

DONEGAL GROUP INC  
Form S-4  
June 25, 2010

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As filed with the Securities and Exchange Commission on June 25, 2010  
Registration No. 333-

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**Form S-4**  
**REGISTRATION STATEMENT**  
**UNDER**  
**THE SECURITIES ACT OF 1933**  
**Donegal Group Inc.**

*(Exact name of registrant as specified in its charter)*

<b>Delaware</b> <i>(State or other jurisdiction of incorporation or organization)</i>	<b>6331</b> <i>(Primary Standard Industrial Classification Code Number)</i>	<b>23-2424711</b> <i>(I.R.S. Employer Identification No.)</i>
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**1195 River Road**  
**Marietta, Pennsylvania 17547**  
**(888) 877-0600**

*(Address, including zip code, and telephone number, including area code,  
of registrant's principal executive offices)*

**Donald H. Nikolaus**  
**President and Chief Executive Officer**  
**Donegal Group Inc.**  
**1195 River Road**  
**Marietta, Pennsylvania 17547**  
**(888) 877-0600**

*(Name, address, including zip code, and telephone number,  
including area code, of agent for service)*

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**Approximate date of commencement of proposed sale of the securities to the public:** Upon the effective date of the merger of Union National Financial Corporation with and into Donegal Financial Services Corporation, a company jointly owned by registrant and Donegal Mutual Insurance Company.

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If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box.

If the securities being registered on this Form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

If applicable, place an X in the box to designate the appropriate rule provisions relied upon in conducting this transaction:

Exchange Act Rule 13e-4(i) (Cross-Border Issuer Tender Offer)

Exchange Act Rule 14d-1(d) (Cross-Border Third-Party Tender Offer)

**CALCULATION OF REGISTRATION FEE**

<b>Title of Each Class of Securities to be Registered</b>	<b>Amount to be Registered(1)</b>	<b>Proposed Maximum Offering Price per Unit</b>	<b>Proposed Maximum Aggregate Offering Price</b>	<b>Amount of Registration Fee</b>
Class A Common Stock \$.01 par value	600,000 shares	N/A	\$24,743,326(2)	\$1,764.20

- (1) Represents the maximum number of shares of Donegal Group Inc. Class A common stock that may be distributed as merger consideration in connection with the proposed merger to which this registration statement relates.
- (2) Pursuant to Rule 457(f), the registration fee was computed on the basis of \$7.475, the market value of the common stock of Union National Financial Corporation to be exchanged or cancelled in the merger, computed in accordance with Rule 457(c) on the basis of the average of the high and low prices per share of such common stock quoted on the OTC Bulletin Board on June 21, 2010 multiplied by 3,310,144 shares of common stock of Union National Financial Corporation that the registrant's affiliate will receive for surrender or cancellation upon consummation of the merger.

**The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this**

**Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.**

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The information in this proxy statement/prospectus is not complete and may be changed. Donegal Financial Services Corporation may not distribute the shares of Class A common stock of Donegal Group Inc. in connection with the merger described in this proxy statement/prospectus until the registration statement filed with the SEC is effective. This proxy statement/prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

**[SUBJECT TO COMPLETION, DATED JUNE 25, 2010]**

**[UNION NATIONAL FINANCIAL CORPORATION LOGO]**

**MERGER PROPOSAL YOUR VOTE IS VERY IMPORTANT**

To the Shareholders of Union National Financial Corporation:

On April 19, 2010, our board of directors unanimously approved an agreement that provides for our merger with Donegal Financial Services Corporation, or DFSC. The merger agreement, as amended on May 20, 2010, also provides for the merger of Union National Community Bank, or UNCB, which we currently own, with and into Province Bank FSB, or Province, which DFSC currently owns. DFSC is a savings and loan holding company that Donegal Mutual Insurance Company, or DMIC, and Donegal Group Inc., or DGI, jointly own.

We are sending this proxy statement/prospectus to you to ask you to vote on the adoption of our merger agreement with DFSC, DMIC, DGI and Donegal Acquisition, Inc., or DAI, and the transactions the merger agreement contemplates.

If our shareholders adopt the merger agreement, and we subsequently complete the merger, each outstanding share of our common stock, other than the 248,999 shares DMIC owns and shares as to which the holders perfect dissenters rights, will be converted into the right to receive \$5.05 in cash and 0.2134 share of Class A common stock of DGI. The merger consideration of \$5.05 in cash and 0.2134 share of Class A common stock of DGI is fixed, and will not change if our stock price or the price of DGI Class A common stock changes. On April 19, 2010, the last trading day before we announced the merger, the closing price of our common stock on the OTC Bulletin Board, or OTCBB, was \$6.00. Based on the closing price of DGI Class A common stock on the NASDAQ Global Select Market, or NASDAQ, on April 19, 2010, 0.2134 share of DGI Class A common stock and \$5.05 in cash represented approximately \$8.18 in value for each share of our common stock.

Based on the average closing price of DGI Class A common stock for the five trading days ended \_\_\_\_\_, 2010, 0.2134 share of DGI Class A common stock and \$5.05 in cash represented approximately \$ \_\_\_\_\_ in value for each share of our common stock.

You should obtain current stock price quotations for DGI Class A common stock which trades on NASDAQ under the symbol **DGICA** and our common stock which trades on the OTCBB under the symbol **UNNF.OB**.

**OUR BOARD OF DIRECTORS HAS UNANIMOUSLY DETERMINED THAT THE MERGER AND THE MERGER AGREEMENT ARE ADVISABLE AND IN THE BEST INTERESTS OF UNNF AND ITS SHAREHOLDERS AND UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR ADOPTION OF THE MERGER AGREEMENT.** We cannot complete the merger unless the holders of 80% of our issued and outstanding shares vote to adopt the merger agreement. Whether or not you plan to attend our special meeting of shareholders,

please vote by completing the enclosed proxy card and returning it to us in the enclosed envelope. **If you sign, date and return your proxy card without indicating how you want to vote, we will count your proxy as a vote *FOR* adoption of the merger agreement. If you fail to vote, or you do not instruct your broker how to vote any shares you hold in street name, it will have the same effect as voting against adoption of the merger agreement.**

The accompanying proxy statement/prospectus describes our special meeting, the merger agreement, the transactions the merger agreement contemplates, the documents related to the merger and related matters. **We recommend that you carefully read this proxy statement/prospectus, including the considerations discussed under Risk Factors beginning on page 66 and the appendices to this proxy statement/prospectus, which include the merger agreement.**

On behalf of our board of directors, I thank you for your prompt attention to this important matter.

Sincerely,

Mark D. Gainer  
Chairman, President and Chief Executive Officer

, 2010

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the DGI Class A common stock to be distributed under this proxy statement/prospectus or determined if this proxy statement/prospectus is accurate or adequate. Any representation to the contrary is a criminal offense.**

**Shares of DGI Class A common stock are not savings or deposit accounts or other obligations of any bank or savings association and they are not insured by the Federal Deposit Insurance Corporation or any other governmental agency.**

**The date of this proxy statement/prospectus is \_\_\_\_\_, 2010, and we are first mailing or otherwise delivering it to our shareholders on or about \_\_\_\_\_, 2010.**

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[UNNF LOGO]

**570 Lausch Lane, Suite 300  
Lancaster, Pennsylvania 17601**

**NOTICE OF SPECIAL MEETING OF SHAREHOLDERS  
TO BE HELD           , 2010**

WE HEREBY GIVE NOTICE that we will hold a special meeting of our shareholders at   a.m., prevailing time, on           , 2010 at The Eden Resort Inn , 222 Eden Road, Lancaster, Pennsylvania 17601, for the following purposes, all of which we describe in greater detail in the subsequent pages of this proxy statement/prospectus:

(1) to consider and vote upon a proposal to adopt the Agreement and Plan of Merger, dated as of April 19, 2010, and as amended as of May 20, 2010, among Donegal Acquisition Inc., Donegal Financial Services Corporation, Donegal Group Inc., and Donegal Mutual Insurance Company and us, and the consummation of the transactions the merger agreement contemplates as discussed in this proxy statement/prospectus.

(2) to consider and vote upon a proposal to approve the adjournment of our special meeting, if necessary, to permit the further solicitation of proxies if sufficient votes have not been cast at the time of our special meeting to adopt the merger agreement; and

(3) to transact any other business properly presented for action at our special meeting and any adjournment or postponement of our special meeting.

You should read this proxy statement/prospectus in its entirety before you vote. We have included a copy of the merger agreement as Appendix A to this proxy statement/prospectus. Only our shareholders as of the close of business on           , 2010 are entitled to notice of, and to vote at, our special meeting and any adjournment or postponement of our special meeting.

This notice also constitutes notice of your right to dissent from the merger and, upon compliance with the requirements of Subchapter D of Chapter 15 of the Pennsylvania Business Corporation Law of 1988, or PBCL, to receive the appraised fair value of your shares. We have included a copy of the relevant sections of the PBCL regarding dissenters' rights as Appendix C to this proxy statement/prospectus.

**Our board of directors has unanimously approved the merger agreement and recommends that you vote *FOR* adoption of the merger agreement and *FOR* the adjournment of our special meeting.**

Whether or not you expect to attend our special meeting in person, we urge you to vote. Please sign, date and promptly return the enclosed proxy. We enclose a self-addressed envelope for your convenience; no postage is required if mailed in the United States. If you submit a signed and dated proxy card but do not indicate how you want to vote your shares, the persons named as proxies in the enclosed proxy will vote your shares ***FOR*** the adoption of the merger agreement and ***FOR*** the adjournment of our special meeting. Returning your proxy will not prevent you from attending our special meeting and voting in person if you wish to vote in person. You may revoke your proxy and vote in person at any time before we vote your proxy.

Please do not send any stock certificates at this time. Thank you for your cooperation.

By order of our board of directors,

Mark D. Gainer  
Chairman, President and Chief Executive Officer

Lancaster, Pennsylvania  
, 2010

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**APPENDICES:**

Appendix A	Agreement and Plan of Merger dated as of April 19, 2010, among Donegal Acquisition Inc., Donegal Financial Services Corporation, Donegal Group Inc., Donegal Mutual Insurance Company and Union National Financial Corporation, as amended and restated to reflect an Amendment to Merger Agreement dated as of May 20, 2010	A-1
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**WHERE YOU CAN FIND MORE INFORMATION**

In this proxy statement/prospectus, you refers to the shareholders of UNNF, we, us, our or UNNF refers to Union National Financial Corporation, UNCB refers to Union National Community Bank, DAI refers to Donegal Acquisition Inc., DMIC refers to Donegal Mutual Insurance Company, DGI refers to Donegal Group Inc., DFSC refers to Donegal Financial Services Corporation, Province refers to Province Bank FSB and the Donegal parties refers to one or more of DAI, DMIC, DGI, DFSC and Province as the context requires. Also, we refer to the mergers between DAI and UNNF and between UNNF and DFSC as the merger, and the agreement and plan of merger dated as of April 19, 2010, and as amended as of May 20, 2010, among the Donegal parties and UNNF as the merger agreement.

Both UNNF and DGI file annual, quarterly and special reports, proxy statements and other information with the Securities and Exchange Commission, or SEC, under the Securities Exchange Act of 1934 as amended, or the 1934 Act. You may obtain copies of these documents by mail from the public reference room of the SEC at 100 F Street, N.E., Room 1580, Washington, D.C. 20549, at prescribed rates. You may also call the SEC at (800) SEC-0330 for further information on the public reference room. In addition, UNNF's and DGI's SEC filings are also available to the public from commercial document retrieval services and at the website the SEC maintains at [www.sec.gov](http://www.sec.gov).

This proxy statement/prospectus incorporates by reference important business and financial information and risk factors about DGI from documents that DGI has previously filed with the SEC. We are not required to include, and have not included, these documents as part of this proxy statement/prospectus. See Incorporation of Certain Documents by Reference on page 126. You may obtain these documents from DGI at DGI's address and telephone number listed below without charge upon written or oral request:

Donegal Group Inc.  
1195 River Road  
Marietta, Pennsylvania 17547  
Attention: Jeffrey D. Miller  
Telephone: (888) 877-0600

*In order to ensure timely delivery of the documents, you must request the information no later than \_\_\_\_\_, 2010.*

DGI has filed a registration statement on Form S-4 to register with the SEC under the Securities Act of 1933, as amended, or the 1933 Act, relating to 600,000 shares of DGI Class A common stock. DFSC will distribute the 600,000 shares of DGI Class A common stock as merger consideration to our shareholders pursuant to the merger agreement. This proxy statement/prospectus is a part of that registration statement. As SEC rules permit, this proxy statement/prospectus does not contain all of the information included in the registration statement or in the exhibits or schedules to the registration statement. You may read and copy the registration statement, including any amendments, schedules or exhibits, at the addresses listed above. Statements contained in this proxy statement/prospectus are not necessarily complete. In each case, you should refer to the copy of the applicable document or contract filed as an exhibit to the registration statement.

DGI Class A common stock trades on the NASDAQ Global Select Market, or NASDAQ, under the symbol DGICA, and UNNF common stock trades on the OTC Bulletin Board, or OTCBB, under the symbol UNNF.OB.





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**QUESTIONS AND ANSWERS ABOUT THE MERGER AND OUR SPECIAL MEETING**

Q. *What items of business will we ask our shareholders to consider at our special meeting?*

A. At our special meeting, we will ask our shareholders to vote in favor of the adoption of the merger agreement. We sometimes refer to this proposal as the merger proposal in this proxy statement/prospectus. We will also ask our shareholders to vote in favor of any necessary adjournment of our special meeting to solicit additional proxies in favor of the adoption of the merger agreement if we have not received sufficient votes to adopt the merger agreement at the time of our special meeting. We sometimes refer to this proposal as the adjournment proposal in this proxy statement/prospectus.

Q. *What should I do now?*

A. You should first carefully read this proxy statement/prospectus, including the appendices and the documents DGI has incorporated by reference in this proxy statement/prospectus. After you have decided how you wish to vote your shares, please return your proxy using one of the methods we describe below so that your shares will be represented and voted at our special meeting.

Q. *What will I receive in exchange for my UNNF shares if the merger takes place?*

A. Upon consummation of the merger, you will have the right to receive in exchange for each share of our common stock:

0.2134 share of DGI Class A common stock; and

\$5.05 in cash.

Q. *What does our board of directors recommend?*

A. Our board of directors has unanimously determined that the merger is fair to you and in your and our best interests and unanimously recommends that you vote **FOR** the merger proposal and the adjournment proposal.

In making this determination, our board of directors considered the opinion of Sandler O'Neill & Partners, L.P., or Sandler O'Neill, our independent financial advisor, as to the fairness to us and you from a financial point of view of the cash and DGICA shares you will receive pursuant to the merger agreement. Our board of directors also reviewed and evaluated the terms and conditions of the merger agreement and the merger with the assistance of our independent legal counsel.

Q. *What was the opinion of our financial advisor?*

A. Sandler O'Neill presented an opinion to our board of directors to the effect that, as of April 19, 2010, and based upon the assumptions Sandler O'Neill made, the matters it considered and the limitations on its review as set forth in its opinion, the merger consideration provided for in the merger agreement is fair to us and you from a financial point of view.

Q. *Why is my vote important?*

A. Pennsylvania law and our articles of incorporation require the affirmative vote of the holders of 80% of our outstanding shares of common stock to approve the merger proposal. Therefore, abstentions, broker non-votes and failures to vote will have the same effect as a vote against adoption of the merger agreement

Q. *How do I vote my shares?*

A. If you are a registered shareholder of UNNF (that is, if your stock is registered in your name), you may attend our special meeting and vote in person or you may vote by proxy. To vote by proxy, please mark, sign and date your proxy card and return it in the postage-paid envelope we have enclosed.

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Q. *What if I do not specify how I want to vote my shares on my proxy card?*

A. If you submit a signed and dated proxy card but do not indicate how you want to vote your shares, we will vote your shares:

**FOR** the adoption of the merger agreement; and

**FOR** approval of any necessary adjournment of our special meeting.

Our board of directors does not currently intend to bring any other proposal before our special meeting. If other proposals requiring a vote of shareholders properly come before our special meeting in compliance with our by-laws, the persons named as proxies will vote your shares in accordance with their judgment.

Q. *What if I fail to instruct my broker?*

A. Your broker may not vote your shares without instructions from you. You should follow the instructions you will receive from your broker and instruct your broker how you want to vote your shares.

Q. *Can I attend the special meeting and vote my shares in person?*

A. Yes. We invite all shareholders to attend our special meeting. Holders of record can vote in person at our special meeting by executing a ballot we will make available at our special meeting. If a broker holds your shares in street name, you are not a holder of record and you must obtain a written proxy in your name from your broker in order to vote those shares at our special meeting.

Q. *May I change my vote after I have voted?*

A. Yes. If you have not voted through your broker, you may change your vote after you have returned your proxy by:

submitting written notice of revocation to our corporate secretary;

submitting a new proxy by mail, telephone or internet; or

voting in person at our special meeting.

However, simply attending our special meeting without voting will not revoke any proxy you previously submitted.

If you have instructed your broker or other nominee to vote your shares, you should follow the instructions of your broker or other nominee regarding the revocation of proxies.

Q. *When do you expect to complete the merger?*

A. We anticipate that DFSC will obtain all necessary regulatory approvals to consummate the merger in the third quarter of 2010, assuming we and DFSC satisfy all of the other conditions to the completion of the merger. However, we cannot assure you when or if the merger will occur. We must first obtain the approval of the holders of 80% of our outstanding common stock at our special meeting and we and DFSC must obtain the requisite

regulatory approvals to complete the merger.

Q. *Should I send my stock certificates now?*

A. No. Holders of our common stock should not submit their stock for exchange until they receive transmittal instructions from the exchange agent.

Q. *What rights do I have to dissent from the merger?*

A. If you do not vote in favor of the merger proposal and you comply precisely with the applicable procedural requirements, the Pennsylvania Business Corporation Law of 1988, or the PBCL, entitles you to request the appraised fair value of your shares. You must carefully and precisely follow the applicable procedures under the PBCL in order to exercise your dissenters' rights. We have included a complete copy of the relevant sections of the PBCL as Appendix C to this proxy statement/prospectus. The fair value of your shares

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as determined in a dissenters' rights proceeding may be more or less than the merger consideration you have the right to receive from DFSC under the merger agreement.

Q. *What will happen to the UNNF shares that DMIC owns?*

A. DMIC currently owns 248,999 shares, or approximately 9.1%, of our outstanding common stock. DMIC has advised us that DMIC will vote those shares in favor of the merger proposal and the adjournment proposal. The merger agreement provides that DMIC will contribute these shares to the capital of DFSC and that DFSC will surrender the shares for cancellation at the effective time of the merger.

Q. *Who can answer my questions?*

A. If you have questions about the merger, please call Michael D. Peduzzi, Executive Vice President and Chief Financial Officer, at (877) 653-1441.

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**SUMMARY**

This summary highlights selected information included in this proxy statement/prospectus but the summary does not contain all of the information that may be important to you. We encourage you to read carefully this entire proxy statement/prospectus and its appendices and the other documents to which we refer before you decide how to vote on the merger proposal. In addition, we incorporate by reference into this proxy statement/prospectus important business and financial information about DGI. For a description of this information, see Incorporation of Certain Documents by Reference on page 126. You may obtain the information incorporated by reference in this proxy statement/prospectus by following the instructions in Where You Can Find More Information on page v. In this summary, we have included page references to direct you to a more detailed description of the matters described in this summary.

This proxy statement/prospectus and the documents DGI incorporates by reference in this proxy statement/prospectus contain forward-looking information within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, but are not limited to:

statements of goals, intentions and expectations;

statements regarding business plans, prospects, growth and operating strategies; and

statements regarding estimates of risks and future costs and benefits.

You can identify forward-looking statements by their use of words such as *expects*, *anticipates*, *intends*, *plans*, *believes*, *seeks*, *estimates* or words of similar meaning. DGI has based its forward-looking statements on the current beliefs and expectations of DGI's management. Such statements are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond the ability of DGI to control. In addition, these forward-looking statements make certain assumptions with respect to future business strategies and decisions that may change. Actual results may differ materially from the anticipated results DGI discusses in these forward-looking statements. See Cautionary Statement Regarding Forward-Looking Statements on page 70.

We have included the entire text of the merger agreement as Appendix A to this proxy statement/prospectus.

UNNF provided the information contained in this proxy statement/prospectus with respect to UNNF, and DGI provided the information in this proxy statement/prospectus with respect to the Donegal parties.

**The Parties**

**The Donegal Parties (DMIC, DGI, DFSC, DAI and Province) (Page 74)**

***DMIC***

DMIC commenced business as a mutual fire insurance company in Pennsylvania in 1889. Since 1986, when DMIC formed DGI and DGI formed an insurance company subsidiary, Atlantic States Insurance Company, or ASIC, DMIC and the insurance company subsidiaries of DGI have conducted business together as the Donegal Insurance Group. The Donegal Insurance Group writes personal and commercial lines of property and casualty insurance in 18 Mid-Atlantic, Southern and Midwestern states. During 2010, A.M. Best Company, a leading insurance rating firm, reported that the Donegal Insurance Group ranked 116th among property and casualty insurance companies in the United States based on net premiums written during 2009, and A.M. Best Company assigned the Donegal Insurance

Group an A.M. Best rating of A (Excellent). The Donegal Insurance Group has also received the Wards Top 50 award for each of the past five years.

In the mid-1980 s, DMIC recognized that, as a small mutual insurance company, it needed to develop additional sources of capital and surplus to remain competitive, have the capacity to expand its business and assure its long-term viability. As a strategic response, in 1986, DMIC formed DGI as a downstream insurance holding company, and DGI organized ASIC as its subsidiary. DMIC and ASIC then entered into a proportional reinsurance agreement, or pooling agreement. Under this pooling agreement, DMIC and ASIC pool

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substantially all of their respective premiums, loss and loss expenses. DMIC currently cedes 80% of the pooled business to ASIC because of its access to public sources of capital as a subsidiary of DGI.

The following summary financial information of DMIC is presented on the statutory basis of accounting required by the National Association of Insurance Commissioners and does not represent financial information prepared in accordance with generally accepted accounting principles. At March 31, 2010, DMIC had admitted assets of \$325.2 million and policyholders' surplus of \$170.0 million. At March 31, 2010, DMIC had total liabilities of \$155.2 million, including debt of \$13.0 million, reserves for net losses and loss expenses of \$46.8 million and unearned premiums of \$29.3 million. DMIC's investment portfolio of \$255.4 million at March 31, 2010 consisted primarily of investment-grade bonds of \$18.0 million and its investment in DGI common stock. At March 31, 2010, DMIC owned 8,355,184 shares, or approximately 42%, of DGI's Class A common stock outstanding at that date, which DMIC carried on its books at March 31, 2010 at \$111.2 million, and 4,180,234 shares, or approximately 75%, of DGI's Class B common stock outstanding at that date, which DMIC carried on its books at March 31, 2010 at \$55.6 million.

***DGI***

DGI is a Delaware business corporation that DMIC formed in 1986 for the reasons described above. DGI currently has six insurance subsidiaries that offer personal and commercial lines of property and casualty coverages exclusively through a network of approximately 2,000 independent insurance agents. The personal lines products consist primarily of homeowners and private passenger automobile policies. The commercial lines products consist primarily of commercial automobile, commercial multi-peril and workers' compensation policies. At March 31, 2010, DGI had assets of \$936.0 million and shareholders' equity of \$385.4 million.

***DFSC***

DFSC is a Delaware business corporation formed in 2000 to own Province. DMIC owns 51.8% of DFSC and DGI owns 48.2% of DFSC. The Office of Thrift Supervision, or the OTS, is the primary federal regulator of Province and also regulates DMIC, DGI and DFSC as members of a unitary savings and loan holding company. DFSC does not currently conduct any business other than its ownership of the stock of Province.

***DAI***

DAI is a Delaware business corporation DFSC formed in April 2010 solely for the purpose of facilitating UNNF's merger with DFSC. DAI will conduct no business activities before or after the merger.

***Province***

Province is a federally chartered savings bank that DMIC and DGI formed in 2000. Province has three branch locations in western Lancaster County and focuses on providing community banking services, including residential and commercial real estate loans, small business loans and consumer loans. At March 31, 2010, Province had assets of \$102.5 million, \$84.5 million in deposits and shareholders' equity of \$17.5 million.

The location of the principal executive offices of the Donegal parties is 1195 River Road, Marietta, Pennsylvania, 17547. DGI's telephone number is (888) 877-0600 and DGI's website address is [www.donegalgroup.com](http://www.donegalgroup.com). The information on DGI's website is not a part of this proxy statement/prospectus.

**UNNF (Page 75)**



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We are a Pennsylvania business corporation UNCB formed in 1986 to serve as a bank holding company. We commenced business on January 2, 1987. Our primary business is the ownership and management of UNCB.

The location of our principal executive offices is 570 Lausch Lane, Suite 300, Lancaster, Pennsylvania 17601. Our telephone number is (717) 492-2222 and our website address is [www.uncb.com](http://www.uncb.com). The information on our website is not part of this proxy statement/prospectus.

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**Our Special Meeting (Page 71)**

This section contains information for our shareholders about the special meeting of shareholders we have called to consider the approval of the merger proposal and related matters.

**General (Page 71)**

We are furnishing this proxy statement/prospectus to you for use at our special meeting and any adjournment or postponement of our special meeting.

**When and Where We Will Hold Our Special Meeting (Page 71)**

We will hold our special meeting held on \_\_\_\_\_, 2010, at \_\_\_\_\_ a.m., prevailing time, at The Eden Resort Inn, 222 Eden Road, Lancaster, Pennsylvania, subject to any adjournment or postponement of our special meeting.

**The Matters Our Shareholders Will Consider (Page 71)**

The purpose of our special meeting is to consider and vote upon:

*Proposal 1* A proposal to adopt the merger agreement;

*Proposal 2* A proposal to grant discretionary authority to adjourn our special meeting if necessary to permit further solicitation of proxies because we have not received sufficient votes at the time of our special meeting to adopt the merger agreement; and

Any other business that properly comes before our special meeting and any adjournment or postponement of our special meeting.

Our shareholders must approve Proposal 1 for the merger to occur. If our shareholders fail to approve this proposal, the merger will not occur.

At this time, our board of directors is unaware of any other matters, other than as set forth above, that we will present for action at our special meeting. If a shareholder presents another matter in compliance with our by-laws, the persons named as proxies will vote in accordance with their judgment with respect to such matter.

**Record Date; Shares Outstanding and Entitled to Vote (Page 72)**

Our board of directors has fixed the close of business on \_\_\_\_\_, 2010 as the record date for the determination of holders of our common stock entitled to notice of, and to vote at, our special meeting and any adjournment or postponement of our special meeting.

On the record date, we had \_\_\_\_\_ issued and outstanding shares of our common stock entitled to vote at our special meeting, held by approximately \_\_\_\_\_ holders of record. Each holder is entitled to cast one vote for each share of our common stock held on all matters that come before our shareholders at our special meeting in compliance with our by-laws.

**Quorum (Page 72)**

The presence, in person or by properly executed proxy, of the holders of at least a majority of our outstanding shares of common stock on the record date is necessary to constitute a quorum at our special meeting. We will count abstentions for the purpose of determining whether a quorum is present. A quorum must be present in order for the vote on the merger proposal and the adjournment proposal to occur.

Based on the number of shares of our common stock issued and outstanding as of the record date,        shares of our common stock must be present in person or represented by proxy at our special meeting to constitute a quorum.

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**Shareholder Vote Required (Page 72)**

*Adopt the Merger Agreement.* The affirmative vote of the holders of 80% of our issued and outstanding common stock entitled to vote thereon is required to approve the adoption of the merger agreement. Accordingly, we urge you to complete, date and sign the accompanying proxy card and return it promptly in the enclosed postage-paid envelope.

When considering our board of directors' recommendation that you vote in favor of the adoption of the merger agreement, you should be aware that certain of our executive officers and directors have interests in the merger that may be different from, or in addition to, your interests as a shareholder. See *The Merger - Interests of Our Directors and Executive Officers in the Merger* beginning on page 94.

*Discretionary Authority to Adjourn Our Special Meeting.* The affirmative vote of the holders of a majority of the votes present, in person or by proxy, at our special meeting entitled to vote on the adjournment proposal is required to approve the proposal to grant discretionary authority to adjourn our special meeting if necessary to permit further solicitation of proxies for the merger proposal.

**Director and Executive Officer Voting (Page 73)**

As of the record date, our directors and executive officers and their affiliates beneficially owned 276,702 shares of our common stock, or approximately 9.7% of the issued and outstanding shares of our common stock entitled to vote at our special meeting.

**Proxies (Page 73)**

*Voting.* You should complete and return the proxy card accompanying this proxy statement/prospectus in order to ensure that your vote will be counted at our special meeting and at any adjournment or postponement of our special meeting, regardless of whether you plan to attend our special meeting. If you sign, date and return your proxy card and do not indicate how you want to vote, we will count your proxy card as a vote in favor of approval of the merger proposal and in favor of approval of the adjournment proposal.

If you hold your shares of our common stock in the name of a bank, broker, nominee or other holder of record, you will receive instructions from the bank, broker, nominee or other holder of record that you must follow in order for them to vote your shares of our common stock on your behalf.

*Revocability.* You may revoke your proxy at any time before we conduct the vote at our special meeting. If you have not voted through a bank, broker, nominee or other holder of record, you may revoke your proxy by:

- submitting written notice of revocation to our corporate secretary any time before we conduct the vote at our special meeting;
- submitting a properly executed proxy with a later date; or
- voting in person at our special meeting.

However, simply attending our special meeting without voting will not revoke an earlier proxy.

You should address any written notice of revocation and other communications regarding the revocation of your proxy to:

Union National Financial Corporation  
570 Lausch Lane, Suite 300  
Lancaster, Pennsylvania 17601  
Attention: Mary K. Rossi, Secretary

If you hold your shares in the name of a bank, broker, nominee or other holder of record, you should follow the instructions of the bank, broker, nominee or other holder of record regarding the revocation of proxies.

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The death or incapacity of a shareholder who executes and returns a proxy will not revoke that shareholder's proxy unless our corporate secretary receives notice of the death or incapacity of that shareholder before the proxies vote the shares of our common stock represented by such proxy.

*How We Count Proxies.* We will vote all shares of our common stock represented by properly executed and dated proxies received before or at our special meeting, and not revoked, in accordance with the instructions indicated in the proxies.

We will count a properly executed and dated proxy marked **ABSTAIN** as present for purposes of determining the presence of a quorum.

Brokers may not vote shares of our common stock that they hold of record either for or against the approval of the merger proposal or the adjournment proposal without specific instructions from the person who beneficially owns those shares. Therefore, if a broker holds your shares, you must give your broker instructions on how to vote your shares.

*Solicitation.* We will pay for the costs of our special meeting and for the mailing of this proxy statement/prospectus to our shareholders, as well as all other costs we incur in connection with the solicitation of proxies from our shareholders. However, DFSC and we will share equally the cost of printing this proxy statement/prospectus and the filing fees paid to the SEC.

In addition to soliciting proxies by mail, our directors, officers and employees and directors of Province may solicit proxies by telephone, over the internet or in person. We will not specially compensate our directors, officers and employees for these activities. We also intend to request that brokers, banks, nominees and other holders of record solicit proxies from their principals, and we will reimburse the brokers, banks, nominees and other holders of record for certain expenses they incur for those activities.

We have retained the firm of Georgeson, Inc. to assist us in the solicitation of proxies, and we have agreed to pay Georgeson, Inc. \$9,000, plus reimbursable expenses, for its services.

## **Recommendation of Our Board of Directors (Page 74)**

Our board of directors unanimously approved the merger agreement and the transactions the merger agreement contemplates. Based on our reasons for the merger we describe in this proxy statement/prospectus, our board of directors believes that the merger is advisable and in our and your best interests. Accordingly, our board of directors unanimously recommends that our shareholders vote **FOR** the merger proposal and **FOR** the adjournment proposal. See *The Merger Our Board of Directors Reasons for the Merger; Recommendation* beginning on page 82, for a more detailed discussion of our board of directors' recommendation.

## **Attending Our Special Meeting (Page 74)**

If you hold your shares in street name and you want to attend our special meeting, you must bring an account statement or letter from your holder of record showing that you were the beneficial owner of the shares on \_\_\_\_\_, 2010, the record date for our special meeting.

## **The Merger**

## **Certain Effects of the Merger (Pages 100 to 101)**

Upon consummation of the merger:

Each share of our common stock, other than the shares DMIC owns and shares held by holders who perfect dissenters' rights, will automatically convert into the right to receive, subject to the provisions of the merger agreement:

0.2134 share of DGI Class A common stock; and

\$5.05 in cash.

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We will cease to exist as a separate legal entity and DFSC and Province will conduct all of our operations. Province will conduct its banking business under a name that DFSC and we will select.

**Stock Options (Page 101)**

The merger agreement provides that we will use commercially reasonable efforts to obtain from each holder of an option to purchase our common stock such holder's consent to the surrender and cancellation of such option prior to the effective date of the merger.

**Opinion of Our Financial Advisor in Connection with the Merger (Pages 84 to 92)**

Sandler O'Neill, our independent financial advisor in connection with the merger, delivered a written fairness opinion to our board of directors on April 19, 2010, the date we executed the merger agreement, that, as of April 19, 2010, and based upon and subject to the factors and assumptions set forth in Sandler O'Neill's opinion, the merger consideration in the merger is fair, from a financial point of view, to the holders of shares of our common stock.

Appendix B to this proxy statement/prospectus sets forth the full text of the Sandler O'Neill opinion and includes the assumptions Sandler O'Neill made, the procedures Sandler O'Neill followed, the matters Sandler O'Neill considered and the limitations on the review Sandler O'Neill undertook in connection with its opinion. **Sandler O'Neill provided its opinion for the information and assistance of our board of directors in connection with its consideration of the merger. The Sandler O'Neill opinion is not a recommendation as to how you should vote with respect to the merger or any related matter.** We encourage you to read the Sandler O'Neill opinion in its entirety.

**Interests of Our Directors and Executive Officers in the Merger (Page 94)**

In considering the recommendation of our board of directors that you vote **FOR** the merger proposal and **FOR** the adjournment proposal, you should be aware that certain of our executive officers and directors have employment and other compensation agreements or plans that give them interests in the merger that are different from, or in addition to, your interests as a shareholder. These interests relate to or arise from, among other things:

the continued indemnification of our current directors and executive officers under the merger agreement and providing these individuals with directors' and officers' insurance;

the agreement of DFSC and Province to honor the existing employment and change of control agreements for eight of our officers, including our executive officers, unless and until such officers individually determine to execute a mutually acceptable employment agreement with DFSC and Province;

the agreement of DFSC and Province to honor Mr. Gainer's existing employment agreement and amended and restated executive salary continuation agreement, or the salary agreement, unless and until Mr. Gainer, DFSC and Province execute a mutually acceptable employment agreement and a mutually acceptable amended and restated salary agreement;

the appointment of Mark D. Gainer and two other current members of our board of directors to DFSC's board of directors and their receipt of directors' fees in connection therewith; and

the appointment of Mark D. Gainer and four other current members of UNCB's board of directors to the board of directors of Province and their receipt of directors' fees in connection therewith.



**Regulatory Approvals Required for the Merger (Page 95)**

We cannot complete the merger without the prior approval of the Office of Thrift Supervision, or OTS, and notice to the Pennsylvania Department of Banking, or the Department. DFSC is in the process of supplying the pro forma financial information the OTS has requested prior to the submission of a formal application for approval of the merger and providing the requisite notice to the Department. While DFSC does

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not know of any reason why the OTS would not grant the necessary approval in a timely manner, we can give you no assurance that the OTS will approve the merger, at all or on a timely basis or that such approval would not be subject to one or more burdensome conditions that would entitle DFSC to terminate the merger agreement. DMIC will not be required to obtain any approval from the Pennsylvania Insurance Department in connection with the merger.

**Conditions to the Merger (Page 106)**

Currently, we expect to complete the merger in the third quarter of 2010. However, the completion of the merger depends on the satisfaction of a number of conditions or, where legally permissible, the waiver of those conditions. These conditions include, among others:

approval of the merger proposal by the holders of 80% of our outstanding shares of common stock entitled to vote at our special meeting;

subject to certain limited exceptions and except as otherwise previously disclosed to the other party, the representations and warranties of the parties to the merger agreement must be true and correct unless the failure of the representations and warranties to be true and correct would not have and would not reasonably be expected to have, individually or in the aggregate, a material adverse effect on the representing party;

the receipt of all regulatory approvals needed to complete the merger, including the approval of the OTS and the provision of specified notice to the Department, and the absence of the imposition of materially burdensome conditions by the OTS and any other regulatory agencies whose regulatory approval is necessary for the completion of the merger;

the absence of any law, statute, rule, regulation, order, decree or injunction that would effectively prohibit the merger or make completion of the merger illegal;

DGI's registration statement, of which this proxy statement/prospectus forms a part, shall have become effective and no stop order suspending its effectiveness shall have been issued and the SEC shall not have initiated or threatened any proceedings for that purpose;

UNCB shall not have delinquent loans, as defined in the merger agreement, that exceed \$37.5 million as of the end of the month preceding the month in which the closing of the merger is scheduled to occur;

NASDAQ shall have approved for listing the shares of DGI Class A common stock that DFSC will distribute to our shareholders as part of the merger consideration;

DFSC shall have delivered the merger consideration to the exchange agent not later than the day prior to the closing date; and

DFSC and we shall have received all necessary third party consents.

Although we anticipate the closing of the merger will occur during the third quarter of 2010, because the satisfaction of certain conditions to the merger is beyond our control, neither DFSC nor we can be certain when, or if, DFSC and we can satisfy the conditions to the merger, or agree to waive such conditions or whether or not we will be able to complete the merger.

**Non-Solicitation (Page 105)**

Subject to certain exceptions, we have agreed not to initiate, solicit, induce or knowingly encourage any third party to make any inquiries or proposals to acquire us or enter into an agreement to acquire us with a third party. However, the merger agreement does permit us, under specified circumstances, to respond to an acquisition proposal we have not solicited or an inquiry from a third party, which our board of directors believes in good faith is or is reasonably likely to result in a merger proposal that is superior to the DFSC merger proposal. In those specified circumstances, we may furnish the third party with information about us and conduct negotiations with such third party.

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**Litigation Related to the Merger (Page 108)**

Certain litigation is pending in connection with the Merger. See The Merger Litigation Related to the Merger.

**Termination of the Merger Agreement (Page 107)**

We and DFSC may mutually agree to terminate the merger agreement before completing the merger, even after our shareholders approve the merger proposal.

Either DFSC or we may terminate the merger agreement, even after our shareholders approve the merger proposal, if certain conditions have not been met, such as:

failure to obtain the necessary regulatory approvals for the merger unless the failure is due to the terminating party's failure to perform or observe its covenants in the merger agreement;

failure to complete the merger by December 31, 2010, unless the reason for the failure not to consummate the merger by that date is a failure by the terminating party to perform or observe its covenants and agreements in the merger agreement;

the non-terminating party's breach of a representation, warranty, covenant, agreement or other obligation contained in the merger agreement that would make it impossible to satisfy the closing conditions, provided the terminating party is not then in material breach of any of its representations, warranties, covenants, agreements or other obligations in the merger agreement; or

failure of the holders of 80% of our outstanding common stock to approve the merger proposal, provided we are not in material breach of our obligations to hold our special meeting and our board of directors is not in breach of its covenant to recommend such approval.

DFSC may terminate the merger agreement at any time prior to our special meeting if we have:

breached our obligation not to initiate, solicit or encourage or take any action to facilitate another proposal to acquire us, participate in any discussions or negotiations relating to another proposal to acquire us or, except as permitted by and subject to certain terms of the merger agreement, approve, recommend or enter into any letter of intent, agreement or other commitment relating to another proposal to acquire us;

failed to have our board of directors recommend approval of the merger proposal by our shareholders or our board of directors shall have changed its recommendation, except as permitted by the merger agreement with respect to a proposal to acquire us on terms and conditions superior to those in the merger agreement;

recommended approval of another proposal to acquire us; or

failed to call, give notice of, convene and hold our special meeting.

We may terminate the agreement at any time prior to the mailing date of this proxy statement/prospectus our special meeting in order to enter into an agreement relating to an acquisition proposal that has terms superior to those of the merger agreement from the perspective of our shareholders.

Except as provided below with respect to termination fees and expenses and the parties' respective confidentiality obligations in the event DFSC or we terminate the merger agreement, neither of us will have any liability or obligation other than liabilities or damages incurred by either of us as a result of our willful breach of any of our respective representations, warranties, covenants or agreements contained in the merger agreement.

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**Expenses; Termination Fee (Page 108)**

The merger agreement provides that we will pay DFSC a termination fee of \$800,000 if:

we terminate the merger agreement in order to enter into an agreement relating to an acquisition proposal that has terms superior to those of the merger agreement from the perspective of our shareholders;

DFSC terminates the merger agreement prior to our special meeting because we have breached our obligation not to encourage or solicit acquisition proposals, we have failed to hold our special meeting or our board of directors has not recommended approval of the merger proposal or has changed its recommendation or has recommended approval of another proposal to acquire us or we fail to hold our special meeting;

a third party makes a tender or exchange offer for 25% or more of our common stock and our board of directors fails to send a statement to our shareholders recommending rejection of that offer within 10 days after the making of the offer; or

the occurrence of any of the following events within 18 months after the termination of the merger agreement, provided that a third party makes a proposal to acquire us after April 19, 2010 and does not withdraw its proposal prior to termination of the merger agreement:

we enter into an agreement to merge with or be acquired by that third party;

that third party acquires substantially all of our assets; or

that third party acquires more than 50% of our common stock.

The merger agreement also provides that upon termination:

by us because DFSC breached its representations, warranties, covenants, agreements or other obligations in the merger agreement, which breach could reasonably be expected to result in a material adverse effect and which breach cannot be or is not cured, assuming we are also not in material breach of our obligations under the merger agreement, DFSC will pay our out-of-pocket expenses in connection with the merger, including fees and expenses of legal counsel, financial advisors and accountants, up to a maximum of \$500,000; and

by DFSC because we breached our representations, warranties, covenants, agreements or other obligations in the merger agreement which breach could reasonably be expected to result in a material adverse effect and which breach cannot be or is not cured, assuming DFSC is also not in material breach of its obligations under the merger agreement, we will pay DFSC's out-of-pocket expenses in connection with the merger, including fees and expenses of legal counsel, financial advisors and accountants, up to a maximum of \$500,000, provided, however, that we do not have to pay DFSC's expenses if we have paid the break-up fee to DFSC.

**Material U.S. Federal Income Tax Consequences of the Merger (Pages 109 to 111)**

The merger will be a taxable transaction to our shareholders for U.S. federal income tax purposes. Each shareholder will generally recognize gain or loss equal to the difference between the amount of cash plus the fair market value, determined at the effective time of the merger, of the DGI Class A common stock such shareholder receives and the holder's tax basis in our common stock surrendered in the merger. The tax consequences of the merger may vary

depending on the particular holder's circumstances. We urge each of you to consult your own tax advisor with respect to the tax consequences of the merger.

**Dividends (Page 123)**

DGI paid cash dividends on its Class A common stock totaling \$0.45 per share for 2009. Based on the exchange ratio and DGI's current Class A annual dividend rate of \$0.46 per share, holders of our common stock can anticipate receiving a dividend at an annual rate of \$.098 per share. We have not paid any dividends

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on our common stock since 2007. Although DGI has no current plan or intention to change its Class A dividend rate, DGI's board of directors may, subject to applicable law, change its dividend rate in the future. DGI's ability to pay dividends on its common stock is subject to various legal and regulatory limitations.

**Certain Differences in Rights of Shareholders (Pages 112 to 123)**

When we and DFSC complete the merger, Delaware law and DGI's certificate of incorporation and by-laws will govern the rights of our shareholders rather than Pennsylvania law and our articles of incorporation and by-laws.

**Comparative Market Prices and Dividends (Page 123)**

DGI's Class A common stock trades on the NASDAQ Global Select Market under the symbol DGICA. Our common stock trades on the OTCBB, under the symbol UNNF.OB. The table on page lists the quarterly price range of DGI Class A common stock and our common stock since January 1, 2008 as well as the quarterly cash dividends DGI has paid on its Class A common stock and we have paid on our common stock since that date. The following table shows the closing price of DGI Class A common stock and our common stock as reported on April 19, 2010, the last trading day before DFSC and we announced the merger, and on , 2010, the last practicable trading day before the date of mailing of this proxy statement/prospectus. This table also shows the pro forma equivalent value of the merger consideration for each share of our common stock, which we calculated by multiplying the closing price of DGI Class A common stock on those dates by 0.2134, the exchange ratio for the stock portion of the merger consideration, and adding \$5.05 in cash.

	<b>DGI Class A Common Stock</b>	<b>Our Common Stock</b>	<b>Pro Forma Equivalent Value of One Share of Our Common Stock</b>
April 19, 2010 , 2010	\$ 14.68	\$ 6.00	\$ 8.18

The market price of DGI Class A common stock may change at any time. Consequently, the total dollar value of the DGI Class A common stock that you will be entitled to receive as a portion of the merger consideration may be higher or lower than its current value. We urge you to obtain a current market quotation for DGI Class A common stock. We make no representation as to the future price of DGI Class A common stock.

**Dissenters Rights (Page 98)**

Our shareholders have dissenters rights under the PBCL and, if a shareholder does not vote in favor of the merger proposal, that shareholder can seek the appraised fair value of his or her shares in a judicial proceeding.

**Questions and Additional Information (Page 74)**

If you have questions about the merger or how to submit your proxy card, or if you need additional copies of this proxy statement/prospectus or the enclosed proxy card, please call Michael D. Peduzzi, our Executive Vice President and Chief Financial Officer, at (877) 653-1441 or Georgeson, Inc., the proxy soliciting firm we have retained, at .





**Table of Contents****SELECTED CONSOLIDATED HISTORICAL FINANCIAL DATA OF DGI**

Set forth below are highlights from DGI's consolidated financial data as of and for the years ended December 31, 2005 through 2009 and DGI's unaudited consolidated financial data as of and for the three months ended March 31, 2009 and 2010. DGI's results of operations for the three months ended March 31, 2010 are not necessarily indicative of DGI's results of operations for the full year of 2010. DGI management prepared the unaudited information on the same basis as it prepared DGI's audited consolidated financial statements. In the opinion of DGI's management, this information reflects all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of this data for these periods. You should read this information in conjunction with DGI's consolidated financial statements and related notes included in DGI's Annual Report on Form 10-K for the year ended December 31, 2009 and DGI's Quarterly Report on Form 10-Q for the three months ended March 31, 2010 which we incorporate by reference in this proxy statement/prospectus and from which we derived this information. See "Where You Can Find More Information" on page v.

**Selected Consolidated Historical Financial Data of DGI**

	<b>Three Months Ended March 31,</b>		<b>Year Ended December 31,</b>				
	<b>2010</b>	<b>2009</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
	<b>(Dollars in thousands, except per share amounts)</b>						
<b>INCOME STATEMENT DATA</b>							
Premiums earned	\$ 91,372	\$ 88,350	\$ 355,025	\$ 346,575	\$ 310,072	\$ 301,478	\$ 294,498
Investment income, net	4,930	5,358	20,631	22,756	22,785	21,320	18,472
Realized investment gains (losses)	22	259	4,480	(2,971)	2,051	1,830	1,803
Total revenues	97,915	95,502	386,733	372,424	340,618	329,967	319,847
Income before income taxes	276	212	20,677	32,092	52,849	56,622	52,345
Income taxes	41	42	1,847	6,550	14,569	16,408	15,396
Net income	235	170	18,830	25,542	38,280	40,215	36,949
Basic earnings per share Class A	0.01	0.01	0.76	1.03	1.55	1.65	1.57
Diluted earnings per share Class A	0.01	0.01	0.76	1.02	1.53	1.60	1.51
Cash dividends per share Class A			0.45	0.42	0.36	0.33	0.30
Basic earnings per share Class B	0.01	0.01	0.68	0.92	1.39	1.48	1.41
Diluted earnings per share Class B	0.01	0.01	0.68	0.92	1.39	1.48	1.41
Cash dividends per share Class B			0.40	0.37	0.31	0.28	0.26

BALANCE SHEET  
DATA AT END OF  
PERIOD

Total investments	657,735	639,618	666,835	632,136	605,870	591,338	547,746
Total assets	936,025	890,379	935,602	880,109	834,096	831,698	781,422
Debt obligations	15,465	15,465	15,465	15,465	30,929	30,929	30,929
Stockholders equity	385,428	368,350	385,506	363,584	352,690	320,802	277,896
Book value per share	15.11	14.47	15.12	14.29	13.92	12.70	11.30

**Table of Contents****SELECTED CONSOLIDATED HISTORICAL FINANCIAL DATA OF UNNF**

Set forth below are highlights from UNNF's consolidated financial data as of and for the years ended December 31, 2005 through December 31, 2009 and UNNF's unaudited consolidated financial data as of and for the three months ended March 31, 2009 and 2010. The results of operations for the three months ended March 31, 2010 are not necessarily indicative of the results of operations of UNNF for the full year of 2010. UNNF management prepared the unaudited information on the same basis as it prepared UNNF's audited consolidated financial statements. In the opinion of UNNF's management, this information reflects all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of this data for these periods. You should read this information in conjunction with UNNF's consolidated financial statements and related notes included elsewhere in this proxy statement/prospectus and from which we derived this information. See **Where You Can Find More Information** on page v and the Index to the UNNF Consolidated Financial Statements on page F-1.

**Selected Consolidated Historical Financial Data of UNNF**

	<b>Three Months Ended March 31,</b>		<b>Year Ended December 31,</b>				
	<b>2010</b>	<b>2009</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
	<b>(Dollars in thousands, except per share amounts)</b>						
<b>Summary of Operations Data:</b>							
Interest income	\$ 5,522	\$ 6,049	\$ 23,758	\$ 28,173	\$ 31,373	\$ 30,290	\$ 23,978
Interest expense	2,263	3,178	11,286	13,579	16,009	15,626	9,662
Net interest income	3,259	2,871	12,472	14,594	15,634	14,664	14,316
Provision for credit losses	496	313	2,627	1,027	1,237	672	681
Net interest income after provision for credit losses	2,763	2,558	9,845	13,567	14,127	13,992	13,635
Non-interest income	1,180	619	5,375	3,807	6,509	8,262	6,011
Non-interest expense	4,022	4,014	16,737	17,118	20,745	19,711	15,627
(Loss) income before income taxes (benefit)	(79)	(837)	(1,517)	256	(109)	2,543	4,019
Benefit from provision for income taxes	(82)	(328)	(802)	(188)	(421)	99	666
Net (loss) income	3	(509)	(715)	444	312	2,444	3,353
Preferred stock dividends	18						
<b>Net (loss) income available to common shareholders</b>	<b>(15)</b>	<b>(509)</b>	<b>(715)</b>	<b>444</b>	<b>312</b>	<b>2,444</b>	<b>3,353</b>
<b>Per Share Data:</b>							
(Loss) earnings per common share	\$ (0.01)	\$ (0.19)	\$ (0.26)	\$ 0.17	\$ 0.12	\$ 0.96	\$ 1.31

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Dividends paid					0.28	0.62	0.63
Book value per share at period end	11.11	11.37	10.97	11.32	11.31	11.31	10.84
Average number of shares outstanding basic and diluted (in thousands)	2,742	2,721	2,730	2,643	2,544	2,537	2,556
<b>Statement of Condition Data (at end of period):</b>							
Assets	\$499,931	\$ 510,922	\$ 489,644	\$ 485,109	\$ 501,776	\$ 517,597	\$ 462,178
Net loans and leases	327,033	351,970	333,416	353,922	360,662	338,043	297,538
Deposits	416,925	407,889	404,765	383,577	376,311	340,075	296,610
Short-term borrowings					6,629	10,544	18,305
Long-term debt	30,834	50,334	33,334	50,334	68,816	117,571	105,815
Junior subordinated debentures	17,341	17,341	17,341	17,341	17,341	17,341	11,341
Total stockholders equity	31,278	30,929	31,336	30,794	28,800	28,548	27,225
<b>Financial Ratios:</b> (Annualized)							
Return on average assets	0.00%	(0.41)%	(0.14)%	0.09%	0.06%	0.50%	0.79%
Return on average equity	0.04	(6.47)	(2.26)	1.48	1.07	8.81	12.59
Ratio of average equity to average assets	6.53	6.31	6.29	6.15	6.05	5.67	6.25

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

The following discussion provides management's analysis of UNNF'S financial condition and results of operations for the three-month periods ended March 31, 2009 and 2010 and for the years ended December 31, 2007, 2008 and 2009. The UNNF financial statements and accompanying notes included elsewhere in this proxy statement/prospectus are an integral part of this discussion and should be read in conjunction with it.

**Overview**

Management's discussion and analysis represents an overview of the financial condition and results of operations, and highlights the significant changes in the financial condition and results of operations, as presented in the accompanying consolidated financial statements for UNNF, a bank holding company, and its wholly owned subsidiary, UNCB. UNNF's consolidated financial condition and results of operations consist primarily of UNCB's financial condition and results of operations. UNNF's trust subsidiaries, Union National Capital Trust I and Union National Capital Trust II, were established for the purpose of issuing \$11,000,000 of trust capital securities during 2003 and 2004.

**Forward Looking Statements**

These financial statements contain forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Actual results and trends of UNNF and UNCB could differ materially from those set forth in such statements due to various risks, uncertainties and other factors. Such risks, uncertainties and other factors that could cause actual results and experience to differ include, but are not limited to, the following:

strategic initiatives and business plans, including prospective business combinations, may not be satisfactorily completed or executed, if at all;

increased demand or prices for UNCB's financial services and products may not occur;

changing economic and competitive conditions;

technological developments;

the effectiveness of UNNF's business strategy due to changes in current or future market conditions;

actions of the U.S. government, the FRB, the OCC and other governmental and regulatory bodies for the purpose of stabilizing the financial markets; enforcement actions with bank regulatory agencies restricting certain transactions of UNNF and UNCB;

effects of deterioration of economic conditions on customers, specifically the effect on the ability of loan customers to repay loans;

UNNF's inability to raise or achieve desired or required levels of regulatory capital; paying significantly higher FDIC premiums in the future;

the effects of competition, and of changes in laws and regulations, including industry consolidation and development of competing financial products and services;

interest rate movements;

relationships with customers and employees;

challenges in establishing and maintaining operations;

volatilities in the securities markets and related potential impairments of investment securities;

deteriorating economic conditions and declines in housing prices and real estate values; and

other risks and uncertainties, including those described in UNNF's filings with the SEC.

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When we use words such as *believes*, *expects*, *anticipates*, or similar expressions, we are making forward-looking statements. UNNF undertakes no obligation to publicly revise or update these forward-looking statements to reflect events or circumstances that arise after the date of this report.

Readers should carefully review the risk factors described in the Annual Report and other documents that we periodically file with the SEC, including our Form 10-K for the year ended December 31, 2009, our Forms 8-K, and other reports, that we have filed during 2010 with the SEC.

### **Three Months Ended March 31, 2010 to Three Months Ended March 31, 2009**

#### **Critical Accounting Policies**

We prepare our consolidated financial statements based upon the application of U.S. generally accepted accounting principles, or GAAP. The reporting of our financial condition and results of operations is impacted by the application of accounting policies by management, some of which are particularly sensitive and require significant judgments, estimates and assumptions to be made in matters that are inherently uncertain. These accounting policies, along with the disclosures presented in other financial statement notes and in this financial review, provide information on how significant assets and liabilities are valued in the financial statements and how those values are determined. Management views critical accounting policies to be those which are highly dependent on subjective or complex judgments, estimates and assumptions, and where changes in those estimates and assumptions could have a significant impact on the consolidated financial statements. Management currently views the determination of the allowance for credit losses, the fair value of investment securities and the fair value of other real estate owned to be critical accounting policies.

#### ***Determination of the Allowance for Credit Losses***

The provision for credit losses and the level of the allowance for credit losses involve significant estimates by management. In evaluating the adequacy of the allowance for credit losses, management considers the specific collectability of impaired and nonperforming loans, past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect borrowers' ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant qualitative factors. While we use available information to make such evaluations, future adjustments to the allowance for credit losses and the provision for credit losses may be necessary if economic conditions, loan credit quality, or collateral issues differ substantially from the factors and assumptions used in making the evaluation.

#### ***Fair Value of Investment Securities***

Investments are carried at fair value with any unrealized gains and losses, considered to be temporary, reported net of tax as an adjustment to stockholders' equity. In order to determine whether unrealized losses in the fair value of investment securities reflect other-than-temporary impairment, or OTTI, management regularly reviews the entire portfolio of investment securities for possible impairment, analyzing factors including, but not limited to, the underlying creditworthiness of the issuing organization, the length of time for which the fair value of the investment securities may be less than cost, and independent analysts' opinions about circumstances that could affect the performance of the investment securities. In assessing potential OTTI for debt securities with fair values less than cost, other considerations include (i) whether management intends to sell the security, or (ii) if it is more likely than not that management will be required to sell the security before recovery, or (iii) if management does not expect to recover the entire amortized cost basis. In assessing potential OTTI for equity securities with fair values less than cost, consideration is given to management's intention and ability to hold the securities until recovery of any unrealized



losses. After considering such factors, it is a matter of judgment on the part of management to make the determination of whether or not the decline in market value is other-than-temporary.

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### ***Fair Value of Other Real Estate Owned***

Other Real Estate Owned, or OREO, includes property acquired through foreclosure, deed in-lieu of foreclosure, and an in-substance foreclosure. OREO is held for sale. The carrying value of the property is recorded at the fair value of the property as determined based upon an independent appraisal, less estimated costs to sell at the time of acquisition. Any excess of the loan balance over the carrying value of the property at the time of transfer from loans to OREO is charged to the allowance for credit losses. Subsequent to the transfer to OREO, if the sales price of the property less actual costs to sell is less than the carrying value of the property, the deficiency is charged against income as a loss on sale. Due to changing market conditions, there are inherent uncertainties upon liquidation with respect to determining the fair value of OREO. Therefore, the amount ultimately realized upon liquidation may differ from the carrying value reflected in the accompanying consolidated financial statements.

### **Financial Condition**

Total assets increased by \$10,287,000 or 2% to \$499,931,000 at March 31, 2010, from \$489,644,000 at December 31, 2009. The increase was primarily the result of strong retail deposit generation, which further strengthened our liquidity position. Total deposits grew by \$12,160,000 or 3% to \$416,925,000 at March 31, 2010 from \$404,765,000 at December 31, 2009.

### **Investment Securities**

Investment securities were \$60,757,000 at March 31, 2010, compared to \$60,546,000 at December 31, 2009. All of our investment securities were classified as available for sale at March 31, 2010 and December 31, 2009. Investment securities classified as available for sale are marketable equity securities, and those debt securities that we intend to hold for an undefined period of time, but not necessarily to maturity. In addition to the investment portfolio generating interest income, it serves other primary financial management functions such as a reliable source of liquidity and a tool to manage interest rate risk. In order to support these functions, the entire investment securities portfolio has been designated as being available for sale. Any decision to sell an available-for-sale investment security would be based on various factors, including significant movements in interest rates, changes in maturity mix of assets and liabilities, liquidity needs, regulatory capital considerations, reasonable gain realization, changes in the creditworthiness of the issuing entity, changes in investment strategy and portfolio mix, and other similar factors. Changes in unrealized gains or losses on available-for-sale investment securities, net of taxes, are recorded as other comprehensive (loss) income, a component of stockholders' equity.

Certain types of mortgage-backed and asset-backed securities are purchased to better position the investment securities portfolio for a subsequent increase or decrease in interest rates, as aligned with our interest rate risk position. These investment securities may be purchased at premiums or discounts, with short, mid, or long-term average expected lives or maturities. Overall yields on these investment securities will increase or decrease based on changes in prepayment speeds and subsequent cash flow reinvestments.

Investment security purchases and sales generally occur to manage UNCB's liquidity requirements, pledging requirements, interest rate risk, and to enhance net interest margin and capital management. The investment securities portfolio is evaluated regularly for possible opportunities to increase earnings through potential sales or portfolio repositioning. In the first three months of 2010, proceeds of \$16,479,000 were received on sales, and \$77,000 was recognized in net gains, while \$18,644,000 of investment securities were purchased. Investment securities of \$57,793,000 and \$57,209,000 were pledged to secure public, trust, and government deposits and for other purposes at March 31, 2010 and December 31, 2009, respectively.

In addition to the credit risk present in the loan portfolio, we also have credit risk associated with our investment security holdings. Based on recent national economic trends and other factors, the private issuer mortgage-backed securities and corporate debt securities credit ratings as published by national statistical rating organizations are being monitored closely.

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Investment securities consisted of the following at of March 31, 2010 and December 31, 2009, (in thousands):

	<b>March 31, 2010</b>	<b>December 31, 2009</b>
Market Value of Debt Securities	\$ 60,690	\$ 60,478
Market Value of Equity Securities	67	68
Total Market Value of Investment Securities	\$ 60,757	\$ 60,546

Debt securities include mortgage-backed securities, obligations of state and political subdivisions, obligations of U.S. government agencies, structured notes and corporate securities. At March 31, 2010, there were fifteen debt securities with unrealized losses of \$153,000 that amounted to 0.4% of their amortized cost, compared to December 31, 2009, when there were twenty-seven debt securities with unrealized losses of \$585,000 that amounted to 1.3% of their amortized cost. Management believes that the unrealized losses reflect temporary declines primarily due to changes in interest rates subsequent to the acquisition of specific securities. These temporary declines have been provided for in other comprehensive income (loss). All of the obligations of state and political subdivisions outstanding at December 31, 2009, were sold in 2010, and as a result of positive market movements, no losses were recognized on the sale of these securities.

Equity securities held are comprised primarily of common stock holdings in other financial institutions. There were nine and ten equity securities with unrealized losses of \$11,000, at both March 31, 2010 and December 31, 2009, respectively. We have the ability and intent to hold these investments for a reasonable period of time sufficient for the fair value of each equity security to increase to our cost. Management does not consider the equity securities to be other-than-temporarily impaired at March 31, 2010.

As of March 31, 2010, \$12,000 of the fair value of the total investment securities portfolio was measured using Level 1 inputs as defined by fair value measurement and disclosure guidance, \$57,848,000 or 95% of the fair value of total investment securities was measured using Level 2 inputs, and \$2,897,000 or 5% of the fair value of total investment securities was measured using Level 3 inputs. For additional information, refer to Note 12 Fair Value Measurement of Assets and Liabilities and Fair Value of Financial Instruments to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

The fair value of Level 3 investment securities decreased to \$2,897,000 at March 31, 2010, compared to \$3,269,000 at December 31, 2009. Of the decrease in value, \$272,000 was related to net proceeds received on the sale of an impaired security, \$172,000 was related to principal and interest payments received and fully applied to principal, offset by \$72,000 of net unrealized gains (with a corresponding after-tax increase to stockholders' equity of \$48,000 recorded as other comprehensive income).

In order to determine whether unrealized losses in the fair value of investment securities are OTTI, management regularly reviews the entire portfolio of investment securities for possible impairment, analyzing factors including but not limited to the underlying creditworthiness of the issuing organization, the length of time for which the fair value of the investment securities has been less than cost, and independent analysts' opinions about circumstances that could affect the performance of the investment securities. In assessing potential OTTI for debt securities, other considerations include (i) whether management intends to sell the security, or (ii) if it is more likely than not that management will be required to sell the security before recovery, or (iii) if management does not expect to recover the entire amortized cost basis. In assessing potential OTTI for equity securities, consideration is given to management's

intention and ability to hold the securities until recovery of any unrealized losses.

As of March 31, 2010, our recorded investment balances include three securities with previously recorded impairments. The fair value of these impaired investments was \$2,897,000 at March 31, 2010, compared to an original amortized cost of \$6,950,000. All principal and interest payments received on impaired investment securities are fully applied to principal.

Accounting Standards Codification, or ASC, Topic 320, Investments – Debt and Equity Securities provides a list of factors that a reporting entity should evaluate to determine whether there has been a

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significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is needed and significant adjustments to the related prices may be necessary to estimate fair value in accordance with fair value measurement and disclosure guidance. Further, fair value measurement and disclosure guidance clarifies that when there has been a significant decrease in the volume and level of activity for the asset or liability, some transactions may not be orderly, and we must evaluate the weight of evidence to determine whether the transactions are orderly. The guidance provides a list of circumstances that may indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value.

As discussed more thoroughly in Note 12 Fair Value of Assets and Liabilities and Fair Value of Financial Instruments to the consolidated financial statements included elsewhere in this proxy statement/prospectus, the fair value of these investment securities was determined by calculating the net present value of the expected future cash flows of each security, with qualitative risk-adjusted discounting for potential credit risks and nonperformance in the underlying issuers, and market sector illiquidity concerns. In accordance with ASC Topic 820, when an active market for a security does not exist, the use of management estimates that incorporate current market participant expectations of future cash flows, and include appropriate risk premiums, is acceptable. Management's judgment was that, as of March 31, 2010 and December 31, 2009, the facts and circumstances indicated significant illiquidity and an inactive market for these types of investments when other relevant observable inputs were not available; therefore, expected cash flows were used as a reasonable basis in determining the fair value of the corporate investment securities.

During 2009, four of UNCB's five private issuer securities were downgraded to below investment grade (one private issuer mortgage-backed security was downgraded to below investment grade in 2008). Accordingly, UNCB recorded \$1,504,000 of other-than-temporary impairment charges in 2009 including (i) \$859,000 related to three corporate securities supported primarily by obligations from other financial industry entities, and (ii) \$645,000 related to two private issuer mortgage-backed securities not guaranteed by the U.S. government. During 2008, we recorded \$1,290,000 of other-than-temporary investment impairment charges related to two securities, including the private-issuer security that was downgraded to below-investment-grade in 2008, and a corporate security. Management determined that, due to severe illiquidity and distress in the financial markets, the unrealized declines in the value of these investments were other-than-temporary and credit related, requiring the write-down and related impairment charge to earnings. For the securities with impairment charges recorded, interest income payments received subsequent to impairment are fully applied to principal further reducing the amortized cost of these investments.

During 2009, one of the previously impaired corporate securities (USCap Funding V) was fully impaired, completely written-off and declared as a worthless asset for tax purposes. This impaired corporate security had a cumulative credit related OTTI of \$936,000 at December 31, 2009. During 2010, another one of the previously impaired corporate securities (InCaps Funding II Senior Note) was sold for \$277,000, leaving UNCB with a total of three impaired investment securities remaining at March 31, 2010. At the time of the sale, the InCaps Funding II Senior Note security had \$631,000 of previously recorded impairments and an adjusted amortized cost of \$272,000, which resulted in a \$5,000 gain that was recorded on the sale.

Management determined that further impairments as of March 31, 2010 were not warranted on the three remaining impaired investment securities based upon the following considerations:

All three impaired investment securities were current, as of March 31, 2010, for scheduled investment payments. Based upon the information reviewed by management in preparing the financial statements, the financial condition and near-term prospects of the issuers do not reflect any specific events which may have influenced the operations of the issuers, such as changes in technology or a discontinuance of a business

segment that may have further impaired the earnings potential of the investments.

The securities experienced very limited trading activity during the last 12 months being in a market sector with a high degree of illiquidity and dislocation; therefore, determining fair value based upon discounted cash flows is considered reasonable.

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Management does not intend to sell the securities, and it is not likely that management will be required to sell the securities before recovery to their adjusted amortized cost, and though management does not expect to recover the original amortized cost of the securities, management expects to hold the securities until a reasonable recovery towards the current carrying value.

**Loans and Leases, Credit Quality and Credit Risk**

Loans and leases at March 31, 2010 were \$333,028,000 compared to \$339,274,000 at December 31, 2009. Outstanding loans decreased by \$6,246,000 from December 31, 2009 to March 31, 2010, primarily due to reduced loan demand from creditworthy borrowers and the impact of certain loans at December 31, 2009, that subsequently involved collateral foreclosure and were classified as OREO at March 31, 2010, in the Consolidated Statements of Financial Condition (for additional information, refer to the discussion on Non-Performing Assets on page 21). We continue to focus lending on creditworthy consumers and businesses, with necessary consideration given to increased credit risks posed by the weak economy and the housing market. The economy and housing market, and increased unemployment, could affect some of UNCB's borrowers, and may result in increased nonperforming loans and credit losses.

At March 31, 2010, UNCB had \$68,708,000 of loans specifically pledged to the Federal Home Loan Bank of Pittsburgh, or FHLB, for providing collateral on FHLB long-term debt, compared to \$72,287,000 of pledged loans at December 31, 2009.

**Allowance for Credit Losses**

In accordance with GAAP, the allowance for credit losses is maintained at a level believed by management to be adequate to absorb estimated probable loan and lease principal losses. The allowance for credit losses is established through provisions charged against net interest income. The uncollectible principal portion of impaired loans and leases is charged against the allowance for credit losses, and subsequent principal recoveries are credited to the allowance for credit losses.

Management's evaluation of the adequacy of the allowance is based on UNCB's past loan and lease loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant qualitative factors. This evaluation is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans and leases that may be susceptible to significant change.

The allowance for credit losses is evaluated based on an assessment of the losses inherent in the loan and lease portfolio. This assessment results in an allowance that consists of specific, general and unallocated components. The specific component relates to loans and leases that are classified as impaired. For such loans and leases, an allowance is established when (i) the discounted cash flows, or (ii) collateral value, or (iii) observable market price of the impaired loan or lease is lower than the carrying value. The general component covers all other loans and leases, including criticized loans that are not impaired, and is based on historical loss experience adjusted for relevant qualitative factors. Separate qualitative adjustments are made for higher-risk criticized loans that are not impaired. An unallocated component is maintained to cover uncertainties that could affect our 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 loan and lease portfolio.



UNCB continues to monitor closely the loan portfolio, and the underlying borrower financial performance and collateral values, identifying credit concerns and risks, including those resulting from the uncertain and weakened economy. Future adjustments may be necessary to the allowance for credit losses, and consequently the provision for credit losses, if economic conditions or loan credit quality differ substantially from the assumptions management used in the evaluation of the level of the allowance compared to the balance of outstanding loans and leases.

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The allowance for credit losses was \$5,995,000 at March 31, 2010, compared to \$5,858,000 at December 31, 2009. A provision for credit losses of \$496,000 was made for the three months ended March 31, 2010, compared to \$313,000 for the same period in 2009. The provision for credit losses for the three months ended March 31, 2010, was significantly higher than the provision for credit losses for the three months ended March 31, 2009 (for additional information, refer to the related discussion on Provision for Credit Losses on page 25) given the increased credit risks in the loan portfolio, including those resulting from the current weak economy and real estate market. With the higher provision exceeding net loan charge-offs of \$359,000 as well as the decrease to the loan and lease portfolio in the first quarter of 2010, the allowance for credit losses increased to 1.80% of loans at March 31, 2010 compared to 1.73% of loans at December 31, 2009. Management believes, based on information then currently available, that the allowance for credit losses as of March 31, 2010, was adequate to meet probable credit losses at that date.

The following table summarizes the changes in the allowance for credit losses for the three months ended March 31, 2010 and 2009 (dollars in thousands):

	<b>Three Months Ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
Allowance for Credit Losses, Beginning of Period	\$ 5,858	\$ 4,358
Charge-Offs	(360)	(363)
Recoveries	1	11
Net Charge-Offs	(359)	(352)
Addition to Provision for Credit Losses	496	313
Allowance for Credit Losses, End of Period	\$ 5,995	\$ 4,319
Loans and Leases Average	\$ 338,341	\$ 356,118
Gross Loans and Leases Actual	\$ 333,028	\$ 356,289
Ratio of Gross Loans and Leases Charged Off to Average Loans and Leases (Annualized)	0.43%	0.41%
Ratio of The Allowance for Credit Losses to Gross Loans and Leases	1.80%	1.21%

**Impaired Loans**

Other than as described herein, management does not believe there are any significant trends, events or uncertainties that are reasonably expected to have a material impact on our loan and lease portfolio to affect future results of operations, liquidity or capital resources. However, based on known information, management believes that the effects of current and past economic conditions and other unfavorable business conditions may impact certain borrowers abilities to comply with their repayment terms and therefore may have an adverse effect on future results of operations, liquidity, or capital resources. Management continues to closely monitor economic and business conditions and the impact on borrowers financial strength. For certain loans and leases, management has determined that it is probable that all principal and interest payments due according to the contractual terms of the loan agreements will not be collected. These loans are considered to be impaired as defined by GAAP.

The balance of loans and leases that were considered to be impaired under GAAP was \$6,174,000 and \$8,715,000, which consisted of eight and ten separate loan and lease relationships to unrelated borrowers, at March 31, 2010 and December 31, 2009, respectively. At March 31, 2010, three of the relationships represented 84% of the total impaired

loans and leases of \$6,174,000. The decrease in impaired loans and leases from December 31, 2009 to March 31, 2010, primarily resulted from several loans, with a related allowance, that were foreclosed on and transferred into other real estate owned at March 31, 2010 (for additional information, refer to the discussion on Non-Performing Assets on page 21). Management continues to diligently monitor and evaluate the impaired loan portfolio, and identify new credit concerns and collectability risks, including those resulting from the current uncertain and weakened economy. The measure

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of impairment is based primarily on the fair value of collateral securing these loans, which is primarily real estate and equipment.

***Impaired Loans With a Related Allowance***

We had \$3,498,000 and \$5,916,000 of impaired loans and leases with a related allowance for credit losses at March 31, 2010 and December 31, 2009, respectively. These consisted of four and five separate loan and lease relationships to unrelated borrowers, with a related allowance for credit losses of \$1,199,000 and \$1,458,000 at March 31, 2010 and December 31, 2009, respectively. This group of impaired loans and leases has a related allowance due to the probability of the borrower not being able to continue to make principal and interest payments due under the contractual terms of the loan or lease. These loans and leases appear to have insufficient collateral and UNNF's principal may be at risk; as a result, a related allowance is necessary to cover future probable losses.

***Impaired Loans without a Related Allowance***

We had \$2,676,000 and \$2,799,000 of impaired loans and leases without a related allowance at March 31, 2010 and December 31, 2009, respectively. These consisted of four and five separate loan and lease relationships at March 31, 2010 and December 31, 2009, respectively. This group of impaired loans and leases is considered impaired due to the likelihood of the borrower not being able to continue to make principal and interest payments due under the contractual terms of the loan or lease. However, these loans and leases appear to have sufficient collateral and our principal does not appear to be at risk of probable principal losses; as a result, our management believes a related allowance is not necessary.

***Substandard Loans and Leases***

Under UNCB's current internal risk rating system, loans and leases with a rating of *substandard* that were performing, and not determined to be impaired, amounted to \$30,885,000 and \$32,410,000 at March 31, 2010 and December 31, 2009, respectively. Despite these credits not being impaired, management believes these substandard credits reflect increased risks to the loan portfolio, including risks resulting from the current weak economy and real estate markets. Management considered such increased risks in determining the provision for credit losses (refer to the related discussion on *Provision for Credit Losses* on page 25). Management continues to closely monitor the loan portfolio, and the underlying borrower financial performance and collateral values, identifying credit concerns and risks, including those resulting from the current weak economy. Management considers both impaired and these substandard loans to be potential problem loans, and believes that the current persisting and weakened economic conditions may result in additional loans being classified or nonperforming in future periods.

**Table of Contents*****Non-Performing Assets***

Nonperforming assets consist of nonperforming loans and leases, OREO, and repossessed assets. The following table provides a summary of nonperforming assets at March 31, 2010 and December 31, 2009 (dollars in thousands):

	<b>March 31, 2010</b>	<b>December 31, 2009</b>
Nonaccruing Loans	\$ 5,255	\$ 8,034
Accruing Loans 90 days or more past due	1,236	506
Total Nonperforming Loans and Leases	6,491	8,540
Other Real Estate Owned	8,170	5,383
Repossessed Assets	190	436
Total Nonperforming Assets	\$ 14,851	\$ 14,359
Gross Loans and Leases	\$ 333,028	\$ 339,274
Allowance for Credit Losses	\$ 5,995	\$ 5,858
Nonperforming Loans and Leases as a % of Gross Loans and Leases	1.9%	2.5%
Nonperforming Assets as a % of Total Assets	3.0%	2.9%
Allowance for Credit Losses as a % of Nonperforming Loans and Leases	92%	69%

Nonperforming loans and leases consist of loans and leases that are nonaccruing, and those that are 90 days or more past due. Nonaccruing loans and leases are no longer accruing interest income because of apparent financial difficulties of the borrower. Interest received on nonaccruing loans and leases is recorded as income only after the past due principal is brought current and deemed collectible in full. Total nonperforming loans and leases decreased to \$6,491,000, or 1.9%, of gross loans and leases at March 31, 2010, compared to \$8,540,000, or 2.5% of gross loans and leases, at December 31, 2009. The decrease in nonperforming loans and leases primarily resulted from several loans being foreclosed on in 2010 and are reported as OREO in the Consolidated Statements of Financial Condition at March 31, 2010. Historically, the percentage of nonperforming loans to gross loans for the five year-end periods ended December 31, 2009, was an average of 1.2%.

OREO includes assets acquired through foreclosure, deed in-lieu of foreclosure, and loans identified as in-substance foreclosures. A loan is classified as an in-substance foreclosure when effective control of the collateral has been taken prior to completion of formal foreclosure proceedings. OREO is held for sale and is recorded at fair value less estimated costs to sell. Costs to maintain OREO and subsequent gains and losses attributable to OREO liquidation are included in the Consolidated Statements of Operations in other income and other expense as realized. No depreciation or amortization expense is recognized. OREO was \$8,170,000 and \$5,383,000 at March 31, 2010 and December 31, 2009, respectively. The increase was primarily the result of foreclosing on two commercial mortgages in 2010. At March 31, 2010, \$7,375,000, or 90% of the total OREO balance, consisted of two commercial properties in Lancaster, Pennsylvania. The remaining \$795,000, or 10% of the total OREO balance, was comprised of five smaller commercial and residential properties.

Repossessed assets consist of (i) vehicles and other equipment acquired from lessees, who defaulted on their contractual lease obligation, and (ii) mobile homes where UNCB does not own the underlying real estate. Repossessed assets were \$190,000 and \$436,000 at March 31, 2010 and December 31, 2009, respectively. The decrease resulted primarily from the write-down of certain repossessed leased assets to fair market value, which amounted to \$144,000.

**Stockholders' Equity**

Stockholders' equity increased by \$392,000 to \$31,728,000 at March 31, 2010, compared to \$31,336,000 at December 31, 2009. The increase in stockholders' equity was primarily the result of other comprehensive income during the period, proceeds received through the Dividend Reinvestment Plan, or DRIP, and increases

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to retained earnings resulting from year-to-date net income, which was offset by scheduled dividends paid to preferred stockholders.

Our regulatory capital position at March 31, 2010 exceeded the current regulatory required minimums as disclosed below.

***Regulatory Capital***

Bank regulatory authorities in the United States issue risk-based capital standards. These capital standards relate a bank's capital to the risk profile of its assets and provide the basis by which all banks are evaluated in terms of its capital adequacy. We and UNCB are 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 our consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, We and UNCB must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The 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 UNCB and us to maintain minimum amounts and ratios of Tier 1 capital to average assets and of total capital (as defined in the regulations) to risk-weighted assets.

As of March 31, 2010 and December 31, 2009, we and UNCB exceeded the current regulatory requirements to be considered a quantitatively well capitalized financial institution, i.e. a leverage ratio exceeding 5%, Tier 1 risk-based capital exceeding 6%, and total risk-based capital exceeding 10%.

In addition to the above regulatory capital standards, effective September 30, 2009, the OCC established individual minimum capital requirements for UNCB. For additional information, refer to Note 9 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus. The specific capital requirements established for UNCB were 8% for Tier 1 capital to average total assets, 9.5% for Tier 1 capital to risk-based assets, and 12% for total capital to risk-based assets. At March 31, 2010, UNCB's measure of Tier I capital to average Total assets was 8.34%, Tier 1 capital to risk-based assets of 10.00% and total capital to risk-based assets of 12.72%. At March 31, 2010, all three ratios exceeded the respective individual minimum capital requirements established by the OCC.

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UNNF and UNCB's regulatory capital levels as of March 31, 2010 and December 31, 2009 were as follows (dollars in thousands):

	Actual		Minimum Required for Capital Adequacy Purposes		To Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio(1)	Amount	Ratio
<b>Union National Financial Corporation</b>						
March 31, 2010:						
Tier 1 (leverage) capital	\$ 42,024	8.52%	\$ 19,733	4.00%	N/A	N/A
Tier 1 risk-based capital	42,024	10.22	16,449	4.00	N/A	N/A
Total risk-based capital	53,669	13.05	32,898	8.00	N/A	N/A
December 31, 2009:						
Tier 1 (leverage) capital	\$ 42,036	8.52%	\$ 19,744	4.00%	N/A	N/A
Tier 1 risk-based capital	42,036	9.93	16,929	4.00	N/A	N/A
Total risk-based capital	53,825	12.72	33,858	8.00	N/A	N/A
<b>Union National Community Bank</b>						
March 31, 2010:						
Tier 1 (leverage) capital	\$ 41,004	8.34%	\$ 19,671	4.00%	\$ 24,589	5.00%
Tier 1 risk-based capital	41,004	10.00	16,400	4.00	24,599	6.00
Total risk-based capital	52,141	12.72	32,799	8.00	40,999	10.00
December 31, 2009:						
Tier 1 (leverage) capital	\$ 40,910	8.31%	\$ 19,686	4.00%	\$ 24,608	5.00%
Tier 1 risk-based capital	40,910	9.69	16,881	4.00	25,322	6.00
Total risk-based capital	52,194	12.37	33,762	8.00	42,203	10.00

(1) The OCC requires UNCB to meet higher individual minimum capital ratios effective September 30, 2009. For additional information, refer to Note 9 Enforcement Actions with Bank Regulatory Agencies included elsewhere in this proxy statement/prospectus.

Included in Tier 1 regulatory capital of UNNF is \$10,507,000 of trust capital securities issued through our UNCT I and UNCT II subsidiaries. The balance of these trust capital securities, \$493,000, is included in our Tier 2 regulatory capital. In addition, included in Tier 2 regulatory capital of UNCB and UNNF is \$6,000,000 of junior subordinated debentures issued by UNCB. These securities would become callable if the FRB makes a determination that trust capital securities can no longer be considered in regulatory capital.

Regulatory capital requirements may be increased in the future. We will closely monitor and evaluate its capital position as the regulatory capital environment changes, and if regulatory capital requirements are changed.

**Restrictions**

Banking regulations limit the amount of investments, loans, extensions of credit and advances UNCB can make to us at any time to 10% of UNCB's total regulatory capital. At March 31, 2010, this limitation amounted to approximately \$5,214,000. These regulations also require any such investment, loan, extension of credit or advance to be secured by



securities having a market value in excess of the amount thereof.

UNCB is subject to certain restrictions in connection with the payment of dividends. National banking laws require the approval of the OCC if the total of all dividends declared by a national bank in any calendar year exceeds the net profits of UNCB for that year (as defined) combined with UNCB's retained net operating results for the preceding two calendar years. Under this formula, UNCB's retained net operating results for the preceding two calendar years was (\$189,000). As a result, in 2010, UNCB may declare dividends to UNNF in

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an amount equal to the net profits of UNCB in 2010 less \$189,000, up to the date of any such dividend declaration. UNCB's net income for the three months ended March 31, 2010 was \$94,000, restricting UNCB from declaring or making any dividend payment to us at March 31, 2010.

On January 28, 2010, we entered into an informal Memorandum of Understanding, or MOU, with the Federal Reserve Bank of Philadelphia, or the Philadelphia FRB. The MOU, which is not a written agreement for purposes of Section 8 of the Federal Deposit Insurance Act, requires, among other things, us to seek prior approval by the Philadelphia FRB before we (i) declare or pay dividends to shareholders, (ii) distribute interest, principal or other sums on UNCT I and UNCT II junior subordinated debentures, and (iii) incur, increase or guarantee any additional debt. Subsequent to March 31, 2010, the Philadelphia FRB did approve the quarterly interest payments for the second quarter of 2010 on the UNCT I and UNCT II junior subordinated debentures and the preferred stock dividend payments.

**Results of Operations For The Three Months Ended March 31, 2010 and 2009**

*Overview*

We reported a net loss available to common stockholders of (\$15,000) or a basic and diluted loss per share of (\$0.01) for the first quarter of 2010, compared to a net loss available to common stockholders of (\$509,000) or a basic and diluted loss per share of (\$0.19) for the same period in 2009. The year-over-year first quarter results improved primarily due to an increased net interest margin for the first quarter of 2010, compared to the same period in 2009, and the first quarter of 2010 not having any impairment charges on investment securities similar to those that occurred in the first quarter 2009.

Our net interest income as adjusted for tax-exempt financial instruments increased \$363,000, or 12%, to \$3,296,000 for the first quarter of 2010, compared to \$2,933,000 for the same period in 2009. The cost of interest-bearing deposits decreased to 1.92% for the first quarter of 2010, compared to 2.65% for same period in 2009, which significantly improved the taxable-equivalent net interest margin percentage to 2.96% for the first quarter of 2010, compared to 2.58% for same period in 2009.

The operating results for the first quarter of 2009 reflected \$839,000 in other-than-temporary investment impairment charges related to three pooled trust preferred debt securities that were downgraded to below-investment-grade in 2009. These other-than-temporary investment impairment charges were offset by \$411,000 of realized net gains on the sale of investment securities during the first quarter of 2009, resulting in \$428,000 of net investment losses. For the first quarter of 2010, gains of \$77,000 were realized on the sale of investment securities and UNCB incurred no additional other-than-temporary impairment charges.

The discussion that follows further explains the changes in the components of the operating results when comparing the three months ended March 31, 2010 to the same period in 2009.

*Net Interest Income*

Net interest income, our primary source of revenue, is the amount by which interest income on loans and investments exceeds interest incurred on deposits and borrowings. The amount of net interest income is affected by changes in interest rates and by changes in the volume and mix of interest-sensitive assets and liabilities. Net interest income and corresponding yields are presented in the discussion and analysis below on a taxable-equivalent basis. Income from tax-exempt assets, primarily loans to or securities issued by state and local governments, is adjusted by an amount equivalent to the federal income taxes which would have been paid if the income received on these assets was taxable at the statutory rate of 34%.

Although the effective interest rate impact on earning assets and funding sources can be reasonably estimated at current interest rate levels, the options selected by customers, and the future mix of the loan, investment and deposit products in UNCB's portfolios, may significantly change the estimates used in the simulation models. In addition, our net interest income may be impacted by further interest rate actions of the FRB and movements in the London Interbank Offered Rate, or LIBOR, upon which certain variable rate loans are priced.

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Net interest income as adjusted for tax-exempt financial instruments was \$3,296,000 for the three months ended March 31, 2010, compared to \$2,933,000 for the same period in 2009. The yield on interest-earning assets decreased by 39 basis points to 4.99% for the first quarter of 2010, compared to 5.38% for the same period in 2009. The interest rate paid on average interest-bearing liabilities decreased by 80 basis points to 2.27% for the first quarter of 2010, compared to 3.07% for the same period in 2009. The decrease in the interest rate paid on average interest-bearing liabilities more than offset the decrease in the yield on interest-earning assets, which resulted in a higher net interest margin for the first quarter of 2010, compared to the same period in 2009. The taxable-equivalent net interest margin percentage for the first quarter of 2010 was 2.96%, compared to 2.58% for the same period in 2009.

Interest and fees on loans and leases on a taxable-equivalent basis decreased by \$385,000, or 7%, to \$5,047,000 for the three months ended March 31, 2010, compared to \$5,432,000 for the same period in 2009. The average yield decreased by 14 basis points to 6.05% for the first quarter of 2010, compared to 6.19% for the same period in 2009. The variable rate structure of many of UNNF's loans reduced the overall yield due to the persistent low market interest rates. The average balance of loans and leases decreased by \$17,777,000 for the first quarter of 2010, compared to the same period in 2009 due to reduced loan demand from creditworthy borrowers, the impact of nearly \$10 million of loan participations sold for capital and risk management purposes in the third quarter of 2009, and the impact of approximately \$8 million of loans that were foreclosed on and transferred to OREO since December 2009. The decrease in interest and fees on loans and leases primarily resulted from the decrease in loans outstanding.

Interest and dividends earned on investment securities on a taxable-equivalent basis decreased by \$191,000, or 30%, to \$438,000 for the three months ended March 31, 2010, compared to \$629,000 for the same period in 2009. The decrease in interest and dividends earned on investment securities primarily resulted from a decrease in the average balance of investment securities, which decreased by \$10,638,000 for the first quarter of 2010, compared to the same period in 2009. A lack of income from impaired and non-accruing investments, and reduced yields on re-invested proceeds from investment maturities and sales, also contributed to lower investment interest income for the first quarter of 2010. As a result, the average yield decreased by 66 basis points to 3.12% for the first quarter of 2010, compared to 3.78% for the same period in 2009.

Interest expense on deposits decreased by \$621,000, or 27%, to \$1,681,000 for the three months ended March 31, 2010, compared to \$2,302,000 for the same period in 2009. The decrease in interest expense on deposits was primarily driven by a decrease of 73 basis points in average rate paid on deposits. The average rate paid on deposits was 1.92% for the first quarter of 2010, compared to 2.65% for the same period in 2009.

Interest expense on long-term debt decreased by \$252,000, or 39%, to \$393,000 for the three months ended March 31, 2010, compared to \$645,000 for the same period in 2009. We continued to take measures to reduce our cost of borrowings, prepaying \$2,500,000 and \$17,000,000 of higher-cost long-term debt in the first quarter of 2010 and for the full year of 2009, respectively, which resulted in a \$18,917,000 decrease in the average balance of long-term debt for the first quarter of 2010, compared to the same period in 2009.

***Provision for Credit Losses***

The provision for credit losses is an expense charged against net interest income to provide for estimated losses attributable to uncollectible loans and leases. The provision is based on management's analysis of the adequacy of the allowance for credit losses. The provision for credit losses was \$496,000 for the three months ended March 31, 2010, compared to \$313,000 for the same period in 2009. The increased provision was the result of increased credit risk related to the loan portfolio at March 31, 2010, compared to March 31, 2009 (refer to the related discussions on the

Allowance for Credit Losses on page 18 and Substandard Loans and Leases on page 20). Management continues to closely monitor the loan portfolio and the adequacy of the allowance for credit loss reserve considering underlying borrower financial performance and collateral values, and increasing credit risks. Future adjustments may be

necessary to the provision for credit losses, and consequently the allowance for credit losses, if economic conditions or loan credit quality differ substantially from the assumptions we used in making our evaluation of the level of the allowance for credit losses compared to the balance of outstanding loans and leases.

**Table of Contents*****Non-Interest Income***

Non-interest income increased by \$561,000, or 91%, to \$1,180,000 for the three months ended March 31, 2010, compared to \$619,000 for the same period in 2009. Increases (decreases) in the components of non-interest income when comparing the three months ended March 31, 2010 to the same period in 2009, are as follows (in thousands):

<b>Non-Interest Income</b>	<b>Three Months Ended March 31,</b>		<b>Increase (Decrease)</b>
	<b>2010</b>	<b>2009</b>	
Service Charges on Deposit Accounts	\$ 458	\$ 473	\$ (15)
Other Service Charges, Commissions, Fees	288	267	21
Alternative Investment Sales Commissions	167	110	57
Income from Fiduciary Activities	47	46	1
Earnings from Bank-Owned Life Insurance	102	108	(6)
Other Income	41	43	(2)
Net Gain on Sale of Investment Securities	77	411	(334)
Other-than-temporary Impairments ( OTTI ) of Securities Portion of OTTI Recognized in Other Comprehensive Income		(839)	839
Net OTTI Losses on Securities		(839)	839
Total Non-Interest Income	\$ 1,180	\$ 619	\$ 561

A significant portion of the \$561,000 increase in non-interest income was related to investment securities activities. The operating results for the first quarter of 2009 reflected \$839,000 in other-than-temporary investment impairment charges related to three pooled trust preferred debt securities that were downgraded to below-investment-grade in 2009. These other-than-temporary investment impairment charges were offset by \$411,000 of realized net gains on the sale of investment securities during the first quarter of 2009, resulting in \$428,000 of net investment losses. For the first quarter of 2010, gains of \$77,000 were realized on the sale of investment securities and UNCB incurred no additional other-than-temporary impairment charges.

***Non-Interest Expense***

Non-interest expense was \$4,022,000 for the three months ended March 31, 2010, compared to \$4,014,000 for the same period in 2009. Increases (decreases) in the components of non-interest expense when comparing the three months ended March 31, 2010, to the same period in 2009, are as follows (in thousands):

<b>Non-Interest Expense</b>	<b>Three Months Ended March 31,</b>		<b>Increase (Decrease)</b>
	<b>2010</b>	<b>2009</b>	
Salaries, Wages, and Employee Benefits	\$ 1,798	\$ 1,946	\$ (148)
Net Occupancy	462	478	(16)
Data and ATM Processing	406	404	2
Professional Fees and Regulatory Assessments	206	257	(51)

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Furniture and Equipment	218	246	(28)
FDIC Insurance	228	120	108
Pennsylvania Shares Tax	95	89	6
Advertising and Marketing	38	67	(29)
Supplies and Postage	60	74	(14)
Other Expense	511	333	178
Total Non-Interest Expense	\$ 4,022	\$ 4,014	\$ 8

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The discussion that follows explains the significant changes in the components of non-interest expense when comparing the three months ended March 31, 2010 to the same period in 2009.

Salaries, wages and employee benefits decreased by \$148,000 for the three months ended March 31, 2010, compared to the same period in 2009. The decrease was related to positions that were eliminated in the first quarter of 2009, savings in health care costs due to UNCB's beneficial participation in a healthcare consortium and savings from the suspension of our 401-K match which began during the second quarter of 2009 and remained suspended through March 31, 2010.

Due to recent changes in deposit premium assessments by the FDIC, FDIC insurance assessments amounted to \$228,000 for the three months ended March 31, 2010, representing a \$108,000 or 90% increase over the three months ended March 31, 2009. The increase in FDIC insurance premiums was primarily the result of increased base assessment rates, as determined by the FDIC.

The increase in other expense was primarily the result of several repossessed assets being written-down by \$144,000 to fair market value. These repossessed assets consisted of vehicles acquired from lessees, who defaulted on their contractual lease obligations, and the write-downs reflect recent significant market devaluations for the types of assets held as repossessed by UNCB. In addition, during the three months ended March 31, 2010, UNCB prepaid \$2,500,000 of FHLB advances to further de-leverage UNCB and reduce current and future borrowing costs. In conjunction with the prepayments, UNCB incurred \$89,000 of prepayment penalties, which also contributed to the increase in other expense for the three months ended March 31, 2010. UNCB did not prepay any FHLB advances in the first quarter of 2009, and therefore, did not incur any prepayment penalties for the three months ended March 31, 2009.

## **Income Taxes**

An income tax benefit of \$82,000 and \$328,000 was recorded for the three months ended March 31, 2010 and 2009, respectively. For both of these periods, the benefit resulted from tax-exempt earnings as well as from a pre-tax loss. Generally, our effective tax rate is below the statutory rate due to tax-exempt earnings on loans, investments, and bank-owned life insurance, and the impact of tax credits. The realization of deferred tax assets is dependent upon future earnings. Management anticipates that future earnings will be adequate to fully utilize deferred tax assets.

## **Liquidity**

Our objective is to maintain adequate liquidity to meet funding needs at a reasonable cost and to provide contingency plans to meet unanticipated funding needs or a loss of funding sources, while minimizing interest rate risk. Adequate liquidity provides resources for credit needs of borrowers, for depositor withdrawals and for funding corporate operations. Sources of liquidity are as follows:

A growing core retail deposit base;

Proceeds from the sale or maturity of investment securities;

Payments received on loans and mortgage-backed securities; and,

Overnight correspondent bank borrowings credit lines, and borrowing capacity available from the FRB.

Management believes that UNCB's core deposits remain fairly stable. Liquidity and funds management is governed by policies and measured on a daily basis, with supplementary weekly and monthly analyses. These measurements indicate that liquidity generally remains stable and exceeds our minimum defined levels of adequacy. Other than the



trends of continued competitive pressures and volatile interest rates, there are no known demands, commitments, events or uncertainties that will result in, or that are reasonably likely to result in, liquidity increasing or decreasing in any material way.

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### **Off-Balance Sheet Commitments**

In the normal course of business, we are party to financial instruments with off-balance sheet risk to meet the financing needs of our customers. These financial instruments include commitments to extend credit and standby letters of credit. Total commitments to extend credit amounted to \$106,597,000 at March 31, 2010 compared to \$110,791,000 at December 31, 2009. Total standby letters of credit amounted to \$5,725,000 at March 31, 2010 compared to \$6,199,000 at December 31, 2009.

In addition, in the normal course of business operations, we routinely enter into contracts for services. These contracts may require payment for services to be provided in the future and may also contain penalty clauses for the early termination of the contracts. In January 2007, the contract with our core data processor was renegotiated, resulting in a new maturity date of November 2013. Any early termination will require the payment of a substantial penalty. For the three months ended March 31, 2010, there has been no material change in contracts for services since this contract was renegotiated.

### **Regulatory Matters**

From time to time, various types of federal and state legislation have been proposed that could result in additional regulation of, and restrictions on, our and UNCB's business. As a consequence of the extensive regulation of commercial banking activities in the United States, our and UNCB's business is particularly susceptible to being affected by federal and state legislation and regulations that may increase the cost of doing business. Also, we are susceptible to changes in tax law that may increase the cost of doing business or impact our ability to realize the value of deferred tax assets. Further, our business is affected by the state of the financial services industry in general. Please refer to Note 9 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus for a discussion on specific regulatory matters impacting us.

### **Year Ended December 31, 2009 Compared to Year Ended December 31, 2008**

#### **Overview**

Management's discussion and analysis represents an overview of the financial condition and results of operations, and highlights the significant changes in the financial condition and results of operations, as presented in our accompanying consolidated financial statements. Our consolidated financial condition and results of operations consist primarily of UNCB's financial condition and results of operations. We established our trust subsidiaries, UNNF Capital Trust I, or UNCT I, and UNNF Capital Trust II, or UNCT II, for the purpose of issuing \$11.0 million of trust capital securities during 2003 and 2004. Refer to Note 16 Residential Mortgage Business Venture to the consolidated financial statements included elsewhere in this proxy statement/prospectus for information about our former subsidiaries Home Team Financial, LLC and TA of Lancaster, LLC.

#### **Financial Condition**

Total assets increased by \$4,535,000 or 1% to \$489,644,000 at December 31, 2009 from \$485,109,000 at December 31, 2008. The increase was primarily the result of strong retail deposit generation, which further strengthened UNNF's liquidity position. The proceeds received from the deposit growth were used to pay down high cost long-term debt and to purchase short-term investments. Total deposits grew by \$21,188,000 or 6% to \$404,765,000 at December 31, 2009 from \$383,577,000 at December 31, 2008.

*Investment Securities*

Investment securities were \$60,546,000 at December 31, 2009 compared to \$64,289,000 at December 31, 2008. All of our investment securities were classified as available for sale at December 31, 2009 and 2008. Investment securities classified as available for sale are marketable equity securities, and those debt securities that we intend to hold for an undefined period of time, but not necessarily to maturity. In addition to the investment portfolio generating interest income, it serves other primary financial management functions such

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as an ultimate source of liquidity and a tool to manage interest rate risk. In order to support these functions, the entire investment securities portfolio has been designated as being available for sale. Any decision to sell an available-for-sale investment security would be based on various factors, including significant movements in interest rates, changes in maturity mix of assets and liabilities, liquidity needs, regulatory capital considerations, changes in the creditworthiness of the issuing entity, changes in investment strategy and portfolio mix, and other similar factors. Changes in unrealized gains or losses on available-for-sale investment securities, net of taxes, are recorded as other comprehensive (loss) income, a component of stockholders' equity.

At December 31, 2009, there were no significant concentrations of investments (greater than 10% of stockholders' equity) in any individual investment security issue. The investment securities portfolio included \$53,394,000 or 88% of U.S. agency mortgage-backed securities at December 31, 2009.

The following is a summary of available-for-sale investment securities recorded at fair value as of December 31, 2009, 2008 and 2007 (in thousands):

	<b>At December 31,</b>		
	<b>2009</b>	<b>2008</b>	<b>2007</b>
U.S. Agency Mortgage-Backed Securities	\$ 53,394	\$ 56,250	\$ 19,572
Private Issuer Mortgage-Backed Securities	2,638	3,219	6,658
Obligations of U.S. Government Agencies		3,396	43,086
Obligations of State and Political Subdivisions	3,815		
Corporate Debt Securities	631	1,218	4,413
Equity Securities	68	206	447
<b>Total</b>	<b>\$ 60,546</b>	<b>\$ 64,289</b>	<b>\$ 74,176</b>

The following table presents the stated maturities of investment securities at fair value and the weighted-average yields as of December 31, 2009. Yields are shown on a taxable-equivalent basis, assuming a 34% federal income tax rate (dollars in thousands).

	<b>Within 1 Year</b>	<b>1-5 Years</b>	<b>5-10 Years</b>	<b>After 10 Years</b>	<b>No Stated Maturity</b>	<b>Total</b>	<b>Yield</b>
U.S. Agency Mortgage-Backed Securities(1)	\$	\$	\$	\$ 53,394	\$	\$ 53,394	4.31%
Private Issuer Mortgage-Backed Securities				2,638		2,638	
Obligations of State and Political Subdivisions				3,815		3,815	5.89
Corporate Debt Securities				631		631	
Equity Securities(2)					68	68	2.67
<b>Total Securities</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$ 60,478</b>	<b>\$ 68</b>	<b>\$ 60,546</b>	<b>4.18%</b>

Yield	%	%	%	4.18%	2.67%(2)	4.18%
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(1) It is anticipated that the mortgage-backed securities will be repaid prior to their contractual maturity dates. The yield for these securities is impacted by normal amortization and estimated prepayments based on current market interest rates.

(2) The yield on the equity securities assumes the same dividend payout ratio as in 2009.

The realized rate of return on average investment securities, including net investment securities gains (losses) and OTTI charges was 3.39% and 3.12% for the years ended December 31, 2009 and 2008,

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respectively. The following table presents the realized rate of return on average investment securities by investment category for the years ended December 31, 2009 and 2008 (dollars in thousands).

	Year Ended December 31, 2009					
	Average Balance	Tax- Equivalent Interest and Dividends	Net Realized Gain on Sale	OTTI Charge	Total Return	Yield
U.S. Agency and Treasury Holdings	\$ 58,661	\$ 1,551	\$ 1,749	\$	\$ 3,300	5.63%
Private Issuer MBS and Corporate Securities	3,834	131		(1,504)	(1,373)	(35.81)
All Other Securities	5,766	294	92		386	6.69
Total	\$ 68,261	\$ 1,976	\$ 1,841	\$ (1,504)	\$ 2,313	3.39%

	Year Ended December 31, 2008					
	Average Balance	Tax- Equivalent Interest and Dividends	Net Realized Gain (Loss) on Sale	OTTI Charge	Total Return	Yield
U.S. Agency and Treasury Holdings	\$ 62,675	\$ 2,904	\$ 256	\$	\$ 3,160	5.04%
Private Issuer MBS and Corporate Securities	6,627	305	(52)	(1,290)	(1,037)	(15.65)
All Other Securities	316		48		48	15.19
Total	\$ 69,618	\$ 3,209	\$ 252	\$ (1,290)	\$ 2,171	3.12%

The total expected cash flows from investment securities, including estimated prepayments and expected call options, is \$8,349,000 for 2010, which represents approximately 14% of the investment securities portfolio as of December 31, 2009. The estimated amount of expected cash flows from investment securities will vary significantly with changes in market interest rates. For example, an increase in interest rates will decrease the level of prepayments received on mortgage-backed securities. The factors affecting the investment securities portfolio are included in our net interest income simulation model, which is discussed in the section **Market Risk Interest Rate Risk** on page 52.

Certain types of mortgage-backed and asset-backed securities are purchased to better position the investment securities portfolio for a subsequent increase or decrease in interest rates, as aligned with our interest rate risk position. These investment securities may be purchased at premiums or discounts, with short, mid, or long-term average expected lives or maturities. Overall yields on these investment securities will increase or decrease based on

changes in prepayment speeds and subsequent cash flow reinvestments.

Investment security purchases and sales generally occur to manage UNCB's liquidity requirements, pledging requirements, interest rate risk, and to enhance net interest margin. The investment securities portfolio is evaluated regularly for possible opportunities to increase earnings through potential sales or portfolio repositioning. In 2009, proceeds of \$197,637,000 were received on sales, and \$1,841,000 was recognized in net gains, while \$233,313,000 of investment securities were purchased during the year. Investment securities of \$57,209,000 and \$59,646,000 were pledged to secure public, trust, and government deposits and for other purposes at December 31, 2009 and 2008, respectively.

In addition to the credit risk present in the loan portfolio, we also have credit risk associated with our investment security holdings. Based on recent national economic trends and other factors, the private issuer mortgage-backed securities and corporate debt securities credit ratings as published by national statistical rating organizations are being monitored closely.

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As of December 31, 2009 and 2008, investment securities consisted of the following (in thousands):

	<b>December 31,</b>	
	<b>2009</b>	<b>2008</b>
Market Value of Debt Securities	\$ 60,478	\$ 64,083
Market Value of Equity Securities	68	206
 Total Market Value of Investment Securities	 \$ 60,546	 \$ 64,289

Debt securities include mortgage-backed securities, obligations of state and political subdivisions, obligations of U.S. Government agencies and corporate securities. At December 31, 2009, there were twenty-seven debt securities with unrealized losses of \$585,000 that amounted to 1.3% of their amortized cost, compared to December 31, 2008, when there were twenty-three debt securities with unrealized losses of \$607,000 that amounted to 3.2% of their amortized cost. Management believes that the unrealized losses reflect temporary declines primarily due to changes in interest rates subsequent to the acquisition of specific securities. These temporary declines have been provided for in other comprehensive (loss) income.

Equity securities held are comprised primarily of common stock holdings in other financial institutions. The market values include net unrealized losses of \$11,000 at December 31, 2009, compared to net unrealized losses of \$63,000 at December 31, 2008. In 2009, proceeds of \$119,000 were received on equity sales, and \$38,000 was recognized in net losses.

As of December 31, 2009, \$13,000 of the fair value of the total investment securities portfolio was measured using Level 1 inputs as defined by fair value measurement and disclosure guidance, \$57,264,000 or 95% of the fair value of total investment securities was measured using Level 2 inputs, and \$3,269,000 or 5% of the fair value of total investment securities was measured using Level 3 inputs. For additional information, refer to Note 20 Fair Value Measurement of Assets and Liabilities and Fair Value of Financial Instruments to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

The fair value of Level 3 investment securities decreased to \$3,269,000 at December 31, 2009, compared to \$4,437,000 at December 31, 2008. Of the decrease in value, \$1,504,000 was related to impairment charges that were included in the Consolidated Statements of Operations and \$733,000 was related to principal and interest payments received (net of accretion) and fully applied to principal, offset by \$1,069,000 of net unrealized gains (with a corresponding after-tax increase to stockholders' equity of \$706,000 recorded as other comprehensive income).

In order to determine whether unrealized losses in the fair value of investment securities are OTTI, management regularly reviews the entire portfolio of investment securities for possible impairment, analyzing factors including but not limited to the underlying creditworthiness of the issuing organization, the length of time for which the fair value of the investment securities has been less than cost, and independent analysts' opinions about circumstances that could affect the performance of the investment securities. In assessing potential OTTI for debt securities, other considerations include (i) whether management intends to sell the security, or (ii) if it is more likely than not that management will be required to sell the security before recovery, or (iii) if management does not expect to recover the entire amortized cost basis. In assessing potential OTTI for equity securities, consideration is given to management's intention and ability to hold the securities until recovery of any unrealized losses.



As of December 31, 2009, we maintain five investment securities with recorded impairments. The fair value of the five impaired investments was \$3,269,000 as of December 31, 2009, compared to an original amortized cost of \$8,950,000. All principal and interest payments received on impaired investment securities are fully applied to principal.

ASC Topic 320, Investments – Debt and Equity Securities provides a list of factors that a reporting entity should evaluate to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability in relation to normal market activity for the asset or liability. When the reporting entity concludes there has been a significant decrease in the volume and level of activity for the asset or liability, further analysis of the information from that market is needed and significant adjustments to

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the related prices may be necessary to estimate fair value in accordance with fair value measurement and disclosure guidance. Further, fair value measurement and disclosure guidance clarifies that when there has been a significant decrease in the volume and level of activity for the asset or liability, some transactions may not be orderly, and UNNF must evaluate the weight of evidence to determine whether the transactions are orderly. The guidance provides a list of circumstances that may indicate that a transaction is not orderly. A transaction price that is not associated with an orderly transaction is given little, if any, weight when estimating fair value.

As discussed in Note 20 Fair Value Measurement of Assets and Liabilities and Fair Value of Financial Instruments to the consolidated financial statements included elsewhere in this proxy statement/prospectus, the fair value of debt investment securities was determined by calculating the net present value of the expected future cash flows of each security, with qualitative risk-adjusted discounting for potential credit risks and nonperformance in the underlying issuers, and market sector illiquidity concerns. Under ASC Topic 320, Investments Debt and Equity Securities when an active market for a security does not exist, the use of management estimates that incorporate current market participant expectations of future cash flows, and include appropriate risk premiums, is acceptable. Management's judgment was that, as of December 31, 2009, the facts and circumstances indicated significant illiquidity and an inactive market for these types of investments when other relevant observable inputs were not available; therefore, expected cash flows were a reasonable basis in determining the fair value of the corporate investment securities. Prior to September 30, 2008, management used other observable inputs to determine the fair value of the corporate investment securities including broker indicated prices and quoted prices in limited trading activity of the issuances.

During 2009, four of UNCB's five private-issuer securities were downgraded to below investment grade. The fifth private-issuer security was downgraded to below-investment-grade in December 2008. Accordingly, UNCB recorded \$1,504,000 of other-than-temporary impairment charges in 2009 including (i) \$859,000 related to three pooled trust-preferred debt securities supported primarily by obligations from other banks, and (ii) \$645,000 related to a mortgage-backed security not guaranteed by the U.S. government. Management determined that, due to severe illiquidity and distress in the financial markets, the unrealized declines in the value of these investments were other-than-temporary, requiring the write-down. For the securities with impairment charges recorded, interest income payments received subsequent to impairment are fully applied to principal further reducing the amortized cost of these investments. For additional information, refer to Note 3 Investment Securities Available for Sale to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

Management determined that further impairments as of December 31, 2009 were not warranted on these five securities based upon the following considerations:

The financial condition and near-term prospects of the issuers reflect only one probable default, which was fully considered when determining the other-than-temporary impairment of the respective security.

Four of the five impaired investment securities were current, as of December 31, 2009, for scheduled investment interest payments, and principal repayments for the two private issuer mortgage-backed securities have occurred regularly since issuance. Based upon the information reviewed by management in preparing the financial statements, the financial condition and near-term prospects of the issuers do not reflect any specific events which may have influenced the operations of the issuers, such as changes in technology or a discontinuance of a business segment that may have further impaired the earnings potential of the investments.

The securities experienced very limited trading activity during the last 12 months being in a market sector with a high degree of illiquidity and dislocation; therefore, determining fair value based upon discounted cash flows is considered reasonable.

Management does not intend to sell the securities, and it is not likely that management will be required to sell the securities before recovery, and though management does not expect to recover the amortized cost of the securities, management expects to hold the securities until a reasonable recovery towards the current carrying value.

**Table of Contents****Loans and Leases, Credit Quality and Credit Risk**

Loans include leases that meet the criteria for direct financing leases. Loans and lease financing receivables may, throughout Management's Discussion and Analysis, together be referred to as loans. Loans and leases were \$339,274,000 at December 31, 2009, compared to \$358,280,000 at December 31, 2008. Loans and leases decreased by \$19,006,000 from December 31, 2008 to December 31, 2009 due to (i) reduced loan demand from creditworthy borrowers, and (ii) the impact of nearly \$10 million of loan participations sold for capital and risk management purposes.

At December 31, 2009, there were no loan or lease concentrations over 10% of total gross loans and leases to any one category or borrower. However, loans secured by real estate constitute 83% of UNCB's loan and lease portfolio; consequently, the quality of these loans is affected by the region's economy and real estate market.

For the most recent five years, loans and leases were composed of the following (in thousands):

	2009	2008	December 31,		
			2007	2006	2005
Real Estate Mortgages:					
First and Second Residential	\$ 112,535	\$ 127,636	\$ 137,724	\$ 130,395	\$ 124,344
Commercial and Industrial	120,610	121,619	115,630	105,158	94,016
Construction and Land Development	21,970	24,757	29,427	23,634	10,618
Agricultural	28,099	27,485	24,839	24,133	23,488
Commercial and Industrial	37,410	35,061	28,741	27,226	20,291
Consumer (Net of Unearned Income)	5,854	7,172	7,832	7,893	8,159
Agricultural	4,464	3,588	4,341	3,733	3,300
Political Subdivisions	5,764	6,553	8,993	9,803	11,029
Lease Financing Receivables (Net of Unearned Income)	1,929	3,792	6,078	8,339	3,707
Other	639	617	732	799	1,261
Total Loans and Leases (Net of Unearned Income)	\$ 339,274	\$ 358,280	\$ 364,337	\$ 341,113	\$ 300,213

Total loans and leases with variable-rate pricing amounted to \$225,434,000 at December 31, 2009, and \$235,635,000 at December 31, 2008. Loan maturities and interest sensitivity of total loans, excluding residential real estate mortgages, leases, and consumer loans at December 31, 2009, are as follows (in thousands):

	Years to Maturity*			Total
	Within 1 Year	1-5 Years	Over 5 Years	
Commercial, Agricultural and Other	\$ 33,040	\$ 42,899	\$ 121,047	\$ 196,986
Construction and Land Development	17,704	1,777	2,489	21,970

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Total	\$ 50,744	\$ 44,676	\$ 123,536	\$ 218,956
Fixed Rate Loans	\$ 5,932	\$ 32,957	\$ 7,828	\$ 46,717
Variable Rate Loans	44,812	11,719	115,708	172,239
Total	\$ 50,744	\$ 44,676	\$ 123,536	\$ 218,956

\* Due to interest rate levels, economic conditions and other relevant factors, it is anticipated that there will be loans repaid prior to their contractual maturity dates.

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Management continues to focus lending on creditworthy consumers and businesses, with necessary consideration given to increased credit risks posed by the weak economy and the housing market. The economy and housing market, and increased unemployment, has affected some of our borrowers, resulting in an increase in nonperforming loans and credit losses.

*Allowance for Credit Losses.* In accordance with GAAP, the allowance for credit losses is maintained at a level believed by management to be adequate to absorb estimated probable loan and lease principal losses. The allowance for credit losses is established through provisions charged against net interest income. The uncollectible principal portion of impaired loans and leases is charged against the allowance for credit losses, and subsequent principal recoveries are credited to the allowance for credit losses.

Management's evaluation of the adequacy of the allowance is based on UNCB's past loan and lease loss experience, known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay (including the timing of future payments), the estimated value of any underlying collateral, composition of the loan portfolio, current economic conditions and other relevant qualitative factors. This evaluation is inherently subjective as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans and leases that may be susceptible to significant change.

The allowance for credit losses is evaluated based on an assessment of the losses inherent in the loan and lease portfolio. This assessment results in an allowance that consists of specific, general and unallocated components. The specific component relates to loans and leases that are classified as impaired. For such loans and leases, an allowance is established when (i) the discounted cash flows, or (ii) collateral value, or (iii) observable market price of the impaired loan or lease is lower than the carrying value. The general component covers all other loans and leases, including criticized loans that are not impaired, and is based on historical loss experience adjusted for relevant qualitative factors. Separate qualitative adjustments are made for higher-risk criticized loans that are not impaired. An unallocated component is maintained to cover uncertainties that could affect our 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 loan and lease portfolio.

UNNF continues to closely monitor the loan portfolio, and the underlying borrower financial performance and collateral values, identifying credit concerns and risks, including those resulting from the current weak economy. Future adjustments may be necessary to the allowance for credit losses, and consequently the provision for credit losses, if economic conditions or loan credit quality differ substantially from the assumptions management used in the evaluation of the level of the allowance compared to the balance of outstanding loans and leases. The allowance for credit losses was \$5,858,000 at December 31, 2009, compared to \$4,358,000 at December 31, 2008. The provision for credit losses for the year ended December 31, 2009, was significantly higher than the provision for credit losses for the year ended December 31, 2008 (for additional information, refer to the related discussion on *Provision for Credit Losses* on page 48) given the increased credit risks in the loan portfolio, including those resulting from the current weak economy and real estate markets, and due to loan charge-offs being significantly higher for the year ended December 31, 2009, compared to the same period in 2008. A provision for credit losses of \$2,627,000 was made for 2009. With the higher provision exceeding net loan charge-offs of \$1,127,000, the allowance for credit losses increased to 1.73% of loans at December 31, 2009 compared to 1.22% of loans at December 31, 2008. Management believes, based on information then currently available, that the allowance for credit losses as of December 31, 2009 of \$5,858,000 was adequate to meet potential credit losses at that date.

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The following table is a five year summary of the changes in the allowance for credit losses (dollars in thousands):

	2009	2008	2007	2006	2005
Allowance for Credit Losses, Beginning of Year	\$ 4,358	\$ 3,675	\$ 3,070	\$ 2,675	\$ 2,288
Charge-Offs:					
Real Estate	(11)			(11)	(150)
Consumer	(152)	(155)	(111)	(43)	(77)
Commercial, Industrial and Agricultural(1)	(1,026)	(209)	(526)	(285)	(100)
Total Charge-Offs	(1,189)	(364)	(637)	(339)	(327)
Recoveries:					
Real Estate				5	5
Consumer	10	14	3	14	9
Commercial, Industrial and Agricultural	52	6	2	43	19
Total Recoveries	62	20	5	62	33
Net Loans and Leases Charged-Off	(1,127)	(344)	(632)	(277)	(294)
Addition to Provision for Credit Losses	2,627	1,027	1,237	672	681
Allowance for Credit Losses, End of Year	\$ 5,858	\$ 4,358	\$ 3,675	\$ 3,070	\$ 2,675
Loans and Leases Average	\$ 350,307	\$ 369,554	\$ 357,795	\$ 318,251	\$ 280,245
Gross Loans and Leases Actual	\$ 339,274	\$ 358,280	\$ 364,337	\$ 341,113	\$ 300,213
Ratio of Gross Loans and Leases Charged Off to Average Loans and Leases	0.34%	0.10%	0.18%	0.11%	0.12%
Ratio of Allowance for Credit Losses to Gross Loans and Leases	1.73%	1.22%	1.01%	0.90%	0.89%

(1) Included in commercial loans were \$93,000, \$163,000 and \$38,000 of charge-offs in direct lease financing receivables in 2009, 2008 and 2007, respectively. There were no financing lease charge-offs in 2006 and 2005. There were no recoveries of financing leases in any of the periods presented.

The specific allocation in any particular category may be reallocated in the future to reflect current conditions. Accordingly, management considers the entire allowance to be available to absorb losses in any

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category. The following table sets forth an allocation of the allowance for credit losses by loan category (dollars in thousands):

	<b>Allowance Amount</b>	<b>Percentage Mix of Total Loans and Leases</b>
December 31, 2009:		
Commercial, Industrial and Agricultural Lease Financing Receivables	\$ 5,306	71%
Real Estate Residential Mortgages	91	1
Consumer	22	5
Unallocated	399	23
	40	
<b>Total Allowance for Credit Losses</b>	<b>\$ 5,858</b>	<b>100%</b>
December 31, 2008:		
Commercial, Industrial and Agricultural Lease Financing Receivables	\$ 3,066	71%
Real Estate Residential Mortgages	155	1
Consumer	102	5
Unallocated	991	23
	44	
<b>Total Allowance for Credit Losses</b>	<b>\$ 4,358</b>	<b>100%</b>
December 31, 2007:		
Commercial, Industrial and Agricultural Lease Financing Receivables	\$ 2,776	58%
Real Estate Residential Mortgages	152	2
Consumer	375	38
Unallocated	243	2
	129	
<b>Total Allowance for Credit Losses</b>	<b>\$ 3,675</b>	<b>100%</b>
December 31, 2006:		
Commercial, Industrial and Agricultural Lease Financing Receivables	\$ 2,228	58%
Real Estate Residential Mortgages	63	2
Consumer	469	38
Unallocated	92	2
	218	
<b>Total Allowance for Credit Losses</b>	<b>\$ 3,070</b>	<b>100%</b>
December 31, 2005:		
Commercial, Industrial and Agricultural Lease Financing Receivables	\$ 1,778	55%
Real Estate Residential Mortgages	25	1
	379	41



Consumer	135	3
Unallocated	358	
Total Allowance for Credit Losses	\$ 2,675	100%

*Impaired Loans.* Other than as described herein, management does not believe there are any trends, events or uncertainties that are reasonably expected to have a material impact on our loan and lease portfolio to affect future results of operations, liquidity or capital resources. However, based on known information,

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management believes that the effects of current and past economic conditions and other unfavorable business conditions may impact certain borrowers' abilities to comply with their repayment terms and therefore may have an adverse effect on future results of operations, liquidity, or capital resources. Management continues to closely monitor economic and business conditions and the impact on borrowers' financial strength. For certain loans and leases, management has determined that it is probable that all principal and interest payments due according to the contractual terms of the loan agreements will not be collected. These loans are considered to be impaired as defined by GAAP.

The balance of loans and leases that were considered to be impaired under GAAP was \$8,715,000 and \$9,360,000, which consisted of 10 and 16 loan and lease relationships to unrelated borrowers, at December 31, 2009 and 2008, respectively. At December 31, 2009, four of the relationships represented 90% of the total impaired loans and leases of \$8,715,000. The decrease in impaired loans and leases during 2009 was primarily the result of loan pay-offs through the loan workout process as well as charge-offs during the year. Management continues to diligently monitor and evaluate the existing portfolio, and identify credit concerns and risks, including those resulting from the current weak economy and real estate market. The measure of impairment is based primarily on the fair value of collateral securing these loans, which is primarily real estate and equipment.

*Impaired Loans with a Related Allowance.* We had \$5,916,000 and \$5,058,000 of impaired loans and leases with a related allowance for credit losses at December 31, 2009 and 2008, respectively. These consisted of five and eight loan and lease relationships to unrelated borrowers, with a related allowance for credit losses of \$1,458,000 and \$1,499,000 at December 31, 2009 and 2008, respectively. This group of impaired loans and leases has a related allowance due to the probability of the borrower not being able to continue to make principal and interest payments due under the contractual terms of the loan or lease. These loans and leases appear to have insufficient collateral and UNNF's principal may be at risk; as a result, a related allowance is necessary to cover future potential losses.

*Impaired Loans without a Related Allowance.* We had \$2,799,000 and \$4,302,000 of impaired loans and leases without a related allowance at December 31, 2009 and 2008, respectively. These consisted of five and eight loan and lease relationships to unrelated borrowers at December 31, 2009 and 2008, respectively. This group of impaired loans and leases is considered impaired due to the likelihood of the borrower not being able to continue to make principal and interest payments due under the contractual terms of the loan or lease. In addition, these loans and leases appear to have sufficient collateral and UNNF's principal does not appear to be at risk; as a result, management believes a related allowance is not necessary.

*Substandard Loans and Leases.* Under UNCB's current internal risk rating system, loans and leases with a rating of substandard that were performing, and not determined to be impaired amounted to \$32,410,000 and \$7,826,000 at December 31, 2009 and 2008, respectively. Despite these credits not being impaired, management believes these substandard credits reflect increased risks to the loan portfolio, including risks resulting from the current weak economy and real estate markets, and considered such increased risks in determining the provision for credit losses (refer to the related discussion on Provision for Credit Losses on page 48). Management continues to closely monitor the loan portfolio, and the underlying borrower financial performance and collateral values, identifying credit concerns and risks, including those resulting from the current weak economy. Management considers both impaired and these substandard loans to be potential problem loans, and believes that the current economic conditions may result in additional loans being classified or nonperforming throughout 2010.

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*Non-Performing Assets.* Nonperforming assets consist of nonperforming loans and leases, other real estate owned, and repossessed assets. The following table provides a five-year summary of nonperforming assets (dollars in thousands):

	2009	2008	December 31, 2007	2006	2005
Nonaccruing Loans	\$ 8,034	\$ 3,271	\$ 2,919	\$ 2,280	\$ 1,814
Accruing Loans 90 days or more past due	506	1,685	120	253	298
Total Nonperforming Loans and Leases	8,540	4,956	3,039	2,533	2,112
Other Real Estate Owned	5,383				
Repossessed Assets	436	479	156	358	214
Total Nonperforming Assets	\$ 14,359	\$ 5,435	\$ 3,195	\$ 2,891	\$ 2,326
Gross Loans and Leases	\$ 339,274	\$ 358,280	\$ 364,337	\$ 341,113	\$ 300,213
Allowance for Credit Losses	\$ 5,858	\$ 4,358	\$ 3,675	\$ 3,070	\$ 2,675
Nonperforming Loans and Leases as a % of Gross Loans and Leases	2.5%	1.4%	0.8%	0.7%	0.7%
Nonperforming Assets as a % of Total Assets	2.9%	1.1%	0.6%	0.6%	0.5%
Allowance for Credit Losses as a % of Nonperforming Loans and Leases	69%	88%	121%	121%	127%

Nonperforming loans and leases consist of loans and leases that are nonaccruing, and those that are 90 days or more past due. Nonaccruing loans and leases are no longer accruing interest income because of apparent financial difficulties of the borrower. Interest received on nonaccruing loans and leases is recorded as income only after the past due principal is brought current and deemed collectible in full. If nonaccrual loans and leases had been current and in accordance with their original terms, gross interest income of approximately \$417,000, \$151,000 and \$203,000 would have been recorded on such loans and leases for the years ended December 31, 2009, 2008 and 2007, respectively. There was no interest income recognized on nonaccruing loans and leases for the years ended December 31, 2009, 2008 and 2007. Total nonperforming loans and leases increased to \$8,540,000, or 2.5%, of gross loans and leases at December 31, 2009, compared to \$4,956,000, or 1.4% of gross loans and leases, at December 31, 2008. Management specifically evaluated the loans and leases that became nonperforming in 2009, and determined that most were well-secured by collateral, not warranting a proportional increase to the allowance for credit losses. Historically, the percentage of nonperforming loans to gross loans for the five-year period ending December 31, 2009, was an average of 1.2%. There were no transactions deemed to be troubled debt restructurings during 2009.

OREO includes assets acquired through foreclosure, deed in-lieu of foreclosure, and loans identified as in-substance foreclosures. A loan is classified as an in-substance foreclosure, when effective control of the collateral has been taken prior to completion of formal foreclosure proceedings. OREO is held for sale and is recorded at fair value less estimated costs to sell. Costs to maintain OREO and subsequent gains and losses attributable to OREO liquidation are included in the Consolidated Statements of Operations in other income and other expense as realized. No depreciation or amortization expense is recognized. At December 31, 2009, we had \$5,383,000 of OREO comprised primarily of a facility in Lancaster, PA housing a non-profit music school. At December 31, 2008, UNNF had no OREO.

Repossessed assets consist of (i) vehicles and other equipment acquired from lessees, who defaulted on their contractual lease obligation, and (ii) mobile homes where UNCB does not own the real estate. We had repossessed assets of \$436,000 and \$479,000 at December 31, 2009 and 2008, respectively.

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***Stockholders Equity***

Stockholders equity increased by \$542,000 to \$31,336,000 at December 31, 2009, compared to \$30,794,000 at December 31, 2008. The increase in stockholders equity was the result of \$1,218,000 of proceeds received (net of costs) on a preferred stock private placement offering and \$68,000 of proceeds received through the DRIP offset by decreases to retained earnings resulting from a net loss for the year and a decrease in accumulated other comprehensive income (loss) for the year.

The ratio of average stockholders equity to average assets, which measures the adequacy of capital, was 6.29% for 2009 compared to 6.15% for 2008. The increase in this ratio was primarily the result of an increase in stockholders equity resulting from the preferred stock private placement offering. We did not pay a dividend in 2009 and our board of directors believed it prudent for UNCB to fully maintain its strong, well-capitalized position in these uncertain economic times. Therefore, the decision was made not to pay dividends to stockholders in 2009 and 2008.

We maintain a DRIP for record holders of common stock to provide a convenient method of investing cash dividends payable upon their common stock and to provide participants with the opportunity to make voluntary cash payments, to purchase additional common stock shares at a 10% discount to the fair market value of the shares on the effective purchase date as defined by the DRIP. In 2009, eligible shareholders made voluntary cash payments totaling \$68,000, which were used to purchase 20,840 common shares.

*Regulatory Capital.* Bank regulatory authorities in the United States issue risk-based capital standards. These capital standards relate a bank's capital to the risk profile of its assets and provide the basis by which all banks are evaluated in terms of its capital adequacy. We and UNCB are 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 our consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, we and UNCB must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The 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 us and UNCB to maintain minimum amounts and ratios of Tier 1 capital to average assets and of total capital (as defined in the regulations) to risk-weighted assets.

As of December 31, 2009 and 2008, we and UNCB exceeded the current regulatory requirements to be considered a quantitatively well capitalized financial institution, i.e. a leverage ratio exceeding 5%, Tier 1 risk-based capital exceeding 6%, and total risk-based capital exceeding 10%.

In addition to the above requirements, effective September 30, 2009, the OCC established individual minimum capital requirements for UNCB. For additional information, refer to Note 18 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus. The specific capital requirements established for UNCB were 8% for Tier 1 capital to average total assets, 9.5% for Tier 1 capital to risk-based assets, and 12% for total capital to risk-based assets. At December 31, 2009, UNCB's measure of Tier 1 capital to average Total assets was 8.31%, Tier 1 capital to risk-based assets of 9.69% and total capital to risk-based assets of 12.37%. At December 31, 2009, all three ratios exceeded the respective individual minimum capital requirements established by the OCC.

Included in our Tier 1 capital is \$10,510,000 of trust capital securities issued through our the UNCT I and UNCT II subsidiaries. The balance of these trust capital securities, \$490,000, is included in our Tier 2 regulatory capital. In addition, included in our and UNCB s regulatory capital is \$6,000,000 of junior subordinated debentures issued by UNCB. These securities would become callable if the Federal Reserve makes a determination that trust capital securities can no longer be considered in regulatory capital.

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Regulatory capital requirements may be increased in the future. We will closely monitor and evaluate our capital position as the regulatory capital environment changes, and if regulatory capital requirements are changed.

*Restrictions.* Banking regulations limit the amount of investments, loans, extensions of credit and advances UNCB can make to UNNF at any time to 10% of UNCB's total regulatory capital. At December 31, 2009, this limitation amounted to approximately \$5,219,000. These regulations also require any such investment, loan, extension of credit or advance to be secured by securities having a market value in excess of the amount thereof.

UNCB is subject to certain restrictions in connection with the payment of dividends. National banking laws require the approval of the Office of the Comptroller of the Currency if the total of all dividends declared by a national bank in any calendar year exceeds the net profits of UNCB for that year (as defined) combined with UNCB's retained net operating results for the preceding two calendar years. Under this formula, UNCB's retained net operating results for the preceding two calendar years was (\$189,000). In 2010, UNCB may declare dividends to the parent company, UNNF, an amount equal to the net profits of UNCB in 2010 less \$189,000, up to the date of any such dividend declaration.

In addition, on January 28, 2010, we entered into an informal MOU with the FRB of Philadelphia. The MOU, which is not a written agreement for purposes of Section 8 of the Federal Deposit Insurance Act, requires us, among other things, to seek prior approval by the FRB before we (i) declare or pay dividends to shareholders, (ii) distribute interest, principal or other sums on UNCT I and UNCT II junior subordinated debentures, and (iii) incur, increase or guarantee any additional debt. Subsequent to December 31, 2009, the FRB did approve the quarterly interest payments for the first quarter of 2010 on the UNCT I and UNCT II junior subordinated debentures and the preferred stock dividend payments.

## **Results of Operations**

### ***Summary of Performance 2009 Compared to 2008***

#### ***Overview***

We reported a net loss of (\$715,000) for the year ended December 31, 2009, compared to net income of \$444,000 for the year ended December 31, 2008. Basic and diluted losses per share for 2009 were (\$0.26), compared to basic and diluted earnings per common share of \$0.17 for 2008. Operating results for 2009 were significantly reduced by (i) certain non-routine expenses, (ii) net interest margin compression, and (iii) an increased provision for credit losses, which are discussed in more detail below.

(i) Non-routine expenses for the year ended December 31, 2009, included \$237,000 related to the FDIC's special assessment on deposit-insured institutions, \$536,000 of penalties on the prepayment of FHLB debt, and \$1,504,000 of OTTI charges primarily related to private-issuer mortgage-backed securities and pooled trust-preferred debt securities that were downgraded to below-investment-grade. The OTTI charges were more than offset by \$1,841,000 of net realized gains on the sale of primarily U.S. Government guaranteed securities that had temporarily appreciated at certain periods during 2009.

(ii) Reduced earning asset yields in the low interest rate environment, while borrowing costs remained at higher fixed rates, resulted in a lower net interest margin in 2009 versus 2008. The variable rate structure of many of our loans reduced overall yield due to the persistent low market interest rates. As a result, interest and fees on loans and leases declined by 12% when comparing the year ended December 31, 2009 to the same period in 2008. A decrease in loans outstanding also contributed to the decline in interest income generated from loans and leases. Outstanding loans decreased by \$19 million from December 31, 2008 to December 31, 2009 due to (i) reduced loan demand from

creditworthy borrowers, and (ii) the impact of nearly \$10 million of loan participations sold for capital and risk management purposes. The lack of income from impaired and non-accruing investments, and reduced yields on re-invested proceeds from investment maturities and sales, contributed to lower investment interest income in 2009. We continued to take measures to reduce its cost of funds, prepaying \$17 million of higher-cost long-term debt with the FHLB during 2009, as well as prepaying



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an additional \$2.5 million subsequent to December 31, 2009. The taxable-equivalent net interest margin percentage for 2009 was 2.73%, compared to 3.28% for 2008.

(iii) Nonperforming loans and leases increased to 2.52% of total loans and leases at December 31, 2009, compared to 1.38% at December 31, 2008. The increasing trend in nonperforming loans is attributable primarily to stressed cash flows among certain commercial borrowers due largely to the weak economy and real estate market. We continue to closely monitor the loan portfolio and the adequacy of the loan loss reserve by regularly evaluating borrower financial performance and underlying collateral values. Accordingly, a significant provision for credit losses of \$2,627,000 was made for the year ended December 31, 2009, compared to \$1,027,000 for the year ended December 31, 2008. With the higher provision exceeding net loan charge-offs of \$1,127,000 for 2009, compared to \$344,000 in 2008, the allowance for credit losses increased to 1.73% of loans at December 31, 2009, compared to 1.22% of loans at December 31, 2008.

***Net Interest Income***

Net interest income, our primary source of revenue, is the amount by which interest income on loans and investments exceeds interest incurred on deposits and borrowings. The amount of net interest income is affected by changes in interest rates and by changes in the volume and mix of interest-sensitive assets and liabilities. Net interest income and corresponding yields are presented in the discussion and analysis below on a taxable-equivalent basis. Income from tax-exempt assets, primarily loans to or securities issued by state and local governments, is adjusted by an amount equivalent to the federal income taxes which would have been paid if the income received on these assets was taxable at the statutory rate of 34%.

Although the effective interest rate impact on earning assets and funding sources can be reasonably estimated at current interest rate levels, the options selected by customers, and the future mix of the loan, investment and deposit products in UNCB's portfolios, may significantly change the estimates used in the simulation models. In addition, our net interest income may be impacted by further interest rate actions of the Federal Reserve Bank.

Net interest income as adjusted for tax-exempt financial instruments was \$12,715,000 for the year ended December 31, 2009, compared to \$14,817,000 for the year ended December 31, 2008. The yield on interest-earning assets decreased by 113 basis points to 5.15% for 2009, compared to 6.28% for 2008. The interest rate paid on average interest-bearing liabilities decreased by 63 basis points to 2.69% for 2009, compared to 3.32% for 2008. Reduced earning asset yields in the low interest rate environment, while borrowing costs remained at higher fixed rates, resulted in a lower net interest margin in 2009 versus 2008. The taxable-equivalent net interest margin percentage for 2009 was 2.73%, compared to 3.28% for 2008.

Interest and fees on loans and leases on a taxable-equivalent basis decreased by \$3,063,000, or by 12%, to \$21,754,000 for the year ended December 31, 2009, compared to \$24,817,000 for the year ended December 31, 2008. The average yield decreased by 51 basis points to 6.21% for 2009, compared to 6.72% for 2008. The variable rate structure of many of our loans reduced overall yield due to the persistent low market interest rates and a decrease in loans outstanding also contributed to the decline in interest income generated from loans and leases. The average balance of loans and leases decreased by \$19,247,000 in 2009, compared to 2008 due to reduced loan demand from creditworthy borrowers, and the impact of nearly \$10 million of loan participations sold for capital and risk management purposes.

Interest and dividends earned on investment securities on a taxable-equivalent basis decreased by \$1,233,000, or by 38%, to \$1,976,000 for the year ended December 31, 2009, compared to \$3,209,000 for the year ended December 31, 2008. The lack of income from impaired and non-accruing investments, and reduced yields on re-invested proceeds from investment maturities and sales, contributed to lower investment interest income in 2009. As a result, the average

yield decreased by 172 basis points to 2.89% for 2009, compared to 4.61% for 2008.

Interest expense on deposits decreased by \$1,076,000, or by 11%, to \$8,394,000 for the year ended December 31, 2009, compared to \$9,470,000 for the year ended December 31, 2008. A decrease in average

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rate of 56 basis points to 2.32% for 2009, compared to 2.88% for 2008 more than offset additional interest expense from a \$32,843,000 increase in the average balance of deposits.

Interest expense on long-term debt decreased by \$741,000, or by 27%, to \$2,054,000 for the year ended December 31, 2009, compared to \$2,795,000 for the year ended December 31, 2008. During 2009, we continued to take measures to reduce our cost of funds, prepaying \$17,000,000 of higher-cost long-term debt with the FHLB, which resulted in a \$14,115,000 decrease in the average balance of long-term debt for 2009, compared to 2008.

**Table of Contents*****Distribution of Assets, Liabilities and Stockholders Equity***

The table below provides average asset and liability balances and the corresponding interest income and expense along with the average interest yields (assets) and interest rates (liabilities) for the years 2009, 2008 and 2007. Interest income and the average interest yields are presented on a taxable-equivalent basis (dollars in thousands).

	Years Ended December 31,								
	2009			2008			2007		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate
<b>Assets</b>									
Interest-Earning Cash in Other Banks	\$ 27,233	\$ 70	0.26%	\$ 165	\$ 6	3.64%	\$ 197	\$ 10	5.0%
Interest-Earning Time Deposits in Other Banks	9,622	143	1.49	1,077	36	3.34			
General Funds Sold	7,010	18	0.26	8,503	214	2.52	9,363	459	4.9%
Investment Securities:(a)									
Available	64,060	1,734	2.71	69,618	3,209	4.61	65,255	3,358	5.1%
Non-Exempt(c)	4,201	242	5.76				8,334	610	7.3%
Leases and Leases(b),(c),(d)	350,307	21,754	6.21	369,554	24,817	6.72	357,795	27,092	7.5%
Restricted Investment in Common Stocks	3,705	40	1.08	3,365	114	3.39	3,950	290	7.3%
Total Earning Assets	466,138	24,001	5.15%	452,282	28,396	6.28%	444,894	31,819	7.1%
Provision for Credit Losses	(4,529)			(3,798)			(3,363)		
Total Interest-Earning Assets	40,664			40,234			38,870		
Total Assets	\$ 502,273			\$ 488,718			\$ 480,401		
<b>Liabilities and Stockholders Equity</b>									
<b>Interest-Bearing Liabilities:</b>									
<b>Interest-Bearing Demand</b>									
Deposits	\$ 133,525	1,458	1.09%	\$ 127,128	1,988	1.56%	\$ 120,637	3,174	2.6%
Savings Deposits	23,607	64	0.27	23,589	66	0.28	25,367	77	0.3%
Money Market Deposits	10,845	508	4.68	14,381	828	5.76	25,211	1,262	5.0%
Other Time Deposits	193,218	6,364	3.29	163,254	6,588	4.04	134,142	6,277	4.6%
Total Demand Deposits	361,195	8,394	2.32	328,352	9,470	2.88	305,357	10,790	3.5%
Short-Term Borrowings				9,090	210	2.31	6,025	299	4.9%
Long-Term Debt	40,386	2,054	5.09	54,501	2,795	5.13	72,586	3,652	5.0%
Junior Subordinated Ventures	17,341	838	4.83	17,341	1,104	6.37	17,341	1,268	7.3%
Total Interest-Bearing Liabilities	418,922	11,286	2.69%	409,284	13,579	3.32%	401,309	16,009	3.9%

Interest Bearing						
Liabilities:						
Demand Deposits	48,310		46,342		46,393	
Other Liabilities	3,439		3,045		3,634	
Stockholders' Equity	31,602		30,047		29,065	
Total Stockholders' Equity	\$ 502,273		\$ 488,718		\$ 480,401	
Interest Income/Spread	\$ 12,715	2.46%	\$ 14,817	2.96%	\$ 15,810	3.1%
Interest Margin		2.73%		3.28%		3.5%

(a) Balances reflect amortized historical cost for available-for-sale securities. The related average unrealized holding gain or loss on securities is included in other non interest-earning assets.

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- (b) Balances of nonaccrual loans and related income recognized have been included for computational purposes.
- (c) Tax-exempt income included in loans and securities has been adjusted to a taxable-equivalent basis using an incremental rate of 34%.
- (d) Includes loan fees of \$481,000 for the year ended December 31, 2009, \$798,000 for the year ended December 31, 2008, and \$771,000 for the year ended December 31, 2007.

**Rate/Volume Analysis of Net Interest Income**

The table below shows changes attributable to the volume and rate components of net interest income on a taxable equivalent basis (in thousands):

	2009 Compared to 2008			2008 Compared to 2007		
	Volume(a)	Rate(a)	Total	Volume(a)	Rate(a)	Total
<b>Interest Earning Assets:</b>						
Interest Bearing Deposits in Other Banks	\$ 984	\$ (920)	\$ 64	\$ (2)	\$ (2)	\$ (4)
Interest Bearing Time Deposits in Other Banks	286	(179)	107	36		36
Federal Funds Sold	(38)	(158)	(196)	(42)	(203)	(245)
<b>Investment Securities:</b>						
Taxable	(256)	(1,219)	(1,475)	226	(375)	(149)
Tax-Exempt(c)		242	242	(610)		(610)
Loans and Leases Net(b),(c)	(1,293)	(1,770)	(3,063)	878	(3,153)	(2,275)
Restricted Investment in Bank Stocks	12	(86)	(74)	(43)	(133)	(176)
<b>Total Earning Assets</b>	<b>(305)</b>	<b>(4,090)</b>	<b>(4,395)</b>	<b>443</b>	<b>(3,866)</b>	<b>(3,423)</b>
<b>Interest-Bearing Liabilities:</b>						
Interest-Bearing Demand Deposits	100	(630)	(530)	172	(1,358)	(1,186)
Savings Deposits		(2)	(2)	(5)	(6)	(11)
Brokered Deposits	(204)	(116)	(320)	(541)	107	(434)
Other Time Deposits	1,209	(1,433)	(224)	1,375	(1,064)	311
<b>Total Deposits</b>	<b>1,105</b>	<b>(2,181)</b>	<b>(1,076)</b>	<b>1,001</b>	<b>(2,321)</b>	<b>(1,320)</b>
Short-Term Borrowings	(210)		(210)	152	(241)	(89)
Long-Term Debt	(741)		(741)	(905)	48	(857)
Junior Subordinated Debentures		(266)	(266)		(164)	(164)
<b>Total Interest-Bearing Liabilities</b>	<b>154</b>	<b>(2,447)</b>	<b>(2,293)</b>	<b>248</b>	<b>(2,678)</b>	<b>(2,430)</b>
<b>Net Interest Income</b>	<b>\$ (459)</b>	<b>\$ (1,643)</b>	<b>\$ (2,102)</b>	<b>\$ 195</b>	<b>\$ (1,188)</b>	<b>\$ (993)</b>

(a)

The change in interest due to both volume and rate has been allocated individually to the change in volume and rate on a proportional basis.

- (b) The balance of nonaccrual loans and related income recognized have been included for computational purposes.
- (c) Tax-exempt income included in loans and securities has been adjusted to a taxable-equivalent basis using an incremental rate of 34%.

***Provision for Credit Losses***

The provision for credit losses is an expense charged against net interest income to provide for estimated losses attributable to uncollectible loans and leases. The provision is based on management's analysis of the

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adequacy of the allowance for credit losses. The provision for credit losses was \$2,627,000 for the year ended December 31, 2009, compared to \$1,027,000 for the same period in 2008. The increased provision was the result of increased credit risk related to additional substandard rated credits at December 31, 2009, compared to December 31, 2008 (refer to the related discussion on *Substandard Loans and Leases* on page 37) and an increase in loans charged-off during 2009 compared to the same period in 2008. Management continues to closely monitor the loan portfolio and the adequacy of the allowance for credit loss reserve considering underlying borrower financial performance and collateral values, and increasing credit risks. Future adjustments may be necessary to the provision for credit losses, and consequently the allowance for credit losses, if economic conditions or loan credit quality differ substantially from the assumptions we used in making our evaluation of the level of the allowance for credit losses compared to the balance of outstanding loans and leases (refer to the related discussion on *Allowance for Credit Losses* on page 34).

***Non-Interest Income***

Non-interest income increased by \$1,568,000, or by 41%, to \$5,375,000 for the year ended December 31, 2009, compared to \$3,807,000 for the same period in 2008. Increases (decreases) in the components of non-interest income when comparing the year ended December 31, 2009 to 2008 are as follows (in thousands):

<b>Non-Interest Income</b>	<b>Year Ended</b>		<b>Increase (Decrease)</b>
	<b>2009</b>	<b>2008</b>	
Service Charges on Deposit Accounts	\$ 2,158	\$ 1,950	\$ 208
Other Service Charges, Commissions, Fees	1,154	1,091	63
Alternative Investment Sales Commissions	662	814	(152)
Income from Fiduciary Activities	180	309	(129)
Earnings from Bank-Owned Life Insurance	431	439	(8)
Mortgage Banking/Brokerage Activities	112	56	56
Other Income	341	186	155
Net Gain on Sale of Investment Securities	1,841	252	1,589
Less: Impairment Charge on Investment Securities	(1,504)	(1,290)	(214)
Net Investment Securities Gains (Losses)	337	(1,038)	1,375
Total Non-Interest Income	\$ 5,375	\$ 3,807	\$ 1,568

A significant portion of the increase in non-interest income was related to net investment securities gains. Realized gains on the sale of investment securities were \$1,841,000 for the year ended December 31, 2009, compared to \$252,000 for the same period in 2008. These investment sales activities related to continued repositioning of the investment portfolio to a lower-risk profile that more effectively supports liquidity, capital, and interest rate risk management, while providing realized gains to offset the impact of investment securities impairment charges. Other-than-temporary investment impairment charges of \$1,504,000 were recognized during the year ended December 31, 2009, related to investment securities that were downgraded to below investment grade. Other-than-temporary investment impairment charges of \$1,290,000 were recognized during the year ended December 31, 2008. The total impairment charges for the year ended December 31, 2009 of \$1,504,000 were more than offset by realized net gains on the sale of investment securities of \$1,841,000.



The increase in other income was the result of a \$279,000 insurance settlement against losses from loans which were fraudulently or otherwise improperly made by one former employee. The settlement provided for substantial reimbursement of a one-time charge of \$370,000 which was recorded and previously disclosed in 2008 related to the irregular activity. Subsequent to December 31, 2009, we received an additional \$7,000 as final settlement and legal restitution from the former employee. This was offset by \$96,000 of income generated from a cash bailment agreement on a network of ATM machines in 2008. This agreement was terminated during the first quarter of 2008 and previously provided transaction fee income. Accordingly, operating results for the year ended December 31, 2009, did not reflect any income generated from this

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agreement, whereas, the operating results for the same period in 2008 reflected income for the first quarter of 2008.

The increase in service charges on deposit accounts was the result of an increase in deposits, which grew by 6% since December 31, 2008. The overall growth in deposits resulted in increased fee income as well as an operational change in the posting of transactions, which impacted net overdraft fee income. The decrease in alternative investment sales commissions was primarily the result of a turbulent investment market and a weak economy, which negatively impacted growth and sales opportunities. The decrease associated with income from fiduciary activities was primarily the result of fewer estate fees.

***Non-Interest Expense***

For the year ended December 31, 2009, non-interest expense decreased by \$381,000, or by 2%, compared to the year ended December 31, 2008. Increases (decreases) in the components of non-interest expense when comparing the year ended December 31, 2009 to 2008 are as follows (in thousands):

<b>Non-Interest Expense</b>	<b>Year Ended</b>		<b>Increase (Decrease)</b>
	<b>2009</b>	<b>2008</b>	
Salaries, Wages, and Employee Benefits	\$ 7,033	\$ 7,676	\$ (643)
Net Occupancy	1,724	1,818	(94)
Data and ATM Processing	1,681	1,641	40
Professional Fees and Regulatory Assessments	1,160	1,036	124
Furniture and Equipment	935	1,017	(82)
FDIC Insurance	1,128	404	724
Pennsylvania Shares Tax	297	273	24
Advertising and Marketing	211	412	(201)
Supplies and Postage	367	401	(34)
Other Expense	2,201	2,440	(239)
<b>Total Non-Interest Expense</b>	<b>\$ 16,737</b>	<b>\$ 17,118</b>	<b>\$ (381)</b>

UNNF has focused on lowering core operating costs and creating efficiencies in a difficult economy, when income growth is challenging, by exploring cost cutting initiatives. The discussion that follows explains the changes in the components of non-interest expense when comparing the year ended December 31, 2009 to the same period in 2008.

Salaries, wages and employee benefits decreased by \$643,000 for the year ended December 31, 2009 compared to the same period in 2008. The decrease was related to positions that were eliminated in the fourth quarter of 2008 and the first quarter of 2009, savings in health care costs, and savings from the elimination of the company 401-K match during the second quarter of 2009.

The increase in professional fees and regulatory assessments was related to an increase in audit fees and legal expenses. We use a third party vendor to perform the internal audit function. During 2008, we were in the process of switching third party vendors to a new relationship. As a result, professional fees and regulatory assessments did not include a full years worth of expenses associated with internal audit services for the year ended December 31, 2008, whereas, the year ended December 31, 2009, included internal audit expenses for the full year. Legal expenses increased primarily due to a third party vendor utilized to help mitigate problem loans, which have become more

prevalent primarily due to stressed cash flows among certain commercial borrowers resulting from the weak economy and real estate market.

Due to recent changes and assessments by the FDIC, FDIC insurance assessments amounted to \$1,128,000 for the entire year of 2009, representing a \$724,000 or 179% increase over the entire year of 2008. The increase in FDIC insurance premiums is the direct result of increased base assessment rates and an emergency special assessment, as determined by the FDIC. The FDIC Board adopted an interim rule imposing

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an emergency special assessment on the industry on June 30, 2009. Our emergency special assessment amounted to \$237,000. The interim rule would also permit the FDIC Board to impose another similar emergency special assessment after June 30, 2009, if necessary, to maintain public confidence in federal deposit insurance. On November 12, 2009, the FDIC board of directors voted to require insured depository institutions to prepay, on December 30, 2009, their estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011, and 2012 (see related discussion on Federal Deposit Insurance Corporation Activity on page 57).

For the year ended December 31, 2009, the decrease in advertising and marketing expense was part of operating more efficiently in a difficult economy.

The decrease in other expense included a decrease in employee related expenses such as training, travel, seminars, and staff recruitment and a decrease in the expense paid for coffee in UNCB's gold café branches. In addition, in 2009, UNCB continued with certain cost-reducing de-leveraging activities by using funds from low-interest earning assets and low-interest cost short-term borrowings to pay down higher interest cost long-term debt. During the year ended December 31, 2009 and 2008, UNCB prepaid \$17,000,000 and \$18,482,000 of FHLB advances, respectively. In conjunction with the prepayments, UNCB incurred \$536,000 and \$72,000 of prepayment penalties for the years ended December 31, 2009 and 2008, respectively, which were included in other non-interest expense. The year ended December 31, 2008 included a loss of \$370,000 related to certain fraudulent loans made by a former employee.

**Income Taxes**

For the year ended December 31, 2009, an income tax benefit was recorded for \$802,000, which primarily resulted from a pre-tax loss, compared to an income tax benefit of \$188,000 for the same period in 2008. Generally, our effective tax rate is below the statutory rate due to tax-exempt earnings on loans, investments, and bank-owned life insurance, and the impact of tax credits. In accordance with ASC Topic 740, *Income Taxes*, no adjustments have been recorded for unrecognized income tax benefits for the periods ended December 31, 2009 and 2008. The realization of deferred tax assets is dependent on future earnings. Management anticipates that future earnings will be adequate to fully utilize deferred tax assets.

**Year Ended December 31, 2008 Compared to Year Ended December 31, 2007****Overview**

We reported net income of \$444,000 for the year ended December 31, 2008, compared to net income of \$312,000 for the year ended December 31, 2007. Basic and diluted earnings per share for 2008 were \$0.17, compared to basic and diluted earnings per share of \$0.12 for 2007. The discussion that follows further explains the changes in the components of net income when comparing the year ended December 31, 2008, to the year ended December 31, 2007.

***Net Interest Income***

Net interest income as adjusted for tax-exempt financial instruments was \$14,817,000 for the year ended December 31, 2008, compared to \$15,810,000 for the year ended December 31, 2007. The yield on interest-earning assets decreased by 87 basis points to 6.28% for 2008, compared to 7.15% for 2007. The interest rate paid on average interest-bearing liabilities decreased by 67 basis points to 3.32% for 2008, compared to 3.99% for 2007. With the decline in interest rates, including the market prime rate decreasing 4% through 2008, our interest rates on interest-earning assets re-priced lower and more quickly than interest-bearing liabilities, resulting in a lower net interest margin in 2008 versus 2007. The taxable-equivalent net interest margin for 2008 was 3.28%, compared to 3.55% for 2007.

Interest and fees on loans and leases decreased by \$2,275,000 to \$24,817,000 for the year ended December 31, 2008, compared to \$27,092,000 for the year ended December 31, 2007. A decrease in average yield of 85 basis points due to interest rate cuts during the year more than offset additional earnings from a \$11,759,000 increase in the average balance of loans and leases from 2007 to 2008.

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Interest and dividends earned on investment securities decreased by \$759,000 to \$3,209,000 for the year ended December 31, 2008, compared to \$3,968,000 for the year ended December 31, 2007. A decrease in the average yield of 78 basis points due to both market rate reductions and generally lower risk investments, coupled with a \$3,971,000 decrease in the average balance of investment securities, resulted in less interest earned on investment securities in comparison to 2007.

Interest expense on deposits decreased by \$1,320,000 to \$9,470,000 for the year ended December 31, 2008, compared to \$10,790,000 for the year ended December 31, 2007. A decrease in average rate of 65 basis points due to interest rate cuts in the past year more than offset additional interest expense from a \$22,995,000 increase in the average balance of deposits. UNNF's average rate on interest-bearing deposits was 2.88% for 2008 compared to 3.53% for 2007.

Interest expense on long-term debt was \$2,795,000 for the year ended December 31, 2008, compared to \$3,652,000 for the year ended December 31, 2007. The \$857,000 decrease was primarily the result of an \$18,085,000 decrease in the average balance of long-term debt. In 2008, UNNF continued with certain cost-reducing de-leveraging activities by using funds from low-interest earning assets and low-interest cost short-term borrowings to pay down higher interest cost long-term debt. As a result, UNCB prepaid a total of \$18,482,000 of FHLB long-term advances, reducing total FHLB long-term borrowings outstanding to \$50,334,000 at December 31, 2008, compared to \$68,816,000 at December 31, 2007.

***Provision for Credit Losses***

The provision for credit losses is an expense charged to earnings to provide for estimated losses attributable to uncollectible loans and leases. The provision is based on our analysis of the adequacy of the allowance for credit losses. The provision for credit losses was \$1,027,000 for the year ended December 31, 2008, compared to \$1,237,000 for the year ended December 31, 2007. Future adjustments may be necessary to the provision for credit losses, and consequently the allowance for credit losses, if economic conditions or loan credit quality differ substantially from the assumptions we used in making our evaluation of the level of the allowance for credit losses compared to the balance of outstanding loans and leases. See additional discussion in the section *Allowance for Credit Losses* on page 34.

***Non-Interest Income***

For the year ended December 31, 2008, non-interest income decreased by \$2,702,000 or 42% compared to the year ended December 31, 2007. Increases (decreases) in the components of non-interest income when comparing the year ended December 31, 2008 to 2007 are as follows (in thousands):

<b>Non-Interest Income</b>	<b>Year Ended</b>		<b>Increase (Decrease)</b>
	<b>December 31, 2008</b>	<b>2007</b>	
Service Charges on Deposit Accounts	\$ 1,950	\$ 1,864	\$ 86
Other Service Charges, Commissions, Fees	1,091	1,059	32
Alternative Investment Sales Commissions	814	845	(31)
Income from Fiduciary Activities	309	347	(38)
Earnings from Bank-Owned Life Insurance	439	426	13
Mortgage Banking/Brokerage Activities	56	2,000	(1,944)
Title Insurance/Settlement Income		317	(317)
Other Income	186	362	(176)

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Net Gain on Sale of Investment Securities	252	89	163
Less: Impairment Charge on Investment Securities	(1,290)	(800)	(490)
Net Investment Securities Gains (Losses)	(1,038)	(711)	(327)
Total Non-Interest Income	\$ 3,807	\$ 6,509	\$ (2,702)

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Much of the decrease in non-interest income was primarily due to reductions in mortgage banking income related to the closure in 2007 of our mortgage brokerage subsidiary, Home Team. For related discussion, see Note 16 Residential Mortgage Business Venture to the consolidated financial statements included elsewhere in this proxy statement/prospectus. Accordingly, consolidated operating results for the year ended December 31, 2008, reflected no mortgage brokerage and title insurance income related to Home Team. Consolidated operating results for the year ended December 31, 2007, included \$1,932,000 of mortgage brokerage income and \$317,000 of title insurance/settlement income related to Home Team.

In December 2008, we recorded \$1,290,000 of impairment charges resulting from fair value reductions in two of our investment securities which are not guaranteed by agencies of the U.S. government. We determined that, due to severe illiquidity and distress in the financial markets, the unrealized declines in the value of these investments were other-than-temporary, requiring the write-down in value. The results for the year ended December 31, 2007 included \$800,000 of other-than-temporary investment impairment charges related to certain corporate debt securities. The impairment charges incurred in 2008 and 2007 are described in more detail in Note 3 Investment Securities Available For Sale to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

For the year ended December 31, 2008, we realized gains on sales of investment securities of \$252,000 compared to \$89,000 for the year ended December 31, 2007. The 2008 investment sales activity related to continued repositioning of our investment portfolio to a lower-risk profile that more effectively supports liquidity and capital management. The 2007 investment sales activity related to securities sold as part of 2007 de-leveraging activities.

***Non-Interest Expense***

For the year ended December 31, 2008, non-interest expense decreased by \$3,627,000 or 17% compared to the year ended December 31, 2007. Increases (decreases) in the components of non-interest expense when comparing the year ended December 31, 2008 to 2007 are as follows (in thousands):

<b>Non-Interest Expense</b>	<b>Year Ended</b>		<b>Increase (Decrease)</b>
	<b>December 31, 2008</b>	<b>2007</b>	
Salaries, Wages, and Employee Benefits	\$ 7,676	\$ 9,723	\$ (2,047)
Net Occupancy	1,818	2,390	(572)
Data and ATM Processing	1,641	1,662	(21)
Professional Fees and Regulatory Assessments	1,036	1,516	(480)
Furniture and Equipment	1,017	1,081	(64)
FDIC Insurance	404	137	267
Pennsylvania Shares Tax	273	243	30
Advertising and Marketing	412	653	(241)
Supplies and Postage	401	377	24
Restructuring Charge		717	(717)
Other Expense	2,440	2,246	194
<b>Total Non-Interest Expense</b>	<b>\$ 17,118</b>	<b>\$ 20,745</b>	<b>\$ (3,627)</b>

The decrease in salaries, wages, and employee benefits expense reflect the savings impact realized from the 2007 staff restructuring, as well as the staff reductions from the closure of operations of Home Team during 2007.



Net occupancy expense decreased due to 2007 including a charge of \$259,000 for a commitment on a parcel of real estate which was to be used for a future retail branch site. In addition, we reduced our net occupancy expense in 2008 by \$197,000 from subleasing two-thirds of our corporate office facility.

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Professional fees and regulatory assessments decreased primarily due to 2007 having additional expenses related to a nonrecurring profit improvement consulting engagement, and consulting and legal fees associated with the 2007 restructuring and complying with the MOU with the OCC. Effective August 27, 2009, UNCB entered into a formal written agreement, or the Agreement, with the OCC. The Agreement supersedes the previous MOU between UNCB and the OCC. For additional information, refer to Note 18 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

Advertising and marketing expenses were higher in 2007 due to marketing expenses related to the now closed Home Team subsidiary.

FDIC insurance premiums increased as the result of a one-time assessment credit which reduced the 2007 expense, and additional premium assessments due to UNCB's status under the MOU. Effective August 27, 2009, UNCB entered into a formal written agreement with the OCC. The Agreement supersedes the previous MOU between UNCB and the OCC. For additional information, refer to Note 18 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

The restructuring charge, as described in Note 17 to the consolidated financial statements included elsewhere in this proxy statement/prospectus, consisted of staff reorganization severance and related costs incurred in 2007.

Other expense variances include the following:

2008 included a one-time charge of \$370,000 that related to certain fraudulent loans made by one employee who has since been terminated. Based upon our investigation of the matter, there were not any additional losses or the involvement of other employees. We evaluated the impact of this incident on current internal controls and procedures and implemented changes necessary to strengthen control processes and address the issues raised by this isolated event. The appropriate governmental authorities were notified and we have cooperated fully with respect to the authorities' investigation. During 2009, a \$279,000 insurance settlement was received and provided for substantial reimbursement of the one-time charge. Subsequent to December 31, 2009, we received an additional \$7,000 as final settlement and legal restitution from the former employee.

We prepaid \$18,482,000 of FHLB advances during 2008, which resulted in \$72,000 of prepayment penalties which were recorded in other non-interest expense.

Other Expense for 2007 included \$157,000 related to the impairment of previously recorded goodwill and minority interest assets associated with our ownership of Home Team.

## **Income Taxes**

We realized a net benefit for income taxes of \$188,000 for 2008, compared to \$421,000 for 2007. Generally, UNCF's effective tax rate is below the statutory rate due to tax-exempt earnings on loans, investments, and bank-owned life insurance, and the impact of tax credits. The realization of deferred tax assets is dependent on future earnings. As a result of our adoption of ASC Topic 740, Income Taxes effective January 1, 2007, no significant income tax uncertainties were identified, therefore, we recognized no adjustment for unrecognized income tax benefits for the periods ended December 31, 2008 and 2007. We currently anticipate that future earnings will be adequate to fully utilize deferred tax assets.

## **Recent Accounting Pronouncements**

Refer to Note 1 Summary of Significant Accounting Policies to the consolidated financial statements included elsewhere in this proxy statement/prospectus for a discussion of recently issued accounting standards.

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### **Liquidity**

Our objective is to maintain adequate liquidity to meet funding needs at a reasonable cost and to provide contingency plans to meet unanticipated funding needs or a loss of funding sources, while minimizing interest rate risk. Adequate liquidity provides resources for credit needs of borrowers, for depositor withdrawals and for funding corporate operations. Sources of liquidity are as follows:

A growing core retail deposit base;

Proceeds from the sale or maturity of investment securities;

Payments received on loans and mortgage-backed securities; and,

Overnight correspondent bank borrowings credit lines, and borrowing capacity available from the Federal Reserve Bank.

Management believes that UNCB's core deposits are fairly stable. Liquidity and funds management is governed by policies and measured on a monthly basis. These measurements indicate that liquidity generally remains stable and exceeds our minimum defined levels of adequacy. Other than the trends of continued competitive pressures and volatile interest rates, there are no known demands, commitments, events or uncertainties that will result in, or that are reasonably likely to result in, liquidity increasing or decreasing in any material way.

In 2009, UNCB focused on growing low-cost retail deposits, while reducing high-cost wholesale funding (i.e., FHLB advances and brokered time deposits). For the year, low-cost retail deposits increased by \$22,732,000, or 12%, while high-cost wholesale funding decreased by \$22,717,000 or 36%. As of December 31, 2009 and 2008, the ratio of wholesale funding to total assets was 8% and 13%, respectively. The decrease in the percentage of these wholesale funding sources was attributable to the de-leveraging which is discussed in Note 17 De-Leveraging and Restructuring Activities to the consolidated financial statements included elsewhere in this proxy statement/prospectus. As such, UNCB prepaid \$17,000,000 of FHLB advances in 2009. Overall, total deposits grew by \$21,188,000 or 6% during 2009.

UNCB has a line of credit with a correspondent bank amounting to \$7,000,000 for overnight federal funds borrowings, none of which was outstanding at December 31, 2009, 2008 or 2007. UNCB also has the ability to borrow overnight funds through the Federal Reserve discount window, which amounted to \$14,839,000 at December 31, 2009. The Federal Reserve borrowing capacity is collateralized by \$15,151,000 of investment securities at December 31, 2009.

In 2008, UNCB had an agreement with the FHLB, for a line of credit available in the amount of \$15,000,000. As a result of the formal agreement entered into with the OCC during 2009. For additional information, refer to Note 18 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus, the \$15,000,000 line of credit is no longer available without UNCB providing collateral to the FHLB. UNCB did not pledge collateral to the FHLB at December 31, 2009.

In 2009, we raised \$1,275,000 (prior to offering costs) through a preferred stock private placement offering. In 2008, \$1,635,000 was obtained (prior to offering costs), through a common stock private placement offering. Both of these private placement stock offerings are discussed in Note 19 Stock Issued Under Private Placement Offerings and Dividend Reinvestment Plan to the consolidated financial statements included elsewhere in this proxy

statement/prospectus.

We have obtained \$17,341,000 of funding in the past through the issuance of junior subordinated debentures as described in Note 11 Junior Subordinated Debentures to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

**Table of Contents****Off-Balance Sheet Arrangements and Aggregate Contractual Obligations**

The following table represents our on and off-balance sheet aggregate contractual obligations to make future payments as of December 31, 2009 (in thousands):

	<b>Less Than 1 Year</b>	<b>1-3 Years</b>	<b>4-5 Years</b>	<b>Over 5 Years</b>	<b>Total</b>
Time Deposits	\$ 117,543	\$ 63,735	\$ 10,949	\$ 81	\$ 192,308
Long-Term Debt	12,500	20,834			33,334
Junior Subordinated Debentures				17,341	17,341
Operating Leases	361	811	980	2,932	5,084
<b>Total</b>	<b>\$ 130,404</b>	<b>\$ 85,380</b>	<b>\$ 11,929</b>	<b>\$ 20,354</b>	<b>\$ 248,067</b>

In addition, in the normal conduct of business operations, contracts for services are routinely entered into. These contracts may require payment for services to be provided in the future and may also contain penalty clauses for the early termination of the contracts. We have contracted with our core data processor for certain services including transaction processing, branch automation and communication services, trust processing, ATM processing and various other services. The current contract was renegotiated in January 2007 with a maturity date of November 2013. Any early termination would require the payment of a substantial penalty. Payments under this contract amounted to \$1,021,000 for the year ended December 31, 2009. Future payments under this contract will vary based on transaction and account volumes and may also reflect inflationary cost adjustments.

We are not aware of any other commitments or contingent liabilities which may have a material adverse impact on our liquidity or capital resources.

We are also party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our customers. These financial instruments include commitments to extend credit and standby letters of credit, which are discussed in Note 14 Commitments, Guarantees and Contingencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

**Inflation**

Inflation has some impact on our operating costs, but unlike many other corporations, substantially all of our assets and liabilities are monetary in nature. As a result, changes in interest rates have a more significant impact on our performance than the general level of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as prices of goods and services. The effects of changes in interest rates are discussed in the following section on Market Risk Interest Rate Risk.

**Market Risk Interest Rate Risk**

As a financial institution, our primary component of market risk is interest rate volatility. Fluctuations in interest rates will ultimately impact the level of income and expense recorded on a large portion of our assets and liabilities. The nature of our current operations is such that we are not subject to foreign currency exchange or commodity price risk.

We do not own any trading assets.

The objective of interest rate risk management is to maintain or increase net interest income over a broad range of market interest rate movements. The Asset and Liability Management Committee is responsible for managing interest rate risk using policies approved by our board of directors. We manage interest rate risk by changing the mix or repricing characteristics of our investment securities portfolio and borrowings, and by the pricing, structure, and promotion of our specific loan and deposit products. We retain an outside consulting group to assist in monitoring our interest rate risk using a net interest income simulation model on a quarterly basis. The simulation model measures the sensitivity of future net interest income to hypothetical changes in market interest rates.

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In addition, we utilize an interest rate-sensitivity report called a *Gap* report, which illustrates the time intervals of cash flows or the next repricing date of interest-earning assets and interest-bearing liabilities. Our *Gap* report at December 31, 2009 reflects a negative rate-sensitivity position throughout the first year, meaning that our rate-sensitive liabilities exceed our rate-sensitive assets. The following analysis reflects cumulative rate-sensitive assets of \$237,140,000 compared to cumulative rate-sensitive liabilities of \$299,510,000 for the one-year time frame. Our cumulative interest-sensitivity gap for the one-year time frame is a negative 12.7% of total assets at December 31, 2009, compared to a negative 3.5% at December 31, 2008. We manage the interest-sensitivity gap for the one-year time frame with a guideline of plus-or-minus 15% of total assets.

The interest rate sensitivity analysis at December 31, 2009, with investment securities presented at fair value, is as follows (dollars in thousands):

	<b>1-90 Days</b>	<b>91-365 Days</b>	<b>1-5 Years</b>	<b>Over 5 Years</b>	<b>Total</b>
<b>Interest Earnings Assets:</b>					
Interest-Bearing Deposits in Other Banks	\$ 35,758	\$ 3,134	\$ 4,870	\$	\$ 43,762
Investment Securities Available for Sale	1,155	4,701	52,453	2,237	60,546
Loans and Leases	125,540	66,852	109,181	37,701	339,274
Restricted Investments in Bank Stocks				3,727	3,727
<b>Total Interest Earning Assets</b>	<b>\$ 162,453</b>	<b>\$ 74,687</b>	<b>\$ 166,504</b>	<b>\$ 43,665</b>	<b>\$ 447,309</b>
<b>Interest Bearing Liabilities:</b>					
Demand and Money Market Deposits	\$ 134,600	\$	\$	\$	\$ 134,600
Savings	23,327	199			23,526
Time Deposits	45,412	72,131	74,684	81	192,308
FHLB Advances and Other Borrowings	11,341	12,500	26,834		50,675
<b>Total Interest Bearing Liabilities</b>	<b>\$ 214,680</b>	<b>\$ 84,830</b>	<b>\$ 101,518</b>	<b>\$ 81</b>	<b>\$ 401,109</b>
<b>Gap</b>	<b>\$ (52,227)</b>	<b>\$ (10,143)</b>	<b>\$ 64,986</b>	<b>\$ 43,584</b>	
<b>Cumulative Gap</b>	<b>\$ (52,227)</b>	<b>\$ (62,370)</b>	<b>\$ 2,616</b>	<b>\$ 46,200</b>	
<b>Cumulative Sensitivity Gap as a Percent of Total Assets</b>	<b>(10.7)%</b>	<b>(12.7)%</b>	<b>0.5%</b>	<b>9.4%</b>	

The amount of assets and liabilities shown, which reprice or mature during a particular period, were determined based on the earlier of when each asset or liability reprices or when it is to be repaid. Callable investment securities are reflected based on the security's anticipated call date where the call on the security is likely when compared to the current interest rate yield curve. Also, loans and mortgage-backed securities are reflected based on contractual amortization or contractual interest rate adjustments and on estimates for prepayments and refinancings based on



current market interest rates. Interest-bearing demand and savings deposits have always been considered a stable source of funds, and although the rates are subject to change, rates on these accounts historically have not changed as quickly or as often as other loan and deposit rates. Based on an historical analysis, during periods of rising interest rates, a portion of these deposits will invest in higher yielding instruments. This portion is deemed to be sensitive to interest rate fluctuations in the earliest periods. We believe that the remaining balances of these deposits are not repriceable based on current industry experience. We currently do not expect to adjust the interest rates on these deposit balances in any significant amount that would materially affect our Gap or income simulation models.

Certain shortcomings are inherent in the method of analysis presented in the foregoing schedule. For example, although certain assets and liabilities may have similar maturities or periods to repricing, they may react in different degrees to changes in market interest rates. Interest rates on certain types of assets and liabilities may fluctuate in advance of, or lag behind, changes in market interest rates. In addition, certain repriceable assets, such as adjustable-rate securities or loans, have features like annual and lifetime rate caps or floors that restrict changes in interest rates both on a short-term basis and over the life of the asset. Further, a change in market interest rates

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from the interest rate scenarios that existed on December 31, 2009 may cause assumptions, such as estimated prepayment speeds, refinancings, embedded options, early withdrawals, and FHLB advance conversion clauses to significantly change from those reflected in the Gap report above. Based on the low current market interest rates, the \$20,000,000 in FHLB convertible advances that are currently convertible on a quarterly basis are presented in the Gap report above at their original scheduled maturity dates. These may convert with a substantial increase in market interest rates and are reflected accordingly in UNCB's simulation model.

In an effort to assess market risk, we utilize a simulation model to determine the effect of gradual increases or decreases in market interest rates on net interest income and net income. We revise the aforementioned assumptions based on defined scenarios of assumed speed and direction of changes in market interest rates. These assumptions are inherently uncertain due to the timing, magnitude and frequency of rate changes and changes in market conditions, as well as management strategies, among other factors. Because it is difficult to quantify into assumptions the reaction of depositors and borrowers to market interest rate changes, our actual net interest income and net income results may differ from simulated results. While assumptions are developed based upon current economic and local market conditions, management cannot make any assurances as to the accuracy and predictive nature of these assumptions.

The simulation model assumes a hypothetical gradual shift in market interest rates over a twelve-month period. This is based on a review of historical changes in market interest rates and the level and curve of current interest rates. The simulation model presents the hypothetical effects to our net interest income and net income from various rate change scenarios. Projections for loan and deposit growth are not factored into the main analysis presented by the simulation model. The simulation model includes all of our earning assets and interest-bearing liabilities and assumes a parallel and prorated shift in interest rates over a twelve-month period. The results of the simulation model could change significantly if there was not a parallel shift in interest rates, therefore causing a change in the assumed shape of the interest rate yield curve. The percentage declines in the table below are measured as percentage changes from the values of simulated net interest income in the current rate scenario and the impact of those changes on the prior year's net income.

UNCB's net interest income and net income sensitivity analysis indicates that as of December 31, 2009 and 2008, a hypothetical 2% (200 basis points) decline in prevailing market interest rates would cause our net interest income to decline 16.8% and 12.2% compared to the current rate scenario at the respective year ends. A hypothetical 2% (200 basis points) increase in interest rates as of December 31, 2009 and 2008 would cause our net interest income to increase by 3.7% and 10.2% compared to the current rate scenario at the respective year ends. These computations do not contemplate any actions management or the Asset and Liability Management Committee could undertake in response to other changes in market conditions or market interest rates. The following table reflects UNCB's net interest income and net income sensitivity analysis as of December 31, 2009 and 2008:

<b>Percent Change in Categories</b>	
<b>Market Interest Rate</b>	<b>Market Interest Rate</b>
<b>Increase of 2%</b>	<b>Decline of 2%</b>
<b>Policy Limit = Change in Net Interest Income +/- Less Than 10%</b>	

Net Interest Income:

Hypothetical Percent Decrease in Net Interest Income from the Current  
Rate Scenario:

As of December 31, 2009	3.7%	(16.8%)*
As of December 31, 2008	10.2%	(12.2%)*

Net Income:

Hypothetical Percent Decrease from Prior Year's Net Income:

As of December 31, 2009	26%	(118%)*
As of December 31, 2008	221%	(265%)*

\* During 2008, the Federal Funds and Prime rates decreased by 4% to record lows of 0.25% and 3.25%, respectively. Given the record low interest rate environment, a 2% market interest rate decline beyond

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December 31, 2009 is deemed by management to be unlikely. In the unlikely event that interest rates would decline by 2%, the decrease in net interest income from a 2% market decline would increase the 2009 net loss and could offset the entire portion of net income in 2008.

We managed our interest rate risk position in 2009, and expect to continue to manage our interest rate risk position going forward into 2010, by the following:

Managing and reducing the interest cost of UNCB's core retail deposit base including deposits obtained in our commercial cash management programs, premium money market accounts, and retail time deposits;

De-leveraging with repayment of higher-cost, fixed rate FHLB long-term debt and brokered CDs;

Managing the use of adjustable- and floating-rate loans, and hybrid loans with initial fixed-rates converting to variable-rates, in comparison to totally fixed-rate loans for new or refinanced commercial and agricultural loans; and

Repositioning of our investment security portfolio mix by purchasing lower-risk shorter term U.S. government agencies, and seasoned mortgage-backed securities, minimizing significant changes in value due to declining interest rates and improving UNCB's regulatory capital ratios by reducing risk-weighted assets.

The above strategies and actions impact interest rate risk and are all included in our quarterly simulation models in order to determine future asset and liability management strategies.

## **Regulatory Matters**

From time to time, various types of federal and state legislation have been proposed that could result in additional regulation of, and restrictions on, our and UNCB's business. As a consequence of the extensive regulation of commercial banking activities in the United States, our and our business is particularly susceptible to being affected by federal and state legislation and regulations that may increase the cost of doing business. See the related discussion of the Emergency Economic Stabilization Act of 2008 in the preceding Recent Developments section. Also, we are susceptible to changes in tax law that may increase the cost of doing business or impact our ability to realize the value of deferred tax assets. Further, our business is affected by the state of the financial services industry in general.

### ***Formal Written Agreement with the Office of the Comptroller of the Currency***

On August 27, 2009, UNCB entered into a formal written agreement, or the Agreement, with the OCC. Specifically, the Agreement requires UNCB to:

establish a compliance committee to monitor and coordinate UNCB's adherence to the provisions of the Agreement;

have the board of directors evaluate and monitor executive management performance;

update its three-year strategic plan in accordance with specific guidelines set forth in the Agreement;

update its three-year capital program;

develop and implement systems to provide for effective loan portfolio management;

take action to protect criticized assets and implement a written program to eliminate the basis of criticism of assets criticized by the OCC;

strengthen UNCB's contingency funding plan;

implement a written consumer compliance program; and

not exceed the level of brokered deposits as of the date of the Agreement without prior OCC approval.

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The Agreement supersedes the previous MOU entered into between UNCB and the OCC on June 20, 2007. The Agreement effectively extends several of the provisions under the MOU, including requiring a three-year strategic plan and three-year capital plan, improving UNCB's loan portfolio management, implementing an effective risk-based consumer compliance audit program, and establishing a compliance committee.

Separate from the Agreement, the OCC has established individual minimum capital requirements for UNCB requiring Tier 1 Capital to Average Total Assets of at least eight percent (8%), Tier 1 Capital to Risk-Based Assets of at least nine and one-half percent (9.5%), and Total Capital to Risk-Based Assets of at least twelve percent (12%) effective beginning September 30, 2009. These minimum capital ratios are similar to the capital ratio targets agreed to between UNCB and the OCC under the MOU which were Tier I Capital to Average Total Assets of 8%, Tier I Capital to Risk-Based Assets of 9%, and Total Capital to Risk-Based Assets of 12%. At December 31, 2009, UNCB's measure of Tier I Capital to Average Total Assets was 8.31%, Tier I Capital to Risk-Based Assets of 9.69% and Total Capital to Risk-Based Assets of 12.37%. At December 31, 2009, all three ratios exceeded the respective OCC individual minimum capital requirements. UNCB's capital ratios reflect the infusion of \$700,000 of the \$1,275,000 proceeds raised in UNNF's preferred stock private placement.

In order to maintain UNCB's capital levels and to continue to meet the OCC's individual minimum capital requirements, UNNF and UNCB may have to raise additional capital, reduce their assets or both. If UNCB does not continue to meet the OCC's requirements, the OCC could subject UNCB to such administrative actions or sanctions as the OCC considers necessary.

Management and the board of directors are committed to taking the necessary actions to fully maintain the new minimum capital ratios and address the provisions of the Agreement, and believe that UNCB has already made measurable progress in addressing these requirements.

This increased supervision by the OCC has negatively impacted our operating results by increasing our FDIC base insurance premiums. Based upon deposit levels and the FDIC base insurance premium assessment criteria as of December 31, 2009, the additional FDIC premiums paid by UNCB as a result of the increased supervision was approximately \$207,000 for the year ended December 31, 2009.

***Memorandum of Understanding with the Federal Reserve Bank***

On January 28, 2010, we entered into an informal MOU with the FRB. We are the registered bank holding company that wholly owns UNCB; however, UNCB is separately supervised by the OCC. The MOU, which is not a written agreement for purposes of Section 8 of the Federal Deposit Insurance Act, requires, among other things, us to seek prior approval by the FRB before (i) declaring or paying dividends to stockholders, (ii) distributing interest, principal or other sums on our subordinated debentures or trust preferred securities, and (iii) incurring, increasing or guaranteeing any additional debt. Subsequent to December 31, 2009, the FRB did approve the quarterly interest payments for the first quarter of 2010 on the UNCT I and UNCT II junior subordinated debentures and the preferred stock dividend payments.

***The Sarbanes-Oxley Act***

The Sarbanes-Oxley Act, enacted in July 2002, represents a comprehensive revision of laws affecting corporate governance, accounting obligations and corporate reporting. We had already implemented many of the provisions of this act, and we have complied with the provisions of Section 404 of the Sarbanes-Oxley Act as required during 2009, including providing a report on our internal control over financial reporting as of December 31, 2009. To support our report on our internal control over financial reporting, we used contracted, independent internal audit services to

identify, document and test key controls over the financial reporting process.

On October 2, 2009, the SEC decided to extend the deadline for small public companies (non-accelerated filers, defined generally as companies with less than \$75 million market capitalization) to file their first auditor's report on internal controls under Sarbanes-Oxley Section 404b. Without the extension, we, as a small

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public company, would have been required to file our first auditor's report on the effectiveness of internal control over financial reporting for the fiscal year ended December 31, 2009. Under the extension, the new deadline for us to file our first auditor's report on internal control will begin for fiscal year ending December 31, 2010.

In 2009, \$10,000 of external audit costs were incurred prior to the extension being granted, associated with complying with the provisions of Sarbanes-Oxley. Additional costs associated with this requirement are expected to be \$25,000 pre-tax for the year ending December 31, 2010.

***Federal Deposit Insurance Corporation Activity***

The Federal Deposit Insurance Reform Act of 2005 amended regulations to create a new risk differentiation system, to establish a new base assessment rate schedule, and to set assessment rates effective January 1, 2007. Also, eligible insured depository institutions shared in a one-time assessment credit, which was approximately \$228,000 for UNCB. UNCB used \$150,000 and \$78,000 of this credit in 2007 and 2008, respectively.

On February 27, 2009, the board of directors of the FDIC voted to amend the restoration plan for the Deposit Insurance Fund, or DIF. The FDIC Board also took action to ensure the continued strength of the insurance fund by imposing a special assessment on insured institutions of 20 basis points, implementing changes to the risk-based assessment system, and setting rates beginning the second quarter of 2009. Under the restoration plan approved in October 2008, the FDIC Board set a rate schedule to raise the DIF reserve ratio to 1.15 percent within five years. The February 27, 2009 restoration plan amendment action extends the restoration plan horizon to seven years in recognition of the current significant strains on banks and the financial system and the likelihood of a severe recession. The amended restoration plan was accompanied by a final rule that sets assessment rates and makes adjustments that improve how the assessment system differentiates for risk.

Currently, most banks are in the best risk category and pay anywhere from 12 cents per \$100 of deposits to 14 cents per \$100 for insurance. Under the final rule, banks in this category will pay initial base rates ranging from 12 cents per \$100 to 16 cents per \$100 on an annual basis, beginning on April 1, 2009. Changes to the assessment system include higher rates for institutions that rely significantly on secured liabilities, which may increase the FDIC's loss in the event of failure without providing additional assessment revenue. Under the final rule, assessments will be higher for institutions that rely significantly on brokered deposits but, for well-managed and well-capitalized institutions, only when accompanied by rapid asset growth. Brokered deposits combined with rapid asset growth have played a role in a number of costly failures, including recent failures. The final rule also would provide incentives in the form of a reduction in assessment rates for institutions to hold long-term unsecured debt and, for smaller institutions, high levels of Tier 1 capital.

The FDIC Board adopted an interim rule imposing an emergency special assessment on the industry on June 30, 2009. The new FDIC emergency premium, to be collected from all federally-insured institutions, will be 5 cents for every \$100 of UNCB's assets minus its Tier 1, or regulatory capital, as of June 30, 2009. The FDIC's previous planned fee was 20 cents per \$100 of UNCB's insured deposits. Based upon UNCB's assets and Tier 1 capital position at June 30, 2009, the additional amount of our FDIC insurance expense related to this special assessment was \$237,000. The interim rule would also permit the FDIC Board to impose a similar emergency special assessment after June 30, 2009, if necessary to maintain public confidence in federal deposit insurance. On November 12, 2009, the FDIC board of directors voted to require insured depository institutions to prepay, on December 30, 2009, their estimated quarterly risk-based assessments for the fourth quarter of 2009 and for all of 2010, 2011, and 2012. The FDIC Board also voted to adopt a uniform three basis point increase in assessment rates effective on January 1, 2011. As a result, UNCB prepaid \$3,400,000 and recorded the entire amount of its assessment as a prepaid expense (asset) as of December 30, 2009. As of December 31, 2009, and each quarter thereafter, UNCB will record an expense (charge to earnings) for its regular quarterly assessment and an offsetting credit to the prepaid assessment until the asset is exhausted. Once the



asset is exhausted, UNCB will record an accrued expense payable each quarter for the assessment

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payment, which would be paid in arrears to the FDIC at the end of the following quarter. If the prepaid assessment is not exhausted by December 31, 2014, any remaining amount would be returned to UNCB.

***Community Reinvestment Act***

The last Community Reinvestment Act performance evaluation by the OCC resulted in a satisfactory rating of UNCB's record of meeting the credit needs of its entire community.

***Pennsylvania Business Corporation Law***

UNNF is subject to restrictions on the payment of dividends to its stockholders pursuant to the PBCL. The PBCL operates generally to preclude dividend payments if the effect thereof would render us insolvent. Payment of dividends is contingent upon the ability to obtain funding in the form of dividends from UNCB. Payment of dividends to UNNF by UNCB is subject to the restrictions set forth in the National Bank Act which requires the approval of the OCC if the total of all dividends declared by a national bank in any calendar year exceeds the net profits of UNCB for that year (as defined) combined with UNCB's retained net operating results for the preceding two calendar years. Under this formula, UNCB's retained net operating results for the preceding two calendar years was (\$189,000). In 2010, UNCB may declare dividends to UNNF in an amount equal to the net profits of UNCB in 2010 less \$189,000, up to the date of any such dividend declaration.

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**UNAUDITED PRO FORMA SELECTED CONDENSED CONSOLIDATED  
FINANCIAL INFORMATION RELATING TO THE UNNF ACQUISITION**

The following tables show information about DGI's consolidated financial condition and operations, including per share data, after giving effect to the proposed merger of UNNF with and into DFSC. The table sets forth the information as if the transaction had become effective on March 31, 2010, with respect to financial condition data, and at the beginning of the periods presented, with respect to operations data. The fair value adjustments contained in the unaudited pro forma condensed consolidated financial information are preliminary estimates based on data as of March 31, 2010. DFSC will determine the final fair value adjustments as of the closing date and the final fair value adjustments could differ significantly from these estimates. DGI's financial information for the interim period ended, March 31, 2010 is unaudited. You should read this entire table in conjunction with the historical financial statements, including the notes thereto, of UNNF and DGI we include in or incorporate by reference in this proxy statement/prospectus. See *Where You Can Find More Information* on page v.

In December 2007, the Financial Accounting Standards Board issued revised guidance under ASC 805, *Business Combinations*, effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2008. ASC 805 retains the fundamental requirements in prior guidance that the acquisition method of accounting be used for all business combinations and for an acquirer to be identified for each business combination.

This new guidance revises the definition of the acquisition date as the date the acquirer obtains control of the acquiree. This date is typically the closing date and is the date DFSC will use to measure the fair value of the consideration paid. Under this new guidance, DFSC will record all loans at fair value, including adjustments for credit, and will not carry over any allowance for credit losses. In addition, the new guidance nullifies Emerging Issues Task Force No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination*, and requires the recognition of costs associated with restructuring or exit activities that do not meet the recognition criteria in ASC 420, *Exit or Disposal Cost Obligations*, as of the acquisition date as post-combination costs when those criteria are met.

DFSC and UNNF anticipate that the merger will provide the combined company with financial benefits that include reduced operating expenses. The pro forma financial information does not reflect the impact of possible revenue enhancements, expense efficiencies and asset dispositions, among other possibilities, and post-merger integration costs that may occur as a result of the merger and, accordingly, does not attempt to predict future results. The pro forma financial information also does not necessarily reflect what the combined historical results of operations of DGI would have been had UNNF and DFSC been merged during these periods.

**Table of Contents****SELECTED CONDENSED CONSOLIDATED UNAUDITED PRO FORMA  
FINANCIAL INFORMATION****Condensed Consolidated Balance Sheet**

	<b>DGI, as Reported</b>	<b>As of March 31, 2010 Pro Forma Adjustments (In thousands)</b>	<b>Pro Forma Combined</b>
<b>ASSETS</b>			
Investments			
Fixed maturities	\$ 607,424	\$	\$ 607,424
Equity securities	10,326		10,326
Investments in affiliates	9,274	12,027(1)	21,301
Short-term investments	30,711		30,711
Total investments	657,735	12,027	669,762
Cash	5,907	(2,027)(2)	3,880
Premium receivable	66,483		66,483
Reinsurance receivable	90,365		90,365
Other assets	115,535		115,535
Total assets	\$ 936,025	\$ 10,000	\$ 946,025
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>			
Liabilities			
Losses and loss expenses	\$ 270,207	\$	\$ 270,207
Unearned premiums	244,968		244,968
Borrowings under line of credit		10,000(3)	10,000
Other liabilities	35,421		35,421
Total liabilities	550,596	10,000	560,596
Stockholders' Equity			
Stockholders' equity	385,429		385,429
Total liabilities and stockholders' equity	\$ 936,025	\$ 10,000	\$ 946,025

Pro Forma Adjustments are discussed in Note 2.

See Notes to Selected Condensed Consolidated Unaudited Pro Forma Financial Information

**Table of Contents****SELECTED CONDENSED CONSOLIDATED UNAUDITED PRO FORMA  
FINANCIAL INFORMATION****Consolidated Statement of Income**

	<b>For the Three Months Ended March 31, 2010</b>		
	<b>DGI, as Reported</b>	<b>Pro Forma Adjustments</b>	<b>Pro Forma Combined</b>
	<b>(In thousands, except share data)</b>		
<b>Revenues:</b>			
Net premiums earned	\$ 91,372	\$	\$ 91,372
Investment income, net of investment expenses	4,930		4,930
Realized gain	22		22
Other income	1,591	(7)(4)	1,584
<b>Total revenues</b>	<b>97,915</b>	<b>(7)</b>	<b>97,908</b>
<b>Expenses:</b>			
Net losses and loss expenses	67,981		67,981
Amortization of deferred policy acquisition costs	16,015		16,015
Other underwriting expenses	12,633		12,633
Other expenses	1,010	48(5)	1,058
<b>Total expenses</b>	<b>97,639</b>	<b>48</b>	<b>97,687</b>
Income before income taxes	276	(55)	221
Income taxes	41	(16)(6)	25
<b>Net income</b>	<b>\$ 235</b>	<b>\$ (39)</b>	<b>\$ 196</b>
<b>Earnings per common share:</b>			
Class A common stock basic and diluted	\$ 0.01	\$	\$ 0.01
Class B common stock basic and diluted	\$ 0.01	\$	\$ 0.01
<b>Weighted-average number of shares outstanding:</b>			
Class A common stock basic and diluted	19,930,641		19,930,641
Class B common stock basic and diluted	5,576,775		5,576,775

Pro Forma Adjustments are discussed in Note 2.

See Notes to Selected Condensed Consolidated Unaudited Pro Forma Financial Information

Table of Contents**SELECTED CONDENSED CONSOLIDATED UNAUDITED STATEMENT OF INCOME****Consolidated Statement of Income**

**For the Year Ended December 31, 2009**  
**DGI, Pro Forma Pro Forma**  
**as Reported Adjustments Combined**  
**(In thousands, except share data)**

Revenues:			
Net premiums earned	\$ 355,025	\$	\$ 355,025
Investment income, net of investment expenses	20,631		20,631
Realized gain	4,480		4,480
Service charge income	5,205		5,205
Other income	1,393	(345)(4)	1,048
<b>Total revenues</b>	<b>386,734</b>	<b>(345)</b>	<b>386,389</b>
Expenses:			
Net losses and loss expenses	250,835		250,835
Amortization of deferred policy acquisition costs	60,292		60,292
Other underwriting expenses	50,844		50,844
Other expenses	4,086	263(5)	4,349
<b>Total expenses</b>	<b>366,057</b>	<b>263</b>	<b>366,320</b>
Income before income taxes	20,677	(608)	20,069
Income taxes	1,847	(89)(6)	1,758
<b>Net income</b>	<b>\$ 18,830</b>	<b>\$ (519)</b>	<b>\$ 18,311</b>
Earnings per common share:			
Class A common stock basic and diluted	\$ 0.76	\$ (0.02)	\$ 0.74
Class B common stock basic and diluted	\$ 0.68	\$ (0.02)	\$ 0.66
Weighted-average number of shares outstanding			
Class A common stock basic and diluted	19,903,069		19,903,069
Class B common stock basic and diluted	5,576,775		5,576,775

Pro Forma Adjustments are discussed in Note 2.

See Notes to Selected Condensed Consolidated Unaudited Pro Forma Financial Information

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**NOTES TO SELECTED UNAUDITED PRO FORMA CONDENSED CONSOLIDATED  
FINANCIAL INFORMATION RELATING TO THE UNNF ACQUISITION**

**Note 1 Basis of Pro Forma Presentation**

The estimated purchase price of \$24.9 million for UNNF reflects the value of the common shares of UNNF that DMIC will contribute to DFSC and the payment per share of merger consideration to UNNF shareholders other than DMIC of \$5.05 in cash and 0.2134 share of DGI Class A common stock. DFSC has used a per share price for DGI Class A common stock of \$14.51, which was the closing price of DGI Class A common stock as of March 31, 2010.

DFSC will account for the merger under the acquisition method of accounting; accordingly, DFSC will allocate the cost of acquiring UNNF to the assets acquired, including identifiable intangible assets, and liabilities assumed from UNNF at their respective fair values on the date DFSC and UNNF complete the merger. You should read this entire table in conjunction with the historical financial statements, including the notes thereto, of UNNF and DGI included in or incorporated by reference in this proxy statement/prospectus. See [Where You Can Find More Information](#) on page v.

The unaudited pro forma condensed consolidated financial information includes estimated adjustments to record UNNF's assets and liabilities at their respective fair values and represent DFSC's estimates based on available information. DGI may revise the pro forma adjustments included in this table as additional information becomes available and as DGI performs additional analyses. DFSC will determine the final allocation of the purchase price after the merger is completed and after completion of a final analysis to determine the fair values of UNNF's tangible, and identifiable intangible, assets and liabilities as of the closing date. Accordingly, the final acquisition accounting adjustments may be materially different from the pro forma adjustments. Increases or decreases in the fair value of UNNF's net assets, commitments, contracts and other items may change the amount of the purchase price DFSC allocates to goodwill and other assets and liabilities and may impact the statement of income due to adjustments in yield and/or amortization of the adjusted assets or liabilities.

The unaudited pro forma condensed consolidated financial information presented in this proxy statement/prospectus does not necessarily indicate the results of operations or the combined financial position that would have resulted had the merger been completed at the beginning of the applicable periods presented, does not reflect the impact of possible revenue enhancements, expense efficiencies or asset dispositions, and therefore is not indicative of the results of operations in future periods or the future financial position of the combined company.

**Note 2 Pro Forma Adjustments**

The unaudited pro forma condensed consolidated financial information for the merger includes the pro forma balance sheet as of March 31, 2010 assuming DFSC and UNNF completed the merger on March 31, 2010. DGI prepared the pro forma income statements for the three months ended March 31, 2010 and the year ended December 31, 2009 assuming DFSC and UNNF completed the merger on January 1, 2010 and January 1, 2009, respectively.

DGI currently owns 48.2% of DFSC and will contribute cash in exchange for DFSC common stock in an amount equal to approximately 48.2% of the total of the merger consideration and fair value of the UNNF shares DMIC will contribute to DFSC. DMIC owns the remaining 51.8% of DFSC and will contribute cash, 248,999 shares of UNNF common stock that it currently owns and up to 600,000 shares of DGI Class A common stock that it currently owns in exchange for DFSC common stock. DMIC will continue to own approximately 51.8% of DFSC. The selected consolidated unaudited pro forma financial information reflects the payment of \$14.2 million in cash and DMIC's contribution to DFSC of 600,000 shares of DGI Class A common stock with an aggregate value of \$8.7 million.

DFSC valued the DGI Class A common stock used in the exchange as discussed in Note 1 above.



**Table of Contents****NOTES TO SELECTED UNAUDITED PRO FORMA CONDENSED CONSOLIDATED FINANCIAL INFORMATION RELATING TO THE UNNF ACQUISITION (Continued)**

The allocation of the purchase price follows (in thousands):

Cash from DGI	\$ 12,027
Cash from DMIC	2,174
Value of 248,999 shares of UNNF common stock contributed by DMIC	2,028
Value of 600,000 shares of DGI Class A common stock contributed by DMIC	8,706
 Total cost of acquisition	 24,935
 UNNF net assets acquired:	
Stockholders' equity	31,728
 Estimated adjustments to reflect assets acquired and liabilities assumed at fair value:	
Total fair value adjustments	(13,912)
Associated deferred income taxes	4,730
 Fair value adjustment to net assets acquired, net of tax	 (9,182)
 Total UNNF net assets acquired	 22,546
 Goodwill resulting from the merger	 \$ 2,389

The significant pro forma adjustments included in the selected condensed consolidated unaudited pro forma financial information are as follows:

(1) Adjustment to record DGI's increased investment in DFSC, including its share of the fair value of UNNF's net assets. The significant fair value adjustments to UNNF's assets and liabilities are as follows:

(A) Adjustment to record the current fair value of UNNF's loan portfolio based on current interest rates. DFSC based the adjustment on current assumptions and valuations, which are subject to change. For purposes of the pro forma adjustments reflected, DFSC reduced the value of UNNF's loan portfolio by \$13.5 million. The combined bank will recognize the adjustment over the estimated remaining life of the loan portfolio. Material changes to the estimated fair value and estimated remaining life could occur once DFSC completes its analyses.

(B) Adjustment to eliminate UNNF's allowance for loan losses and record general and specific credit adjustments within UNNF's loan portfolio in accordance with ASC Topic 805 and ASC Topic 310-30, which provides guidance for accounting for loans acquired in a transfer. DFSC based the adjustments on current assumptions and valuations, which are subject to change. For purposes of the pro forma adjustments reflected, DFSC reduced the net value of UNNF's loan portfolio by \$14.2 million. Material changes to the estimated fair value could occur once DFSC completes its analyses.

(C) Adjustment to record UNNF's core deposit intangible assets at estimated fair value. DFSC is studying the nature, amount and amortization method of various possible identified intangibles. DFSC based the adjustment on current assumptions and valuations, which are subject to change. For purposes of the pro forma adjustments reflected, the

estimated fair value of the core deposit intangible is \$4.5 million. DFSC estimates that it will amortize the core deposit intangible on an accelerated basis over ten years. Material changes to this estimated fair value and estimated useful life could occur once DFSC completes its analyses.

(D) Adjustment to record the fair value of UNNF's bank premises and property leases. DFSC will recognize the adjustment over the remaining life of the bank premises and property leases.

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**NOTES TO SELECTED UNAUDITED PRO FORMA CONDENSED CONSOLIDATED  
FINANCIAL INFORMATION RELATING TO THE UNNF ACQUISITION (Continued)**

(E) Adjustment to record the fair value of UNNF's time deposit liabilities based on current interest rates for similar instruments. DFSC will recognize the adjustment over the estimated remaining term of the related deposit liability.

(F) Adjustment to record the fair value of UNNF's outstanding long-term debt instruments. DFSC based the adjustment on current assumptions and valuations, which are subject to change. For purposes of the pro forma adjustments reflected, DFSC reduced the value of UNNF's outstanding long-term debt by \$9.3 million. DFSC will recognize the adjustment over the remaining life of the debt instruments. Material changes to the estimated fair value and estimated remaining life could occur once DFSC completes its analyses.

(G) Adjustment to eliminate UNNF's historical shareholders' equity.

(H) Adjustment to record the tax effect of the pro forma adjustments using DFSC's statutory tax rate of 34%.

(2) Adjustment to reflect use of cash for the amount of DGI's capital contribution to DFSC in excess of anticipated borrowings under DGI's line of credit facility.

(3) Adjustment to reflect anticipated borrowings under DGI's line of credit facility in the amount of \$10 million.

(4) Adjustment to record DGI's share of UNNF's historical net loss, which is presented as an offset to DGI's equity investment income from DFSC.

(5) Adjustment to record interest expense related to borrowings under DGI's line of credit based on average interest rates of 1.91% and 2.63% for the three months ended March 31, 2010 and the year ended December 31, 2009, respectively. These rates were based on a fixed margin over the average six-month LIBOR rates in effect for the respective periods pursuant to the terms of DGI's current line of credit facility.

(6) Adjustment to record income tax benefit related to DGI's interest expense using DGI's statutory tax rate of 34%.

**Note 3 Merger-Related Charges and Benefits**

In connection with the merger, DFSC and UNNF are developing integration plans. DFSC has not yet determined the total integration costs and has not included such costs in the pro forma adjustments. DFSC will continue to refine the specific details of these plans over the next several months. Currently, DFSC's merger integration team is assessing the two companies' operations, including information systems, premises, branch offices, equipment, benefit plans, service contracts, product offerings and personnel to determine optimum strategies to realize additional cost savings.

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**RISK FACTORS**

In addition to the other information contained in or incorporated by reference in this proxy statement/prospectus, including the matters addressed under Forward-Looking Statements, you should carefully consider the following risk factors in deciding whether to vote in favor of the merger proposal and the adjournment proposal. We also incorporate by reference in this proxy statement/prospectus the Risk Factors section of DGI's Form 10-K annual report for the year ended December 31, 2009.

**Risks Related to the Merger**

*DFSC may not receive the required regulatory approvals, the required regulatory approvals may take longer than we expect and such approvals, if received, could contain conditions that permit DFSC to terminate the merger agreement.*

DFSC must obtain various approvals and consents from the OTS and other bank regulatory authorities before we may complete the merger and the bank merger. The OTS and the other bank regulatory agencies may impose conditions on the completion of the merger and the bank merger or require changes to the terms of the merger agreement. We can give no assurance that we will receive the required regulatory approvals or that such approvals would not have conditions that would permit DFSC to terminate the merger agreement.

*DFSC could terminate the merger agreement and the merger would not occur.*

DFSC's obligation to consummate the transactions the merger agreement contemplates is subject to a number of conditions precedent including adoption of the merger agreement by the affirmative vote of the holders of 80% of our outstanding common stock, regulatory approvals, the continued accuracy of certain representations and warranties, the performance of certain covenants and agreements and UNCB not having delinquent loans in excess of \$37.5 million as of the end of the month prior to the closing date. We have the right to terminate the merger agreement if DFSC does not receive required regulatory approvals, or if the holders of 80% of our outstanding shares do not vote to adopt the merger agreement or vote to accept a superior proposal.

*Our asset quality could deteriorate*

At March 31, 2010, we had non-performing assets of \$14.9 million compared to \$14.4 million at December 31, 2009 and \$5.4 million at December 31, 2008. We had net charge-offs of \$0.4 million for the first quarter of 2010, compared to \$0.4 million for the first quarter of 2009, and our allowance for loan losses increased to \$6.0 million at March 31, 2010 from \$5.9 million at December 31, 2009. If our asset quality were to deteriorate in the future, it could have a material adverse effect on us and could result in our failure to satisfy a condition precedent to DFSC's obligation to consummate the merger.

*DFSC could have future impairment losses on UNNF's portfolio of available for sale investment securities.*

For the first quarter of 2010, we did not recognize any OTTI charges on our available for sale investment securities. After the merger, DFSC could determine in one or more future reporting periods that these investment securities have suffered a further impairment that is other than temporary and DFSC could incur material losses as a result.

*Because the market price of DGI Class A common stock may fluctuate, our shareholders cannot be certain of the market value of the DGI Class A common stock that they will receive in the merger.*

Upon completion of the merger, each share of our common stock will be converted into the right to receive 0.2134 share of DGI Class A common stock and \$5.05 in cash. Any change in the price of DGI Class A common stock prior to the merger will affect the market value of the stock that you will receive in the merger. Stock price changes may result from a variety of factors, including general market and economic conditions, changes in DGI's businesses, operations and prospects and regulatory considerations.

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The prices of DGI Class A common stock and our common stock at the closing of the merger may vary from their respective prices on the date we executed the merger agreement, on the date of this proxy statement/prospectus and on the date of our special meeting. As a result, the value represented by the exchange ratio may also vary. For example, based on the range of closing prices of DGI Class A common stock during the period from April 19, 2010, the last full trading day before public announcement of the merger, through \_\_\_\_\_, 2010, the last practicable full trading day prior to the date of the printing of this proxy statement/prospectus, the exchange ratio represented a value ranging from a high of \$ \_\_\_\_\_ on \_\_\_\_\_, 2010 to a low of \$ \_\_\_\_\_ on \_\_\_\_\_, 2010 for each share of our common stock. Because the date we complete the merger will necessarily be after the date of our special meeting, at the time of our special meeting, our shareholders will not know the market value of DGI's Class A common stock upon completion of the merger.

***DFSC may encounter integration difficulties or may fail to realize the anticipated benefits the merger.***

In determining that the merger is in the best interests of DFSC and us, our respective boards of directors considered that greater capital and enhanced earnings may result from the consummation of the merger, including from anticipated cost savings, improved efficiency, cross-marketing opportunities and the strong capitalization of Province. The success of the merger will depend, in part, on the ability of the combined company to realize the anticipated benefits of the merger, which may not be realized as anticipated or at all and may take longer to realize than anticipated. Failure to achieve the anticipated benefits of the merger could result in increased costs and decreases in the revenues of the combined banks.

Province and UNCB may not be able to integrate their respective operations without encountering difficulties, including, without limitation, the loss of key employees and customers, the disruption of their and our respective ongoing businesses or possible inconsistencies in standards, controls, procedures and policies.

***If we cannot complete the merger, we will have incurred substantial expenses without realizing the expected benefits of the merger.***

We have incurred substantial expenses in connection with the negotiation and execution of the merger agreement described in this proxy statement/prospectus and the seeking of regulatory approval of the transactions the merger agreement contemplates. The completion of the merger depends on the satisfaction of specified conditions and the receipt of regulatory approvals. If we are unable to complete the merger, we will have to recognize these expenses currently under applicable accounting standards.

***The merger agreement limits our ability to pursue alternatives to the merger.***

The merger agreement contains provisions that, subject to limited exceptions, restrict our ability to discuss, facilitate or enter into agreements with third parties to acquire us. If we avail ourselves of those limited exceptions, we will be obligated to pay DFSC a break-up fee of \$800,000 if DFSC or we terminate the merger agreement under specified circumstances. From our perspective, these provisions could discourage a potential competing acquiror that might have an interest in acquiring us from proposing or considering an acquisition of us even if that potential acquiror were prepared to pay a higher price to our shareholders than the price DFSC proposes to pay under the merger agreement.

***Some of our directors and executive officers have interests in the merger besides those of a shareholder.***

Our officers and directors have economic interests in the merger other than their interests as shareholders. Those interests include:

eight of our executive officers are parties to severance agreements and employment agreements with us that provide for potential cash payments after the completion of the merger with DFSC if the executive officer

terminates his or her employment for good reason or if DFSC terminates the executive officer's employment without cause;

Mark D. Gainer and two other current members of our board of directors will become directors of DFSC and will receive directors' fees for such service;

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Mark D. Gainer and four other current members of UNCB's board of directors will become directors of Province and will receive director's fees from Province in connection therewith;

the potential payment of certain benefits to Mark D. Gainer under his existing salary continuation agreement and his existing employment agreement; and

the agreement by DFSC to indemnify our directors and officers for six years following the completion of the merger.

Our board of directors was aware of these interests at the time it approved the merger agreement. These interests may cause our directors and executive officers to view the merger proposal differently and more favorably than you may view it.

***Our shareholders will have an insignificant ownership and voting interest in DGI after the merger; DMIC has voting control of DGI and can elect all of its directors.***

After the merger, our shareholders will have significantly reduced influence on the management and policies of DGI than they now have on our management and policies. Our shareholders in the aggregate will own less than 3% of DGI's outstanding Class A common stock.

DMIC owns approximately 42% of DGI's Class A common stock and approximately 75% of DGI's Class B common stock. This ownership provides DMIC with approximately 66% of the aggregate voting power of DGI's Class A common stock and Class B common stock. As a result, DMIC has sufficient voting control to:

elect all of the members of DGI's board of directors, who determine DGI's management and policies; and

control the outcome of any corporate transaction or other matter submitted to DGI's shareholders for approval, including mergers and other acquisition proposals and the sale of all or substantially all of DGI's assets, in each case regardless of how DGI's other shareholders vote their shares.

***Termination of the merger agreement could negatively impact us.***

DFSC has the right to terminate the merger agreement for the reasons set forth in the merger agreement, including if our delinquent loans exceed \$37.5 million as of the end of the month preceding the month when the closing time of the merger is scheduled. Termination of the merger agreement could have adverse consequences to us, including the following:

Our business may be harmed by the failure to realize the benefits of the merger and the loss of the significant capitalization Province would have contributed to the combined bank; and

the market price of our stock would likely decline to the price prevailing before we announced the merger.

If DFSC terminates the merger agreement or we do not receive the required regulatory approvals, we may not be able to reach a merger agreement with another third party that would be willing to pay an equivalent or greater price than DFSC has agreed to pay in the merger agreement.

***Our financial advisor is not obligated to update its fairness opinion.***



Sandler O'Neill, our independent financial advisor, provided its opinion dated April 19, 2010 to our board of directors that, as of that date and based upon and subject to the factors and assumptions set forth in its opinion, the merger consideration provided for in the merger agreement is fair from a financial point of view to the holders of our common stock. Sandler O'Neill has no obligation to update or reaffirm its opinion to reflect circumstances or developments after the date of its opinion.

Our results of operations and prospects and those of DGI could change adversely between the date of the Sandler O'Neill opinion and the closing date of the merger. The price of DGI Class A common stock could

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also decline between the date of the Sandler O'Neill opinion and the closing date of the merger. In addition, the recommendation of our board of directors that you vote **FOR** the adoption of the merger agreement is as of the date of this proxy statement/prospectus.

See The Merger Opinion of UNNF's Financial Advisor for information about Sandler O'Neill's opinion and The Merger UNNF's Reasons for the Merger for information about our board's decision to enter into the merger agreement and recommend that our shareholders vote to adopt it.

**Risks Related to Owning DGI Class A Common Stock**

*The limited trading volume of DGI's Class A common stock may adversely affect its price.*

DGI's Class A common stock has limited trading volume. Reported average daily trading volume in DGI's Class A common stock for the year ended December 31, 2009 was approximately 27,000 shares. This limited trading volume could subject DGI's shares of Class A common stock to greater price volatility.

*Certain provisions of DGI's certificate of incorporation and by-laws and Delaware law may discourage takeovers.*

DGI's certificate of incorporation and by-laws contain certain anti-takeover provisions that may discourage or may make more difficult or expensive a tender offer, change in control or takeover attempt that is opposed by DGI's board of directors. In particular, DGI's certificate of incorporation and by-laws:

- classify its board of directors into three classes, so that shareholders elect only one-third of its board of directors each year;

- permit shareholders to remove directors only for cause;

- do not permit shareholders to take action except at an annual or special meeting of shareholders;

- require shareholders to give DGI advance notice to nominate candidates for election to its board of directors or to make other shareholder proposals at a shareholders' meeting; and

- permit DGI's board of directors to issue, without shareholder approval unless otherwise required by law, preferred stock with such terms as its board of directors may determine.

These provisions of DGI's certificate of incorporation and by-laws and of Delaware law could discourage potential acquisition proposals and could delay or prevent a change in control, even though a majority of DGI's shareholders may consider such proposals desirable. In addition, DMIC beneficially owns approximately two-thirds of the voting power in DGI and therefore can control the outcome of any matter that DGI's board of directors submits to DGI's shareholders for approval. Such provisions could also make it more difficult for third parties to remove and replace the members of DGI's board of directors. DGI's voting power may also inhibit increases in the trading price of DGI's Class A common stock because DGI's Class A common stock will never trade with a take-over premium.

In addition, DGI has 2,000,000 authorized shares of preferred stock that DGI could issue in one or more series without shareholder approval, to the extent applicable law permits, and upon such terms and conditions, and having such rights, privileges and preferences, as DGI's board of directors may determine. DGI's ability to issue preferred stock could make it difficult for a third party to acquire DGI. DGI has no current plans to issue any preferred stock.

Moreover, Delaware law contains certain provisions that prohibit certain business combination transactions under certain circumstances. In addition, state insurance laws and regulations generally prohibit any person from acquiring, or seeking to acquire, a 10% or greater interest in an insurance company without the prior approval of the state insurance commissioner of the states where the insurer is domiciled and the states of domicile of any of its insurance subsidiaries.

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***DGI's status as a holding company makes it dependent on dividends from its subsidiaries to meet its obligations.***

DGI is a holding company and conducts almost all of its operations through its subsidiaries. DGI does not have any significant assets other than the stock of its subsidiaries. Accordingly, DGI depends on dividends from its subsidiaries to meet its obligations. DGI's right to participate in any distribution of earnings or assets of its subsidiaries is subject to the prior claims of creditors of such subsidiaries and various state insurance laws. Under federal and state law, Province is limited in the amount of dividends it may pay to DFSC and DFSC is limited in the amount of dividends it may pay to DMIC and DGI, in each case without prior regulatory approval. Also, bank regulators have the authority to prohibit Province from paying dividends if the bank regulators determine that Province is in an unsound or unsafe condition or that the payment of a dividend would be an unsafe and unsound banking practice.

***DGI could experience significant difficulties and complications in connection with its growth and acquisition strategy.***

DGI has grown significantly over the last few years through the acquisition of other insurance companies and intends to continue to do so. However, the market for acquisitions is highly competitive. DGI's acquisition strategy involves the risk that DGI will not be able to manage growth by acquisition adequately and profitably. For example, acquiring any insurance company will involve risks commonly associated with acquisitions, including:

- potential exposure to unknown or contingent liabilities of insurance companies DGI acquires;
- exposure to potential asset quality issues of insurance companies DGI acquires;
- potential diversion of the time and attention of DGI's management; and
- the possible loss of key employees and customers of the insurance companies DGI may acquire.

**Other Risk Factors Relating to the Donegal Entities**

We strongly suggest that you read the DGI Form 10-K Annual Report for the year ended December 31, 2009 for information about a number of risks inherent in the property and casualty insurance business in which the Donegal Insurance Group engages.

**CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This proxy statement/prospectus contains a number of forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 regarding the financial condition, results of operations, earnings outlook, business and prospects of DGI and us, and the potential combined company, as well as statements applicable to the period following the completion of the merger. You can find many of these statements by looking for words such as plan, believe, expect, intend, anticipate, estimate, project, potential, possible or other similar expressions.

These forward-looking statements involve certain risks and uncertainties. The ability of either DGI or us to predict results or the actual effects of their plans and strategies, particularly after the merger, is inherently uncertain. Accordingly, actual results may differ materially from anticipated results. Some of the factors that may cause actual results or earnings to differ materially from those the forward-looking statements contemplate include, but are not limited to, those discussed under "Risk Factors" beginning on page 66, as well as the following:

- Province and UNCB may not successfully integrate their businesses or the integration may be more difficult, time-consuming or costly than DFSC and we currently anticipate;

DFSC may not realize the expected revenue synergies and cost savings from the merger within the time frame it anticipates or at all;

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revenues may be lower than expected following the merger;

Province may experience greater deposit attrition, operating costs, loss of customers and business disruption, including, without limitation, difficulties in maintaining relationships with our employees, customers or suppliers than it currently anticipates following the merger;

DFSC may not obtain the regulatory approvals for the merger or the approvals may contain terms not acceptable to DFSC;

the requisite percentage of our shareholders may not vote to adopt the merger agreement;

competitive pressure among financial services companies is intense;

general economic conditions may be less favorable than we expect;

political conditions and related actions by the U.S. military abroad may adversely affect economic conditions as a whole;

changes in the interest rate environment may reduce interest margins and impact funding sources;

changes in market rates and prices may adversely impact the value of financial products and assets;

legislation or changes in the regulatory environment may adversely affect the businesses in which Province and UNCB engage; and

litigation liabilities, including costs, expenses, settlements and judgments, may adversely affect either company or their businesses.

Because these forward-looking statements are subject to assumptions and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements. We caution you not to place undue reliance on these statements, which speak only as of the date of this proxy statement/prospectus or as of the date of any document incorporated by reference in this proxy statement/prospectus.

All forward-looking statements concerning the merger or other matters addressed in this proxy statement/prospectus and attributable to DGI or us or any authorized person acting on their behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. Except to the extent required by applicable law or regulation, DGI and we undertake no obligation to update these forward-looking statements to reflect events or circumstances after the date of this proxy statement/prospectus or to reflect the occurrence of unanticipated events.

**OUR SPECIAL MEETING**

This section contains information for our shareholders about the special meeting of shareholders we have called to consider the approval of the merger proposal and the adjournment proposal.

**General**

We furnish this proxy statement/prospectus to holders of our common stock for use at our special meeting and any adjournment or postponement of our special meeting.

**When and Where We Will Hold Our Special Meeting**

We will hold our special meeting on \_\_\_\_\_, 2010, at \_\_\_\_\_ a.m., prevailing time, at The Eden Resort, 222 Eden Road, Lancaster, Pennsylvania, subject to any adjournment or postponement of our special meeting.

**The Matters Our Shareholders Will Consider**

The purpose of our special meeting is to consider and vote upon:

*Proposal No. 1* A proposal to adopt the merger agreement;

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*Proposal No. 2* A proposal to grant discretionary authority to adjourn our special meeting if necessary to permit further solicitation of proxies because we have not received sufficient votes at the time of our special meeting to approve the merger proposal; and

Any other business that properly comes before our special meeting and any adjournment or postponement of our special meeting.

Our shareholders must approve Proposal No. 1 for the merger to occur. If our shareholders fail to approve this proposal, the merger will not occur.

At this time, our board of directors is unaware of any matter, other than as set forth above, that may be presented for action at our special meeting. If a shareholder properly presents another matter, the proxies will vote in accordance with their judgment with respect to any such matter.

### **Record Date; Shares Outstanding and Entitled to Vote**

Our board of directors has fixed the close of business on \_\_\_\_\_, 2010 as the record date for the determination of holders of our common stock entitled to notice of, and to vote at, our special meeting and any adjournment or postponement of our special meeting.

On the record date, we had \_\_\_\_\_ issued and outstanding shares of our common stock that are entitled to vote at our special meeting, held by approximately \_\_\_\_\_ holders of record. This total assumes the 1,275 issued and outstanding shares of preferred stock convert into common stock prior to the record date for our special meeting. Each share of our common stock entitles the holder to cast one vote on all matters that properly come before our shareholders at our special meeting. Holders of our preferred stock do not have voting rights with respect to the merger proposal or the adjournment proposal.

### **Quorum**

The presence, in person or by properly executed proxy, of the holders of at least a majority of our outstanding shares of common stock on the record date will constitute a quorum at our special meeting. Abstentions will be counted for the purpose of determining whether a quorum is present. We must have a quorum present in order to vote on the merger proposal and the adjournment proposal.

Based on the number of shares of our common stock issued and outstanding as of the record date, we must have \_\_\_\_\_ shares of our common stock present in person or represented by proxy at our special meeting to constitute a quorum.

### **Shareholder Vote Required**

*Adopt the Merger Agreement.* The adoption of the merger agreement requires an affirmative vote of the holders of 80% of our common stock entitled to vote thereon. Accordingly, we urge you to complete, date and sign the accompanying proxy card and return it promptly in the enclosed postage-paid envelope. DMIC has advised us that DMIC will vote its 248,999 shares of our common stock, or approximately 9.1% of our outstanding common stock, for the merger proposal and for the adjournment proposal.

When considering our board of directors' recommendation that you vote **FOR** the adoption of the merger agreement, we want you to know that certain of our executive officers and directors have interests in the merger that may be



different from, or in addition to, your interests as a shareholder. See "The Merger - Interests of Our Directors and Executive Officers in the Merger" beginning on page 94.

*Discretionary Authority to Adjourn Our Special Meeting.* The proposal to grant our board of directors authority to adjourn the special meeting if necessary to obtain additional affirmative votes required to adopt the merger agreement. Approval of the adjournment proposal requires the affirmative vote of a majority of the votes present, in person or by proxy, at our special meeting.

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**Director and Executive Officer Voting**

As of the record date, our directors and executive officers and their affiliates beneficially owned 276,702 shares of our common stock, or approximately 9.7% of the issued and outstanding shares of our common stock entitled to vote at our special meeting. This number does not include options to purchase shares of our common stock because we anticipate all of our executive officers and directors will surrender their options for cancellation.

**Proxies**

*Voting.* You should complete and return the proxy card accompanying this proxy statement/prospectus in order to ensure that we can count your vote at our special meeting and at any adjournment or postponement of our special meeting, regardless of whether you plan to attend our special meeting. If you sign, date and return your proxy card and do not indicate how you want to vote, we will count your proxy card as a vote **FOR** the merger proposal and **FOR** the adjournment proposal.

If you hold your shares of our common stock in the name of a bank, broker, nominee or other holder of record, you will receive instructions from the bank, broker, nominee or other holder of record that you must follow in order for you to vote your shares of our common stock.

*Revocability.* You may revoke your proxy at any time before we conduct the vote at our special meeting. If you have not voted through a bank, broker, nominee or other holder of record, you may change your vote after you have returned your proxy by:

- submitting written notice of revocation to our corporate secretary;
- submitting a new proxy by mail, telephone or internet; or
- voting in person at our special meeting.

However, simply attending our special meeting without voting will not revoke any proxy you have submitted.

You should address any written notices of revocation and other communications regarding your proxy to:

Union National Financial Corporation  
570 Lausch Lane, Suite 300  
Lancaster, Pennsylvania 17601  
Attention: Mary K. Rossi, Secretary

If you have instructed your bank, broker, nominee or other holder of record to vote your shares, you should follow the instructions of the bank, broker, nominee or other holder of record regarding the revocation of proxies.

The death or incapacity of a shareholder will not revoke a proxy appointment unless our corporate secretary receives notice of the death or incapacity of the shareholder who executed the proxy prior to the voting of the proxy at our special meeting.

*How We Count Proxies.* We will vote all shares of our common stock represented by properly executed proxies received before or at our special meeting, and not revoked, in accordance with the instructions indicated in the

proxies.

We will count a properly executed proxy marked **ABSTAIN** as present for purposes of determining the presence of a quorum.

Brokers may not vote shares of our common stock that they hold beneficially either for or against the approval of the merger proposal or the adjournment proposal without specific instructions from the person who beneficially owns those shares. Therefore, if a broker holds your shares, you must give your broker instructions on how to vote your shares.

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*Solicitation.* We will pay for the costs of our special meeting and for the mailing of this proxy statement/prospectus to our shareholders, as well as all other costs we incur in connection with the solicitation of proxies from our shareholders. DFSC and we will share equally the cost of printing this proxy statement/prospectus and the filing fees paid to the SEC.

In addition to soliciting proxies by mail, our directors, officers and employees may solicit proxies by telephone or in person. Our directors, officers and employees will not receive any additional compensation for these activities. We also intend to request that brokers, banks, nominees and other holders of record solicit proxies from their principals, and we will reimburse the brokers, banks, nominees and other holders of record for certain expenses they incur for those activities.

We have retained the firm of Georgeson, Inc. to assist us in the solicitation of proxies for our special meeting. We will pay such firm a fee of \$9,000, plus reimbursable expenses, for its services.

## **Recommendation of Our Board of Directors**

Our board of directors unanimously approved the merger agreement and the transactions the merger agreement contemplates. Based on our reasons for the merger we describe in this proxy statement/prospectus, our board of directors believes that the merger is advisable and in our and your best interests. Accordingly, our board of directors unanimously recommends that you vote **FOR** the merger proposal and **FOR** the adjournment proposal. See *The Merger Our Board of Directors Reasons for the Merger; Recommendation* beginning on page 82, for a more detailed discussion of our board of directors recommendation.

## **Attending Our Special Meeting**

If you hold your shares in street name and you want to attend our special meeting, you must bring an account statement or letter from your holder of record showing that you were the beneficial owner of the shares on \_\_\_\_\_, 2010, the record date for our special meeting.

## **Questions and Additional Information**

If you have questions about the merger or how to submit your proxy card, or if you need additional copies of this proxy statement/prospectus or the enclosed proxy card, please call Michael D. Peduzzi, our Executive President and Chief Financial Officer, at (877) 653-1441. You may also call Georgeson, Inc., which firm is assisting us in the solicitation of proxies for our special meeting, at \_\_\_\_\_.

## **INFORMATION ABOUT DONEGAL AND US**

### **Donegal**

DGI is an insurance holding company whose insurance subsidiaries offer personal and commercial lines of property and casualty insurance to small businesses and individuals in 18 Mid-Atlantic, Midwestern and Southeastern states. DGI's insurance subsidiaries provide their policyholders with a selection of insurance products at competitive rates, while pursuing profitability by adhering to a strict underwriting discipline.

DGI's insurance subsidiaries derive a substantial portion of their insurance business from small to mid-sized regional communities. DGI believes this focus provides its insurance subsidiaries with competitive advantages in terms of local market knowledge, marketing, underwriting, claims servicing and policyholder service. At the same time, DGI believes its insurance subsidiaries have cost advantages over many smaller regional insurers because of the centralized

accounting, administrative, data processing, investment and other services available to DGI insurance subsidiaries on a cost-effective basis because of economies of scale.

DMIC owns approximately 42% of DGI's Class A common stock and approximately 75% of DGI's Class B common stock. DMIC's stock ownership in DGI represents in the aggregate approximately two-thirds of the total voting power of both classes of its common stock.

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DGI's insurance subsidiaries and DMIC have interrelated operations. While each company maintains its separate corporate existence, DGI's insurance subsidiaries and DMIC conduct business together as the Donegal Insurance Group. As such, DMIC and DGI's insurance subsidiaries have the same business philosophy, the same management, the same employees and the same facilities and offer the same types of insurance products.

For additional information about the Donegal parties, see "Where You Can Find More Information" beginning on page v.

The principal executive offices of the Donegal parties are located at 1195 River Road, Marietta, Pennsylvania, 17547. DGI's telephone number is (888) 877-0600 and DGI's website address is [www.donegalgroup.com](http://www.donegalgroup.com). The information on DGI's website is not a part of this proxy statement/prospectus.

**UNNF**

We are a Pennsylvania business corporation, a bank holding company registered under the BHCA and is supervised by the FRB. We were incorporated on June 26, 1986, under the PBCL. We commenced operations on January 2, 1987, upon consummation of its acquisition of all of the outstanding shares of The Union National Mount Joy Bank, which effective February 6, 1998, changed its name to UNCB. Our business consists primarily of managing and supervising UNCB, and our principal source of income is dividends paid by UNCB. We have two trust subsidiaries, UNCT I and UNCT II. UNCT I and UNCT II were formed on December 19, 2003 and October 23, 2004, respectively, for the purpose of issuing trust capital securities. Home Team Financial, LLC, a subsidiary of UNCB, and its subsidiary, TA of Lancaster, LLC, or together, the Home Team, began operations in July 2005 and ceased operations in October 2007. Home Team operated a mortgage banking and brokerage business and also offered title insurance and settlement services. In accordance with agreements between UNCB and the minority interest owners, UNCB's ownership interest in Home Team was 98%, and UNCB's interest in Home Team's net profits and losses was 30% until June 30, 2007, and 62.31% thereafter until Home Team ceased operating on October 31, 2007. UNCB also had a wholly owned subsidiary, Union National Insurance Agency, Inc., or UNIA, which was formed on May 21, 2001 and ceased operations on December 31, 2009. UNIA provided insurance-related products to UNCB's customers. UNIA was subject to supervision and regulation by the Insurance Department of the Commonwealth of Pennsylvania, the OCC and other regulatory agencies.

UNCB was organized in 1865 under a national bank charter. UNCB is a national association, a member of the Federal Reserve System and is regulated by the OCC. The deposits of UNCB are insured by the FDIC to the maximum extent permitted by law. UNCB is a full-service commercial bank, providing a wide range of services to individuals and small to medium sized businesses in its south central Pennsylvania market area. UNCB accepts time, demand, and savings deposits and makes secured and unsecured commercial, real estate and consumer loans. UNCB also had a full service trust department, which subsequent to December 31, 2009, we sold to Security National Trust Company, or Security National. Closing, subject to regulatory approval, is expected in the second quarter of 2010. Under the agreement, UNNF will continue to share in the revenues generated from Security National's management of these assets and will receive a share of revenues on future trust business referrals. Through a third-party provider affiliation, UNCB offers to its customers certain non-depository products, including annuities and brokerage services.

UNCB has ten branch locations within Lancaster County, Pennsylvania.

Our executive offices are located at 570 Lausch Lane, Suite 300, Lancaster, Pennsylvania 17601. Our telephone number is (717) 492-2222.

UNCB experiences substantial competition in attracting and retaining deposits and in lending funds. Financial institutions compete for deposits by offering attractive rates and convenient office locations. Direct competition for

deposits comes primarily from other commercial banks and thrift institutions. Competition for deposits also comes from money market mutual funds, corporate and government securities, and credit unions. The primary factors in the competition for loans are interest rates, loan origination fees and the range of products and services offered. Competition for origination of real estate loans normally comes from other commercial banks, thrift institutions, mortgage bankers and brokers, and insurance companies.

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For additional information concerning our business activities, refer to Management's Discussion and Analysis in UNNF's Financial Condition and Results of Operations elsewhere in this proxy statement/prospectus.

### **Supervision and Regulation of UNNF**

We operate in a heavily regulated environment. Changes in laws and regulations affecting us and UNCB may have an impact on our results of operations.

Without the prior approval of the FRB under the BHCA, we are prohibited from:

- acquiring direct or indirect control of more than 5% of the voting stock of any bank; or
- acquiring substantially all of the assets of any bank; or
- merging with another bank holding company.

The Department also must approve any similar consolidation. Pennsylvania law permits Pennsylvania bank holding companies to control an unlimited number of banks. The BHCA restricts us from engaging in activities other than those that the FRB has found to be closely related to banking, and which are expected to produce benefits for the public that will outweigh any potentially adverse effects. To this end, the BHCA prohibits us from:

- engaging in most non-banking businesses; or
- acquiring ownership or control of more than 5% of the outstanding voting stock of any company engaged in a non-banking business, unless the FRB has determined that the non-banking business is closely related to banking.

Under the BHCA, the FRB may require a bank holding company to end a non-banking business if it constitutes a serious risk to the financial soundness and stability of any bank subsidiary of the bank holding company.

Other than making equity investments in low to moderate income housing limited partnerships, we do not at this time engage in any other permissible activities, nor do we have any current plans to engage in any other permissible activities in the foreseeable future.

Subsidiary banks of a bank holding company are subject to restrictions imposed by the Federal Reserve Act on any extensions of credit to the bank holding company or any of its subsidiaries, on investments in the stock or other securities of the bank holding company and on taking of such stock or securities as collateral for loans to any borrower.

There are various legal restrictions on the extent to which we and our non-bank subsidiaries can borrow or otherwise obtain credit from UNCB. In general, these restrictions require that any such extensions of credit must be secured by designated amounts of specified collateral and are limited, as to us or any one of such non-bank subsidiaries, to 10% of UNCB's capital stock and surplus, and as to us and all such non-bank subsidiaries in the aggregate, to 20% of UNCB's capital stock and surplus. Further, we and UNCB are prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, lease or sale of property or furnishing of services.

### **Legislation and Regulatory Changes**



From time to time, Congress or the Pennsylvania legislature enacts legislation which has the effect of increasing the cost of doing business, limiting or expanding permissible activities or affecting the competitive balance between banks and other financial institutions. Proposals to change the laws and regulations governing the operations and taxation of banks, bank holding companies and other financial institutions are frequently made in Congress, and before various bank regulatory agencies. We cannot predict the likelihood of any major changes or the impact such changes might have on us and UNCB. The following paragraphs discuss legislative

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or regulatory changes of potential significance to us which Congress has recently enacted and others which Congress or various regulatory or professional agencies currently are discussing.

The FRB, the FDIC and the OCC have issued certain risk based capital guidelines, which supplement existing capital requirements. The guidelines require all United States banks and bank holding companies to maintain a minimum risk based capital ratio of 8%, of which at least 4% must be in the form of common stockholders' equity. Assets are assigned to five risk categories, with higher levels of capital required for the categories perceived as representing greater risk. The required capital will represent equity and, to the extent permitted, nonequity capital as a percentage of total risk weighted assets. The risk based capital rules are designed to make regulatory capital requirements more sensitive to differences in risk profiles among banks and bank holding companies and to minimize disincentives for holding liquid assets. On the basis of an analysis of the rules and the projected composition of our consolidated assets, we do not believe that the risk based capital rules have a material effect on our business and capital plans. UNCB has capital ratios exceeding the regulatory requirements and meets UNCB regulatory criteria to be considered well capitalized. For additional information regarding our and UNCB's capital ratios, refer to Note 15 Regulatory Restrictions to the consolidated financial statements included elsewhere in this proxy statement/prospectus.

In addition to the above requirements, effective September 30, 2009, the OCC established individual minimum capital requirements for UNCB. For additional information, refer to Note 18 Enforcement Actions with Bank Regulatory Agencies to the consolidated financial statements included elsewhere in this proxy statement/prospectus. The specific capital requirements established for UNCB were 8% for Tier I capital to average total assets, 9.5% for Tier I capital to risk-based assets, and 12% for total capital to risk-based assets. At December 31, 2009, UNCB's measure of Tier I capital to average total assets was 8.31%, Tier I capital to risk-based assets of 9.69% and total capital to risk-based assets of 12.37%. At December 31, 2009, all three ratios exceeded the respective individual minimum capital requirements the OCC established for UNCB.

## **Effects of Inflation**

Inflation has some impact on our operating costs, but unlike many other corporations, substantially all of our assets and liabilities are monetary in nature. As a result, changes in interest rates have a more significant impact on our performance than the general level of inflation. Interest rates do not necessarily move in the same direction or in the same magnitude as prices of goods and services.

## **Monetary Policy**

Domestic economic conditions and the monetary and fiscal policies of the United States Government and its agencies affect our earnings and those of UNCB. An important function of the FRB is to regulate the money supply and interest rates. Among the instruments used to implement those objectives are open market operations in United States government securities and changes in reserve requirements against member bank deposits. The FRB uses these instruments in varying combinations to influence overall growth and distribution of bank loans, investments and deposits, and their use may also affect rates charged on loans or paid for deposits.

UNCB is a member of the Federal Reserve System. The policies and regulations of the FRB have a significant effect on UNCB's deposits, loans and investment growth, as well as the rate of interest earned and paid, and are expected to affect UNCB's operations in the future. The effect of Federal Reserve Board policies and regulations upon the future business and our earnings and those of UNCB cannot be predicted.

## **Supervision and Regulation of UNCB**

The operations of UNCB are subject to federal and state statutes applicable to banks chartered under the banking laws of the United States, to members of the Federal Reserve System and to banks whose deposits are insured by the FDIC. UNCB's operations are also subject to regulations of the OCC, the FRB and the FDIC.

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The primary supervisory authority of UNCB is the OCC, which regulates and examines UNCB. The OCC has the authority under the Financial Institutions Supervisory Act to prevent a national bank from engaging in an unsafe or unsound practice in conducting its business.

Federal and state banking laws and regulations govern, among other things, the scope of a bank's business, the investments a bank may make, the reserves against deposits a bank must maintain, loans a bank makes and collateral it takes, the maximum interest rates a bank may pay on deposits, the activities of a bank with respect to mergers and consolidations and the establishment of branches.

As a subsidiary of a bank holding company, UNCB is subject to certain restrictions imposed by the Federal Reserve Act on any extensions of credit to the parent bank holding company or its subsidiaries, on investments in the stock or other securities of UNCB holding company or its subsidiaries, and on taking such stock or securities as collateral for loans. The Federal Reserve Act and FRB regulations also place certain limitations and reporting requirements on extensions of credit by a bank to principal shareholders of its parent holding company, among others, and to related interests of such principal shareholders. In addition, such legislation and regulations may affect the terms upon which any person becoming a principal shareholder of a holding company may obtain credit from banks with which the subsidiary bank maintains a correspondent relationship.

Under the Community Reinvestment Act, UNCB has a continuing and affirmative obligation, consistent with its safe and sound operation, to help meet the credit needs of its entire community, including low and moderate income neighborhoods. However, the Community Reinvestment Act, or CRA, does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community. The CRA also requires:

the applicable regulatory agency to assess an institution's record of meeting the credit needs of its community;

public disclosure of an institution's CRA rating; and

that the applicable regulatory agency provides a written evaluation of an institution's CRA performance utilizing a four-tiered descriptive rating system.

### **PROPOSAL NO. 1 PROPOSAL TO ADOPT THE MERGER AGREEMENT**

*The following discussion contains material information pertaining to the merger. This discussion is subject, and qualified in its entirety by reference, to the merger agreement included as Appendix A to this proxy statement/prospectus. We encourage you to carefully read the merger agreement as well as the discussion in this proxy statement/prospectus.*

#### **The Donegal Parties Reasons for the Merger**

DGI and DMIC have long-believed that the ability to offer banking services as well as insurance products may provide certain limited opportunities to cross-sell products and services. For these reasons, DGI and DMIC started Province as a de novo savings association in 2000, and have seen it grow to an institution with \$100 million in assets with three branches in western Lancaster County. Province and UNCB have jointly participated in a number of loan transactions where the amount of the loan exceeded the legal lending limit of Province but where the two institutions could together pool their resources and make the loan.

DMIC began to invest in our common stock and over time has acquired approximately 9.1% of our common stock.



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In approving the merger agreement in April 2010, the boards of directors of the Donegal parties considered the following factors:

the complementary nature of Province and UNCB, and that combining their products and services could result in an opportunity to form a larger community bank and to realize synergies as we cross-market products and distribute them over broader customer bases;

the scale, scope, strength and diversity of operations, products and services and distribution systems that could be achieved by combining Province and us;

their understanding of our business, operations, financial condition, results of operations and prospects, including the presence of DMIC, DGI and Province in Lancaster County which is the location of all of UNCB's branches;

their understanding of the current and prospective environment in which Province and we operate, including local economic conditions, the competitive environment for financial institutions generally and the continuing consolidation in the financial services industry;

the proposed board and management personnel which will provide the combined bank with strong leadership and experienced operating management;

the recent prices of stocks of depository institutions and the opportunity to expand Province's banking operations at an attractive valuation; and

the review by DMIC's and DGI's boards of directors, with the assistance of Keefe, Bruyette & Woods, Inc., DMIC's and DGI's financial advisor, and our management, of the structure and terms of the merger, includes the merger consideration and the likelihood that the strong financial condition of the Donegal parties would facilitate timely receipt of the regulatory approvals needed to complete the merger.

The boards of directors of the Donegal parties also considered the fact that the merger will result in a combined bank with assets of approximately \$600 million. Those boards of directors also believe that the growth prospects of the greater Lancaster County area will provide sustained business development opportunities for the combined bank.

The foregoing discussion of the factors the boards of directors of the Donegal parties considered in evaluating the acquisition of UNNF is not intended to be exhaustive, but, rather, includes all material factors the boards of directors considered. In reaching their decision to approve the merger agreement and the merger, the boards of directors of the Donegal parties did not quantify or assign relative weight to the factors considered, and individual directors may have given different weight to different factors. The boards of directors of the Donegal parties considered all of the above factors as a whole and on an overall basis considered them to be favorable to, and support, the determination of the Donegal parties, to enter into the merger agreement.

## **Background of the Merger**

Our board of directors has regularly reviewed and evaluated strategic options available to us with the goals of strengthening our capital and financial position, identifying internal and external opportunities for growth and profitability consistent with safe and sound banking operations and enhancing long-term shareholder value. This strategic evaluation process has included assessment of our ability to maintain adequate capital to support our business and achieve our goals independently, evaluation of opportunities to acquire other financial institutions or their branch offices, consideration of our expansion into other geographic markets and consideration of a merger or affiliation with

another financial institution with greater capital and sources of capital.

The duration and severity of the current economic recession and the persistent low interest rate environment have significantly reduced our net interest income, a substantial portion of which we generate from variable rate loans. This decline in net interest income, coupled with historically high FDIC deposit

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insurance assessments and significant impairment charges we had to recognize on a number of investment securities not guaranteed by the U.S. government, has had an adverse effect on our results of operations and has caused us to incur net losses in 2009 and to suspend the payment of cash dividends in order to preserve capital. Concurrently, economic and real estate market conditions have adversely affected the cash flows and underlying collateral values for our commercial loan customers, resulting in a higher level of nonperforming loans and charge-offs compared to our historical averages. The increased stress to UNCB's commercial loan portfolio, and the adverse development in our results of operations in recent periods, resulted in the OCC imposing individual minimum capital requirements (IMCR) on UNCB effective September 30, 2009. These IMCRs exceed the requirements for an institution to be considered well capitalized under applicable regulatory guidelines, as disclosed elsewhere in this proxy statement/prospectus.

In an effort to meet and exceed these higher minimum capital requirements, we have had to minimize asset expansion, which has further hampered our net interest income growth potential and profitability improvement prospects in the continuing low interest rate environment. We were able to raise privately approximately \$1.3 million of new capital through a preferred stock offering in the fall of 2009; however, that amount fell considerably short of our target level of between \$5 million and \$10 million. Faced with the continuing need for additional capital to satisfy higher regulatory capital requirements the OCC had imposed on us and to provide a basis for our efforts to return to historical profitability, our board of directors expanded its evaluation of strategic options.

Over the past few years, DMIC has accumulated shares of our common stock, becoming our largest shareholder with a current ownership interest of approximately 9.1% of our outstanding common stock. Donald H. Nikolaus, DMIC's and DGI's President and Chief Executive Officer, and Mark D. Gainer, our Chairman, President and Chief Executive Officer, have met periodically after the public issuance of our annual and quarterly financial results to discuss our financial performance and efforts to address our regulatory issues. Mr. Nikolaus also addressed the interests of DMIC as our largest shareholder and expressed DMIC's desire to maintain our strong community banking presence in Lancaster County, Pennsylvania.

On January 14, 2010, we and UNCB executed a confidentiality agreement with DMIC (on behalf of itself and its subsidiaries and affiliates).

On or about January 14, 2010, DMIC submitted to us an informal non-binding term sheet setting forth certain terms, including pricing, under which DMIC (and its subsidiaries and affiliates) would be interested in pursuing a potential business combination with us if we would also be interested in having such a discussion. The term sheet indicated a price range of \$6.00 to \$7.25 per share of our common stock, payable 55% in cash and 45% in shares of DGI Class A common stock, subject to the completion of DMIC's due diligence.

At a special meeting on February 23, 2010, our board of directors discussed DMIC's informal non-binding term sheet in general terms within the context of our current financial condition, our challenges to sustain growth and our limited ability to raise capital given the current economic conditions. We engaged qualified legal and financial advisors to assist us in evaluating strategic alternatives, including the alternative presented by DMIC.

At its regular meeting on February 25, 2010, our board of directors met with a representative of Sandler O'Neill, a leading national financial advisory firm. The Sandler O'Neill representative discussed with our board of directors Sandler O'Neill's qualifications and experience and the current mergers and acquisitions environment, among other matters.

At a special meeting on March 3, 2010, our board of directors met with representatives of Kilpatrick Stockton LLP, a law firm with significant experience advising financial institutions. The representatives of Kilpatrick Stockton LLP discussed with our board of directors their qualifications and made a presentation regarding the fiduciary duties and



responsibilities of our board of directors in the context of mergers and acquisitions. At this meeting, the UNNF board of directors retained Kilpatrick Stockton LLP and Sandler O'Neill as our legal advisor and financial advisor, respectively. Sandler O'Neill representatives provided a valuation analysis of us, provided an overview of DMIC and DGI's corporate profile, and reviewed the terms of DMIC's informal non-binding term sheet. The Sandler O'Neill representatives also discussed the challenges

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faced by institutions with financial profiles similar to us in raising capital in the current economic environment and reviewed DGI's profile, historical financial position and the numerical range of per share merger consideration proposed by DMIC relative to the valuation analyses of us. Following this discussion, our board of directors authorized Sandler O'Neill to contact DMIC's financial advisor to pursue discussions with DMIC.

From March 16, 2010 through March 20, 2010, representatives of DMIC and of its legal and financial advisors conducted due diligence on us at our main offices.

On March 22, 2010, our representatives and representatives of our legal and financial advisors conducted due diligence on DGI and DMIC at their main offices.

On March 24, 2010, DMIC presented to us a revised non-binding term sheet with updated terms pursuant to which DMIC and its subsidiaries and affiliates would be willing to consider a merger transaction, providing for a price range of \$7.25 to \$7.75 per share of our common stock, payable 55% in cash and 45% in shares of DGI Class A common stock, subject to the completion of DMIC's due diligence.

At a regular meeting on March 25, 2010, at which representatives of Sandler O'Neill and Kilpatrick Stockton LLP were present, our board of directors discussed in detail DMIC's revised non-binding term sheet. Among other things, our board of directors discussed our prospects as an independent institution in light of our limited ability to raise additional capital in the current economic environment. Following lengthy discussions, the board of directors authorized our management and Sandler O'Neill to negotiate the terms of a potential business combination with DMIC.

On March 30, 2010, DMIC's legal counsel delivered a draft of a proposed merger agreement to our legal counsel. The draft merger agreement included a credit-related price adjustment mechanism that would decrease the per share consideration paid to our shareholders if our asset quality deteriorated before the closing date of the proposed transaction.

On April 5, 2010, DMIC filed a Schedule 13D with the SEC to report its ownership in our common stock that it had previously reported on a Schedule 13G. The Schedule 13D disclosed the existence of the ongoing discussions between DMIC and us regarding a potential business combination and the delivery of a proposed draft of a merger agreement to our counsel on March 30, 2010.

On April 9, 2010, we received a written non-binding indication of interest from a regional bank holding company (Company A) to engage in a proposed business combination, indicating a price of \$8.00 per share of our common stock, payable 60% to 70% in Company A common stock and the remainder in cash, subject to the completion of Company A's due diligence. The non-binding indication of interest included the requirement that DMIC execute a voting agreement to vote its shares of our common stock in favor of any transaction between us and Company A.

On April 12, 2010, we received a written non-binding indication of interest from a second regional bank holding company (Company B) to engage in a proposed business combination. The indication of interest did not indicate a proposed price or range of prices to be paid for each share of our common stock.

On April 13, 2010, we received a revised written non-binding indication of interest from Company B, providing for a price range of \$5.00 to \$7.50 per share payable in Company B common stock, subject to due diligence.

At a special meeting on April 14, 2010, at which representatives of Sandler O'Neill and Kilpatrick Stockton LLP participated by telephone, our board of directors discussed the non-binding indications of interest from Company A and Company B. The Sandler O'Neill representative reviewed the terms of the non-binding indications of interest from

Company A and from Company B, in comparison to each other and in comparison to the DMIC non-binding indication of interest. Our legal counsel led a discussion regarding our board of directors' fiduciary duties in the context of competing offers and the factors that may be appropriately considered in weighing competing offers, including the requirement under our articles of incorporation that we receive the affirmative vote of at least 80% of our shareholders in order to engage in a business combination. The board of directors considered this shareholder vote requirement in the context of the competing indications of interest given DMIC's 9.1% ownership interest in us. After further discussion, the board of directors

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authorized Sandler O'Neill to contact representatives of Company A and Company B regarding their indications of interest and to determine their level of interest in pursuing a proposed transaction with us.

Following the meeting, representatives of Sandler O'Neill had further discussions with the respective representatives of Company A and Company B regarding their indications of interest. After further discussions between Sandler O'Neill and Company B's representatives, and subsequent deliberations by our board of directors, our board of directors determined that the potential range of values Company B was prepared to offer to our shareholders (\$5.00 to \$7.50 per share) was lower than that offered by DMIC.

On April 15, 2010, Company A submitted a revised written non-binding indication of interest, indicating a price of \$9.22 per share of UNNF common stock, 60% of which would be paid in Company A common stock and 40% in cash. The non-binding indication of interest was further conditioned upon completion of due diligence, the receipt of an executed voting agreement from DMIC and the expectation that any proposed definitive agreement would include a credit-related price adjustment mechanism that would decrease the per share consideration paid to our shareholders if our asset quality deteriorated before the closing date of a proposed transaction.

On April 19, 2010, our board of directors convened to discuss the terms of Company A's revised non-binding indication of interest and to receive an update from the Sandler O'Neill representative regarding further discussions with DMIC's financial advisor. The Sandler O'Neill representative reported that DMIC agreed to remove the credit-related price adjustment provision and to set the merger consideration at \$5.05 in cash and 0.2134 of a share of DGI Class A common stock, which indicated a value of \$8.22 per share based on the closing price of DGI Class A common stock on April 16, 2010. The Sandler O'Neill representative also reported that DMIC's financial advisor advised that DMIC was unwilling to participate in a competitive bidding process or to continue discussions with us should we decide to explore a potential business combination with another party and that DMIC would likely vote its shares of our common stock against a competing merger proposal if brought to a shareholder vote. Legal counsel then led a discussion regarding the fiduciary duties of our board of directors and the relevant considerations should our board of directors vote to enter into a definitive agreement with DMIC rather than Company A. Upon further discussion and deliberation, our board of directors determined that the 80% vote requirement contained in our articles of incorporation, DMIC's 9.1% ownership position in us, Company A's indication of interest being subject to due diligence, Company A's intention to include a credit-related price adjustment mechanism in any definitive agreement, Company A's requirement that DMIC execute a voting agreement, and DMIC's stated position that it would unlikely vote its shares in favor of a competing merger proposal, were significant factors in favor of DMIC's proposal.

Our board of directors then discussed the proposed definitive merger agreement that had been negotiated by our management and legal and financial advisors, who were present by telephone. Representatives of Sandler O'Neill presented to our board of directors Sandler O'Neill's financial analysis of the proposed merger and rendered Sandler O'Neill's opinion that the consideration to be received by our shareholders in the proposed merger with DMIC was fair, from a financial point of view, to our shareholders. Legal counsel reviewed the terms of the definitive merger agreement and related documents. Following discussion, our board of directors determined unanimously that execution of the merger agreement with the Donegal parties was advisable and in our best interests and the best interests of our shareholders and authorized Mr. Gainer to execute and deliver the merger agreement on our behalf and to take all actions necessary to effect the proposed transaction according to the terms of the definitive merger agreement.

Before the opening of stock trading on April 20, 2010, we and DGI issued a joint press release announcing the adoption and execution of the definitive merger agreement.

## **Our Board of Directors' Reasons for the Merger; Recommendation**

Our board of directors has unanimously approved the merger agreement and unanimously recommends that our shareholders vote FOR approval of the merger agreement.

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Our board of directors has determined that the merger is advisable and in our best interests and the best interests of our shareholders. In approving the merger agreement, our board of directors consulted with Sandler O'Neill regarding the fairness of the transaction to our shareholders from a financial point of view and with our legal counsel regarding its legal duties and the terms of the merger agreement and ancillary documents. In determining to approve the merger agreement and recommend that shareholders approve the merger, our board of directors, in consultation with our senior management and financial and legal advisors, considered a number of factors, including the following material factors:

The understanding of our board of directors of the strategic options available to us and our board of directors assessment of those options with respect to the prospects and estimated results of the execution of our business plan as an independent entity under various scenarios, and the determination that none of those options or the execution of our business plan under the best case scenarios were likely to create greater present value for our shareholders than the value to be paid by DMIC;

Our board of directors' understanding of our current need for additional capital to support our current operations and their assessment, in consultation with Sandler O'Neill, that the financial terms that we would likely have to offer to attract potential investors would be highly dilutive to our existing shareholders, creating materially less present value for our shareholders than the value to be paid by DMIC;

Our ability to execute on our business plan in light of the MOU to which we are subject and the IMCRs to which UNCB is subject and the prospects of the imposition of additional regulatory action on us;

The ability of our shareholders to participate in the future success of the combined post-merger bank through ownership of DGI Class A common stock;

The substantially increased liquidity afforded to our shareholders by an investment in DGI Class A common stock;

Our shareholders ability to receive regular cash dividends as holders of DGI Class A common stock (assuming that DGI maintains its current dividend practice);

Sandler O'Neill's written opinion that, as of April 19, 2010, the merger consideration was fair to our shareholders from a financial point of view;

Information concerning the business, earnings, operations, financial condition and prospects of DGI. Our board of directors took into account the results of our due diligence review of DGI:

DMIC's knowledge of the Lancaster market and the likelihood that all of our current branch offices would remain open after the merger due to the lack of market overlap;

DMIC's commitment to retaining a significant number of our employees, including substantially all of our management and lending team, and that our employees to be retained after the merger would have opportunities for career advancement in a substantially larger organization;

The likelihood of timely receiving regulatory and shareholder approvals of a transaction with DMIC because of its and DGI's strong financial condition;

The ability of our shareholders to satisfy their own investment interests by receiving cash and DGI Class A common stock for their shares of our common stock; and

Mark D. Gainer and two other current members of our board of directors will be appointed to the board of directors of DFSC and that the directors of the resulting combined bank will consist of six current directors of Province and five current directors of UNCB.

The foregoing information and factors considered by our board of directors is not exhaustive, but includes all material factors that our board of directors considered and discussed in approving the merger agreement and recommending that our shareholders vote to approve the merger. In view of the wide variety of factors considered and discussed by our board of directors in connection with its evaluation of the merger and the

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complexity of these factors, our board of directors did not consider it practical to, nor did it attempt to, quantify, rank or otherwise assign any specific or relative weights to the specific factors that it considered in reaching its decision; rather it considered all of the factors as a whole. Our board of directors discussed and considered the foregoing factors and reached general consensus that the merger with DFSC was in our best interest and the best interests of our shareholders. In considering the foregoing factors, individual directors may have assigned different weights to different factors. Our board of directors relied on the experience and expertise of Sandler O'Neill for quantitative analysis of the financial terms of the merger agreement. See Opinion of Our Financial Advisor in Connection with the Merger on page 84. This explanation of the reasoning of our board of directors and all other information presented in this section is forward-looking in nature and, therefore, should be read in light of the factors discussed under Cautionary Statement Regarding Forward-Looking Statements on page 70.

**Opinion of Our Financial Advisor in Connection with the Merger**

By letter dated March 18, 2010, UNNF retained Sandler O'Neill to act as its independent financial advisor in connection with a possible business combination with DGI or one of its affiliated entities. Sandler O'Neill is a nationally recognized investment banking firm whose principal business specialty is financial institutions. In the ordinary course of its investment banking business, Sandler O'Neill is regularly engaged in the valuation of financial institutions and their securities in connection with mergers and acquisitions and other corporate transactions.

Sandler O'Neill acted as financial advisor to UNNF in connection with the proposed transaction and participated in certain of the negotiations leading to the execution of the merger agreement. At the April 19, 2010 meeting at which UNNF's board considered and approved the merger agreement Sandler O'Neill delivered to the board its oral opinion, that, as of such date, the merger consideration was fair to the holders of UNNF common stock from a financial point of view. **We have included the full text of Sandler O'Neill's opinion as Appendix B to this proxy statement/prospectus. The opinion outlines the procedures followed, assumptions made, matters considered and qualifications and limitations on the review undertaken by Sandler O'Neill in rendering its opinion. The description of the opinion set forth below is qualified in its entirety by reference to the opinion. UNNF's shareholders are urged to read the entire opinion carefully in connection with their consideration of the proposed merger.**

**Sandler O'Neill's opinion speaks only as of the date of the opinion. The opinion was directed to UNNF's board and is directed only to the fairness of the merger consideration to UNNF's shareholders from a financial point of view. It does not address the underlying business decision of UNNF to engage in the merger or any other aspect of the merger and is not a recommendation to any UNNF shareholder as to how such shareholder should vote at our special meeting with respect to the merger or any other matter.**

In connection with rendering its April 19, 2010 opinion, Sandler O'Neill reviewed and considered, among other things:

- (1) the merger agreement;
- (2) certain publicly available financial statements and other historical financial information of UNNF that Sandler O'Neill deemed relevant;
- (3) certain publicly available financial statements and other historical financial information of DGI and its subsidiaries that Sandler O'Neill deemed relevant;
- (4) internal financial projections for UNNF for the calendar years ending December 31, 2010 through December 31, 2014 as provided by senior management of UNNF;



(5) publicly available consensus earnings estimates for DGI for the years ending December 31, 2010 and 2011 and publicly available median long-term growth rate for the years ending December 31, 2012 through 2014;

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- (6) the pro forma financial impact of the merger on DGI, based on assumptions relating to transaction expenses, acquisition accounting adjustments and cost savings determined by the senior management of DGI;
- (7) the publicly reported historical price and trading activity for UNNF's common stock and DGI's Class A common stock, including a comparison of certain financial and stock market information for UNNF and DGI and similar publicly available information for certain other companies the securities of which are publicly traded;
- (8) the financial terms of certain recent business combinations in the banking industry, to the extent publicly available;
- (9) the current market environment generally and the banking environment in particular; and
- (10) such other information, financial studies, analyses and investigations and financial, economic and market criteria as Sandler O'Neill considered relevant;

Sandler O'Neill also discussed with certain members of senior management of UNNF the business, financial condition, results of operations and prospects of UNNF and held similar discussions with certain members of senior management of DGI regarding the business, financial condition, results of operations and prospects of DGI.

In performing its review, Sandler O'Neill has relied upon the accuracy and completeness of all of the financial and other information that was available to it from public sources, that was provided to it by UNNF and DGI or its respective representatives or that was otherwise reviewed by it and Sandler O'Neill assumed such accuracy and completeness for purposes of rendering its opinion. Sandler O'Neill has further relied on the assurances of management of each of UNNF and DGI that it is not aware of any facts or circumstances that would make any of such information inaccurate or misleading. Sandler O'Neill has not been asked to and has not undertaken an independent verification of any of such information and it did not assume any responsibility or liability for the accuracy or completeness thereof. Sandler O'Neill did not make an independent evaluation or appraisal of the specific assets, the collateral securing assets or the liabilities (contingent or otherwise) of UNNF and DGI or any of their subsidiaries, or the collectability of any such assets, nor was it furnished with any such evaluations or appraisals.

Sandler O'Neill did not make an independent evaluation of the adequacy of the allowance for loan losses of UNNF and Province and has not reviewed any individual credit files relating to UNNF and Province. Sandler O'Neill has assumed, with UNNF's consent, that the respective allowances for loan losses for both UNNF and DGI are adequate to cover such losses and will be adequate for the future for the combined entity.

With respect to the internal financial projections prepared by the senior management of UNNF and the publicly available earnings estimates and estimated long-term growth rates for DGI and in each case reviewed with respective managements of UNNF and DGI and used by Sandler O'Neill in its analysis, the respective managements of UNNF and DGI confirmed to Sandler O'Neill that they reflected the best currently available estimates and judgments of each respective management of the future financial performance of UNNF and DGI. With respect to the anticipated transaction costs, acquisition accounting adjustments and expected cost savings as determined by and reviewed with senior management of DGI, management confirmed to Sandler O'Neill that these estimates reflected the best currently available estimates and judgments of management with respect thereto and Sandler O'Neill assumed that such performances would be achieved. Sandler O'Neill expresses no opinion as to such financial projections or the assumptions on which they are based. Sandler O'Neill has also assumed that there has been no material change in UNNF's and DGI's assets, financial condition, results of operations, business or prospects since the date of the most recent financial statements and other financial information made available to Sandler O'Neill. Sandler O'Neill has assumed in all respects material to its analysis that UNNF and DGI will remain as going concerns for all periods relevant to the analyses, that each party to the merger agreement will perform, satisfy or waive all of the material covenants required to be performed by such party under the Agreement, and that the conditions precedent in the

merger agreement are satisfied. Sandler O'Neill expressed no opinion as to any of the legal, accounting or tax matters relating to the Merger and the other transactions the merger agreement contemplates.

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Sandler O'Neill necessarily based its opinion on financial, economic, market and other conditions as in effect on, and the information made available to Sandler O'Neill as of, the date of the opinion. Events occurring after the date of Sandler O'Neill's opinion could materially affect this opinion. Sandler O'Neill has not undertaken to update, revise, reaffirm or withdraw this opinion or otherwise comment upon events occurring after the date of this proxy statement/prospectus. Sandler O'Neill expresses no opinion in this proxy statement/prospectus as to what the value of DGI's Class A common stock will be when issued to UNNF's shareholders pursuant to the Agreement or the prices at which UNNF's and DGI's Class A common stock may trade at any time.

Sandler O'Neill's opinion is directed to the board of directors of UNNF in connection with its consideration of the merger and does not constitute a recommendation to any shareholder of UNNF as to how such shareholder should vote at any meeting of shareholders called to consider and vote upon the merger. Sandler O'Neill's opinion is directed only to the fairness, from a financial point of view, of the merger consideration to holders of UNNF common stock and does not address the underlying business decision of UNNF to engage in the merger, the relative merits of the merger compared to any other alternative business strategies that might exist for UNNF or the effect of any other transaction in which UNNF might engage. Sandler O'Neill's opinion may not be quoted or referred to, in whole or in part, in a registration statement, prospectus, proxy statement or in any other document, nor shall its opinion be used for any other purposes, without Sandler O'Neill's prior written consent, which will not be unreasonably withheld. Sandler O'Neill's fairness opinion committee approved Sandler O'Neill's opinion. Sandler O'Neill does not express any opinion as to the fairness of the amount or nature of the compensation to be received in the merger by UNNF's officers, directors, or employees, or class of such persons, relative to the compensation to be received in the merger by any other shareholders of UNNF.

*Summary of Proposal.* Sandler O'Neill reviewed the financial terms of the proposed transaction. Using the fixed exchange ratio of 0.2134 share of DGI Class A common stock for each share of UNNF common stock and \$5.05 per share in cash (based upon DGI's closing stock price of DGI's Class A common stock as of April 16, 2010 of \$14.85), Sandler O'Neill calculated a transaction value of \$8.22 per share, or an aggregate transaction value of \$25.2 million. Based upon financial information for UNNF as of or for the year ended December 31, 2009, Sandler O'Neill calculated the following transaction ratios:

**Transaction Ratios**

Transaction value/Tangible book value	80.0%
Transaction value/Stated book value per share	80.0%
Tangible book premium/Core Deposits	(1.8)%
Transaction Value/Market Value(1)	125.2%

(1) Based on UNNF's closing price as of April 5, 2010, prior to DGI's Schedule 13D filing.

The aggregate transaction value of approximately \$25.2 million was based upon the offer price per share of \$8.22 and 2,742,395 UNNF common shares outstanding and 318,750 shares associated with the conversion of outstanding UNNF convertible preferred stock.

*Comparable Company Analysis.* Sandler O'Neill used publicly available information to perform a comparison of selected financial and market trading information for UNNF and DGI.

Sandler O'Neill also used publicly available information to compare selected financial and market trading information for UNNF and a group of financial institutions selected by Sandler O'Neill. The UNNF peer group



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consisted of the following publicly-traded commercial banks headquartered in Pennsylvania and Maryland with total assets greater than \$400 million and less than \$650 million:

American Bank Incorporated	DNB Financial Corporation
Annapolis Bancorp, Inc.	Emclair Financial Corp.
Carrollton Bancorp	Fidelity D & D Bancorp, Inc.
CB Financial Services, Inc.	Honat Bancorp, Inc.
CCFNB Bancorp, Inc.	Juniata Valley Financial Corp.
Cecil Bancorp, Inc.	Mid Penn Bancorp, Inc.
Delmar Bancorp	Norwood Financial Corp.
Dimeco, Inc.	Peoples Financial Services Corp.

The analysis compared publicly available financial information for UNNF and the high, low, mean, and median financial and market trading data for the UNNF peer group as of and for the year ended December 31, 2009. The table below sets forth the data for UNNF and the median data for the UNNF peer group as of and for the year ended December 31, 2009, with pricing data as of April 16, 2010 for the peer group and April 5, 2010 for UNNF.

**Comparable Group Analysis**

	UNNF	Comparable Group Median Result
Total Assets ( <i>in millions</i> )	\$ 490	\$ 513
Tangible Common Equity/Tangible Assets	6.1%	7.4%
Total Risk Based Capital Ratio	12.7%	12.8%
Return on Average Assets	(0.14)%	0.32%
Return on Average Equity	(2.30)%	4.00%
Net Interest Margin	2.73%	3.66%
Loan Loss Reserve/Gross Loans	1.73%	1.48%
Loan Loss Reserve/Non-performing Assets	40.8%	67.0%
Net Charge-Offs/Average Loans	0.32%	0.37%
Non-performing Assets/Assets	2.93%	1.59%
Price/Tangible Book Value	34%	94%
Price/LTM Core Earnings per Share	NM	12.7x
Dividend Yield	0.00%	3.33%
Market Capitalization ( <i>in millions</i> )	\$ 8.8	\$ 34.8

DGI peer group consisted of selected publicly-traded property and casualty insurers:

Baldwin & Lyons, Inc.	Mercury General Corporation
EMC Insurance Group, Inc.	Safety Insurance Group, Inc.
Hanover Insurance Group, Inc.	Selective Insurance Group, Inc.
Harleysville Group, Inc.	State Auto Financial Corporation
Mercer Insurance Group, Inc.	United Fire & Casualty Company

The analysis compared publicly available financial and market trading information for DGI and the median data for DGI peer group as of and for the year ended December 31, 2009. The table below sets forth the data for DGI and the median data for the DGI peer group as of and for the year ended December 31, 2009, with pricing data as of April 16, 2010.

**Table of Contents****Comparable Group Analysis**

	<b>DGI</b>	<b>Comparable Group Median Result</b>
Operating Return on Average Equity	4.2%	8.1%
Price/2010 Consensus Estimated EPS	12.8x	11.9x
Price/2011 Consensus Estimated EPS	11.5x	11.1x
Price/Tangible Book Value	0.98x	0.90x
Price/Tangible Book Value ex. AOCI	1.02x	0.92x
Dividend Yield	3.1%	3.3%

*Stock Trading History.* Sandler O'Neill reviewed the history of the publicly reported trading prices of UNNF's common stock for the one-year period ended April 16, 2010. Sandler O'Neill also reviewed the relationship between the movements in the price of UNNF's common stock and the movements in the prices of the Standard & Poor's Bank Index, NASDAQ Bank Index, and the median performance of a composite peer group of publicly traded commercial banks selected by Sandler O'Neill for UNNF. The composition of the respective peer groups for DGI is discussed under the relevant section under "Comparable Group Analysis" above.

**UNNF's One-Year Common Stock Performance**

	<b>Beginning Index Value April 16, 2009</b>	<b>Ending Index Value April 16, 2010</b>
UNNF	100.00%	20.0%
Selected Peer Group(1)	100.00	(8.1)
S&P Bank Index	100.00	59.4
NASDAQ Bank Index	100.00	18.0

(1) Refers to the peer group outlined in the Comparable Group Analysis section above.

Sandler O'Neill reviewed the history of the publicly reported trading prices of DGI's Class A common stock for the five-year period ended April 16, 2010. Sandler O'Neill also reviewed the relationship between the movements in the price of DGI's Class A common stock and the movements in the prices of the Standard & Poor's 500 Index, the Standard & Poor's Property & Casualty Index, and the median performance of a composite peer group of publicly traded property and casualty insurers selected by Sandler O'Neill for DGI. The composition of the respective peer groups for DGI is discussed under the relevant section under "Comparable Group Analysis" above.

**DGI's Five-Year Class A Common Stock Performance**

	<b>Beginning Index Value April 15, 2005</b>	<b>Ending Index Value April 16, 2010</b>
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DGI	100.00%	16.1%
Selected Peer Group(1)	100.00	(22.3)
S&P 500 Index	100.00	4.3
S&P P&C Index	100.00	(14.8)

(1) Refers to the peer group outlined in the Comparable Group Analysis section above.

*Net Present Value Analysis.* Sandler O Neill performed an analysis that estimated the present value per Class A common share of DGI through December 31, 2014. Sandler O Neill based the analysis on DGI's projected earnings and dividend stream as derived from mean analyst estimates for 2010 and 2011 and using the mean publicly available analyst estimated long-term growth rate for 2012 through 2015. To approximate the terminal value of DGI's Class A common stock at December 31, 2014, Sandler O Neill applied price to

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forward earnings multiples of 11.0x to 15.0x and multiples of shareholders' equity ranging from 90% to 130%. The dividend income streams and terminal values were then discounted to present values using different discount rates ranging from 11.0% to 15.0% chosen to reflect different assumptions regarding required rates of return of holders or prospective buyers of DGI common stock.

As illustrated in the following tables, the analysis indicated an imputed range of values per share for DGI's common stock of \$13.22 to \$19.98 when applying the price/earnings multiples to the analyst estimates, \$11.87 to \$18.64 when applying multiples of tangible book value to the analyst estimates.

**Forward Earnings Per Share Multiples**

Discount Rate	11.0x	12.0x	13.0x	14.0x	15.0x
11.00%	\$ 15.51	\$ 16.63	\$ 17.75	\$ 18.87	\$ 19.98
12.00%	14.89	15.96	17.03	18.10	19.17
13.00%	14.31	15.33	16.35	17.37	18.40
14.00%	13.75	14.73	15.71	16.68	17.66
15.00%	13.22	14.16	15.09	16.03	16.97

**Tangible Book Value Per Share Multiples**

Discount Rate	90%	100%	110%	120%	130%
11.00%	\$ 13.90	\$ 15.08	\$ 16.27	\$ 17.46	\$ 18.64
12.00%	13.35	14.48	15.62	16.75	17.89
13.00%	12.83	13.91	15.00	16.09	17.17
14.00%	12.34	13.37	14.41	15.45	16.49
15.00%	11.87	12.86	13.85	14.85	15.84

Sandler O'Neill performed an analysis that estimated the present value per common share of UNNF through December 31, 2014, assuming no projected dividend payments, that UNNF performed in accordance with the financial projections for 2010 through 2014 provided by management, and the conversion of \$1.275 million in currently outstanding convertible preferred stock into 318,750 shares of UNNF common stock. To approximate the terminal value of UNNF's common stock at December 31, 2014, Sandler O'Neill applied price to last twelve months earnings multiples of 10.0x to 15.0x and multiples of tangible book value ranging from 65% to 140%. The dividend income streams and terminal values were then discounted to present values using different discount rates ranging from 14.0% to 17.0% chosen to reflect different assumptions regarding required rates of return of holders or prospective buyers of UNNF common stock. In addition, the terminal value of UNNF's common stock at December 31, 2014 was calculated using the same range of price to LTM earnings multiples (10.0x - 15.0x) applied to a range of discounts and premiums to management's budget projections. The range applied to the budgeted net income was 15% under budget to 15% over budget, using a discount rate of 16.21% for the tabular analysis. As illustrated in the following tables, this analysis indicated an imputed range of values per share for UNNF's common stock of \$5.77 to \$9.85 when applying the price/earnings multiples to the matched budget, \$4.43 to \$10.87 when applying multiples of tangible book value to the matched budget, and \$5.07 to \$10.29 when applying the price/earnings multiples to the -15% / +15% budget variance range.

**Earnings Per Share Multiples**

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Discount Rate	10.0x	11.0x	12.0x	13.0x	14.0x	15.0x
14.00%	\$ 6.56	\$ 7.22	\$ 7.88	\$ 8.53	\$ 9.19	\$ 9.85
15.00%	6.28	6.91	7.54	8.17	8.80	9.43
16.00%	6.02	6.62	7.22	7.82	8.43	9.03
17.00%	5.77	6.34	6.92	7.49	8.07	8.65

**Table of Contents*****Tangible Book Value Per Share Multiples***

Discount Rate	65%	80%	95%	110%	125%	140%
14.00%	\$ 5.05	\$ 6.21	\$ 7.37	\$ 8.54	\$ 9.70	\$ 10.87
15.00%	4.83	5.94	7.06	8.17	9.29	10.40
16.00%	4.62	5.69	6.76	7.83	8.89	9.96
17.00%	4.43	5.45	6.48	7.50	8.52	9.54

***Earnings Per Share Multiples***

Budget Variance	10.0x	11.0x	12.0x	13.0x	14.0x	15.0x
(15.0)%	\$ 5.07	\$ 5.58	\$ 6.08	\$ 6.59	\$ 7.10	\$ 7.60
(10.0)%	5.37	5.90	6.44	6.98	7.51	8.05
(5.0)%	5.67	6.23	6.80	7.37	7.93	8.50
0.0%	5.96	6.56	7.16	7.75	8.35	8.95
5.0%	6.26	6.89	7.51	8.14	8.77	9.39
10.0%	6.56	7.22	7.87	8.53	9.18	9.84
15.0%	6.86	7.54	8.23	8.92	9.60	10.29

In addition, Sandler O'Neill performed an analysis that estimated the present value per common share of UNNF through December 31, 2014 using the aforementioned parameters and also considering a \$10 million common stock offering by UNNF at \$4.00 per share. To approximate the terminal value of UNNF's common stock at December 31, 2014 under this scenario, Sandler O'Neill applied the same price to LTM earnings multiples of 10.0x to 15.0x and multiples of tangible book value ranging from 65% to 140%. The dividend income streams and terminal values were then discounted to present values using different discount rates ranging from 14.0% to 17.0% chosen to reflect different assumptions regarding required rates of return of holders or prospective buyers of UNNF common stock. In addition, the terminal value of UNNF's common stock at December 31, 2014 was calculated using the same range of price to LTM earnings multiples (10.0x - 15.0x) applied to a range of common equity raised from \$5 million to \$15 million. The range was discounted using a discount rate of 16.21% for the tabular analysis. As illustrated in the following tables, this analysis indicated an imputed range of values per share for UNNF's common stock of \$3.41 to \$5.82 when applying the price/earnings multiples, \$3.01 to \$7.38 when applying multiples of tangible book value, and \$2.98 to \$6.59 when applying the price/earnings multiples to the \$5 million to \$15 million of common equity raised.

***Earnings Per Share Multiples***

Discount Rate	10.0x	11.0x	12.0x	13.0x	14.0x	15.0x
14.00%	\$ 3.88	\$ 4.27	\$ 4.66	\$ 5.05	\$ 5.43	\$ 5.82
15.00%	3.72	4.09	4.46	4.83	5.20	5.57
16.00%	3.56	3.91	4.27	4.63	4.98	5.34
17.00%	3.41	3.75	4.09	4.43	4.77	5.11

***Tangible Book Value Per Share Multiples***

Discount Rate	65%	80%	95%	110%	125%	140%
14.00%	\$ 3.43	\$ 4.22	\$ 5.01	\$ 5.80	\$ 6.59	\$ 7.38

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15.00%	3.28	4.04	4.79	5.55	6.31	7.06
16.00%	3.14	3.87	4.59	5.31	6.04	6.76
17.00%	3.01	3.70	4.40	5.09	5.79	6.48

**Table of Contents*****Earnings Per Share Multiples***

Capital Raised	10.0x	11.0x	12.0x	13.0x	14.0x	15.0x
\$5 million	\$ 4.39	\$ 4.83	\$ 5.27	\$ 5.71	\$ 6.15	\$ 6.59
\$10 million	3.53	3.88	4.23	4.58	4.94	5.29
\$15 million	2.98	3.28	3.57	3.87	4.17	4.47

In connection with its analyses, Sandler O'Neill considered and discussed with UNNF's board how the present value analyses would be affected by changes in the underlying assumptions, including variations with respect to net income. Sandler O'Neill noted that the discounted dividend stream and terminal value analysis is a widely used valuation methodology, but the results of such methodology are highly dependent upon the numerous assumptions that must be made, and the results thereof are not necessarily indicative of actual values or future results.

*Analysis of Selected Merger Transactions.* Sandler O'Neill reviewed nine merger transactions announced from September 1, 2008 through April 16, 2010 involving banks and thrifts in New Jersey and Pennsylvania with announced transaction values less than \$100 million. Sandler O'Neill reviewed the following multiples: transaction price at announcement to last twelve months earnings per share, transaction price to stated book value, transaction price to stated tangible book value, tangible book premium to core deposits, and market price premium at announcement. As illustrated in the following table, Sandler O'Neill compared the proposed merger multiples to the median multiples of comparable transactions.

**Comparable Transaction Multiples**

	DGI/UNNF	Median Group Multiple
Transaction price/Last Twelve Months Earnings Per Share	NM	37.8x
Transaction price/Book value	80%	101%
Transaction price/Tangible book value	80%	103%
Tangible book premium/Core deposits	(1.8)%	0.9%
Premium to market price at announcement	125.2%	38.4%

*Pro Forma Merger Analysis.* Sandler O'Neill analyzed certain potential pro forma effects of the merger, assuming the following: (1) the merger closes at the end of the third quarter of 2010; (2) UNNF shares are exchanged for DGI Class A common stock at a fixed exchange ratio of 0.2134 and for cash consideration of \$5.05 per share; (3) internal financial projections for UNNF for the calendar years ending December 31, 2010 through December 31, 2014 as provided by senior management of UNNF; (4) publicly available consensus earnings estimates for DGI for the years ending December 31, 2010 and 2011 and publicly available median long-term growth rates for the years ending December 31, 2012 through 2014; (5) business combination accounting adjustments, including a \$17.5 million credit mark against UNNF's loan portfolio in aggregate, including the reversal of UNNF's loan loss reserve, (6) cost savings of 7%, or \$1.1 million, fully phased in by 2011, (7) 3.00% core deposit intangible amortized over 10 years using a sum-of-the-year's digits methodology, (8) 3.25% opportunity cost of cash and (9) approximately \$1.0 million in pre-tax transaction costs and expenses associated with the merger, determined by the senior managements of UNNF and DGI.

For each of the years 2011 and 2012, Sandler O'Neill compared the earnings per share of DGI common stock to the EPS, on a GAAP basis, of the combined company common stock using the foregoing assumptions. The following

table sets forth the results of the analysis:

	<b>GAAP Basis Accretion/(Dilution)</b>
2010 Estimated EPS	(1.1)%
2011 Estimated EPS	5.8%
2012 Estimated EPS	5.9%

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The analyses indicated that the merger would be dilutive to DGI's projected 2010 EPS and accretive to DGI's projected 2011 and 2012 EPS. The actual results achieved by the combined company may vary from projected results and the variations may be material.

Sandler O'Neill has acted as financial advisor to the board of directors of UNNF in connection with the Merger and will receive a fee for its services, a substantial portion of which is contingent upon consummation of the Merger. Sandler O'Neill will also receive a fee for rendering this opinion. UNNF has also agreed to indemnify Sandler O'Neill against certain liabilities arising out of its engagement.

*Miscellaneous.* In the ordinary course of their respective broker and dealer businesses, Sandler O'Neill may purchase securities from and sell securities to UNNF and DGI and their affiliates. Sandler O'Neill may also actively trade the debt and/or equity securities of UNNF or DGI or their affiliates for their own accounts and for the accounts of their customers and, accordingly, may at any time hold a long or short position in such securities.

## **Structure of the Merger and the Merger Consideration**

*Structure.* Subject to the terms and conditions of the merger agreement, and in accordance with Pennsylvania and Delaware law, the merger will include the following steps:

DAI will merge with and into UNNF with UNNF as the surviving corporation in that merger;

immediately after that merger, UNNF will merge with and into DFSC with DFSC as the surviving corporation in that merger; and

immediately after that merger, UNCB will merge with and into Province with Province as the surviving bank in that merger.

Each share of our common stock issued and outstanding at the effective time of the merger, other than the shares DMIC holds and the shares held by dissenting shareholders, will be converted into \$5.05 in cash and 0.2134 share of DGI Class A common stock.

When we complete the merger, our separate corporate existence will terminate. After the merger, your rights as a shareholder of DGI will be governed by Delaware law, DGI's certificate of incorporation and DGI's by-laws.

The board of directors of Province will continue as the board of directors of the combined bank, except that at the completion of the bank merger, Province will appoint to its board of directors Mark D. Gainer and four other persons from among the current members of UNCB's board of directors, as mutually agreed upon by DFSC and us. The board of directors of DFSC after the merger will consist of the current members of the board of directors of DFSC plus Mark D. Gainer and two other persons from among the current members of our board of directors as mutually agreed by DFSC and us.

*Merger Consideration.* The merger agreement provides that at the effective time of the merger each share of our common stock issued and outstanding immediately prior to the effective time, other than shares DMIC holds and shares held by persons who perfect dissenters' rights, will be converted into the right to receive:

0.2134 share of DGI Class A common stock; and

\$5.05 in cash.



As of May 1, 2010, our executive officers had outstanding options to purchase an aggregate of 33,900 shares of our common stock at exercise prices ranging from \$16.10 to \$22.14 per share. In the merger agreement, we have agreed to use commercially reasonable efforts to obtain from each holder of an option such holder's consent to the surrender and cancellation of such options because the options have no current value.

Since the market value of DGI Class A common stock may fluctuate due to a variety of factors and because the exchange ratio of 0.2134 share of DGI Class A common stock and the \$5.05 in cash for each

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share of UNNF common stock are both fixed, we can provide no assurance that the value of 0.2134 share of DGI Class A common stock received in the merger and \$5.05 in cash will be substantially equivalent to \$8.18 in cash. In addition, we can provide no assurance that the value of 0.2134 share of DGI Class A common stock you will receive following the effective time of the merger will be substantially equivalent to the value of 0.2134 share of DGI Class A common stock at the time of the vote to approve the merger proposal or at the time the merger becomes effective. As the market value of DGI Class A common stock fluctuates, the value of 0.2134 share of DGI Class A common stock that you will receive will correspondingly fluctuate.

If, between the date of the merger agreement and the effective time of the merger, DGI changes its shares of Class A common stock into a different number or class of shares by reason of any reorganization, recapitalization, reclassification, stock dividend, stock split, reverse stock split or other similar change in DGI's capitalization other than a business combination transaction with another bank holding company, insurance company or financial services company, then DGI will make proportionate adjustments to the per share merger consideration.

*Treasury Shares.* Upon consummation of the merger, DFSC will cancel and retire any shares of our common stock that we or any of our subsidiaries hold or that DMIC or any of its subsidiaries holds, other than in a fiduciary capacity or as a result of debts previously contracted in good faith, and DFSC will provide no merger consideration with respect to those shares.

**Procedures for the Exchange of the Merger Consideration for Our Common Stock**

*Exchange Fund.* Immediately prior to the effective time of the merger, DFSC will deposit with the exchange agent certificates representing the 600,000 shares of DGI Class A common stock and approximately \$14.2 million in cash for exchange by the exchange agent for shares of our common stock.

*Exchange Procedures.* After the effective time of the merger, each holder of one or more certificates representing our common stock, other than treasury shares, shares DMIC holds and shares held by dissenting shareholders who has surrendered such certificate or customary affidavits and indemnification regarding the loss or destruction of such certificate, together with duly executed transmittal materials to the existing agents, will be entitled to receive a certificate representing DGI Class A common stock and cash in accordance with the procedures described above.

If your certificate representing our common stock is lost, stolen or destroyed, you may receive shares of DGI Class A common stock and cash if you sign an affidavit of that fact. DGI may also require that you post a bond in a reasonable amount as an indemnity against any claim made against DGI with respect to the lost, stolen or destroyed UNNF stock certificate.

Until you exchange your certificates representing our common stock, you will not receive any dividends or distributions in respect of any shares of DGI Class A common stock you are entitled to receive in connection with the merger. Once you exchange your certificates representing our common stock for DGI Class A stock certificates and cash, you will be entitled to receive any dividends or distributions with a record date after the effective time of the merger and payable with respect to your shares of DGI Class A common stock.

After completion of the merger, we will not make any transfers of our common stock issued and outstanding immediately prior to the completion of the merger, except as required to settle trades executed prior to the completion of the merger. If a shareholder presents certificates representing shares of our common stock for transfer after the completion of the merger, the exchange agent will cancel the certificates and exchange them for the merger consideration into which the shares represented by such certificates have been converted.

Computershare Trust Company, or Computershare, whom DFSC appointed as exchange agent, will issue a DGI Class A stock certificate, and a check representing cash, in a name other than the name in which a surrendered certificate representing our common stock is registered only if the surrendered certificate representing our common stock is properly endorsed and otherwise in proper form for transfer. The person requesting such exchange shall either affix any requisite stock transfer tax stamps to the surrendered certificate

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representing our common stock, provide funds for their purchase or establish to the satisfaction of Computershare that such transfer taxes are not payable.

You may exchange your stock certificates for cash and DGI Class A common stock certificates with Computershare for up to 12 months after the completion of the merger. At the end of that period, Computershare will return any DGI Class A common stock certificates and cash to DFSC. Any holders of our stock certificates who have not exchanged their certificates within that nine-month period will then be entitled to look only to DGI to seek payment of their claim for cash and DGI Class A common stock to be received as merger consideration.

DFSC and the exchange agent are entitled to deduct and withhold from any amounts payable to any holder of shares of our common stock such backup withholding as is required under the Code, or any state, local or foreign tax law or regulation. Any amounts that are withheld will be treated as having been paid to such holder of our common stock.

Neither we nor any Donegal party will be liable to any former holder of our common stock for any shares of DGI Class A common stock or cash that DFSC pays to a public official pursuant to any applicable abandoned property, escheat or similar laws.

### **Resales of DGI Class A Common Stock**

The DGI Class A common stock distributed to our shareholders in connection with the merger will be freely transferable, except that any shares issued to any of our shareholders who may be deemed to be an affiliate of DGI will be subject to restrictions on the resale of such DGI Class A common stock under Rule 144 adopted by the SEC.

### **Interests of Directors and Executive Officers of the Donegal Parties in the Merger**

None of the executive officers or directors of any Donegal party has any direct or indirect interest in the merger, except insofar as the ownership of our common stock might be deemed such an interest.

### **Interests of Our Directors and Executive Officers in the Merger**

In considering the recommendation of our board of directors that you vote **FOR** the approval of the merger proposal, you should be aware that some of our executive officers and directors have interests in the merger that are different from, or in addition to, your interests as our shareholders. Our board of directors was aware of these interests and took them into account in its decision to approve the merger agreement.

These interests relate to or arise from, among other things:

- the continued indemnification of our current directors and executive officers under the merger agreement and providing these individuals with directors and officers insurance;

- the agreement of DFSC and Province to honor the existing employment and change of control agreements for eight of our officers, including our executive officers, unless and until such officers individually determine to execute a mutually acceptable employment agreement with DFSC and Province;

- the agreement of DFSC and Province to honor Mr. Gainer's existing employment agreement and his existing amended and restated executive salary continuation agreement, or the salary agreement, unless and until Mr. Gainer, DFSC and Province execute a mutually acceptable employment agreement and a mutually acceptable amended and restated salary agreement;

the appointment of Mr. Gainer and two other current members of our board of directors to DFSC's board of directors and their receipt of directors' fees in connection therewith; and

the appointment of Mr. Gainer and four other current members of UNCB's board of directors to the board of directors of Province and their receipt of directors' fees in connection therewith.

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*Indemnification and Directors and Officers Insurance.* DFSC has agreed in the merger agreement that for six years following the effective time of the merger, DFSC will indemnify and hold harmless each of our present and former directors, officers and employees and those of our subsidiaries against any costs or expenses including reasonable attorneys' fees, judgments, fines, losses, claims, damages or liabilities incurred in connection with any claim, action, suit, proceeding or investigation, whether civil, criminal, administrative or investigative, arising out of matters existing or occurring at or prior to the effective time of the merger including the transactions the merger agreement contemplates, whether asserted or claimed prior to, at or after the effective time of the merger, to the fullest extent that the person would have been indemnified pursuant to (i) our articles of incorporation and by-laws and (ii) any agreement, arrangement or understanding we disclosed to DFSC, in each case as in effect on the date of the merger agreement.

DFSC has also agreed in the merger agreement that for a period of six years after the effective time of the merger, it will cause the persons serving as our directors and officers immediately prior to the effective time of the merger to be covered by the directors' and officers' liability insurance policy we currently maintain. DFSC is permitted to provide a substitute insurance policy of at least the same coverage and amounts that contains terms and conditions that are not materially less advantageous than the insurance policy we presently maintain. In no case, however, will DFSC be required to expend in any one year an amount in excess of 175% of the annual premium we currently pay for such insurance. If DFSC is unable to maintain or obtain such insurance for that amount, then DFSC will use its commercially reasonable efforts to obtain the most advantageous coverage as is available for that amount.

*Change of Control Agreements.* We have employment or change of control agreements with nine of our officers that entitle each of them to certain compensation and benefits in the event that Province terminates them within 180 days following the merger between Province and UNCB unless such termination is for cause, as defined in the change of control agreements or if such officer resigns his or her employment for good reason as defined in the change of control agreements. With the exception of Mr. Gainer, these agreements provide for a payment ranging from 12 months of salary to 18 months of salary for aggregate payments of approximately \$ plus benefits. In the case of Mr. Gainer, he would be entitled to receive \$1.45 million in compensation and benefits if he were terminated for other than cause within 180 days after the merger or if he resigns his employment for good reason.

*Province and DFSC Boards of Directors.* DFSC has agreed to add Mark D. Gainer and two other current members of our board of directors, who have not yet been identified, to the existing board of directors of DFSC, all of whom will remain directors of DFSC after the merger. DFSC has also agreed to appoint Mark D. Gainer and four other current members of the board of directors of UNCB, who have not yet been identified, to the board of directors of Province.

*Surrender of Our Stock Options.* Because all stock options to purchase shares of our common stock held by our directors and officers are exercisable at prices substantially in excess of the merger consideration, we have agreed in the merger agreement to use commercially reasonable efforts to cause each of our officers and directors to surrender such options for cancellation.

Other than as set forth above, none of our directors or executive officers has any direct or indirect material interest in the merger, except insofar as ownership of our common stock might be deemed such an interest.

**Regulatory Approvals Required for the Merger and the Bank Merger**

Completion of the merger and the merger of Province and UNCB are each subject to several federal and state bank regulatory agency filings and approvals. We cannot complete the merger unless DFSC and Province receive prior approval from the OTS and we have made certain filings with the Department and the SEC.

Neither DFSC nor we can predict whether or when DFSC will receive the required regulatory approvals. As of the date of this proxy statement/prospectus, DFSC has filed all applications, requests for waivers and notices with the OTS, the FRB, the Department and the SEC.

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*OTS.* The merger of UNCB with and into Province is subject to the prior approval of the OTS under the Bank Merger Act. DFSC and Province intend to file certain pro forma financial information the OTS has requested before DFSC and Province file their application for approval of the bank merger with the OTS. DFSC and Province will file their application for approval as soon as practicable after the OTS advises DFSC and Province the OTS is ready for the filing of the application. In reviewing applications under the Bank Merger Act, the OTS must consider, among other factors, the financial and managerial resources and future prospects of the existing and proposed institutions, the convenience and needs of the communities to be served and the effectiveness of both institutions in combating money laundering. In addition, the OTS may not approve a merger:

that will result in a monopoly or be in furtherance of any combination or conspiracy to monopolize or to attempt to monopolize the business of banking in any part of the United States;

if its effect in any section of the country may be substantially to lessen competition or tend to create a monopoly; or

if it would in any other manner be a restraint of trade,

unless the OTS finds that the public interest and the probable effect of the merger on meeting the convenience and needs of the communities to be served clearly outweigh the anticompetitive aspects of the merger.

Under the CRA, the OTS, in the case of Province, and the OCC, in the case of UNCB, must also take into account the record of performance of each of the merging banks in meeting the credit needs of the entire community, including low and moderate income neighborhoods served by each institution. As part of the merger review process, the federal supervisory agencies frequently receive comments and protests from community groups and others. Each of UNCB and Province received Satisfactory performance ratings in their most recent CRA evaluations.

The OTS is also authorized to, but generally does not, hold a public hearing or meeting in connection with an application under the Bank Merger Act. A decision by the OTS that such a hearing or meeting would be appropriate regarding any application could prolong the period during which the application is subject to review.

Mergers the OTS approves under the Bank Merger Act, with certain exceptions, may not be consummated until 30 days after such approval, during which time the U.S. Department of Justice may challenge such merger on antitrust grounds and may require the divestiture of certain assets and liabilities. With the approval of the OTS and the Department of Justice, the waiting period may be, and customarily is, reduced to no less than 15 days. We can provide no assurance that the Department of Justice will not challenge the merger or, if such a challenge is made, as to the result of such challenge.

*Pennsylvania Department of Banking.* We do not need the prior written approval of the Department for the proposed merger of UNCB, which is a national association, with and into Province, which is a federal savings bank, because the resulting institution will be a federal savings bank. UNCB must provide certain notice and documents to the Department regarding the proposed merger. Pursuant to the Pennsylvania Banking Code, UNCB must:

notify the Department of the proposed merger;

provide such evidence of the adoption of plan of merger as the Department may request;

notify the Department of any abandonment or disapproval of the plan of merger; and



file with the Department and with the Pennsylvania Department of State a certificate of the approval of the merger by the OTS.

*Other Regulatory Approvals.* Neither we nor DFSC are aware of any other regulatory approvals that are required for completion of the merger except as described above. Should there be any other required approvals, we and DFSC presently contemplate that we would promptly seek such approvals. We can provide no assurance, however, that we will obtain any other approvals, if required.

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We also cannot provide any assurance that the regulatory authorities described above will approve the merger or the bank merger, and if such mergers are approved, we cannot provide any assurance as to the date we will receive such approvals. The mergers cannot proceed in the absence of the receipt of all requisite regulatory approvals. See The Merger Agreement Conditions to Completion of the Merger and The Merger Agreement Amendment, Waiver and Termination of the Merger Agreement.

The approval of any application merely implies the satisfaction of regulatory criteria for approval, which do not include review of the merger from the standpoint of the adequacy of the merger consideration our shareholders will receive. Further, regulatory approvals do not constitute an endorsement or recommendation of the merger.

## **Public Trading Markets**

DGI Class A common stock trades on the NASDAQ Global Select Market under the symbol DGICA. Our common stock trades on the OTCBB under the symbol UNNF.OB. Upon completion of the merger, our common stock will no longer trade on the OTCBB and DFSC will deregister our common stock under the 1934 Act. DGI has agreed to list the DGI Class A common stock our shareholders will receive pursuant to the merger agreement on the NASDAQ Global Select Market.

The shares of DGI Class A common stock DFSC will deliver as merger consideration in connection with the merger will be freely transferable under the Securities Act of 1933, as amended, or the 1933 Act, except for shares issued to any of our shareholders that may be deemed to be an affiliate of DGI at or after the effective time of the merger, as discussed in Resales of DGI Class A Common Stock beginning on page 94.

As reported on the NASDAQ Global Select Market, the closing price per share of DGI Class A common stock on April 19, 2010 was \$14.68. The closing price per share of our common stock as reported on the OTCBB on April 19, 2010 was \$6.00. Based on the DGI closing price per share on the NASDAQ Global Select Market and the exchange ratio, the pro forma equivalent per share value of our common stock was \$8.18 as of that date. On , 2010, the last practicable day before the mailing of this proxy statement/prospectus, the closing price per share of DGI Class A common stock on the NASDAQ Global Select Market was \$ , and the closing price per share of our common stock on the OTCBB was \$ resulting in a pro forma equivalent per share value of our common stock of \$ as of that date.

## **Dividends**

DGI paid cash dividends on its Class A common stock totaling \$0.45 per share for 2009. Based on the share exchange ratio and DGI's current annual dividend rate of \$0.46 per Class A share, holders of our common stock would experience an anticipated dividend at an annual rate of \$0.098 per UNNF share based on the exchange ratio, compared to no current dividend on our common stock.

DGI shareholders are entitled to receive cash dividends when and if declared by the DGI board of directors out of funds legally available for dividends. The DGI board of directors quarterly considers the payment of dividends, taking into account DGI's financial condition and level of net income, DGI's future prospects, economic conditions, industry practices and other factors, including applicable banking laws and regulations.

The primary source of DGI's funds for cash dividends to its shareholders is dividends DGI receives from its insurance subsidiaries. Province and DGI's insurance subsidiaries are subject to various regulatory policies and requirements relating to the payment of dividends to DGI, including requirements to maintain capital above regulatory minimums. The appropriate federal regulatory authority is authorized to determine under certain circumstances relating to the financial condition of a bank or bank holding company that the payment of dividends would be an unsafe or unsound

practice and to prohibit the payment of any dividend. In addition, the ability of DGI and the ability of Province and DGI's insurance subsidiaries to pay dividends may be affected by the various minimum capital requirements and the capital and non-capital standards established under the Federal Deposit Insurance Corporation Improvement Act.

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**Appraisal Rights of Dissenting Shareholders**

Dissenters' rights are statutory rights that enable shareholders to dissent from an extraordinary corporate transaction, such as our merger with DFSC, and to demand that the corporation pay the fair value for their shares as determined by a court in a judicial proceeding instead of receiving the consideration offered to shareholders in connection with the extraordinary corporate transaction.

A holder of shares of our common stock is entitled to exercise these rights under Subchapter D of the PBCL, which we refer to as Subchapter D in this proxy statement/prospectus, by objecting to the merger and making a written demand that we pay in cash the fair value of the shares the shareholder holds as determined in accordance with Subchapter D. The following summary is a materially complete summary of the provisions of Subchapter D, but does not purport to be a complete statement of the provisions of Subchapter D. We qualify the summary in its entirety by reference to the provisions of Subchapter D which we have included as Appendix C to this proxy statement/prospectus.

Subchapter D defines the fair value of our shares of common stock as the fair value of the shares immediately before the effective time of the merger, taking into account all relevant factors, but excluding any appreciation or depreciation in anticipation of the merger. You should recognize that the fair value of your shares could be more, the same or less than the per share merger consideration of that you would receive under the terms of the merger agreement of \$5.05 in cash and 0.2134 share of DGI Class A common stock if you do not exercise your dissenters' rights with respect to your UNNF shares. Opinions of investment banking firms as to the fairness from a financial point of view of the merger consideration you will receive upon the closing of the merger, such as the opinion delivered by Sandler O'Neill, are not necessarily determinative of fair value under Subchapter D.

Except as otherwise provided below, only a record holder of shares of our common stock may assert dissenters' rights with respect to the UNNF shares registered in such holder's name. A record holder, such as a broker or a depository nominee, who holds our shares as a nominee for others, may exercise dissenters' rights with respect to all, but not less than all, of the UNNF shares held for one or more beneficial owners, while not exercising such rights for other beneficial owners. The demand for payment described below must show the name and address of the person or persons on whose behalf the dissenters' rights are being exercised. A beneficial owner who is not a record holder who wishes to exercise dissenters' rights may do so only if the shareholder submits a written consent of the record holder with such shareholder's demand for payment. Accordingly, if you are a beneficial owner of shares, we advise you to consult promptly with your record holder as to the timely exercise of dissenters' rights. A beneficial owner may not assert dissenters' rights with respect to some, but less than all, shares of the same class or series such shareholder owns, whether or not the shares such shareholder owns are registered in such shareholder's name.

To exercise dissenters' rights and obtain payment of the fair value of your shares, you must satisfy all of the following conditions:

You must notify us in writing before the date of our special meeting of your intention to demand that you be paid the fair value of your UNNF shares if we complete the merger. Neither a no vote by proxy on the merger proposal nor a no vote by ballot at our special meeting will constitute the required notice;

You must make no change in the beneficial ownership of your UNNF shares from the date you file a notice of intention to demand payment continuously through the effective time of the merger; and

You must refrain from voting your shares in favor of the merger proposal. Neither an abstention from voting with respect to, nor a failure to vote in person or by proxy against approval of, the merger proposal will constitute a waiver of your dissenters' rights. However, a signed and dated proxy that is returned without any instruction as to how the proxy should be voted will be voted **FOR** the merger proposal and will be deemed a waiver of your dissenters' rights.

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A notice of intention to demand payment must clearly state that you intend to demand to be paid the fair value of your shares if we complete the merger and must file the notice with us. If you exercise dissenters' rights, you will retain all of your other rights as a shareholder until we complete the merger.

If our shareholders adopt the merger agreement at our special meeting, we will mail to each shareholder who complied with the procedures listed above a notice stating where and when you must send a demand for payment of the fair value of your shares, and where and when you must deposit your UNNF stock certificates to obtain payment of fair value. We will send a demand-for-payment form with our notice and will include a request that you certify the date on which you, or any person exercising dissenters' rights on your behalf, acquired beneficial ownership of your shares. You will have 30 days from the date on which we mail our notice to you to send in your demand-for-payment form and to deposit your stock certificates. If you fail to send in your demand-for-payment form or your stock certificates on a timely basis, you will lose your dissenters' rights under Subchapter D, but you will retain all other rights as an UNNF shareholder until we complete the merger.

If we have not completed the merger within 60 days after the deadline set for demanding payment and the deposit of UNNF stock certificates, we will return any UNNF stock certificates that have been deposited. Once we return any deposited stock certificates, we may thereafter send a new notice to demand payment, which will have the same effect as the original notice.

Promptly after completion of the merger, or upon our timely receipt of a demand-for-payment form if we have already completed the merger, we will either remit to you, if you have submitted a demand-for-payment form and deposited your stock certificates, the amount we estimate to be the fair value of your shares, or give written notice to you that we will not make a remittance. We will include with the remittance or notice the following documents:

our closing balance sheet and statement of income for our fiscal year ending not more than 16 months before the date of our remittance or our notice, together with our latest available interim financial statements;

a statement of our estimate of the fair value of your shares; and

a notice of your right to demand payment or supplemental payment, as the case may be, accompanied by a copy of Subchapter D.

If we do not remit the amount of our estimate of the fair value of your shares, we will return all stock certificates you deposited. We may make a notation on your stock certificates that you made a demand for payment. If you transfer stock certificates on which such a notation has been made, the transferee of your shares will not acquire, by virtue of the transfer, any rights in such shares other than those rights you originally had before you made a demand for payment.

If we give notice of our estimate of the fair value of your shares without remitting payment, or if we remit payment for the fair value of your shares and you believe that the amount stated or remitted is less than the fair value of your shares, you may elect to send us your estimate of the fair value of your shares, which we will deem a demand for payment of the amount of the deficiency. If you do not file your own estimate within 30 days after we mail of our remittance or notice, you will be entitled to no more than the amount stated in our notice or the amount we remitted to you.

If any demand for payment has not been settled by the date that is 60 days after the latest to occur of:

completion of the merger;

timely receipt of any demand for payment; or

timely receipt of any estimate by a shareholder of the fair value of such shareholder's UNNF shares,

we may file an application for relief in court requesting that the court determine the fair value of the shares. While we do not anticipate filing an application for the court to determine the fair value of the shares, if we were to elect to file such an application, the court's determination of the fair market value of the shares may

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be higher or lower than the merger consideration that you would have received under the terms of the merger agreement.

Any UNNF shareholder who exercises dissenters' rights, wherever residing, whose demand for payment has not been settled, will be made a party to any such court proceedings and a copy of the application for relief will be served on each such UNNF shareholder. If such shareholder is a nonresident of Pennsylvania, the application will be served in the manner provided or prescribed by or under applicable provisions of Pennsylvania law relating to bases of jurisdiction and interstate and international procedure. The jurisdiction of the Pennsylvania court will be plenary and exclusive. The court may appoint an appraiser to receive evidence and to recommend a decision on the issue of fair value. The appraiser will have the power and authority that is specified in the order of appointment or in any amendment of the order. Each shareholder who becomes a party will be entitled to recover the amount by which the fair value of each shareholder's shares is found to exceed the amount, if any, previously remitted, plus interest from the effective date of the merger until the date of payment. Interest will be at a rate that is fair and equitable under all of the circumstances, taking into account all relevant factors.

If we do not file an application for relief, any shareholder who made a demand for payment and who has not already settled such shareholder's claim against us may file an application for relief in our name at any time within 30 days after the expiration of the 60-day period referred to above. If a shareholder does not file an application within said 30-day period, such shareholder will be paid our estimate of the fair value of such shareholder's shares and no more, and may bring an action to recover any amount not previously remitted.

In general, the costs and expenses of any valuation proceeding, including the reasonable compensation and expenses of any appraiser appointed by the court, will be determined by the court and assessed against us. However, any part of the cost and expenses may be apportioned and assessed as the court deems appropriate against all or some of the shareholders who are parties to the proceeding and whose actions in demanding supplemental payment the court finds to be dilatory, obdurate, arbitrary, vexatious or in bad faith. If the court finds that the services of counsel for any shareholder were of substantial benefit to other shareholders similarly situated and should not be assessed against us, it may award to those counsel reasonable fees to be paid out of the amount awarded to the shareholders who received the benefit.

From and after the effective time of the merger, shareholders who exercise their dissenters' rights will not be entitled to payment of any dividends or other distributions DGI declares on its Class A common stock.

We advise any shareholder considering the exercise of dissenters' rights under Subchapter D to consult with legal counsel. Any shareholder who fails to follow with particularity all of the steps required to preserve and perfect dissenters' rights under the PBCL loses the right to seek appraisal under Subchapter D, in which event, upon the surrender of certificates representing shares of our common stock by such UNNF shareholder, such shareholder will receive the per share merger consideration set forth in the merger agreement without interest.

## **THE MERGER AGREEMENT**

*The following section describes certain aspects of the merger, including the material provisions of the merger agreement. The following description of the merger agreement is subject to, and qualified in its entirety by reference to, the merger agreement, which we have included as Appendix A to this proxy statement/prospectus and which we incorporate by reference in this proxy statement/prospectus. We urge you to read the merger agreement carefully and in its entirety.*

## **Terms of the Merger**



The merger agreement provides for the merger of DAI with and into UNNF followed immediately thereafter by the merger of UNNF with and into DFSC. DFSC will be the surviving corporation in the UNNF-DFSC merger and will continue its corporate existence as a Delaware corporation, and our separate corporate existence will cease. The merger will cancel each share of our common stock issued and outstanding immediately prior to the completion of the merger, except for shares of our common stock held by DMIC,

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shares as to which dissenters' rights are perfected and shares held by us as treasury shares, and convert each share into the right to receive 0.2134 share of DGI Class A common stock and \$5.05 in cash.

Immediately after the completion of the merger, UNCB will merge into Province, which will continue as a federal savings bank.

## **Stock Options**

Because all of the stock options to purchase shares of our common stock are exercisable at prices substantially in excess of merger consideration, we have agreed in the merger agreement to use commercially reasonable efforts to cause each holder of an option to purchase UNNF common stock to surrender their options for cancellation.

## **Closing and Effective Time of the Merger**

The parties will complete the merger only if all of the following conditions are satisfied:

our shareholders adopt the merger agreement and the merger by the necessary vote;

DFSC and we obtain all required governmental and regulatory consents and approvals; and

all other conditions to the merger set forth in this proxy statement/prospectus and the merger agreement are either satisfied or waived.

The UNNF-DFSC merger will become effective when we file articles of merger with the Secretary of State of the State of Delaware and with the Secretary of the Commonwealth of Pennsylvania. In the merger agreement, DFSC and we have agreed to cause the completion of the merger to occur no later than the fifth business day following the satisfaction or waiver of the last of the conditions specified in the merger agreement or on another mutually agreed date. We currently anticipate that the effective time of the merger will occur in the third quarter of 2010, but neither DFSC nor we can guarantee when or if we complete the merger. DFSC's certificate of incorporation and DFSC's by-laws as in effect immediately prior to the effective time will be DFSC's certificate of incorporation and DFSC's by-laws upon completion of the merger.

## **Representations, Warranties, Covenants and Agreements**

The merger agreement contains generally reciprocal customary representations and warranties of the Donegal parties and us relating to our respective businesses. We will not deem any representation or warranty untrue or incorrect as a consequence of the existence or absence of any fact, event or circumstance unless that fact, event or circumstance has had or is reasonably likely to have a material adverse effect on the party making the representation or warranty, disregarding any materiality or material adverse effect qualifications in any representations or warranties. The representations and warranties in the merger agreement will not survive the effective time of the merger.

In the merger agreement, the Donegal parties and we have made representations and warranties to each other regarding, among other things:

corporate matters, including due organization, qualification and authority of both DFSC and us and each of our respective subsidiaries;

capitalization;

authority relative to execution and delivery of the merger agreement and the absence of conflicts with, or violations of, such party's organizational documents or other obligations as a result of the merger;

required governmental filings and consents for approval of the merger and the absence of any defaults;

the timely filing of reports with governmental entities, and the absence of investigations by or disputes with regulatory agencies;

financial statements;

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brokers' fees payable in connection with the merger;  
the absence of certain material changes or events;  
legal proceedings;  
tax matters;  
employee benefit plans;  
compliance with applicable laws;  
material contracts and the absence of defaults thereunder;  
the absence of agreements with regulatory agencies;  
undisclosed liabilities;  
environmental liabilities;  
loans and nonperforming and classified assets;  
fiduciary accounts; and  
allowances for loan losses.

In addition, we have made representations and warranties regarding:

the receipt of an opinion from our independent financial advisor;  
real property;  
insurance;  
the inapplicability of state anti-takeover laws;  
intellectual property; and  
investment securities.

In addition, DGI made representations and warranties regarding its filings with the SEC.

We have agreed to certain customary covenants that place restrictions on us and our subsidiaries until the effective time of the merger. In general, we have agreed to:

conduct our business and that of our subsidiaries in the ordinary course in all material respects; and

use our reasonable best efforts to maintain and preserve intact our respective business organizations, employees and advantageous business relationships.

We have further agreed in the merger agreement that until the completion of the merger, except with DFSC's prior written consent, or the merger agreement otherwise permits, we will not, among other things, undertake the following actions:

declare, set aside or pay any dividends or make any other distributions on any shares of our capital stock, or split, combine, reclassify, redeem, purchase or otherwise acquire any shares of our common stock or any rights, warrants or options to acquire such shares;

grant any stock options, restricted stock units or other equity-based awards with respect to shares of our common stock under any of our stock plans or grant any individual, corporation or other entity any right to acquire shares of our common stock or issue any additional shares of our common stock or other securities, other than the issuance of our common stock upon the exercise of our outstanding stock options;

amend our articles of incorporation or by-laws;

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acquire or agree to acquire by merging or consolidating with, or by purchasing any assets or equity securities of, any business or other person or entity or otherwise acquire or agree to acquire any assets, except inventory or other similar assets in the ordinary course of business consistent with past practice or open, acquire, sell or close any of our branches;

sell, lease, license, mortgage or otherwise encumber any of our properties or assets other than securitizations and other transactions in the ordinary course of business consistent with past practice;

except for borrowings having a maturity of not more than 30 days under existing credit facilities, or renewals or extensions thereof or replacements therefor that do not increase the aggregate available borrowing amount and that do not provide for termination fees or penalties or prohibit pre-payment or provide for pre-payment penalties or contain less advantageous financial terms than existing credit facilities that are incurred in the ordinary course of business consistent with past practice or for borrowings under outstanding credit facilities in additional amounts not to exceed \$1.5 million, incur any indebtedness for borrowed money, issue any debt securities or assume, guarantee, endorse or otherwise become responsible for the obligation of any person, or, other than in the ordinary course of business consistent with past practice, make any investment in any person other than our subsidiaries;

change in any material respect our accounting methods, principles or practices in effect as of the date of the merger agreement, except as required by changes in generally accepted accounting principles or regulatory accounting principles;

change in any material respect our underwriting, operating, investment, risk management or other similar policies except as required by applicable law or regulatory policies;

make, change or revoke any material tax election, file any material amended tax return, enter into any closing agreement with respect to a material amount of taxes, settle any material tax claim or surrender any right to a refund of a material amount of taxes;

other than in the ordinary course of business consistent with past practice, terminate or waive any material provision of any material contract or enter into or renew any agreement containing restrictions on our business;

incur any capital expenditure in excess of \$100,000 individually or \$250,000 in the aggregate;

except as required by agreements in effect on the date of the merger agreement, alter in any material respect any material interest in any business entity in which we had any ownership interest on the date of the merger agreement, other than by foreclosure or debt restructuring in the ordinary course of business;

agree or consent to any material agreement or material modifications of an existing agreement with any regulatory authority or governmental entity;

pay, discharge or settle any action, proceeding, order or investigation to which we are a party other than a monetary settlement that involves the payment of not more than \$100,000 individually or \$500,000 in the aggregate;

issue any broadly distributed communication of a general nature to our employees or customers without the prior approval of DFSC, except for communications in the ordinary course of business that do not relate to the merger or the transactions the merger agreement contemplates;

take any action or knowingly fail to take any action that would reasonably be expected to prevent the merger from qualifying as a reorganization for U.S. federal income tax purposes;

take any action that would materially impede or delay the ability of DFSC and us to obtain any regulatory approvals required for the transactions the merger agreement contemplates;

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take any action that is intended or is reasonably likely to result in:

any of our representations or warranties in the merger agreement being or becoming untrue in any material respect;

any of the conditions precedent to DFSC's obligations under the merger agreement not being satisfied; or

a violation of any provision of the merger agreement;

make, renew or otherwise modify any loan, loan commitment or other extension of credit to any person or entity without the approval of DFSC if the loan is classified substandard-non-accrual, doubtful or loss on our books or, if the loan is classified as substandard-non-accrual or special mention and is in an amount in excess of \$1,500,000 without DFSC's approval, or make, renew or modify any of the following loans if DFSC shall object to such loan within two business days after receiving notice thereof from UNCB:

an unsecured loan rated pass to any person if immediately after making such loan the person would be indebted to UNCB in an aggregate amount in excess of \$500,000 on an unsecured basis;

a secured loan rated pass to any person if immediately after making such loan the person would be indebted to UNCB in an aggregate amount in excess of \$500,000 except for a loan secured by a first mortgage on owner-occupied real estate;

a loan rated pass secured by an owner-occupied 1-4 single-family residence with a principal balance in excess of \$500,000; or

any loan that does not conform with UNCB's credit policy manual;

enter into, amend or renew any employment, consulting, severance or similar agreements with any of our directors, officers or employees or grant any wage or salary increase or increase any employee benefit, including discretionary or other incentive or bonus payments, except in accordance with the terms of our benefit plans, or accelerate the vesting of any unvested stock options, except for:

normal increases in the ordinary course of business consistent with past practice that, in the aggregate, do not exceed 3.5%, or, in the case of any one individual, 5%;

changes required by applicable law;

payments we disclosed to DFSC in a disclosure schedule to the merger agreement; and

severance payments pursuant to severance agreements or employment agreements we disclosed to DFSC in a disclosure schedule to the merger agreement;

hire or promote any officer, except to satisfy existing contractual obligations, to fill vacancies on the date of the merger agreement as disclosed by us to DFSC in a schedule to the merger agreement or to fill vacancies arising after the date of the merger agreement at a comparable level of compensation with officers whose employment is terminable at will, provided that the total annual compensation for any one such officers shall not exceed \$100,000;



enter into any futures contract, option, interest rate cap, interest rate floor, interest rate exchange agreement or other agreement or take any other actions for the purpose of hedging the exposure of its interest-earning assets and interest-bearing liabilities to changes in market rates of interest;

except for the execution of the merger agreement and actions taken in accordance with the merger agreement and the performance of the merger agreement, take any action that would give rise to a right of payment to any individual under any employment agreement, severance agreement or change of control agreement;

make any change in policies in existence on the date of the merger agreement with regard to the extension of credit or the establishment of reserves with respect to possible loan losses or the charge-

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off of losses incurred on loans, investments, asset/liability management, deposit pricing or gathering or other material banking policies except as required by changes in applicable laws or regulations or as directed by a bank regulatory agency; or

agree to take, make any commitment to take or adopt any resolutions of our board of directors in support of any of the foregoing prohibited actions.

The Donegal parties have agreed that until completion of the merger, except with our prior written consent or as otherwise permitted by the merger agreement, they will not, among other things, undertake the following actions:

take any action that is intended, or is reasonably likely, to result in:

any of the Donegal parties' respective representations or warranties in the merger agreement being or becoming untrue in any material respect;

any of the conditions precedent to our obligations under the merger agreement not being satisfied; or

a violation of the merger agreement;

take any action that would materially impede or delay the ability of the Donegal parties or us in obtaining any necessary governmental or regulatory approvals required for the transactions the merger agreement contemplates; or

agree to take or make any commitment to take or allow the Donegal parties' respective board of directors to adopt any resolutions in support of any of the foregoing prohibited actions.

The merger agreement also contains mutual covenants relating to the use of DFSC's and our commercially reasonable efforts to complete the merger, the preparation of this proxy statement/prospectus, the preparation of the required regulatory applications and notices, the holding of our special meeting of shareholders, access to information of the other party and public announcements with respect to the transactions the merger agreement contemplates.

**Declaration and Payment of Dividends**

We have agreed that, until we complete the merger, we will not pay or make any dividends or distributions on our common stock unless we have received any required regulatory approval to do so. We suspended the payment of dividends on our common stock in 2008.

**Agreement Not to Solicit Other Offers**

We have agreed that we and our officers, directors, employees, agents and representatives will not, directly or indirectly:

initiate, solicit, encourage or take any action to facilitate any inquiries or proposals for any Acquisition Proposal, as defined below; or

enter into or participate in any discussions or negotiations with, furnish any information to or cooperate with, any person or entity seeking to make, or who has made, an Acquisition Proposal; or

approve, recommend or enter into any letter of intent, agreement or other commitment regarding any Acquisition Proposal.

However, prior to the effective time of the merger, we may consider and participate in discussions and negotiations with respect to a Superior Proposal, as defined below, if:

we have first entered into a confidentiality agreement with the party proposing the Superior Proposal with confidentiality terms no less favorable to us than those contained in our confidentiality agreement with DMIC; and

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our board of directors concludes in good faith, after consultation with its outside legal counsel, that failure to take these actions could reasonably be expected to cause our board of directors to violate its fiduciary duties under applicable law.

We have also agreed, at least 72 hours prior to providing any information to any person or entering into any discussions or negotiations with any person, to notify DFSC in writing of the name of such person and the material terms and conditions of any such Superior Proposal. The merger agreement permits our board of directors to withdraw or qualify its recommendation of the merger with DFSC if our board of directors concludes in good faith, after consultation with our outside legal counsel and our financial advisors, that failure to take such actions could reasonably be expected to breach its fiduciary duties under applicable law.

We have agreed:

to notify DFSC promptly, and in any event within 24 hours, after we receive any Acquisition Proposal, or any information related to an Acquisition Proposal, which notification shall describe the Acquisition Proposal and the third party making it; and

to cease any discussions or negotiations existing on the date of the merger agreement with any persons with respect to any Acquisition Proposal.

As used in the merger agreement, an Acquisition Proposal means any inquiry, proposal, offer, regulatory filing or disclosure of an intention relating to any:

direct or indirect acquisition of a substantial (i.e., 20% or more) portion of the net revenues, net income or net assets of us and our subsidiaries taken as a whole;

direct or indirect acquisition of 10% or more of our common stock after April 19, 2010 by a person who on April 19, 2010 did not own 10% or more of our common stock;

direct or indirect acquisition of 5% or more of our common stock after April 19, 2010 by a person who owned 10% or more of our common stock on April 19, 2010;

tender offer or exchange offer that if consummated would result in any person beneficially owning 10% or more of our common stock; or

merger, consolidation, business combination, recapitalization, liquidation or dissolution involving us, other than our proposed merger with DFSC.

As used in the merger agreement, Superior Proposal means any bona fide, unsolicited written Acquisition Proposal made by a third party to acquire more than 50% of the voting power of our then outstanding shares of common stock or all or substantially all of our consolidated assets for consideration consisting of cash and/or securities, that our board of directors, in good faith, concludes, after consultation with our financial advisors and our outside legal counsel, taking into account, among other things, all legal, financial, regulatory and other aspects of the proposal and the person making the proposal, including any termination fees, expense reimbursement provisions and conditions to consummation:

is on terms that in the good faith judgment of our board of directors are more favorable to us than the terms of the proposed merger with DFSC;

for which there is either no financing contingency or the third party has received a highly confident letter with respect to all necessary funding from an investment banking firm of national standing; and

is reasonably capable of being completed.

**Conditions to Completion of the Merger**

The respective obligations of DMIC and us to complete the merger are subject to the fulfillment or waiver of certain conditions, including:

the adoption of the merger agreement and the approval of the merger by the affirmative vote of the holders of 80% of our outstanding shares of common stock as well as the approval of the listing on the

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NASDAQ Global Select Market of the DGI Class A common stock to be used as a portion of the merger consideration;

the receipt and effectiveness of all governmental and other approvals, registrations and consents and the expiration of all related waiting periods required to complete the merger and, in the case of DMIC, none of the regulatory approvals shall have resulted in a materially burdensome regulatory condition;

the absence of any law, statute, regulation, judgment, decree, injunction or other order in effect by any court or other governmental entity that prevents, prohibits or makes illegal completion of the transactions contemplated by the merger agreement;

the registration statement with respect to the DGI Class A common stock to be used as part of the merger consideration in the merger shall have become effective under the 1933 Act and no stop order or proceedings for that purpose will have been initiated or threatened by the SEC;

we do not have delinquent loans in excess of \$37.5 million as of the end of the month preceding the month in which the merger closing is scheduled to occur;

We shall have considered to the extent requested by DFSC and at its expense, any Regulation Z/Real Estate Settlement Program and delivered a report with respect thereto to DFSC; and

the truth and correctness of the representations and warranties of DFSC and us in the merger agreement and the performance by each of DFSC and us in all material respects of our respective obligations under the merger agreement and the receipt by each of DFSC and us of certificates from the other to that effect.

Neither DFSC nor we can provide assurance as to when or if all of the conditions to the merger can or will be satisfied or waived by the appropriate party. As of the date of this proxy statement/prospectus, neither DFSC nor we have any reason to believe that any of these conditions will not be satisfied.

**Amendment, Waiver and Termination of the Merger Agreement**

Subject to applicable law, the Donegal parties and we may amend the merger agreement by written agreement authorized by our respective boards of directors. However, after approval of the merger proposal by our shareholders, there may not be, without further approval of our shareholders, any amendment of the merger agreement that requires such further approval under applicable law. Either the Donegal parties or we may, subject to applicable law, may extend the time for the performance of any obligations or acts of the other party or waive any inaccuracies in the representations and warranties of the other party or compliance by the other party with any of the other agreements or conditions contained in the merger agreement. The merger agreement may be terminated at any time prior to closing by mutual consent and by either party in the following circumstances:

if any of the required regulatory approvals for the merger are denied and the denial is final and nonappealable unless the denial is due to the terminating party's breach of its covenants in the merger agreement;

if the merger has not been completed by December 31, 2010, unless the failure to complete the merger by that date is due to the terminating party's actions;

provided the terminating party is not then in material breach, if there is a breach of the merger agreement by the other party that would cause the failure of the closing conditions described above, unless the breach is capable of being, and is, cured within 30 days of notice of the breach; or

if the holders of 80% of our outstanding common stock do not adopt the merger agreement, provided that we are not in material breach of our covenant to hold our special meeting and our board of directors is not in breach of its covenant to recommend such approval.

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DFSC may terminate the merger agreement at any time prior to the effective date in the following circumstances:

if we have breached in any material respect our obligations with respect to Acquisition Proposals and Superior Proposals as described on pages 105 through 106;

if we have failed to have our board of directors recommend that our shareholders adopt the merger agreement, or if our board of directors has withdrawn or modified its recommendation in a manner adverse to DFSC;

if our board of directors shall have recommended the approval of an Acquisition Proposal; or

if we have breached in any material respect our obligation to hold our special meeting.

The merger agreement also provides us with certain rights to terminate the merger agreement in connection with a Superior Proposal.

**Expenses and Fees**

In general, each of DFSC and we will be responsible for all expenses each of us incurs in connection with the negotiation and completion of the transactions the merger agreement contemplates. However, DFSC and we will share equally the costs and expenses of printing and mailing this proxy statement/prospectus, and all filing and other fees paid to the SEC in connection with the merger.

**Litigation Relating to the Merger**

As of June 15, 2010, we became aware that a complaint had been filed in the Court of Common Pleas of Lancaster County, Pennsylvania against us, each of our directors and the Donegal parties. The complaint includes allegations that our board of directors violated their fiduciary duties to our shareholders to obtain the highest price by agreeing to certain provisions in the merger agreement regarding competing offers.

The allegations in the complaint seek equitable relief in the form of an injunction enjoining the consummation of the merger or, if the merger is consummated, the rescission of the merger for unspecified monetary damages, in addition to costs and disbursements and legal fees. Both DGI and UNNF believe the allegations in the complaint are factually incorrect and do not properly state a cause of action under Pennsylvania law. DGI and UNNF intend to defend the complaint vigorously and believe they have meritorious defenses.

**Effect of Termination; Termination Fee; Expenses**

If the merger agreement is terminated, it will become void, and there will be no liability on the part of any Donegal party or us, except that:

termination will not relieve a breaching party from liability for its willful breach giving rise to the termination; and

the confidentiality agreement between DMIC and UNNF will survive termination.

The merger agreement obligates us to pay DFSC a break-up fee of \$800,000 in the following circumstances:



if DFSC terminates the merger agreement because we have breached our obligation not to initiate, solicit or encourage any third parties to make an Acquisition Proposal or otherwise breached our obligations with respect to Acquisition Proposals or Superior Proposals in a manner adverse to DFSC, our board of directors fails to make or withdraws its recommendation of the merger proposal or we fail to hold our special meeting;

if we terminate the merger agreement and accept an Acquisition Proposal that is a Superior Proposal and, after giving DFSC an opportunity to adjust the terms of the merger agreement such that the

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Acquisition Proposal no longer remains a Superior Proposal, the Acquisition Proposal remains a Superior Proposal;

the termination of the merger agreement following the commencement of a tender offer or exchange offer for 25% or more of our common stock and we have not sent to our shareholders, within 10 days after the commencement of such offer, a statement that our board of directors recommends the rejection of such tender offer or exchange offer; or

the occurrence of any of the following events within 18 months after termination of the merger agreement, provided that a third party makes a proposal to acquire us after April 19, 2010 and does not withdraw it prior to termination of the merger agreement:

enter into an agreement to merge with or be acquired by that third party;

that third party acquires substantially all of our assets; or

that third party acquires more than 50% of our common stock.

The Donegal parties and we have also agreed that if either the Donegal parties or we breach our respective representations, warranties, covenants or agreements in the merger agreement, which breach could reasonably be expected to result in a material adverse effect and which breach cannot be or is not cured, the breaching party, assuming the other party is not also in material breach of its obligations under the merger agreement, will pay the out-of-pocket expenses, including fees and expenses of legal counsel, financial advisors and accountants, of the non-breaching party, up to a maximum of \$500,000. If we are liable for the payment of the break-up fee, we will not be liable for the payment of the Donegal parties' out-of-pocket expenses.

## **Employee Benefit Plans**

The merger agreement provides that our employee benefit plans other than those plans that provide for the purchase of our common stock will continue in effect without material change after the merger. DGI intends to offer to our employees the existing DGI plans that provide its employees with rights to purchase DGI Class A common stock.

## **ACCOUNTING TREATMENT**

DFSC will account for the merger as a purchase, as that term is used under GAAP, for accounting and financial reporting purposes. Under acquisition accounting, DFSC will record our assets, including our identifiable intangible assets and liabilities, including executory contracts and other commitments, as of the effective time of the merger at their respective fair values and add such items to its balance sheet. DFSC will record any excess of the purchase price over the fair values as goodwill. Financial statements of DFSC issued after the merger will reflect these fair values and our results of operations from the date of acquisition.

## **MATERIAL U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER**

The following discussion summarizes the material U.S. federal income tax consequences of the merger that are generally applicable to holders of our shares. This discussion is based on the Code, judicial decisions and administrative regulations and interpretations in effect as of the date of this proxy statement/prospectus, all of which are subject to change, possibly with retroactive effect. Accordingly, the U.S. federal income tax consequences of the merger to the holders of our shares could differ from those described below.

The discussion assumes that you hold your shares as a capital asset. This discussion does not address all aspects of U.S. federal income taxation that may be relevant to holders of our shares in light of their particular circumstances, nor does it address the U.S. federal income tax consequences to shareholders that are subject to special rules under U.S. federal income tax law, including:

dealers in securities or foreign currencies;

tax-exempt organizations;

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foreign persons;

financial institutions or insurance companies;

shareholders who have a functional currency other than the U.S. dollar;

shareholders who own their shares indirectly through partnerships, trusts, or other entities that may be subject to special treatment;

shareholders all or part of whose DGI Class A common stock received in the merger will be subject to forfeiture provisions;

shareholders who acquired their shares in connection with stock options or stock purchase plans or other compensatory transactions; and

shareholders who hold their shares as a hedge or as part of a straddle, constructive sale, conversion transaction, or other risk management transaction.

In addition, this discussion does not address the U.S. federal income tax consequences of any transaction other than those affecting our shareholders resulting from the merger. In addition, this discussion does not address any tax consequences of the merger under foreign, state or local law or U.S. federal estate and gift tax laws. We have not and will not request or obtain any ruling from the Internal Revenue Service regarding any matter relating to the merger. We cannot provide any assurance that the Internal Revenue Service will not assert, or that a court will not sustain, a position contrary to any aspect of this discussion. We urge holders to consult their own tax advisors as to the U.S. federal income tax consequences of the merger, as well as the effects of state, local and foreign tax laws in light of their own situations.

We expect that the merger will be a fully taxable transaction for United States federal income tax purposes. As a result, a UNNF shareholder will generally recognize gain or loss as a result of the merger in an amount equal to the difference between the amount of cash plus the fair market value, determined at the effective time of the merger, of the DGI Class A common stock such shareholder receives and such shareholder's tax basis in UNNF common stock surrendered in the merger. A shareholder will determine gain or loss separately for each block of shares (that is, shares acquired at the same price per share in a single transaction) surrendered for cash and DGI Class A common stock pursuant to the merger. Such gain or loss will be a long-term capital gain or loss if the holder's holding period is greater than one year as of the effective time of the merger. The maximum federal income tax rate on net long-term capital gain recognized by individuals is 15% under current law. The maximum federal income tax rate on net long-term capital gain recognized by a corporation is 35%. Capital losses are subject to limitations on deductibility for both corporations and individuals.

The tax basis of DGI Class A common stock received in the merger will equal the fair market value of the stock at the effective time of the merger, and the holder's holding period for the DGI Class A common stock received will begin on the day after the date of the effective time of the merger. Gain or loss realized upon any subsequent sale or other taxable disposition of the DGI Class A common stock received in the merger will equal the difference between the holder's tax basis in the DGI Class A common stock at the time of that subsequent disposition and the amount realized on the disposition.

Under Pennsylvania law, UNNF shareholders have the right to dissent from the merger and receive payment in cash for the fair value of their UNNF common stock. If a UNNF shareholder receives cash pursuant to the exercise of such

appraisal rights, such shareholder generally will recognize gain or loss in an amount equal to the difference between the cash received and such holder's tax basis in its UNNF common stock. Such gain or loss will be a long-term capital gain or loss if the shareholder's holding period is greater than one year as of the effective time of the merger. UNNF shareholders who exercise appraisal rights are urged to consult their own tax advisors.

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Non-corporate holders of our shares may be subject to information reporting and backup withholding at a rate of 28% on any cash payments received. Generally, backup withholding will not apply, however, if a holder of our shares:

furnishes a correct taxpayer identification number and certifies that such holder is not subject to backup withholding on the substitute Form W-9 or successor form included in the letter of transmittal you will receive; or

is otherwise exempt from backup withholding.

Any amounts withheld under the backup withholding rules will generally be allowed as a refund or credit against a holder's U.S. federal income tax liability, provided the required information is furnished to the Internal Revenue Service.

THE PRECEDING DISCUSSION IS INTENDED ONLY AS A SUMMARY OF CERTAIN U.S. FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER AND DOES NOT PURPORT TO BE A COMPLETE ANALYSIS OR DISCUSSION OF ALL OF THE MERGER'S POTENTIAL TAX EFFECTS. WE URGE UNNF SHAREHOLDERS TO CONSULT THEIR OWN TAX ADVISORS AS TO THE SPECIFIC TAX CONSEQUENCES TO THEM OF THE MERGER, INCLUDING TAX RETURN REPORTING REQUIREMENTS, AND THE APPLICABILITY AND EFFECT OF FEDERAL, STATE, LOCAL AND OTHER APPLICABLE TAX LAWS.

## **DESCRIPTION OF DGI STOCK**

### **General**

DGI is authorized to issue 2,000,000 shares of preferred stock, par value \$1.00 per share, of which no shares were outstanding as of March 31, 2010, 30,000,000 shares of Class A common stock, par value \$.01 per share, of which 19,924,944 shares were issued and outstanding as of March 31, 2010 and 10,000,000 shares of Class B common stock, par value \$0.01 per share, of which 5,576,775 shares were issued and outstanding as of March 31, 2010. DGI Class A common stock and DGI Class B common stock are both traded on the NASDAQ Global Select Market under the symbol DGICA and DGICB, respectively. The transfer agent and registrar for DGI Class A common stock and DGI Class B common stock is Computershare. Except as described below with respect to dividends and voting rights, shares of DGI Class A common stock and DGI Class B common stock are identical in all respects. As of March 31, 2010, approximately 3.3 million shares of DGI Class A common stock were reserved for issuance under employee stock plans.

### **DGI Class A Common Stock and DGI Class B Common Stock**

The following is a materially complete summary of the rights, preferences and limitations of DGI's Class A common stock and Class B common stock.

*Voting and Other Rights.* The holders of DGI Class A common stock are entitled to one-tenth of a vote per share on any matter submitted to a vote of the shareholders of DGI, while the holders of DGI Class B common stock are entitled to one vote per share on any matter submitted to a vote of the shareholders of DGI. Except as required by the DGCL or DGI's certificate of incorporation, the holders of DGI Class A common stock and DGI Class B common stock vote together as a single class on all matters submitted to a vote of the shareholders of DGI.

Under DGI's certificate of incorporation and the DGCL, at any election of directors, those nominees receiving the highest number of votes cast for the number of directors to be elected will be elected as directors. Because DGI's

certificate of incorporation does not authorize cumulative voting in the election of directors, DMIC, as the holder of approximately 66% of the aggregate voting power of DGI's Class A common stock and DGI's Class B common stock, has the power to control the election of all of the members of DGI's board of directors, and the holders of the remainder of the outstanding shares of DGI Class A common stock and DGI Class B common stock will not be able to cause the election of any director of DGI.

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Under DGI's certificate of incorporation and the DGCL, only the affirmative vote of the holders of a majority in voting power represented by the DGI Class A common stock and the DGI Class B common stock, voting as a single class, is required to amend DGI's certificate of incorporation, to authorize additional shares of capital stock of any class, to approve any merger or consolidation of DGI with or into any other corporation or the sale of all or substantially all of DGI's assets or to approve the dissolution of DGI.

Under the DGCL, the holders of DGI Class A common stock or DGI Class B common stock are entitled to vote as a separate class on any proposal to change the par value of such class or to alter or change the rights, preference and limitations of such class in a way that would adversely affect any such rights of such class.

*Merger and Consolidation.* In the event of a merger, consolidation or liquidation, holders of DGI Class A common stock and DGI Class B common stock are entitled to receive pro rata any assets legally available for distribution to shareholders with respect to shares held by them, subject to any prior rights of the holders of any DGI preferred stock then outstanding.

Neither DGI Class A common stock nor DGI Class B common stock has any preemptive rights, redemption privileges, sinking fund privileges or conversion rights. All outstanding shares of DGI Class A common stock and DGI Class B common stock are validly issued, fully paid and nonassessable.

*Dividends and Distributions.* The holders of DGI Class A common stock are entitled to receive such dividends or distributions as the DGI board of directors may declare out of funds legally available for such payments. Each share of DGI Class A common stock outstanding at the time of any dividend or distribution payable in cash upon the outstanding shares of DGI Class B common stock is entitled to a cash dividend or distribution payable at the same time and to shareholders of record as of the same date in an amount that is at least 10% greater than any dividend or distribution declared upon the shares of Class B common stock. The payment of distributions by DGI is subject to the restrictions of Delaware law applicable to the declaration of distributions by a business corporation. A corporation generally may not authorize and make distributions if, after giving effect thereto, it would be unable to meet its debts as they become due in the usual course of business or if the corporation's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if it were to be dissolved at the time of distribution, to satisfy claims upon dissolution of shareholders who have preferential rights superior to the rights of the holders of its common stock. In addition, the payment of distributions to shareholders is subject to any prior rights of any then outstanding DGI preferred stock. Stock dividends, if any are declared, may be paid from authorized but unissued shares.

The ability of DGI to pay distributions is affected by the ability of its subsidiaries to pay dividends. The ability of DGI's subsidiaries, as well as of DGI, to pay dividends in the future is influenced by bank and insurance company regulatory requirements and capital guidelines.

## **DGI Preferred Stock**

*General.* DGI is authorized to issue 2,000,000 shares of preferred stock, par value \$1.00 per share, of which no shares were outstanding as of March 31, 2010. The DGI board of directors has the authority to issue DGI preferred stock in one or more series and to fix the dividend rights, dividend rates, liquidation preferences, conversion rights, voting rights, rights and terms of redemption, including sinking fund provisions and the number of shares constituting any such series, without any further action by the shareholders of DGI unless such action is required by applicable rules or regulations or by the terms of any other outstanding series of DGI preferred stock. Any shares of DGI preferred stock that may be issued may rank prior to shares of DGI Class A common stock or Class B common stock as to payment of dividends and upon liquidation.



**COMPARISON OF SHAREHOLDER RIGHTS**

**Summary**

We are incorporated under the laws of the Commonwealth of Pennsylvania, while DGI is incorporated under the laws of the State of Delaware. After the merger, you will become shareholders of DGI and DGI s

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certificate of incorporation, by-laws and the DGCL will govern your rights as a shareholder of DGI. The following summary discusses differences between DGI's certificate of incorporation and by-laws and our articles of incorporation and by-laws and the differences between the PBCL and the DGCL. The merger will not change DGI's certificate of incorporation and by-laws. For information as to how to get the full text of each party's respective articles of incorporation or by-laws, see "Where You Can Find More Information" beginning on page v.

The following summary is not intended to be a complete statement of the material differences affecting the rights of our shareholders who become DGI shareholders, but rather summarizes the more significant differences affecting the rights of such shareholders. The summary is qualified in its entirety by reference to the articles of incorporation and by-laws of DGI, our articles of incorporation and by-laws and applicable laws and regulations.

	<b>DGI</b>	<b>UNNF</b>
Board of Directors Size of Board	Currently fixed by the by-laws at not less than seven nor more than 12.	Currently has nine directors, but the bylaws authorize the board to change this number to not less than seven or more than 25.
Classification	Divided into three classes as nearly equal as possible with each class serving a staggered three-year term.	Divided into three classes as nearly equal as possible, with each class serving a staggered three-year term.
Removal of Director	Delaware law provides that directors may be removed with or without cause by holders of a majority of the shares which would be entitled to vote at an election of directors, unless the board is classified.	Under Pennsylvania law, the entire board of directors, a class or a director can only be removed for cause and not by less than a majority of the votes entitled to be cast on the matter.
Vacancies	By-laws provide that vacancies on the DGI Board may be filled by the remaining directors or the shareholders may do so at a special meeting.	Bylaws provide that vacancies may be filled by the remaining directors.
Limitation of Director Liability	Delaware law permits a corporation to limit a director's personal liability, with certain specified exceptions. The corporation's certificate of incorporation must set forth any such limitation.  The certificate of incorporation of DGI specifically eliminates a director's personal liability for monetary damages unless the director has breached his or her duty of loyalty to the corporation or its shareholders, or has taken actions which were not in good faith or which constituted intentional misconduct or a knowing violation of the law. In addition, the limitation of liability will not apply to a declaration of an improper dividend, to an improper	Pennsylvania law permits a corporation to limit a director's personal liability, with certain specified exceptions. The corporation's bylaws must set forth any such limitation.  The articles of incorporation and bylaws of UNNF eliminate a director's liability to the fullest extent permitted by Pennsylvania law. Under Pennsylvania law, a director is not be liable for monetary damages for any action taken or omitted unless the director breaches or fails to perform his or her duties and the breach or failure to perform constitutes self-dealing, willful misconduct or recklessness. Under Pennsylvania law, a director also

redemption of stock or to any transaction from which the director derived an improper personal benefit.

remains, personally liable where the responsibility or liability is under any criminal statute or is for the nonpayment of taxes under federal, state or local law.

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	<b>DGI</b>	<b>UNNF</b>
Indemnification of Directors and Officers General	<p>Delaware law permits a corporation to indemnify any person involved in a third party action because of such person's service as an officer, director or employee of the corporation, against expenses incurred and amounts paid in such an action (and against expenses incurred in any derivative action), if such person acted in good faith and reasonably believed that his actions were in, or not opposed to, the best interests of the corporation. In a criminal proceeding, such person is also required not to have had reasonable cause to believe that his conduct was unlawful. A corporation may advance expenses incurred in defending any action as long as the person agrees to repay the amount advanced if it is ultimately determined that such person is not entitled to indemnification.</p>	<p>The relevant provisions of Pennsylvania law are essentially the same as those of Delaware law.</p>
Expenses in Derivative Actions	<p>In general, Delaware law does not permit a corporation to indemnify a person for expenses in a derivative action if the person has been adjudged liable to the corporation, unless a court finds such person entitled to such indemnification. If, however, the person has successfully defended a third party or derivative action, the corporation is required to provide indemnification for expenses incurred.</p>	<p>The relevant provisions of Pennsylvania law are essentially the same as those of Delaware law.</p>
Exclusion of Other Rights	<p>The statutory provisions for indemnification do not exclude any other rights a person seeking indemnification may have under any by-law, agreement, vote of shareholders, vote of disinterested directors or otherwise.</p>	<p>The relevant provisions of Pennsylvania law are essentially the same as those of Delaware law.</p>

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	<b>DGI</b>	<b>UNNF</b>
Amendment to Charter	Delaware law provides that the holders of a majority of the outstanding shares of each class of stock entitled to vote must approve any charter amendment.	Unless a corporation's articles of incorporation require a greater percentage, Pennsylvania law only requires the affirmative vote of a majority of the votes of each class of shares actually cast on a proposed amendment at a meeting at which a quorum is present. Pennsylvania law also does not require shareholder approval of certain non-material amendments to the articles of incorporation. However, the articles of incorporation of UNNF require the approval of the holders of 80% of the votes entitled to be cast in order to amend the provisions in the UNNF articles relating to any merger, consolidation, liquidation or dissolution or any action that would result in the sale as other disposition of all or substantially all of the assets of UNNF.
Mergers and Other Fundamental Transactions	Delaware law provides that the holders of a majority of the shares entitled to vote must approve any fundamental corporate transactions such as mergers, sales of all or substantially all of the corporation's assets, dissolutions, etc. A corporation may increase the minimum percentage vote required, but the certificate of incorporation of DGI does not contain any super-majority vote requirements to approve any fundamental corporate transaction.	A corporation may increase the minimum percentage vote required, and the articles of incorporation of UNNF require the vote of the holders 80% of UNNF's outstanding shares to approve any fundamental transactions.
Authorized Capital Stock	The DGI certificate of incorporation authorizes the issuance of up to 30,000,000 shares of Class A common stock, par value \$.01 per share, 10,000,000 shares of Class B common stock, par value \$.01 per share and 2,000,000 shares of preferred stock, par value \$1.00 per share. As of March 31, 2010, 19,924,944 shares of class A common stock and 5,576,775 shares of Class B common stock no shares of preferred stock were issued and outstanding.	The UNNF articles of incorporation authorize the issuance of up to 20,000,000 shares of common stock, par value \$.25 per share and up to 5,000 shares of preferred stock, par value \$1.00 per share. As of March 31, 2010, approximately 2,742,395 shares of common stock and 1,275 shares of Class A preferred stock were issued and outstanding.



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	<b>DGI</b>	<b>UNNF</b>
Dividends	Delaware law permits a corporation to pay dividends out of surplus, which is the excess of net assets of the corporation over capital, or, if the corporation does not have adequate surplus, out of net profits for the current or immediately preceding fiscal year, unless the net assets are less than the capital of any outstanding preferred stock.	Pennsylvania law permits a corporation to pay dividends unless doing so would make the corporation unable to pay its debts as they become due in the ordinary course of business, or unless, as a result of paying such dividends, the corporation's total assets would be less than its total liabilities plus the amount that would be needed to pay the holders of shares having a liquidation preference if the corporation were dissolved.
Stock Repurchases	Under Delaware law, a corporation may not purchase or redeem its own shares if its capital is impaired or if the purchase or redemption would cause its capital to be impaired. However, a Delaware corporation may purchase or redeem preferred shares out of capital if the shares will then be retired, reducing the capital of the corporation.	Pennsylvania law permits a corporation to redeem any and all classes of its shares and treats such redemption or repurchase like a dividend distribution, subject to the same limitations described under Dividends above.
Election of Directors	Delaware law permits shareholders to cumulate their votes and either cast them for one candidate or distribute them among two or more candidates in the election of directors only if expressly authorized in a corporation's charter. The DGI certificate of incorporation does not expressly authorize cumulative voting.	Pennsylvania law automatically gives shareholders cumulative voting rights unless a corporation's articles of incorporation provide otherwise. The UNNF articles of incorporation expressly prohibit cumulative voting.
Appraisal or Dissenters Rights	Delaware law does not afford appraisal rights to holders of shares that are either listed on a national securities exchange, quoted on NASDAQ or held of record by more than 2,000 shareholders, provided that such shares will be converted solely into cash in lieu of fractional shares or into stock of the surviving corporation or another corporation, which corporation in either case must also be listed on a national securities exchange, quoted on NASDAQ or held of record by more than 2,000 shareholders. In addition, Delaware law denies appraisal rights to shareholders of the surviving	Pennsylvania law is similar to Delaware law with respect to appraisal rights.  The definition of fair value in payment for shares upon exercise of appraisal or dissenters' rights is substantially similar under both states' laws.  Any valuation methods that are generally acceptable in the financial community may be used.

corporation in a merger if the surviving  
corporation's shareholders are not  
required to approve the merger.



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	<b>DGI</b>	<b>UNNF</b>
Amendments to By-laws	<p>If the certificate of incorporation of a Delaware company gives the board of directors the power to amend the by-laws, which the DGI certificate does, Delaware law does not limit the board's power to make changes in the by-laws.</p> <p>Under Delaware law, shareholders may amend a corporation's by-laws at any meeting, without the consent of the board of directors. However, Article 12 of DGI's by-laws provides that shareholders may only amend DGI's by-laws at any meeting if the notice of that meeting contains a statement with respect to the proposed amendment.</p>	<p>With the approval of the holders of 80% of the outstanding common stock of UNNF or by a majority vote of its board of directors, UNNF may amend its bylaws. Under Pennsylvania law, a copy or summary of any proposed amendment must be included with the notice of the meeting.</p>
Action by Written Consent	<p>Delaware law permits a majority of shareholders to act by written consent, without a meeting, unless a corporation's charter provides otherwise. DGI's charter does not prohibit the shareholders from acting by written consent.</p>	<p>Under Pennsylvania law, shareholders of a registered corporation, such as UNNF, may act without a meeting by less than unanimous consent only if permitted by the corporation's articles of incorporation. UNNF's articles currently do not permit such action.</p>
Annual Meeting of Shareholders	<p>Held on the third Thursday in April.</p> <p>If an annual meeting for the election of directors is not held on a designated date, Delaware law requires the directors to cause the meeting to be held as soon thereafter as convenient. If they fail to do so for a period of 30 days after the designated date, or if no date has been designated for a period of 13 months after the organization of the corporation or after its last annual meeting, then, upon application of any shareholder or director, the Court of Chancery may order a meeting to be held.</p>	<p>Held no later than May 31 of each year.</p> <p>Under Pennsylvania law, if the annual meeting for the election of directors is not called and held within six months after the designated time, any shareholder may call such meeting at any time thereafter without application to any court.</p>

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	<b>DGI</b>	<b>UNNF</b>
Special Meeting of Shareholders	Delaware law permits the board of directors or any other person authorized by a corporation's charter or by-laws to call a special meeting of shareholders. The DGI by-laws permit its president and the board of directors to call a special meeting of shareholders. The DGI by-laws also require its board of directors to call a special meeting of shareholders upon the written request of shareholders entitled to cast at least one-fifth of the votes which all shareholders are entitled to cast.	Pennsylvania law permits the board of directors or any other person authorized by a corporation's articles or bylaws to call a special meeting of shareholders. Pennsylvania law, however, explicitly states that shareholders of a registered corporation, such as UNNF, do not have a statutory right to call special meetings, except that an interested shareholder may call a meeting in order to seek approval of a business combination between the corporation and such interested shareholder. Under UNNF's bylaws, the chairman of the board, the president, the executive vice president, if any, a majority of the board of directors or of its executive committee or holders of 35% of the outstanding common stock of UNNF may call a special meeting of shareholders.
Advance Notice Requirements for Shareholder Nominations and Other Business	A shareholder wishing to nominate directors or bring other business before an annual meeting of DGI shareholders must give notice not less than 90 nor more than 120 days before the first anniversary of the day written notice of the previous year's meeting was given as long as it is brought within 10 days of the date DGI makes such a public announcement. A shareholder wishing to nominate directors at a special meeting of DGI shareholders must deliver notice within 10 days after DGI publicly announces the special meeting.	A shareholder wishing to nominate directors at an annual meeting of UNNF shareholders must provide written notice at least 90 days before the anniversary date of the prior year's meeting.
Rights of Inspection	Under Delaware law, a shareholder may inspect a corporation's books and records during normal business hours as long as such inspection is for a proper purpose, and as long as the shareholder has made proper written demand stating the purpose of the inspection. A proper purpose is any purpose reasonably related to the interests of the inspecting person as a shareholder.	Under Pennsylvania law, a shareholder may inspect a corporation's books and records during normal business hours as long as such inspection is for a proper purpose, and as long as the shareholder has made proper written and verified demand stating the purpose of the inspection. A proper purpose is any purpose reasonably related to the interests of the inspecting person as a shareholder.

Case Law

There is a substantial body of case law in Delaware interpreting the corporation laws of that state.

Pennsylvania does not have a comparable body of judicial interpretation.

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	<b>DGI</b>	<b>UNNF</b>
Court Systems	Delaware has established a system of Chancery Courts to adjudicate matters arising under the DGCL.	Pennsylvania has not established an equivalent court system and matters arising under the PBCL are adjudicated by general state courts.

**General**

Both Delaware and Pennsylvania law provide that the board of directors has the ultimate responsibility for managing the business and affairs of a corporation. In discharging this function, directors of Pennsylvania and Delaware corporations owe fiduciary duties of care and loyalty to the corporations they serve. Directors of Delaware corporations also owe fiduciary duties of care and loyalty to shareholders.

The fiduciary duty provisions included in Pennsylvania law, which apply to us, may provide significantly broader discretion, and increased protection from liability, to directors in exercising their fiduciary duties, particularly in the context of a change in control.

The following summarizes certain aspects of Delaware and Pennsylvania law as they relate to fiduciary duties of directors:

**Standard of Care**

Delaware courts have held that the directors of a Delaware corporation are required to exercise an informed business judgment in performing their duties. An informed business judgment means that the directors have informed themselves of all material information reasonably available to them. Delaware courts have also imposed a heightened standard of conduct on directors in matters involving a contest for control of the corporation.

A director of a Pennsylvania business corporation stands in a fiduciary relationship to the corporation (unlike in Delaware, where a director also stands in a fiduciary relationship to shareholders) and must perform his or her duties as a director in good faith, in a manner he or she reasonably believes to be in the best interests of the corporation and with such care, including reasonable inquiry, skill and diligence, as a person of ordinary prudence would use under similar circumstances.

**Justifiable Reliance**

A director of a Delaware corporation, in performing his or her duties, is fully protected in relying, in good faith, upon the records of the corporation and upon such information, opinions, reports or statements presented to the corporation by any of the corporation's officers or employees, or by committees of the board of directors, or by any other person as to matters the director reasonably believes are within such other person's professional or expert competence. Such person must also have been selected with reasonable care by or on behalf of the corporation.

In performing his or her duties, a director of a Pennsylvania business corporation is entitled to rely, in good faith, on information, opinions, reports or statements (including financial statements and other financial data) prepared or presented by any of the following:

officers or employees of the corporation, so long as the director reasonably believes them to be reliable and competent in the matters presented;

counsel, public accountants, investment bankers or other persons as to matters which the director reasonably believes to be within the professional or expert competence of such persons; and

a duly designated committee of the board which the director reasonably believes merits confidence and upon which the director does not serve, but only as to matters within the committee's designated authority.

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However, a director will not be considered to be acting in good faith if he or she has knowledge concerning the matter in question which would cause such reliance to be unwarranted.

### **Consideration of Factors**

Delaware law does not contain any statutory provision permitting the board of directors, committees of the board and individual directors, when discharging their duties, to consider the interests of any constituencies other than the corporation or its shareholders.

Pennsylvania law, on the other hand, provides that in discharging their duties, the board of directors, committees of the board and individual directors may, in considering what is in the best interests of the corporation, consider, to the extent they deem appropriate:

the effects of any action upon any groups affected by such action, including shareholders, employees, suppliers, customers and creditors of the corporation, and on communities served by the corporation;

the corporation's short-term and long-term interests, including benefits which may accrue to the corporation from its long-term plans and the possibility that these interests may be best served by the corporation's continued independence;

the resources, intent and conduct (past, stated and potential) of any person seeking to acquire control of the corporation; and

all other pertinent factors.

Under current Delaware law, it is unclear whether the board of directors, committees of the board and individual directors of a Delaware corporation may, in considering what is in the corporation's best interests or what the effects of any action on the corporation may be, take into account the interests of any constituency other than the corporation's shareholders. In contrast to Delaware law, Pennsylvania law provides that a director owes a duty only to the corporation and not to the shareholders, and in considering what is in the best interests of the corporation, may choose to subordinate the interests of shareholders to the interests of employees, suppliers, customers or creditors of the corporation or to the interests of the communities served by the corporation.

In addition, the duty of the board of directors, committees of the board and individual directors of a Delaware corporation may be enforced directly by the corporation, or may be enforced by a shareholder, as such, by an action in the right of the corporation, or may be enforced directly by a shareholder or by any other person or group. In contrast, the duty of the board of a Pennsylvania corporation may not be enforced directly by a shareholder.

### **Specific Applications**

Delaware courts have imposed a heightened standard of conduct upon directors of a Delaware corporation who take any action designed to defeat a threatened change in control of the corporation. The heightened standard has two elements. First, the board must demonstrate some basis for concluding that a proper corporate purpose is served by implementation of any defensive measure, and, second, that measure must be reasonable in relation to the perceived threat posed by the change in control.

The fiduciary duty of directors of a Pennsylvania corporation does not require them to act solely because of the effect such action might have on an acquisition or potential or proposed acquisition of control of the corporation or on the

consideration which might be offered or paid to shareholders in such an acquisition. In particular, directors of a Pennsylvania corporation are not required to redeem rights under any shareholder rights plan, and under existing case law, have the statutory authority under Pennsylvania law simply to reject a potential or proposed acquisition of the corporation's shares.

In addition, under Delaware law, unlike under Pennsylvania law, when the board of directors approves the sale of a corporation, the board of directors may have a duty to obtain the highest value reasonably available to the shareholders.

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Also, our articles of incorporation contain provisions that allow the board of directors to oppose a tender or other offer for our securities, whether the offer is in cash or in the securities of a corporation or otherwise. Our board of directors may consider any relevant, germane or pertinent issue when considering whether to oppose an offer, including:

- whether the offer price is acceptable based on historical and present operating results or financial condition;
- whether a more favorable price could be obtained;
- the social and economic effects of the offer or transaction;
- the reputation and business practice of the offeror and its management;
- the value of the securities that the offeror is offering in exchange;
- the business and financial condition and earnings prospects of the offeror; and
- any antitrust or other legal or regulatory issues that are raised by the offer.

If our board of directors determines that an offer should be rejected, it may take any lawful action to accomplish its purpose.

## **Presumption**

Under Delaware law, there is a presumption that the directors of a Delaware corporation acted on an informed basis, in good faith and in the honest belief that their actions were in the best interest of the corporation. This presumption may be overcome, however, if a preponderance of the evidence shows that the directors' decision involved a breach of fiduciary duty such as fraud, overreaching, lack of good faith, failure of the board to inform itself properly or actions by the board to entrench itself in office.

Under Pennsylvania law, unless there is a breach of fiduciary duty, a lack of good faith or self-dealing (in other words, entering into a contract or transaction with a director or an entity in which a director has a financial or other interest), there is a presumption that any act of the board of directors, any committee of the board or any individual director is in the corporation's best interest. No higher burden of proof or greater obligation to justify applies to any act relating to or affecting an acquisition or a potential or proposed acquisition of control of the corporation than to any other action.

Pennsylvania law presumes any board action relating to an acquisition or potential or proposed acquisition of control that a majority of the corporation's disinterested directors approve to satisfy the statutory duty of care under Pennsylvania law, unless there is clear and convincing evidence that the disinterested directors did not assent to such act in good faith, after reasonable investigation. Disinterested directors are those who are not affiliated with the person seeking control and are not officers or employees of the corporation.

## **Anti-Takeover Laws**

Section 203 of the DGCL contains certain anti-takeover provisions that apply to a Delaware corporation, unless the corporation elects not to be governed by such provisions in its certificate of incorporation or bylaws. Neither the certificate of incorporation nor the bylaws of DGI contain such an election. Thus, Section 203 applies to DGI. Section 203 precludes a corporation from engaging in any business combination with any person that owns 15% or more of its outstanding voting stock for a period of three years following the time that such shareholder obtained ownership of more than 15% of the outstanding voting stock of the corporation. A business combination includes any



merger, consolidation or sale of substantially all a corporation's assets.

The three-year waiting period does not apply, however, if any of the following conditions are met:

the board of directors of the corporation approved either the business combination or the transaction which resulted in such shareholder owning more than 15% of such stock before the shareholder obtained ownership of more than 15% of the corporation's stock;

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once the transaction which resulted in the shareholder owning more than 15% of the outstanding voting stock of the corporation is completed, such shareholder owns at least 85% of the voting stock of the corporation outstanding at the time that the transaction commenced; or

at or after the time the shareholder obtains more than 15% of the outstanding voting stock of the corporation, the board of directors approves the business combination and the shareholders authorized the business combination at an annual or special meeting of shareholders (and not by written consent) by the affirmative vote of at least 66 $\frac{2}{3}$ % of the outstanding voting stock that is not owned by the acquiring shareholder.

In addition, Section 203 does not apply to any person who became the owner of more than 15% of a corporation's stock if it was as a result of action taken solely by the corporation. Section 203 also does not apply to the corporation itself or to any of the corporation's majority-owned subsidiaries.

Chapter 25 of the PBCL contains several anti-takeover provisions that apply to registered corporations such as us.

Section 2538 of the PBCL, which is similar to Section 203 of the DGCL, requires shareholder approval for certain transactions between a registered corporation and an interested shareholder, which generally is a shareholder who owns 20% of the stock entitled to vote in an election of directors. Section 2538 applies if an interested shareholder, together with anyone acting jointly with such shareholder and any affiliates of such shareholder:

is to be a party to a merger or consolidation, a share exchange or certain sales of assets involving the corporation or one of its subsidiaries;

is to receive a disproportionate amount of any of the securities of any corporation which survives or results from a division of the corporation;

is to be treated differently from others holding shares of the same class in a voluntary dissolution of such corporation; or

is to have his or her percentage of voting or economic share interest in such corporation materially increased relative to substantially all other shareholders in a reclassification.

In such a case, the affirmative vote of the holders of shares representing at least a majority of the votes that all shareholders are entitled to cast is required to approve the proposed transaction. Shares held by the interested shareholder are not included in calculating the number of shares entitled to be cast, and the interested shareholder is not entitled to vote on the transaction. This special voting requirement does not apply if the proposed transaction has been approved in a prescribed manner by the corporation's board of directors or if the transaction satisfies certain other conditions, including conditions relating to the amount of consideration to be paid to certain shareholders.

Section 2555 of the PBCL may also apply to a transaction between a registered corporation and an interested shareholder, even if Section 2538 also applies. Section 2555 prohibits a corporation from engaging in a business combination with an interested shareholder unless one of the following conditions is met:

the board of directors has previously approved either the proposed transaction or the interested shareholder's acquisition of shares;

the interested shareholder owns at least 80% of the stock entitled to vote in an election of directors and, no earlier than three months after the interested shareholder reaches the 80% level, the majority of the remaining

shareholders approve the proposed transaction, the shareholders receive a minimum fair price for their shares in the transaction and the transaction meets other conditions of Section 2556 of the PBCL;

holders of all outstanding common stock approve the transaction;

no earlier than five years after the interested shareholder became an interested shareholder, a majority of the remaining shares entitled to vote in an election of directors approve the transaction; or

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no earlier than five years after the interested shareholder became an interested shareholder, a majority of all the shares approve the transaction, all shareholders receive a minimum fair price for their shares, and certain other conditions are met.

Pennsylvania law deems a person or group of persons acting in concert that holds 20% of the shares of a registered corporation entitled to vote in the election of directors to be a control group. A shareholder who objects to the transaction that makes the control group a control group can, under procedures set forth in the PBCL, require the control group to purchase his or her shares at fair value, as defined under Pennsylvania law.

We have opted out of certain other provisions of Pennsylvania law that apply to a registered corporation which, under certain circumstances, permit a corporation to redeem control shares, as defined under Pennsylvania law, remove the voting rights of control shares and require the disgorgement of profits by a controlling person, as defined under Pennsylvania law.

**COMPARATIVE MARKET PRICES AND DIVIDENDS**

The following table sets forth for the periods indicated:

the high and low sales prices of shares of DGI Class A common stock as reported on the NASDAQ Global Select Market;

the high and low sales prices of shares of our common stock as reported on the OTCBB; and

quarterly cash dividends paid per share by DGI and UNNF.

	DGI Class A Common Stock			UNNF Common Stock		
	High	Low	Dividend	High	Low	Dividend
2008:						
First quarter	\$ 18.00	\$ 15.60	\$	\$ 11.50	\$ 9.40	\$
Second quarter	17.95	15.51	.105	10.20	9.05	
Third quarter	23.00	15.31	.105	9.15	5.26	
Fourth quarter	18.00	11.24	.21	8.50	4.76	
2009:						
First quarter	\$ 17.00	\$ 12.25	\$	\$ 5.00	\$ 3.51	\$
Second quarter	17.47	13.61	.1125	5.00	3.50	
Third quarter	16.60	14.31	.1125	6.10	3.20	
Fourth quarter	16.02	14.22	.1125	4.25	2.82	
2010:						
First quarter	\$ 15.95	\$ 13.94	\$	\$ 4.95	\$ 3.00	\$
Second quarter (through June 21)	15.00	12.12	.115	7.80	3.65	

On April 19, 2010, the business day immediately preceding our announcement of the merger, the closing price of DGI Class A common stock was \$14.68 and on \_\_\_\_\_, 2010, the last day before we printed this proxy statement/prospectus, the closing price of DGI Class A common stock was \$ \_\_\_\_\_ per share.



**Table of Contents****BENEFICIAL OWNERSHIP OF OUR COMMON STOCK**

The following table sets forth information pertaining to the beneficial ownership of the outstanding shares of our common stock as of March 31, 2010 by: (1) persons known by us to own more than five percent of the outstanding shares of our common stock, (2) each director and (3) our directors and executive officers as a group. The information contained herein has been obtained from our records and from information furnished to us by each individual named below. We know of no person who owns, beneficially or of record, either individually or with associates, more than five percent of our common stock, except as set forth below.

<b>Name of Individual or Identity of Group</b>	<b>Shares Owned</b>	<b>Additional Shares if Convert Preferred</b>	<b>Additional Shares if Exercise Stock Options</b>	<b>Total Beneficial Ownership</b>	<b>Percent of Class</b>
<b>5% or Greater shareholders:</b>					
Donegal Mutual Insurance Company	248,999			248,999(6)	9.08%
<b>Directors:</b>					
Donald Cargas, Jr.	12,200			12,200(7)	
Kevin D. Dolan	12,165	6,250		18,415(8)	
Mark D. Gainer	30,126	25,000	23,650	78,776(9)	2.07
James R. Godfrey	4,444		1,157	5,601(10)	
Barry C. Huber	17,337	12,500		29,837(11)	1.04
Thomas J. McGrath	12,191			12,191(12)	
William M. Nies	12,680	6,250	1,157	25,087(13)	
Darwin A. Nissley	12,316		4,928	17,344(14)	
Lloyd C. Pickell	17,796	12,500	2,314	32,610(15)	
<b>Other Named Executive Officers:</b>					
Stephen D. Staman	18,413	6,250	11,250	35,913(16)	1.26
Michael D. Peduzzi	5,000			5,000(17)	
Charles R. Starr	3,303		525	3,828(18)	
All Directors and Executive Officers as a Group (12 persons)	162,971	68,750	44,981	276,702	9.69

(1) Information furnished by our directors and officers.

(2) The securities beneficially owned by an individual are determined in accordance with the definition of beneficial ownership set forth in the General Rules and Regulations of the SEC and may include securities owned by or for the individual's spouse and minor children and any other relative who has the same home, as well as securities to which the individual has or shares voting or investment power. Beneficial ownership may be disclaimed as to certain of the securities. Except as otherwise indicated, the address for each of the following persons is our principal corporate address.

- (3) Through September 14, 2010, each share of our preferred stock may be converted into 250 shares of our common stock.
- (4) As of May 1, 2010, none of the options had any intrinsic value.
- (5) Less than 1% unless otherwise indicated.
- (6) Based on a Schedule 13D/A DMIC filed with the SEC on May 6, 2010.
- (7) Includes 1,600 shares of common stock Mr. Cargas holds individually and 10,600 shares of common stock he holds jointly with his spouse.
- (8) Includes 2,879 shares of common stock Mr. Dolan holds individually, 8,788 shares of common stock held in a 401(k) plan for the benefit of Mr. Dolan, 419 shares of common stock Mr. Donald holds jointly with

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his spouse and 79 shares of common stock held by a real estate partnership of which Mr. Dolan is a partner. Mr. Dolan also holds 25 shares of our preferred stock.

- (9) Includes 3,325 shares of common stock Mr. Gainer holds individually, 486 shares of common stock Mr. Gainer's spouse holds individually, 26,315 shares of common stock held in an IRA for the benefit of Mr. Gainer and options to purchase 23,650 shares. An IRA for the benefit of Mr. Gainer also holds 100 shares of our preferred stock.
- (10) Includes 1,794 shares of common stock Mr. Godfrey holds individually, 2,650 shares of common stock held in an IRA for the benefit of Mr. Godfrey and options to purchase 1,157 shares.
- (11) Includes 17,337 shares of common stock Mr. Huber holds individually and 50 shares of preferred stock Mr. Huber holds individually.
- (12) Includes 1,782 shares of common stock Dr. McGrath holds individually and 10,405 shares of common stock held in an IRA for the benefit of Dr. McGrath.
- (13) Includes 17,680 shares of common stock Mr. Nies holds individually and options to purchase 1,157 shares. Mr. Nies also holds 25 shares of our preferred stock.
- (14) Includes 12,086 shares of common stock Mr. Nissley holds individually, 115 shares of common stock Mr. Nissley holds jointly with his spouse, 115 shares of common stock Mr. Nissley's son holds and options to purchase 4,928 shares.
- (15) Includes 17,323 shares of common stock Mr. Pickell holds individually, 473 shares of common stock Mr. Pickell holds jointly with his spouse and options to purchase 2,314 shares. An IRA for the benefit of Mr. Pickell holds 50 shares of our preferred stock.
- (16) Includes 18,413 shares of common stock Mr. Staman holds individually and options to purchase 11,250 shares. Mr. Staman also holds 25 shares of our preferred stock.
- (17) Includes 4,000 shares of common stock Mr. Peduzzi holds individually and 1,000 shares held in an IRA for the benefit of Mr. Peduzzi.
- (18) Includes 650 shares of common stock Mr. Starr holds individually, 2,673 shares of common stock Mr. Starr holds jointly with his spouse and options to purchase 525 shares.

**PROPOSAL NO. 2**

**ADJOURNMENT PROPOSAL**

**The Adjournment Proposal**

In the event sufficient votes are not present at our special meeting to constitute a quorum or approve the merger proposal, our shareholders cannot approve the merger proposal unless our special meeting is adjourned in order to permit further solicitation of proxies. In order to allow shares present in person or by proxy at our special meeting to vote for the adjournment of our special meeting, if necessary, we request that our shareholders approval a proposal to approve an adjournment of our special meeting if necessary to solicit additional proxies. The proxies will vote in favor of the adjournment proposal, unless otherwise indicated on the proxy. If shareholders approve the adjournment



proposal, we will not give any notice of the time and place of our adjourned meeting other than an announcement of the time and place that we will give at our special meeting.

**Recommendation of Our Board of Directors**

Our board of directors recommends that our shareholders vote **FOR** the approval of the merger proposal and **FOR** the approval of the adjournment proposal.

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**LEGAL MATTERS**

The validity of the DGI Class A common stock being registered in connection with the merger has been passed upon for DGI by Duane Morris LLP, Philadelphia, Pennsylvania. Frederick W. Dreher, a partner of Duane Morris LLP, owns 90,901 shares of DGI Class A common stock and 33,022 shares of DGI Class B common stock.

**EXPERTS**

The consolidated financial statements of DGI and subsidiaries as of December 31, 2009 and 2008, and for each of the years in the three-year period ended December 31, 2009, and management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2009 have been incorporated by reference herein in reliance upon the reports of KPMG LLP, independent registered public accounting firm, incorporated by reference herein, and upon the authority of said firm as experts in accounting and auditing.

Our consolidated financial statements as of December 31, 2009 and 2008 and for each of the three years in the period ended December 31, 2009 have been audited by ParenteBeard LLC, independent registered public accounting firm, as set forth in their report set forth elsewhere in this proxy statement/prospectus. We have included such consolidated financial statements in this proxy statement/prospectus in reliance upon such reports given on the authority of such firm as experts in accounting and auditing.

**OTHER MATTERS**

As of the date of this proxy statement/prospectus, neither the Donegal parties nor we know of any matter that will come before our special meeting other than the approval of the merger proposal and the adjournment proposal. However, if any other matters properly come before our special meeting or any adjournment or postponement of our special meeting and be voted upon, the enclosed proxies shall be deemed to confer discretionary authority on the individuals named as proxies therein to vote the shares represented by such proxies as to any such matters in accordance with their judgment.

No person is authorized to give any information or make any representation other than those contained or incorporated by reference in this proxy statement/prospectus, and, if given or made, such information or representation should not be relied upon as having been authorized by DGI or us.

This proxy statement/prospectus does not constitute an offer to exchange or sell, or a solicitation of an offer to exchange or purchase, the DGI Class A common stock this proxy statement/prospectus offers, nor does it constitute the solicitation of a proxy, in any jurisdiction in which such offer or solicitation is not authorized or to or from any person to whom it is unlawful to make such offer or solicitation.

The information contained in this proxy statement/prospectus speaks as of the date hereof unless otherwise specifically indicated. The delivery of this proxy statement/prospectus shall not, under any circumstances, create any implication that there has been no change in the affairs of DGI or us since the date of this proxy statement/prospectus or that the information in this proxy statement/prospectus or in the documents DGI incorporates by reference in this proxy statement/prospectus is correct at any time subsequent to that date.

This proxy statement/prospectus does not cover any resales of the DGI Class A common stock offered hereby to be received by our shareholders deemed to be an affiliate of DGI upon the consummation of the merger. No person is authorized to make use of this proxy statement/prospectus in connection with any such resales.

**INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE**

The SEC allows the incorporation by reference of information into this proxy statement/prospectus, which means that DGI can disclose important information to you by referring to another document DGI has separately filed with the SEC. The information DGI has incorporated by reference in this proxy statement/

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prospectus is deemed to be part of this proxy statement/prospectus, except for any such information that information in this proxy statement/prospectus supersedes. This proxy statement/prospectus incorporates by reference the documents set forth below that DGI has previously filed with the SEC.

The following documents that DGI has previously filed with the SEC are incorporated by reference into this proxy statement/prospectus (SEC File No. 0-15341).

DGI's Annual Report on Form 10-K for the year ended December 31, 2009.

DGI's Quarterly Report on Form 10-Q for the quarter ended March 31, 2010.

DGI's Current Reports on Form 8-K filed on February 17, 2010, April 15, 2010, April 16, 2010, April 21, 2010, April 23, 2010, May 24, 2010 and June 16, 2010, other than the portions of those documents not deemed to be filed.

The description of the Class A common stock and Class B common stock of Donegal Group Inc. set forth in the registration statement on Form 8-A filed pursuant to Section 12 of the 1934 Act, including any amendment or report filed with the SEC, for the purpose of updating this description.

In addition, DGI incorporates by reference any documents it may file with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the 1934 Act, as amended, after the date of this proxy statement prospectus and prior to the date of the special meeting of our shareholders.

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**UNION NATIONAL FINANCIAL CORPORATION**

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	<b>December 31,</b>	
	<b>2009</b>	<b>2008</b>
	<b>(Dollars in thousands, except share data)</b>	
<b>ASSETS</b>		
Cash and Due from Banks	\$ 8,807	\$ 17,621
Interest-Bearing Demand Deposits in Other Banks	34,533	66
Federal Funds Sold		14,150
Total Cash and Cash Equivalents	43,340	31,837
Interest-Bearing Time Deposits in Other Banks	9,229	1,775
Investment Securities Available for Sale	60,546	64,289
Loans and Leases, Net of Unearned Income	339,274	358,280
Less: Allowance for Credit Losses	(5,858)	(4,358)
Net Loans and Leases	333,416	353,922
Premises and Equipment, Net	11,403	12,088
Restricted Investment in Bank Stocks	3,727	3,703
Bank-Owned Life Insurance	11,539	11,108
Other Real Estate Owned	5,383	
Other Assets	11,061	6,387
Total Assets	\$ 489,644	\$ 485,109
<b>LIABILITIES</b>		
Deposits:		
Noninterest-Bearing	\$ 54,331	\$ 46,875
Interest-Bearing	350,434	336,702
Total Deposits	404,765	383,577
Long-Term Debt	33,334	50,334
Junior Subordinated Debentures	17,341	17,341
Other Liabilities	2,868	3,063
Total Liabilities	458,308	454,315
Stockholders' Equity		
Preferred Stock (Series A), liquidation value \$1,000 per share		
Shares authorized 5,000; Issued 1,275 and 0 at December 31, 2009 and 2008, respectively	1,275	
Common Stock, par value \$0.25 per share		
Shares authorized 20,000,000; Issued 3,109,105 and 3,138,265 at December 31, 2009 and 2008, respectively; Outstanding 2,740,916 and 2,720,076 at December 31, 2009	777	785

and 2008, respectively		
Surplus	13,891	14,868
Retained Earnings	22,921	23,434
Accumulated Other Comprehensive (Loss) Income	(195)	36
Treasury Stock, at cost; 368,189 and 418,189 at December 31, 2009 and 2008, respectively	(7,333)	(8,329)
Total Stockholders' Equity	31,336	30,794
Total Liabilities and Stockholders' Equity	\$ 489,644	\$ 485,109

See accompanying notes to consolidated financial statements.

**Table of Contents****CONSOLIDATED STATEMENTS OF OPERATIONS**

	<b>Years Ended December 31,</b>		
	<b>2009</b>	<b>2008</b>	<b>2007</b>
	<b>(Dollars in thousands, except share data)</b>		
<b>Interest Income</b>			
Interest and Fees on Loans and Leases	\$ 21,593	\$ 24,594	\$ 26,834
Investment Securities:			
Taxable Interest	1,734	3,209	3,358
Tax-Exempt Interest	160		403
Dividends	40	114	290
Other	231	256	488
<b>Total Interest Income</b>	<b>23,758</b>	<b>28,173</b>	<b>31,373</b>
<b>Interest Expense</b>			
Deposits	8,394	9,470	10,790
Long-Term Debt	2,054	2,795	3,652
Junior Subordinated Debentures	838	1,104	1,268
Short-Term Borrowings		210	299
<b>Total Interest Expense</b>	<b>11,286</b>	<b>13,579</b>	<b>16,009</b>
<b>Net Interest Income</b>	<b>12,472</b>	<b>14,594</b>	<b>15,364</b>
Provision for Credit Losses	2,627	1,027	1,237
<b>Net Interest Income after Provision for Credit Losses</b>	<b>9,845</b>	<b>13,567</b>	<b>14,127</b>
<b>Non-Interest Income</b>			
Service Charges on Deposit Accounts	2,158	1,950	1,864
Other Service Charges, Commissions, Fees	1,154	1,091	1,059
Alternative Investment Sales Commissions	662	814	845
Income from Fiduciary Activities	180	309	347
Earnings from Bank-Owned Life Insurance	431	439	426
Mortgage Banking/Brokerage Activities	112	56	2,000
Title Insurance/Settlement Income			317
Other Income	341	186	362
Net Gain on Sale of Investment Securities	1,841	252	89
Other-than-temporary Impairments ( OTTI ) of Securities	(1,504)	(1,290)	(800)
Portion of OTTI Recognized in Other Comprehensive Loss			
<b>Net OTTI Losses on Securities</b>	<b>(1,504)</b>	<b>(1,290)</b>	<b>(800)</b>
<b>Total Non-Interest Income</b>	<b>5,375</b>	<b>3,807</b>	<b>6,509</b>
Non-Interest Expense			



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Salaries, Wages, and Employee Benefits	7,033	7,676	9,723
Net Occupancy	1,724	1,818	2,390
Data and ATM Processing	1,681	1,641	1,662
Professional Fees and Regulatory Assessments	1,160	1,036	1,516
Furniture and Equipment	935	1,017	1,081
FDIC Insurance	1,128	404	&