)
FHLB stock dividends	(120)	(95)
Proceeds from sale of loans held for sale	2,282	0
Originations of loans held for sale	(2,234)	0
Gain on sale of loans	(48)	0
Changes in		
Interest receivable	(15)	34
Other assets	379	(491)
Interest payable and other liabilities	399	(51)
Net cash provided by operating activities	<u>1,861</u>	<u>673</u>
Investing Activities		
Purchases of available-for-sale securities	(17,985)	(9,968)
Proceeds from maturities of available-for-sale securities	19,151	7,986
Proceeds from redemption of Intrieve Incorporated stock	360	0
Proceeds from the sales of available-for-sale securities	0	555
Net change in loans	2,000	(3,755)
Purchase of premises and equipment	(27)	(27)
Net cash provided by (used in) investing activities	<u>3,499</u>	<u>(5,209)</u>

	<u>2005</u>	<u>2004</u>
Financing Activities		
Net increase (decrease) in demand deposits, money market, NOW and savings accounts	\$ (17,665)	\$ 3,701
Net increase (decrease) in certificates of deposit	8,916	(419)
Proceeds from Federal Home Loan Bank advances	10,800	4,500
Repayment of Federal Home Loan Bank advances	(9,583)	(4,144)
Proceeds from stock options exercised	0	769
Dividends paid	(368)	(363)
Purchase of Treasury Stock	0	(411)
Net increases (decrease) in advances from borrowers for taxes and insurance	<u>(209)</u>	<u>25</u>
Net cash provided by (used in) financing activities	<u>(8,109)</u>	<u>3,658</u>
Decrease in Cash and Cash Equivalents	(2,749)	(878)
Cash and Cash Equivalents, Beginning of Year	<u>9,595</u>	<u>10,473</u>
Cash and Cash Equivalents, End of Year	<u>\$ 6,846</u>	<u>\$ 9,595</u>
Supplemental Cash Flows Information		
Interest paid	\$ 4,394	\$ 4,371
Income taxes paid (net of refunds)	\$ 590	\$ 441

Home City Financial Corporation
Notes to Consolidated Financial Statements
December 31, 2005 and 2004
(Table Dollar Amounts in Thousands)

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Home City Financial Corporation (“Company”) is a thrift holding company whose principal activity is the ownership and management of its wholly-owned subsidiary, Home City Federal Savings Bank of Springfield (“Bank”). The Bank is primarily engaged in providing a full range of banking and financial services to individual and corporate customers in Clark County, Ohio. The Bank is subject to competition from other financial institutions. The Bank is subject to the regulation of certain federal and state agencies and undergoes periodic examinations by those regulatory authorities. The Bank’s wholly-owned subsidiary, Homciti Service Corporation (“Service Corp.”), had held the stock of the Bank’s data service provider, Intrieve Incorporated, until redemption of Intrieve’s stock in 2005. The Service Corp. is dormant as of December 31, 2005.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, the Bank and the Service Corp. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of 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 relate to the determination of the allowance for loan losses. In connection with the determination of the allowance for loan losses, management obtains independent appraisals for significant properties.

Cash Equivalents

The Company considers all liquid investments with original maturities of three months or less to be cash equivalents.

Securities

All securities are classified as available for sale. Available-for-sale securities, which include any security for which the Company has no immediate plan to sell but which may be sold in the future,

are carried at fair value. Unrealized gains and losses are recorded, net of related income tax effects, in other comprehensive income.

Amortization of premiums and accretion of discounts are recorded as interest income from securities. Realized gains and losses are recorded as net security gains (losses). Gains and losses on sales of securities are determined on the specific-identification method.

The Company evaluates its securities portfolio for impairment throughout the year. An impairment is recorded against individual equity securities if their cost significantly exceeds their fair value for a substantial amount of time. An impairment is also recorded for investments in debt securities, unless the decrease in fair value is attributed to interest rates and management has the intent and ability to retain the investment in the issuer for a period of time sufficient to allow for any anticipated recovery in market value.

Loans

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoffs are reported at their outstanding principal balances adjusted for any charge-offs, the allowance for loan losses, any deferred fees or costs on originated loans and unamortized premiums or discounts on purchased loans. Interest income is reported on the interest method and includes amortization of net deferred loan fees and costs over the loan term. Generally, loans are placed on non-accrual status at ninety days past due and interest is considered a loss, unless the loan is well-secured and in the process of collection.

Allowance for Loan Losses

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to income. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

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 and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogenous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment measurements.

Premises and Equipment

Depreciable assets are stated at cost less accumulated depreciation. Depreciation is charged to expense using the straight-line method over the estimated useful lives of the assets.

Federal Home Loan Bank Stock

Federal Home Loan Bank stock is a required investment for institutions that are members of the Federal Home Loan Bank system. The required investment in the common stock is based on a predetermined formula.

Foreclosed Assets Held for Sale

Assets acquired through, or in lieu of, loan foreclosure are held for sale and are initially recorded at fair value at the date of foreclosure, establishing a new cost basis. Subsequent to foreclosure, valuations are periodically performed by management and the assets are carried at the lower of carrying amount or fair value less cost to sell. Revenue and expenses from operations and changes in the valuation allowance are included in net income or expense from foreclosed assets.

Treasury Shares

Treasury shares are stated at cost. Cost is determined by the first-in, first-out method.

Stock Options

Stock options are granted for a fixed number of shares to employees with an exercise price equal to the fair value of the shares at the date of grant. The Bank accounts for and will continue to account for stock option grants in accordance with APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and, accordingly, recognizes no compensation expense for the stock option grants.

	Year Ended December 31	
	2005	2004
Net income, as reported	\$ 837	\$ 682
Less: Total stock-based employee compensation cost determined under the fair value based method, net of income taxes	<u>9</u>	<u>9</u>
Pro forma net income	<u>\$ 828</u>	<u>\$ 673</u>
Earnings per share:		
Basic – as reported	<u>\$ 1.02</u>	<u>\$.86</u>
Basic – pro forma	<u>\$ 1.01</u>	<u>\$.85</u>
Diluted – as reported	<u>\$ 1.01</u>	<u>\$.84</u>
Diluted – pro forma	<u>\$ 1.00</u>	<u>\$.83</u>

Income Taxes

Deferred tax assets and liabilities are recognized for the tax effects of differences between the financial statement and tax bases of assets and liabilities. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that a deferred tax asset will not be realized. The Company files consolidated income tax returns with its subsidiaries.

Earnings Per Share

Earnings per share have been computed based upon the weighted-average common shares outstanding during each year. Unearned ESOP shares and RRP shares which have not vested have been excluded from the computation of average shares outstanding.

Note 2: Securities

The amortized cost and approximate fair values of securities are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Approximate Fair Value
Available-for-Sale Securities:				
December 31, 2005:				
U.S. Treasury and government agencies	\$ 3,249	\$ 0	\$ (3)	\$ 3,246
Mortgage-backed securities	1,066	1	(14)	1,053
Other asset-backed securities	271	0	(3)	268
Equity securities	<u>909</u>	<u>0</u>	<u>(215)</u>	<u>694</u>
	<u>\$ 5,495</u>	<u>\$ 1</u>	<u>\$ (235)</u>	<u>\$ 5,261</u>
December 31, 2004:				
U.S. Treasury and government agencies	\$ 3,604	\$ 0	\$ (9)	\$ 3,595
Mortgage-backed securities	1,705	11	(11)	1,705
Other asset-backed securities	483	1	(8)	476
Equity securities	<u>909</u>	<u>0</u>	<u>(253)</u>	<u>656</u>
	<u>\$ 6,701</u>	<u>\$ 12</u>	<u>\$ (281)</u>	<u>\$ 6,432</u>

The amortized cost and fair value of securities available for sale at December 31, 2005, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Amortized Cost	Available for Sale Fair Value
U.S. Treasury and government agencies		
Within one year	\$ <u>3,249</u>	\$ <u>3,246</u>
	3,249	3,246
Mortgage-backed securities	1,066	1,053
Other asset-backed securities	271	268
Equity securities	<u>909</u>	<u>694</u>
Totals	<u>\$ 5,495</u>	<u>\$ 5,261</u>

The carrying value of securities pledged as collateral, to secure public deposits and for other purposes, was \$0 at December 31, 2005 and 2004.

Gross gains of \$0 and \$6,000 and gross losses of \$0 and \$0 resulting from sales of available-for-sale securities were realized for 2005 and 2004, respectively. The tax expense for net gains on security transactions for 2005 and 2004 was \$0 and \$2,000, respectively.

Certain investments in debt and equity securities are reported in the financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2005, was \$5,191,000, which is approximately 99% of the Company's available-for-sale investment portfolio. These declines primarily resulted from recent increases in market interest rates.

Equity securities consist of two issues of Fannie Mae preferred stock. Management's conclusion that the declines in fair value for these securities is based on its evaluation of Fannie Mae stock performance in historic interest rate environments and projections. Management believes that mortgage-backed and other asset-backed security declines in fair value are temporary based on available evidence of recent changes in market interest rates. Management has both the intent and ability to hold these investments until more favorable market interest rate scenarios are attained.

Should the impairment of any of these securities become other than temporary, the cost basis of the investment will be reduced and the resulting loss recognized in net income in the period the other-than-temporary impairment is identified.

The following table shows our 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:

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Available-for-Sale Securities:						
December 31, 2005:						
U.S. Treasury and government agencies	\$ 2,998	\$ 1	\$ 248	\$ 2	\$ 3,246	\$ 3
Mortgage-backed securities	236	3	747	11	983	14
Other asset-backed securities	86	1	182	2	268	3
Equity securities	<u>0</u>	<u>0</u>	<u>694</u>	<u>215</u>	<u>694</u>	<u>215</u>
	\$ <u>3,320</u>	\$ <u>5</u>	\$ <u>1,871</u>	\$ <u>230</u>	\$ <u>5,191</u>	\$ <u>235</u>
December 31, 2004:						
U.S. Treasury and government agencies	\$ 3,595	\$ 9	\$ 0	\$ 0	\$ 3,595	\$ 9
Mortgage-backed securities	333	3	823	8	1,156	11
Other asset-backed securities	0	0	296	8	296	8
Equity securities	<u>0</u>	<u>0</u>	<u>656</u>	<u>253</u>	<u>656</u>	<u>253</u>
	\$ <u>3,928</u>	\$ <u>12</u>	\$ <u>1,775</u>	\$ <u>269</u>	\$ <u>5,703</u>	\$ <u>281</u>

Note 3: Loans and Allowance for Loan Losses

Categories of loans at December 31, include:

	2005	2004
Residential real estate		
One-to-four family residential	\$ 61,896	\$ 64,663
Multi-family residential	9,939	9,208
Construction	3,242	4,678
Nonresidential real estate and land	34,363	32,303
Commercial	16,385	15,059
Consumer and other	<u>4,546</u>	<u>6,619</u>
Total loans	130,371	132,530
Less		
Deferred loan fees	(348)	(375)
Undisbursed portion of loans	(1,237)	(1,328)
Allowance for loan losses	<u>(1,377)</u>	<u>(760)</u>
Net loans	<u>\$ 127,409</u>	<u>\$ 130,067</u>

Activity in the allowance for loan losses was as follows:

	<u>2005</u>	<u>2004</u>
Balance, beginning of year	\$ 760	\$ 995
Provision charged to expense	705	200
Losses charged off, net of recoveries of \$10,000 for 2005, and \$6,000 for 2004	<u>(88)</u>	<u>(435)</u>
Balance, end of year	<u>\$ 1,377</u>	<u>\$ 760</u>

Impaired loans totaled \$3,851,000 and \$3,707,000 at December 31, 2005 and 2004. An allowance for loan losses of \$393,000 and \$67,000 relates to impaired loans of \$2,470,000 and \$1,290,000 at December 31, 2005 and 2004. At December 31, 2005 and 2004 impaired loans of \$1,380,000 and \$2,417,000 had no related allowance for loan losses.

Interest of \$274,000 and \$239,000 was recognized on average impaired loans of \$3,557,000 and \$3,105,000 for 2005 and 2004. Interest of \$270,000 and \$236,000 was recognized on impaired loans on a cash basis during 2005 and 2004.

At December 31, 2005 and 2004, accruing loans delinquent 90 days or more totaled \$23,000 and \$0, respectively. Non-accruing loans at December 31, 2005 and 2004 were \$846,000 and \$195,000, respectively.

Note 4: Premises and Equipment

Major classifications of premises and equipment, stated at cost, are as follows:

	<u>2005</u>	<u>2004</u>
Land	\$ 806	\$ 806
Buildings and improvements	2,493	2,489
Equipment	<u>1,656</u>	<u>1,639</u>
	4,955	4,934
Less accumulated depreciation	<u>(1,557)</u>	<u>(1,332)</u>
Net premises and equipment	<u>\$ 3,398</u>	<u>\$ 3,602</u>

Note 5: Interest-Bearing Deposits

Interest-bearing time deposits in denominations of \$100,000 or more were \$23,329,000 on December 31, 2005 and \$15,248,000 on December 31, 2004.

At December 31, 2005, the scheduled maturities of time deposits are as follows:

2006	\$ 34,747
2007	19,828
2008	3,301
2009	730
2010	<u>1,106</u>
	\$ <u>59,712</u>

Note 6: Federal Home Loan Bank Advances

Aggregate annual maturities of FHLB advances at December 31, 2005, are:

2006	\$ 3,723
2007	1,894
2008	1,858
2009	9,523
2010	8,339
Thereafter	<u>11,000</u>
	\$ <u>36,337</u>

The Federal Home Loan Bank advances are secured by mortgage loans totaling \$40,880,000 at December 31, 2005. Advances, at interest rates from 3.05 percent to 7.28 percent, are subject to restrictions or penalties in the event of prepayment.

The Bank has unused letters of credit with the Federal Home Loan Bank aggregating \$3,270,000 expiring at various dates from March 7, 2006, through December 19, 2006.

Note 7: Income Taxes

The provision for income taxes includes these components:

	<u>2005</u>	<u>2004</u>
Taxes currently payable	\$ 595	\$ 212
Deferred income taxes (credit)	<u>(214)</u>	<u>95</u>
Income tax expense	\$ <u><u>381</u></u>	\$ <u><u>307</u></u>

A reconciliation of income tax expense at the statutory rate to the Company's actual income tax expense from continuing operations is shown below:

	<u>2005</u>	<u>2004</u>
Computed at the statutory rate (34%)	\$ 414	\$ 336
Increase (decrease) resulting from:		
Tax exempt interest	0	(3)
Cash surrender value of life insurance	(44)	(39)
Nondeductible expenses	6	4
Other	<u>5</u>	<u>9</u>
Actual tax expense from continuing operations	\$ <u><u>381</u></u>	\$ <u><u>307</u></u>

The tax effects of temporary differences related to deferred taxes shown on the balance sheets were:

	<u>2005</u>	<u>2004</u>
Deferred tax assets		
Allowance for loan losses	\$ 468	\$ 258
Employee benefits	216	185
Nonaccrual loan interest	6	0
Other	31	29
Unrealized losses on available-for-sale securities	<u>80</u>	<u>92</u>
	<u>801</u>	<u>564</u>
Deferred tax liabilities		
Depreciation	(102)	(104)
Federal Home Loan Bank stock dividend	(311)	(271)
Deferred loan fees	<u>(47)</u>	<u>(50)</u>
	<u>(460)</u>	<u>(425)</u>
Net deferred tax asset	\$ <u><u>341</u></u>	\$ <u><u>139</u></u>

Retained earnings at December 31, 2005 and 2004, include approximately \$1,084,000, for which no deferred federal income tax liability has been recognized. These amounts represent an allocation of income to bad debt deductions for tax purposes only. Reduction of amounts so allocated for purposes other than tax bad debt losses or adjustments arising from carryback of net operating losses would create income for tax purposes only, which would be subject to the then-current corporate income tax rate. The deferred income tax liabilities on the preceding amounts that would have been recorded if they were expected to reverse into taxable income in the foreseeable future were approximately \$368,000 at December 31, 2005 and 2004.

Note 8: Other Comprehensive Income (Loss)

Other comprehensive income (loss) components and related taxes were as follows:

	<u>2005</u>	<u>2004</u>
Unrealized gains (losses) on securities available for sale	\$ 35	\$ (125)
Reclassification for realized amount included in income	<u>0</u>	<u>6</u>
Other comprehensive income (loss) before tax effect	35	(131)
Tax benefit (expense)	<u>(12)</u>	<u>45</u>
Other comprehensive income (loss)	\$ <u><u>23</u></u>	\$ <u><u>(86)</u></u>

Note 9: Regulatory Matters

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and 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 in the table below). 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 Office of Thrift Supervision categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based and Tier I leverage ratios as set forth in the table. There are no conditions or events since that notification that management believes have changed the Bank's category.

As of August 22, 2005, Home City Federal Savings Bank of Springfield entered into a supervisory agreement with the OTS. Disclosure of the supervisory agreement was filed in a Form 8-K. Management believes it is adhering responsibly to the directives of this agreement and that Home City will have enhanced its ability to provide excellent customer service to the community while strengthening and maintaining its regulatory compliance and performance.

The Bank's actual capital amounts and ratios are also presented in the table

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2005						
Total risk-based capital (to risk-weighted assets)	\$ 14,483	13.3%	\$ 8,730	8.0%	\$ 10,913	10.0%
Tier I capital (to risk-weighted assets)	13,119	12.0	—	N/A	6,548	6.0
Tier I capital (to adjusted total assets)	13,119	8.8	5,977	4.0	7,471	5.0
Tangible capital (to adjusted tangible assets)	13,119	8.8	2,241	1.5	—	N/A
As of December 31, 2004						
Total risk-based capital (to risk-weighted assets)	\$ 12,964	11.6%	\$ 8,981	8.0%	\$ 11,226	10.0%
Tier I capital (to risk-weighted assets)	12,204	10.9	—	N/A	6,736	6.0
Tier I capital (to adjusted total assets)	12,204	7.8	6,245	4.0	7,806	5.0
Tangible capital (to adjusted tangible assets)	12,204	7.8	2,342	1.5	—	N/A

The Bank is subject to certain restrictions on the amount of dividends that it may declare without prior regulatory approval. At December 31, 2005, all dividend declarations are subject to prior regulatory approval under the terms of the Bank's supervisory agreement with the OTS.

Note 10: Related Party Transactions

The Bank has entered into transactions with certain directors, executive officers, significant shareholders and their affiliates or associates (related parties). In management's opinion, such loans and other extensions of credit and deposits were made in the ordinary course of business and were made on substantially the same terms (including interest rates and collateral) as those prevailing at the time for comparable transactions with other persons. Further, in management's opinion, these loans did not involve more than normal risk of collectibility or present other unfavorable features.

The aggregate amount of loans, as defined, to such related parties were as follows:

Balances, January 1, 2005	\$ 3,220
New loans, including renewals	40
Payments, etc., including renewals	<u>(1,249)</u>
Balances, December 31, 2005	<u>\$ 2,011</u>

Deposits from related parties held by the Bank at December 31, 2005 and 2004 totaled \$660,000 and \$407,000, respectively.

Note 11: Employee Benefits

The Company has a retirement savings 401(k) plan covering substantially all employees. Employees may contribute up to 15% of their compensation with the Company matching 75% of the employee's contribution on the first 6% of the employee's compensation. Employer contributions charged to expense for 2005 and 2004 were \$42,000 and \$41,000, respectively.

As part of the conversion in 1996, the Company established an ESOP covering substantially all employees of the Company and Bank. The ESOP acquired shares of the Company common stock at \$10 per share in the conversion with funds provided by a loan from the Company. Accordingly, the common stock acquired by the ESOP was shown as a reduction of shareholders' equity. Shares are released to participants proportionately as the loan is repaid. Dividends on allocated shares are recorded as dividends and charged to retained earnings. Dividends on unallocated shares are used to repay the loan and are treated as compensation expense. Compensation expense is recorded equal to the fair market value of the stock when contributions, which are determined annually by the Board of Directors of the Company and Bank, are made to the ESOP.

ESOP expense for the years ended December 31, 2005 and 2004 was \$149,000 and \$175,000.

	<u>2005</u>	<u>2004</u>
Allocated shares	70,812	61,363
Shares released for allocation	9,449	9,449
Unearned shares	<u>7,612</u>	<u>17,061</u>
Total ESOP shares	<u>87,873</u>	<u>87,873</u>
Fair value of unearned shares at December 31	<u>\$ 120,000</u>	<u>\$ 263,000</u>

The Company also has a Recognition and Retention Plan (RRP) which provides for the award and issuance of up to 38,088 shares of the Company's stock to members of the Board of Directors and management. At December 31, 2005, 36,792 shares had been awarded net of 2,414 which had been forfeited. Common stock awarded under the RRP vests ratably over a five-year period, commencing with the date of the award. Expense recognized under the RRP plan totaled approximately \$37,000 and \$26,000 for 2005 and 2004, respectively.

Note 12: Stock Option Plan

The Company has a fixed option plan under which the Company may grant options that vest over five years to selected employees for up to 131,422 shares of common stock. The exercise price of each option is intended to equal the fair value of the Company's stock on the date of grant. An option's maximum term is ten years.

At December 31, 2005, the weighted average remaining contractual life of all options was 5.5 years. A summary of the status of the plan at December 31, 2005 and 2004, and changes during the years then ended is presented below:

	2005		2004	
	Shares	Weighted-Average Exercise Price	Shares	Weighted-Average Exercise Price
Outstanding, beginning of year	53,796	\$ 12.76	120,506	\$ 12.22
Granted	-0-	-0-	-0-	-0-
Exercised	-0-	-0-	(65,710)	11.70
Forfeited	-0-	-0-	(1,000)	17.03
Expired	<u>-0-</u>	-0-	<u>-0-</u>	-0-
Outstanding, end of year	<u>53,796</u>	\$ 12.76	<u>53,796</u>	\$ 12.76
Options exercisable, end of year	<u>33,653</u>	\$ 12.38	<u>26,939</u>	\$ 12.12

There were no additional options granted during the year 2005.

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

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
\$11.70 to \$13.175	51,796	5.38 years	\$12.60	32,853	\$12.27
\$17.03	2,000	7.97 years	\$17.03	800	\$17.03

Note 13: Earnings Per Share

Earnings per share (EPS) were computed as follows:

	Year Ended December 31, 2005		
	Income	Weighted- Average Shares	Per Share Amount
Basic earnings per share			
Income from continuing operations available to common shareholders	\$ 837	820,575	\$ <u>1.02</u>
Effect of dilutive securities			
Stock options and awards	<u>—</u>	<u>9,540</u>	
Diluted earnings per share			
Income from continuing operations available to common shareholders and assumed conversions	\$ <u>837</u>	<u>830,115</u>	\$ <u>1.01</u>

Stock Awards and options to purchase 2,000 shares of common stock at a price of \$17.03 per share were outstanding at December 31, 2005, but were not included in the computation of diluted EPS because the options' exercise price was greater than the average market price of the common shares.

	Year Ended December 31, 2004		
	Income	Weighted- Average Shares	Per Share Amount
Basic earnings per share			
Income from continuing operations available to common shareholders	\$ 682	793,233	\$ <u>0.86</u>
Effect of dilutive securities			
Stock options and awards	<u>—</u>	<u>15,453</u>	
Diluted earnings per share			
Income from continuing operations available to common shareholders and assumed conversions	\$ <u>682</u>	<u>808,686</u>	\$ <u>0.84</u>

Stock Awards and options to purchase 4,400 shares of common stock between the price of \$17.03 and \$17.25 per share were outstanding at December 31, 2004, but were not included in the computation of diluted EPS because the options' exercise price was greater than the average market price of the common shares.

Note 14: Disclosures about Fair Value of Financial Instruments

The following table presents estimated fair values of the Company's financial instruments. The fair values of certain of these instruments were calculated by discounting expected cash flows, which involves significant judgments by management and uncertainties. Fair value is the estimated amount at which financial assets or liabilities could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale. Because no market exists for certain of these financial instruments and because management does not intend to sell these financial instruments, the Company does not know whether the fair values shown below represent values at which the respective financial instruments could be sold individually or in the aggregate.

	December 31, 2005		December 31, 2004	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets				
Cash and cash equivalents	\$ 6,846	\$ 6,846	\$ 9,595	\$ 9,595
Available-for-sale securities	5,261	5,261	6,432	6,432
Loans, net	127,409	129,971	130,067	134,468
Stock in FHLB	2,480	2,480	2,360	2,360
Interest receivable	559	559	544	544
Financial liabilities				
Deposits	98,455	98,105	107,204	107,438
FHLB advances	36,337	37,423	35,120	37,688
Interest payable	190	190	178	178

For purposes of the above disclosures of estimated fair value, the following assumptions were used as of December 31, 2005 and 2004. The estimated fair value for cash and cash equivalents, interest-bearing deposits, FHLB stock, accrued interest receivable, demand deposits, savings accounts, NOW accounts, certain money market deposits, and interest payable is considered to approximate cost. The estimated fair value for securities is based on quoted market values for the individual securities or for equivalent securities. The estimated fair value for loans receivable, including loans held for sale, net, is based on estimates of the rate the Bank would charge for similar loans at December 31, 2005 and 2004 applied for the time period until the loans are assumed to reprice or be paid. The estimated fair value for fixed-maturity time deposits as well as borrowings is based on estimates of the rate the Bank would pay on such liabilities at December 31, 2005 and 2004, applied for the time period until maturity. The fair value of commitments is 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 letters of credit and lines of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate or otherwise settle the obligations with the counterparties at the reporting date.

Note 15: Commitments and Credit Risk

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

At December 31, 2005 and 2004, the Bank had outstanding commitments to originate loans aggregating approximately \$863,000 and \$2,238,000, respectively. The commitments extended over varying periods of time with the majority being disbursed within a one-year period. Loan commitments at fixed rates of interest amounted to \$733,000 and \$1,023,000 at December 31, 2005 and 2004, respectively, with the remainder at floating market rates.

Letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements, including commercial paper, bond financing and similar transactions. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers.

The Bank had total outstanding letters of credit amounting to \$104,000 and \$187,000 at December 31, 2005 and 2004, respectively, with a term of seven months.

Lines of credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Lines of credit generally have fixed expiration dates. Since a portion of the line may expire without being drawn upon, the total unused lines do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary, is based on management's credit evaluation of the counterparty. Collateral held varies but may include accounts receivable, inventory, property, plant and equipment, commercial real estate and residential real estate. Management uses the same credit policies in granting lines of credit as it does for on-balance-sheet instruments.

At December 31, 2005, the Bank had granted unused lines of credit to borrowers aggregating approximately \$6,776,000 and \$3,980,000 for commercial lines and open-end consumers lines, respectively. At December 31, 2004, the Bank had granted unused lines of credit to borrowers aggregating approximately \$4,454,000 and \$4,034,000 for commercial lines and open-end consumer lines, respectively.

At December 31, 2005, approximately \$719,000 and \$1,581,000 were on deposit at Great Lakes Bankers Bank and US Bank, respectively. In the latter part of the year US Bank became our cash letter depository replacing Fifth Third Bank. At December 31, 2004, approximately \$2,579,000 and \$1,460,000 were on deposit at Great Lakes Bankers Bank and Fifth Third Bank, respectively.

Note 16: Future Change in Accounting Principle

The Financial Accounting Standards Board recently issued Statement No. 123(R) "Share-Based Payment," which requires the compensation cost relating to share-based payment transactions be recognized in financial statements. The Company expects to first apply the new statement during its first quarter ending in 2006. The Company has determined to use the modified prospective method and no material impact is expected.

Note 17: Subsequent Event

On January 26, 2006, Home City Financial Corporation announced that its Board of Directors had approved a plan to end the Corporation's obligation to file reports with the Securities and Exchange Commission (the "SEC"). The going private transaction would be accomplished through a 1-for-210 reverse split of HCFC's common shares to be followed immediately by a 210-for-1 forward split. As a result, shareholders with fewer than 210 common shares of HCFC held of record in their name immediately before the stock splits will receive a cash payment equal to \$16.20 per pre-split share. Shareholders holding 210 or more shares of HCFC common shares immediately before the stock splits will not receive a cash payment and will continue to hold the same number of HCFC shares.

If the stock splits are completed, HCFC expects to have fewer than 300 shareholders of record, enabling it to deregister its common shares under the Securities Exchange Act of 1934. As a result, HCFC would not be required to file periodic reports and other information with the Securities and Exchange Commission so long as it has fewer than 300 shareholders of record. If HCFC deregisters its common shares and suspends reporting obligations under the Securities Exchange Act of 1934, the common shares will cease to be eligible for trading on the NASDAQ Capital Market. However, HCFC anticipates that its common shares will be quoted on the OTC Bulletin Board or in the Pink Sheets, to the extent market makers continue to make a market in the shares.

The proposed stock splits are subject to approval by the holders of a majority of the issued and outstanding common shares of HCFC. Shareholders will be asked to approve the stock splits at HCFC's annual meeting of shareholders. HCFC has filed a preliminary proxy statement and Schedule 13E-3 with the SEC outlining the transaction. HCFC will also mail a copy of the definitive proxy statement prior to the meeting to its shareholders entitled to vote at the meeting.

Note 18: Condensed Financial Information (Parent Company Only)

Presented below is condensed financial information as to financial position, results of operations and cash flows of the Company:

Condensed Balance Sheets

	<u>2005</u>	<u>2004</u>
Assets		
Cash	\$ 137	\$ 260
Investment in common stock of subsidiary Bank	13,106	12,232
Advances to subsidiary	13	140
Other assets	<u>150</u>	<u>103</u>
Total assets	<u>\$ 13,406</u>	<u>\$ 12,735</u>
Shareholders' Equity	<u>\$ 13,406</u>	<u>\$ 12,735</u>

Condensed Statements of Income

	2005	2004
Income		
Dividends from subsidiary Bank	\$ 0	\$ 0
Interest income	<u>15</u>	<u>22</u>
Total income	<u>15</u>	<u>22</u>
Expenses		
Other expenses	<u>93</u>	<u>85</u>
Income (Loss) Before Income Tax and Equity in Undistributed Income of Subsidiary	(78)	(63)
Income Tax Benefit	<u>(26)</u>	<u>(22)</u>
Income (Loss) Before Equity in Undistributed Income of Subsidiary	(52)	(41)
Equity in Undistributed Income of Subsidiary	<u>889</u>	<u>723</u>
Net Income	<u>\$ 837</u>	<u>\$ 682</u>

Condensed Statements of Cash Flows

	2005	2004
Operating Activities		
Net income	\$ 837	\$ 682
Items not requiring (providing) cash	<u>(719)</u>	<u>(537)</u>
Net cash provided by operating activities	<u>118</u>	<u>145</u>
Investing Activities—advances to subsidiaries	<u>127</u>	<u>139</u>
Financing Activities		
Cash dividends paid	(368)	(363)
Purchase of treasury shares	0	(411)
Proceeds from stock options exercised	<u>0</u>	<u>769</u>
Net cash used in financing activities	<u>(368)</u>	<u>(5)</u>
Net Change in Cash and Cash Equivalents	(123)	1
Cash and Cash Equivalents at Beginning of Year	<u>260</u>	<u>259</u>
Cash and Cash Equivalents at End of Year	<u>\$ 137</u>	<u>\$ 260</u>

Note 19: Quarterly Financial Data (Unaudited)

The following tables summarize selected quarterly results of operations for 2005 and 2004.

December 31, 2005	March	June	September	December
Interest and dividend income	\$ 2,227	\$ 2,290	\$ 2,293	\$ 2,301
Interest expense	1,069	1,083	1,113	1,142
Net interest income	1,158	1,207	1,180	1,159
Provision for loan losses	80	475	80	70
Noninterest income	36	419	116	64
Noninterest expense	829	853	855	879
Income tax expense	92	94	115	80
Net income	193	204	246	194
Earnings per share				
Basic	0.24	0.25	0.30	0.24
Diluted	0.23	0.25	0.30	0.23
Dividends per share	0.11	0.11	0.11	0.11
December 31, 2004				
Interest and dividend income	\$ 2,190	\$ 2,159	\$ 2,179	\$ 2,244
Interest expense	1,094	1,084	1,090	1,102
Net interest income	1,096	1,075	1,089	1,142
Provision for loan losses	50	50	42	58
Noninterest income	52	49	57	81
Noninterest expense	867	818	881	886
Income tax expense	63	75	72	97
Net income	168	181	151	182
Earnings per share				
Basic	0.21	0.23	0.19	0.23
Diluted	0.21	0.22	0.19	0.22
Dividends per share	0.11	0.11	0.11	0.11