BAY NATIONAL CORP
Form 10-K
March 31, 2003

[GRAPHIC OMITTED][GRAPHIC OMITTED]

FORM 10-KSB
U.S. Securities and Exchange Commission
Washington, D.C. 20549

(Mark One)

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the year ended December 31, 2002

[ ] TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 333-87781

Bay National Corporation
(Name of small business issuer in its charter)

Maryland	52-2176710
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2328 West Joppa Road, Lutherville, Maryland 21093
(Address of principal executive offices) (Zip Code)

Issuer's telephone number: 410-494-2580

Securities registered under Section 12(b) of the Exchange Act: None

Securities registered under Section 12(g) of the Exchange Act: Common stock, par value $1.00 per share

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No __

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. [x]

The issuer's revenues for its most recent fiscal year were $4,204,032.

The aggregate market value of the common equity held by non-affiliates was $8,407,980 as of March 24, 2003, based on a sales price of $9.00 per share of Common Stock, which is the sales price at which shares of Common Stock were last sold in over the counter trading on March 24, 2003.

The number of shares outstanding of the issuer's Common Stock was 1,242,020 as of March 24, 2003.

Transitional Small Business Disclosure Format (check one):

Yes __ No X

PART I

Item 1. Description of Business

General

Bay National Corporation was incorporated under the laws of the State of Maryland on June 3, 1999, primarily to serve as a bank holding company for a proposed federally chartered commercial bank to be named Bay National Bank.

Bay National Bank commenced operations on May 12, 2000 with its main office in North Baltimore, Maryland and a branch office in Salisbury, Maryland. Bay National Bank accepts checking and savings deposits and offers a wide range of commercial and industrial, real estate, consumer and residential mortgage loans.

Marketing Focus

Bay National Bank was formed by a group of individuals active in business, professional, banking, financial and charitable activities in the Baltimore, Maryland metropolitan area and the Eastern Shore of Maryland. These individuals believed that the banking needs of certain segments of these communities were not being served adequately by existing banks. Specifically, as a result of bank mergers in the 1990's, many banks in the Baltimore metropolitan area and the Eastern Shore of Maryland became local branches of large regional and national banks. Although size gave the larger banks some advantages in competing for business from large corporations, including economies of scale and higher lending limits, the organizers believed that these "megabanks" were focused on a mass market approach which de-emphasized personal contact and service. The organizers also believed that the centralization of decision-making power at these large institutions had resulted in a lack of customer service. At many of these institutions, determinations were made at the "home office" by individuals who lacked personal contact with customers as well as an understanding of the customers' needs and scope of the relationship with the institution.

Bay National Bank's management believes that this trend is ongoing, and has been particularly frustrating to owners of small and mid-sized businesses, business professionals and high net worth individuals who traditionally were accustomed to dealing directly with a bank executive who had an understanding of their banking needs with the ability to deliver a prompt response.

Bay National Bank targets its commercial banking services to small and mid-sized businesses and targets its retail banking services to the owners of these businesses and their employees, to business professionals and high net worth individuals.

Bay National Bank seeks to distinguish itself by

- Developing personal relationships with its customers.
- Customizing its products to fit the needs of its customers instead of adopting a "one size fits all" mentality.
- Streamlining the decision making process.
- Offering its customers additional complementary services, such as insurance and investment advice, through relationships with strategic partners.

Bay National Bank's offices are not organized in the traditional retail branch structure, which is transaction and "bank teller" oriented. Instead, Bay National Bank has adopted a "sit-down" model where customers are greeted by a personal banker and taken to a private desk. We believe that this approach makes service more individualized and enhances the banker's understanding of the customer's needs. Furthermore, Bay National Bank's branch locations do not focus on capturing every customer within the surrounding area. Instead, they are strategically located in areas convenient to Bay National Bank's target customer base.

Market Area and Facilities

Bay National Bank's headquarters and Baltimore branch office are located at 2328 West Joppa Road, Lutherville, Maryland 21093. Bay National Bank serves the Baltimore metropolitan area from that location, with its primary service area being Towson, Lutherville-Timonium, Cockeysville, Hunt Valley, Ruxton and Roland Park. Bay National Bank's Salisbury, Maryland branch office is located at 109 Poplar Hill Avenue, Salisbury, Maryland 21801, from which it serves Maryland's Eastern Shore.

Products and Services

Loan Portfolio.

Bay National Bank offers a full range of loans, including commercial and industrial loans, real estate loans, consumer loans and residential mortgage and home equity loans. Commercial business and commercial real estate loans for owner-occupied properties are Bay National Bank's primary loan products, accounting for approximately 75% of the loan portfolio as of December 31, 2002.

Generally, Bay National Bank is subject to a lending limit to any one borrower of 15% of Bay National Bank's unimpaired capital and surplus. However, management is able to originate loans and to participate with other lenders in loans that exceed Bay National Bank's lending limits.

The following is a description of the types of loans Bay National Bank has targeted in building its loan portfolio:

- Commercial and industrial loans for business purposes including working capital, equipment purchases, lines of credit and government contract financing. Asset-based lending, accounts receivable financing and lease financing are also available. As of December 31, 2002, these loans represented approximately 62% of Bay National Bank's loan portfolio. Bay National Bank is targeting small and mid-sized businesses in its market area with credit needs in the range of up to $5,000,000.

- Non-mortgage real estate loans, including land development and construction loan financing, primarily for owner-occupied premises. As of December 31, 2002, these loans represented approximately 11% of Bay National Bank's loan portfolio.

- Consumer loans including automobile and personal loans. In addition, Bay National Bank offers personal lines of credit. As of December 31, 2002, these loans represented approximately 6% of Bay National Bank's loan portfolio. Bay National Bank's consumer loans are targeted to business owners and their employees, business professionals and high net worth individuals.

- Residential mortgage loans, including first and second mortgage loans on owner occupied and investment properties, and home equity loans secured by single-family owner-occupied residences. As of December 31, 2002, these loans represented approximately 21% of Bay National Bank's loan portfolio. Like its consumer loans, Bay National Bank's residential mortgage loans are targeted to business owners and their employees, business professionals and high net worth individuals.

  Bay National Bank's conventional first and second residential mortgage loans adhere to standards developed by FNMA/FHLMC. Management requires private mortgage insurance for loans in excess of 80% of a property's value. Bay National Bank sells most of its first and second residential mortgage loans in the secondary market. Therefore, management sells those loans that have a lower degree of risk, and a lower yield, relative to the other types of loans that Bay National Bank is expected to make. As of December 31, 2002, mortgage loans held for sale, totaled $2,818,500.

Deposits.

Bay National Bank offers a wide range of interest-bearing and non-interest-bearing accounts, including commercial and retail checking accounts, money market accounts, individual retirement accounts, interest-bearing statement savings accounts and certificates of deposit with fixed and variable rates and a range of maturity date options.

Other Banking and Financial Services.

Bay National Bank offers commercial customers cash management services such as sweep accounts, account reconciliation, lockbox services and wire transfers of funds. Additionally, Bay National Bank makes available telephone banking, ATM/debit cards, safe keeping boxes, after-hours deposit services, travelers checks, direct deposit of payroll and automatic drafts for various accounts. These services are provided either directly by Bay National Bank or through correspondent banking relationships. Bay National Bank does not have it's own network of ATM machines. In general, Bay National Bank waives fees on a predetermined number of ATM transactions per month, thereby allowing its customers to use any ATM machine.

In addition, Bay National Bank's customers are able to access information about their accounts and view information about Bay National Bank's services and products on Bay National Bank's website, which is located at http://www.baynational.com. Bay National Bank's website also permits customers to make transfers of funds among accounts, pay bills, and send e-mail to Bay National Bank personnel.

Bay National Bank offers, through strategic partners, investment advisory, risk management and employee benefit services. Through these affiliations, banking clients can receive a full range of financial

services, including investment advice, personal and business insurance products and employee benefit products such as pension and 401(k) plan administration. To the extent permitted by applicable regulations, the strategic partners may share fees and commissions with Bay National Bank. As of December 31, 2002, Bay National Bank had not entered in to any such fee arrangements. When sufficient volume is developed in any of these lines of business, Bay National Bank may provide these services if permitted by applicable regulations.

Competition

Deregulation of financial institutions and acquisitions of banks across state lines has resulted in widespread changes in the financial services industry. In both the Baltimore metropolitan area and on Maryland's Eastern Shore, Bay National Bank faces strong competition from large banks headquartered within and outside of Maryland. Bay National Bank also competes with other community banks, savings and loan associations, credit unions, mortgage companies, finance companies and others providing financial services. In addition, insurance companies, securities brokers and other non-bank entities or their affiliates may provide services, which historically have been considered banking in nature.

Many of Bay National Bank's competitors can finance extensive advertising campaigns, maintain extensive branch networks and technology investments, and offer services, which Bay National Bank cannot offer or will not offer initially. Also, larger institutions have substantially higher lending limits than Bay National Bank. Some of Bay National Bank's competitors have other advantages, such as tax exemption in the case of credit unions, and lesser regulation in the case of mortgage companies and finance companies.

Employees

As of March 25, 2003, Bay National Bank employed twenty-eight individuals. Nineteen people operate from Bay National Bank's headquarters and banking office in North Baltimore and nine people from the Salisbury, Maryland banking office. Bay National Corporation has no employees.

Supervision and Regulation

Bay National Corporation and Bay National Bank are subject to extensive regulation under state and federal banking laws and regulations. These laws impose specific requirements and restrictions on virtually all aspects of operations and generally are intended to protect depositors, not stockholders. The following discussion is only a summary and readers should refer to particular statutory and regulatory provisions for more detailed information. In addition, management cannot predict the nature or the extent of the effect on business and earnings that new federal or state legislation may have in the future.

Bay National Corporation.

Federal Bank Holding Company Regulation. Bay National Corporation is a bank holding company registered under the Bank Holding Company Act of 1956, as amended, and is subject to supervision by the Federal Reserve Board. As a bank holding company, Bay National Corporation is required to file with the Federal Reserve Board an annual report and such other additional information as the Federal Reserve Board may require by statute. The Federal Reserve Board may also examine Bay National Corporation and each of its subsidiaries.

The Federal Reserve Board must approve, among other things, the acquisition by a bank holding company of control of more than five percent (5%) of the voting shares, or substantially all the assets, of any bank or bank holding company or the merger or consolidation by a bank holding company with another bank holding company. Under the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, the

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restrictions on interstate acquisitions of banks by bank holding companies were repealed as of September 29, 1995. The effect of the repeal of these restrictions is that, subject to certain time and deposit base requirements, Bay National Corporation may acquire a bank located in Maryland or any other state, and a bank holding company located outside of Maryland can acquire any Maryland-based bank holding company or bank.

Unless it chooses to become a financial holding company, as further described below, a bank holding company is prohibited from acquiring control of any voting shares of any company which is not a bank or bank holding company and from engaging directly or indirectly in any activity other than banking, or managing or controlling banks or furnishing services for its authorized subsidiaries. There are limited exceptions. A bank holding company may, for example, engage in activities which the Federal Reserve Board has determined by order or regulation to be so closely related to banking or managing or controlling banks as to be "properly incident thereto." In making such a determination, the Federal Reserve Board is required to consider whether the performance of such activities can reasonably be expected to produce benefits to the public, such as convenience, increased competition or gains in efficiency, which outweigh possible adverse effects, such as undue concentration of resources, decreased or unfair competition, conflicts of interest or unsound banking practices. The Federal Reserve Board is also empowered to differentiate between activities commenced de novo and activities commenced by the acquisition, in whole or in part, of a going concern. Some of the activities that the Federal Reserve Board has determined by regulation to be closely related to banking include servicing loans, performing certain data processing services, acting as a fiduciary, investment or financial advisor, and making investments in corporations or projects designed primarily to promote community welfare.

Subsidiary banks of a bank holding company are subject to certain restrictions imposed by statute on any extensions of credit to the bank holding company or any of its subsidiaries, or investments in their stock or other securities, and on taking such stock or securities as collateral for loans to any borrower. Further, a bank holding company and any subsidiary bank are prohibited from engaging in certain tie-in arrangements in connection with the extension of credit. In 1997, the Federal Reserve Board adopted amendments to its Regulation Y, creating exceptions to the Bank Holding Company Act's anti-tying prohibitions that give bank subsidiaries of holding companies greater flexibility in packaging products and services with their affiliates.

In accordance with Federal Reserve Board policy, Bay National Corporation is expected to act as a source of financial strength to Bay National Bank and to commit resources to support Bay National Bank in circumstances in which Bay National Corporation might not otherwise do so. The Federal Reserve Board may require a bank holding company to terminate any activity or relinquish control of a non-bank subsidiary (other than a non-bank subsidiary of a bank) upon the Federal Reserve's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any subsidiary depository institution of the bank holding company. Further, federal bank regulatory authorities have additional discretion to require a bank holding company to divest itself of any bank or non-bank subsidiary if the agency determines that divestiture may aid the depository institution's financial condition.

On November 12, 1999, President Clinton signed into law the Gramm-Leach-Bliley Act ("GLBA"). Effective March 11, 2000, pursuant to authority granted under the GLBA, a bank holding company may elect to become a financial holding company and thereby engage in a broader range of financial and other activities than are permissible for traditional bank holding companies. In order to qualify for the election, all of the depository institution subsidiaries of the bank holding company must be well capitalized and well managed, as defined by regulation, and all of its depository institution subsidiaries must have achieved a rating of satisfactory or better with respect to meeting community credit needs.

Pursuant to the GLBA, financial holding companies will be permitted to engage in activities that are "financial in nature" or incidental or complementary thereto, as determined by the Federal Reserve Board.

The GLBA identifies several activities as "financial in nature," including, among others, insurance underwriting and agency, investment advisory services, merchant banking and underwriting, and dealing or making a market in securities. Being designated a financial holding company will allow insurance companies, securities brokers and other types of financial companies to affiliate with and/or acquire depository institutions.

The Federal Reserve Board imposes risk-based capital measures on bank holding companies in order to insure their capital adequacy. As a bank holding company with less than $150,000,000 in assets, Bay National Corporation initially is exempt from most of these risk-based capital measures. However, the Federal Reserve Board still requires that Bay National Corporation remain adequately capitalized and have the ability to retire any debt within 25 years from the date it is incurred.

The status of Bay National Corporation as a registered bank holding company under the Bank Holding Company Act does not exempt it from certain federal and state laws and regulations applicable to corporations generally, including, without limitation, certain provisions of the federal securities laws.

State Bank Holding Company Regulation. Bay National Corporation is a Maryland-chartered bank holding company and is subject to various restrictions on its activities as set forth in Maryland law, in addition to those restrictions set forth in federal law.

Under Maryland law, a bank holding company that desires to acquire a

Maryland state-chartered bank or trust company, a federally chartered bank with its main office in Maryland, or a bank holding company that has its principal place of business in Maryland, must file an application with the Maryland Commissioner of Financial Regulation (the "Commissioner"). In approving the application, the Commissioner must consider whether the acquisition may be detrimental to the safety and soundness of the entity being acquired or whether the acquisition may result in an undue concentration of resources or a substantial reduction in competition in Maryland. The Commissioner may not approve an acquisition if, on consummation of the transaction, the acquiring company, together with all its insured depository institution affiliates, would control 30% or more of the total amount of deposits of insured depository institutions in Maryland. The Commissioner has authority to adopt by regulation a procedure to waive this requirement for good cause. In a transaction for which the Commissioner's approval is not required due to an exemption under Maryland law, or for which federal law authorizes the transaction without application to the Commissioner, the parties to the acquisition must provide written notice to the Commissioner at least 15 days before the effective date of the acquisition.

Bay National Bank.

General. Bay National Bank, as a national banking association whose accounts are insured by the Bank Insurance Fund ("BIF") of the Federal Deposit Insurance Corporation ("FDIC") up to the maximum legal limits, is subject to regulation, supervision and regular examinations by the Office of the Comptroller of the Currency ("OCC"). Bay National Bank is a member of the Federal Reserve System and, as such, is subject to certain regulations issued by the Federal Reserve Board. Bay National Bank also is subject to applicable banking provisions of Maryland law insofar as they do not conflict with or are not preempted by federal law. The regulations of these various agencies govern most aspects of Bay National Bank's business, including setting required reserves against deposits, loans, investments, mergers and acquisitions, borrowing, dividends and location and number of branch offices.

The GLBA authorizes expanded activities for national banks, but requires (with the exception of underwriting municipal revenue bonds and other state and local obligations) that any expanded activities be conducted in a new entity called a "financial subsidiary" that is a subsidiary of the bank rather than the bank itself. A financial subsidiary may engage in any activities in which a financial holding company or a

financial holding company's non-bank subsidiaries can engage, except that a financial subsidiary may not underwrite most insurance, engage in real estate development or conduct merchant banking activities. A financial subsidiary may be established through acquisition or de novo.

In order for a national bank to operate a financial subsidiary, it must be well capitalized and well managed, have a satisfactory or better rating with respect to meeting community credit needs and the aggregate assets of all of the bank's financial subsidiaries may not exceed 45% of the total assets of the bank, subject to certain exceptions. Existing authority of the OCC and the FDIC to review subsidiary activities are preserved.

Banking is a business which depends on interest rate differentials. In general, the differences between the interest paid by a bank on its deposits and its other borrowings and the interest received by a bank on loans extended to its customers and securities held in its investment portfolio constitute the major portion of a bank's earnings. Thus, the earnings and growth of Bay

National Bank will be subject to the influence of economic conditions generally, both domestic and foreign, and also on the monetary and fiscal policies of the United States and its agencies, particularly the Federal Reserve Board, which regulates the supply of money.

Branching and Interstate Banking. Beginning on June 1, 1997, the federal banking agencies were authorized to approve interstate bank merger transactions without regard to whether such a transaction is prohibited by the law of any state, unless the home state of one of the banks has opted out of the interstate bank merger provisions of the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994. Furthermore, under the Riegle-Neal Act, interstate acquisitions of branches are permitted if the law of the state in which the branch is located permits such acquisitions. The Riegle-Neal Act also authorizes the OCC and FDIC to approve interstate branching de novo by national and non-member banks, respectively, but only in states which specifically allow for such branching.

The District of Columbia, Maryland, Delaware and Pennsylvania have all enacted laws which permit interstate acquisitions of banks and bank branches and permit out-of-state banks to establish de novo branches.

Capital Adequacy Guidelines. The Federal Reserve Board, the OCC and the FDIC have all adopted risk-based capital adequacy guidelines by which they assess the adequacy of capital in examining and supervising banks and bank holding companies and in analyzing bank regulatory applications. Risk-based capital requirements determine the adequacy of capital based on the risk inherent in various classes of assets and off-balance sheet items.

Since December 31, 1992, national banks have been expected to meet a minimum ratio of total qualifying capital (the sum of core capital (Tier 1) and supplementary capital (Tier 2)) to risk-weighted assets (a "Total Risk-Based Capital Ratio") of 8%. At least half of this amount (4%) should be in the form of core capital. These requirements apply to Bay National Bank.

Tier 1 capital for national banks generally consists of the sum of common stockholders' equity and perpetual preferred stock (subject in the case of the latter to limitations on the kind and amount of such stock which may be included as Tier 1 capital), less goodwill, without adjustment in accordance with Statement of Financial Accounting Standards No. 115. Tier 2 capital consists of the following: hybrid capital instruments, perpetual preferred stock which is not otherwise eligible to be included as Tier 1 capital, term subordinated debt and intermediate-term preferred stock, and, subject to limitations, general allowances for loan losses. Assets are adjusted under the risk-based guidelines to take into account different risk characteristics, with the categories ranging from 0% (requiring no risk-based capital) for assets such as cash, to 100% for the bulk of assets which are typically held by a bank holding company, including certain multi-family residential and commercial real estate loans, commercial business loans and consumer loans. Residential first mortgage loans

on one-to-four-family residential real estate and certain seasoned multi-family residential real estate loans, which are not 90 days or more past-due or non-performing and which have been made in accordance with prudent underwriting standards, are assigned a 50% level in the risk-weighing system, as are certain privately issued mortgage-backed securities representing indirect ownership of such loans. Off-balance sheet items also are adjusted to take into account certain risk characteristics.

In addition to the risk-based capital requirements, the OCC has established a minimum 3% Leverage Capital Ratio (Tier 1 capital to total adjusted assets) requirement for the most highly-rated national banks, with an additional cushion of at least 100 to 200 basis points for all other national banks, which effectively increases the minimum Leverage Capital Ratio for such other banks to 4%-5% or more. Under the OCC's regulations, highest-rated banks are those that the OCC determines are not anticipating or experiencing significant growth and have well diversified risk, including no undue interest rate risk exposure, excellent asset quality, high liquidity, good earnings and, in general, those which are considered a strong banking organization. A national bank that has less than the minimum Leverage Capital Ratio requirement must submit to the applicable district office for review and approval a reasonable plan describing the means and timing by which the bank will achieve its minimum Leverage Capital Ratio requirement. A national bank which fails to file such a plan is deemed to be operating in an unsafe and unsound manner and could be subject to a cease-and-desist order.

The OCC's regulations also provide that any insured depository institution with a Leverage Capital Ratio less than 2% is deemed to be operating in an unsafe or unsound condition. Operating in an unsafe or unsound manner could lead the FDIC to terminate deposit insurance. However, such an institution will not be subject to an enforcement proceeding solely on account of its capital ratios if it has entered into and is in compliance with a written agreement with the OCC to increase its Leverage Capital Ratio to such level as the OCC deems appropriate and to take such other action as may be necessary for the institution to be operated in a safe and sound manner. The capital regulations also provide, among other things, for the issuance by the OCC or its designee(s) of a capital directive, which is a final order issued to a bank that fails to maintain minimum capital or to restore its capital to the minimum capital requirement within a specified time period. Such directive is enforceable in the same manner as a final cease-and-desist order.

Prompt Corrective Action. Each federal banking agency is required to implement a system of prompt corrective action for institutions which it regulates. Under applicable regulations, a bank will be deemed to be: (i) "well capitalized" if it has a Total Risk-Based Capital Ratio of 10% or more, a Tier 1 Risk-Based Capital Ratio of 6% or more, a Leverage Capital Ratio of 5% or more and is not subject to any written capital order or directive; (ii) "adequately capitalized" if it has a Total Risk-Based Capital Ratio of 8% or more, a Tier 1 Risk-Based Capital Ratio of 4% or more and a Leverage Capital Ratio of 4% or more (3% under certain circumstances); (iii) "undercapitalized" if it has a Total Risk-Based Capital Ratio that is less than 8%, a Tier 1 Risk-Based Capital Ratio that is less than 4% or a Leverage Capital Ratio that is less than 4% (3.3% under certain circumstances); (iv) "significantly undercapitalized" if it has a Total Risk-Based Capital Ratio that is less than 6%, a Tier 1 Risk-Based Capital Ratio that is less than 3% or a Leverage Capital Ratio that is less than 3%; and (v) "critically undercapitalized" if it has a ratio of tangible equity to total assets that is equal to or less than 2%. Bay National Bank is "well capitalized" as of December 31, 2002.

An institution generally must file a written capital restoration plan which meets specified requirements with an appropriate federal banking agency within 45 days of the date the institution receives notice or is deemed to have notice that it is undercapitalized, significantly undercapitalized or critically undercapitalized. The federal banking agency must provide the institution with written notice of approval or disapproval within 60 days after receiving the capital restoration plan, subject to extensions by the applicable agency.

An institution which is required to submit a capital restoration plan must concurrently submit a performance guaranty by each company that controls the institution. Such guaranty is limited to the lesser of

(i) an amount equal to 5% of the institution's total assets at the time the institution was notified or deemed to have notice that it was undercapitalized or (ii) the amount necessary at such time to restore the relevant capital measures of the institution to the levels required for the institution to be classified as adequately capitalized. Such a guaranty expires after the federal banking agency notifies the institution that it has remained adequately capitalized for each of four consecutive calendar quarters. An institution which fails to submit a written capital restoration plan within the requisite period, including any required performance guaranty, or fails in any material respect to implement a capital restoration plan, is subject to the restrictions in Section 38 of the Federal Deposit Insurance Act which are applicable to significantly undercapitalized institutions.

A critically undercapitalized institution will be placed in conservatorship or receivership within 90 days unless the FDIC formally determines that forbearance from such action would better protect the deposit insurance fund. Unless the FDIC or another appropriate federal banking regulatory agency makes specific further findings and certifies that the institution is viable and is not expected to fail, an institution that remains critically undercapitalized on average during the four calendar quarters after the date it becomes critically undercapitalized must be placed in receivership.

Immediately upon becoming undercapitalized, an institution becomes subject to statutory provisions which (i) restrict payment of capital distributions and management fees; (ii) require that the appropriate federal banking agency monitor the condition of the institution and its efforts to restore its capital; (iii) require submission of a capital restoration plan; (iv) restrict the growth of the institution's assets and (v) require prior approval of certain expansion proposals. The appropriate federal banking agency for an undercapitalized institution also may take any number of discretionary supervisory actions if the agency determines that any of these actions is necessary to resolve the problems of the institution at the least possible long-term cost to the deposit insurance fund, subject in certain cases to specified procedures. These discretionary supervisory actions include requiring the institution to raise additional capital, restricting transactions with affiliates, requiring divestiture of the institution or the sale of the institution to a willing purchaser, and any other supervisory action that the agency deems appropriate. Significantly undercapitalized and critically undercapitalized institutions are subject to these and additional mandatory and permissive supervisory actions.

Regulatory Enforcement Authority. The Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA") included substantial enhancement to the enforcement powers available to federal banking regulators. This enforcement authority included, among other things, the ability to assess civil money penalties, to issue cease-and-desist or removal orders and to initiate injunctive actions against banking organizations and institution-affiliated parties, as defined in FIRREA. In general, these enforcement actions may be initiated for violations of laws and regulations and unsafe or unsound practices. Other actions or inactions may provide the basis for enforcement action, including misleading or untimely reports filed with regulatory authorities. FIRREA significantly increased the amount of and grounds for civil money penalties and requires, except under certain circumstances, public disclosure of final enforcement actions by the federal banking agencies.

Deposit insurance. The FDIC has adopted a risk-based deposit insurance assessment system. The FDIC assigns an institution to one of three capital categories based on the institution's financial information, as of the reporting period ending seven months before the assessment period, consisting of (i) well capitalized, (ii) adequately capitalized or (iii) undercapitalized, and one of three supervisory subcategories within each capital group. The supervisory subgroup to which an institution is assigned is based on a supervisory evaluation provided to the FDIC by the institution's primary federal regulator and information that the FDIC determines to be relevant to the institution's financial condition and the risk posed to the deposit insurance funds. An institution's assessment rate depends on the capital category and supervisory subcategory to which it is assigned. Assessment rates for BIF deposits currently range from 0 basis points to

27 basis points. As a new bank, Bay National Bank was initially assigned to a capital and supervisory subcategory that has an assessment rate of 0. The FDIC is authorized to raise the assessment rates in certain circumstances, including to maintain or achieve the designated reserve ratio of 1.25%, which requirement the BIF currently meets. The FDIC has exercised its authority to raise rates in the past and may raise insurance premiums in the future. If such action is taken by the FDIC, it could have an adverse effect on the earnings of Bay National Bank.

Under the Federal Deposit Insurance Act, insurance of deposits may be terminated by the FDIC upon a finding that the institution has engaged in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

Transactions with Affiliates and Insiders. Bay National Bank is subject to the provisions of Section 23A of the Federal Reserve Act, which place limits on the amount of loans or extensions of credit to affiliates, investments in or certain other transactions with affiliates and on the amount of advances to third parties collateralized by the securities or obligations of affiliates. Section 23A limits the aggregate amount of transactions with any individual affiliate to ten percent (10%) of the capital and surplus of Bay National Bank and also limits the aggregate amount of transactions with all affiliates to twenty percent (20%) of capital and surplus. Loans and certain other extensions of credit to affiliates are required to be secured by collateral in an amount and of a type described in Section 23A, and the purchase of low quality assets from affiliates is generally prohibited.

Bay National Bank also is subject to the provisions of Section 23B of the Federal Reserve Act which, among other things, prohibit an institution from engaging in certain transactions with certain affiliates unless the transactions are on terms substantially the same, or at least as favorable to such institution and/or its subsidiaries, as those prevailing at the time for comparable transactions with non-affiliated entities. In the absence of comparable transactions, such transactions may only occur under terms and circumstances, including credit standards that in good faith would be offered to or would apply to non-affiliated companies.

Bay National Bank also is subject to the restrictions contained in Section 22(h) of the Federal Reserve Act and the Federal Reserve Board's Regulation O thereunder on loans to executive officers, directors and principal stockholders. Under Section 22(h), loans to a director, an executive officer or a greater-than-10% stockholder of a bank as well as certain affiliated interests of any of the foregoing may not exceed, together with all other outstanding loans to such person and affiliated interests, the loans-to-one-borrower limit applicable to national banks (generally 15% of the institution's unimpaired capital and surplus), and all loans to all such persons in the aggregate may not exceed the institution's unimpaired capital and unimpaired surplus. Regulation O also prohibits the making of loans in an amount greater than $25,000 or 5% of capital and surplus but in any event not over $500,000, to directors, executive officers and greater-than-10% stockholders of a bank, and their respective affiliates, unless such loans are approved in advance by a majority of the Board of Directors of the bank with any "interested" director not participating in the voting. Further, Regulation O requires that loans to directors, executive officers and principal stockholders be made on terms substantially the same as those that are offered in comparable transactions to other persons. Regulation O also prohibits a depository institution from paying overdrafts over $1,000 of any of its executive officers or directors unless they are paid pursuant to written pre-authorized extension of credit or transfer of funds plans.

Loans to One Borrower. As a national bank, Bay National Bank is subject to the statutory and regulatory limits on the extension of credit to one borrower. Generally, the maximum amount of total outstanding loans that a national bank may have to any one borrower at any one time is 15% of the bank's unimpaired capital and surplus. A national bank may lend an additional 10% on top of the 15% if the amount

that exceeds 15% of the bank's unimpaired capital and surplus is fully secured by readily marketable collateral.

Liquidity. Bay National Bank is subject to the reserve requirements of Federal Reserve Board Regulation D, which applies to all depository institutions. Specifically, amounts in Bay National Bank's transaction accounts above $5,000,000 and under $44,300,000 must have reserves held against them in the ratio of three percent (3%) of the amount.

Community Reinvestment Act. The Community Reinvestment Act ("CRA") requires that, in connection with examinations of financial institutions within their respective jurisdictions, the Federal Reserve Board, the FDIC, the OCC or the Office of Thrift Supervision shall evaluate the record of the financial institutions in meeting the credit needs of their local communities, including low and moderate income neighborhoods, consistent with the safe and sound operation of those institutions. The 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, consistent with the CRA. An institution's CRA activities are considered in, among other things, evaluating mergers, acquisitions and applications to open a branch or facility as well as determining whether the institution will be permitted to exercise certain of the powers allowed by the GLBA. The CRA also requires all institutions to make public disclosure of their CRA ratings.

USA PATRIOT Act. On October 26, 2001, the President signed into law comprehensive anti-terrorism legislation known as the USA PATRIOT Act of 2001 (the "USA Patriot Act"). Title III of the USA Patriot Act substantially broadened the scope of U.S. anti-money laundering laws and regulations by imposing significant new compliance and due diligence obligations, creating new crimes and penalties and expanding the extra-territorial jurisdiction of the United States. The U.S. Treasury Department ("Treasury") has issued a number of implementing regulations which apply to various requirements of the USA Patriot Act to financial institutions such as Bay National Bank. Those regulations impose new obligations on financial institutions to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. Treasury is expected to issue a number of additional regulations which will further clarify the USA Patriot Act's requirements.

Failure of a financial institution to comply with the USA Patriot Act's requirements could have serious legal and reputational consequences for the institution. The Company has adopted appropriate policies, procedures and controls to address compliance with the requirements of the USA Patriot Act under the existing regulations and will continue to revise and update its policies, procedures and controls to reflect changes required by the USA Patriot Act and Treasury's regulations.

Factors Affecting Future Results

Some of the information in this annual report includes "forward-looking statements." These statements use words such as "may," "will," "expect," "anticipate," "plan," "estimate" or similar words, and they discuss future expectations, projections of financial results or strategies that are subject to risks and uncertainties. When you read a forward-looking statement, you should keep in mind the risk factors described below and any other information contained in this annual report which identifies a risk or uncertainty. Bay National Corporation's actual results and the actual outcome of Bay National Corporation's expectations and strategies could be different from that described in this annual report because of these risks and uncertainties and you should not put undue reliance on any forward-looking statements. All forward-looking statements speak only as of the date of this filing, and Bay National Corporation undertakes no obligation to make any revisions to the forward-looking statements to reflect events or circumstances after the date of this filing or to reflect the occurrence of unanticipated events.

Bay National Corporation has limited operating history upon which to evaluate future success, and Bay National Corporation does not expect to be profitable initially. Bay National Corporation and Bay National Bank commenced operations in May 2000, and their operating history is limited. Bay National Corporation's profitability depends on the results of operations of its principal asset, Bay National Bank. Bay National Corporation incurred operating losses during each of the years ended December 31, 2002, 2001 and 2000, and management expects that Bay National Corporation will continue to incur operating losses and may not achieve profitability, if at all, until the second or third quarter of 2003. In addition, management expects that additional capital may be required in the future to support growth of Bay National Bank.

If Bay National Bank decides to open additional offices, that decision may further delay profitability because of the increased expenses of expansion and because the new branch offices may not enhance the results of operations as anticipated. Bay National Bank has no current plans to open additional branch offices.

Bay National Corporation and Bay National Bank depend heavily on one key employee, Mr. Hugh W. Mohler, and business would suffer if something were to happen to Mr. Mohler. Mr. Mohler is the Chairman, President and Chief Executive Officer of Bay National Bank. If he were to leave for any reason, Bay National Corporation's and Bay National Bank's business would suffer because he has banking experience and relationships with clients and potential clients that would not be easy to replace. In addition, because Bay National Bank's business is relationship driven, the loss of an employee who has primary contact with one or more of Bay National Bank's clients could cause Bay National Bank to lose those clients' business, possibly resulting in a decline in revenues.

Bay National Bank's lending strategy involves risks resulting from the choice of loan portfolio. Bay National Bank's loan strategy emphasizes commercial business loans and commercial real estate loans. At December 31, 2002, such loans accounted for approximately 75% of the loan portfolio. Bay National Bank also offers construction loans, consumer loans and mortgage loans for owner-occupied residential properties, although most of the residential mortgage loans are sold in the secondary market. Commercial business and commercial real estate loans generally carry a higher degree of credit risk than do residential mortgage loans because of several factors including larger loan balances, dependence on the successful operation of a business or a project for repayment, or loan terms with a balloon payment rather than full amortization over the loan term.

Bay National Bank's lending limit may limit its growth and the growth of Bay National Corporation. Bay National Bank is limited in the amount it can loan to a single borrower by the amount of its capital. Specifically, under current law, Bay National Bank may lend up to 15% of its unimpaired capital and surplus to any one borrower. Furthermore, until Bay National Bank is profitable, Bay National Bank's capital will decrease which will result in a decrease to the lending limit. Bay National Bank's lending limit is significantly less than that of many of its competitors and may discourage potential borrowers who have credit needs in excess of Bay National Bank's lending limit from conducting business with Bay National Bank. Management is often able to accommodate larger loans by selling participations in those loans to other financial institutions.

Bay National Bank faces substantial competition which could adversely affect its ability to attract depositors and borrowers. Bay National Bank operates in a competitive market for financial services and faces intense competition from other institutions both in making loans and in attracting deposits. Many of these institutions have been in business for many years, are significantly larger, have established customer bases, have greater financial resources and lending limits than Bay National Bank, and are able to offer certain services that Bay National Bank is not able to offer. If Bay National Bank cannot attract deposits and make loans at a sufficient level, its operating results will suffer, as will its opportunities for growth.

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Government regulation could restrict Bay National Corporation's or Bay National Bank's growth or cause Bay National Corporation or Bay National Bank to incur higher costs. Bay National Corporation and Bay National Bank operate in a highly regulated environment and are subject to examination, supervision and comprehensive regulation by several federal and state regulatory agencies. Banking regulations, designed primarily for the safety of depositors, may limit the growth of Bay National Bank and the return to investors by restricting activities such as the payment of dividends; mergers with, or acquisitions by, other institutions; investments; loans and interest rates; interest rates paid on deposits; and the creation of branch offices. Laws and regulations could change at any time, and changes could adversely affect Bay National Corporation's and Bay National Bank's business. In addition, the cost of compliance with regulatory requirements could adversely affect Bay National Corporation's and Bay National Bank's ability to operate profitably.

Bay National Bank's ability to compete may suffer if it cannot take advantage of technology to provide banking services or if its customers fail to embrace that technology. Bay National Bank's business strategy relies less on customers' access to a large branch network and more on access to technology and personal relationships. Further, the market for financial services is increasingly affected by advances in technology, including developments in telecommunications, data processing, computers, automation, Internet-based banking, telephone banking, debit cards and so-called "smart" cards. Bay National Bank's ability to compete successfully may depend on the extent to which Bay National Bank can take advantage of technological changes and the extent to which Bay National Bank's customers embrace technology to complete their banking transactions.

Item 2. Description of Property

On July 16, 1999, Bay National Corporation entered into two lease agreements for its main office, which is located at 2328 West Joppa Road, Lutherville, Maryland 21093.

The first lease, which commenced on July 26, 1999, is for 947 square feet of space. This space, which is on the first floor of a three-story building, was initially used for administrative office space. Upon the opening of Bay National Bank, this space became Bay National Bank's Baltimore branch office. The lease term runs for five years and five months. Bay National Corporation has the option to extend the term of this lease for one five-year renewal term. During the first year of the lease term, Bay National Corporation paid monthly rent of approximately $1,900, which amount increases at the rate of four percent per year. The monthly rent as of December 31, 2002 was $2,138. The monthly rent includes Bay National Corporation's share of taxes and building operating costs.

The second lease, which commenced on March 1, 2000, is for 5,130 square feet of space and runs for five years. Approximately 3,400 square feet of this space, which is on the third floor of the same building, is used for Bay National Corporation and Bay National Bank's administrative offices. Bay National Corporation also has the option to extend the term of this lease for one five-year renewal term. During the first year of the lease term, Bay National Corporation paid monthly rent of approximately $10,773, which amount increases at the rate of four percent per year. The monthly rent as of December 31, 2002 was $11,652. The monthly rent includes Bay National Corporation's share of taxes and building operating costs. Beginning April 1, 2000, Bay National Corporation sublet approximately 1,800 square feet of this space for a three-year term at a monthly rent for the first year of $3,173, which amount increases at the rate of four percent per year. The monthly rent as of December 31, 2002 was $3,432. Upon the termination of the sublease in March 2003, management will convert a portion of this space for use by Bay National Corporation and Bay National Bank and will attempt to enter into a new sublease agreement for the remaining space. The additional space will be used to accommodate current and future growth.

On September 16, 1999, Bay National Corporation entered into a lease agreement for Bay National Bank's Salisbury, Maryland branch office, which is located at 109 Poplar Hill Avenue, Salisbury Maryland

21801 in a two-story building containing approximately 2,500 square feet of office space. This lease, which became effective as of September 1, 1999, is for a term of five years with Bay National Corporation having the option to extend the term for three five-year renewal terms. During the initial lease term, Bay National Corporation is paying monthly rent of approximately $1,980, plus all real estate taxes and utilities. Pursuant to this lease, Bay National Corporation has a right of first refusal to purchase the building in the event the landlord receives a bona fide offer to sell.

Item 3. Legal Proceedings

There are no pending legal proceedings to which Bay National Corporation or Bay National Bank is a party or to which any of their properties are subject, nor are there proceedings known to Bay National Corporation to be contemplated by any governmental authority. There are no material proceedings known to Bay National Corporation, pending or contemplated, in which any director, officer or affiliate or any principal security holder of Bay National Corporation is a party adverse to Bay National Corporation or Bay National Bank or has a material interest adverse to Bay National Corporation or Bay National Bank.

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

No matter was submitted during the fourth quarter of the year ended December 31, 2002 to a vote of security holders of Bay National Corporation.

PART II

Item 5. Market for Common Equity and Related Stockholder Matters

As of March 24, 2003, the number of holders of record of Bay National Corporation's common stock was approximately 350. Bay National Corporation's common stock is traded on the Over the Counter Bulletin Board ("OTCBB") under the symbol "BANI.OB."

Bay National Corporation completed an initial public offering ("IPO") of its common stock on April 30, 2000. Stock prices subsequent to the IPO are based upon limited trading on the OTCBB. Quotations reflect inter-dealer prices, without retail mark-up, mark-down, or commission and may not represent actual transactions.

	2002		2001	
	Bid Price Range		Bid Price Ra	
Quarter	Low	High	Low	
1st	$ 7.00	$ 7.30	$ 7.50	$
2nd	6.71	7.25	6.05	
3rd	6.70	7.50	6.18	
4th	7.00	8.60	7.00	

To date, Bay National Corporation has not declared or paid any dividends on its common stock. Management anticipates that Bay National Corporation will retain all earnings, if any, in order to provide more funds to operate and expand Bay National Corporation's business and, therefore, Bay National Corporation has no plans to pay any cash dividends at least until it has achieved profitability that supports capital growth in excess of regulatory capital needs. If Bay National Corporation decides to pay dividends in the future, its ability to do so will depend on the ability of Bay National Bank to pay dividends to Bay National Corporation. In addition, management would consider a number of other factors before deciding to pay dividends, including Bay National Corporation's earnings prospects, financial condition and cash needs.

The amount of dividends that may be paid by Bay National Bank to Bay National Corporation depends on Bay National Bank's earnings and capital position and is limited by statute, regulations and regulatory policies. As a national bank, Bay National Bank may not pay dividends from its paid-in surplus. All dividends must be paid out of undivided profits then on hand, after deducting expenses, including provisions for loan losses and bad debts. In addition, a national bank is prohibited from declaring a dividend on its shares of common stock until its surplus equals its stated capital, unless there has been transferred to surplus no less than one-tenth of the bank's net profits for the preceding two consecutive half-year periods (in the case of an annual dividend). The approval of the OCC is required if the total of all dividends declared by a national bank in any calendar year exceeds the total of its net profits for that year combined with its retained net profits for the preceding two years, less any required transfers to surplus. In addition, Bay National Bank may not pay a dividend if, after paying the dividend, it would be "undercapitalized" as defined in the applicable regulations.

Recent Sales of Unregistered Securities

On October 31, 2002, Bay National Corporation commenced a private offering to accredited investors only of an aggregate of 550,000 shares of its common stock, which was subsequently increased to 620,690 shares of its common stock. The purchase price per share is $7.25 for an aggregate purchase price of $4,500,002. The private offering will terminate no later than April 30, 2003. As of December 31, 2002, Bay National Corporation had received and accepted subscriptions from accredited investors to purchase 41,500

shares in the private offering. As of March 24, 2003, Bay National Corporation had received and accepted subscriptions from accredited investors to purchase 364,484 shares in the private offering.

There were and will be no underwriting discounts or commissions paid with respect to the private offering. Bay National Corporation believes that the private offering is exempt from the registration requirements of the Securities Act of 1933 by virtue of Section 4(2) of the Securities Act of 1933 and Rule 506 promulgated thereunder. The transaction is not being conducted by any form of general solicitation or general advertising and, in connection with the transaction, Bay National Corporation is taking reasonable care to assure that the investors are not underwriters within the meaning of Section 2(11) of the Securities Act by, among other things, making reasonable inquiry of each investor to confirm that the investor is taking his or her securities for investment only and not with a view to or for sale in connection with any distribution of the securities and will place appropriate legends on the share certificates.

SELECTED FINANCIAL DATA
AS OF DECEMBER 31, 2002, 2001 and 2000
(dollars in thousands, except per share data)

	2002	2001

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Total assets	$ 84,609	$ 47,026
Cash and due from banks	363	3,065
Federal funds sold and other overnight investments	11,753	6,488
Loans held for sale	2,819	682
Investment securities available for sale	948	-
Federal Reserve Bank stock	276	276
Federal Home Loan Bank stock	80	-
Loans, net	67,227	35,415
Deposits	76,079	38,139
Short-term borrowings	507	-
Stockholders' equity	7,610	8,602
Common shares outstanding	1,242,020	1,242,020
Book value per share	$ 6.13	$ 6.93
Ratio of interest earning assets to interest bearing liabilities	127.68%	134.86%
Stockholders' equity as a percentage of assets	8.99%	18.29%

SELECTED FINANCIAL RATIOS
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 and 2000

Weighted average yield/rate on:	2002	2001
Loans	6.52%	7.38%
Investments and interest bearing cash balances	1.43%	3.85%
Deposits and short-term borrowings	2.84%	3.70%
Net interest spread	2.80%	2.31%
Net interest margin	3.43%	3.58%

SELECTED OPERATIONAL DATA
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001 and 2000
(dollars in thousands, except per share data)

	2002	2001
Interest income	$ 3,486	$ 1,882
Interest expense	1,367	760
Net interest income	2,119	1,122
Provision for credit losses	405	377
Net interest income after provision for credit losses	1,714	745
Non-interest income	718	271
Non-interest expenses	3,424	2,632
Loss before income taxes	(992)	(1,616)
Income taxes	-	-
Net loss	$ (992)	$ (1,616)
PER COMMON SHARE		
Basic and diluted net loss per share	$ (.80)	$ (1.30)
Average shares outstanding (Basic and Diluted)	1,242,020	1,242,020

Item 6. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion of Bay National Corporation's financial condition and results of operations should be read in conjunction with Bay National Corporation's consolidated financial statements, the notes thereto and the other information included in this annual report.

This discussion and analysis provides an overview of the financial condition and results of operations of Bay National Corporation ("Parent") and its national bank subsidiary, Bay National Bank ("Bank"), (collectively the "Company"), as of December 31, 2002 and 2001 and for the years ended December 31, 2002, 2001, and 2000. Comparative discussion of the results of operations for the year ended December 31, 2000 is limited by the fact that the Company had no operations other than organizational activity until May 2000. As such, comparisons may not provide accurate or meaningful information regarding the Company's results of operations during the period.

General

The Parent was organized on June 3, 1999. From inception through May 12, 2000, the Parent's activities were limited to those related to its organization and capitalization of the Bank. These limited activities were financed solely by the Parent's sale of an aggregate of 112,500 shares of common stock at a purchase price of $10.00 per share in its organizational offering.

The Parent completed its initial public offering of 1,129,520 shares of its common stock, at an offering price of $10.00 per share, on April 30, 2000. The primary purpose of the offering was to raise the necessary capital to form and capitalize the Bank.

On May 12, 2000, the Parent became a bank holding company by purchasing all of the common stock issued by the Bank. The Bank opened its first office on May 12, 2000, and a second office on May 26, 2000. The Bank was formed to serve the business communities of North Baltimore and Salisbury, Maryland.

Application Of Critical Accounting Policies

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America and follow general practices within the industries in which it operates. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions, and judgments are based on information available as of the date of the financial statements; accordingly, as this information changes, the financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions, and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when available.

The most significant accounting policies followed by the Company are presented in Note 1 to the consolidated financial statements. These policies, along with the disclosures presented in the 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. Based on the valuation techniques used and the sensitivity of financial statement amounts to the methods, assumptions, and estimates underlying those amounts, management has identified the determination of the allowance for credit losses as the accounting area that requires the most subjective or complex judgments, and as such could be most subject to revision as new information becomes available.

The allowance for credit losses represents management's estimate of probable credit losses inherent in the loan portfolio. Determining the amount of the allowance for credit losses is considered a critical accounting estimate because it requires significant judgment and the use of estimates related to the amount and timing of expected future cash flows on impaired loans, estimated losses on pools of homogeneous loans based on historical loss experience, and consideration of current economic trends and conditions, all of which may be susceptible to significant change. The loan portfolio also represents the largest asset type on the consolidated balance sheets. Note 1 to the consolidated financial statements describes the methodology used to determine the allowance for credit losses and a discussion of the factors driving changes in the amount of the allowance for credit losses is included in the Credit Risk Management section of this financial review.

Recent Accounting Pronouncements And Developments

Note 1 to the consolidated financial statements discusses new accounting policies adopted by the Corporation during 2002 and the expected impact of accounting policies recently issued or proposed but not yet required to be adopted. To the extent the adoption of new accounting standards materially affects the Corporation's financial condition, results of operations, or liquidity, the impacts are discussed in the applicable section(s) of this financial review and notes to the consolidated financial statements.

Risk Management

The Board of Directors is the foundation for effective corporate governance and risk management. The Board demands accountability of management, keeps stockholders' and other constituencies' interests in focus, and fosters a strong internal control environment. Through its Executive, Loan, Investment and Audit Committees, the Board actively reviews critical risk positions, including market, credit, liquidity, and operational risk. The Company's goal in managing risk is to reduce earnings volatility, control exposure to unnecessary risk, and ensure appropriate returns for risk assumed. Senior management actively manages risk at the line of business level, supplemented with corporate-level oversight through the Asset Liability Committee, the internal audit process and quality control functions, and other risk management groups within the Company. This risk management structure is designed to surface risk issues through a systematic process, enabling timely and appropriate action to avoid and mitigate risk. The risk management process establishes risk limits and other measurement systems, with a focus on risk reduction strategies, and capital allocation practices.

Financial Overview

The Company recorded a net loss of $992,494 for the year ended December 31, 2002. This is a 38.6% improvement over a net loss of $1,615,879 for the year ended December 31, 2001, and a 40.0% improvement over a net loss of $1,652,920 for the year ended December 31, 2000. The loss for the year ended December 31, 2000 included $331,906 of losses incurred as the result of organizational activities performed prior to the opening of the Bank.

The losses for the years ended December 31, 2002, 2001 and 2000 were expected since loan and deposit growth initially were not expected to produce net interest income sufficient to cover operating expenses. On average, start-up community banks do not achieve profitability for the first 24 to 36 months of operation.

As of December 31, 2002, total assets of the Company were $84,609,183 as compared to total assets of $47,025,826 as of December 31, 2001. This represents growth of approximately $37.6 million since December 31, 2001. The growth in assets was a direct result of growth in deposits. Deposits at December 31, 2002 were $76,078,731 as compared to deposits of $38,139,127 at December 31, 2001. Deposit growth was attributable to the marketing efforts of officers and directors of the Bank, and the use of two Internet based listing services for certificates of deposit. Management has set the interest rates paid on deposits to be competitive in the market and has continued to increase marketing activities throughout the year. As of December 31, 2002, the Company has outstanding certificates of deposit totaling approximately $4.0 million that have been classified as "Brokered Deposits" for bank regulatory purposes. These "Brokered Deposits" were issued in average amounts of approximately $99,000 with an average yield of 3.26% and an average term of 16 months.

As of December 31, 2002, loans including loans held for sale (net of a $851,500 allowance for credit losses) totaled $70,045,261. This represents an increase of $33,948,206 or 94.1% from December 31, 2001. The composition of the loan portfolio as of December 31, 2002 was approximately $42.6 million of commercial loans (excluding real estate loans), $4.0 million of consumer loans, and $21.5 million of real estate loans excluding $2.8 million of mortgage loans held for sale. The composition of the loan portfolio as of December 31, 2001 was approximately $23.5 million of commercial loans (excluding real estate loans), $2.1 million of consumer loans, and $10.3 million of real estate loans excluding $0.7 million of mortgage loans held for sale. Growth in the loan portfolio is a direct result of the marketing efforts of bank employees as well as members of the Board of Directors, and the Baltimore and Salisbury Advisory Boards. The mix of loans is consistent with the initial plans for the business.

Funds not extended in loans are held in cash and due from banks, and various investments including federal funds sold and other overnight investments, United States Treasury securities, Federal Reserve Bank stock and Federal Home Loan Bank stock. At December 31, 2002, such investments totaled $13,056,906 as compared to $6,764,401 at December 31, 2001. Other than the investments in Federal Reserve Bank stock and Federal Home Loan Bank stock, totaling $355,840 at December 31, 2002, all investments have maturities of 90 days or less. Management has made a decision to maintain liquidity in the investment portfolio in order to ensure that funds are readily available to fund the rapid growth of the loan portfolio.

Total capital at December 31, 2002 was $7,609,658 as compared to $8,602,152 at December 31, 2001. The decrease in capital is a result of the losses incurred in 2002 and is consistent with the initial expectations of management.

NET INTEREST INCOME / MARGINS

Net interest income is the difference between income on assets and the cost of funds supporting those assets. Earning assets are composed primarily of loans, investments, and federal funds sold; interest-bearing deposits, and other short-term borrowings make up the cost of funds. Non-interest bearing deposits and capital are also funding sources. Changes in the volume and mix of earning assets and funding sources along with changes in associated interest rates determine changes in net interest income.

Interest income from loans and investments for the year ended December 31, 2002 was $3,486,302, compared to 1,881,987, and $782,590 for the years ended December 31, 2001 and 2000, respectively. The 85.2% increase over 2001, and the 345.5% increase over 2000 are directly related to the 97.4% increase in average interest earning assets from 2001, and the 407.2% increase in average interest earning assets from 2000. The increases in average earning assets were somewhat offset by declines in average yields due to a declining interest rate environment. The yields on these assets declined from 6.42% for the year ended

December 31, 2000 to 6.01% for the year ended December 31, 2001 to 5.64% for the year ended December 31, 2002.

Growth in the percentage of interest-earning assets represented by the loan portfolio would normally be expected to result in an increase in average yields on interest-earning assets. This would occur because the yields on loans are normally higher than yields on investment securities. However, the significant loan growth in 2002, and 2001 was partially offset by a reduction in loan yields as a result of actions taken by the Federal Reserve to reduce its target for the federal funds rate from 6.50% at December 31, 2000 to 1.75% at December 31, 2001 to 1.25% at December 31, 2002. For the year ended December 31, 2002, the average yield on the loan portfolio decreased to 6.52% from 7.38% for the year ended December 31, 2001. This decrease is due to the fact that the rate environment in 2002 was weak at the beginning of the year and remained weak throughout. In contrast, in 2001 the rate environment was initially strong and declined steadily throughout the year. As a result, in 2001 the Company received some benefit from the initial stronger rate environment. For the year ended December 31, 2001, the average yield on the loan portfolio actually increased to 7.38% from 7.19% for the year ended December 31, 2000. The increase in average yield was the result of maintaining pricing discipline throughout 2001, as well as increasing the percentage of fixed rate loans in the loan portfolio.

The average yield on the investment portfolio was 1.36% for the year ended December 31, 2002 as compared to 3.79%, and 6.35% for the years ended December 31, 2001 and 2000, respectively. These yield declines were a direct result of the Federal Reserve actions discussed above. The percentage of average earning assets represented by investment securities declined from 91.7% to 38.0% to 17.0% for the years ended December 31, 2000, 2001, and 2002, respectively. This decline is a direct result of the emphasis on development of the loan portfolio.

As of December 31, 2002, the weighted average gross yield on the loans outstanding, excluding loans held for sale, was 6.15%; the weighted average yield on federal funds sold and other overnight investments held on December 31, 2002 was 1.36%. As of December 31, 2001, the weighted average gross yield on the loans outstanding, excluding loans held for sale, was 6.68%; the weighted average yield on federal funds sold and other overnight investments held on December 31, 2001 was 1.69%.

The market in which the Company operates is very competitive, and the rates of interest paid on deposits are affected by rates paid by other depository institutions. Management closely monitors rates offered by other institutions, and seeks to be competitive within the market. The Company has chosen to selectively compete for large certificates of deposits. The Company will choose to pursue such deposits when expected loan growth provides for adequate spreads to support the cost of those funds. As of December 31, 2002, the Company had outstanding certificates of deposit of approximately $15.9 million that were obtained through the listing of certificate of deposit rates on two Internet based listing services. These certificates of deposit were issued with an average yield of 3.36% and an average term of 25 months. Included in the $15.9 million of Internet originated certificates of deposit are approximately $4.0 million that have been classified as "Brokered Deposits" for bank regulatory purposes. These "Brokered Deposits" were issued in average amounts of approximately $99,000 with an average yield of 3.26%, and an average term of 16 months.

The following tables set forth, for the periods indicated, information regarding the average balances of interest-earning assets and interest-bearing liabilities, the amount of interest income and interest expense and the resulting yields on average interest-earning assets and rates paid on average interest-bearing liabilities. Average balances are also provided for non-interest-earning assets and non-interest-bearing liabilities.

	Year Ended December 31, 2002	
	Average Balance	Interest and fees
ASSETS		
Loans:		
Real Estate - Home Equity Line of Credit	$ 7,632,755	$ 370,279
Real Estate - Construction	1,618,539	105,006
Commercial	37,471,778	2,525,572
Consumer	2,914,756	152,603
Loans held for sale *	1,629,502	189,330
Total Loans	51,267,330	3,342,790
Investment Securities	796,439	25,949
Federal funds sold and other overnight investments	9,724,297	117,563
Total Earning Assets	61,788,066	3,486,302
Less: Allowance for credit losses	(607,823)	
Cash and due from banks	688,916	
Premises and equipment, net	770,440	
Accrued interest receivable and other assets	287,930	
Total Assets	$ 62,927,529	
LIABILITIES AND STOCKHOLDERS' EQUITY		
Interest-bearing demand deposits	$ 22,882,007	495,510
Regular savings deposits	2,530,480	30,352
Time deposits	22,379,802	836,763
Short-term borrowings	325,786	4,877

Total interest-bearing liabilities	48,118,075	1,367,502
Net interest income and spread		$ 2,118,800
Non-interest-bearing demand deposits	6,512,685	
Accrued expenses and other liabilities	226,776	
Stockholders' equity	8,069,993	
Total Liabilities and Stockholders' Equity	$ 62,927,529	
Interest and fee income/earning assets	5.64 %	
Interest expense/earning assets	2.21	
Net interest margin	3.43 %	
Return on Average Assets	(1.58)%	
Return on Average Equity	(12.30)%	
Average Equity to Average Assets	12.82 %	

* Interest and fee income on Loans held for sale includes certain fees collected from the borrower and as a result, average yields on these loans are not indicative of actual rates paid by the borrower.

Year Ended December 31, 2001

	Average Balance	Interest and fees
ASSETS		
Loans:		
Real Estate - Home Equity Line of Credit	$ 3,570,447	$ 240,646
Real Estate - Construction	618,755	40,392
Commercial	13,182,861	984,383
Consumer	1,394,337	106,320
Loans held for sale *	628,646	59,289
Total Loans	19,395,046	1,431,030
Investment Securities	275,940	16,200
Federal funds sold and other overnight investments	11,624,139	434,757
Total Earning Assets	31,295,125	1,881,987
Less: Allowance for credit losses	(234,580)	
Cash and due from banks	769,649	
Premises and equipment, net	889,748	
Accrued interest receivable and other assets	115,669	

Total Assets	$ 32,835,611	
LIABILITIES AND STOCKHOLDERS' EQUITY		
Interest-bearing demand deposits	$ 14,119,718	519,783
Regular savings deposits	2,435,613	52,000
Time deposits	3,993,259	188,155
Total interest-bearing liabilities	20,548,590	759,938
Net interest income and spread		$ 1,122,049
Non-interest-bearing demand deposits	2,710,623	
Accrued expenses and other liabilities	141,699	
Stockholders' equity	9,434,699	
Total Liabilities and Stockholders' Equity	$ 32,835,611	
Interest and fee income/earning assets	6.01 %	
Interest expense/earning assets	2.43	
Net interest margin	3.58 %	
Return on Average Assets	(4.92)%	
Return on Average Equity	(17.13)%	
Average Equity to Average Assets	28.73 %	

* Interest and fee income on Loans held for sale includes certain fees collected from the borrower and as a result, average yields on these loans are not indicative of actual rates paid by the borrower.

Year Ended December 31, 2000

	Average Balance	Interest
ASSETS		
Loans:		
Real Estate - Home Equity Line of Credit	$ 410,181	$ 27,875
Real Estate - Construction	3,070	209
Commercial	441,235	33,498
Consumer	162,235	11,536
Total Loans	1,016,721	73,118

Investment Securities	1,292,289	79,600
Federal funds sold and other overnight investments	9,872,259	629,872
Total Earning Assets	12,181,269	782,590
Less: Allowance for credit losses	(9,583)	
Cash and due from banks	240,876	
Premises and equipment, net	547,483	
Accrued interest receivable and other assets	25,834	
Total Assets	$ 12,985,879	
LIABILITIES AND STOCKHOLDERS' EQUITY		
Interest-bearing demand deposits	$ 3,310,811	170,684
Regular savings deposits	39,094	879
Time deposits	518,329	31,457
Total interest-bearing liabilities	3,868,234	203,020
Net interest income and spread		$ 579,570
Non-interest-bearing demand deposits	531,623	
Accrued expenses and other liabilities	175,041	
Stockholders' equity	8,410,981	
Total Liabilities and Stockholders' Equity	$ 12,985,879	
Interest income/earning assets	6.42 %	
Interest expense/earning assets	1.67	
Net interest margin	4.75 %	
Return on Average Assets	(12.73)%	
Return on Average Equity	(19.65)%	
Average Equity to Average Assets	64.77 %	

RATE/VOLUME ANALYSIS

A rate/volume analysis, which demonstrates changes in taxable-equivalent interest income and expense for significant assets and liabilities, appears below. The calculation of rate, volume and rate/volume variances is based on a procedure established for banks by the Securities and Exchange Commission. Rate, volume and rate/volume variances presented for each component may not total to the variances presented on totals of interest income and interest expense because of shifts from year to year in the relative mix of interest-earning assets and interest-bearing liabilities.

	Year ended December 31,		
	2002 vs. 2001		
		Due to variances in	
	Total	Rates	Volumes
Interest earned on:			
Loans:			
Real Estate - Home Equity Line of Credit	$ 129,633	$ (67,437)	$ 273,797
Real Estate - Construction	64,614	(249)	65,265
Commercial	1,541,189	(95,867)	1,813,688
Consumer	46,283	(33,319)	115,934
Loans held for sale	130,041	13,753	94,393
Investment Securities	9,749	(7,210)	30,558
Federal funds sold and other overnight investments	(317,194)	(294,226)	(71,056)
Total interest income	1,604,315	(484,555)	2,322,579
Interest paid on:			
Interest-bearing demand deposits	(24,273)	(214,020)	322,562
Regular savings deposits	(21,648)	(22,786)	2,025
Time deposits	648,608	(38,850)	866,340
Short-term borrowings	4,877	-	-
Total interest expense	607,564	(275,656)	1,190,927
Net interest earned	$ 996,751	$ (208,899)	$ 1,131,652

	Year ended December 31,		
	2001 vs. 2000		
		Due to variances in	
	Total	Rates	Volumes
Interest earned on:			
Loans:			
Real Estate - Home Equity Line of Credit	$ 212,771	$ (229)	$ 214,765
Real Estate - Construction	40,183	(9)	41,915
Commercial	950,885	(550)	967,328
Consumer	94,784	835	87,611
Loans held for sale	59,289	-	-
Investment Securities	(63,400)	(3,732)	(62,603)
Federal funds sold and other overnight investments	(195,115)	(260,638)	111,774
Total interest income	1,099,397	(264,323)	1,360,790
Interest paid on:			
Interest-bearing demand deposits	349,099	(48,804)	557,237
Regular savings deposits	51,121	(44)	53,884
Time deposits	156,698	(7,034)	210,891

Total interest expense	556,918	(55,882)	822,012
Net interest earned	$ 542,479	$ (208,441)	$ 538,778

COMPOSITION OF LOAN PORTFOLIO

As previously discussed, the yields on loans are normally higher than yields on investment securities. As of December 31, 2002, and 2001, the weighted average yields on the loan portfolio were 4.79% and 4.99% higher than the weighted average yields on the investment portfolio. This difference in yields makes it important for the Company to continue to increase the overall level of loans, as well as maintain a relatively high percentage of loans to total earning assets. Accomplishing this goal will ultimately result in maximizing net interest margin. As of December 31, 2002 and 2001, loans represented 81.09% and 82.81% of total earning assets, respectively.

The following table sets forth the composition of the principal balances of Company's loan portfolio as of December 31, 2002 and 2001, respectively.

	2002		2001
Real Estate - Home Equity Line of Credit	$ 9,960,943	14.63%	$ 5,641,198
Real Estate - Construction	3,700,389	5.44	2,230,067
Real Estate - Mortgage	7,816,997	11.48	2,448,595
Commercial	42,566,165	62.52	23,488,566
Consumer	4,033,767	5.93	2,053,629
Total loans	$ 68,078,261	100.00%	$ 35,862,055

The following table sets forth the maturity distribution for the Company's loan portfolio at December 31, 2002. Some of the loans may be renewed or repaid prior to maturity. Therefore, the following table should not be used as a forecast of future cash flows.

	Within one year	One to three years	Three to five years
Real Estate - Home Equity Line of Credit	$ 9,960,943	$ -	$ -
Real Estate - Construction	3,337,935	362,454	-
Real Estate - Mortgage	4,422,294	815,336	2,579,367
Commercial	28,333,281	5,136,119	7,585,327
Consumer	3,726,344	155,915	151,508
Total	$ 49,780,797	$ 6,469,824	$ 10,316,202

Fixed interest rate	$ 6,204,893	$ 6,469,824	$ 10,316,202
Variable interest rate	43,575,904	-	-
Total	$ 49,780,797	$ 6,469,824	$ 10,316,202

The scheduled repayments as shown above are reported in the maturity category in which the payment is due, except for the adjustable rate loans, which are reported in the period of repricing.

The Company's loan portfolio composition as of December 31, 2002 reflects a 64.01% concentration in variable rate loans. Fixed rate loans total $24,502,357 or 35.99% of the Company's loan portfolio. Interest rates on variable rate loans adjust to the current interest rate environment, whereas fixed rates do not allow this flexibility. If interest rates were to increase in the future, the interest earned on the variable rate loans would improve, and if rates were to fall, the interest earned would decline.
See "- Liquidity and Interest Rate Sensitivity."

The officers and directors of the Company have loans due to the Bank of $4,972,128 at December 31, 2002. All loans made to officers and directors are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unaffiliated third parties and do not involve more than the normal risk of repayment or present other unfavorable features.

CREDIT RISK MANAGEMENT

The provision for credit losses represents an expense to fund the allowance for credit losses. This allowance is established to absorb credit losses in the current loan portfolio. The amount of the allowance is determined by management based on many factors, including economic conditions and trends, the value and adequacy of collateral, the volume and mix of the loan portfolio, the performance of the portfolio, and internal loan processes of the Company.

Management uses a loan grading system where all loans are graded based on management's evaluation of the risk associated with each loan. A factor, based on the loan grading, is applied to the loan balance to reserve for potential losses. In addition, management judgmentally establishes an additional unallocated reserve. The unallocated portion of the allowance reflects management's estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions, delays in obtaining information, including unfavorable information about a borrower's financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors.

Based upon management's analysis of the loan portfolio as of December 31, 2002, the allowance for credit losses increased to $851,500 as compared to $447,000 at December 31, 2001. The increase is reflective of the overall increase in the size of the loan portfolio. The amount equates to 1.25% of outstanding loans, net of loans held for sale, as of December 31, 2002 and 2001. This percentage has remained consistent because no additional information has indicated that the overall level of reserves is inappropriate. This is an estimate based on limited historical information, and may be revised over time for changes in economic conditions, experience with the portfolio, and other factors which may arise.

Management considers the year-end allowance appropriate and adequate to cover possible losses inherent in the loan portfolio; however, management's judgment is based upon a number of assumptions, which are believed to be reasonable, but which may or may not prove valid. Thus, there can be no assurance that charge-offs in future periods will not exceed the allowance for credit losses or that additional increases in the allowance will not be required. Management considers, among other things, the findings and recommendations of the Bank's primary regulator and, an independent loan review service in evaluating management's underwriting decisions, and in determining the adequacy of the allowance.

The following table presents the allocation of the allowance for credit losses, reflecting use of the methodology presented above, along with the percentage of total loans in each category as of December 31, 2002 and 2001.

As of December 31, 2002		Amount	Loan M
Real Estate - Home Equity Line of Credit	$	52,720	1
Real Estate - Construction		33,961	
Real Estate - Mortgage		84,548	1
Commercial		626,699	6
Consumer		26,256	
Unallocated		27,316	-
Total Allowance	$	851,500	10

As of December 31, 2001		Amount	Loan M
Real Estate - Home Equity Line of Credit	$	30,987	1
Real Estate - Construction		23,551	
Real Estate - Mortgage		27,069	
Commercial		244,308	6
Consumer		8,811	
Unallocated		112,274	-
Total Allowance	$	447,000	10

The allocated portion of the allowance for credit losses increased in 2002 as a result of an increase in the average risk grade of the loan portfolio.

As of December 31, 2002, the Company has not charged off any loans.

NONPERFORMING LOANS AND OTHER DELINQUENT ASSETS

Management performs reviews of all delinquent loans. Management will generally classify loans as non-accrual when collection of full principal and interest under the original terms of the loan is not expected or payment of principal or interest has become 90 days past due. Classifying a loan as non-accrual results in the Company no longer accruing interest on such loan and reversing any interest previously accrued but not collected. A non-accrual loan may be restored to accrual status when delinquent principal and interest payments are brought current and future monthly principal and interest payments are expected to be collected. The Company will recognize interest on non-accrual loans only when received. As of December 31, 2002 and 2001, the Company did not have any non-accrual loans.

Any property acquired by the Company as a result of foreclosure on a mortgage loan will be classified as "real estate owned" and will be recorded at the lower of the unpaid principal balance or fair value at the date of acquisition and subsequently carried at the lower of cost or net realizable value. Any required write-down of the loan to its net realizable value will be charged against the allowance for credit losses. Upon foreclosure, the Company generally will require an appraisal of the property and, thereafter, appraisals of the property on at least an annual basis and external inspections on at least a quarterly basis. As of December 31, 2002, and December 31, 2001, the Company held no real estate acquired as a result of foreclosure.

The Company applies the provisions of Statements of Financial Accounting Standards No. 114 ("SFAS No. 114"), "Accounting by Creditors for Impairment of a Loan," as amended by Statements of Financial Accounting Standards No. 118 ("SFAS No. 118"), "Accounting by Creditors for Impairment of a Loan-

Income Recognition and Disclosure." SFAS No. 114 and SFAS No. 118 require that impaired loans, which consist of all modified loans and other loans for which collection of all contractual principal and interest is not probable, be measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment is recognized through a valuation allowance and corresponding provision for credit losses. The Company considers consumer loans as homogenous loans and thus does not apply the SFAS No. 114 impairment test to these loans. Impaired loans will be written off when collection of the loan is doubtful.

The Company had no impaired loans as of December 31, 2002, or December 31, 2001.

LIQUIDITY AND INTEREST RATE SENSITIVITY

The Company's principal sources of liquidity are cash and assets that can be readily converted into cash, including investment securities maturing within one year. As of December 31, 2002, the Company had $363,031 in cash and due from banks, and $11,752,705 in federal funds sold and other overnight investments. As of December 31, 2001, the Company had $3,065,479 in cash and due from banks, and $6,488,461 in federal funds sold and other overnight investments. The increase in the overall level of liquid assets is the result of an ongoing effort by management to maintain adequate liquidity to fund loan growth and declines in deposit levels. Growth in the Company's loan portfolio, without corresponding growth in deposits, would reduce liquidity, as would reductions in the level of customer deposits.

The primary objective of asset/liability management is to ensure the steady growth of the Company's primary earnings component, net interest income. Net interest income can fluctuate with significant interest rate movements. To minimize the risk associated with these rate swings, management works to structure the Company's balance sheet so that the ability exists to adjust pricing on interest-earning assets and interest-bearing liabilities in roughly equivalent amounts at approximately the same time intervals. Imbalances in these repricing opportunities at any point in time constitute interest rate sensitivity.

The measurement of the Company's interest rate sensitivity, or "gap," is one of the principal techniques used in asset/liability management. The interest sensitive gap is the dollar difference between assets and liabilities which are subject to interest rate pricing within a given time period, including both floating rate or adjustable rate instruments and instruments which are approaching maturity.

The following table sets forth the amount of the Company's interest-earning assets and interest-bearing liabilities as of December 31, 2002, which are expected to mature or reprice in each of the time periods shown:

			Maturity or repricing		
	Amount	Percent of Total	0 to 3 Months	4 to 12 Months	1 Y
Interest-earning assets					
Federalfunds sold and other overnight investments	$ 11,752,70	14.00%	$ 11,752,705	-	$ -
Loans held for sale	2,818,500	3.36	2,818,500	-	-
Investment securities available for sale	948,361	1.13	948,361	-	-
Loans - Variable rate	43,575,904	51.90	43,575,904	-	-
Loans - Fixed rate	24,502,357	29.19	2,603,994	3,600,899	16,78
Other earning assets	355,840	.42	-	-	-
Total interest-earning assets	$ 83,953,667	100.00%	$ 61,699,464	3,600,899	$ 16,78
Interest-bearing liabilities					
Deposits - Variable rate	$ 31,149,815	47.38%	$ 31,149,815	-	$ -
Deposits - Fixed rate	34,094,566	51.85	4,069,077	10,471,212	19,55
Short-term borrowings	507,000	.77	507,000	-	-
Total interest-bearing liabilities	$ 65,751,381	100.00%	$ 35,725,892	10,471,212	$ 19,5
Periodic repricing differences					

Periodic gap	$ 25,973,572	(6,870,313)	$ (2,76
Cumulative gap	$ 25,973,572	19,103,259	$ 16,33
Ratio of rate sensitive assets to rate sensitive liabilities	172.70%	34.39%	

The Company has 65.90% of its interest-earning assets, and 48.15% of its interest-bearing liabilities in variable rate balances. The excess of interest-earning assets over interest-bearing liabilities of $19,103,259 in the categories of items maturing or repricing within 12 months comprises the majority of the overall gap. This gap is generally reflective of the Company's emphasis on originating variable rate loans, and the demand in the market for higher yielding fixed rate deposits. This analysis indicates that the Company generally will benefit from increasing market rates of interest. However, since all interest rates and yields do not adjust at the same pace, the gap is only a general indicator of interest rate sensitivity. The analysis of the Company's interest-earning assets and interest-bearing liabilities presents only a static view of the timing of maturities and repricing opportunities, without taking into consideration the fact that changes in interest rates do not affect all assets and liabilities equally. Net interest income may be affected by other significant factors in a given interest rate environment, including changes in the volume and mix of interest-earning assets and interest-bearing liabilities.

Management will constantly monitor and manage the structure of the Company's balance sheet, control interest rate exposure, and evaluate pricing strategies. Strategies to better match maturities of interest-earning assets and interest-bearing liabilities include structuring loans with rate floors and ceilings on variable rate notes and by providing for repricing opportunities on fixed rate notes. Management believes that a lending strategy focusing on variable rate loans and short-term fixed rate loans will best facilitate the goal of minimizing interest rate risk. However, management will opportunistically enter into longer term fixed rate

loans and/or investments when, in management's judgment, rates adequately compensate the Company for the interest rate risk. The Company's current investment concentration in federal funds sold and other overnight investments provides the most flexibility and control over rate sensitivity since it generally can be restructured more quickly than the loan portfolio. On the liability side, deposit products can be restructured so as to offer incentives to attain the maturity distribution desired although competitive factors sometimes make control over deposits difficult.

In theory, maintaining a nominal level of interest rate sensitivity can diminish interest rate risk. In practice, this is made difficult by a number of factors, including cyclical variation in loan demand, different impacts on interest sensitive assets and liabilities when interest rates change, and the availability of funding sources. Management generally attempts to maintain a balance between rate-sensitive assets and liabilities as the exposure period is lengthened to minimize the overall interest rate risk to the Company.

INVESTMENT PORTFOLIO

The Company has chosen to invest its available funds primarily in federal funds sold and other overnight investments. As a result, investment securities as of December 31, 2002, consist only of $275,940 of Federal Reserve

Bank stock, $79,900 of Federal Home Loan Bank stock, and $948,361 of U.S. Treasury securities which mature within 3 months. Investment securities as of December 31, 2001, consisted only of $275,940 of Federal Reserve Bank stock. Management has made the decision to maintain its available funds in highly liquid assets because it desires to ensure that funds are readily available to fund the growth of the loan portfolio, and because the yields available on other longer-term securities are not substantially better than those currently being earned on short-term investments. Management believes that this strategy will allow the Company to maximize interest margins while maintaining appropriate levels of liquidity to fund loan growth.

SOURCES OF FUNDS

Deposits and short-term borrowings in the form of repurchase agreements and initial capital are the only current source of funds utilized by the Company for lending and investment activities, and other general business purposes.

The Company offers a variety of deposit products having a range of interest rates and terms. The Company's deposits consist of checking accounts, savings accounts, money market accounts and certificates of deposit. As of December 31, 2002, the Company has outstanding certificates of deposit totaling approximately $4.0 million that have been classified as "Brokered Deposits" for bank regulatory purposes. These "Brokered Deposits" were issued in average amounts of approximately $99,000 with an average yield of 3.26% and an average term of 16 months.

The following table sets forth the composition of the Company's deposits as of December 31, 2002 and December 31, 2001:

	2002		2001
Demand Deposits	$ 25,154,309	33.06%	$ 6,678,275
Savings	2,632,826	3.46	2,728,594
Money Market and sweep	14,197,030	18.66	18,851,242
Certificates of deposit	34,094,566	44.82	9,881,016
Total deposits	$ 76,078,731	100.00%	$ 38,139,127

The following table sets forth the maturity distribution for the Company's deposits at December 31, 2002. Some of the deposits may be renewed or withdrawn prior to maturity. Therefore, the following table should not be used as a forecast of future cash flows.

	Within one year	One to three years	Three to five years

Demand deposits	$ 25,154,309	$ -	$ -
Savings	2,632,826	-	-
Money Market and sweep	14,197,030	-	-
Certificates of deposit	14,510,289	7,397,176	12,187,101
Total	$ 56,494,454	$ 7,397,176	$ 12,187,101

Certificates of deposit in amounts of $100,000 or more and their remaining maturities at December 31, 2002 are as follows:

Three months or less	$ 2,412,699
Over three months through six months	1,746,820
Over six months through twelve months	2,512,425
Over twelve months	4,726,376
Total	$ 11,398,320

Large certificate of deposit customers tend to be extremely sensitive to interest rate levels, making these deposits less reliable sources of funding for liquidity planning purposes than the remainder of the Company's deposits. Management will selectively pursue such deposits in order to mitigate interest rate risk on fixed rate loans. Competitively pricing certificates of deposit and advertising the rates in the newspaper or on the Internet has facilitated the acquisition of these deposits.

NON-INTEREST INCOME

Non-interest income consists primarily of gains on the sale of mortgage loans, mortgage origination fees, deposit account service charges, and cash management fees. For the year ended December 31, 2002, the Company realized non-interest income in the amount of $717,730 as compared to $270,779 and $14,832 for the years ended December 31, 2001 and 2000, respectively. Gains on the sale of mortgage loans of $574,029 are the most significant element of non-interest income, comprising 80.00% of the total for the year ended December 31, 2002. This compares to gains on the sale of mortgage loans of $204,598 or 75.56% of total non-interest income for the year ended December 31, 2001. The increase in gains on the sale of mortgage loans is due to the fact that the Company began originating mortgages in February 2001 and, as a result, production was limited for the year ended December 31, 2001. In addition, the prevailing low interest rate environment, combined with a strong housing market aided 2002 production. An increase in interest rates or a slow down in the housing market could negatively impact the Bank's ability to maintain the same level of income associated with mortgage loan production.

Service charges on deposit accounts totaled $105,766 for the year ended December 31, 2002, as compared to $26,630 and $3,017 for the years ended December 31, 2001 and 2000, respectively. The increases of 297.17% over 2001, and 3405.67% over 2000 can be directly attributed to the growth in the Company's deposit portfolio, and to the fact that the Company introduced additional commercial deposit products in 2002 that typically generate fee income.

The Company will continue to seek ways to expand its sources of non-interest income. The Company is working aggressively to enhance its ability to offer cash management services to commercial customers in order to generate additional deposits or increase cash management fee income. In the future, the Company may also enter into fee arrangements with strategic partners that offer investment advisory services, and risk management and employee benefit services. No assurance can be given that such fee arrangements will be obtained or maintained.

NON-INTEREST EXPENSE

Non-interest expense for the year ended December 31, 2002, totaled $3,424,524. This compares to non-interest expense for the comparable period in 2001 and 2000 of $2,631,707, and $2,177,322, respectively. The increase of $792,817 or 30.13% for 2002 over 2001 resulted primarily from an increase in salaries and benefits of $560,572 related to staff growth to increase marketing efforts, manage the growth of the loan and deposit portfolios, and support increased operational volume. The increase in salaries and benefits includes approximately $183,000 of increased mortgage commissions and benefits resulting from the heavy mortgage volume experienced during the period. Advertising and marketing expense increased $45,806 or 35.77%, from $128,048 to $173,854 for the year ended December 31, 2002 as compared to the same period in 2001. This was primarily the result of increased expenditures made to increase public awareness of the Company and its services, and to grow the Company's deposit and loan portfolios. Other expenses increased $87,406 or 40.77%, from $214,393 to 301,799 for the year ended December 31, 2002 as compared to the same period in 2001. This was primarily the result of increased operating expenses such as telephone, postage, courier, and printing expenses of approximately $56,000 which have increased with the growing customer base, and increased insurance expense of approximately $12,000 related to rising prices for insurance coverage.

The increase in non-interest expense of $454,385 or 20.87%, from $2,177,322 for the year ended December 31, 2000 to $2,631,707 for the year ended December 31, 2001, resulted from an increase in salaries and benefits of $282,282, from $1,209,989 for the year ended December 31, 2000 to $1,492,271 for the year ended December 31, 2001, related to increasing staff levels upon opening the Bank, increased occupancy, furniture and equipment costs of $23,805, from $343,419 for the year ended December 31, 2000 to $367,224 for the year ended December 31, 2001, resulting from the opening and operation of two branch offices, increased data processing and other outside services of $107,539, from $192,644 for the year ended December 31, 2000 to $300,183 for the year ended December 31, 2001, primarily related to the development and servicing of the Bank's customer base, and increases in advertising and marketing expenses of $50,660, from $77,388 for the year ended December 31, 2000 to $128,048 for the year ended December 31, 2001, related to the effort to grow the bank.

The growth of the Company's customer base will continue to require additional staffing to service customers, and manage the business properly. Management believes that continued growth in the customer base can be accommodated without proportionate increases in these costs.

FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business. These financial instruments may include commitments to extend credit, standby letters of credit and purchase commitments. The Company uses these financial instruments to meet the financing needs of its customers. Financial instruments involve, to varying degrees, elements of credit, interest rate, and liquidity risk. These do not represent unusual risks and management does not anticipate any losses which would have a material effect on the Company.

Outstanding loan commitments and lines and letters of credit at December 31 are as follows:

	2002	2001
Loan commitments	$ 2,421,928	$ 2,558,598
Unused lines of credit	19,989,764	9,882,798
Letters of credit	733,278	348,358

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. The Company generally requires collateral to support financial instruments with credit risk on the same basis as it does for on-balance sheet instruments. The collateral is based on management's credit evaluation of the counter party. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. Each customer's credit-worthiness is evaluated on a case-by-case basis.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

CAPITAL RESOURCES

The Company had stockholders' equity at December 31, 2002 of $7,609,658 as compared to $8,602,152 at December 31, 2001. The decrease in capital is a result of the losses incurred in 2002 and is consistent with the initial expectations of management. The Company has declared no cash dividends since its inception.

Banking regulatory authorities have implemented strict capital guidelines directly related to the credit risk associated with an institution's assets. Banks and bank holding companies are required to maintain capital levels based on their "risk adjusted" assets so that categories of assets with higher "defined" credit risks will require more capital support than assets with lower risks. The Bank has exceeded its capital adequacy requirements to date.

Banking regulations also limit the amount of dividends that may be paid without prior approval of the Bank's regulatory agencies. Regulatory approval is required to pay dividends that exceed the Bank's net profits for the current year plus it's retained net profits for the preceding two years. The Bank could not have paid dividends to the Company without approval from bank regulatory agencies at December 31, 2002.

Management and the Board of Directors regularly monitor capital levels, and proactively evaluate various alternatives for raising capital in advance of the actual need. See "Item 5 Market for Common Equity and Related Stockholder Matters - Recent Sales of Unregistered Securities." If adequate capital is not obtained, the Company may be required to curtail significantly its expected growth strategy.

The tables below present the Bank's capital position relative to its various minimum regulatory capital requirements as of December 31, 2002, and 2001. For a discussion of these capital requirements, see "Item 1 Description of Business - Supervision and Regulation - Bay National Bank - Capital Adequacy Guidelines."

December 31, 2002

	Actual Amount	Actual Ratio	For Capital Adequacy Purpose Amount	For Capital Adequacy Purpose Ratio	
Total Capital (to Risk Weighted Assets):	$ 7,808,473	10.21%	$ 6,120,000	8.00%	$ 7,
Tier I Capital (to Risk Weighted Assets):	6,956,973	9.09%	3,060,000	4.00%	4,
Tier I Capital (to Average Assets):	6,956,973	9.13%	2,286,000	3.00%	3,

December 31, 2001

	Actual Amount	Actual Ratio	For Capital Adequacy Purpose Amount	For Capital Adequacy Purpose Ratio	
Total Capital (to Risk Weighted Assets):	$ 6,417,511	15.26%	$ 3,365,000	8.00%	$ 4,
Tier I Capital (to Risk Weighted Assets):	5,970,511	14.19%	1,683,000	4.00%	2,
Tier I Capital (to Average Assets):	5,970,511	14.87%	1,205,000	3.00%	2,

IMPACT OF INFLATION AND CHANGING PRICES

The consolidated financial statements and notes thereto presented herein have been prepared in accordance with accounting principles generally accepted in the United States of America, which require the measurement of financial position and operating results in terms of historical dollars without considering the change in the relative purchasing power of money over time and due to inflation. The impact of inflation is reflected in the increased cost of the Company's operations. Unlike most industrial companies, nearly all the assets of the Company are monetary in nature. As a result, interest rates have a greater impact on the Company's performance than do the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or to the same extent as the price of goods and services.

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Item 7. Financial Statements

The following consolidated financial statements are filed with this report:

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INDEPENDENT AUDITORS' REPORT

Audit Committee of the
Board of Directors and Stockholders
Bay National Corporation

We have audited the accompanying consolidated balance sheets of Bay National Corporation and subsidiary as of December 31, 2002 and 2001, and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Bay National Corporation and subsidiary as of December 31, 2002 and 2001, and the results of their operations and cash flows for each of the three years in the period ended December 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

/s/ Stegman & Company
Baltimore, Maryland
January 31, 2003

BAY NATIONAL CORPORATION

CONSOLIDATED BALANCE SHEETS

December 31, 2002 and 2001

		2002
ASSETS		
Cash and due from banks	$	363,031
Federal funds sold and other overnight investments		11,752,705
Loans held for sale		2,818,500
Investment securities available for sale (AFS) - at fair value		948,361
Other equity securities		355,840
Loans, net of unearned fees		68,078,261
Less: Allowance for credit losses		(851,500)
Loans, net		67,226,761
Premises and equipment, net		709,203
Accrued interest receivable and other assets		434,782
Total Assets	$	84,609,183
LIABILITIES		
Non-interest-bearing deposits	$	10,834,350
Interest-bearing deposits		65,244,381
Total deposits		76,078,731
Short-term borrowings		507,000
Accrued expenses and other liabilities		413,794

Total Liabilities		76,999,525
STOCKHOLDERS' EQUITY		
Common stock - $.01 par value, authorized: 9,000,000 shares authorized, 1,242,020 issued and outstanding		12,420
Additional paid in capital		12,407,780
Accumulated deficit		(4,810,542)
Total Stockholders' Equity		7,609,658
Total Liabilities and Stockholders' Equity	$	84,609,183

See accompanying notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF OPERATIONS

For the years ended December 31, 2002, 2001 and 2000

		2002		2001
INTEREST INCOME:				
Interest and fees on loans	$	3,342,790	$	1,431,03
Interest on federal funds sold and other overnight investments		117,563		434,75
Taxable interest and dividends on investment securities		25,949		16,20
Total interest income		3,486,302		1,881,98
INTEREST EXPENSE:				
Interest on deposits		1,362,625		759,93
Interest on short-term borrowings		4,877		-
Total interest expense		1,367,502		759,93
Net interest income		2,118,800		1,122,04
Provision for credit losses		404,500		377,00

Net interest income after provision for credit losses	1,714,300	745,04
NON-INTEREST INCOME:		
Service charges on deposit accounts	105,766	26,63
Gain on sale of mortgage loans	574,029	204,59
Other income	37,935	39,55
Total non-interest income	717,730	270,77
NON-INTEREST EXPENSE:		
Salaries and employee benefits	2,052,843	1,492,27
Occupancy expenses	212,667	191,84
Furniture and equipment expenses	192,900	175,37
Legal and professional fees	143,778	129,58
Data processing and other outside services	346,683	300,18
Advertising and marketing related expenses	173,854	128,04
Other expenses	301,799	214,39
Total non-interest expenses	3,424,524	2,631,70
Loss before income taxes	(992,494)	(1,615,87
Income tax benefit	-	-
Net Loss	$ (992,494)	$ (1,615,87
Per Share Data:		
Net Loss (Basic and Diluted)	$ (.80)	$ (1.3
Average Shares Outstanding (Basic and Diluted)	1,242,020	1,242,02

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

For the years ended December 31, 2002, 2001 and 2000

	Common Stock	Additional Paid in Capital	Accumulated Deficit	
Balances at December 31, 1999	$ 1,125	$ 1,123,875	$ (549,249)	$

Issuance of Common Stock	11,295	11,283,905	-
Net Loss	-	-	(1,652,920)
Balances at December 31, 2000	12,420	12,407,780	(2,202,169)
Net Loss	-	-	(1,615,879)
Balances at December 31, 2001	12,420	12,407,780	(3,818,048)
Net Loss	-	-	(992,494)
Balances at December 31, 2002	$ 12,420	$ 12,407,780	$ (4,810,542) $

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended December 31, 2002, 2001 and 2000

	2002	2001
Cash Flows From Operating Activities:		
Net loss	$ (992,494)	$ (1,615,879)
Adjustments to reconcile net loss to net cash used by operating activities:		
Depreciation	189,872	179,736
Amortization of investment (discounts) premiums, net	(7,648)	-
Provision for credit losses	404,500	377,000
Gain on sale of loans	(574,029)	(204,598)
Origination of loans held for sale	(32,594,732)	(13,710,790)
Proceeds from sale of loans	31,032,261	13,233,388
Net increase in accrued interest receivable and other assets	(166,517)	(184,720)
Net (decrease) increase in accrued expenses and other liabilities	129,247	133,393
Net cash used by operating activities	(2,579,540)	(1,792,470)
Cash Flows From Investing Activities:		
Purchases of investment securities	(2,440,713)	-
Maturities of investment securities	1,500,000	-

Purchase of Federal Home Loan Bank of Atlanta stock	(79,900)	-
Net increase in loans	(32,216,206)	(30,213,734)
Expenditures for premises and equipment	(68,449)	(70,858)
Net cash used by investing activities	(33,305,268)	(30,284,592)
Cash Flows From Financing Activities:		
Net increase in deposits	37,939,604	24,482,487
Net increase in short-term borrowings	507,000	-
Issuance of common stock	-	-
Net cash provided by financing activities	38,446,604	24,482,487
Net increase in cash and cash equivalents	2,561,796	(7,594,575)
Cash and cash equivalents at beginning of year	9,553,940	17,148,515
Cash and cash equivalents at end of period	$ 12,115,736	$ 9,553,940
Cash paid for:		
Interest	$ 1,296,200	$ 731,603
Income taxes	$ -	$ -

See accompanying notes to consolidated financial statements.

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements include the accounts of Bay National Corporation and its subsidiary, Bay National Bank (the "Bank"), collectively (the "Company"). All significant intercompany balances and transactions have been eliminated in consolidation. The investment in subsidiary is recorded on the parent's books on the basis of its equity in the net assets. The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America and to general practices in the banking industry.

Nature of Business

Bay National Corporation was incorporated on June 3, 1999 under the laws of the State of Maryland to operate as a bank holding company of a national bank with the name Bay National Bank. On May 12, 2000, the Company purchased all the shares of common stock issued by the Bank. The Company's operations through that date were limited to taking the necessary actions to organize and capitalize the Company and the Bank. The Bank commenced operations on May 12, 2000 after successfully meeting the conditions of the Office of the Comptroller of the Currency (the "OCC") to receive its charter authorizing it to commence operations as a national bank, and obtaining the approval of the Federal Deposit Insurance Corporation to insure its deposit accounts, and meeting certain other regulatory requirements.

The principal business of the Company is to make loans and other investments and to accept time and demand deposits. The Company's primary market areas are in Baltimore and Salisbury, Maryland, although the Company's business development efforts generate business outside of these areas. The Company offers a broad range of banking products, including a full line of business and personal savings and checking accounts, money market demand accounts, certificates of deposit, and other banking services. The Company funds a variety of loan types including commercial and residential real estate loans, commercial term loans and lines of credit, consumer loans, and letters of credit. The Company's customers are primarily individuals and small businesses.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company has included cash and due from banks, and federal funds sold and other overnight investments as cash and cash equivalents for the purpose of reporting cash flows.

Investment Securities

Investment securities may be classified into three categories: trading, held-to-maturity, and available-for-sale. Trading securities are purchased and held principally for the purpose of reselling them within a short period of time. Their unrealized gains and losses are included in non-interest income. The Company held no securities classified as trading during 2002, 2001 and 2000. Securities classified as held-to-maturity are reported at amortized cost, and require the Company to have both the positive intent and the ability to hold those securities to maturity. Securities not classified as either trading or held-to-maturity are considered to be available-for-sale. Unrealized holding gains or losses on available-for-sale securities are excluded from earnings and reported, net of any deferred taxes, as accumulated other comprehensive income, a separate component of stockholders' equity. Realized gains or losses on the sale of investment securities are recognized at the time of the sale using the specific identification method, and are classified as non-interest income in the accompanying consolidated statements of operations.

The Company also invests in Federal Reserve Bank stock and Federal Home Loan Bank stock, which is considered restricted as to marketability.

Loans Held for Sale

The Company engages in sales of residential mortgage loans originated by the Bank. Loans held for sale are carried at the lower of aggregate cost or fair value. Fair value is derived from secondary market quotations for similar instruments. Gains and losses on sales of these loans are recorded as a component of non-interest income in the accompanying consolidated statements of operations.

Loans

Loans are stated at the principal amount outstanding net of any deferred fees and costs. Interest income on loans is accrued at the contractual rate on the principal amount outstanding. It is the Company's policy to discontinue the accrual of interest when circumstances indicate that collection is doubtful. Fees charged and costs capitalized for originating certain loans are being amortized on the interest method over the term of the loan.

Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, except that as a practical expedient, the Company may measure impairment based on a loan's observable market price or the fair value of the collateral, if the loan is collateral dependent. The Company recognizes interest income on impaired loans on a cash basis if the borrower demonstrates the ability to meet the contractual obligation and collateral is sufficient. If there is doubt regarding the borrowers ability to make payments or the collateral is not sufficient, payments received are accounted for as a reduction in principal.

Allowance for Credit Losses

The allowance for credit losses is established through a provision for credit losses charged to expense. Loans are charged against the allowance for credit losses when management believes that the collectibility of the principal is unlikely. The allowance, based on evaluations of the collectibility of loans, is an amount that management believes will be adequate to absorb possible losses on existing loans that may become uncollectible. The evaluations take into consideration such factors as changes in the nature and volume of the loan portfolio, overall portfolio quality, review of specific problem loans, and current economic conditions and trends that may affect the borrowers' ability to pay.

The allowance for loan losses represents an estimation done pursuant to either Statement of Financial Accounting Standards ("SFAS") No. 5 "Accounting for Contingencies", or SFAS No. 114 "Accounting by Creditors for Impairment of a Loan." The Company uses a loan grading system where loans are graded based on management's evaluation of the risk associated with each loan. A factor, based on the loan grading is applied to the loan balance to reserve for potential losses. In addition, management judgmentally establishes an additional unallocated reserve. The unallocated portion of the allowance reflects management's estimate of probable inherent but undetected losses within the portfolio due to uncertainties in economic conditions, delays in obtaining information, including unfavorable information about a borrower's financial condition, the difficulty in identifying triggering events that correlate perfectly to subsequent loss rates, and risk factors that have not yet manifested themselves in loss allocation factors.

While management believes it has established the allowance for credit losses in accordance with generally accepted accounting principles and has taken into account the views of its regulators and the current economic environment, there can be no assurance that in the future the Company's regulators or the economic environment will not require further increases in the allowance.

Premises and Equipment

Premises and equipment are stated at cost less accumulated depreciation and amortization computed using the straight-line method. Premises and equipment are depreciated over the useful lives of the assets, except for leasehold improvements which are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Useful lives range from five to 10 years for furniture, fixtures, and equipment; three to five years for software, hardware, and data handling equipment; and leasehold improvements are amortized over the term of the respective lease plus the first optional renewal period, if applicable. Maintenance and repairs are charged to expense as incurred, while improvements, which extend the useful life, are capitalized and depreciated over the estimated remaining life of the asset.

Long-lived depreciable assets are evaluated periodically for impairment when events or changes in circumstances indicate the carrying amount may not be recoverable. Impairment exists when the expected undiscounted future cash flows of a long-lived asset are less than its carrying value. In that event, the Company recognizes a loss for the difference between the carrying amount and the estimated fair value of the asset based on a quoted market price, if applicable, or a discounted cash flow analysis.

Stock-Based Compensation

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123), but applies Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its stock option plan. Compensation expense for stock option awards is disclosed as a pro forma income adjustment ratably recognized over the vesting period, based on the fair value of the stock on the date of grant under SFAS No. 123, and SFAS No. 148

"Accounting for Stock-Based Compensation - Transition and Disclosure."

Advertising Costs

Advertising costs are generally expensed as incurred.

Costs Associated with Start-Up Activities

The Company expensed costs incurred during the start-up phase of organization in accordance with the American Institute of Certified Public Accountants' Statement of Position 98-5 Reporting on the Costs of Start-Up Activities, which requires such costs to be expensed in the period incurred.

Income Taxes

The Company uses the liability method of accounting for income taxes. Under the liability method, deferred-tax assets and liabilities are determined based on differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities (i.e., temporary differences) and are measured at the enacted rates that will be in effect when these differences reverse. Deferred income taxes will be recognized when it is deemed more likely than not that the benefits of such deferred income taxes will be realized; accordingly, no deferred income taxes or income tax benefits have been recorded by the Company.

Earnings Per Share

Basic net loss per common share is computed by dividing the net loss by the weighted average number of common shares outstanding during the period. Diluted net loss per common share is computed by dividing the net loss by the weighted average number of common shares outstanding during the period, including any potential dilutive common shares outstanding, such as options and warrants. No consideration was given to the outstanding options and warrants because of their anti-dilutive effect.

New Accounting Standards

In August 2001, the Financial Accounting Standards Board issued SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, which supersedes both SFAS No. 121, Accounting for the Impairment of Long-Lived Assets to Be Disposed Of and the accounting and reporting provisions of APB Opinion No. 30, Reporting the Results of Operations--Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions,

for the disposal of a segment of a business (as previously defined in that Opinion). SFAS No. 144 retains the fundamental provisions in SFAS No. 121 for recognizing and measuring impairment losses in long-lived assets held for use and long-lived assets to be disposed of by sale, while also resolving significant implementation issues associated with SFAS No. 121. The provisions of SFAS No. 144 are effective for years beginning after December 15, 2001, and its adoption had no affect on the financial position or results of operations of the Company.

In December 2002, the Financial Accounting Standards Board issued SFAS No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure which amends SFAS No. 123, Accounting for Stock-Based Compensation. SFAS No. 148 provides alternative methods of transition for voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS No. 148 amends the disclosure requirements of SFAS No. 123 to require additional and more frequent disclosures in financial statements about the effects of stock-based compensation. Adoption of SFAS No. 148 had no effect on the financial position or results of operations of the Company.

2. INVESTMENT SECURITIES

Investments available-for-sale

The amortized cost and estimated fair values of investments available-for-sale at December 31, 2002 are as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealize Losses
U.S. Treasury securities	$ 948,361	$ -	$ -
Total investments available-for-sale	$ 948,361	$ -	$ -

The amortized cost and estimated fair values of debt securities available-for-sale at December 31, 2002 by contractual maturity are shown below.

	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 948,361	$ 948,361
Total investments available-for-sale	$ 948,361	$ 948,361

There were no investments available-for-sale as of December 31, 2001 or 2000, and there were no sales of investments available-for-sale during 2002, 2001 or 2000.

At December 31, 2002 investments available-for-sale with a carrying value of $507,000 were pledged as collateral for certain short-term borrowings.

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

Other equity securities

At December 31 the Company's investment in other equity securities consisted of:

		2002	
Federal Reserve Bank stock	$	275,940	$
Federal Home Loan Bank stock		79,900	
Total investments in other equity securities	$	355,840	$

3. LOANS AND ALLOWANCE FOR CREDIT LOSSES

Major loan categories at December 31 are presented below:

		2002		2001
Real Estate - Home Equity Line of Credit	$	9,960,943	$	5,641
Real Estate - Construction		3,700,389		2,230
Real Estate - Mortgage		7,816,997		2,448
Commercial		42,566,165		23,488
Consumer		4,033,767		2,053
Total Loans		68,078,261		35,862
Less: Allowance for credit losses		(851,500)		(447
Net Loans	$	67,226,761	$	35,415

Activity in the allowance for credit losses for the year ended December 31, 2002, 2001 and 2000 is shown below:

		2002		2001	
Balance at beginning of year	$	447,000	$	70,000	$
Provision for credit losses		404,500		377,000	
Loan charge-offs		-		-	
Loan recoveries		-		-	
Net charge-offs		-		-	
Balance at end of year	$	851,500	$	447,000	$

There were no loans that were considered impaired under SFAS No. 114 as of December 31, 2002, 2001 and 2000 and for the years then ended.

Notes to Consolidated Financial Statements

4. PREMISES AND EQUIPMENT

Premises and equipment at December 31 include the following:

		2002
Furniture and equipment	$	348,98
Computer hardware and software		540,65
Leasehold improvements		293,97
		1,183,61
Less accumulated depreciation		(474,40
Net premises and equipment	$	709,20

The Company rents office space in two locations under three non-cancelable lease arrangements accounted for as operating leases. The initial lease periods are for five years and provide for one or more five-year renewal options. The two leases for the Baltimore location provide for percentage annual rent escalations. The lease for the Salisbury location requires that the lessee pay certain operating expenses applicable to the leased space.

Rent expense applicable to operating leases for the periods ended December 31, was as follows:

		2002		2001
Minimum rentals	$	187,760	$	181,0
Less: Sublease rentals		(40,784)		(39,2
Net rent expense	$	146,976	$	141,8

At December 31, 2002, future minimum lease payments under non-cancelable operating leases having an initial term in excess of one year are as follows:

Years ending December 31:		
2003	$	193,854
2004		181,179
2005		37,809
2006		-
2007		-
Total minimum lease payments	$	412,842

Total minimum future rental payments have not been reduced by $10,295 of sublease rentals expected to be received in 2003 under a non-cancelable sublease expiring in March 2003.

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

5. DEPOSITS

Certificates of deposit in amounts of $100,000 or more and their remaining maturities at December 31 are as follows:

	2002	2001
Three months or less	$ 2,412,699	$ 643,254
Over three months through six months	1,746,820	1,343,447
Over six months through twelve months	2,512,425	1,138,179
Over twelve months	4,726,376	901,499
Total	$ 11,398,320	$ 4,026,379

Interest expense on deposits for the year ended December 31 is as follows:

	2002	2001
Interest-bearing transaction	$ 141,073	$ 8,7
Savings and money market	384,789	563,0
Time, $100,000 or more	281,304	82,9
Other time	555,459	105,1
Total interest on deposits	$ 1,362,625	$ 759,9

6. SHORT-TERM BORROWINGS

Information relating to short-term borrowings as of December 31, 2002 is as follows:

	Amount	Rate
As of year end	$ 507,000	1.00%
Average for the year	$ 325,786	1.50%
Maximum month end balance	$ 724,035	

The Company had no short-term borrowings during the years ended December 31, 2001 and 2000.

The Company pledges U.S. Government Treasury Securities, based upon their market values, as collateral for 100% of the principal and accrued interest of its short-term borrowings.

7. ISSUANCE OF COMMON STOCK

On April 30, 2000, the Company completed its initial public offering and sold 1,129,520 shares of its common stock, $0.01 par value per share, for a price of $10 per share and received aggregate consideration of $11,295,200.

8. OPTIONS AND WARRANTS

On August 31, 1999, the Board of Directors of the Company authorized the issuance on September 10, 1999, to each stockholder of record of the Company on August 31, 1999, a warrant to purchase one share of common stock at $10 per share for every two shares that the stockholder purchased in the organizational offering. As a result, the Company issued warrants to purchase 56,250 shares. The warrants were issued in recognition of the financial and organizational risk undertaken by the purchasers in the organizational offering. The warrants became exercisable on April 30, 2001 and are exercisable in whole or in part until November 16, 2004. No warrants have been exercised as of December 31, 2002.

The Company's 2001 Stock Option Plan ("Option Plan") provides for the granting of incentive and non-qualifying stock options to the Company's directors and to selected employees on a periodic basis at the discretion of the Board of Directors. The Option Plan authorizes the issuance of up to 200,000 shares of common stock, has a term of ten years, and is administered by the Compensation Committee of the Board of Directors. The Compensation Committee consists of at least two non-employee directors appointed by the Board of Directors. In general, the options have an exercise price, which may not be less than 100% of the fair market value on the date of the grant, must be exercised within eight years and vest over a period of six years.

The following is a summary of changes in shares under options for the years ended December 31, 2002 and 2001:

		Number of Shares
Balance, January 1, 2001		-
Granted		141,533
Cancelled		-
Exercised		-
Balance, December 31, 2001		141,533
Granted		16,815
Cancelled		(9,523)
Exercised		-
Balance, December 31, 2002		148,825
Weighted average fair value of options granted during 2001	$	3.05
Weighted average fair value of options granted during 2002	$	3.05

The following table summarizes information about options outstanding at December 31, 2002:

Range of Exercise Price	Options Outstanding				Option
Price	Number	Weighted Average Remaining Contractual Life (in years)		Weighted Average Exercise Price	Number
$ 7.58	132,010	7	$	7.58	8,250
$ 8.37	16,815	8		8.37	-
	148,825				

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants during the year ended December 31:

	2002	2001
Dividend yield	-	-
Expected volatility	20.00%	20.00%
Risk-free interest rate	4.17%	5.23%
Expected lives (in years)	8	8

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" (SFAS No. 123), but applies Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its stock option plans. No compensation expenses related to the Company's stock option plans was recorded during the years ended December 31, 2002 and 2001.

The following table illustrates the effect on net loss and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to stock-based employee compensation for the years ending December 31:

	2002	2001
Net loss, as reported	$ (992,494)	$ (1,615,879
Less pro forma stock-based compensation expense determined under the fair value method, net of related tax effects	(15,445)	-
Pro forma net loss	$ (1,007,939)	$ (1,615,879
Net loss per share:		
Basic and Diluted - as reported	$ (.80)	$ (1.30
Basic and Diluted - pro forma	$ (.81)	$ (1.30

8. RETIREMENT PLAN

The Company has a 401(k) profit sharing plan covering substantially all full-time employees. The plan requires the Company to match 25% of employee contributions of up to 3% of compensation as defined under the plan. The Company has also elected to make a safe harbor contribution to the plan on behalf of all eligible employees, as defined under the plan. The safe harbor contribution is equal to 3% of compensation as defined under the plan. The plan permits additional contributions at the discretion of management. Expense under this plan totaled $58,447, $32,069 and $29,445 for the years ended December 31, 2002, 2001 and 2000, respectively.

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BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

9. INCOME TAXES

Federal and state income tax expense (benefit) consists of the following for the periods ended December 31:

	2002	2001
Current federal income tax	$ -	$ -
Current state income tax	-	-
Deferred federal income tax expense (benefit)	-	-
Deferred state income tax expense (benefit)	-	-
Total income tax expense (benefit)	$ -	$ -

The following table is a summary of the tax effect of temporary differences that give rise to a significant portion of deferred tax assets:

Deferred tax assets:	2002
Net operating loss carryforwards	$ 1,620,000
Other	6,000
Deferred loan fees, net	12,000
Allowance for credit losses	205,000
Total deferred tax assets	1,843,000
Less valuation allowance	(1,783,000)
Deferred tax assets, net of valuation allowance	60,000
Deferred tax liabilities:	
Depreciation and amortization	(60,000)
Net deferred tax assets (liabilities)	$ -

No income tax benefit or deferred tax asset is reflected in the financial statements. Deferred tax assets are recognized for future deductible temporary differences and tax loss carryforwards if their realization is "more likely than not".

At December 31, 2002 the Company had approximately $4.2 million in tax loss carryforwards, which expire between 2019 and 2022. Realization depends on generating sufficient taxable income before the expiration of the loss carryforward periods. The amount of loss carryforward available for any one year may be limited if the Company is subject to the alternative minimum tax.

10. RELATED PARTY TRANSACTIONS

Certain directors and executive officers have loan transactions with the Company. Such loans were made in the ordinary course of business on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with outsiders. The following schedule summarizes changes in amounts of loans outstanding, both direct and indirect, to these persons during 2002 and 2001.

	2002	2001
Balance at beginning of period	$ 2,670,548	$ 618,500
Additions	11,124,909	3,479,790
Repayments	(8,823,329)	(1,427,742)
Balance at December 31	$ 4,972,128	$ 2,670,548

An individual who is a director of the Company owns an office building, which is leased to the Company. The lease term commenced September 1, 1999 and is for a term of five years and contains renewal options for three additional five-year terms. Rent expense under this agreement was $23,756 for each of the periods ended December 31, 2002, 2001 and 2000, respectively. Management believes that the terms of the foregoing lease are no more and no less favorable to the Company than those which could have been received from unaffiliated parties.

11. FINANCIAL INSTRUMENTS WITH OFF-BALANCE SHEET RISK

The Company is a party to financial instruments with off-balance sheet risk in the normal course of business. These financial instruments may include commitments to extend credit, standby letters of credit and purchase commitments. The Company uses these financial instruments to meet the financing needs of its customers. Financial instruments involve, to varying degrees, elements of credit, interest rate, and liquidity risk. These do not represent unusual risks and management does not anticipate any losses which would have a material effect on the accompanying financial statements.

Outstanding loan commitments and lines and letters of credit at December 31 are as follows:

	2002	2001
Loan commitments	$ 2,421,928	$ 2,558,598
Unused lines of credit	19,989,764	9,882,798
Letters of credit	733,278	348,358

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. The Company generally requires collateral to support financial instruments with credit risk on the same basis as it does for on-balance sheet instruments. The collateral is based on management's credit evaluation of the counter party. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amount does not necessarily represent future cash requirements. Each customer's credit-worthiness is evaluated on a case-by-case basis.

Standby letters of credit are conditional commitments issued to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

12. REGULATORY MATTERS

As of December 31, 2002 and 2001, the Company was not required to maintain non-interest-bearing deposits with the Federal Reserve Bank. The actual balance maintained with the Federal Reserve Bank at December 31, 2002 and 2001 were $189,609 and $2,950,896, respectively.

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

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain amounts and ratios (set forth in the table below) of total and Tier I capital (as defined in the regulations) to risk-weighted assets (as defined), and of Tier I capital (as defined) to average assets (as defined). Management believes, as of December 31, 2002, that the Bank met all capital adequacy requirements to which it is subject.

The Bank has been categorized as "well capitalized" by the OCC under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios. There are no conditions or events that management believes would prevent the Bank from continuing to be categorized as well capitalized.

The Bank's actual capital amounts and ratios as of December 31, 2002 and 2001 are presented in the following table:

December 31, 2002

	Actual Amount	Actual Ratio	For Capital Adequacy Purpose Amount	For Capital Adequacy Purpose Ratio	
Total Capital (to Risk Weighted Assets):	$ 7,808,473	10.21%	$ 6,120,000	8.00%	$ 7,
Tier I Capital (to Risk Weighted Assets):	6,956,973	9.09%	3,060,000	4.00%	4,
Tier I Capital (to Average Assets):	6,956,973	9.13%	2,286,000	3.00%	3,

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

December 31, 2001

	Actual Amount	Actual Ratio	For Capital Adequacy Purpose Amount	For Capital Adequacy Purpose Ratio	
Total Capital (to Risk Weighted Assets):	$ 6,417,511	15.26%	$ 3,365,000	8.00%	$ 4,
Tier I Capital (to Risk Weighted Assets):	5,970,511	14.19%	1,683,000	4.00%	2,
Tier I Capital (to Average Assets):	5,970,511	14.87%	1,205,000	3.00%	2,

Banking regulations also limit the amount of dividends that may be paid without prior approval of the Bank's regulatory agencies. Regulatory approval is required to pay dividends which exceed the Bank's net profits for the current year, plus it's retained net profits for the preceding two years. The Bank could not have paid dividends to the Company without approval from bank regulatory agencies at December 31, 2002.

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

13. PARENT COMPANY FINANCIAL INFORMATION

Condensed financial information for Bay National Corporation (Parent Only) is as follows:

CONDENSED BALANCE SHEETS

December 31, 2002 and 2001

		2002	
ASSETS			
Cash and cash equivalents	$	652,241	$
Due from subsidiary		250,736	
Investment in subsidiary		6,956,973	
Total Assets	$	7,859,950	$
LIABILITIES			
Accrued expenses and other liabilities	$	250,292	$
Total Liabilities		250,292	
STOCKHOLDERS' EQUITY			
Common stock - $.01 par value, authorized: 9,000,000 shares authorized, 1,242,020 issued and outstanding:		12,420	
Additional paid in capital		12,407,780	
Accumulated Deficit		(4,810,542)	
Total Stockholders' Equity		7,609,658	
Total Liabilities and Stockholders' Equity	$	7,859,950	$

BAY NATIONAL CORPORATION

CONDENSED STATEMENTS OF OPERATIONS

For the years ended December 31, 2002, 2001 and 2000

	2002	2001
Interest and dividends on investment securities	$ 23,931	$ 98,61
Non-interest expense	2,886	6,01
Income (loss) before income taxes and equity in undistributed losses of subsidiary	21,045	92,59
Income tax expense (benefit)	-	-
Loss before equity in undistributed losses of subsidiary	21,045	92,59
Equity in undistributed losses of subsidiary	(1,013,539)	(1,708,47
Net Loss	$ (992,494)	$ (1,615,87

CONDENSED STATEMENTS OF CASH FLOWS

For the years ended December 31, 2002, 2001 and 2000

	2002	2001
Cash Flows From Operating Activities		
Net Loss	$ (992,494)	$ (1,615,87
Adjustments to reconcile net loss to net cash used by operating activities:		
Equity in undistributed loss of subsidiary	1,013,539	1,708,47
Net decrease (increase) in other assets	(250,736)	-
Net (decrease) increase in other liabilities	250,240	(194,38
Net cash used by operating activities	20,549	(101,79
Cash Flows From Investing Activities		
Investment in subsidiary	(2,000,000)	-
Net cash used by investing activities	(2,000,000)	-
Cash Flows From Financing Activities		
Issuance of common stock	-	-
Net cash provided by financing activities	-	-
Net (decrease) increase in cash and cash equivalents	(1,979,451)	(101,79
Cash and cash equivalents at beginning of year	2,631,692	2,733,48

Cash and cash equivalents at end of period	$ 652,241	$ 2,631,69

BAY NATIONAL CORPORATION

Notes to Consolidated Financial Statements

Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

There has been no occurrence requiring a response to this Item.

PART III

Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act

Directors, Executive Officers, Promoters and Control Persons

The directors of Bay National Corporation, their ages, the years in which their terms expire and the year in which they became directors are as follows:

Name	Age	Term to Expire (1)	Direc
Hugh W. Mohler	57	2003 Annual Meeting	Jun
Carroll A. Bodie	57	2005 Annual Meeting	Jun
Charles E. Bounds	84	2005 Annual Meeting	Jun
Gary T. Gill	50	2003 Annual Meeting	Janu
John R. Lerch	58	2005 Annual Meeting	Jun
Donald G. McClure, Jr.	59	2003 Annual Meeting	Apr
Robert L. Moore	49	2003 Annual Meeting	Febru
H. Victor Rieger, Jr.	65	2003 Annual Meeting	Jun
Margaret Knott Riehl	69	2003 Annual Meeting	Jun
William B. Rinnier	61	2004 Annual Meeting	Augu
Edwin A. Rommel, III	53	2004 Annual Meeting	Jun
Henry H. Stansbury	63	2004 Annual Meeting	Jun
Kenneth H. Trout	54	2004 Annual Meeting	Octo
Eugene M. Waldron, Jr.	59	2004 Annual Meeting	Jun
Carl A.J. Wright	48	2003 Annual Meeting	Mar

Biographical information concerning the directors is set forth below.

Hugh W. Mohler serves as chairman, president, and chief executive officer, and has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mr. Mohler has 35 years' experience in the financial services industry, holding positions in executive management, commercial lending and business development. From 1977 to 1999, Mr. Mohler was affiliated with Mercantile Bankshares Corporation, which is headquartered in Baltimore, Maryland, most recently serving as executive vice president with responsibility for 20 community banks in a three-state area. For 17 years, from 1977 to 1994, he was president of Mercantile's Salisbury, Maryland-based affiliate, Peninsula Bank, the largest financial institution on Maryland's Eastern Shore. Earlier he was a vice president in commercial lending at First National Bank of Maryland.

A native of Baltimore, Mr. Mohler earned his undergraduate degree in economics from Loyola College of Maryland and his master of business administration degree from the University of Baltimore. He is immediate past president of the board of trustees of Associated Catholic Charities, Inc. in the Roman Catholic Archdiocese of Baltimore. Currently he serves as a trustee of Loyola Blakefield and Goucher College. Mr. Mohler also serves on the Board of Directors of the Independent College Fund of Maryland and the Board of Sponsors of the Sellinger School of Business at Loyola College of Maryland. He also serves on the Board of Governors of The Maryland Club.

Mr. Mohler's prior civic experiences include serving as chairman of the Greater Salisbury Committee, chairman of the Salisbury School, and chairman of the Governor's Lower Shore Economic Task Force. He also served on the boards of Peninsula Regional Medical Center, Maryland Chamber of Commerce, Salisbury-Wicomico Economic Development Committee, and the Somerset County Economic Development Committee. Mr. Mohler also served as president of the Maryland Bankers Association and on several committees of the American Bankers Association.

Carroll A. Bodie has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mr. Bodie is vice president, general counsel and secretary of Noxell Corporation, a Hunt Valley, Maryland-based subsidiary of Procter & Gamble Company for which he also serves as associate general counsel. Mr. Bodie has served in that capacity since 1987. Prior to joining Noxell, Mr. Bodie spent more than two decades in the brewing industry, his most recent position being with the Miller Brewing Company subsidiary of Philip Morris Companies, Inc.

A Baltimore native, Mr. Bodie holds an undergraduate degree in marketing from the University of Baltimore and earned his law degree from the University of Baltimore School of Law. Admitted to practice before numerous courts, including those in the State of Maryland and the United States Supreme Court, he is a member of the Baltimore County, Maryland Bar Association, the American Bar Association and the American Corporate Counsel Association. Mr. Bodie is chairman of the board of trustees of Loyola Blakefield, a board and executive committee member for the Independent College Fund of Maryland, and a Trustee at the College of Notre Dame of Maryland. He is a past director and board chairman for the YMCA of Central Maryland.

Charles E. Bounds has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mr. Bounds is a retired executive who served from 1944 to 1969 as director of purchases and inventory for Symington Wayne Corporation, an international conglomerate headquartered in Salisbury, Maryland, which operated businesses in the United States and seven foreign countries. From 1969 to 1999, he was a vice president-investments for Morgan Stanley Dean Witter, working in the Salisbury, Maryland office of the investment banking firm.

A native of Salisbury, Maryland, Mr. Bounds is past chairman of the Salvation Army Boys Club in Salisbury, Maryland, and headed the Salisbury, Maryland Salvation Army administrative board. He has also chaired fund raising efforts for the Boy Scouts of America, Delmarva District. Mr. Bounds was an original member of the Ward Foundation, which is a Salisbury, Maryland based non-profit organization, which operates The Ward Museum of Wildfowl Art. Mr. Bounds is an alumnus of Beacom College.

Gary T. Gill has been a director of Bay National Corporation and Bay National Bank since January 2003. Mr. Gill is President and Chief Executive Officer of the MacKenzie Companies, a Baltimore-based full-service commercial real estate firm comprising Mackenzie Commercial Real Estate Services, LLC, Mackenzie Management Corporation, MacKenzie Services Corporation, MacKenzie Contracting Company, LLC, and MacKenzie Drywall Construction. Mr. Gill joined MacKenzie in 1977 and has served in his capacity as president since 1985. Mr. Gill serves also as Executive Vice President of MacKenzie Properties, Inc., the managing partner of over 35 partnerships of income-producing commercial properties.

A native of Towson, Maryland, Mr. Gill received his Bachelor of Arts degree in Business Administration in 1974 from Towson University. Mr. Gill currently serves on the Baltimore County Economic Advisory Board, Towson University Stadium Committee, USLacrosse Foundation Board, and chairs the Lax 4 Baltimore Committee for the NCAA National Men's Lacrosse Championships.

John R. Lerch has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Since January 1999, Mr. Lerch has been self-employed as a private investor trading as the Chesapeake Venture Group. From 1973 to January 1999, Mr. Lerch was president of Chesapeake Insurance-The Harris Riggin Agency, an independent insurance agency based in Salisbury, Maryland. Mr. Lerch began his business career in the securities industry, serving as a stockbroker at firms in Washington, D.C. and Salisbury, Maryland. Mr. Lerch is a past director of the Independent Insurance Agents of Maryland.

Mr. Lerch is an alumnus of Dickinson College of Carlisle, Pennsylvania. He served as an officer in the U.S. Army and holds a Bronze Star from his service in Vietnam. He is a director of Barr International, Inc., a regional medium and heavy truck sales and service organization. He is a past director of Peninsula Bank, a subsidiary of Baltimore-based Mercantile Bankshares Corporation. He is a past director and vice-chairman of the Greater Salisbury Committee, past trustee of the Peninsula Regional Medical Center in Salisbury, past president of Salisbury-Wicomico Economic Development Corporation and past president and campaign chairman of the United Way of the Lower Eastern Shore. He also has served as a director for the Mid-Delmarva Family YMCA and was a former chairman and a current trustee for The Ward Foundation.

Donald G. McClure, Jr. has been a director of Bay National Corporation and Bay National Bank since April 2000. Mr. McClure is a principal in the McClure Group, Inc, a Baltimore-based private equity investment firm originated in 1979. He is the former Chairman and Co-Chief Executive of Americom Wireless Services, Inc., which merged with a Fortune 200 company in 2000.

Mr. McClure serves on several private company boards as well as devoting substantial time to various civic, charitable and educational organizations here and in other states.

Robert L. Moore has been a director of Bay National Corporation since February 2001 and Bay National Bank since June 2001. Mr. Moore is a certified public accountant. He received his CPA designation twenty-five years ago, and is the owner and founder of the Salisbury, Maryland accounting firm of Moore & Company, P.A. His professional concentration is income tax and all facets of business consulting.

Mr. Moore received his Bachelor of Science degree from the University of Virginia in 1976. Currently, he serves as Chairman of the Trustees of the Wicomico County Pension System, a board member of Salisbury-Wicomico Economic Development Corporation, a member of the Performance Review Committee for Wicomico County, and a member of the Salisbury Area Chamber of Commerce.

Mr. Moore is a past president of the Eastern Shore Chapter of the Maryland Association of CPAs. He served as Chairman of the Administrative Board of Asbury United Methodist Church. In addition, Mr. Moore served on the Board of Directors of the Bank of Fruitland, Maple Shade Residential Homes, Inc., and the Holly Foundation. He was also a member of the Executive Committee and Board of Directors of the Green Hill Yacht & Country Club and a member and officer of the Salisbury Jaycees.

H. Victor Rieger, Jr. has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mr. Rieger retired from Signet Banking Corporation, successor to Union Trust Company of Maryland, in December 1997 after nearly four decades of service. Mr. Rieger served in numerous capacities for Signet, including regional executive vice president of international banking and as part of Signet's Maryland commercial banking group. Mr. Rieger has extensive experience in commercial relationship banking, credit administration and loan policy.

An alumnus of Johns Hopkins University, Mr. Rieger is a graduate of the Stonier School of Banking at Rutgers University. He is past president and a current trustee of Family and Children's Services of Central Maryland, past treasurer and board member of the National Flag Day Foundation and a past vice-president and director of the Baltimore Junior Association of Commerce. He is a former member of the loan committee for the Minority Small Business Investment Company and a past advisory board member of the U.S. Small Business Administration. Mr. Rieger also is past president of the Chesapeake Chapter of Robert Morris Associates.

Margaret K. Riehl has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mrs. Riehl is a retired nurse and civic volunteer. She is currently a trustee of the Marion I. and Henry J. Knott Foundation, a Baltimore, Maryland-based philanthropic organization and has served in that capacity from 1978 to 1985 and again from 1993 to present. She serves as chair of the board of trustees of Baltimore's Associated Catholic Charities, Inc., and as a trustee of St. Mary's Seminary & University, also in Baltimore. Mrs. Riehl is a former trustee of the Community Foundation of Baltimore, Mercy Medical Center, the Institute of Notre Dame and St. Paul's School for Girls. A Baltimore native, Mrs. Riehl is an alumna of the Mercy Hospital School of Nursing.

William B. Rinnier has been a director of Bay National Corporation since August 1999, and a director of Bay National Bank since April 2000. Mr. Rinnier is the owner and president of Rinnier

Development Company, a Salisbury, Maryland based real estate development company, which specializes in the development and sale or management of resort condominiums, multi-family apartments, and commercial and industrial buildings. He joined Rinnier Development Company nearly three decades ago after his honorable discharge from the U.S. Navy.

A native of Salisbury, Maryland, Mr. Rinnier earned a degree in aerospace engineering from the Georgia Institute of Technology and attended the Graduate School of Business at the University of Virginia. He is a board member of the Greater Salisbury Committee and is past president of the Salisbury-Wicomico Economic Development Corporation and the Coastal Board of Realtors.

Edwin A. Rommel III has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mr. Rommel is a certified public accountant that, since 1974, has been a partner in the Salisbury, Maryland, accounting firm of Twilley, Rommel & Stephens, P.A. Mr. Rommel has been certified as a valuation analyst and accredited in business evaluation by the American Institute of Certified Public Accountants.

A Baltimore native, Mr. Rommel earned his undergraduate degree from Loyola College of Maryland. Mr. Rommel is a current director of the Greater Salisbury Committee and past president of the Salisbury Area Chamber of Commerce. He serves as a director of the Maryland Association of Certified Public Accountants and an officer of its Eastern Shore Chapter. Mr. Rommel is past president of the St. Francis de Sales Board of Trustees and past member of the Wicomico County Democratic Central Committee.

Henry H. Stansbury has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Since 1975, Mr. Stansbury has been the chief executive officer of Agency Services, Inc., an independently owned premium finance company. Since 1989, Mr. Stansbury has been the chief executive officer of Agency Insurance Company of Maryland, Inc., a privately owned multi-line property/casualty insurance company. Mr. Stansbury is a past president of the Maryland Association of Premium Finance Companies and is a past president of the National Association of Premium Finance Companies.

Mr. Stansbury is a vice president and trustee of the Maryland Historical Society, and a trustee of the Ward Museum of Wildfowl Art. He served as director and chairman of the museum committee for the Lacrosse Hall of Fame at the Johns Hopkins University and is vice president and a trustee of the St. Paul's School for Boys. He is also past president of ReVisions, Inc., a nonprofit organization that serves the mentally ill. Mr. Stansbury is a graduate of Leadership Maryland and a director of Leadership Baltimore County. He is the author of LLOYD J. TYLER: FOLK ARTIST AND DECOY MAKER and a contributing writer for Decoy Magazine. Mr. Stansbury is an alumnus of the University of Maryland and holds a master of business administration degree from George Washington University.

Kenneth H. Trout has been a director of Bay National Corporation since October 1999, and a director of Bay National Bank since April 2000. Since January 1999, Mr. Trout has served as the executive vice president and chief operating officer of Rosemore, Inc., a Baltimore-based privately held investment company primarily engaged in the business of oil and gas exploration and production. He also serves as a director of Rosemore Holdings, Inc., Rosemore Calvert, Inc., Tema Oil and Gas Company and Gateway Gathering and Marketing Company, which are all subsidiaries of Rosemore, Inc. He is also a director of KCI

Technologies, Inc. From 1970 to November 1997, Mr. Trout was employed by Signet Banking Corporation. During his last five years of tenure with Signet, he served as senior executive vice president-commercial banking and as president and chief executive officer of Signet Bank-Maryland. Mr. Trout was retired from December 1997 to December 1998.

A Bridgeton, New Jersey native, Mr. Trout received his undergraduate degree in economics and business administration from Methodist College in North Carolina. He is vice chairman of the Board of Trustees of The College of Notre Dame of Maryland.

Eugene M. Waldron, Jr. has been a director of Bay National Corporation since June 1999, and a director of Bay National Bank since April 2000. Mr. Waldron is a chartered financial analyst and since September 1998 has been a senior vice president in the Washington, D.C., office of Capital Guardian Trust Company, an employee-owned firm based in Los Angeles dedicated to institutional investment management. From March 1994 to August 1998, Mr. Waldron was employed by Loomis, Sayles & Company, an investment management firm. Mr. Waldron's more than three decades of investment experience include employment at CS First Boston Asset Management, Fidelity Management Trust Company, T. Rowe Price Associates and Baker, Watts & Company.

An alumnus of Mt. St. Mary's College, Emmitsburg, Maryland, Mr. Waldron earned his master of business administration degree at the Bernard M. Baruch College of the City University of New York. A native of Annapolis, Maryland, he is a member of the Mt. St. Mary's Board of Trustees and the Newton, Massachusetts Country Day School of the Sacred Heart's Endowment Committee.

Carl A.J. Wright has been a director of Bay National Corporation and Bay National Bank since March 2003. Mr. Wright is the Senior Vice President of Spherion (formerly Interim Financial Solutions), an executive search and staffing firm specializing in finance, human resources and information systems. Along with his corporate responsibilities, he is an involved community member and active in professional, civic and political organizations.

Mr. Wright received his B.A. in Accounting from Loyola College in 1976, then began his professional career with Ernst & Young. He served in the firm's auditing and tax departments. He joined A.J. Burton in 1980. Throughout his career, Carl has been active in professional organizations. He became a Certified Public Accountant in 1978 and he has served on a number of committees and boards for the Maryland Association of CPAs.

Mr. Wright has demonstrated his continuing commitment to education through membership of boards and committees of both Loyola College and Loyola Blakefield. He is Past President of the Baltimore Junior Association of Commerce and serves on Maryland Governor Robert Ehrlich's Strategic and Finance Committees. In addition, he is an active supporter of the Catholic Charities and Maryland Business for Responsive Government.

Other than Mr. Mohler and Mr. Waldron who are first cousins, there are no family relationships between any director or executive officer and any other director or executive officer of Bay National Corporation.

The one executive officer and significant employee of Bay National Corporation and Bay National Bank that does not serve on the Board of Directors of Bay National Corporation is Mark A. Semanie.

Mr. Semanie, age 39, serves as Executive Vice President and Chief Financial Officer, Treasurer and Secretary of Bay National Corporation and Vice President and Chief Financial Officer, Chief Compliance Officer, Treasurer and Secretary of Bay National Bank. Mr. Semanie is a Certified Public Accountant. Mr. Semanie worked in the insurance industry for over 7 years. From July 1996 to October 2000, he served as Executive Vice President and Chief Financial Officer for Agency Holding Company of Maryland, Inc., parent company of Baltimore-based Agency Services, Inc., an independently owned premium finance company, and Agency Insurance Company of Maryland, Inc., a privately owned multi-line property/casualty insurance company. From March 1993 to July 1996, he was associated with USF&G Corporation where he served in various capacities, including Manager of SEC and External Reporting. From August 1985 to March 1993, Mr. Semanie worked in the Boston and Baltimore offices of the international accounting firm of KPMG LLP. He last served as a Senior Manager in the Audit practice with the firm. His background includes experience in financial planning and reporting, backroom operations, human resources and compliance issues.

A native of Connecticut, Mr. Semanie earned a Bachelor of Science degree in accounting from Bentley College. He currently serves on the Board of Directors of Agency Insurance Company of Maryland, Inc. He also serves as a director of the Baltimore Child Abuse Center and as Chairman of its Finance Committee. He is a member of the American Institute of Certified Public Accountants, the American Institute of Chartered Property Casualty Underwriters, and Financial Executives International.

Bay National Corporation's charter and bylaws provide that Bay National Corporation shall have at least three (3) directors, and that the number of directors may be increased or decreased by the Board of Directors. As of March 24, 2003, the number of directors has been fixed at 15 with all positions filled. Pursuant to Bay National Corporation's charter and bylaws, the Board of Directors is divided into three classes, with each class serving a three-year term, and the term of one class expiring each year. A director may only be removed by the affirmative vote of at least 80% of the votes entitled to be cast on the matter and only for cause.

Bay National Corporation's officers are appointed by the Board of Directors and hold office at the will of the board or as otherwise provided in an employment agreement between an officer and Bay National Corporation.

As Bay National Corporation is the sole stockholder of Bay National Bank, each director of Bay National Bank is elected by the Board of Directors of Bay National Corporation. Directors of Bay National Bank serve for a term of one year and are elected each year at Bay National Bank's annual meeting of stockholders. Bay National Bank's officers are appointed by its Board of Directors and hold office at the will of the board.

Bay National Corporation has established an advisory board of directors, which is comprised of professionals and business persons, who provide advice to Bay National Corporation's and Bay National Bank's Board of Directors and who promote the interests of Bay National Corporation and Bay National Bank. An advisory board of directors is not required by any Maryland or federal law or regulation and advisory directors are not subject to regulatory approval or supervision. The advisory directors do not have

the power to vote on any matter considered by the Board of Directors and they serve at the pleasure of the board.

Compliance with Section 16(a) of the Exchange Act

The Company did not have a class of equity securities registered pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"), at any time during the Company's fiscal year ended December 31, 2002. Accordingly, there is no requirement upon the Company's officers, directors and 10% or greater shareholders to file any reports required pursuant to Section 16(a) of the Exchange Act.

Item 10. Executive Compensation

Director Compensation

Except for discretionary grants of options to purchase shares of common stock as described below and discretionary payments based on special circumstances, the directors of Bay National Corporation and Bay National Bank are not compensated for their attendance at regularly scheduled or special board meetings or for other services. Bay National Corporation and Bay National Bank do not intend to pay directors fees until Bay National Bank is profitable. However, Bay National Corporation and Bay National Bank reserve the right to pay directors' fees at any time. Directors are reimbursed for reasonable expenses incurred on behalf of Bay National Corporation and Bay National Bank.

In December 2002 and October 2001, the Board of Directors of Bay National Corporation authorized special payments of $10,000 to Mr. H. Victor Rieger, Jr., a director of Bay National Corporation and Bay National Bank. These payments were authorized in recognition of Mr. Rieger's outstanding service as a key member of the Bay National Bank Loan Committee. These amounts were paid in December 2002 and December 2001.

In November 2001, each then director of Bay National Corporation was granted options to purchase 3,000 shares of Bay National Corporation common stock. The options vest in four (4) equal installments with the first 25% installment vesting on the third anniversary of the individual directors appointment to the Board of Directors of Bay National Corporation. The remaining 25% installments vest on the fourth, fifth, and sixth anniversary of the individual director's appointment to the Board of Directors of Bay National Corporation. As of December 31, 2002, options to purchase 8,250 shares were exercisable. The options expire on November 19, 2009. They are exercisable at $7.58 per share. None have been exercised.

Executive Compensation

Summary Compensation Table

The following table sets forth the compensation paid by Bay National Corporation and Bay National Bank to the Chief Executive Officer of Bay National Corporation and Bay National Bank and to any other executive officer of Bay National Corporation and Bay National Bank who received compensation in excess of $100,000 during 2002. Other than the grant of options, all compensation below was paid by the Bay National Bank.

Summary Compensation Table

Long Term Compensation

Name and Principal Position	Year	Salary($)	Bonus($)	Other Annual Compensation ($)	Restricted Stock Award(s) ($)	Securities Underlying Options/ SARs (#)	LTI Pay
		Annual Compensation			Awards		Pay
Hugh W. Mohler President and Chief Executive Officer (1)	2002	$164,000					
	2001	$154,000	-	-	-	40,261	
	2000	$ 96,318	-	-	-	-	
Mark Semanie Vice President (2)	2002	$135,000	$ 30,000	-	-	-	
	2001	$125,000	-	-	-	18,630	
	2000	$ 19,232	-	-	-	-	

Aggregate Options Table

The following table sets forth information on the aggregate number of shares of common stock underlying unexercised options held as of December 31, 2002 by Mr. Mohler and Mr. Semanie and the aggregate dollar value of in-the-money unexercised options held as of December 31, 2002 by Mr. Mohler and Mr. Semanie.

Name	Number of Securities Underlying Unexercised Options at December 31, 2002		Value of Unexercised in-the-Money Options at December 31, 2002	
	Exercisable	Unexercisable	Exercisable	Unexercisab
Hugh W. Mohler	750	39,511	$ 390	$ 20,54
Mark A. Semanie	-	18,630	-	9,68

The exercise price of these options is $7.58 per share. The market value of the common stock was $8.10 per share, which is the sales price at which shares of common stock were last sold in over the counter trading on December 31, 2002.

Employment Arrangements

Bay National Bank has entered into a written employment agreement with Mr. Mohler effective as of May 12, 2000. Under this agreement, Mr. Mohler serves as the president of Bay National Bank at an initial annual base salary of $154,000, subject to annual review. However, pursuant to Mr. Mohler's agreement, Mr. Mohler did not receive any compensation until May 2000. The agreement has an initial term of three years, automatically renewable for one-year terms unless written notice is provided by either party 90 days before expiration of a term. Written notice was not provided by either party 90 days before the expiration of the initial term and accordingly the new term will expire in May 2004.

Bay National Bank may terminate the employment agreement without cause upon 30 days' prior written notice and may terminate the employment agreement for cause at any time without prior notice. Mr. Mohler may terminate his employment agreement at any time upon 30 days' prior written notice. In the event Mr. Mohler is terminated without cause, he will continue to receive salary payments for the earlier of six months from the date of termination or until he has found comparable employment. Mr. Mohler is required to use his best efforts to obtain comparable employment.

Pursuant to this agreement, if Mr. Mohler is employed by Bay National Bank on the date of a "change of control," he is entitled to a payment of 290% of his base salary from Bay National Bank. The employment agreements define "change of control" as (i) the acquisition by any person of forty percent (40%) or more of the outstanding shares of common stock of Bay National Bank or Bay National Corporation; (ii) the election of a majority of the members of the Board of Directors who were not approved or nominated by then incumbent board or (iii) the approval by the stockholders of Bay National Bank or Bay National Corporation of (a) a reorganization, merger or consolidation of Bay National Bank or Bay National Corporation, subject to certain exceptions; (b) a liquidation or dissolution of Bay National Bank or Bay National Corporation or (c) the sale or other disposition of all or substantially all of the assets of Bay National Bank or Bay National Corporation.

In the employment agreement, Mr. Mohler agrees that for a period of six (6) months after employment with Bay National Bank or any affiliate, he will not, directly or indirectly, own, operate or otherwise be associated with, any financial institution which is located in the Bank's market area. Mr. Mohler also agrees that for a period of one (1) year after employment with Bay National Bank or any affiliate, he will not (i) solicit any person or entity which at the time of his termination was, or within one (1) year prior thereto had been, a customer of Bay National Bank or any of its affiliates or (ii) solicit the employment of any person who was employed by Bay National Bank or any of its affiliates on a full or part time basis at the time of his termination of employment, unless such person (a) was involuntarily discharged by Bay National Bank or the affiliate or (b) voluntarily terminated his relationship with Bay National Bank or the affiliate prior to Mr. Mohler's termination of employment.

In addition, pursuant to the employment agreement, upon adoption of a stock option plan by Bay National Corporation's Board of Directors, Mr. Mohler was entitled to options to purchase 3% of the shares of common stock outstanding after the initial public offering. Accordingly, options to purchase 37,261 shares of common stock were granted to Mr. Mohler in November 2001. These options are exercisable at $7.58 per share.

Bay National Bank has purchased "key man" life insurance on Mr. Mohler.

Bay National Bank and Bay National Corporation have not entered into written employment agreements with any other employees.

Item 11. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Securities Authorized For Issuance Under Equity Compensation Plans

The following table sets forth certain information as of December 31, 2002, with respect to compensation plans under which equity securities of Bay National Corporation are authorized for issuance.

Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding options and warrants (a)	Weighted-average exercise price of outstanding options and warrants (b)	N s
Equity compensation plans approved by security holders	148,825	$ 7.67	
Equity compensation plans approved by security holders	56,250	10.00	
Total	205,075	$ 8.31	

Bay National Corporation issued warrants to purchase 56,250 shares of common stock on September 10, 1999 to purchasers of Bay National Corporation's organizational offering. The warrants were issued in recognition of the financial and organizational risks undertaken by those investors. The warrants became exercisable on April 30, 2001, and they expire on November 16, 2004. Investors were given one warrant for every two shares purchased in the organizational offering. The warrants are exercisable at $10 per share. None of the warrants have been exercised.

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Security Ownership

The following table sets forth the beneficial ownership of Bay National Corporation's common stock as of March 24, 2003 by its directors, executive officers named in the Summary Compensation Table in Item 10 above, directors and officers as a group and persons believed by management to beneficially own more than five percent (5%) of the common stock. The table includes warrants and options beneficially owned by these persons. Unless otherwise noted below, management believes that each person named in the table has the sole voting and sole investment power with respect to each of the shares of common stock reported as beneficially owned by such person.

Name and Address of Beneficial Owner (16)	Number of Shares (16)	Percentage of Class

Carroll A. Bodie (1) 4005 Greenway Baltimore, MD 21218	16,750	1.01%
Charles E. Bounds (2) 1707 Upper Millstone Lane Salisbury, MD 21801	6,880	.41%
Citizens, Inc. (3) P.O. Box 1550 Butler, PA 16003	112,500	6.76%
Gary T. Gill 6 Brierleigh Court Lutherville, Maryland 21093	2,500	.15%
John R. Lerch (4) 618 Indian Lane Salisbury, MD 21801	43,750	2.63%
Donald G. McClure, Jr. (5) 11520 Pebble Creek Drive Lutherville, MD 21093	14,750	.89%
Hugh W. Mohler (6) 23 Buchanan Road Baltimore, MD 21212	63,865	3.84%
Robert L. Moore (7) 5673 N. Nithsdale Drive Salisbury, MD 21801	7,500	.45%

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H. Victor Rieger, Jr. (8) 1015 Ivy Hill Road Cockeysville, MD 21030	28,750	1.73%
Margaret K. Riehl (9) 6200 Gentry Lane Baltimore, MD 21210	23,250	1.40%
William B. Rinnier (10) 616 Manor Drive Salisbury, MD 21801	13,250	.80%
Edwin A. Rommel, III (11) 5281 Silver Run Lane Salisbury, MD 21801	31,250	1.88%
Mark A. Semanie (12) 1200 Corinthian Court Bel Air, MD 21014	1,680	.10%
Henry H. Stansbury (13) 6200 Foxhall Farm Road Catonsville, MD 21228	39,550	2.38%

Kenneth H. Trout (14) 804 Hillstead Drive Lutherville, MD 21093	2,750	.17%
Eugene M. Waldron, Jr. (15) 5309 Woodlawn Avenue Chevy Chase, MD 20815	30,750	1.85%
Carl A.J. Wright 8609 Marburg Manor Drive Lutherville, MD 21093	14,000	.84%
All directors and executive officers as a group: Sixteen persons	341,225	20.51%

(1) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003.

(2) Includes 1,250 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003.

(3) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date.

(4) Includes 4,000 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003. Includes 6,000 shares held by LFI partnership, of which Mr. Lerch is a general partner; and 2,000 shares held by Mr. Lerch's spouse, and 1,000 shares issuable upon the exercise of warrants by Mrs. Lerch that are exercisable within 60 days of the record date. Mr. Lerch disclaims beneficial ownership as to the shares and warrants held by his spouse.

(5) Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in April 2004. Includes 9,000 shares held in trust for the benefit of Mr. McClure's children for which Mr. McClure is a co-trustee.

(6) Includes 5,000 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 10,065 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 30,196 shares issuable upon the exercise of options that are exercisable starting in June 2003. Includes 1,000 shares held by Mr. Mohler's spouse. Mr. Mohler disclaims beneficial ownership as to the shares held by his spouse.

(7) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Excludes 3,000 shares issuable upon the exercise of options that are exercisable starting in February 2004.

(8) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003. Includes 1,000 shares held by Mr. Rieger's spouse. Mr. Rieger disclaims beneficial ownership as to the shares held by his spouse.

(9) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003. Includes 1,000 shares held by Mrs. Riehl's spouse. Mrs. Riehl disclaims beneficial ownership as to the shares held by her spouse.

(10) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable

starting in August 2003. Includes 3,000 shares held by Mr. Rinnier's spouse, and 2,000 shares held by Mr. Rinnier's children. Mr. Rinnier disclaims beneficial ownership as to the shares held by his spouse and his children.

(11) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003.

(12) Excludes 18,630 shares issuable upon the exercise of options that are exercisable starting in October 2003.

(13) Includes 2,500 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003. Includes 10,000 shares held by Mr. Stansbury's spouse, and 2,500 shares issuable upon the exercise of warrants by Mrs. Stansbury that are exercisable within 60 days of the record date. Mr. Stansbury disclaims beneficial ownership as to the shares and warrants held by his spouse.

(14) Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in October 2003.

(15) Includes 5,000 shares issuable upon the exercise of warrants that are exercisable within 60 days of the record date. Includes 750 shares issuable upon the exercise of options that are exercisable within 60 days of the record date. Excludes 2,250 shares issuable upon the exercise of options that are exercisable starting in June 2003. Includes 3,000 shares held by Mr. Waldron's children. Mr. Waldron disclaims beneficial ownership as to the shares held by his children.

(16) All of the named individuals, other than Mr. Semanie, are directors of Bay National Corporation. Mr. Mohler is a director and executive officer of Bay National Corporation.

The number of shares beneficially owned includes shares of common stock subject to options or warrants held by the named persons that are exercisable as of, or within 60 days of, March 24, 2003. Such shares are deemed outstanding for the purpose of computing the percentage ownership of the person holding the options or warrants, but are not deemed outstanding for the purpose of computing the percentage ownership of any other person.

The number of shares beneficially owned also includes 88,860 shares of common stock subscribed under the private offering to accredited investors commenced on October 31, 2003 (see "Item 5. Market for Common Equity and Related Stockholder Matters") which are expected to be issued within 60 days of, March 24, 2003. Such shares are deemed outstanding for the purpose of computing the percentage ownership of the person holding the subscriptions, but are not deemed outstanding for the purpose of computing the percentage ownership of any other person.

Bay National Corporation issued warrants to purchase 56,250 shares of common stock on September 10, 1999 to purchasers of Bay National Corporation's organizational offering. The warrants were issued in recognition of the financial and organizational risks undertaken by those investors. The warrants became exercisable on April 30, 2001, and they expire on November 16, 2004. Investors were given one warrant for every two shares purchased in the organizational offering. The warrants are exercisable at $10 per share. None of the warrants have been exercised.

In November 2001, each director of Bay National Corporation was granted options to purchase 3,000 shares of Bay National Corporation common stock. The options vest in four (4) equal installments with the first 25% installment vesting on the third anniversary of the individual director's appointment to the Board of Directors of Bay National Corporation. The remaining 25% installments vest on the fourth, fifth, and sixth anniversary of the individual director's appointment to the Board of Directors of Bay National Corporation. A total of 9,000 of these options to purchase shares were exercisable as of, or within 60 days of March 24, 2003. The options expire on November 19, 2009. They are exercisable at $7.58 per share. None have been exercised.

In November 2001, Mr. Mohler was granted options to purchase 37,261 shares of Bay National Corporation common stock, and Mr. Semanie was granted options to purchase 18,630 shares of Bay National Corporation common stock. The options vest in four (4) equal installments with the first 25% installment vesting on the third anniversary of the officer's date of employment with Bay National Bank. The remaining 25% installments vest on the fourth, fifth, and sixth anniversary of the individual officer's date of employment with Bay National Bank. A total of 9,315 of these options to purchase shares were exercisable as of, or within 60 days of March 24, 2003.The options expire on November 19, 2009. They are exercisable at $7.58 per share. None have been exercised.

Item 12. Certain Relationships and Related Transactions

Prior to Bay National Corporation's initial public offering, the organizers of Bay National Corporation and Bay National Bank and certain other investors purchased an aggregate of 112,500 shares of Bay National Corporation's common stock at a purchase price of $10.00 per share. The primary purpose of this "organizational offering" was to provide Bay National Corporation and Bay National Bank with the capital necessary to fund some of the initial organizational and prepaid operating expenses.

In recognition of the financial and organizational risk undertaken by the purchasers in the organizational offering, on September 10, 1999, the purchasers in the organizational offering received, for no additional consideration, a warrant to purchase one share of common stock at $10.00 per share for every two shares that they purchased in the organizational offering. As a result, Bay National Corporation issued warrants to purchase an aggregate of 56,250 shares of common stock to the purchasers in the organizational offering.

The warrants became exercisable on April 30, 2001 and are exercisable in whole or in part until November 16, 2004. The warrants and the shares of common stock issuable upon the exercise of the warrants are transferable subject to compliance with applicable securities laws. Among other requirements, if the OCC issues a capital directive or other order requiring Bay National Bank to obtain additional capital, the warrants are forfeited if not immediately exercised.

Director John R. Lerch owns a 100% interest in the property being leased for Bay National Bank's Salisbury, Maryland branch office. Pursuant to that lease, which is for a five-year term and commenced as of September 1, 1999, Bay National Corporation agreed to pay Mr. Lerch monthly rent of approximately $1,980 plus all real estate taxes and utilities. Bay National Corporation believes that the lease rate is at fair market value, based, in part, on an evaluation of the lease terms by William E. Martin of ERA Martin Associates, a Salisbury-based real estate brokerage firm. Bay National Corporation engaged Mr. Martin to review the lease terms for the purpose of determining whether the terms were consistent with the lease terms for similar properties in the downtown Salisbury area.

Some of Bay National Bank's directors and officers and the business and professional organizations with which they are associated have banking transactions with Bay National Bank in the ordinary course of business. It is Bay National Bank's policy that any loans and loan commitments will be made in accordance with applicable laws and on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other persons of comparable credit standing. Loans to directors and officers must comply with Bay National Bank's lending policies and statutory lending limits, and directors with a personal interest in any loan application will be excluded from considering any such loan application.

The officers and directors of Bay National Corporation and Bay National Bank have loans due to Bay National Bank of $4,972,128 at December 31, 2002. All loans were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with unaffiliated third parties and do not involve more than the normal risk of repayment or present other unfavorable features.

Item 13. Exhibits and Reports on Form 8-K

(a) Exhibits. The following exhibits are filed with or incorporated by reference into this report.

Exhibit No.	Description of Exhibit
3.1*	Articles of Incorporation of Bay National Corporation
3.2*	Bylaws of Bay National Corporation
4.1*	Rights of Holders of Common Stock (as contained in Exhibit 3.1)
4.2*	Form of Common Stock Certificate
4.3*	Form of Warrant
10.1*	Form of Employment Agreement between Bay National Corporation and Hugh W. Mohle
10.2*	Form of Employment Agreement between Bay National Bank and Hugh W. Mohler
10.3*	Office Lease Agreement dated July 16, 1999 between Bay National Corporation an Partnership
10.4*	Office Lease Agreement dated July 16, 1999 between Bay National Corporation and
10.5*	Lease Agreement dated September 16, 1999 between Bay National Corporation and J
10.6#	Bay National Corporation Stock Option Plan
21.1*	Subsidiaries of Bay National Corporation
23.1	Consent of Stegman & Company
99.1	Certification of Periodic Financial Report pursuant to 18 U.S.C. Section 1350
99.2	Certification of Periodic Financial Report pursuant to 18 U.S.C. Section 1350

The exhibits which are denominated with an asterisk (*) were previously filed by Bay National Corporation as a part of, and are hereby incorporated by reference from, Bay National Corporation's Registration Statement on Form SB-2, as amended, under the Securities Act of 1933, Registration Number 333-87781.

The exhibit which are denominated by the number sign (#) was previously filed by Bay National Corporation as a part of, and is hereby incorporated by reference from, Bay National Corporation's Registration Statement on Form S-8, as amended, under the Securities Act of 1933, Registration Number 333-69428.

(b) Reports of Form 8-K. No reports on Form 8-K were required to be filed for the fourth quarter of 2002.

Item 14. Controls and Procedures

Within 90 days prior to the date of this report, Bay National Corporation's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the design and operation of Bay National Corporation's disclosure controls and procedures. Based upon that evaluation, Bay National Corporation's Chief Executive Officer and Chief Financial Officer concluded that Bay National Corporation's disclosure controls and procedures are effective. Disclosure controls and procedures are controls and procedures that are

designed to ensure that information required to be disclosed in Bay National Corporation's reports filed or submitted under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

In addition, since the Chief Executive Officer's and Chief Financial Officer's most recent review of Bay National Corporation's internal controls, there have been no significant changes in Bay National Corporation's internal controls or in other factors that could significantly affect those controls.

SIGNATURES

In accordance with Section 13 or 15(d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

BAY NATIONAL CORPORATION

Date: March 24, 2003

By: /s/ Hugh W. Mohler

Hugh W. Mohler, President

In accordance with the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Name	Position	Date
/s/ Hugh W. Mohler Hugh W. Mohler	Director and President (Principal Executive Officer)	March 24, 2003
/s/ Mark A. Semanie Mark A. Semanie	Treasurer (Principal Accounting and Financial Officer)	March 24, 2003
/s/ Carroll A. Bodie Carroll A. Bodie	Director	March 27, 2003
/s/ Charles E. Bounds Charles E. Bounds	Director	March 25, 2003
Gary T. Gill	Director	March --, 2003
/s/ John R. Lerch John R. Lerch	Director	March 27, 2003
/s/ Donald G. McClure, Jr. Donald G. McClure, Jr.	Director	March 26, 2003
/s/ Robert L.Moore	Director	March 25, 2003

------------------------------------ Robert L. Moore		
/s/ H. Victor Rieger ------------------------------------ H. Victor Rieger, Jr.	Director	March 26, 2003
/s/ Margaret Knott Riehl ------------------------------------ Margaret Knott Riehl	Director	March 25, 2003

/s/ William B. Rinnier ------------------------------------ William B. Rinnier	Director	March 24, 2003
/s/ Edwin A. Rommel, III ------------------------------------ Edwin A. Rommel, III	Director	March 25, 2003
/s/ Henry H. Stansbury ------------------------------------ Henry H. Stansbury	Director	March 24, 2003
/s/ Kenneth H. Trout ------------------------------------ Kenneth H. Trout	Director	March 27, 2003
/s/ Eugene M. Waldron, Jr. ------------------------------------ Eugene M. Waldron, Jr.	Director	March 24, 2003
------------------------------------ Carl A.J. Wright	Director	March --, 2003

CERTIFICATIONS

I, Hugh W. Mohler, certify that:

1. I have reviewed this annual report on Form 10-KSB of Bay National Corporation;

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

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

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

   c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's Board of Directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could

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significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 26, 2003

By: /s/ Hugh W. Mohler

Name: Hugh W. Mohler
Title: Chairman, President and Chief Executive Officer

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I, Mark A. Semanie, certify that:

1. I have reviewed this annual report on Form 10-KSB of Bay National Corporation;

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

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

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   d) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

   e) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

   f) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's Board of Directors (or persons performing the equivalent function):

   c) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   d) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation,

including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 26, 2003

By: /s/ Mark A. Semanie
Name: Mark A. Semanie
Title: Executive Vice President and Chief Financial Officer

SUPPLEMENTAL INFORMATION TO BE FURNISHED WITH REPORTS FILED PURSUANT TO SECTION 15(D) OF THE EXCHANGE ACT BY NON-REPORTING ISSUERS

Bay National Corporation has not sent and will not send to its security holders an annual report other than this annual report on Form 10-KSB. Subsequent to the date of this filing, Bay National Corporation intends to provide proxy materials to its security holders in connection with its annual meeting of security holders. A copy of such proxy materials will be furnished to the Securities and Exchange Commission for its information and Bay National Corporation understands that such materials will not be considered to be filed or subject to the liabilities of Section 18 of the Exchange Act.

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* Previously filed by Bay National Corporation as a part of Bay National Corporation's Registration Statement on Form SB-2, as amended, under the Securities Act of 1933, Registration Number 333-87781

Previously filed by Bay National Corporation as a part of Bay National Corporation's Registration Statement on Form S-8, as amended, under the Securities Act of 1933, Registration Number 333-69428