HARBOR BANKSHARES CORP
Form SC 13E3/A
August 01, 2006

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 13E-3

(Rule 13e-100)

TRANSACTION STATEMENT UNDER SECTION 13(E) OF THE SECURITIES

EXCHANGE ACT OF 1934 AND RULE 13E-3 THEREUNDER

RULE 13E-3 TRANSACTION STATEMENT UNDER SECTION 13(E) OF THE

SECURITIES EXCHANGE ACT OF 1934)

Amendment No. 1

HARBOR BANKSHARES CORPORATION

(Name of the Issuer)

HARBOR BANKSHARES CORPORATION

HARBOR MERGER CORPORATION

Joseph Haskins, Jr., Teodoro J. Hernandez, Darius L. Davis, James H. DeGraffereidt, Jr., Louis J. Grasmick, Nathaniel Higgs, Delores G. Kelley, Erich March, Garnetta Massey, John Paterakis, John D. Ryder, James Scott, Jr., Edward St. John, Walter S. Thomas, Stanley W. Tucker, and George F. Vaeth, Jr.

(Name of Person(s) Filing Statement)

Common Stock $.01 par value

411465 10 7

(CUSIP Number of Class of Securities)

Joseph Haskins, Jr.	With a copy to:
Chairman, President and	James I. Lundy, III
Chief Executive Officer	Attorney at Law
Harbor Bankshares Corporation	Suite 400
25 West Fayette Street	1700 Pennsylvania Avenue, NW
Baltimore, MD 21201	Washington, DC 20006

(410) 528-1800 202.349.7130
(Name, Address and Telephone Number of Person Authorized to Receive Notices

and Communications on Behalf of Person(s) Filing Statement)

This statement is filed in connection with (check the appropriate box):

a. The filing of solicitation materials or an information statement subject to Regulation 14A, Regulation 14C or Rule 13e-3(c) under the Securities Exchange Act of 1934.

b. The filing of a registration statement under the Securities Act of 1933.
c. A tender offer.
d. None of the above.

Check the following box if the soliciting materials or information statement referred to in checking box (a) are preliminary copies:

Check the following box if the filing is a final amendment reporting the results of the transaction:

Calculation of Filing Fee

Transaction Valuation *	Amount of Filing Fee
$386,818	$41.39

* The transaction value is calculated based on the $31.00 per share to be paid for an estimated 12,478 shares expected to be cashed out in the Rule 13e-3 transaction. The filing fee is $107 per million dollars of the total transaction value of $386,818.

Check box if any part of the fee is offset as provided by Rule 0-11(a)(2) and identify the filing with which the offsetting fee was previously paid. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

Amount Previously Paid:	$41.39	Filing Party:	Harbor Bankshares Corporation
Form or Registration No.: Schedule 14A		Date Filed:	May 2, 2006

INTRODUCTORY STATEMENT

This Amendment No. 1 to Schedule 13E-3 is being filed in connection with the proposed merger (the merger) of Harbor Merger Corporation, a wholly-owned subsidiary of Harbor (merger subsidiary), with and into Harbor, with Harbor being the surviving corporation following the merger, pursuant to an Agreement and Plan of Merger (the merger agreement). Pursuant to the merger agreement, shares owned by holders of Harbor common stock, par value $0.01 per share, who own of record 100 or fewer shares would be converted into the right to receive $31.00 per share. The shares owned by other holders would not be affected. Following the merger, Harbor would have fewer than 300 shareholders of record. Harbor intends to terminate registration of its common stock under the Securities Exchange Act of 1934 (the Exchange Act) and to suspend its reporting obligations under Section 13 of the Exchange Act following the merger.

This Schedule 13E-3 is being filed concurrently with a preliminary proxy statement (the Proxy Statement) filed by Harbor as Amendment No. 1 to the Schedule 14A under the Exchange Act for Harbor s 2006 annual meeting of shareholders. That meeting has been called to consider and vote upon a proposal to approve the merger agreement; approve an adjournment of the Annual Meeting to solicit additional proxies for approval of the merger agreement, if necessary, to elect four Class II Directors, each to serve for a three-year term; and to act upon such other matters as may properly come before the Annual Meeting or any adjournments or postponements thereof. The Proxy Statement is attached hereto as Exhibit (a)(1).

In accordance with the requirements of General Instruction G to Schedule 13E-3 this Schedule 13E-3 incorporates, where applicable, the information contained in the Proxy Statement in response to the Items hereof.

Item 1. Summary Term Sheet.
The information set forth in the Proxy Statement under the caption Summary Term Sheet is incorporated herein by reference.

Item 2. Subject Company Information.
(a), (b) The information set forth in the Proxy Statement under the caption Introduction is incorporated herein by reference.

(c), (d) The information set forth in the Proxy Statement under the caption Market for Common Stock and Dividends is incorporated herein by reference.

(e) No underwritten public offering or Regulation A exempt offering of the common stock for cash has been made during the past three years.

(f) The information set forth in the Proxy Statement under the captions, The Parties Recent Transactions and Prior Stock Purchases is incorporated herein by reference.

Item 3. Identity and Background of Filing Person.
(a) The information set forth under Notice of Annual Meeting of Shareholders and The Parties Directors and Executive Officers of Harbor is incorporated herein by reference.

(b) Not applicable.

(c) (1), (2) The information set forth under the caption Election of Directors and Compensation of Directors and Executive Officers is incorporated herein by reference.

(3) None of such persons has been convicted in a criminal proceeding during the past five years (excluding traffic violations and similar misdemeanors).

(4) None of such persons was a party to any judicial or administrative proceeding during the past five years that resulted in a judgment, decree or final order enjoining the person from future violations of, or prohibiting activities subject to, federal or state securities laws, or a finding if any violation of federal or state securities laws. See Directors and Executive Officers in the Proxy Statement.

(5) Each of such persons is a citizen of the United States.

(d) Not applicable.

Item 4. Terms of the Transaction.

(a) The information set forth under Summary Term Sheet, Special Factors Background of the Merger, Special Factors Reasons for the Merger, Special Factors Effects of the Merger, Special Factors Effect of the Merger on Shareholders, Special Factors Accounting Treatment, Special Factors Certain U.S. Federal Income Tax Consequences, The Merger Agreement Conversion of Shares in the Merger, and The Annual Meeting Shares Entitled to Vote; Quorum and Vote Required is incorporated herein by reference.

(b) The information set forth under Summary Term Sheet How does the board recommend that I vote? and Compensation of Directors and Executive Officers Certain Relationships and Related Transactions is incorporated herein by reference.

(c) The information set forth under Summary Term Sheet, Special Factors Background of the Merger, Special Factors Effects of the Merger, Special Factors Effects of the Merger on Shareholders, and The Merger Agreement Conversion of Shares in the Merger is incorporated herein by reference.

(d) Appraisal Rights. The information set forth in the Proxy Statement under Summary Term Sheet Do I have appraisal or dissenter s rights? and Appraisal Rights of Harbor Shareholders is incorporated herein by reference.

(e) None.

(f) Not applicable.

Item 5. Past Contacts, Transactions, Negotiations and Agreements.

(a) The information set forth in The parties Recent Transactions, The Parties-Prior Stock Purchases, and Compensation of Directors and Executive Officers is incorporated herein by reference.

(2) The information set forth in the Proxy Statement under the caption Compensation of Directors and Executive Officers Certain Relationships and Related Transactions is incorporated herein by reference.

(b), (c) Not applicable.

(e) The information set forth under The Parties Security Ownership of Certain Beneficial Owners and Management and Election of Directors Compensation of Directors and Executive Officers is incorporated herein by reference.

Item 6. Purposes of the Transaction and Plans or Proposals.

(b) The information set forth under Summary Financial Information Summary Unaudited Pro Forma Financial Information is incorporated herein by reference.

(c) (1-8) The information set forth under Summary Term Sheet, Special Factors Background of the Merger, Special Factors Conduct of Harbor s Business After the Merger, Special Factors Effects of the Merger, Market for Common Stock and Dividends, and The Merger Agreement is incorporated herein by reference.

Item 7. Purposes, Alternatives, Reasons and Effects.

(a) The information set forth under Summary Term Sheet, Special Factors Background of the Merger, Special Factors Reasons for the Merger, and Special Factors Fairness Determination by Filing Persons is incorporated herein by reference.

(b) The information set forth in the Proxy Statement under Special Factors Background of the Merger and Special Factors Fairness Determination by Filing Persons is incorporated herein by reference.

(c) The information set forth under Summary Term Sheet, Special Factors Background of the Merger, Special Factors Reasons for the Merger, and Special Factors Fairness Determination by Filing Persons is incorporated herein by reference.

(d) The information set forth under Special Factors Certain Effects of the Merger, Special Factors Effect of the Merger on Shareholders, Special Factors Certain U.S. Federal Income Tax Consequences, and Special Factors Conduct of Harbor s Business After the Merger is incorporated herein by reference.

Item 8. Fairness of the Transaction.

(a)-(e) The information set forth under Summary Term Sheet, Special Factors Background of the Merger, Special Factors Reasons for the Merger, Special Factors Recommendation of the Board of Directors; Fairness of the Merger Proposal, Special Factors Merger Subsidiary s Determination of Fairness of the Merger Proposal, Special Factors Fairness Determination by Filing Persons, and Special Factors Opinion of Financial Advisor is incorporated herein by reference.

(f) Other Offers. Not applicable.

Item 9. Reports, Opinions, Appraisals and Certain Negotiations.

The information set forth under Special Factors Background of the Merger, Special Factors Reasons for the Merger, Special Factors Opinion of Financial Advisor, and Special Factors Price Adjustment Since Opinion Date is incorporated herein by reference.

Item 10. Source and Amounts of Funds or Other Consideration.

(a)-(b) The information set forth under Special Factors Effects of the Merger Financial Effects of the Merger; Financing of the Merger is incorporated herein by reference.

(c) Expenses. The information set forth in the Proxy Statement under Special Factors Fees and Expenses, and Unaudited Pro Forma Consolidated Financial Statements is incorporated herein by reference.

(d) The information set forth under Special Factors Effects of the Merger Financial Effects of the Merger; Financing of the Merger is incorporated herein by reference.

Item 11. Interest in Securities of the Subject Company.

(a) The information set forth under The Parties Securities Ownership of Beneficial Owners and Management and Owners of more than 5% of Harbor Common Stock is incorporated herein by reference.

(b) The information set forth under The Parties Recent Transactions is incorporated herein by reference.

Item 12. The Solicitation or Recommendation.

(d)-(e) The information set forth under Summary Term Sheet How does the Board of Directors recommend that I vote? and Special Factors Recommendation of the Board of Directors; Fairness of the Merger Proposal is incorporated herein by reference.

Item 13. Financial Information.

(a)
(1) The financial statements set forth under Item 7 in Harbor s Annual Report on Form 10-KSB for the year ended December 31, 2005, included at Appendix D to the Proxy Statement, are incorporated herein by reference. (Previously filed.)
(2) The unaudited financial statements set forth in Harbors Quarterly Report on Form 10-QSB for the quarterly period ended March 31, 2006, included at Appendix E to the Proxy Statement, are incorporated herein by reference.
(3) The unaudited statement of Earnings to Fixed Charges included under the caption Summary Financial Information Selected Historical Financial Information is incorporated herein by reference.
(4) The information set forth under Selected Financial Data is incorporated herein by reference.

(b) The information set forth under Summary Financial Information Summary Unaudited Pro Forma Financial Information is incorporated herein by reference.

Item 14. Persons/ Assets, Retained, Employed, Compensated or Used.

(a), (b) None.

Item 15. Additional Information

None.

Item 16. Exhibits.

(a) Preliminary Proxy Statement for the Annual Meeting of Shareholders

(b) Not applicable.

(c)	(i)	Opinion of Danielson Associates dated December 8, 2006 (Previously filed as Exhibit (c) to Schedule 13E-3 filed May 2, 2006 and Appendix B to Preliminary Proxy Statement filed May 2, 2006.)
	(ii)	Opinion of Danielson Associates, as amended (Included as Appendix B to Amendment No. 1. to Preliminary Proxy Statement filed simultaneously herewith.)
	(iii)	Fairness Opinion and Report of Danielson Associates dated as of December 8, 2006.
	(iv)	Fairness Opinion and Report of Danielson Associates dated as of December 8, 2006, amended to clarify opinion with respect to fairness to shareholders and valuation methodology.
(d)		Not applicable.
(f)		Form of Proxy for the Annual Meeting of Shareholders.

(g) Not applicable.

SIGNATURES

After due inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

July 31, 2006

HARBOR BANKSHARES CORPORATION

By: /s/ Joseph Haskins, Jr.

Joseph Haskins, Jr.
Chairman, President, and Chief Executive Officer

July 31, 2006

HARBOR MERGER CORPORATION
By: /s/ Joseph Haskins, Jr.

Joseph Haskins, Jr.
President

By: /s/ Joseph Haskins, Jr.

Joseph Haskins, Jr.
Date: July 31, 2006

By: /s/ Delores J. Kelly

Delores J. Kelly
Date: July 31, 2006

By: /s/ Nathaniel Higgs

Nathaniel Higgs
Date: July 31, 2006

By: /s/ James H. DeGraffereidt

James H. DeGraffereidt
Date: July 31, 2006

By: /s/ George F. Vaeth, Jr.

George F. Vaeth, Jr.
Date: July 31, 2006

By: /s/ Louis Grasmick

Louis Grasmick
Date: July 31, 2006

By: /s/ Stanley W. Tucker

Stanley W. Tucker
Date: July 31, 2006

By: /s/ John D. Ryder

John D. Ryder
Date: July 31, 2006

By: /s/ James Scott, Jr.

James Scott, Jr.
Date: July 31, 2006

By: /s/ Erich W. March

Erich W. March
Date: July 31, 2006

By: /s/ John Paterakis

John Paterakis
Date: July 31, 2006

By: /s/ Edward St. John

Edward St. John
Date: July 31, 2006

By:	/s/ Walter S. Thomas, Sr.	By:	/s/ Teodoro J. Hernandez
	Walter S. Thomas, Sr.		Teodoro J. Hernandez
Date:	July 31, 2006	Date:	July 31, 2006
By:	/s/ Garnetta Massey	By:	/s/ Darius L. Davis
	Garnetta Massey		Darius L. Davis
Date:	July 31, 2006	Date:	July 31, 2006

Exhibit (a) to Schedule 13E-3

[PRELIMINARY]

HARBOR BANKSHARES CORPORATION

25 West Fayette Street

Baltimore, Maryland 21201

__________, 2006

To Our Shareholders:

On behalf of our Board of Directors, we cordially invite you to attend the Annual Meeting of Shareholders of Harbor Bankshares Corporation to be held at Harbor s main office at 25 West Fayette Street, Baltimore, Maryland 21201 on Wednesday, __________ 2006, at 12:00 noon Eastern Time. The formal Notice of Annual Meeting appears on the next page.

At the Annual Meeting, you will be asked to consider and vote on the approval of a merger agreement which provides for the merger of Harbor Bankshares Corporation with Harbor Merger Corporation, its wholly-owned subsidiary, in what is commonly referred to as a going private transaction. Harbor Bankshares Corporation will continue after the merger as the surviving company.

The purpose of the merger is to reduce the number of our shareholders of record to fewer than 300, as required for the suspension of our reporting requirements under Section 13 of the Securities Exchange Act of 1934, in order to eliminate the significant expense required to comply with the those requirements.

If you approve the merger agreement and the merger is completed, each share of Harbor Bankshares Corporation common stock owned of record at the effective time of the merger by a shareholder owning 100 or fewer shares (other than shareholders who properly exercise their rights as objecting shareholders) will be converted into the right to receive from Harbor Bankshares Corporation $31.00 in cash per share, without interest. Shares owned of record by a holder of more than 100 shares will remain as outstanding shares of Harbor Bankshares Corporation common stock after the merger and those shareholders will not receive any cash payment.

Because Harbor Bankshares Corporation has a large number of shareholders who own 100 or fewer shares each, we expect that the merger will reduce the number of shareholders of record by approximately 58%, but will reduce the number of total outstanding shares by less than 2%.

Our Board of Directors believes that the merger agreement is fair to our shareholders and is in the best interests of Harbor Bankshares Corporation and its affiliated and unaffiliated shareholders and unanimously recommends that shareholders vote **FOR** approval of the merger agreement, and **FOR** adjournment of the meeting if necessary to solicit additional votes for approval of the merger agreement. The approval of the merger agreement requires the affirmative vote of the holders of at least two-thirds (2/3) of the outstanding voting shares of Harbor Bankshares Corporation common stock, including a majority of voting shares held by shareholders who are not Directors or executive officers of Harbor.

The enclosed proxy statement gives you detailed information about the Annual Meeting, the merger, and related matters. We urge you to read carefully the enclosed proxy statement, including the considerations discussed under SPECIAL FACTORS, beginning on page 12, and the appendices to the proxy statement, which include the merger agreement. Shareholders also are asked to reelect Nathaniel Higgs, Delores G. Kelley, Erich March, and Stanley W. Tucker as Class II Directors for three-year terms.

In deciding how to vote, you should consider that Directors and executive officers of Harbor have interests in addition to those as shareholders that may conflict with the interests of unaffiliated shareholders. Please see How do the Board of Directors and the executive officers recommend that I vote? on page 8.

It is important that your views be represented whether or not you attend the Annual Meeting. Your vote is important, whether you own a few shares or many. We urge you to vote your shares either in person at the Annual Meeting or by returning your proxy as soon as possible. **The Board of Directors recommends that shareholders vote FOR approval of the merger, FOR adjournment of the Annual Meeting, if necessary, and FOR reelection of the four Class II Directors.**

Sincerely,

Joseph Haskins, Jr.
Chairman, President, and Chief
Executive Officer

HARBOR BANKSHARES CORPORATION

25 West Fayette Street

Baltimore, Maryland 21201

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD __________ 2006

To Our Shareholders:

The Annual Meeting of Shareholders of Harbor Bankshares Corporation will be held at Harbor s main office at 25 West Fayette Street, Baltimore, Maryland 21201 on Wednesday, __________ 2006, at 12:00 noon Eastern Time, for the following purposes:

Proposal I To consider and vote upon a proposal to approve the Agreement and Plan of Merger, dated as of __________, 2006, by and between Harbor Bankshares Corporation and Harbor Merger Corporation, a Maryland corporation and wholly-owned subsidiary of Harbor Bankshares Corporation (the merger subsidiary), pursuant to which the merger subsidiary will merge with and into Harbor Bankshares Corporation, with Harbor Bankshares Corporation being the surviving corporation;

Proposal II To consider and vote upon the proposal for an adjournment of the Annual Meeting to solicit additional proxies for approval of Proposal I, if necessary.

Proposal III To elect four Class II Directors, each to serve for a three-year term; and

To act upon such other matters as may properly come before the Annual Meeting or any adjournments or postponements thereof.

Note: The Board of Directors is not aware of any other business to come before the Special meeting.

The Board of Directors has fixed the close of business on __________, 2006, as the record date for determination of shareholders entitled to vote at the Annual Meeting. The Harbor Board of Directors unanimously recommends that you vote **FOR** approval of the merger agreement, **FOR** an adjournment of the Annual Meeting to solicit additional proxies for approval of the merger agreement, if necessary, and **FOR** the election of four Class II Directors.

Only shareholders of record of Harbor Bankshares Corporation voting common stock at the close of business on the record date will be entitled to notice of, and to vote at the Annual Meeting or any adjournment thereof. To grant a proxy to vote your shares, you may complete and return the enclosed proxy card. You also may vote in person at the Annual Meeting. Please vote promptly whether or not you expect to attend the Annual Meeting. In the event that there are not sufficient votes to vote upon the merger or to approve other business properly before the Annual Meeting, the Annual Meeting may be adjourned in order to permit further solicitation of proxies by Harbor Bankshares Corporation.

You are requested to fill in and sign the enclosed Form of Proxy and to mail it in the enclosed envelope. The Proxy will not be used if you attend and choose to vote in person at the Annual Meeting. **Executed but unmarked proxies will be voted FOR Proposal I to approve the Agreement and Plan of Merger, FOR Proposal II for an adjournment of the Annual Meeting to solicit additional proxies for approval of Proposal I, if necessary. and FOR the election of the four Class II Directors.**

Harbor Bankshares Corporation s only class of voting stock is its common stock, par value $0.01 per share. A complete list of shareholders entitled to vote at the Annual Meeting will be available for inspection by any shareholder at the offices of Harbor Bankshares Corporation during ordinary business hours for a period of at least ten days prior to the Annual Meeting.

By Order of the Board of Directors,

George F. Vaeth, Jr.
Corporate Secretary

Baltimore, Maryland

__________2, 2006

Your Vote Is Important. Please promptly sign, date, and return the enclosed proxy card. If you attend the Annual Meeting and decide that you wish to vote in person or for any other reason desire to revoke your proxy, you can do so at any time prior to its use.

HARBOR BANKSHARES CORPORATION

25 West Fayette Street

Baltimore, Maryland 21201

PROXY STATEMENT

FOR THE ANNUAL MEETING OF SHAREHOLDERS

TO BE HELD ON __________ 2006

INTRODUCTION

This Proxy Statement is being sent to holders of the common stock, $0.01 par value, of Harbor Bankshares Corporation, a Maryland corporation (Harbor or the Company), in connection with the solicitation of proxies by the Board of Directors of Harbor for use at the 2006 Annual Meeting of Shareholders to be held at Harbor s main office at 25 West Fayette Street, Baltimore, Maryland 21201 on Wednesday, __________, 2006, at 12:00 noon Eastern Time, and at any adjournment or postponement of the meeting, for the following purposes:

Proposal I To consider and vote upon a proposal to approve the Agreement and Plan of Merger, dated as of __________, 2006, by and between Harbor Bankshares Corporation and Harbor Merger Corporation, a Maryland corporation and wholly-owned subsidiary of Harbor Bankshares Corporation (the merger subsidiary), pursuant to which the merger subsidiary will merge with and into Harbor Bankshares Corporation, with Harbor Bankshares Corporation being the surviving corporation;

Proposal II To consider and vote upon the proposal for an adjournment of the Annual Meeting to solicit additional proxies for approval of Proposal I, if necessary.

Proposal III To elect four Class II Directors, each to serve for a three-year term; and

To act upon such other matters as may properly come before the Annual Meeting or any adjournments or postponements thereof.

The purpose of the Agreement and Plan of Merger is to allow Harbor to eliminate the substantial expenses of being a Securities and Exchange Commission (SEC) reporting company under the Securities Exchange Act of 1934. If approved and completed, the merger will reduce the number of Harbor record shareholders to fewer than 300, and will allow Harbor to terminate the registration of its common stock under the Exchange Act.

In the merger, holders of record of 100 or fewer shares will receive $31.00 per share in exchange for their shares; holders of more than 100 shares will remain shareholders of Harbor after the merger. The merger cannot occur unless the merger agreement is approved by the holder of at least two-thirds (2/3) of the outstanding shares of Harbor common stock that are eligible to vote, including a majority of voting shares held by shareholders who are not Directors or executive officers of Harbor.

This document provides you with detailed information about the proposed merger. Please see the Summary Term Sheet on page 4 and the other material referred to therein for important additional information and WHERE YOU CAN FIND MORE INFORMATION on page 48 for additional information about Harbor on file with the SEC.

This Proxy Statement and the accompanying form of proxy are being sent to Harbor shareholders on or about __________, 2006.

Only shareholders of record of voting common stock at the close of business on __________, 2006, the record date, are entitled to notice of and to vote at the annual meeting and any adjournment or postponement of the meeting. As of __________, 2006, there were 675,579 shares of Harbor common stock, par value $0.01 per share, outstanding, consisting of 641,784 shares of voting common stock and 33,795 shares of nonvoting common stock.

The cost of soliciting proxies will be borne by Harbor. In addition to the solicitation of proxies by mail, Harbor also may solicit proxies personally or by telephone or other means through its Directors, officers, and regular employees. Harbor also will request persons, firms, and corporations holding shares in their names or in the name of nominees that are beneficially owned by others to send proxy materials to and obtain proxies from those beneficial owners and will reimburse the holders for their reasonable expenses in doing so.

For additional information regarding the annual meeting and related corporate matters, please see COMPANY CORPORATE GOVERNANCE on page 39 and THE ANNUAL MEETING on page 46.

This transaction has not been approved or disapproved by the Securities and Exchange Commission nor has the Commission passed upon the fairness or merits of such transaction or upon the accuracy or adequacy of the information contained in this document. Any representation to the contrary is unlawful.

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HARBOR BANKSHARES CORPORATION

PROXY STATEMENT

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PROPOSAL I AGREEMENT AND PLAN OF MERGER

SUMMARY TERM SHEET

This summary highlights selected information from this proxy statement regarding the proposed transaction and may not contain all of the information that is important to you. For a more complete description of the terms and conditions of the transaction and its effects, you should carefully read this entire document, the attachments, and any other documents to which we refer.

Why is Harbor proposing the merger?

The purpose of the merger is to reduce the number of shareholders of record below 300, which will enable Harbor to terminate the registration of its common stock under the Securities Exchange Act of 1934.

By terminating the Harbor s registration under that Act, we hope to:

- Achieve significant savings in ongoing legal and accounting costs related to the reporting process and shareholder communications required by the Act;
- Avoid significant expenses and efforts that would be necessary for the Company to comply with additional procedures relating to internal control that otherwise are required by year-end 2007 under the Sarbanes-Oxley Act and SEC regulations; and.
- Enable management, employees, and the Board of Directors to focus their efforts on the operations and management of the Company s business, rather than the reporting processes.

See SPECIAL FACTORS Reasons for the Merger on page 14.

What are the effects of not being a reporting company?

After we terminate the registration of our common stock, we will no longer prepare and file the quarterly, annual, and other reports and proxy statements with the Securities and Exchange Commission. We will continue to issue reports and proxy materials, but these may not contain all of the information that is contained in the annual report and proxy statements that Harbor currently distributes.

Harbor common stock is not currently traded on any exchange and will not be listed or quoted on any exchange following the merger, but is traded from time to time in the over the counter market. After we terminate the registration of our common stock, we will not be eligible for future quotation or listing on any stock exchange or organized market, and the number of trading markets where the shares may be traded by market makers will be limited.

Harbor and Harbor Bank will continue to be highly regulated and subject to periodic examination by federal and state bank regulatory agencies

See Special Factors Effects of the Merger on page 23 and Reasons for the Merger on page 14

What will I receive if the merger is approved by shareholders and becomes effective?

If the merger is approved by shareholders and becomes effective:

- Each holder of 100 or fewer shares of common stock will receive $31.00 in cash per share. Share ownership will be calculated by adding all shares registered in the same manner under procedures established by Harbor.
- Each holder of 101 or more shares of common stock will continue as a Harbor shareholder and will own the same number of shares as the holder owned before the merger.

When will the merger become effective?

The Board of Directors currently plans to make the merger effective within thirty calendar days of the date on which shareholders approve the merger.

Who are Filing Persons and Affiliates ?

Harbor, the merger corporation, and each of their Directors and executive officers are Filing Persons and Affiliates under the SEC rules that govern going-private transactions. Each of the Filing Persons and Affiliates has determined that the terms of the merger are substantively and procedurally fair to shareholders who will receive cash for their shares in the merger, unaffiliated shareholders who will not receive cash in the merger, and affiliated shareholders. No executive officers or Directors of Harbor own fewer than 101 shares of Harbor common stock, and, accordingly, no executive officers or Directors of Harbor will receive cash in the merger. As a result of the merger, the percentage of common shares beneficially owned by Directors and executive officers of Harbor will increase by less than 2%. See SPECIAL FACTORS INTRODUCTION on page 26.

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Does the Board of Directors believe that the terms of the merger are fair?

Yes. The Board of Directors and each of the executive officers believes that the terms of the merger, including the amount to be paid per share, are fair to and in the best interests of Harbor and all of its shareholders. In reaching its conclusion, the Board considered, among other things:

The matters discussed under Reasons for the Merger ;

The opinion of Harbor s financial advisor, Danielson Associates, as to the fair value of the common stock;

Harbor s financial performance since the date of the Danielson Associates opinion;

Harbor s current financial position and its available sources of liquidity;

Harbor s business and financial prospects;

The continued costs of compliance with Harbor s reporting obligations under the Exchange Act; and

The current and historical prices for our common stock and the liquidity of the market for the common stock.

The members of the Board of Directors and the executive officers have specifically determined that the transaction is financially and procedurally fair to unaffiliated shareholders. See Special Factors-Reasons for the Merger on page 14, -Recommendation of the Board of Directors; Fairness of the Merger Proposal on page 15, -Fairness Determination by Filing Persons on page 16, -Opinion of Financial Advisor on page 17, and -Price Adjustment since Opinion Date on page 22.

What is the merger, and how will Harbor be operated after the merger?

In the merger, Harbor Merger Corporation, a newly formed wholly-owned subsidiary of Harbor, will merge with and into Harbor, with harbor being the surviving corporation. As a result of the merger, shareholders who own 100 or fewer shares of Harbor common stock, except for shares owned by shareholders who properly exercise their rights to object to the merger, will receive $31.00 in cash for each share owned, without interest. Shareholders who own more than 100 shares of Harbor common stock will continue to hold shares of Harbor common stock and will not receive any cash in connection with the merger. Approximately 12,500 shares, or less than 2% of total outstanding shares, are expected to be exchanged for cash in the merger. The estimated costs of the merger, including cash to be paid to shareholders with 100 or fewer shares, is $442, 143, or less than 3% of total stockholder s equity at March 31, 2006.

After the merger, Harbor will continue to operate as a bank holding company and as the parent corporation for Harbor Bank, and expects its business and operations to continue as they are currently being conducted, but without the need to file reports with the SEC. Also, the executive officers and Directors of Harbor will continue to be the executive officers and Directors of Harbor following the merger. We expect to complete the merger in ________ 2006.

See: THE MERGER AGREEMENT on page 34 and the copy of the merger agreement attached as Appendix A.

What vote is required to approve the merger agreement?

The affirmative vote of least two-thirds (2/3) of the outstanding shares of Harbor common stock eligible to vote is needed for approval of the merger. Members of Harbor s Board of Directors and executive officers having the power to vote approximately 193,177 or 30.1% of the 641,784 outstanding voting shares have indicated that they intend to vote FOR the merger. The members of the Board of Directors and the executive officers do not intend to acquire any additional shares of common stock prior to approval of the merger. The approval of approximately 52% of the remaining 448,607 outstanding voting shares owned by other, unaffiliated shareholders will be required for approval of the merger. All holders of record of Harbor voting common stock as of _________________, 2006, will receive a copy of this proxy statement and are entitled to vote at the Annual Meeting.

Who is entitled to vote?

Shareholders of voting common stock as of the close of business on __________, 2006, the record date, are entitled to vote at the meeting. Each share of voting common stock is entitled to one vote. See The Annual Meeting-Shares Entitled to Vote; Quorum and Vote Required on page 46.

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How do the Board of Directors and the executive officers recommend that I vote?

The Board of Directors, by a unanimous vote, has approved the merger agreement and recommends that you vote FOR approval of the merger agreement. Executive officers who are not Directors also recommend that you vote FOR approval. You should note that all of the Directors and executive officers own more than 100 shares and expect to remain Harbor shareholders after the merger, and that no Director or executive officer is expected to receive cash in the merger. As you consider the recommendation of the Board of Directors, you should be aware that the Directors and officers of Harbor have interests in addition to their interests as shareholders of Harbor that may conflict with the interests of shareholders who will be cashed out in the merger or non-affiliated shareholders who will not be cashed out in the merger. See Special Factors-Interests of Executive Officers and Directors in the Merger on page 26.

How do I vote?

Each shareholder should sign and date the enclosed proxy card and return it to us in the prepaid envelope. Unless contrary instructions are indicated on the proxy, all shares represented by valid proxies received pursuant to this solicitation will be voted in favor of the merger and in favor of the election of all nominees as Director. If you own your shares through a bank, broker, or other nominee, you must vote through your record holder. See THE ANNUAL MEETING on page 46.

Do I have appraisal or dissenter s rights?

Yes. If the merger is approved by the shareholders and is completed, any shareholder who properly perfects his or her right to object to the merger will be entitled to receive an amount of cash equal to the fair value of his shares rather than the consideration provided by the merger agreement. See APPRAISAL RIGHTS OF HARBOR SHAREHOLDERS on page 30.

What are the federal income tax implications of the merger?

The receipt of cash in the merger will be taxable for United States federal income tax purposes. You will be treated as either having sold your shares of Harbor common stock for the cash received or as having received the cash as a dividend. In general, your receipt of cash in exchange for your shares of Harbor common stock will be treated as a sale or exchange and you will recognize gain or loss in an amount equal to the cash received less your adjusted tax basis of your shares exchanged for such cash if you actually and constructively own no shares of Harbor common stock immediately after the exchange. If you actually or constructively own shares of Harbor common stock after the exchange, your receipt of cash in exchange for your shares of Harbor common stock may be taxed as a dividend. Shareholders who do not receive cash should not recognize any gain or loss on continuing to hold their shares of Harbor common stock as a result of the merger.

See SPECIAL FACTORS Material U.S. Federal Income Tax Consequences on page 28.

Should I send in my certificates now?

No. After the effectiveness of the merger, holders of 100 or fewer shares will be sent a letter of transmittal and instructions for submitting shares for payment. Holders of 101 or more shares will not be required to exchange their certificates. See THE MERGER AGREEMENT Exchange of Certificates on page 35.

Who can help answer my questions?

If you have additional questions about the merger, you should contact Teodoro J. Hernandez, Vice President and Treasurer, at Harbor Bankshares Corporation, 25 West Fayette Street, Baltimore, MD 21201, telephone (410) 528-1800.

STATEMENT REGARDING FORWARD-LOOKING INFORMATION

This proxy statement and the documents incorporated by reference in this proxy statement include forward-looking statements such as: statements of Harbor s goals, intentions, and expectations; estimates of risks and of future costs and benefits; and statements of Harbor s ability to achieve financial and other goals. These forward-looking statements are subject to significant uncertainties because they are based upon: the amount and timing of future changes in interest rates, market behaviors, and other economic conditions; future laws and regulations; and a variety of other matters. Because of these uncertainties, the actual future results may be materially different from the results indicated by these forward-looking statements. In addition, Harbor s past performance does not necessarily indicate its future results.

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SUMMARY FINANCIAL INFORMATION

Selected Historical Financial Information

	As of and for the Three Months Ended March 31,		As of and for the Years Ended December				
	2006	**2005**	**2005**	**2004**	**2003**	**2002**	**2001**
	(Dollars in thousands, except per share data)						
Operations Data:							
Interest income	$4,144	$3,428	$15,014	$12,648	$11,886	$11,647	$13,609
Interest expense	1,346	743	3,787	2,283	2,411	3,402	5,973
Net interest income	2,798	2,685	11,227	10,365	9,475	8,245	7,636
Provision for loan losses	55	120	410	360	755	340	400
Non-interest income	375	492	1,771	1,514	2,506	2,220	2,329
Non-interest expense	2,415	2,598	9,638	9,295	8,610	8,575	8,526
Income before taxes	703	459	2,950	2,224	2,616	1,550	1,039
Income taxes	256	165	1,067	762	831	473	309
Net income	$447	$294	$1,883	$1,462	$1,785	$1,077	$730
Per Share Data:							
Net income-basic	$0.66	$0.42	$2.73	$2.07	$2.46	$1.47	$1.02
Net income-diluted	0.62	0.39	2.55	1.93	2.36	1.43	0.99
Cash dividends declared per share	0.50	0.40	0.40	0.35	0.25	0.25	0
Book value per share	24.82	22.62	24.73	23.04	21.69	19.23	16.72
Balance Sheet Data:							
Total assets	$250,955	$234,799	$256,636	$235,464	$219,547	$210,234	$186,586
Deposits	221,917	210,230	229,845	210,224	195,901	193,294	171,531
Total net loans	200,545	177,291	188,936	172,205	149,729	120,523	105,847
Total shareholders equity	16,785	15,796	16,954	16,240	15,274	14,149	12,241
Performance Ratios:							
Return on average assets	0.70 %	0.50 %	0.78 %	0.63 %	0.84 %	0.54 %	0.37 %
Return on average equity	10.72	7.29	11.57	9.33	12.23	8.20	6.20
Dividends declared to diluted net income	80.65	102.56	15.69	18.13	10.59	17.48	NA
Capital Ratios:							
Tier 1 regulatory capital to average assets	7.20 %	7.40 %	7.31 %	7.36 %	7.46 %	5.20 %	5.40 %
Average equity to average assets	6.53	6.90	6.74	7.27	6.48	5.24	4.77

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Summary Unaudited Pro Forma Financial Information

The following table sets forth the Harbor s shareholders equity accounts as of March 31, 2006, and pro forma equity accounts as of such date as if the merger were then effective, resulting in the cashing out of 12,478 shares of common stock for an aggregate payment of $442,143, including payments for shares of stock of $386,818 and payment of related professional and other costs of $55,325. Shares acquired will be classified as authorized and unissued. Harbor s shareholder s equity as of the date of this proxy statement, the date of the Annual Meeting, or as of any other day, may be higher or lower than the amount set forth below, as a result of earnings or losses from operations, the payment of dividends or other distributions, and changes in the value of Harbor s available for sale securities. This table indicates that, on a pro forma basis, book value per share decreases by $0.20, or less than 1%, as a result of the merger,

(In thousands, except per share data)	**Actual**	**Pro forma**
Common stock (par value $0.01 per share):		
Authorized 10,000,000 shares; issued 675,579, including 33,795 common nonvoting Shares	$7	$7
Additional paid in capital	6,365	5,923
Retained earnings	10,958	10,958
Accumulated other comprehensive loss	(565)	(565)
Total Shareholders Equity	$16,765	$16,323
Common equity per share	$24.82	$24.62

The following table sets forth Harbor s and the Bank s actual and estimated pro forma regulatory capital ratios as of December 31, 2005, as if the merger were effective as of that date, resulting in the cashing out of 12,478 shares of common stock for an aggregate payment of $442,143.

	Actual	**Pro forma**
Total Capital to risk weighted assets		
Harbor Bankshares Corporation	11.17%	10.98%
Harbor Bank of Maryland	11.07%	10.83%
Tier I Capital to risk weighted assets		
Harbor Bankshares Corporation	8.65%	8.43%
Harbor Bank of Maryland	10.06%	9.83%
Tier I Capital to average assets		
Harbor Bankshares Corporation	7.20%	7.102%
Harbor Bank of Maryland	8.38%	8.19%

The above table indicates that, on a pro forma basis, regulatory capital ratios decrease by less than 25 one-hundredth of a percent and remain in excess of the levels required for well capitalized status for regulatory purposes.

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CONSOLIDATED UNAUDITED RATIO OF EARNINGS TO FIXED CHARGES

Ratio of Earnings to Fixed Charges

	Quarter Ended March 31, 2006	Years ended December 31 2005	2004	2003	2002	2001
INCLUDING INTEREST ON DEPOSITS						
Earnings:						
Pre-tax income (loss)	$ 703	$2,951	$2,224	$2,616	$1,550	$1,039
Plus: Fixed charges	1,368	3,851	2,333	2,514	3,541	6,118
Total Earnings	$ 2,071	$6,802	$4,557	$5,130	$5,091	$7,157
Fixed Charges:						
Interest expensed and capitalized interest	$ 1,346	$3,787	$2,283	$2,411	$3,402	$5,973
Rent expense (for operating leases)	73	213	168	343	464	482
Ratio of interest expense included in rent expense	30 %	30 %	30 %	30 %	30 %	30 %
Estimated interest within rental expense	21.9	63.9	50.4	102.9	139.2	144.6
Total Fixed Charges	$ 1,368	$3,851	$2,333	$2,514	$3,541	$6,118
Ratio of Earnings to Fixed Charges with Interest on Deposits	151 %	177 %	195 %	204 %	144 %	117 %
EXCLUDING INTEREST ON DEPOSITS						
Earnings:						
Pre-tax income (loss)	$ 703	$2,951	$2,224	$2,616	$1,550	$1,039
Plus: Fixed charges	153	529	381	278	280	296
Total Earnings	$ 856	$3,480	$2,605	$2,894	$1,830	$1,335
Fixed Charges:						
Interest expensed and capitalized interest	$ 131	$465	$331	$175	$141	$151
Rent expense (for operating leases)	73	213	168	343	464	482
Ratio of interest expense included in rent expense	30 %	30 %	30 %	30 %	30 %	30 %
Estimated interest within rental expense	21.9	63.9	50.4	102.9	139.2	144.6
Total Fixed Charges	$ 153	$529	$381	$278	$280	$296
Ratio of Earnings to Fixed Charges without Interest on Deposits	560 %	658 %	683 %	1041 %	653 %	451 %

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SPECIAL FACTORS

Background of the Merger

Harbor was organized in 1992 to be the registered holding company for the Bank. Harbor became a public company filing reports with the Securities and Exchange Commission in 1992. No organized market for the Harbor common stock has ever existed, however, and trading is infrequent and sporadic. From time to time over the years, management has informally discussed the alternatives available to the Company to cease being a reporting company and the relative benefits and costs of deregistration with counsel to the Company. No formal presentations were made by counsel or management on this issue, and no outside evaluation or opinion as to the value of the Company s common stock was solicited. No follow-up on these discussions occurred, and the Company continued to file reports and other documents with the Securities and Exchange Commission.

In July 2002, the Public Company Accounting Reform and Investor Protection Act of 2002, commonly referred to as Sarbanes-Oxley, was signed into law. Although Sarbanes-Oxley was enacted in 2002, many of its provisions and the provisions of regulations of the Securities and Exchange Commission that were required by Sarbanes-Oxley, did not immediately take effect, but instead have been implemented over time. Some provisions are still in the process of implementation. Since its enactment, Sarbanes-Oxley has created significant additional and increasing regulatory burdens and costs for Harbor. However, Harbor will not bear the full burden of Sarbanes-Oxley until, at the earliest, the application to Harbor of the requirements regarding internal controls over financial reporting under Sarbanes-Oxley Section 404, which is now scheduled for year end 2007. Harbor estimates of the costs of Section 404 compliance and the experience of the larger companies that were required to comply at year-end 2004 with these requirements indicates that significant costs and burdens will result from compliance with Section 404 in addition to the substantial burdens and costs that currently apply to Harbor.

Management and the Board of Directors from time to time received information from Company counsel, its independent accountants, banking industry trade groups, and other sources regarding the requirements of these new provisions of law and regulation. As a result of the implementation of these new provisions, management and the Board of Directors became concerned that the new procedures and disclosures required to comply with Sarbanes-Oxley would significantly increase the management, staff, and Board time and resources dedicated to the securities reporting and disclosure process, including the time needed for training employees in the particulars of the new provisions and additional procedures involved in the management attestations and certifications of internal controls and financial statements. Concern also arose with respect to potential increases in expenses incurred for those processes, including the fees of counsel, accountants, and other compliance advisors and service providers. The Board of Directors and management were also concerned about the potential additional civil and criminal proceedings or liabilities to which the President and Chief Financial Officer could become subject as a result of the new financial statement certification requirements, and Harbor s potential liability to indemnify them if they successfully defended themselves, and the costs of the Company s participation in any such suit, investigation, or proceeding.

In the third quarter of 2004, management informally discussed with Harbor s special legal counsel the ability to deregister, and the procedure Harbor should follow in pursuing a possible deregistration transaction. Following those discussions, management began a study of the potential costs and benefits to Harbor of deregistration, and, from time to time, had additional discussions with legal counsel regarding deregistration and the costs of Sarbanes-Oxley compliance and of fulfilling the reporting obligations of a public company. At a regular meeting of the Board of Directors on May 11, 2005, management discussed the effects on Harbor and its shareholders of deregistration and the related costs and benefits, and formally proposed that the Board of Directors consider a transaction which would result in the reduction of the number of shareholders of record sufficient to permit the Company to deregister the common stock under the Securities Act of 1934. Following discussion, the Board voted to proceed with the process in general, but did not at that time determine the timing, structure, or terms of any transaction. Following that meeting, members of management engaged in further discussions with legal counsel and Harbor s independent accountants regarding the process of deregistration, and began the preparation of the necessary filings. After considering the proposals of several investment banking and financial advisory firms experienced in the valuation and appraisal of financial institutions, Harbor retained the firm of Danielson Associates, Inc., Rockville, Maryland, to provide it with an appraisal of the shares and an opinion that the price to be paid for shares which would be cashed out was a fair price for the common stock. Danielson Associates was selected because of its extensive experience, over a twenty year period, in the valuation and appraisal of financial institutions in connection with mergers, acquisitions, stock offerings, repurchases, fairness opinions, and similar matters; its reputation in the financial services industry for providing such services; the recommendation of counsel, who had previously worked with Danielson Associates; and the price of obtaining the appraisal and opinion from Danielson Associates, which was substantially below the prices quoted by other investment banks. Danielson Associates also had assisted Harbor with respect to the valuation of its common stock in the past. The opinion of Danielson Associates is summarized below, and its fairness opinion is attached as Appendix B hereto.

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Harbor s Board of Directors considered the deregistration at its regular meeting on December 14, 2005. In attendance for its consideration of this matter were a representative of Danielson Associates and outside legal counsel as well as the President and CEO and the Treasurer. At that meeting, the Board discussed the structure and effects of deregistration of Harbor as a public company and the merger; the effects of the merger on Harbor, on shareholders whose shares would be acquired in the merger, and on the remaining shareholders; the fiduciary duties of Directors to shareholders; and related matters. In the meeting, outside legal counsel described the process and alternative structures of deregistration to the Board, and the representative of Danielson Associates presented its report, which had previously been distributed to the Board, regarding the fair value of Harbor common stock. Following discussion, the Board unanimously determined that the merger was fair to Harbor and its shareholders, established a price of $29.00 per share to be paid per share to shareholders whose shares would be purchased in the merger, and authorized and directed executive management to proceed with the appropriate actions to effect the merger. The Board of Directors subsequently increased the price to $31.00 per share. See Price Adjustment since Opinion Date on page 22.

As described below, Harbor s Board of Director s determined that the accomplishing the deregistration by merger was superior to each of the alternatives discussed at its meeting of December 14, 2006:

Tender Offer. In a tender offer, Harbor would offer to purchase common shares, following the rules established for tender offers by the Securities and Exchange Commission. This method allows shareholders to choose whether or not to have their shares cashed out, as long as the conditions to the tender offer are met. The primary disadvantage to this method is the lack of certainty that a sufficient number of holders will tender their shares to allow the deregistration.

Reverse Split. In a reverse split, Harbor would exchange one new share of common stock for a fixed number of outstanding shares, but would pay cash instead of issuing any fractional shares. The exchange ratio in a reverse split would be based upon the estimated number of shareholders to be cashed out in order to reduce the number of record holders below 300. Just as in the case of the merger: (i) approval of more than 2/3 of the common stock entitled to vote would be required; (ii) shares would be required to be cashed out; and (iii) shareholders would be entitled to appraisal rights. The primary disadvantage of this method is the increased cost necessitated by the cashing out of fractional shares of holders who would remain record holders after the reverse split. In addition, Harbor believes that reverse splits are more complex and more difficult to explain to shareholders than mergers.

Market Acquisition of Shares. Acquisition of shares on the market was believed to be impractical, given the lack of an established trading market. This method also (i) would not provide any certainty that the number of shareholders would be reduced by a sufficient number, and (ii) would allow shareholders to sell a part of their holdings, while continuing to be record holders of other shares.

The Board of Directors determined the 100-share threshold for determination of shareholders who will be cashed out in the merger based upon the round number of shares held of record to be cashed out that would be likely to result in fewer than 300 post-merger record holders without unnecessary cost. The determination was not based upon the identity of any shareholders or on any characteristics of any holder or group of holders other than the number of shares held of record.

At its meeting of April 19, 2006, the Board reviewed the price to be paid to shareholders whose shares will be purchased in the merger based upon factors it previously had considered and upon the performance of Harbor since the original price was determined. As a result of that review, the Board unanimously increased the price to be paid per share in the merger to $31.00 per share from the original $29.00 per share. See Price Adjustment since Opinion Date on page 22.

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See Special Factors Recommendation of the Board of Directors; Fairness of the Merger Proposal on page 15, and SUMMARY FINANCIAL INFORMATION on page 9.

Reasons for the Merger

The primary purpose of the merger is to reduce the number of holders of the common stock below 300, which will enable Harbor to suspend filing periodic and annual reports with the SEC and to no longer incur the significant costs of complying with the reporting requirements of the Exchange Act. The elimination of those requirements will allow management to refocus the time spent preparing reporting documents and engaging in securities law compliance activities onto the pursuit of operational and business goals. In considering the proposed amendments, the Board of Directors considered the benefits and costs to Harbor and the shareholders set forth below, and the factors discussed under the caption Background of the Merger.

Harbor believes that as a result of the merger it will be able to realize cost savings of at least $87,600 annually by eliminating the requirements to make periodic public reports and by reducing the expenses of shareholder communications, including legal expense ($12,000), accounting expense ($30,000), printing ($20,000), postage ($1,800), data entry, stock transfer, and other administrative expenses ($7,500), as well as a result of reduced staff and management time ($10,000) spent on reporting and securities law compliance matters, and reduction in aggregate total dividend costs ($6,300). In addition, Harbor will avoid the costs of initial compliance with the internal control over financial reporting systems requirements of the Sarbanes Oxley Act, currently expected to be required for public companies of Harbor s size by year-end 2007, which are estimated to range from $150,000 to $200,000, and continued annual costs of related compliance and reporting in amounts not determined. The Board of Directors believes that the increased disclosure and procedural requirements will result in continuing increased legal, accounting, and administrative expense, and the diversion of Board of Directors, management, and staff effort without a commensurate benefit to the shareholders.

Given the absence of a public market for the common stock, and the sporadic and limited trading in the common stock, the Board of Directors does not believe that the costs of reporting are justified. Harbor s earnings are sufficient to permit Harbor s expected growth, and Harbor is not dependent on access to the capital markets to obtain additional financing. If it becomes necessary to raise additional capital, Harbor believes that there are adequate sources of additional capital available, whether through borrowing at the holding company level, or through private or institutional sales of equity or debt securities, although there can be no assurance that Harbor will be able to raise additional capital when required, or that the cost of such capital will be attractive.

The merger is expected to result in the cashing-out at a price determined to be fair by the Board of Directors of the common stock owned by approximately 360 shareholders (58% of the total number of record holders) who, at the Effective Time of the merger, own 100 or fewer shares of Harbor common stock. However, these shareholders together own less that 2% of Harbor s outstanding common stock.

Harbor and the Bank would continue to be minority-owned institutions after the merger.

The merger will enable small shareholders to divest themselves of their positions without the expenditure of efforts disproportionate to the value of their holdings, without transaction expenses, and at a price which is significantly higher than recent trades of which Harbor is aware, which have ranged from $25.00 to $28.00 per share. Shareholders who receive cash in the merger generally are expected to be subject to federal income taxes on any gains as if the shares were sold on the market. (See SPECIAL FACTORS Material U.S. Federal Income Tax Consequences on page 28.)

The merger and deregistration will have little if any effect on the ability to trade common stock, as no organized market currently exists. Trades will continue to be the result of direct communications between buyers and sellers. The amount paid for the shares being cashed out may result in an increase in the pricing level of future trades, although there can be no assurance that higher prices for the common stock will result or that a continuing shareholder will be able to sell shares at the price being paid to shareholders being cashed out.

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Operating as a private company will allow management to better focus its efforts on the operations of the Bank, which will benefit our customers and the communities in which we operate.

The merger will permit a significant percentage of our shareholders to continue as shareholders and to enjoy the benefits of share ownership, including dividends, when and if declared, potential capital appreciation, and civic benefits from owning shares in a community oriented institution such as Harbor. At the same time, Harbor will be relieved of significant expense and diversion of management time and effort, which may result in improved operating efficiencies and reduced need for additional compliance-related employees, and in potentially increased net earnings.

Harbor and the Bank would continue to be highly regulated and subject to periodic examination by the federal and state bank regulatory agencies. The management and Board of Directors of Harbor would not be affected by the transaction. Substantial information about Harbor s financial affairs would remain available to interested shareholders.

Harbor believes that no material adverse impact on Harbor s financial position would result from the transaction. The payment of cash from Harbor s capital accounts, however, could result in a future reduction in earnings or reduced asset levels as a result of reduced capital levels and compliance with regulatory capital requirements. The Board of Directors considered the impact of reduced capital levels, but determined that Harbor s and Bank s capital levels would remain more than sufficient to meet the levels required for well capitalized status under applicable regulations after the merger, and that any reduction in income resulting from reduced assets would likely be offset by cost savings realized as a result of deregistration.

The Board of Directors has determined that the price to be paid for the shares of Harbor common stock to be cashed out in the merger is fair and that this deregistration transaction is procedurally fair to Harbor shareholders who will be cashed out in the merger. The Board of Directors also has determined that the transaction is financially and procedurally fair to the remaining shareholders of Harbor, including non-affiliates and affiliates. The Board of Directors has determined that the price at which shares will be cashed out is a fair price for the Harbor common stock. In reaching this conclusion the Board of Directors considered the valuation factors summarized in the opinion of its financial advisor, the performance of Harbor since that opinion was rendered, and the factors stated above and under Recommendation of the Board of Directors; Fairness of the Merger Proposal, below. In particular, the Board considered that the $31.00 price represents 11.2 times trailing twelve month earnings at March 31, 2006, and 125% of book value per common share at March 31, 2006.

Recommendation of the Board of Directors; Fairness of the Merger Proposal

The Board of Directors has unanimously determined that the merger is in the best interests of Harbor and all of its shareholders, and is substantively and procedurally fair to: (i) shareholders who will receive cash for their shares in the merger, and (ii) other unaffiliated shareholders. The Board also believes that the process by which the transaction was approved is fair to all of Harbor s shareholders, and fair to unaffiliated shareholders receiving cash in the merger as well as those unaffiliated shareholders who will retain their shares after the merger. The Board s determination as to the per share price of $31.00 was made at following a vote of the members of the Board of Directors at which the price was approved by a unanimous vote. As set forth in the section entitled Special Factors Background of the merger, prior to voting upon the per share price, the members of the Board of Directors agreed that the going-private transaction is in the best interests of Harbor and all of its shareholders and, based upon the report and opinion provided by Danielson Associates and other factors, unanimously agreed that the per share price to be paid in the merger is fair to all of the shareholders of Harbor and unanimously approved the merger agreement, which included the $31.00 per share price. The Board of Directors adopted the conclusions and analysis of the Danielson Report. The Board of Directors also believes that the process by which the transaction is to be approved by shareholders is fair. The Board of Directors established that the transaction is procedurally fair to the unaffiliated shareholders although it did not retain separate, independent counsel or appraisers to represent solely unaffiliated shareholders. The Board of Directors, however, satisfied the procedural and other requirements of Maryland law, which require it to act in the best interests of all of its shareholders, require the approval of a super-majority of more than 2/3 of the shares entitled to vote as a condition to the merger; and provide dissenter s appraisal rights. Because officers and Directors own approximately 30% of outstanding shares that will be entitled to vote in the merger and have pledged not purchase any additional shares of common stock prior to the vote of shareholders, approval of the merger effectively requires the approval of more than a majority of unaffiliated shareholders. As described further below, the Board of Directors obtained the opinion of an independent financial advisor as to the fairness of the cash-out price to all shareholders, including, specifically, unaffiliated shareholders. The Board of Directors has increased the cash out price consistent with the analysis of the financial advisor. In light of these factors, the Board believes that appointing separate independent counsel or appraisers is unnecessary, and would unnecessarily require additional expense.

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The Board of Directors unanimously recommends that the shareholders vote **FOR** approval of the merger agreement. Each member of the Board of Directors and each executive officer of Harbor has advised Harbor that he or she intends to vote his or her shares in favor of the merger agreement for the reasons described above. As you consider the recommendation of the Board of Directors, you should be aware that the Directors and officers of Harbor have interests in addition to their interests as shareholders of Harbor that may conflict with the interests of shareholders who will be cashed out in the merger or non-affiliated shareholders who will not be cashed out in the merger. See Special Factors-Interests of Executive Officers and Directors in the Merger on page 26.

As of __________, 2006, the Directors and executive officers of Harbor and the Bank (16 persons) beneficially owned a total of 193,177 shares of Harbor s outstanding common stock, or approximately 30.1% (not including any shares that may be acquired pursuant to the exercise of stock options), of the total shares entitled to vote at the Annual Meeting. None of these officers or Directors intends to acquire additional shares of common stock before the merger agreement is approved. Accordingly, the approval of unaffiliated shareholders owning an additional 234,679 shares is necessary for the approval of the merger agreement.

The Board has the authority to reject (and not implement) the merger (even after approval thereof by shareholders) if it determines subsequently that the merger is not then in the best interests of Harbor and its shareholders.

Merger Subsidiary s Determination of Fairness of the Merger Proposal

The merger subsidiary and its Board of Directors believe that the merger is fair to, and in the best interests of, all of Harbor s shareholders. The merger subsidiary and its Board of Directors have determined that the merger is fair to the unaffiliated shareholders who will receive cash in the merger and those who will retain their shares of Harbor common stock after the merger. The merger subsidiary and its Board also believe that the process by which the transaction was approved is fair to all of Harbor s shareholders and have concluded that the process was fair to unaffiliated shareholders receiving cash in the merger as well as those unaffiliated shareholders who will retain their shares after the merger. In reaching its conclusions, the merger subsidiary relied upon the factors considered by, and has expressly adopted the analyses and conclusions of, Harbor s Board of Directors. See Special Factors Recommendation of the Board of Directors; Fairness of the Merger Proposal on page 15. Merger subsidiary has not received a report, opinion, or appraisal from an outside party. The merger agreement has been approved by merger subsidiary s Board of Directors and by Harbor, as the sole shareholder of merger subsidiary.

Fairness Determination by Filing Persons

Our Directors and executive officers are deemed to be filing persons under the SEC rules that govern going-private transactions. These rules require each filing person to state whether he or she believes that the transaction is fair to unaffiliated security holders. The filing persons consist of the following individuals: Joseph Haskins, Jr., Teodoro J. Hernandez, Darius L. Davis, James H. DeGraffereidt, Jr., Louis J. Grasmick, Nathaniel Higgs, Delores G. Kelley, Erich March, Garnetta Massey, John Paterakis, John D. Ryder, James Scott, Jr., Edward St. John, Walter S. Thomas, Stanley W. Tucker, and George F. Vaeth, Jr. (together, the Filing Persons).

In forming his or her belief as to the fairness of the transaction to the unaffiliated shareholders, each of the Filing Persons has relied upon the factors considered by Harbor s Board of Directors, including Danielson Associates analyses and opinion, and has adopted Harbor s Board of Directors analysis and conclusions. See Special Factors Recommendation of the Board of Directors; Fairness of the Merger Proposal. Based on those factors, each of the Filing Persons believes that the merger agreement and the process by which the transaction was approved are fair to each of the unaffiliated shareholders, including those who will receive cash in the merger and those who will retain their shares of Harbor common stock. The Filing Persons have not received any report, opinion, or appraisal from an outside party that is materially related to the merger other than the report of Danielson Associates. The belief of each of the Filing Persons is his or her individual belief and does not constitute investment advice. If a shareholder is unsure of whether to vote in favor of the merger agreement, that shareholder should consider the recommendation of the Board of Directors or consult with the shareholder s personal financial advisor.

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Each of the Filing Persons also adopts the purpose and reasons for the merger, and the decision regarding the alternative structures for the going private transaction of the Board of Directors. See SPECIAL FACTORS Background of the Merger on page 12, and Reasons for the Merger on page 14.

Opinion of Financial Advisor

Harbor retained Danielson Associates Inc. (Danielson Associates) to perform an independent appraisal of the fair market value of the common stock of Harbor as of December 8, 2005. Market value is defined as the price at which the common stock would change hands between a willing seller and a willing buyer, each having reasonable knowledge of relevant facts and assuming a significant amount of stock changing hands daily to assure a true reflection of market forces. Danielson Associates rendered its written and oral opinion as of December 8, 2005, to the Harbor at its meeting of the Board of Directors on December 14, 2005. No limitations were imposed by Harbor s Board of Directors upon Danielson Associates with respect to the investigation made or procedures followed by it in arriving at its opinion. The description of the opinion in this proxy statement has been reviewed by Danielson Associates, and is in a form acceptable to it.

Danielson Associates is regularly engaged in the valuation of banks and bank holding companies in connection with mergers, acquisitions, and other securities transactions; and has knowledge of, and experience with Maryland and other mid-Atlantic markets and banking organizations operating in those markets. Danielson Associates was selected by Harbor because of its knowledge of, expertise with, and reputation in the financial services industry.

In arriving at its opinion, Danielson Associates:

- Reviewed certain business and financial information relating to Harbor including reports of condition and income and related schedules (commonly referred to as call reports) filed by the Bank with federal banking regulators from 1990 through September 30, 2005, the annual reports of Harbor on Form 10-KSB for 2003 and 2004 and the quarterly report of Harbor on Form 10-QSB for September 30, 2005.
- Discussed the past and current operations, financial condition, and prospects of Harbor with its senior executives.
- Reviewed and compared the pricing ratios, to the extent publicly available, with those of comparable institutions.
- Considered such other factors as it deemed appropriate.

Danielson Associates did not obtain any independent appraisal of assets or liabilities of Harbor. Further, Danielson Associates did not independently verify the information provided by Harbor and assumed the accuracy and completeness of all such information.

In arriving at its opinion, Danielson Associates performed a variety of financial analyses. Danielson Associates believes that its analyses must be considered as a whole and that consideration of portions of such analyses could create an incomplete view of Danielson Associates appraisal. The preparation of an appraisal of fair market value is a complex process involving subjective judgments and is not necessarily susceptible to partial analysis or summary description.

In its analyses, Danielson Associates made certain assumptions with respect to industry performance, business and economic conditions, and other matters, many of which were beyond Harbor s control. Any estimates contained in Danielson Associates analyses are not necessarily indicative of future results of value, which may be significantly more or less favorable than such estimates. Estimates of the value of companies do not purport to be appraisals or necessarily reflect the prices at which companies or their securities may actually be sold.

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The following is a summary of selected analyses considered by Danielson Associates in connection with its opinion.

Comparable Companies. In determining what is a fair price for the outstanding shares of Harbor common stock, Harbor was compared with four groups of publicly-traded banking organizations. The first group is comprised of fourteen commercial banking organizations based in urban areas that have assets between $150 and $500 million, have returns on average assets above .50%, and trade on a national exchange (urban exchange group). The second group consists of eleven commercial banking organizations with the same restrictions as the urban exchange group but which trade instead on the over-the-counter bulletin Board market (urban OTC group). These banking organizations are sometimes referred to as banks for simplicity. The banks in these groups are either small urban banks or minority-owned banks. The analysis was complicated by the fact that very few small urban banks or banks that are minority-owned have publicly traded stock. However, the banks in these four groups are similar to Harbor and are believed to provide the best measurement of Harbor s stock value. The initial comparisons are to three groups of non-minority banks in urban areas, but the primary comparison on which Harbor s valuation is based is to a group comprised of other minority-owned banks. The composition of the comparable company groups is described below.

Urban Exchange Group This group is comprised of fourteen commercial banks based in urban areas along the east coast that have assets between $150 and $500 million, have returns on average assets above .50%, and trade on a national exchange. The stocks of these banks, with three exceptions, trade on average more than 2,000 shares each day.

Urban OTC Group This group consists of eleven commercial banks with the same restrictions as the urban exchange group, but which trade on the over-the-counter bulletin board market. The stocks of most of these banks are less liquid than those of the urban exchange group and trade on average a little over 900 shares each day.

Urban Most Applicable Group Since the first two groups contained several newly-formed banks and banks with much better performance than Harbor, a third group was created from the banks in the urban exchange group and the urban OTC group which eliminated those less comparable banks. The remaining seven banks are the banks most applicable to Harbor based on location, performance, and history.

Minority-Owned Group Includes banks that are among the total seventeen minority-owned publicly-traded banks. Several different minorities are represented in the total seventeen institutions African-American, Hispanic, and Asian and women. Some of these banks are comparable to Harbor but others because of their size, performance, or minority orientation are not comparable. Accordingly, banks with assets over $900 million or other attributes that would make them not comparable to Harbor were excluded from this group. The remaining four minority-owned banks are most comparable to Harbor

The first two groups of urban comparables, and the third group which is a mix of the first two, provides a base from which to view the pricing of a non-minority-owned bank located in a city. As will be discussed later, minority-owned banks tend to serve larger more densely populated urban areas and typically have a lower valuation.

Financial Comparisons

Urban Exchange Group. The urban exchange group s financial performance was comparable to Harbor s. The urban exchange group s median returns on average assets and equity of .78% and 9.74% were similar to Harbor s .74% and 10.94%, respectively. Additionally, nonperforming assets (NPAs) as a percent of assets were .38% for Harbor which was higher, but not much higher, than the .22% for the comparable group. The urban exchange group had equity-to-assets of 8.24% while Harbor s was 6.66%. Harbor s net interest income of 4.61% of average assets in the nine months ending September 30, 2005, was much higher than the urban exchange group median of 3.65%, but this was more than offset by net operating expense that was about one and a half times the comparative group s median. The urban exchange group s stock price multiples were diverse. The price times earnings multiples for the fourteen banks, ranged from 12.8 to 34.0 times earnings, with a median of 22.7 times earnings. The price-to-book ratios also had a wide range with a low of 143%, a high of 288% and the median was 178%.

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Urban OTC Group. The urban OTC group performed much better than Harbor with median returns on average assets and equity of 1.12% and 14.18%, respectively, compared to .74% and 10.94%, respectively, for Harbor. Equity-to-assets was similar with the urban OTC group having a median of 6.53% to Harbor s 6.66%. Once again the NPAs of the comparable group were lower than Harbor s, but at .23% of assets versus .38% of assets for Harbor the difference was negligible. In comparing income and expense ratios, Harbor outperformed the OTC group in terms of net interest income but gave away its advantage with higher net operating expense. Harbor had net interest income to average assets of 4.59% for the first nine months ended September 30, 2005 versus a median of 3.96% for the urban OTC group. Net operating expense was the opposite with Harbor having a much higher net operating expense to average assets of 3.23% compared to 2.12% for the comparable group. As a result Harbor s net operating income as a percent of assets was lower than that of the comparable group s median 1.36% to 2.04%. The pricing ratios for the urban OTC group were just as diverse as the urban exchange group s. Price-to-earnings multiples ranged from 11.6 to 30.7, with a median of 17.8. Price-to-book multiples ranged from 159% to 296% of book with a median of 223%.

Urban Most Applicable Group. Since the members of the urban exchange group and the urban OTC group were selected based on their having similar assets to Harbor and being in urban markets, there were differences in their other characteristics that distort their comparability to Harbor. For example, the pricing multiples of the urban exchange group and the urban OTC group were in the range of 18 to 23 times earnings and 170% to 230% of book, but these groups contain several newly formed banks and banks with far superior performance that are valued at high multiples. As noted above, the Urban Most Applicable Group was created by eliminating less comparable banks that were new or high performance banks. The urban most applicable group s seven banks had median returns on average assets and equity of .91% and 11.30%, respectively. While this was higher than Harbor s .74% and 10.94%, respectively, both are in the range of moderate performing banks.

Minority-Owned Group. There are seventeen publicly traded minority-owned institutions as defined by the Federal Reserve Bank. These banks represent African-American, Hispanic, Asian and women minorities. Some of these banks are comparable to Harbor but others because of their size, performance, or minority orientation are not comparable and have been excluded. Danielson Associates determined that the remaining four banks that are most comparable to Harbor provide the best basis on which to value its stock.

The minority-owned institutions that were non-comparable were excluded based on size, performance, or minority orientation. The five banks with assets over $900 million were so much larger than Harbor that they were not comparable. In terms of performance there were three banks whose performance was too far above Harbor s to be comparable and five banks whose performance was too far below Harbor s to be comparable. The three top performers all had returns on equity near 14% or more and the five poorly performing banks all had returns on equity below 4%. In addition two of these poor performers with assets under $100 million and were too small to be comparable, and a third had high NPAs which might add another reason that it would be not comparable. One of the top performers Abigail Adams has performance that could be considered comparable but it was also eliminated based on being a women s owned bank, rather than an African-American owned bank, and it does not market itself as a minority-owned institution.

The remaining four minority-owned institutions (the minority-owned group) were all African-American owned, three of which were banks and the other a thrift. The largest in the group was the New York City based thrift Carver Bancorp, Inc. (Carver) with assets of $648 million and the smallest was the Miami, Florida based PanAmerican Bancorp (PanAmerican) with assets of $244 million The other two banks were the Atlanta, Georgia based Citizens Bancshares Corporation (Citizens) and the Washington, D.C. based IBW Financial Corporation (IBW). Harbor with assets of $247 million was nearly identical in assets to PanAmerican.

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Equity as a percent of assets was similar for three of the banks, but the fourth was substantially higher. The three with similar capital-to-asset ratios Carver, Citizens, and IBW all had ratios between 7.33% and 8.29%. Harbor had capital-to-assets of 6.66%. The fourth bank PanAmerican had capital-to-assets of 17.59% but it just raised about $15 million in new equity in the third quarter of 2005.

In terms of performance the four banks in the minority-owned group had performance comparable but below that of Harbor. Returns on average equity ranged from 5.93% to 8.66% with a median of 7.24%. Harbor s return on average equity was 10.94% but it was aided by its low capital ratio. Returns on average assets were closer with the four banks posting returns of .45%, .48%, .69%, and .99%. Harbor had a return on average assets of .74%, above all but one of the minority owned group. In terms on NPAs none of the four banks in the minority-owned group has significant NPAs. The bank with the lowest NPAs-to-assets was PanAmerican at .02% and the highest was Citizens with 1.23%. Harbor had NPAs-to-assets of .38%.

Harbor s net interest income and net operating expense as a percent of average assets was similar to that of three of the four banks in the minority-owned group. Harbor s net interest income to average assets of 4.59% was inside the range of 4.48% to 4.65% posted by Citizens, IBW, and PanAmerican. In terms on net operating expense to average assets Harbor s 3.23% was again inside the range of the same three banks 3.16% to 3.87%. The fourth bank Carver posted net interest income and net operating income as a percent of average assets of 3.05% and 2.29%, respectively.

The pricing of three of the four banks in the minority-owned group were similar. Citizens, Carver and IBW all had price times earnings multiples in a fairly tight range with multiples of 9.8, 14.0 and 14.0 times earnings, respectively. These same banks had price-to-book ratios of 82%, 80%, and 90%, respectively. The fourth bank, PanAmerican had a price times earnings multiple of 22.2 and price-to-book of 141%. The pricing of PanAmerican can be discounted as it recently raised a substantial amount of new capital after years of losses and its stock trades for less than $5.00.

Absent adjustments for illiquidity of the market for the stock discussed below, Harbor s common stock would be expected to trade within the comparative groups normal range of earnings multiples, as its financial characteristics are comparable with those of the comparative groups. However, the banking organizations most similar to Harbor, the urban minority owned banks, do not trade in line with the pricing values of the other comparable groups , and as a result the fair value of Harbor will similarly not be in line with the pricing values of the other groups.

Valuation Methods. A number of methodologies can be used to establish a fair price for shares of an unlisted stock, including (a) sale prices of similar companies, (b) liquidation value, (c) discounted dividends analysis under certain earnings and growth assumptions, and (d) comparisons with stock prices of similar companies that are publicly-traded. Danielson Associates determined that a comparison with stock prices of similar publicly traded companies was the best method for the valuation of Harbor s common stock. The first three methods are primarily utilized when there is either a likely sale of the company, a possibility of failing, or adequate comparisons do not exist. These last three methods were not used for the Harbor valuation because Harbor is not considering a sale, it is not in danger of failing, and there are applicable market comparables on which to base a valuation of its stock. Thus, Harbor s value has been established on a going-concern value basis by comparisons to stock prices of urban and minority-owned banks with similar size, performance, and market characteristics after which certain discounts were applied.

Earnings Derived Valuation. The methods by which bank stocks are normally valued are (a) price times earnings, (b) price-to-book, and (c) price-to-assets. Generally, the best method of valuation when earnings are normal, or can be normalized, is price times earnings. Price-to-book is used when price times earnings cannot be used because earnings are not normal or cannot easily be normalized. Price-to-assets is used when price-to book does not provide a meaningful valuation. As Harbor s earnings had been sustained for several years through September 30, 2005, Danielson determined that the valuation should be based primarily on earnings. (But see Price Adjustment since Opinion Date on page 22, below.)

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The first two groups considered were the urban exchange group and the urban OTC group. A number of the banks in these two groups were eliminated to form a single group with more similarities to Harbor, but the pricing multiples of the larger groups than were reviewed for reference. The urban exchange group had fourteen banks and a median price times earnings multiple of 22.7. The urban OTC group had eleven banks and had a median price times earnings multiple of 17.8.

When the new banks and high performers in the urban exchange group and the OTC group were eliminated there were seven banks remaining. These seven banks comprise the urban most applicable group and had financial conditions and performance similar to Harbor s. The median price times earnings of this group were 15.5. That the price times earnings were lower than those of the larger groups is not surprising as new banks are often valued based on anticipated future performance and high performing banks may merit a higher multiple.

The final comparative group and the most relevant to Harbor is the minority-owned group. These four banks all are African-American owned and serve large urban areas like Harbor. In addition, they all have similarities in financial condition and performance. The median price times earnings for this group is 14.0.

The price times earnings multiples for the four comparables groups were 22.7X, 17.8X, 15.5X and 14.0X. The latter two multiples for the urban most applicable and the minority-owned group are the most comparable.

Stock Transactions. There were few stock transactions in the first nine months of 2005. Each of these trades was at $25 per share. At this price based on September 30, 2005 financial data, the trades were for 10.4 times fully-diluted earnings and 112% of book. Danielson Associates determined that the number of shares traded was too small on which to base a valuation and did not consider them in the valuation. (See on page 32.

Discounted Dividends Analysis. Danielson Associates applied present value calculations to Harbor s estimated dividend stream under several specific growth and earnings scenarios. The projected dividend streams and terminal values, which were based on a range of earnings multiples, were then discounted to present value using discount rates based on assumptions regarding the rates of return required by holders or prospective buyers of Harbor common stock. In performing this analysis, Danielson Associates used the following assumptions: (a) growth rate of 6%; (b) ending price/earnings ratios of 12X and 14X; (c) tax rate of 36%; (d) discount rates of 10% and 12%; and (e) dividends in amounts so that capital over 6.50% is paid out as dividends. Based on this analysis, the value of the Harbor common stock would be between $24.54 and $33.72 per share.

Other Factors. In addition to performing the analyses summarized above, Danielson Associates also considered other factors. These included the general trading levels for comparable banks, the past financial performance, their market positions and future prospects and general economic conditions.

Value Adjustments. In order to determine the fair price for shares of Harbor common stock, it was necessary to consider how it differs from the comparable banks and make the adjustments reflecting the differences. These adjustments considered such items as profitability, capital, growth momentum, market, deposit mix, asset mix and quality, management, liquidity of common stock as well as any unique circumstances. These valuation adjustments, other than the minority ownership discount which is based on the comparative pricing levels of the comparative groups, are not mathematically derived, but are based on a subjective analysis based on the experience of Danielson Associates and its review of market reactions to valuation issues over more than 20 years. In performing its analysis, Danielson believed that a discount of between 5% and 15% was appropriate to account for the illiquidity of the common stock, and an additional discount of 15% was appropriate to account for the other interrelated factors of market, growth, and minority ownership.

When all of the elements of possible adjustments to the value of Harbor are considered, it merits discounts based on market, stock liquidity, and minority ownership.

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Market. Harbor has continued to look for branches in growing areas within its market, but the majority of its branches and deposits are in Baltimore City, a declining market. This is particularly important in a valuation since part of the value of a banking organization is its growth opportunities and the likelihood that it will be acquired. Harbor s market limits both its potential growth and is likely to deter most potential acquirers. Thus, market is a reason for a downward value adjustment in comparison to the urban most applicable group, which generally served better markets, but not the minority-owned group, which served similar large urban markets.

Stock Liquidity. Harbor differs from most of the comparable banking organizations in the illiquidity of its stock. The comparable banks, generally, do not trade extensively, but they are listed on either a national exchange or trade over-the-counter. Harbor is not listed on any exchange, and its stock trades very sporadically.

Minority Ownership. A significant characteristic of Harbor is its minority ownership, particularly its African-American ownership. This characteristic is reflected in the minority-owned group, but not in the urban most applicable group. This minority-ownership adversely affects the value of the stock by decreasing the likelihood Harbor will be sold, and thus its potential sale value. Investors do not consider minority banks likely to sell, and, thus, no acquisition premium is normally included in the value. The reason for this perception is that minority banks seldom are sold willingly because there is a stronger community commitment than for most non-minority urban banks and non-minority banks, which represent the bulk of possible buyers, have minimal interest in acquiring minority banks because of the poor economic dynamics of the urban markets they normally serve and the potential run-off of customers after a merger. In the view of Danielson Associates, a non-minority bank may buy a minority bank, but it is unlikely to pay a full premium for it.

Conclusion. In the opinion of Danielson Associates, the best guide as to the value of Harbor s stock is the price times earnings multiples of other African-American banks having similar size and performance, and being located in similar urban markets, and that the value determined by the urban most applicable group which is slightly lower should also be considered, but only to determine that the value is to the lower half of the range determined by the minority-owned group.

Since no comparable banking organizations used in the various analyses are totally identical to Harbor, the results do not represent mathematical certainty. Instead the comparisons rely on the likelihood that the median stock prices of comparable banks are applicable to the stock value of Harbor.

Based on these comparisons, an analysis of Harbor s past performance and future potential and by applying discounts for market, stock liquidity and its minority ownership, Danielson Associates arrived at its opinion that the fair value of its common stock as of December 8, 2005 is between $28.13 and $29.63 per share with the midpoint being $28.88 per share. In Danielson Associates opinion, any price in this range would be a fair price for purposes of the merger.

The summary set forth above is not a complete description of the analyses and procedures performed by Danielson Associates in the course of arriving at its opinion. The full text of the report of Danielson Associates dated December 8, 2005, which sets forth the assumptions made and matters considered, is available for inspection and copying at Harbor s principal executive offices during regular business hours by any interested shareholder, or the representative of any shareholder designated in writing. Danielson Associates opinion is directed only to the fairness of the value of Harbor common stock and does not constitute a recommendation to any Harbor shareholder as to how such shareholder should vote.

Compensation of Danielson Associates. Pursuant to an agreement, Danielson Associates was paid a fee of $8,000, plus reasonable out-of-pocket expense not to exceed $250.

Price Adjustment since Opinion Date

At its meeting of December 14, 2005, the Board originally established a price of $29.00 per share for shares to be purchased in the merger in consideration of the opinion of Danielson Associates and other factors. At its meeting of April 19, 2006, the Board reviewed the price to be paid to shareholders whose shares will be purchased in the merger based upon factors it previously had considered and upon the performance of Harbor since the opinion of Danielson Associates was rendered and the original price was determined. The Board believes that the time and cost of obtaining an update of the Danielson Associates fairness opinion was not necessary. The Board of Directors believes the Danielson Report s analysis and conclusions are correct as of their date, and plans to continue to rely upon them, subject to the adjustment in price based upon performance since that date. The Board of Directors does not expect that any additional price adjustments will be necessary.

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In its review the Board considered the significant growth in net income and the resulting effect on book value since September 30, 2006. As a result of that review, the Board unanimously increased the price to be paid per share in the merger to $31.00 per share from the original $29.00 per share. This increase was consistent with the analytical method described above under Earnings Derived Valuation using book value, which the Board considered to be more representative of value than earnings for the twelve months ending March 31, 2006. Net income for that twelve month period increased by 45% over the twelve month period ending March 31, 2005, primarily due to two quarters that occurred after the fairness opinion date the fourth quarter of 2005 (up 165% over the same period of 2004) and the first quarter of 2006 (up 52% over the same period in 2005), and was up 33% over the twelve month period ending September 30, 2005, which was used for the Danielson Associates fairness opinion. The adjusted $31.00 per share cash out price is 125% of per share book value at March 31, 2006. The original $29.00 valuation was 121% of book value per share at September 30, 2006. The total increase in consideration to be paid to shareholders who are cashed out in the merger by reason of this change is expected to be approximately $25,000, an increase of approximately 7%, or fifteen one-hundredths of one percent of total stockholders equity at March 31, 2006, and will have no discernable effect on Harbor s operations or condition.

Effects of the Merger

The merger will have various effects on Harbor, as described below.

Reduction in the Number of Shareholders. We believe that the merger will reduce the number of record shareholders from approximately 626 to approximately 266, and the number of outstanding shares of voting common stock from 641,784 as of the record date, to approximately 629,306 after the merger. The merger will have no effect on the number of shares nonvoting common stock (33,795).

Decrease in Book Value. Assuming: the price to be paid to holders of 100 or fewer shares of common stock will be $31.00 per share, (ii) the maximum number of shares of common stock expected to be cashed-out as a result of the merger is 12,478, (iii) the total cost to Harbor (including expenses) of effecting the merger is expected to be approximately $442,000, and (iv) at March 31, 2006, aggregate shareholders equity in Harbor was approximately $16.8 million, or $24.82 per share. Based upon these facts and assumptions, Harbor expects that, as a result of the merger:

Aggregate shareholders equity of Harbor as of March 31, 2006, will be reduced from approximately $16.8 million on a historical basis to approximately $16.3 million on a pro forma basis; and

The book value per share of common stock as of March 31, 2006, will be reduced from $24.82 per share on a historical basis to $24.62 per share on a pro forma basis.

Decrease in Capital. The merger will reduce Harbor s capital. However, Harbor expects that its regulatory capital ratios will continue to exceed the levels required for well capitalized banking organizations. Harbor s tier 1 capital to risk-weighted assets ratio will decrease from 8.65% on a historical basis to approximately 8.43% on a pro forma basis. Harbor s tier 1 to average assets ratio will decrease from 7.20% on a historical basis to approximately 7.12% on a pro forma basis, and its total risk-based capital ratio will decrease from 11.17% on a historical basis to approximately 10.98% on a pro forma basis. All regulatory capital ratios have been calculated assuming that 12,478 shares are cashed-out in the merger.

Suspension of Exchange Act Reporting Obligations. Once our common stock is no longer held by 300 or more shareholders of record, we will suspend filing reports required by the Exchange Act. Suspension of our reporting obligations under Section 13 of the Exchange Act and the Sarbanes-Oxley Act will substantially reduce the information we are required to furnish to our shareholders and to the SEC. It would also make certain provisions of the Exchange Act, such as proxy statement disclosure in connection with shareholder meetings and the related requirement of an annual report to shareholders, no longer applicable to Harbor. Accordingly, we estimate it will eliminate costs and expenses associated with continuance of the Exchange Act registration, estimated at approximately $87,600 per year. In addition, Harbor will avoid the costs of initial compliance with the internal control systems requirements of the Sarbanes Oxley Act of 2002, currently expected to be required for public companies of Harbor s size by year-end 2007, which are estimated to range from $150,000 to $200,000, and continued annual compliance costs related to those requirements in amounts not determined. We intend to apply for such suspension of registration as soon as practicable following completion of the merger.

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Effect on Market for Shares. Harbor common stock is not currently traded on any exchange. Following the merger, Harbor s common stock will not be listed or quoted on any exchange following the merger, and the number of trading markets where the shares could be traded by market makers will be limited.. Because we will no longer be required to file reports under the Exchange Act, the market for shares of Harbor common stock may be adversely affected. Currently, there is minimal liquidity in our shares of common stock and there may be a further reduction in the liquidity of our common stock after the merger.

Effect on Dividends. The principal source of our cash revenues comes from dividends received from the Bank. The amount of dividends that may be paid by the Bank to us depends on the Bank s earnings and capital position and is limited by federal and state law, regulations, and policies. In addition to the availability of funds from the Bank, our future dividend policy is subject to the discretion of our Board of Directors and will depend upon a number of factors, including future earnings, financial condition, cash needs, and general business conditions. If dividends should be declared in the future, the amount of such dividends cannot be estimated and it cannot be known whether such dividends would continue for future periods.

We anticipate that the merger will not have a material effect on our dividend policy, and we intend to continue paying an annual cash dividend; however, any future declaration and payment of dividends will depend upon, among other factors, our results of operations and financial condition, future prospects, regulatory limitations and capital requirements, and other factors deemed relevant by the Board of Directors.

Furthermore, in 2003 in connection with the private placement of trust preferred securities, we formed Harbor Bankshares Corporation Capital Trust (the Trust) as a subsidiary and issued $7.2 million of floating rate junior subordinated debentures to the Trust. The floating rate junior subordinated debentures pay interest quarterly, and as a result, we may be required to reduce the amount of, or stop paying, dividends on Harbor common stock in order to make such payments of interest and repayment of principal. See Financial Effects of the Merger; Financing of the Merger, below.

Financial Effects of the Merger; Financing of the Merger. We expect that the purchase of the cashed-out shares in the merger will cost no more than approximately $387,000 which does not include approximately $58,000 in professional fees and other expenses we anticipate incurring in the course of the transaction. In addition, we do not expect that the completion of the merger will have any material adverse effect on our capital adequacy, liquidity, results of operations, or cash flow. Because we currently do not know the actual number of shares that will be cashed-out in the merger, we do not know the exact amount of cash we will pay to shareholders in the merger. However, our obligation to consummate the merger under the merger agreement is conditioned on the aggregate number of shares of Harbor common stock owned by shareholders who are to be cashed-out or who have properly perfected their rights as objecting shareholders not exceeding 1.0% of the issued and outstanding shares of Harbor common stock. It is anticipated, however, that, if necessary, we will waive the condition to closing that limits the amount of shareholders being cashed out to 1% of our shares and, therefore, that all shareholders who own 100 or fewer shares will be cashed out. You should read the discussion under The Merger Agreement Conditions to the Completion of the Merger on page 33 for a description of conditions to the obligations of the parties to consummate the merger and Special Factors Fees and Expenses on page 23 for a description of the fees and expenses that we expect to incur in connection with the merger. Funds for the acquisition of shares are expected to be obtained by means of a dividend from the Bank, the funds for which would be obtained from the Bank s general working capital. As of March 31, 2006, the Bank could pay in excess of $9 million in dividends to Harbor without regulatory approval, and, accordingly, no alternative financial arrangements have been made.

Ownership Percentage of Officers and Directors. As a result of the merger, we expect that (a) the percentage ownership of all shares of outstanding common stock of Harbor held by current executive officers and Directors of Harbor and the Bank as a group (16 persons) will increase by less than 1%, from 28.6% to approximately 29.1% (excluding the effect of options); (b) the percentage ownership of all shares of outstanding voting common stock of Harbor held by current executive officers and Directors of Harbor and the Bank as a group will increase less than 1%, from 30.1% to 30.7%; (c) the percentage of beneficial ownership of voting common stock (including shares issuable upon the exercise of stock options that are or will become exercisable within 60 days of __________, 2006) held by current executive officers will increase by less than 1%, from 40.9% to 41.6%; (c) the collective book value as of March 31, 2006, of the shares of Harbor common stock held by our current officers and Directors, as a group, will decrease from approximately $4.79 million on a historical basis to approximately $4.75 million on a pro forma basis; and (d) the collective pro rata interest of our current officers and Directors, as a group, in the net income of Harbor for the quarter ended March 31, 2006, will increase from $175,000 on a historical basis (based on the number of shares beneficially owned by such officers and Directors as of the record date) to approximately $178,000 on a pro forma basis (based on the number of shares we anticipate such officers and Directors to own beneficially immediately after the merger). For a description of the assumptions used in determining the numbers of shares and related percentages that we expect to be held by executive officers and Directors immediately following the merger, please see footnotes under THE PARTIES Security Ownership of Certain Beneficial Owners and Management on page 33.

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The Board of Directors of Harbor was aware of these interests and considered them in approving the merger agreement. See SPECIAL FACTORS Background of the Merger on page 12.

No Further Reporting Obligations under the Exchange Act. After the merger and the resulting suspension of our reporting obligations under Section 13 of the Exchange Act, we no longer will file Forms 10-QSB, 10-KSB or 8-K, or any other reports with the SEC.

Effects of the Merger on Shareholders

General. The merger will affect Harbor shareholders as described below (Shareholders who elect to exercise rights as objecting shareholder should refer to APPRAISAL RIGHTS OF HARBOR SHAREHOLDERS on page 30.

Shareholders with 100 or fewer shares of Harbor common stock. If you are a shareholder who holds 100 or fewer shares of Harbor common stock before the merger:

- You will receive $31.00 in cash, without interest, for each share you own at the effective time of the merger.
- You will not have to pay any brokerage commissions or other service charges in connection with the merger.
- All amounts owed to you will be subject to applicable federal, state, and local income taxes.
- You will have no further interest in Harbor with respect to your cashed-out shares. Your only right will be to receive cash for those shares.
- You will receive a letter of transmittal from Harbor as soon as practicable after the merger with instructions on how to surrender your existing certificate(s) in exchange for your cash payment.

If you want to continue to remain a shareholder of Harbor after the merger, you may do so by purchasing a sufficient number of shares of Harbor common stock from other shareholders prior to the effective time of the merger so that you hold more than 100 shares at the effective time of the merger. As described in the section THE MERGER AGREEMENT Conversion of Shares in the Merger on page 34, there are specific provisions regarding the treatment of shares held in nominee form, or street name.

The merger will have the same effect on shareholders regardless of whether they are affiliated or unaffiliated shareholders. As used in this proxy statement, the term affiliated shareholder means any shareholder who is a Director or executive officer of Harbor, and the term unaffiliated shareholder means any holder of Harbor common stock who is not an affiliate of Harbor. The effects of the merger on a shareholder will vary depending on whether all of the shareholder s shares will be cashed-out in the merger. The determination of whether or not any particular shares of Harbor common stock will be cashed-out in the merger will be based on whether the holder of those shares holds either 100 or fewer shares or more than 100 shares. Since a shareholder may beneficially own shares held by more than one holder of shares, a shareholder may beneficially own both shares that will be cashed-out in the merger and shares that will remain outstanding in the merger.

Cashed-Out Shareholders. Shareholders owning 100 or fewer shares immediately prior to the effective time of the merger will, upon consummation of the merger:

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- Receive $31.00 in cash, without interest, per share;
- No longer have any equity interest in Harbor and therefore will not participate in its future potential earnings or growth, if any, as a shareholder; and
- Be required to pay federal and, if applicable, state and local income taxes on the cash amount received in the merger. See SPECIAL FACTORS Material U.S. Federal Income Tax Consequences on page 28.

Remaining Shareholders. The effects of the merger on shareholders owning more than 100 shares immediately prior to the effective time of the merger will upon consummation of the merger include:

- Continued Ownership of Shares. Shareholders who own more than 100 shares immediately prior to the effective time of the merger will continue to be shareholders of Harbor and will own the same number of shares after the merger as they owned immediately before the merger.
- Ownership Percentage. Remaining shareholders will have an increased ownership percentage in Harbor as a result of the merger. However, fewer than 2% of the Harbor s outstanding shares of voting common stock will be exchanged for cash in the merger. Accordingly, the percentage changes in the ownership of the remaining affiliated and unaffiliated shareholders will be immaterial. The aggregate beneficial ownership of affiliated shareholders will not increase by a material amount and, after the merger, unaffiliated shareholders will continue to own more shares that affiliates. The aggregate beneficial ownership of voting common stock by affiliated shareholders, including the effect of unexercised stock options, will increase by less than 1%, from 40.91% to 41.59%, as result of the merger, while the aggregate beneficial of voting common stock owned by unaffiliated shareholders will decrease by less than 1%, from 59.09 % to 58.41%, calculated on the same basis. Accordingly, there will be no material change in the ownership of Harbor s shareholders who are not cashed out in the merger.
- Decreased Access to Information. If the merger is effected, we intend to suspend our reporting obligations to the SEC under the Exchange Act. As a result, we will no longer be subject to the periodic reporting requirements and the proxy rules of the Exchange Act.
- Decreased Liquidity. The liquidity of the shares of our common stock held by remaining shareholders may be further reduced by the merger due to the suspension of our filing requirements under the Exchange Act.
- Reduced Capital. Harbor s regulatory capital ratios will be reduced. Harbor s tier 1 capital to risk-weighted assets ratio will decrease from 8.65% on a historical basis to approximately 8.43% on a pro forma basis. Harbor s tier 1 to average assets ratio will decrease from 7.20% on a historical basis to approximately 7.12% on a pro forma basis, and its total risk-based capital ratio will decrease from 11.17% on a historical basis to approximately 10.98% on a pro forma basis. All regulatory capital ratios have been calculated assuming that 12,478 shares are cashed-out in the merger. It is anticipated that Harbor and the Bank will continue to meet the tests for well capitalized status for regulatory capital purposes.
- Reduced Book Value Per Share. The book value per share of Harbor common stock as of March 31, 2006, will be reduced from $24.82 per share on a historical basis to approximately $24.62 per share on a pro forma basis.

Interests of Executive Officers and Directors in the Merger

The Board of Directors believes that it has acted in the best interests of Harbor and its shareholders. However, as you consider the recommendation of the Board of Directors, you should be aware that the Directors and officers of Harbor have interests in addition to their interests as shareholders of Harbor that may conflict with the interests of shareholders who will be cashed out in the merger or unaffiliated shareholders who will not be cashed out in the merger.

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As a result of the merger, we expect that (a) the percentage ownership of all shares of outstanding common stock of Harbor held by current executive officers and Directors of Harbor and the Bank as a group (16 persons) will increase by less than 1%, from 28.6% to approximately 29.1% (excluding the effect of options); (b) the percentage ownership of all shares of outstanding voting common stock of Harbor held by current executive officers and Directors of Harbor and the Bank as a group will increase less than 1%, from 30.1% to 30.7%; (c) the percentage of beneficial ownership of voting common stock (including shares issuable upon the exercise of stock options that are or will become exercisable within 60 days of __________, 2006) held by current executive officers will increase by less than 1%, from 40.9% to 41.6%; (c) the collective book value as of March 31, 2006, of the shares of Harbor common stock held by our current officers and Directors, as a group, will decrease from approximately $4.79 million on a historical basis to approximately $4.75 million on a pro forma basis; and (d) the collective pro rata interest of our current officers and Directors, as a group, in the net income of Harbor for the quarter ended March 31, 2006, will increase from $175,000 on a historical basis (based on the number of shares beneficially owned by such officers and Directors as of the record date) to approximately $178,000 on a pro forma basis (based on the number of shares we anticipate such officers and Directors to own beneficially immediately after the merger). For a description of the assumptions used in determining the numbers of shares and related percentages that we expect to be held by executive officers and Directors immediately following the merger, please see footnotes under THE PARTIES Security Ownership of Certain Beneficial Owners and Management on page 33.

The Board of Directors of Harbor was aware of these interests and considered them in approving the merger agreement. See Special Factors Background of the Merger on page 12.

Conduct of Harbor s Business after the Merger

Harbor will complete the deregistration process by filing a Form 15 with the SEC promptly following the merger. Harbor s filing obligations under the Exchange Act will be immediately suspended upon the filing of the Form 15. These filing obligations would resume if the Form 15 were withdrawn by Harbor or denied by the Securities and Exchange Commission, if Harbor registers shares under the Securities Act of 1933, or if the number of Harbor s record holders subsequently exceeds 500. Harbor has no plans to withdraw the Form 15, to register securities under the Securities Act, or to increase its number of record holders to more than 500.

Following the merger and deregistration, Harbor and its subsidiaries, including the Bank, will continue to conduct their existing operations in the same manner as now conducted. The executive officers and Directors immediately prior to the merger will be the executive officers and Directors of Harbor after the merger. The articles of incorporation and bylaws of Harbor will remain in effect and unchanged by the merger. The deposits of the Bank will continue to be insured by the Federal Deposit Insurance Corporation and Harbor and the Bank will continue to be regulated by the federal and state bank regulatory agencies as before the merger.

Harbor believes that there are significant advantages in becoming a private company, including the substantial savings in costs and management time described above, and Harbor plans to avail itself of any other opportunities it may have as a private company, including, but not limited to, making any public or private offering of its shares, expansion by creation of new offices or by acquisition, or entering into any other arrangement or transaction as it may deem appropriate. Although management does not now have an intent to enter into any such transaction nor is management currently in negotiations with respect to any such transaction, there exists the possibility that Harbor may enter into such an arrangement or transaction in the future, and the remaining shareholders of Harbor may receive payment for their shares in any such transaction at amounts lower than, equal to, or in excess of the amount paid to cashed-out shareholders in the merger. Any future decision to publicly offer shares or take any other action that would result in Harbor s again being subject to the reporting obligations of the Exchange Act would be made only after consideration of the related disadvantages and costs of re-registration versus the advantages of such action. The Board of Directors does not anticipate that Harbor will take any such action in the foreseeable future, and intends that Harbor will remain deregistered after the filing of the Form 15.

Other than as described in this proxy statement, neither Harbor nor its management has any current plans or proposals to effect any extraordinary corporate transaction, such as a merger, reorganization, or liquidation; to sell or transfer any material amount of its assets; to change its Board of Directors or management; to change materially its indebtedness or capitalization; or otherwise to effect any material change in its corporate structure or business.

Fees and Expenses

Harbor estimates that merger related fees and expenses, consisting primarily of financial advisory fees, SEC filing fees, fees and expenses of attorneys and accountants and other related charges, will total approximately $55,350, assuming the merger is completed. This amount consists of the following estimated fees:

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Description	Amount
Advisory fees and expenses	$8,250
Legal fees and expenses	32,000
Accounting fees and expenses	7,500
SEC filing fee	75
Printing, solicitation and mailing costs	7,500
Total	$55,325

Accounting Treatment

Harbor anticipates that it will account for the purchase of outstanding Harbor common stock in the merger from shareholders as a purchase and retirement of stock.

Material U.S. Federal Income Tax Consequences

The following discussion summarizes the material U.S. federal income tax consequences to the shareholders of Harbor with respect to the merger. The discussion is based upon the Internal Revenue Code, its legislative history, applicable U.S. Treasury regulations, existing administrative interpretations, and court decisions currently in effect. Any of these authorities could be repealed, overruled, or modified at any time after the date of this proxy statement, and any such change could be applied retroactively. This discussion does not address any alternative minimum tax consequences or the tax consequences under state, local, or foreign laws.

The discussion that follows neither binds nor precludes the Internal Revenue Service from adopting a position contrary to that expressed in this document, and we cannot assure you that such a contrary position could not be asserted successfully by the Internal Revenue Service or adopted by a court if the positions were litigated. Harbor has not obtained a ruling from the Internal Revenue Service or a written opinion from tax counsel with respect to the United States federal income tax consequences discussed below.

This discussion assumes that you hold your shares of Harbor common stock as a capital asset within the meaning of Section 1221 of the Internal Revenue Code. This discussion is only for general information and does not address all aspects of federal income taxation that may be important to you in light of your particular circumstances or if you are subject to certain rules, such as those rules relating to shareholders who are not citizens or residents of the United States, financial institutions, tax-exempt organizations and entities (including IRAs), insurance companies, dealers in securities, shareholders, who hold options to acquire shares of our common stock, and shareholders who acquired their shares of common stock through the exercise of employee stock options or similar derivative securities or otherwise as compensation.

Federal income tax consequences to shareholders who do not receive cash in the merger. If you (a) continue to hold shares of Harbor common stock immediately after the merger, and (b) you receive no cash as a result of the merger, then you will not recognize any gain or loss in the merger and you will have the same adjusted tax basis and holding period in your shares of Harbor common stock as you had in such stock immediately prior to the merger.

Federal income tax consequences to shareholders who receive cash in the merger. An exchange of your shares of Harbor common stock for cash pursuant to the merger will be a taxable transaction. If you receive cash in exchange for your Harbor common stock as a result of the merger, the cash you received will be treated as a redemption of your shares of Harbor common stock exchanged therefor under Section 302 of the Internal Revenue Code. Under Section 302 of the Internal Revenue Code, a shareholder who exchanges his or her shares of Harbor common stock for cash will be treated as having sold his or her shares of Harbor common stock if the exchange meets one of the following three tests:

The exchange results in a complete termination of his or her equity interest in Harbor;

The exchange is substantially disproportionate with respect to the shareholder; or

The cash received is not essentially equivalent to a dividend with respect to the shareholder.

For purposes of these tests, in addition to the shares of Harbor common stock you actually own, you may be deemed to own constructively certain shares of Harbor common stock under the constructive ownership rules of Section 318 of the Internal Revenue Code. Generally, the constructive ownership rules under Section 318 of the Internal Revenue Code treat a shareholder as owning:

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(a) Shares of stock owned by certain relatives, related corporations, partnerships, estates or trusts, and
(b) Shares of stock the shareholder has an option to acquire.

Because the constructive ownership rules are complex, each shareholder should consult his or her own tax advisor as to the applicability of these rules.

Cashed-out shareholders who do not actually or constructively own any shares of Harbor common stock after the merger. In general, if you receive cash in exchange for your shares of Harbor common stock as a result of the merger but do not actually or constructively own any shares of Harbor common stock immediately after the merger, you will be treated as having sold your shares of Harbor common stock for the cash received. You will recognize gain or loss on the exchange in an amount equal to the difference between the cash you receive for your cashed-out shares of Harbor common stock and your aggregate adjusted tax basis in such stock. Your gain will be a capital gain provided you held your shares of Harbor common stock as a capital asset within the meaning of Section 1221 of the Internal Revenue Code as of the effective time change effective time of the merger.

Shareholders receiving cash who actually or constructively continue to own any shares of Harbor common stock after the merger. If you receive cash in exchange for your shares of Harbor common stock as a result of the merger and are treated as directly or constructively owning shares of Harbor common stock immediately after the merger, then you will be treated as having sold your shares of Harbor common stock for the cash received only if you meet one of the three tests mentioned above and described below.

You will satisfy the complete termination test if you receive cash in exchange for your shares of Harbor common stock pursuant to the merger and you completely terminate your direct and constructive ownership interest in Harbor. If you would otherwise satisfy the complete termination requirement but for your constructive ownership of shares of Harbor common stock held by family members, you may, in certain circumstances, be entitled to disregard such constructive ownership. You should check with your own tax advisor as to whether you would be entitled to disregard such constructive ownership and the required filings with the Internal Revenue Service pursuant to such a decision.

You will satisfy the substantially disproportionate test if immediately after the merger you actually and constructively own less than 50% of the total combined voting power of all classes of Harbor stock entitled to vote and your percentage interest in Harbor (i.e., the number of voting shares actually and constructively owned by you divided by the number of voting shares outstanding) is less than 80% of your percentage interest in Harbor immediately prior to the merger.

You will satisfy the not essentially equivalent to a dividend test if the reduction in your percentage interest in Harbor, as described above, constitutes a meaningful reduction of your proportionate interest given your particular facts and circumstances. The Internal Revenue Service has indicated in published rulings that a minority shareholder whose relative stock interest is minimal (i.e., less than 1%) and who exercises no control with respect to corporate affairs is considered to have a meaningful reduction generally if the shareholder has some reduction in the shareholder s stock ownership percentage.

If you satisfy one of these three tests, you will be treated as having sold your shares of Harbor common stock for the cash exchanged therefor and will recognize gain or loss on the exchange in an amount equal to the difference between the cash you receive for your cashed-out shares of Harbor common stock and your aggregate adjusted tax basis in such stock. Your gain will be a capital gain provided you held your shares of Harbor common stock as a capital asset within the meaning of Section 1221 of the Internal Revenue Code as of the effective time of the merger.

If you do not satisfy one of these three tests, you will be treated as having received a dividend to the extent of our current and accumulated earnings and profits, which we anticipate will be sufficient to cover the amount of any such dividend and will be includible in your gross income as ordinary income in its entirety, without reduction for the adjusted tax basis of your shares of Harbor common stock exchanged for cash. No loss will be recognized. If the exchange is treated as a dividend, your adjusted tax basis in your shares of Harbor common stock exchanged for cash generally will be added to your tax basis in your remaining shares of Harbor common stock. To the extent that cash received in exchange for your shares of Harbor common stock is treated as a dividend to a corporate shareholder, the corporate shareholder will be: (i) eligible for a dividends-received deduction (subject to applicable limitations); and (ii) subject to the extraordinary dividend provisions of the Internal Revenue Code. To the extent, if any, the cash received by you exceeds our current and accumulated earnings and profits, it will be treated first as a tax-free return of your adjusted tax basis in the shares surrendered and thereafter as a capital gain.

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Capital gain and loss. For individuals, net capital gain (defined generally as your total capital gains in excess of capital losses for the year) recognized upon the sale of capital assets that have been held for more than 12 months generally are subject to tax at a rate not to exceed 15%. Net capital gain recognized from the sale of capital assets that have been held for 12 months or less will continue to be subject to tax at ordinary income tax rates. In addition, capital gain recognized by a corporate taxpayer will continue to be subject to tax at the ordinary income tax rates applicable to corporations. There are limitations on the deductibility of capital losses.

Backup withholding. If you receive cash in the merger, you will be required to provide your social security or other taxpayer identification numbers (or, in some instances, additional information) in connection with the merger to avoid backup withholding requirements that might otherwise apply. The letter of transmittal will require you to deliver such information when your shares of Harbor common stock certificates are surrendered following the effective time of the merger. Failure to provide such information may result in backup withholding.

As explained above, the amounts paid to you as a result of the merger may result in dividend income, capital gain income, or some combination of dividend and capital gain income to you depending on your individual circumstances. The U.S. federal income tax discussion set forth above is based upon current law, which is subject to change possibly with retroactive effect. You should consult your tax advisor as to the particular federal, state, local, foreign, and other tax consequences of the transaction that are applicable to you in light of your specific circumstances.

APPRAISAL RIGHTS OF HARBOR SHAREHOLDERS

Any shareholder of Harbor who does not vote in favor of the merger and the transactions contemplated by the merger agreement and who has given prior written notice to Harbor of his or her objection to the proposed transaction and who otherwise complies with the procedures set forth in Title 3, Subtitle 2 of the MGCL, will be entitled to receive payment in cash of the fair value of his or her shares of Harbor common stock instead of receiving the merger consideration. A copy of Title 3, Subtitle 2 of the MGCL is included as Appendix C to this proxy statement.

If you want to demand payment of the fair value of your shares of Harbor common stock, you must fully comply with the procedures set out in the MGCL. The required procedures are summarized below. The following summary is not intended to be a compete statement of all aspects of the procedures set forth in the MGCL, and is qualified in its entirety by reference to the text of the statute included in Appendix C. If you intend to exercise your rights as an objecting shareholder, you should be aware that cash paid to you will likely result in receipt of taxable income. (See Material U.S. Federal Income Tax Consequences).

Only holders of record of shares of Harbor common stock can object to the merger and demand to receive the fair value of the shares in cash. If your shares are not registered in your name, your record holder must follow the procedures to perfect your right to object to the merger and receive cash for the fair value of your shares.

First, you must submit a written notice to Harbor at or prior to the meeting, stating that you object to the proposed merger. You should send your notice to:
Harbor Bankshares Corporation

25 West Fayette Street

Baltimore, MD 21201
Attention: Teodoro J. Hernandez

Vice President and Treasurer
You must then not vote your shares in favor of the merger. This means that you should either (a) not return a proxy card and not vote in person in favor of the adoption of the merger agreement, (b) return a proxy card with the Against or Abstain box checked; (c) vote in person against the approval of the merger agreement; or (d) register in person an abstention from the proposal to approve the merger agreement. Merely voting against the merger or abstaining from or not voting in favor of the merger will not constitute notice of objection or dissent, and will not entitle you to payment in cash of the fair value of your shares.

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Promptly after the effectiveness of the merger, Harbor will write to objecting shareholders of Harbor, notifying them of the date on which the articles of merger were accepted for record. This notice will be sent by certified mail, return receipt requested, to the address you provide in your notice, or if no address is indicated, to the address which appears on Harbor s shareholder records.

Within twenty (20) days of the date on which the articles of merger were accepted for record, an objecting shareholder must make a written demand for payment of the fair value of his or her stock, stating the number and class of shares for which payment is demanded. The written demand for payment should be sent to:

Harbor Bankshares Corporation

25 West Fayette Street

Baltimore, MD 21201

Attention: Teodoro J. Hernandez

Vice President and Treasurer

Harbor s notice of the date on which the articles of merger were accepted may contain an offer of payment of the amount which Harbor believes is the fair value of the Harbor common stock, and certain financial disclosures. If you have followed all of the procedural steps required to demand payment of fair value and have not received payment for your shares, you may, or Harbor may, within fifty (50) days of the acceptance of the articles of merger, petition the court for an appraisal of the fair value of your shares of Harbor common stock as of the date of the Harbor shareholder meeting, without including any appreciation or depreciation resulting directly or indirectly from the merger or its proposal.

Any shareholder who files a notice of objection, but fails to file a written demand for the payment of fair value in a timely manner will be bound by the shareholder vote and will not be entitled to receive payment in cash as a holder of objecting shares.

If you demand payment for your stock as an objecting shareholder, you have no right to receive any dividends or other distributions on such shares, or the cash consideration into which such shares would be converted, after close of business on the date of the Harbor shareholder meeting at which the merger is approved, and have no other rights, including voting rights, with respect to such shares, except the payment of fair value.

If you demand payment for your shares, your rights as a shareholder will be restored if the demand for payment is withdrawn, a petition of appraisal is not filed within the time required, a court determines that you are not entitled to relief, or the merger is abandoned or rescinded. A demand for payment may be withdrawn only with the consent of Harbor.

If the court finds that a shareholder is entitled to an appraisal of his or her stock, the court will appoint three disinterested appraisers to determine the fair value of the stock on the terms and conditions the court considers proper. Within sixty (60) days after appointment, or such longer period as the court may direct, the appraisers must file with the court and mail to each shareholder who is a party to the proceeding their report stating their conclusion as to the fair value of the stock. Within fifteen (15) days after the filing of the report, any party may object to the report and request a rehearing. The court, upon motion of any party, will enter an order either confirming, modifying, or rejecting the report and, if confirmed or modified, enter judgment directing the time within which payment must be made.

If the report is rejected, the court may determine the fair value or remit the proceeding to the same or other appraisers. Any judgment entered pursuant to a court proceeding will include interest from the date of the shareholders vote at the meeting, unless the court finds that the shareholder s refusal to accept a written offer to purchase the shares was arbitrary and vexatious or not in good faith.

The costs of the appraisal proceedings, including compensation and expenses of the appraisers, will be the responsibility of Harbor, except that all or any part of such expenses may be apportioned and assessed against any or all of the objecting shareholders to whom an offer to pay for such shareholder s shares has been made, if the court finds the failure to accept such offer was arbitrary, vexatious, or not in good faith. Costs of the proceedings may not include fees and expenses of counsel. Costs of the proceedings may include fees and expenses of experts only if Harbor did not make an offer of payment for your stock or if the value of the stock as determined in the appraisal proceeding materially exceeds the amount offered by Harbor.

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The preceding is a summary of the material aspects of Title 3, Subtitle 2 of the MGCL, and is qualified by reference to the text of the statute. The full text of Title 3, Subtitle 2, which we urge you to read in its entirety, is included as Appendix C to this proxy statement.

GOVERNMENTAL REQUIREMENTS

In connection with the merger, Harbor will be required to make a number of filings with and obtain a number of approvals from various federal and state governmental agencies, including:

- Filing of articles of merger with the Maryland Department of Assessments and Taxation in accordance with the MGCL after the approval of the merger agreement by Harbor s shareholders; and
- Complying with federal and state securities laws, including Harbor s and merger subsidiary s filing, prior to the date of this proxy statement, of a Rule 13e-3 Transaction Statement on Schedule 13E-3 with the SEC.

MARKET FOR COMMON STOCK AND DIVIDENDS

Harbor Bankshares Corporation is traded is traded in the Other OTC market or privately and is not listed on any exchange. During 2005 and 2004, there was little trading activity in the stock. The bid and asked price during 2005 and 2004 was $25.00 per share. Quotes are available under the symbol HRBK.PK. The most recent known trade was at $28.00 on June 14, 2006.

Dividends when and if declared, are paid annually in the first quarter. See Summary Financial Information on page 9.

THE PARTIES

Harbor Bankshares Corporation

Harbor Bankshares Corporation (the Corporation) is a bank holding company with one bank subsidiary and two other Community Development financial subsidiaries, one for profit, The Harbor Bank of Baltimore LLC and a non-profit, The Harbor Bank CDC. Both were established during 2002. The Corporation had no investment in either subsidiary as of __________, 2006. The Corporation was organized under the laws of the State of Maryland in 1992. On November 2, 1992, Harbor Bankshares Corporation acquired all outstanding stock of The Harbor Bank of Maryland (the Bank), headquartered in Baltimore, Maryland.

The Harbor Bank of Maryland

The Harbor Bank of Maryland is a Maryland chartered commercial bank headquartered in Baltimore, Maryland. The Bank was opened on September 13, 1982. The deposits of the Bank are insured by the Federal Deposit Insurance Corporation.

The Bank conducts general banking business in seven (7) locations and serves primarily the Baltimore Metropolitan area. It offers checking, savings, and time deposits, commercial, real estate, personal, home improvement, automobile and other installment loans, credit cards and term loans. The Bank is also a member of a local and national ATM network. The retail nature of the Bank allows for full diversification of deposits and borrowers so it is not dependent upon a single or a few customers.

Harbor Financial Services, a company dealing with the sale of mutual funds, stocks, insurance, etc., was established as a subsidiary of the Bank during May 1997 in order to compete with that expanding market.

Harbor Merger Corporation

Harbor Merger Corporation, or the merger subsidiary, is a recently-formed Maryland corporation. It was organized as a wholly-owned subsidiary of Harbor for the sole purpose of facilitating the merger. It has engaged in no business activities and has no assets or liabilities of any kind, other than those incident to its formation. The merger subsidiary does not own any shares of Harbor common stock, nor will it acquire any such shares before the merger. Its existence will cease upon consummation of the merger. The address and telephone number of principal offices of the merger subsidiary are the same as Harbor s.

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Security Ownership of Certain Beneficial Owners and Management

There were 675,579 shares of the Common Stock issued and outstanding on __________, 2006, of which 641,784 were shares of voting common stock. The following table shows the beneficial ownership of the voting common stock as of this date by: (1) each of Harbor s current named executive officers and Directors and (2) all of Harbor s current Directors and executive officers as a group.

Name of Beneficial Owner(1)(2)	Number of Shares Beneficially Owned(3)	Percentage of Shares Beneficially Owned	
Joseph Haskins, Jr. (4)	95,538	13.79	%
Teodoro J. Hernandez (5)	8,775	1.35	%
Darius L. Davis (6)	3,048	*	
James H. DeGraffereidt, Jr. (7)	13,928	2.14	%
Louis J. Grasmick (8)	23,227	3.56	%
Nathaniel Higgs (9)	9,545	1.48	%
Delores G. Kelley (10)	16,923	2.60	%
Erich March (11)	26,093	4.00	%
John Paterakis (12)	58,789	9.16	%
John D. Ryder	3,219	*	
James Scott, Jr. (13)	3,747	*	
Edward St. John	13,488	2.10	%
Walter S. Thomas (14)	228	*	
Stanley W. Tucker (15)	13,268	2.07	%
George F. Vaeth, Jr. (16)	20,725	3.18	%
All Directors and executive officers as a group (16 persons) (17)	307,493	40.91	%

* Less Than 1%

(1) Unless otherwise specified, the address of these persons is c/o Harbor Bankshares Corporation, 25 West Fayette Street, Baltimore, Maryland 21201.

(2) The Corporation uses the SEC s definition of beneficial ownership. This means that the person named in this table have sole or shared voting and/or investment power over the shares shown. Beneficial ownership also includes shares underlying options currently exercisable or exercisable within 60 days.

(3) Unless otherwise specified, the number of shares shown represents shares of Common Stock.

(4) Represents 44,600 shares of Common Stock and 50,938 shares of Common Stock issuable upon the exercise of options.

(5) Represents 8,775 shares of Common Stock issuable upon the exercise of options.

(6) Represents 3,048 shares of Common Stock issuable upon the exercise of options.

(7) Represents 4,325 hares of Common Stock and 9,603 shares of Common Stock issuable upon the exercise of options.

(8) Represents 13,227 shares of Common Stock (including 3,848 shares jointly owned with Mr. Grasmick and his son and 8,780 shares jointly owned by Mr. Grasmick and his wife) and 10,000 shares of Common Stock issuable upon the exercise of options.

(9) Represents 4,545 shares of Common Stock (including 4,175 shares jointly owned by Reverend Higgs and his wife) and 5,000 shares of Common Stock issuable upon the exercise of options.

(10) Represents 6,923 shares of Common Stock (including 619 shares jointly owned by Dr. Kelley and her husband) and 10,000 shares of Common Stock issuable upon the exercise options.

(11) Represents 16,093 shares of Common Stock (including 15,435 shares owned by a corporation over which Mr. March has the power to vote) and 10,000 shares of Common Stock issuable upon the exercise of options.

(12) Includes 32,874 shares of Common Stock owned by three corporations controlled by Mr. Paterakis (J and B Associates, Inc. 16,437 shares; H & S Bakery, Inc. 6,164 shares; Northeast Food, Inc. 10,273 shares) and 11,300 shares of Common Stock owned by Paterakis Limited Partnership, LLP.

(13) Includes 3,430 shares of Common Stock jointly owned by Mr. Scott and his wife.

(14) The number of shares of Common Stock owned does not include 3,757 shares owned by a religious organization over which Pastor Thomas has the power to vote.

(15) Includes 13,234 shares of Common Stock owned by MMG ventures L.P. over which Mr. Tucker has authority to vote.

(16) Represents 10,725 shares of Common Stock and 10,000 shares of Common Stock issuable upon the exercise of options.

(17) Represents 193,177 shares of Common Stock and 117,364 shares of Common Stock issuable upon the exercise of options.

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Recent Transactions

On February 13, 2006, Harbor repurchased 10,000 shares of common stock beneficially owned by Director Stanley W. Tucker at a price of $25.00 per share. Neither Harbor nor any Filing Person or Affiliate engaged in any other purchase, sale, or other transaction in the common stock during the sixty days preceding the date of this proxy statement.

Prior Stock Purchases

During the years 2005 and though __________, 2006, Harbor has repurchased a total of 42,000 shares beneficially owned by Director Stanley W. Tucker, including the 10,000 shares noted above in Recent Transactions, all at a per share price of $25.00.

Since December 31, 2002, no Filing Persons have purchased any other shares other than upon exercise of stock options under the Harbor stock option plans. Directors and officers have agreed not to purchase any additional shares of voting common stock prior to approval of the merger.

THE MERGER AGREEMENT

Following is a summary of the material terms of the merger agreement, a copy of which is attached as Appendix A to this proxy statement. Because this is a summary, it does not include all of the information that may be important to you. You should read the entire merger agreement and this proxy statement and related appendices before deciding how to vote at the Annual Meeting.

Structure of the Merger

The merger subsidiary will be merged with and into Harbor, which will be the surviving corporation. The merger will occur following the approval of the merger agreement by the shareholders of Harbor and the satisfaction of other conditions to the merger.

Conversion of Shares in the Merger

The merger agreement provides that, at the effective time of the merger:

- Subject to the following, all outstanding shares of Harbor common stock held of record by a holder holding 100 or fewer shares of Harbor common stock immediately prior to the effective time will, without any action on the part of the holder thereof, be converted into the right to receive to $31.00 per share, without interest (the merger consideration). Harbor may presume that all street shares are held by holders holding 100 or fewer shares immediately prior to the effective time unless a beneficial owner of street shares is able to demonstrate to Harbor s satisfaction that such shares are held beneficially by a holder holding more than 100 shares immediately prior to the merger date. In that case, such shares will remain outstanding with all rights, privileges, and powers existing immediately before the merger;
- All outstanding shares of Harbor common stock other than those described above as being converted into the right to receive the merger consideration or shares for which rights objecting shareholders are perfected will remain outstanding with all rights, privileges, and powers existing immediately before the merger; and
- The outstanding shares of merger subsidiary will, without any action on the part of the holder thereof, be canceled.

The merger agreement further provides that:

- No holder holding, of record or beneficially, immediately prior to the merger more than 100 shares (including any combination of record shares or street shares) in the aggregate will be entitled to receive any merger consideration with respect to the shares so held other than by exercising his or her dissenter s rights; and
- It is a condition precedent to the right of any holder to receive the merger consideration, if any, payable with respect to the shares held by such holder that such holder certify to Harbor in the letter of transmittal delivered by Harbor as described below that such holder held, of record and beneficially, immediately prior to the merger 100 or fewer shares (including any combination of record shares and street shares) in the aggregate.

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In general, calculations of shares held of record shall be made in accordance with Securities and Exchange Commission Rule 12g5-1, and accordingly:

- The number of shares held of record will be calculated by adding all shares registered in the same manner;
- Shares held in street name beneficially owned by a shareholder will not be aggregated with shares registered in such shareholder s own name, and
- Shares owned by related persons or in different capacities will not be aggregated.

Harbor may in its sole discretion, but shall not have any obligation to (a) presume that any shares of Common Stock held in a discrete account (whether record or beneficial) are held by a person distinct from any other person, notwithstanding that the registered or beneficial holder of a separate discrete account has the same or a similar name as the holder of a separate discrete account; and (b) aggregate the shares of Common Stock held (whether of record or beneficially) by any person or persons that Harbor determines to constitute a single shareholder for purposes of determining the number of shares of Common Stock held by such shareholder.

Harbor will presume that all shares held in street name are held by shareholders holding more than 100 shares of Common Stock immediately prior to the Effective Time unless Harbor determines, or a beneficial owner of shares held in street name is able to demonstrate to Harbor s satisfaction, that such shares are held beneficially by a shareholder holding 100 or fewer shares of Common Stock immediately prior to the Effective Time, in which case such shares will be deemed to be Cash-Out shares.

Harbor (and any other person or entity to which it may delegate or assign any responsibility or task with respect thereto) shall make all decisions regarding the application of this section in good faith and in accordance with the principles of Securities and Exchange Commission Rule 12g5-1 and the rules and presumptions stated above. Harbor shall have full discretion and exclusive authority to (i) make such inquiries, whether of any shareholder(s) or otherwise, as it may deem appropriate and (ii) resolve and determine all ambiguities, questions of fact, and interpretive and other matters relating to this Section. All such determinations by Harbor shall be final.

Treatment of Options

The merger agreement provides that at the effective time each option to acquire shares of Harbor common stock which is outstanding and unexercised immediately prior thereto pursuant to the Harbor Stock Option Plan, shall remain outstanding.

Exchange of Certificates

The merger agreement provides that promptly after the merger, Harbor will mail a letter of transmittal to each shareholder, who based on information available to Harbor, appears to have their shares converted into the right to receive the merger consideration (other than shares as to which objecting shareholder rights have been perfected). The letter of transmittal will contain a certification as to the number of shares held and such other matters as Harbor may determine and will specify that delivery will be effected, and risk of loss and title to the certificates representing shares of Harbor common stock (Certificates) will pass, only upon delivery of the Certificates to Harbor and instructions to effect the surrender of the Certificates in exchange for the merger consideration, if any, payable with respect to such Certificates.

Upon surrender of a Certificate for cancellation to Harbor, together with a letter of transmittal, duly completed and executed and containing the certification that the holder of the Certificate holds 100 or fewer shares, and such other customary documents as may be required pursuant to such instructions, the holder of such Certificate will, subject to the above provisions of the merger agreement, be entitled to receive the merger consideration. In the event of a transfer of ownership of shares which is not registered in the share transfer records of Harbor, the merger consideration, if any, payable in respect of such shares may be paid or issued to the transferee if the Certificate representing such shares is presented to Harbor, accompanied by all documents required to evidence and effect such transfer and by evidence that any applicable stock transfer taxes have been paid.

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You should not send your stock certificates now. You should send them only after you receive a letter of transmittal from Harbor. Letters of transmittal and related instructions will be mailed soon after the merger is completed.

Effective Time of the Merger

If the merger agreement is approved by the Harbor shareholders, the merger will close as soon as practicable after the Annual Meeting, provided that all other conditions to the merger have been satisfied or waived. After all of the conditions to the merger have been satisfied or waived, articles of merger will be filed with the Maryland Department of Assessment and Taxation. The merger will become effective on the date and at the time specified on the certificate of merger.

Directors and Officers

The merger agreement provides that the Directors and executive officers of Harbor immediately prior to the merger will be the Directors and executive officers of Harbor, as the surviving corporation, immediately after the merger.

Articles of Incorporation and Bylaws

The merger agreement provides that the articles of incorporation and bylaws of Harbor in effect immediately prior to the merger will be the articles of incorporation and bylaws of Harbor, as the surviving corporation, immediately after the merger.

Representations and Warranties

The merger agreement contains customary representations and warranties made by Harbor and merger subsidiary regarding various matters, including representations by them as to the enforceability of the merger agreement.

Conditions to the Completion of the Merger

The obligations of Harbor and merger subsidiary to complete the merger are subject to the satisfaction or waiver of all of the following conditions:

- Approval of the merger agreement by the holders of at least two-thirds (2/3) of the outstanding shares of Harbor common stock which cannot be waived;
- All requisite regulatory approvals relating to the Merger, if any, shall have been obtained and continue to be in full force and effect, and all waiting and notice periods under applicable law shall have expired.
- The aggregate number of shares of Common Stock owned by those shareholders of Harbor who will receive merger consideration or have perfected and are entitled to exercise their objecting shareholders rights shall not exceed 1.0% of the issued and outstanding shares of Common Stock.
- No injunction, restraining order, stop order, or other order or action of any Federal or state court or agency in the United States which prohibits, restricts, or makes illegal the consummation of the transactions contemplated by the merger agreement shall be in effect, and no action, suit or other proceeding seeking such shall have been instituted or threatened, and no statue, rule, or regulation shall have been enacted, issued, or promulgated by and state or Federal government or government agency which prohibits, restricts, or makes illegal the consummation of those transactions.

As set forth above, the merger agreement includes a provision designed to protect Harbor in the event that the aggregate of the number of shares to be cashed-out in the merger plus the number of shares held by shareholders who object to the merger pursuant to the provisions of the MGCL exceeds 1% of the total number of outstanding shares of Harbor common stock. The purpose of this provision is to provide Harbor with the opportunity to terminate the merger agreement prior to consummation of the transaction in the event that the total consideration to be paid to Harbor shareholders in connection with the merger exceeds approximately $386,818. Based upon the list of beneficial shareholders on __________, 2006, it is expected that the number of shares of Harbor common stock to be cashed-out in the merger will be approximately 12,478, and Harbor is prepared to waive the condition to the merger agreement and consummate the transaction. Further, the merger agreement provides that it may be terminated at any time by either Harbor or merger subsidiary prior to consummation of the merger.

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Termination of Merger Agreement

The merger agreement may be terminated by either Harbor or merger subsidiary at any time prior to the effective time of the merger.

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PROPOSAL II ADJOURNMENT OF THE ANNUAL MEETING

If Harbor does not receive a sufficient number of votes to approve Proposal I, Harbor may propose to adjourn the Annual Meeting, if a quorum is present, from time to time for a period of not more than 120 days after the record date, with the approval of a majority of shares present in person or by proxy and entitled to vote. Harbor currently does not intend to propose an adjournment of the Annual Meeting if there are sufficient votes to approve the merger agreement.

Harbor s Board of Directors and each Filing Person and Affiliate has determined and believes that the Proposal to adjourn the Annual Meeting, if necessary to solicit additional proxies if there are not sufficient votes in favor of Proposal I is advisable and procedurally fair to, and in the bests interests of Harbor and its shareholders, including unaffiliated shareholders, and has approval and adopted the proposal. Accordingly, the Harbor Board of Directors recommends that shareholders vote **FOR** Proposal II for adjournment of the Annual Meeting.

PROPOSAL III ELECTION OF DIRECTORS

The charter and by-laws of the Company provide that the Directors shall be classified into three classes as equal in number as possible, with each Director serving a three-year term. Currently, the Board of Directors is composed of 13 members with Classes I and II each consisting of four member and Class III consisting of five members. The Board of Directors currently also has three open Board seats which will remain open until suitable candidates are located. The terms of the Class II Directors are scheduled to expire at the 2006 annual meeting or until their respective successors have been duly elected and qualified.

Directors are elected by a plurality of the votes cast by the holders of shares of Common Stock present in person or represented by proxy.

Directors to be elected at the 2006 Annual Meeting to serve until the 2008 Annual Meeting (Class II)

Nathaniel Higgs	Reverend Higgs is 75 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1981. From December 1966 to December 2002, he served as the Pastor of Southern Baptist Church and has now retired.
Delores G. Kelley	Dr. Kelley is 69 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1980. She is a retired educator and Senator in the Maryland State Senate.
Erich March	Mr. March is 54 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1981. He is Vice President of March Funeral Homes, Inc.
Stanley W. Tucker	Mr. Tucker is 58 years old and has served as a Director of the Corporation and of the Bank since 1996. He is President of Meridian management Company, Inc., which is the managing general partner of MMG Ventures, L.P., an investment management company.

Continuing Directors

The following information is provided with respect Directors who will continue to serve as Directors of the Company until the expiration of their terms at the times indicated.

Directors continuing to serve until 2007 Annual Meeting (Class III)

John Paterakis	Mr. Paterakis is 77 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1982. He is President and Chief Executive Officer of H & S Bakery, Inc. and Northeast Foods, Inc.
James Scott, Jr.	Mr. Scott is 48 years old and has served as a Director of the Corporation and the Bank since November 2000. He is a principal of Pennan & Scott P.C., an accounting firm. Mr. Scott is a certified public accountant.
Edward St. John	Mr. St. John is 68 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1990. He is President and Chief Executive Officer of M.I.E. Investment Company, a real estate development company.

Walter S. Thomas	Pastor Thomas is 55 years old and has served as a Director of the Corporation and the Bank since November 2000. He is the Pastor of New Psalmist Church.
George F. Vaeth, Jr.	Mr. Vaeth is 72 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1981. He has served as Secretary of the Company since its formation and of the Bank since 1986. He is an architect with G.V.A., an architectural and interior design firm.

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Directors continuing to serve until 2008 Annual Meeting (Class I)

James H. DeGraffereidt, Jr.	Mr. DeGraffereidt is 52 years old and has served as a Director of the Corporation and of the Bank since 1996. He is Chairman and Chief Executive Officer of WGL Holdings, Inc., distributors of natural gas.
Louis J. Grasmick	Mr. Grasmick is 76 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1982. He is Chief Executive Officer of Louis J. Grasmick Lumber Company, Inc.
Joseph Haskins, Jr.	Mr. Haskins is 58 years old and has served as a Director of the Corporation since its formation in 1992 and of the Bank since 1980. He has served as Chief Executive Officer of the Company since its formation in 1992, Chairman of the Board of the Company Bank since 1995 and Chief Executive Officer of the Bank since 1987.
John D. Ryder	Mr. Ryder is 58 years old and has served as a Director of the Corporation and the Bank since January 2000. He was President and Chief Operating Officer of Metro Food Markets, a supermarket chain, until 2000. He was President of AXS Technologies, a software company, until July 2003. Currently, he is President of Tree Top Kids, Inc.

COMPANY CORPORATE GOVERNANCE

General

The Corporation s business is managed under the direction of its Board of Directors. The Board of Directors seeks to increase shareholder value and promote the Corporation s long-term growth. The Board of Directors establishes Corporation policies and strategies and regularly monitors the effectiveness of the Corporation s management in carrying out these policies and strategies. As part of the Board of Director s commitment to these principles, the Board of Directors regularly reviews the Corporation s corporate governance policies and practices. This review includes comparing the Corporation s current policies and practices to the policies and practices suggest by various groups and authorities active in corporate governance and policies and practices of public companies in general. The Board of Directors will continue to consider the adoption of changes, as appropriate, to enhance the Corporation s corporate governance policies and practices, and to comply with any rule changes made by the SEC.

Board Organization and Operation

Members of the Board of Directors are kept informed of the Corporation business through discussions with key member of the Corporation s management team, by reviewing materials provided to the Board of Directors and by participating in meetings of the Board and its committees.

The Board of Directors has adopted standards for Director independence that are in accordance with the standards adopted by the National Association of Securities Dealers, Inc. (the NASD) and utilized by companies with securities quoted on Nasdaq. The Board of Directors is not required to adhere to the independence standards adopted by the NASD because the common Stock is not quoted or listed on NASDAQ or any other quotation system or exchange. The Board of Directors believes, however, that a Board with at least a majority of independent Directors is an important part of good corporate governance principles. Based on the Board of Directors adopted standards, the Board of Directors has determined that none of its members has a material relationship with the Corporation and that all of its members are independent Directors, except for Messrs. Haskins and Paterakis who are not independent Directors because each is an executive officer of the Corporation. As a result, a significant majority of the members of the Board of Directors is independent.

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During 2005, the Board of Directors met 12 times. Each of the nominees and the other Directors attended at least 75% of the total Board of Directors meetings and meetings of the Board committees on which he or she served, with the exception of Mr. Thomas who attended 60% of these meetings. When necessary or appropriate, the Corporation s independent Directors meet in executive sessions without the presence of the Corporation s management. This gives the independent Directors the opportunity to discuss management s performance and any other matter that one or more independent Directors would like to discuss.

Board Committees

Each Director who serves on the Board of Directors is also a Director on the Bank s Board of Directors. The Board of Directors has one standing committee: the Audit Committee (the Audit Committee). The Bank s Board of Directors has a Compensation Committee (the Compensation Committee) and an Executive Committee (the Executive Committee)

Audit Committee. The Audit Committee responsibilities include the appointment of the Corporation s independent accountants, the preapproval of all audit services and permitted non-audit services provided to the Corporation by the Corporation s independent accountants, reviews of the independence of the Corporation s independent accountants, and review of the adequacy of internal accounting and disclosure controls of the Corporation. The Audit Committee operates under a written charter adopted by the Board of Directors. In 2005, the Audit Committee met four times. The current members of the Audit Committee are: Messrs. Vaeth, Chair, Higgs, March, Scott and Tucker. Each member of the Audit Committee is an independent Director as defined by the current NASD rules. Mr. Scott has the professional experience deemed necessary o qualify as an audit committee financial expert under the SEC s rules and regulations.

Compensation Committee. The Compensation Committee structures the compensation of the Corporation s executive officers and administers the Corporation s employee benefit plans. The Compensation Committee currently does not operate under written charter. The Compensation Committee met once in 2005. The current members of the Compensation Committee are: Messrs. Grasmick, Chair, DeGraffereidt, and St. John. Each member of the Compensation Committee is an independent Director as defined by the current NASD rules.

Executive Committee. The Executive Committee generally has the authority to exercise all of the power of the Bank s Board of Director in the management and direction of the business affairs of the Bank, subject to specific directions of the Bank s Board of Directors and the limitation of Maryland law. The Executive Committee met 13 times in 2005. The current members of the Executive Committee are: Messrs. Paterakis, Chair, Haskins, DeGraffereidt, Grasmick, March, Vaeth and Dr. Kelley. A majority of the members of the Executive Committee is independent as defined by the current NASD rules.

Nomination Process

The Board of Directors does not have a nominating committee. The full Board of Directors performs the functions of a nominating committee. The Board of Directors does not believe it needs a separate nominating committee because the full Board is comprised predominantly of independent Directors and has the time and resources to perform the function of selecting Board nominees. When the Board of Directors performs nominating function, the Board of Directors acts in accordance with the Corporation s corporate charter and bylaws but does not have a separate charter related to the nomination process. Under the Corporation s charter, nominations for Director may be made by the Board of Directors or by a shareholder of record who delivers notice along with the additional information and materials required by the Corporation s charter to the Corporation Corporate Secretary not less then 30 days and no more than 60 days before the annual meeting date. For the Corporation s annual meeting in 2007, the Corporation must receive this notice on or after February 18, 2007 and on or before March 20, 2007. The Corporation s shareholders may obtain a copy of the Corporation charter by writing to the Corporation Corporate Secretary, Harbor Bankshares Corporation, 25 West Fayette Street, Baltimore, Maryland 21201.

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The Corporation s Directors have a critical role in guiding the Corporation s strategic direction and in overseeing the Corporation s management. The Board of Directors considers candidates for the Board based upon several criteria, including their broad-based business and professional skills and experiences, concern for the long-term interests of shareholders, and personal integrity and judgment. Candidates should have reputations, both personal and professional, consistent with the Corporation s image and reputation. Because diversity is important, the Board of Directors seeks to ensure that its Directors reflect the gender and ethnic diversity of the Corporation s community. The majority of Directors on the Board of Directors should be independent, not only as that term may be legally defined, but also without the appearance of any conflict in serving as a Director. In addition, Directors must have time available to devote to Board activities and to enhance their knowledge of the banking industry. Accordingly, the Board of Directors seeks to attract and retain highly qualified Directors who have sufficient time to attend to their substantial duties and responsibilities to the Corporation.

The Board of Directors utilizes the following process for identifying and evaluating nominees to the Board. In the case of incumbent Directors whose terms of office are set to expire, the Board of Directors review such Directors overall service to the company during their term, including the number of meetings attended, level of participation and quality of performance. In the case of new Director candidates, the Directors on the Board of Directors are polled for suggestions as to potential candidates that may meet the criteria above, discuss candidates suggested by the Corporation s shareholders and may also engage, if the Board of Directors deems appropriate, a professional search firm. To date, the Board of Directors has not engaged professional search firms to identify or evaluate potential nominees but may do so in the future, if necessary. The Board of Directors then meets to discuss and consider these candidates qualifications and then chooses a candidate by a majority vote.

Director Attendance at the Corporation Annual Meeting

The Corporation does not have a formal policy regarding attendance by members of the Board of Director at the Corporation s annual meetings of shareholders. The Corporation has always encouraged its Directors to attend its annual meetings of shareholders and expects to continue this policy. In 2005, 13 Corporation Directors attended the Corporation s annual meeting of shareholders.

Shareholder Communication with the Board

The Corporation does not have a formal process for shareholder communications with the Board of Directors. The Corporation has made an effort to ensure that the Board of Directors or individual Directors, as applicable, hear the views of Corporation s shareholders. The Corporation believes that it has been responsive regarding conveying shareholder communications to the Board of Directors.

Shareholder Proposals

Under the proxy rules established by the SEC and currently applicable to Harbor, shareholder proposals intended to be presented at the 2007 Annual Meeting of Shareholders may be eligible for inclusion in Bancorp s proxy materials for that Annual Meeting if received by Bancorp at its executive offices not later than __________________, 200_ unless the date of the 2007 annual meeting is more than 30 days from_________________, 2007, in which case the deadline is a reasonable time before Bancorp begins to print and mail proxy materials.

In addition, Bancorp s Bylaws require that to be properly brought before an annual meeting, shareholder proposals for new business must be delivered to or mailed and received by Bancorp not less than thirty nor more than sixty days prior to the date of the meeting; provided, however, that if less than thirty-one days notice of the date of the meeting is given to shareholders, such notice by a shareholder must be received not later than the tenth day following the date on which notice of the date of the meeting was mailed to shareholders. Each such notice given by a shareholder must set forth certain information specified in the Bylaws concerning the shareholder and the business proposed to be brought before the meeting.

Section 16(a) Beneficial Ownership Reporting Compliance.

Based solely on the Corporation s review of the copies of initial statements of beneficial ownership on Form 3 and reports of changes in beneficial ownership on Form 4 that it has received in the past year, annual statements of changes in beneficial ownership on Form 5 with respect to the last fiscal year, and written representations that no such annual statement of change in beneficial ownership was required, all Directors, executive officers, and beneficial owners of more than 10% of its common stock have timely filed those reports with respect to 2005. The Corporation makes no representation regarding persons who have not identified themselves as being subject to the reporting requirements of Section 16(a) of the Securities Exchange Act of 1934, or as to the appropriateness of disclaimers of beneficial ownership.

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Code of Ethics and Business Conduct

For years the Corporation has had policies regarding conflicts of interest and securities law compliance. The Corporation has adopted a Code of Ethics and Business Conduct that reflects these longstanding policies and contains additional policy initiatives. The Corporation requires all its Directors, executive officers, and employees to adhere to the Code of Ethics and Business Conduct in addressing the legal and ethical issues encountered in conducting their work. The Code of Ethics and Business Conduct requires that the Corporation s Directors, executive officers and employees avoid conflict of interest, comply with securities laws and other legal requirements and conduct business in an honest and ethical manner. The Corporation conveys to its Directors, executive officers, and employees both their obligations and responsibilities under and the importance of the Code of Ethics and Business Conduct.

Directors, executive officers, and employees are required to report any conduct that they believe in good faith to be an actual or apparent violation of the Code of Ethics and Business Conduct. The Corporation has established procedures for receiving, retaining and treating complaints received regarding accounting, internal accounting controls or auditing matters and for the confidential and anonymous submission by employees of concerns regarding questionable accounting or auditing matters. The Corporation s shareholders may obtain a copy of the Code of Ethics and Business conduct by writing to the Corporation s Corporate Secretary, Harbor Bankshares Corporation, 25 West Fayette Street, Baltimore, Maryland 21201. A Copy of the Code of Ethics and Business Conduct has been filed with the SEC as an exhibit to the Corporation s Annual Report on Form 10-KSB for the fiscal year ended December 31, 2004.

OWNERS OF MORE THAN 5% OF HARBOR COMMON STOCK

Beneficial owners of more than 5% of the common stock are required to file certain ownership reports under the federal securities laws. The following table shows the common stock beneficially owned by persons who have filed these reports reporting beneficial ownership that exceeds 5% of Harbor s outstanding common stock at March 31, 2006.

Name	Amount and Nature of Beneficial Ownership (1)		Percentage of Shares Outstanding (2)	
Joseph Haskins, Jr.	95,538	(3)	13.79	%
John Paterakis	58,789	(4)	9.16	%
Joe Louis Gladney.	50,312	(5)	7.84	%

(1) Beneficial ownership is defined by rules of the Securities and Exchange Commission, and includes shares that the person has or shares voting or investment power. A decision to disclaim beneficial ownership or to include shares held by others is made by the shareholder, not by Southwest.

(2) Calculated by Southwest based upon shares reported as beneficially owned by the listed persons and shares of Southwest common stock outstanding at March 3, 2006.

(3) The address of Mr. Haskins is 25 West Fayette Street, Baltimore, MD 21201.

(4) The address of Mr. Paterakis is 601 S. Carolina Street, Baltimore, Maryland. Includes shares owned by J&B Associates, Inc., H&S Bakery, Inc., and Northeast Foods, Inc., companies controlled by Mr. Paterakis.

(5) The address of Mr. Gladney is 2301 Sinclair Lane, Baltimore, MD 21213 Includes shares owned by 2301 Incorporated and New Life LLC, companies controlled by Mr. Gladney.

COMPENSATION OF DIRECTORS AND EXECUTIVE OFFICERS

Summary Compensation Table

The following table shows compensation paid to certain executive officers of the Corporation for the three-year period ended December 31, 2005. No other executive officer of the Corporation received total annual compensation in excess of $100,000 during such period.

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Name and Position	Year	Annual Compensation Salary	Bonus	All Other Compensation
Joseph Haskins, Jr. (1)(2)	2005	$213,383	170,706	$ 6,191
Chairman, President and	2004	207,168	165,734	6,191
Chief Executive Officer	2003	203,105	182,795	6,191
Teodoro J. Hernandez	2005	99,548	14,955	
Vice President and Treasurer	2004	91,781	9,179	
	2003	90,000	17,000	
Darius L. Davis	2005	101,904	15,000	
Executive Vice President/Bank	2004	86,797	8,680	

(6) Bonus paid pursuant to the terms of Mr. Haskins employment agreement.

(7) All other compensation represents premiums for term life benefit paid by the Corporation.

Option Grants in Last Fiscal Year

The Corporation has adopted stock option plans, pursuant to which it has reserved 226,886 shares of its Common Stock for the issuance of options. The following table sets forth information regarding the options granted to the named executive officers during 2005.

Name Expiration Date	Number of Shares Underlying Options Granted	Percent of Total Options Granted to Employees in Fiscal Year		Exercise or Base Price Per Share	Market Price Per Share on Date of Grant
Joseph Haskins, Jr.	2,560	42.3 %	$25.00	$25.00	1/1/2016
Teodoro J. Hernandez	796	13.2	25.00	25.00	1/1/2016
Darius L. Davis	1,223	20.2	25.00	25.00	1/1/2016

Aggregated Option Exercises in Last Fiscal Year and Year End Value of Options

The following table set for the aggregated option exercises in 2005 and the option values at December 31, 2005, based upon a market value for Company Common Stock of $25.00 per share:

Name	Number of Shares Acquired On Exercise	Value Realized	Number of Unexercised Options at Fiscal Year-End(1)	Value of Unexercised In-the-Money Options at Fiscal Year-End
Joseph Haskins, Jr.	4,053	41,330	50,938	$345,989
Teodoro J. Hernandez			8,775	59,085
Darius L. Davis			3,048	5,024

(1) Currently exercisable options.

Compensation of Directors

Directors of the Corporation receive a fee of $533 for each Board meeting attended ($1,066 if the Director is a member of the Corporation s Executive Committee), but do not receive a fee for attendance at the committee meetings. Mr. Vaeth received an additional fee of 4,340 for acting as secretary at each of the Board and Board committee meetings. Total fees paid to Directors of the Corporation during 2005 were $104,605. Directors who are not employed by the Corporation or the Bank are permitted to elect whether to receive their fees in the form of cash or in the form of options to purchase Common Stock of the Corporation under the 1995 Director Stock Option Plan which has been approved by the Corporation s shareholders. The exercise prices of the options will equal the market price of the Common Stock on the date of grant. The Corporation did not grant any options to its Directors in 2005.

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Mr. Haskins Employment Agreement and Retirement Benefit

Joseph Haskins, Jr. has an employment agreement with the Corporation and the Bank for a four-year term commencing as of January 1, 2000, which term may be automatically renewed for additional three-year terms unless earlier terminated. The employment agreement provides that Mr. Haskins will serve as Chairman of the Board, President and Chief Executive Officer of the Corporation and Chairman of the Board and Chief Executive Officer of the Bank at an annual salary of $182,330, subject to annual increases approved by the Corporation and the Bank. Under the employment agreement, Mr. Haskins may also receive an annual incentive bonus based upon the attainment of goals and objectives set by the Corporation s Board of Directors. If the minimum level of such goals and objectives is not met, Mr. Haskins will not be entitled to an incentive bonus. If the Corporation s Board of Directors awards Mr. Haskins an incentive bonus, the amount of the bonus will range from 60% to 100% of Mr. Haskins s then current salary, as determined by the Board of Directors. In addition to the benefit programs, plans, and arrangements of the Corporation and the Bank generally available to their employees and the normal perquisites provided to their senior executive officers, the employment agreement provides that Mr. Haskins will receive long-term disability insurance, life insurance, and an automobile allowance. Further, the Corporation must maintain a key man life insurance policy on the life of Mr. Haskins in order to provide the funds necessary to buy his shares of Corporation Common Stock from his estate or his heirs.

If the Corporation terminates Mr. Haskins employment because he becomes disabled, the Corporation will continue to provide Mr. Haskins with long-term disability insurance and medical and group life insurance until he attains age 65. Upon termination without cause or resignation with good reason (as those terms are used in the employment agreement), Mr. Haskins would be entitled to (1) severance pay equal to three times his base salary at the time of termination, payable in three equal annual installments, the first of which is due within 30 day of termination, (2) a pro rated bonus based upon the bonus paid in the year prior to termination or resignation, and (3) immediate vesting of his outstanding options. If Mr. Haskins voluntarily resigns without good reason or if the Corporation terminates his employment for cause, the Corporation would not have any further obligations to Mr. Haskins under his employment agreement.

The Corporation must pay a change of control benefit to Mr. Haskins if either (1) within 12 months after a change of control of the Corporation, the Corporation terminates Mr. Haskins employment without cause or Mr. Haskins terminate his employment for good reason or (2) within 30 days after the expiration of six month after the change in control, Mr. Haskins terminates his employment for any reason. The change of control benefit would equal the greater of (1) 2.99 times the average of Mr. Haskins gross compensation from the Corporation over the five-year period before the termination or (2) the amount Mr. Haskins would receive if he was terminated without cause, as described in the prior paragraph. Further, in such event, Mr. Haskins would be entitled to the immediate vesting of his options.

Mr. Haskins may be entitled to receive a retirement benefit under an executive supplemental retirement plan. Mr. Haskins will receive 15 annual payments of the greater of (1) 63% of his final base salary or (2) $200,000, payable at the time of retirement, if he retires at or after age 62. Mr. Haskins will receive 15 annual payments, each payment being equal to 63% of his final base salary, payable at the time of retirement or termination (or in the case of a disability, at the age of 65), if before age 62:

- Mr. Haskins terminates his employment for good reason or, within 30 days after the expiration of six months after a change of control of the Corporation, Mr. Haskins terminates his employment with or without good reason; or
- the Corporation terminates Mr. Haskins employment without cause or because of a disability.

If Mr. Haskins terminates his employment before age 62 without good reason, Mr. Haskins will be entitled to a prorated amount of 63% of his final base salary based upon the number of years he provided services to the Corporation from the year 2000 until such time has he retires. However, if the Corporation terminates Mr. Haskins employment for cause, Mr. Haskins will forfeit his retirement benefit. In the event of Mr. Haskins death, Mr. Haskins beneficiaries would be entitled to receive the reminder of the retirement benefit should he die before receipt of the full retirement benefit.

Information Regarding Mr. Hernandez

Mr. Hernandez is 61 years old and has served as Vice President and Cashier of the Bank since 1982 and Vice President and Treasurer of the Corporation since its formation in 1992. He became a Senior Vice President of the Bank in 1998.

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Mr. Hernandez may be entitled to receive a retirement benefit under an executive supplemental retirement plan. Mr. Hernandez will receive 15 annual payments of $40,000, payable at the time of retirement, if he retires at or after age 65. Mr. Hernandez will receive 15 annual payments, in amounts ranging from $5,309 to $40,000, if Mr. Hernandez retires before age 65. In the event of a change of control of the Bank, if Mr. Hernandez s employment is terminated for any reason (other than a Bank-approved leave of absence), Mr. Hernandez will be entitled to receive the same benefit as if he retired at or after age 65. Mr. Hernandez s beneficiaries would be entitled to receive the remainder of the retirement benefit should he die before receipt of the full retirement benefit. In the event of Mr. Hernandez s death while in active services of the Bank, Mr. Hernandez s beneficiaries would be entitled to receive a lump sum payment ranging from $38,676 to $396,987, depending upon the year of his death. However, if the Board of Directors terminates Mr. Hernandez s employment for cause, Mr. Hernandez will forfeit his retirement benefit.

Certain Relationships and Related Transactions

During the past year the Bank has had loan transactions in the ordinary course of its banking business with Directors and executive officers of the Bank and with their affiliates. Loans to such persons were made in the ordinary course of business and did not and do not currently involve more than the normal risk of collectibility or present other unfavorable features. All such loans were made on substantially the same terms including interest rates and collateral requirements, as those prevailing at the time for comparable transactions with non-affiliates. The bank expects to enter into such transaction in the future. As of December 31, 2005, loans to Directors and executive officers of the Bank, and their affiliates, including loans guaranteed by such persons and unfunded commitments made in 2005, aggregated $13,466,000 or approximately 63.2% of tangible shareholders equity of the Bank.

Since May 1997, the Bank has leased approximately 2,600 square feet from Harbor East Office, LLC for one of the Bank s branch offices located in Baltimore, Maryland. A majority of the outstanding membership interests of Harbor East Office, LLC is beneficially owned by John Paterakis, who serves as a Director of the Company and the Bank and as Chairman of the Executive Committee of the Bank s Board of Directors. In 2005, the Bank s monthly lease payments for these premises were approximately $6,333. The current lease term expires in May 2007, and the Bank has two five-year options to renew. The Company believes that this lease is on terms no less favorable to the Bank than those that would be available to the Bank in an arm s length transaction with a third party.

INDEPENDENT PUBLIC ACCOUNTANTS

General

The Audit Committee has retained Stegman & Company as independent public accountants to audit the Corporation s 2006 consolidated financial statements. Stegman & Company also audited the Corporation s consolidated financial statements for 2004 and 2005. A representative of Stegman & Company is expected to be present at the Annual Meeting, with the opportunity to make a statement if he or she decides, and will respond to appropriate questions.

Audit and Non-Audit Fees

	2005	**2004**
Audit Fees	$60,500	$59,950
Audit-Related Fees	1,950	2,250
Tax Fees	10,425	10,725
All Other Fees		
Total	$72,875	$72,925

Fees that the Corporation paid to Stegman & Company in 2004 and 2005 are set forth in the above table. Audit fees are fees the Corporation paid Stegman & Company for the audit and quarterly reviews of the Corporation s consolidated financial statements, assistance with the review of documents filed with the SEC, consent procedures and accounting consultation related to transaction and the adoption of new accounting pronouncements. Audit-related fees are fees for services that are reasonably related to the performance of the audit or the review of the Corporation s consolidated financial statements and principally included consultation concerning financial accounting and reporting standards. Tax fee primarily included tax compliance services. Stegman & Company did not provide any other services to the Corporation in 2004 and 2005.

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Policy on Audit Committee Pre-Approval of Audi and Non-Audit Services

The Audit committee s policy is to pre-approve all audit and non-audit services proved by the independent public accountants. These services may include audit services, and audit-related services, tax services and other services. Pre-approval is generally provided for up to one year and any pre-approval is derailed as to the particular service or category of services and is generally subject to a specific budget. The Audit Committee has delegated pre-approval authority to its Chair when expedition of services is necessary. The Chair is required to report any decision to pre-approve such services to the full Audit Committee at its next meeting. The independent public accountants and management are required to periodically report to the full Audit Committee regarding the extent of services provided by the independent public accountants in accordance with this pre-approval, and the fees for the services performed to date.

THE ANNUAL MEETING

Purpose

This proxy statement is furnished to shareholders of Harbor in connection with the solicitation of proxies by Harbor s Board of Directors for use at the Annual Meeting.

Date, Place and Time of Annual Meeting

The Annual Meeting of Harbor s shareholders will be held at Harbor s main office at 25 West Fayette Street, Baltimore, Maryland 21201 on Wednesday __________ 2006, at 12:00 noon Eastern Time.

Shares Entitled to Vote; Quorum and Vote Required

The holders of record of the outstanding shares of Harbor voting common stock at the close of business on __________, 2006, will be entitled to notice of and to vote at the Annual Meeting and any adjournment or postponement of the Annual Meeting. At the close of business on that date, there were 641,784 shares of Harbor common stock issued and outstanding and entitled to vote at the Annual Meeting.

At the Annual Meeting Harbor shareholders will be entitled to one vote for each share of Harbor common stock owned of record on the record date. The holders of a majority of the Harbor common stock must be present, either in person or by proxy, to constitute a quorum at the meeting. Shares of Harbor common stock present in person or represented by proxy, including shares whose holders abstain or do not vote and shares held of record by a broker or nominee that are voted on any matter, will be counted for purposes of determining whether a quorum exists at the Annual Meeting.

The affirmative vote of at least two-thirds (2/3) of the issued and outstanding Harbor voting common stock is required to approve the merger agreement. Directors are elected by a plurality of the votes cast by the holders of shares of common stock present in person or represented by proxy at the Annual Meeting with a quorum present. Abstentions and broker non-votes are not considered to be votes cast. The affirmative vote of at least a majority of the Harbor common stock present at the meeting, either in person or by proxy, is required to approve an adjournment of the Annual Meeting and any other matters that may be properly presented at the meeting.

The proposal to approve the merger agreement and the proposal for adjournment are non-discretionary items, meaning that brokers and banks who hold shares in an account for customers who are the beneficial owners of such shares may not give a proxy to vote those shares on those items without specific instructions from their customers. Any abstentions and broker non-votes will have the same effect as votes against approval of the merger agreement. Accordingly, the Harbor Board of Directors encourages you to complete, date and sign the accompanying proxy card and return it promptly in the enclosed postage-paid envelope.

On the record date, the Directors and executive officers of Harbor and the Bank (16 persons) were entitled to vote, in the aggregate, 193,177 shares of Harbor common stock, or approximately 30.1% of the outstanding shares of Harbor voting common stock. These shares are expected to be voted FOR approval of the merger agreement. If these shares are voted in favor of the merger agreement, then shareholders owning an additional 234,679 shares would be required to vote in favor of the merger in order for the proposal to receive approval by two-thirds (2/3) of the outstanding shares of Harbor common stock.

A list of shareholders will be available for examination by holders of the Harbor common stock for any purpose related to the Annual Meeting at the Annual Meeting and during the 10 days prior to the Annual Meeting at our offices at 25 West Fayette Street, Baltimore, MD 21201.

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Voting Procedures and Revocation of Proxies

Proxies, in the form enclosed, which are properly executed by the shareholders and returned to Harbor and not subsequently revoked, will be voted in accordance with the instructions indicated on the proxies. Any properly executed proxy on which voting instructions are not specified will be voted FOR the proposal to approve the merger agreement, FOR the propose to adjourn the Annual Meeting, if necessary, and FOR the election of the four nominated Class II Directors. The proxy also grants authority to the persons designated in the proxy to vote in accordance with their own judgment if an unscheduled matter is properly brought before the meeting.

If you are the record holder of your shares, you may revoke any proxy given pursuant to this solicitation by the Harbor Board of Directors at any time before it is voted at the Annual Meeting by:

- Giving written notice to the Secretary of Harbor;
- Executing a proxy bearing a later date filed with the Secretary of Harbor at or before the meeting; or
- Attending and voting in person at the meeting. Attendance without voting at the Annual Meeting will not in and of itself constitute revocation of a proxy.

All written notices of revocation and other communications with respect to revocation or proxies should be sent to: Harbor Bankshares Corporation, 25 West Fayette Street, Baltimore, MD 21201 Attention: Teodoro J. Hernandez, Vice President and Treasurer. If you hold your shares in street name with a bank or broker, you must contact the bank or broker if you wish to revoke your proxy.

Attending the Annual Meeting

All of our shareholders are invited to attend the Annual Meeting. If you are a beneficial owner of Harbor common stock held by a broker, bank or other nominee (i.e., in street name), you will need proof of ownership to be admitted to the Annual Meeting. A recent brokerage statement or a letter from a bank or broker are examples of proof of ownership. If you want to vote your shares of Harbor common stock held in street name in person at the Annual Meeting, you will have to get a written proxy in your name from the broker, bank, or other nominee who holds your shares.

Annual Report

Our Annual Report to the SEC on Form 10-KSB for the fiscal year ended December 31, 2005, and our Quarterly Report on Form 10-QSB for the period ended March 31, 2006, are attached to this proxy statement as Appendixes D and E, and are incorporated herein by reference. See Where You Can Find More Information and Documents Incorporated by Reference.

Other Matters to be Considered

Our Board of Directors is not aware of any business or matter other than the proposal to approve the merger agreement. If, however, any matter properly comes before the Annual Meeting, the proxy holders will vote on these matters in their discretion.

Solicitation of Proxies and Expenses

This proxy solicitation is made by the Board of Directors of Harbor. Harbor is responsible for its expenses incurred in preparing, assembling, printing, and mailing this proxy statement. Proxies will be solicited through the mail. Additionally, Directors, officers and other employees of Harbor or its subsidiaries may solicit proxies personally, by telephone or other means of communications. None of these people will receive any special compensation for solicitation activities. Harbor will reimburse banks, brokers and other custodians, nominees and fiduciaries for their reasonable expenses in forwarding the proxy materials to beneficial owners.

OTHER MATTERS

Management of Harbor knows of no other business to be presented at the Annual Meeting, other than procedural matters relating to the conduct of the Annual Meeting, but if other matters do properly come before the Annual Meeting, unless otherwise instructed, it is intended that the persons named in the proxy card will vote shares according to their best judgment.

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WHERE YOU CAN FIND MORE INFORMATION

Harbor files reports, proxy statements and other information with the SEC under the Exchange Act. Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. You may read and copy, at the prescribed rates, this information at the SEC s Public Reference Room, 100 F Street, N.E., Washington, D.C. 20549. The SEC also maintains an Internet world wide web site that contains reports, proxy statements and other information about issuers, including Harbor, who file electronically with the SEC. The address of that site is http://www.sec.gov.

Harbor, the merger subsidiary, and the Filing Persons have filed with the SEC a Rule 13e-3 Transaction Statement on Schedule 13E-3 in respect of the merger. As permitted by the SEC, this proxy statement omits certain information contained in the Schedule 13E-3. The Schedule 13E-3, including any amendments and exhibits filed or incorporated by reference as a part thereof, is available for inspection or copying as set forth above or is available electronically at the SEC s website.

DOCUMENTS INCORPORATED BY REFERENCE

The SEC allows Harbor to incorporate by reference information into this document. This means that we can disclose important information to you be referring you to another document filed separately with the SEC. The information incorporated by reference is considered to be a part of this document, except for any information that is superseded by information that is included directly in this document or in any other subsequently filed document that also is incorporated by reference herein.

This document incorporates by reference the documents listed below that Harbor has filed previously with the SEC. They contain important information about Harbor and its financial condition:

Harbor s Annual Report on Form 10-KSB for the year ended December 31, 2005; and

Harbor s Quarterly Report on Form 10-QSB for the quarter ended March 31, 2006.

We also incorporate by reference any additional documents that we may file with the SEC under Section 13(a), 13(c), 14, or 15(d) of the Exchange Act, between the date of this document and the date of Harbor s Annual Meeting.

We will provide, without charge, to each person to whom this proxy statement is delivered, upon written or oral request of such person and by first class mail or other equally prompt means within one business day of receipt of such request, a copy of any and all information that has been incorporated by reference, without exhibits unless such exhibits are also incorporated by reference in this proxy statement. You may obtain a copy of these documents and any amendments thereto by writing to Teodoro J. Hernandez, Vice President and Treasurer at the following address: Harbor Bankshares Corporation, 25 West Fayette Street, Baltimore, MD 21201.

These documents are also included in our SEC filings, which you can access electronically at the SEC s website at http://www.sec.gov.

We have not authorized anyone to give any information or make any representation about the merger or us that differs from, or adds to, the information in this proxy statement or in our documents that are publicly filed with the SEC. If anyone does give you different or additional information, you should not rely on it.

By Order of the Board of Directors

Joseph Haskins, Jr.
Chairman, President, and Chief Executive Officer

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Appendix A

AGREEMENT AND PLAN OF MERGER

This **AGREEMENT AND PLAN OF MERGER** (this Agreement) dated as of _________, 2006 is by and between **HARBOR BANKSHARES CORPORATION** (Harbor), a Maryland corporation, and **HARBOR MERGER CORPORATION** (Merger Corp), a Maryland corporation.

W I T N E S S E T H:

WHEREAS, Merger Corp has been formed in order to effect the merger that is the subject of this Agreement.

WHEREAS, the Boards of Directors of Harbor and Merger Corp have approved this Agreement and the transactions proposed herein, pursuant to which Merger Corp will be merged with and into Harbor.

NOW THEREFORE, IN CONSIDERATION of the premises and the mutual covenants and agreements contained in this Agreement, and for other good and valuable consideration the receipt and sufficiency of which is hereby acknowledged, the parties hereto, intending legally to be bound, agree and covenant as follows:

ARTICLE I THE MERGER

1.1 **Merger.**
Upon the terms and subject to the conditions of this Agreement, and in accordance with the Maryland General Corporation Law (the MGCL), at the Effective Time, Merger Corp shall be merged with and into Harbor and the separate existence of Merger Corp shall thereupon cease, and Harbor (the Surviving Corporation), shall by virtue of the merger continue its corporate existence under the laws of the State of Maryland (the Merger) under the name Harbor Bankshares, Inc.

1.2 **Effective Time of the Merger.**
The Merger shall become effective at the date and time (the Effective Time) when subject to the terms and conditions of this Agreement, the parties file articles of merger with the Secretary of State of the State of Maryland in accordance with the MGCL, following fulfillment of the conditions set forth in Articles VI and VII hereof.

1.3 **The Surviving Corporation.**

(a) The Certificate of Incorporation of Harbor in effect at the Effective Time shall be the certificate of incorporation of the Surviving Corporation, until further amended in accordance with its terms and as provided by law.

(b) The bylaws of Harbor as in effect at the Effective Time shall be the bylaws of the Surviving Corporation, until further amended in accordance with their terms and as provided by law.

(c) The directors of Harbor immediately prior to the Effective Time shall be the directors of the Surviving Corporation and the officers of Harbor immediately prior to the Effective Time shall be the officers of the Surviving Corporation, in each case as of the Effective Time until their respective successors are duly elected and qualified.

(d) The Merger shall have the effects set forth in the MGCL.

(e) All options for Harbor common stock outstanding at the Effective Time shall remain outstanding without change.

1.4 **Merger Consideration.**
At the Effective Time, by virtue of the Merger and without any action on the part of the holders thereof,

(a) All outstanding shares of Common Stock (other than Objecting Shares) held of record by a shareholder holding 100 or fewer shares of Common Stock immediately prior to the Effective Time shall, without any action on the part of the shareholder thereof, be canceled and converted into the right to receive, upon the surrender of the certificate representing such shares, $31.00 in cash per share of Common Stock without interest thereon, (the Merger Consideration).

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(b) Each share of Common Stock held in the treasury of Harbor and each share of Common Stock owned by any direct or indirect wholly-owned subsidiary of Harbor immediately prior to the Effective Time shall be cancelled without any conversion and no payment or distribution shall be made with respect thereto;

(c) All outstanding shares of Common Stock other than those described in paragraphs (a) and (b) as being converted into the right to receive the Merger Consideration shall remain outstanding with all rights, privileges, and powers existing immediately prior to the Effective Time; and

(d) The outstanding shares of Merger Corp Stock shall, without any action on the part of the holder thereof, be canceled.

(e) Except as provided in Section 1.6 with respect to Objecting Shares, in no event shall any shareholder holding of record immediately prior to the Effective Time more than 100 shares of Common Stock in the aggregate be entitled to receive any Merger Consideration with respect to the shares of Common Stock so held.

(f) For purposes hereof, the term Cash-Out Shares shall mean any shares of Common Stock that are converted into the right to receive the Merger Consideration pursuant to this Section 1.4.

1.5 **Manner of Calculating Shares Held of Record.**

(a) Subject to Sections 1.5 (b) through (d), below, calculations of shares held of record shall be made in accordance with Securities and Exchange Commission Rule 12g5-1, and accordingly:

(i) The number of shares held of record will be calculated by adding all shares registered in the same manner;

(ii) Shares held in street name beneficially owned by a shareholder will not be aggregated with shares registered in such shareholder s own name, and

(iii) Shares owned by related persons or in different capacities will not be aggregated.

(b) For purposes of this Section 1.5, Harbor may in its sole discretion, but shall not have any obligation to do so, (i) presume that any shares of Common Stock held in a discrete account (whether record or beneficial) are held by a person distinct from any other person, notwithstanding that the registered or beneficial holder of a separate discrete account has the same or a similar name as the holder of a separate discrete account; and (ii) aggregate the shares of Common Stock held (whether of record or beneficially) by any person or persons that Harbor determines to constitute a single shareholder for purposes of determining the number of shares of Common Stock held by such shareholder.

(c) Harbor will presume that all shares held in street name are held by shareholders holding more than 100 shares of Common Stock immediately prior to the Effective Time unless Harbor determines, or a beneficial owner of shares held in street name is able to demonstrate to Harbor s satisfaction, that such shares are held beneficially by a shareholder holding 100 or fewer shares of Common Stock immediately prior to the Effective Time, in which case such shares will be deemed to be Cash-Out shares.

(d) Harbor (and any other person or entity to which it may delegate or assign any responsibility or task with respect thereto) shall make all decisions regarding the application of this section in good faith and in accordance with the principles of Securities and Exchange Commission Rule 12g5-1 and sections 1.5(b) and (c). Harbor shall have full discretion and exclusive authority (subject to its right and power to so delegate or assign such authority) to (i) make such inquiries, whether of any shareholder(s) or otherwise, as it may deem appropriate for purposes of this Section 1.5 and (ii) resolve and determine all ambiguities, questions of fact, and interpretive and other matters relating to this Section All such determinations by Harbor under this Section 1.5 shall be final..

1.6 **Objecting Shares.**

(a) Each share of Common Stock issued and outstanding immediately prior to the Effective Time, the shareholder of which has not voted in favor of the Merger and who has delivered a written demand for payment of the fair value of such shares within the time and in the manner provided in Title 3, Subtitle 2 of the MGCL, is referred to herein as a Objecting Share.

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(b) Notwithstanding anything in this Agreement to the contrary, Objecting Shares shall not be converted into or represent the right to receive the Merger Consideration pursuant to Section 1.5 hereof unless and until such shareholder shall have failed to perfect or shall have effectively withdrawn or lost his right to appraisal and payment under the MGCL. If any such shareholder shall have so failed to perfect or shall have effectively withdrawn or lost such right, such shareholder s Objecting Shares shall thereupon be deemed to have been converted into and to have become exchangeable for, at the Effective Time, the right to receive the Merger Consideration without any interest thereon.

1.7 **Exchange of Shares.**

(a) Harbor shall deposit or cause to be deposited prior to the Effective Time cash, an aggregate amount necessary to pay the Merger Consideration to Cash-Out Shareholders and to make appropriate cash payments to shareholders of Objecting Shares pursuant to Section 1.6 hereof, if any, (such amounts being hereinafter referred to as (the Exchange Fund).

(b) As soon as practicable after the Effective Time, the Exchange Agent selected by Harbor in its discretion shall mail to each shareholder of record of an outstanding certificate or certificates which represent shares of Common Stock (the Certificates), a form letter of transmittal which will specify that delivery shall be effected, and risk of loss and title to the Certificates shall pass, only upon proper delivery of the Certificates to the Exchange Agent and contain instructions for use in effecting the surrender of the Certificates for payment therefor. At and after the Closing (as defined herein) and upon surrender to the Exchange Agent of a Certificate, together with such letter of transmittal duly executed, the holder of such Certificate shall be entitled to receive in exchange therefor the amount of cash provided in Section 1.4 hereof and such Certificate shall forthwith be canceled. The Exchange Agent shall, upon surrender of Certificates representing shares of Common Stock, promptly deliver the Merger Consideration with respect to such shares of Common Stock formerly represented by such Certificate. No interest will be paid or accrued on the Merger Consideration payable upon surrender of the Certificates. If payment of cash is to be made to a person other than the person in whose name the Certificate surrendered is registered, it shall be a condition of payment that the Certificate so surrendered shall be properly endorsed or otherwise in proper form for transfer and that the person requesting such payment shall pay any transfer or other taxes required by reason of the payment to a person other than the registered holder of the Certificate surrendered or established to the satisfaction of Harbor that such tax has been paid or is not applicable. Until surrendered in accordance with the provisions of this Section 1.7, each Certificate (other than Certificates representing Objecting Shares) shall represent for all purposes the right to receive the Merger Consideration without any interest thereon.

(c) Any portion of the Exchange Fund (including the proceeds of any investments thereof) that remains unclaimed by the shareholders of Harbor for six months after the Exchange Agent mails the letter of transmittal pursuant to this Section 1.7 shall be returned to Harbor upon demand, and the holders of shares of Common Stock who have not theretofore complied with the exchange procedures in this Section 1.7 shall look to Harbor only, and not the Exchange Agent, for the payment of any of the Merger Consideration in respect of such shares.

(d) None of Harbor, Merger Corp, the Exchange Agent or any other person shall be liable to any former holder of shares of Common Stock for any cash properly delivered to a public official pursuant to applicable abandoned property, escheat, or similar laws.

(e) In the event any Certificate shall have been lost, stolen or destroyed, upon the making of an affidavit of that fact by the person claiming such Certificate to be lost, stolen or destroyed and, if required by Harbor or the Exchange Agent, the posting by such person of a bond in such amount as Harbor or the Exchange Agent may direct as indemnity against any claim that may be made against it with respect to such Certificate, the Exchange Agent will issue in exchange for such lost, stolen or destroyed Certificate the Merger Consideration deliverable in respect thereof pursuant to this Agreement.

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1.8 **Approval by Shareholders.**
This Agreement shall be submitted to the shareholders of Harbor and Merger Corp in accordance with applicable provisions of law and the Articles of Incorporation and Bylaws of Harbor and Merger Corp. Harbor and Merger Corp shall proceed expeditiously and cooperate fully in the procurement of any other consents and approvals and the taking of any other actions in satisfaction of all other requirements prescribed by law or otherwise necessary for consummation of the Merger on the terms herein provided, including, without limitation, the preparation and submission of all necessary filings, requests for waivers, and certificates with the regulatory authorities, if any.

ARTICLE II REPRESENTATIONS AND WARRANTIES OF HARBOR

Harbor hereby represents and warrants to Merger Corp as follows:

2.1 **Organization and Authority.**
Harbor is a corporation duly organized, validly existing and in good standing under the laws of the State of Maryland, is a registered bank holding company under the Bank Holding Company Act of 1956, as amended, and has full corporate power to own its properties, to carry on its business, and to enter into this Agreement.

2.2 **Capital Structure.**
The authorized capital stock of Harbor is 10,000,000 shares of Common Stock, 641,784 shares of which are validly issued and outstanding, fully paid and nonassessable.

2.3 **Authorization.**

(a) The Board of Directors of Harbor has approved this Agreement and the transactions contemplated hereby, subject to the approval by the shareholders of Harbor as required by law. This Agreement has been duly executed and delivered by Harbor and when executed by Harbor and duly approved by the shareholders of Harbor, it will be a binding agreement of Harbor enforceable against it in accordance with its terms.

(b) Subject to the receipt of all required regulatory approvals and compliance with all applicable federal and state securities laws, the execution, delivery and performance of this Agreement and the transactions contemplated hereby and thereby will not violate any provision of, or constitute a default under any order, writ, injunction or decree of any court or other governmental agency, or any contract, agreement or instrument to which Harbor is a party or by which it is bound, or constitute an event which with the lapse of time or action by a third party could result in any default under any of the foregoing or result in the creation of any lien, charge or encumbrance upon any of the assets or properties of Harbor or upon shares of Common Stock.

ARTICLE III REPRESENTATIONS AND WARRANTIES OF MERGER CORP

Merger Corp hereby represents and warrants to Harbor as follows:

3.1 **Organization.**
Merger Corp is a Maryland corporation duly organized, validly existing and in good standing under the laws of Maryland, and has full corporate power and authority to own its properties, and to enter into this Agreement. Merger Corp does not have any subsidiaries.

3.2 **Capital Structure.**
The authorized capital stock of Merger Corp consists of 1,000 shares of common stock, $1.00 par value (the Merger Corp Stock), all of which are issued and outstanding. All such shares are validly issued, fully paid, and nonassessable. There are no existing options, warrants, calls, or commitments of any kind obligating Merger Corp to issue any of its authorized and unissued capital stock.

3.3 **Authorization.**

(a) The Board of Directors of Merger Corp has approved this Agreement and the transactions contemplated hereby, subject to the approval thereof by the shareholders of the Merger Corp as required by law. This Agreement has been duly executed and delivered by Merger Corp and when executed by Harbor and duly approved by the shareholders of Merger Corp, it will be a binding agreement of Merger Corp enforceable against it in accordance with its terms.

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(b) No Conflict with Other Instruments. Subject to the receipt of all required regulatory approvals and compliance with all applicable federal and state securities laws, the execution, delivery and performance of this Agreement and the transactions contemplated hereby and thereby will not violate any provision of, or constitute a default under, any order, writ, injunction or decree of any court or other governmental agency, or any contract, agreement or instrument to which Merger Corp is a party or by which it is bound, or constitute an event which with the lapse of time or action by a third party could result in any default under any of the foregoing or result in the creation of any lien, charge or encumbrance upon any of the assets or properties of Merger Corp or upon shares of capital stock of Merger Corp.

ARTICLE IV COVENANTS OF HARBOR

Harbor hereby covenants to and with Merger Corp as follows:

4.1 **Actions.**
Harbor will use its best efforts to take or cause to be taken all actions necessary, proper, or advisable to consummate this Agreement, including such actions Merger Corp may reasonably consider necessary, proper, or advisable in connection with filing applications and other instruments with, or obtaining approvals of, governmental bodies to the transactions contemplated by this Agreement.

4.2 **Conduct.**
From and after the date of this Agreement to the Effective Time of the Merger, Harbor will maintain its corporate existence, will not (i) amend its articles of incorporation by-laws, (ii) will not issue any securities, and (iii) will not declare or make any dividend or other distribution with respect to the outstanding shares of the Common Stock without written consent of Merger Corp.

4.3 **Payments.**
Harbor will deliver, when and if required by the provisions of this Agreement, such amounts of cash into which certain shares of Common Stock are to be converted pursuant to this Agreement.

ARTICLE V COVENANTS OF MERGER CORP

Merger Corp hereby covenants to and with Harbor as follows:

5.1 **Actions.**
Merger Corp will use its best efforts to take or cause to be taken all other actions necessary, proper or advisable to consummate this Agreement, including such actions as Harbor may reasonably consider necessary, proper or advisable in connection with filing applications and other instruments with, or obtaining approvals of, governmental bodies to the transactions contemplated by this Agreement.

5.2 **Conduct.**
From and after the date of this Agreement to the Effective Time, Merger Corp (i) will maintain its corporate existence; (ii) will not amend its charter or bylaws; and (iii) will not issue any securities.

ARTICLE VI CONDITIONS TO THE OBLIGATIONS OF HARBOR

The obligation of Harbor to effect the Merger shall be subject to the satisfaction prior to the Effective Time of the Merger of the following conditions:

6.1 **Shareholder Approval.**
The shareholders of Harbor shall have voted affirmatively to approve the Merger by not less than two-thirds of the outstanding voting stock of Harbor.

6.2 **Other Approvals.**
All requisite regulatory approvals relating to the Merger, if any, shall have been obtained and continue to be in full force and effect, and all waiting and notice periods under applicable law shall have expired.

6.3 **Rights of Objecting Shareholders and Other Shareholders Receiving Cash.**
The aggregate number of shares of Common Stock owned by those shareholders of Harbor who (i) have perfected and shall be entitled to exercise their objecting shareholders rights pursuant to the MGCL, or (ii) are shareholders of Cash-Out Shares (as defined in Section 1.4 herein) shall not exceed 1.0% of the issued and outstanding shares of Common Stock.

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6.4 **No Injunctions or Restraints; Illegality.**
No injunction, restraining order, stop order, or other order or action of any Federal or state court or agency in the United States which prohibits, restricts, or makes illegal the consummation of the transactions contemplated hereby shall be in effect, and no action, suit or other proceeding seeking such shall have been instituted or threatened, and no statue, rule, or regulation shall have been enacted, issued, or promulgated by and state or Federal government or government agency which prohibits, restricts, or makes illegal the consummation of the transactions contemplated hereby.

ARTICLE VII CONDITIONS TO THE OBLIGATIONS OF MERGER CORP

The obligation of Merger Corp to effect the Merger shall be subject to the satisfaction prior to the Effective Time of the Merger of the following conditions:

7.1 **Shareholder Approval.**
The sole shareholder of Merger Corp shall have voted affirmatively to approve the Merger by not less than two-thirds of the outstanding voting stock of Merger Corp.

7.2 **Other Approvals.**
All requisite regulatory approvals relating to the Merger, if any, shall have been obtained and continue to be in full force and effect, and all waiting and notice periods under applicable law shall have expired.

7.3 **Rights of Objecting Shareholders and Other Shareholders Receiving Cash.**
The aggregate number of shares of Common Stock owned by those shareholders of Harbor who (i) have perfected and shall be entitled to exercise their objecting shareholders rights pursuant to the MGCL, or (ii) are shareholders of Cash-Out Shares (as defined in Section 1.4 herein) shall not exceed 1.0% of the issued and outstanding shares of Common Stock.

7.4 **No Injunctions or Restraints; Illegality.**
No injunction, restraining order, stop order, or other order or action of any Federal or state court or agency in the United States which prohibits, restricts, or makes illegal the consummation of the transactions contemplated hereby shall be in effect, and no action, suit or other proceeding seeking such shall have been instituted or threatened, and no statue, rule, or regulation shall have been enacted, issued, or promulgated by and state or Federal government or government agency which prohibits, restricts, or makes illegal the consummation of the transactions contemplated hereby.

ARTICLE VIII TERMINATION AND AMENDMENT

8.1 **Termination.**
This Agreement may be terminated at anytime prior to the Effective Time by the Boards of Directors of either Merger Corp or Harbor.

8.2 **Effect of Termination.**
In the event of termination of this Agreement as provided in this Article VIII hereof, this Agreement shall forthwith become void and there shall be no liability or obligation on the part of Merger Corp or Harbor or their respective officers, directors or shareholders.

8.3 **Amendment.**
This Agreement may be amended by the parties hereto by action taken or authorized by their respective Boards of Directors. This Agreement may not be amended except by an instrument in writing signed on behalf of each of the parties hereto.

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ARTICLE IX GENERAL PROVISIONS

9.1 **Nonsurvival of Agreements.**
None of the agreements in this Agreement or in any instrument delivered pursuant to this Agreement shall survive the Effective Time of the Merger.

9.2 **Notices.**
All notices and other communications hereunder shall be in writing and shall be deemed given if delivered personally, telecopied (with confirmation), or mailed by registered or certified mail (return receipt requested) to Harbor or Merger Corp, respectively, at the following addresses:

(a) If to Harbor:
Joseph Haskins, Jr.

Chairman, President and CEO

Harbor Bancorp, Inc.

25 West Fayette Street

Baltimore, MD 21201

(b) If to Merger Sub:
Teodoro J. Hernandez

Vice President, Secretary, and Treasurer

Harbor Bancorp, Inc.,

25 West Fayette Street

Baltimore, MD 21201

9.3 **Interpretation.**
When a reference is made in this Agreement to Sections, such reference shall be to a Section of this Agreement unless otherwise indicated. The headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement. Whenever the words include, includes or including are used in this Agreement, they shall be deemed to be followed by the words without limitation.

9.4 **Counterparts.**
This Agreement may be executed in two counterparts, both of which shall be considered one and the same agreement and shall become effective when both counterparts have been signed by each of the parties and delivered to the other party, it being understood that both parties need not sign the same counterpart.

9.5 **Entire Agreement.**
This Agreement (including the documents and the instruments referred to herein) constitutes the entire agreement and supersedes all prior agreements and understandings, both written and oral, among the parties with respect to the subject matter hereof.

9.6 **Assignment.**
Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned by any of the parties hereto (whether by operation of law or otherwise) without the prior written consent of the other party.

9.7 **Governing Law.**
This Agreement shall be governed by and construed in accordance with the laws of the State of Maryland applicable to agreements made and entirely to be performed within such jurisdiction.

[Signature Page Follows]

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IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed as of the date first above written.

ATTEST: [SEAL]		**HARBOR BANKSHARES CORPORATION**
______________________________	By:	______________________________
		Joseph Haskins, Jr. Chairman, President, and CEO
ATTEST: [SEAL]		**HARBOR MERGER CORPORATION**
______________________________	By:	______________________________
		Teodoro J. Hernandez Vice President, Secretary, and Treasurer

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Appendix B Fairness Opinion

Danielson Associates Inc.

6001 Montrose Road, Suite 405

Rockville, Maryland 20852

(301) 468-4884 phone

(301) 468-0013 fax

December 8, 2006

The Board of Directors

Harbor Bankshares Corporation

25 West Fayette Street

Baltimore, Maryland 21201

Dear Members of the Board,

Set forth herein is Danielson Associates Inc. s (Danielson Associates) independent appraisal of the fair market value of the common stock of Harbor Bankshares Corporation (Harbor or the Bank) of Baltimore, Maryland as of December 8, 2005. Market value is defined as the price at which the common stock would change hands between a willing seller and a willing buyer, each having reasonable knowledge of relevant facts and assuming a significant amount of stock changing hands daily to assure a true reflection of market forces.

This fairness opinion is provided in connection with a proposed going private transaction, in the form of a merger in which Harbor common stock owned by shareholders who own 100 or fewer shares would be exchanged for cash.. Record holders of more than 100 shares of Harbor common stock would not receive cash for their shares in the merger and would remain Harbor shareholders. Harbor would be the surviving company in the merger.

This fairness opinion is based on data supplied by Harbor to Danielson Associates and its regulators, but relies on some public information, all of which is believed to be reliable, but the accuracy or completeness of such information cannot be guaranteed. In particular, this fairness opinion assumes that there are no significant loan quality problems beyond what has been stated in Harbor s quarterly reports to the Federal Deposit Insurance Corporation (FDIC).

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In determining the fair value of the common stock of Harbor, primary emphasis has been given to the stock prices of publicly-traded banks that have comparable financial, market and structural characteristics, and the relationship of these prices to earnings.

Based on these comparisons, an analysis of Harbor s past performance and future potential and by applying discounts for market, stock liquidity and its minority ownership, it has been established that the fair value of its common stock as of December 8, 2005 is between $28.13 and $29.63 per share with the midpoint being $28.88 per share. Any price in this range would be fair to current shareholders, including shareholders who would be cashed out in the merger and shareholders who would not be cashed out in the merger.

Respectfully submitted,

/s/ David G. Danielson

David G. Danielson
President

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Appendix C-Rights of Objecting Shareholders

Title 3. Corporations in General Extraordinary Actions
Subtitle 2. Rights of Objecting Stockholders

§ 3-201. Definition of successor

(a) In this subtitle, except as provided in subsection (b) of this section, "successor" includes a corporation which amends its charter in a way which alters the contract rights, as expressly set forth in the charter, of any outstanding stock, unless the right to do so is reserved by the charter of the corporation.

(b) When used with reference to a share exchange, "successor" means the corporation the stock of which was acquired in the share exchange.

§ 3-202. Fair value, right to from successors

(a) Except as provided in subsection (c) of this section, a stockholder of a Maryland corporation has the right to demand and receive payment of the fair value of the stockholder's stock from the successor if:

(1) The corporation consolidates or merges with another corporation;

(2) The stockholder's stock is to be acquired in a share exchange;

(3) The corporation transfers its assets in a manner requiring action under § 3-105(e) of this title;

(4) The corporation amends its charter in a way which alters the contract rights, as expressly set forth in the charter, of any outstanding stock and substantially adversely affects the stockholder's rights, unless the right to do so is reserved by the charter of the corporation; or

(5) The transaction is governed by § 3-602 of this title or exempted by § 3-603(b) of this title.

(b)(1) Fair value is determined as of the close of business:

(i) With respect to a merger under § 3-106 of this title of a 90 percent or more owned subsidiary with or into its parent corporation, on the day notice is given or waived under § 3-106; or

(ii) With respect to any other transaction, on the day the stockholders voted on the transaction objected to.

(2) Except as provided in paragraph (3) of this subsection, fair value may not include any appreciation or depreciation which directly or indirectly results from the transaction objected to or from its proposal.

(3) In any transaction governed by § 3-602 of this title or exempted by § 3-603(b) of this title, fair value shall be value determined in accordance with the requirements of § 3-603(b) of this title.

(c) Unless the transaction is governed by § 3-602 of this title or is exempted by § 3-603(b) of this title, a stockholder may not demand the fair value of the stockholder's stock and is bound by the terms of the transaction if:

(1) The stock is listed on a national securities exchange, is designated as a national market system security on an interdealer quotation system by the National Association of Securities Dealers, Inc., or is designated for trading on the NASDAQ Small Cap Market:

(i) With respect to a merger under § 3-106 of this title of a 90 percent or more owned subsidiary with or into its parent corporation, on the date notice is given or waived under § 3-106; or

(ii) With respect to any other transaction, on the record date for determining stockholders entitled to vote on the transaction objected to;

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(2) The stock is that of the successor in a merger, unless:

(i) The merger alters the contract rights of the stock as expressly set forth in the charter, and the charter does not reserve the right to do so; or

(ii) The stock is to be changed or converted in whole or in part in the merger into something other than either stock in the successor or cash, scrip, or other rights or interests arising out of provisions for the treatment of fractional shares of stock in the successor;

(3) The stock is not entitled, other than solely because of § 3-106 of this title, to be voted on the transaction or the stockholder did not own the shares of stock on the record date for determining stockholders entitled to vote on the transaction;

(4) The charter provides that the holders of the stock are not entitled to exercise the rights of an objecting stockholder under this subtitle; or

(5) The stock is that of an open-end investment company registered with the Securities and Exchange Commission under the Investment Company Act of 1940 and the value placed on the stock in the transaction is its net asset value.

§ 3-203. Duties of objecting stockholders

(a) A stockholder of a corporation who desires to receive payment of the fair value of the stockholder's stock under this subtitle:

(1) Shall file with the corporation a written objection to the proposed transaction:

(i) With respect to a merger under § 3-106 of this title of a 90 percent or more owned subsidiary with or into its parent corporation, within 30 days after notice is given or waived under § 3-106; or

(ii) With respect to any other transaction, at or before the stockholders' meeting at which the transaction will be considered or, in the case of action taken under § 2-505(b) of this article, within 10 days after the corporation gives the notice required by § 2-505(b) of this article;

(2) May not vote in favor of the transaction; and

(3) Within 20 days after the Department accepts the articles for record, shall make a written demand on the successor for payment for the stockholder's stock, stating the number and class of shares for which the stockholder demands payment.

(b) A stockholder who fails to comply with this section is bound by the terms of the consolidation, merger, share exchange, transfer of assets, or charter amendment.

§ 3-204. Effect of demand

A stockholder who demands payment for his stock under this subtitle:

(1) Has no right to receive any dividends or distributions payable to holders of record of that stock on a record date after the close of business on the day as at which fair value is to be determined under § 3-202 of this subtitle; and

(2) Ceases to have any rights of a stockholder with respect to that stock, except the right to receive payment of its fair value.

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§ 3-205. Consent to demand withdrawal

A demand for payment may be withdrawn only with the consent of the successor.

§ 3-206. Restoration of stockholder rights

(a) The rights of a stockholder who demands payment are restored in full, if:

(1) The demand for payment is withdrawn;

(2) A petition for an appraisal is not filed within the time required by this subtitle;

(3) A court determines that the stockholder is not entitled to relief; or

(4) The transaction objected to is abandoned or rescinded.

(b) The restoration of a stockholder's rights entitles him to receive the dividends, distributions, and other rights he would have received if he had not demanded payment for his stock. However, the restoration does not prejudice any corporate proceedings taken before the restoration.

§ 3-207. Successor's duty, notice and offer

(a)(1) The successor promptly shall notify each objecting stockholder in writing of the date the articles are accepted for record by the Department.

(2) The successor also may send a written offer to pay the objecting stockholder what it considers to be the fair value of his stock. Each offer shall be accompanied by the following information relating to the corporation which issued the stock:

(i) A balance sheet as of a date not more than six months before the date of the offer;

(ii) A profit and loss statement for the 12 months ending on the date of the balance sheet; and

(iii) Any other information the successor considers pertinent.

(b) The successor shall deliver the notice and offer to each objecting stockholder personally or mail them to him by certified mail, return receipt requested, bearing a postmark from the United States Postal Service, at the address he gives the successor in writing, or, if none, at his address as it appears on the records of the corporation which issued the stock.

§ 3-208. Petition for appraisal

(a) Within 50 days after the Department accepts the articles for record, the successor or an objecting stockholder who has not received payment for his stock may petition a court of equity in the county where the principal office of the successor is located or, if it does not have a principal office in this State, where the resident agent of the successor is located, for an appraisal to determine the fair value of the stock.

(b)(1) If more than one appraisal proceeding is instituted, the court shall direct the consolidation of all the proceedings on terms and conditions it considers proper.

(2) Two or more objecting stockholders may join or be joined in an appraisal proceeding.

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§ 3-209. Submission of certificate for notation

(a) At any time after a petition for appraisal is filed, the court may require the objecting stockholders parties to the proceeding to submit their stock certificates to the clerk of the court for notation on them that the appraisal proceeding is pending. If a stockholder fails to comply with the order, the court may dismiss the proceeding as to him or grant other appropriate relief.

(b) If any stock represented by a certificate which bears a notation is subsequently transferred, the new certificate issued for the stock shall bear a similar notation and the name of the original objecting stockholder. The transferee of this stock does not acquire rights of any character with respect to the stock other than the rights of the original objecting stockholder.

§ 3-210. Report of appraisers

(a) If the court finds that the objecting stockholder is entitled to an appraisal of his stock, it shall appoint three disinterested appraisers to determine the fair value of the stock on terms and conditions the court considers proper. Each appraiser shall take an oath to discharge his duties honestly and faithfully.

(b) Within 60 days after their appointment, unless the court sets a longer time, the appraisers shall determine the fair value of the stock as of the appropriate date and file a report stating the conclusion of the majority as to the fair value of the stock.

(c) The report shall state the reasons for the conclusion and shall include a transcript of all testimony and exhibits offered.

(d)(1) On the same day that the report is filed, the appraisers shall mail a copy of it to each party to the proceedings.

(2) Within 15 days after the report is filed, any party may object to it and request a hearing.

§ 3-211. Court order upon appraisers report

(a) The court shall consider the report and, on motion of any party to the proceeding, enter an order which:

(1) Confirms, modifies, or rejects it; and

(2) If appropriate, sets the time for payment to the stockholder.

(b)(1) If the appraisers' report is confirmed or modified by the order, judgment shall be entered against the successor and in favor of each objecting stockholder party to the proceeding for the appraised fair value of his stock.

(2) If the appraisers' report is rejected, the court may:

(i) Determine the fair value of the stock and enter judgment for the stockholder; or

(ii) Remit the proceedings to the same or other appraisers on terms and conditions it considers proper.

(c)(1) Except as provided in paragraph (2) of this subsection, a judgment for the stockholder shall award the value of the stock and interest from the date as at which fair value is to be determined under § 3-202 of this subtitle.

(2) The court may not allow interest if it finds that the failure of the stockholder to accept an offer for the stock made under § 3-207 of this subtitle was arbitrary and vexatious or not in good faith. In making this finding, the court shall consider:

(i) The price which the successor offered for the stock;

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(ii) The financial statements and other information furnished to the stockholder; and

(iii) Any other circumstances it considers relevant.

(d)(1) The costs of the proceedings, including reasonable compensation and expenses of the appraisers, shall be set by the court and assessed against the successor. However, the court may direct the costs to be apportioned and assessed against any objecting stockholder if the court finds that the failure of the stockholder to accept an offer for the stock made under § 3-207 of this subtitle was arbitrary and vexatious or not in good faith. In making this finding, the court shall consider:

(i) The price which the successor offered for the stock;

(ii) The financial statements and other information furnished to the stockholder; and

(iii) Any other circumstances it considers relevant.

(2) Costs may not include attorney's fees or expenses. The reasonable fees and expenses of experts may be included only if:

(i) The successor did not make an offer for the stock under § 3-207 of this subtitle; or

(ii) The value of the stock determined in the proceeding materially exceeds the amount offered by the successor.

(e) The judgment is final and conclusive on all parties and has the same force and effect as other decrees in equity. The judgment constitutes a lien on the assets of the successor with priority over any mortgage or other lien attaching on or after the effective date of the consolidation, merger, transfer, or charter amendment.

§ 3-212. Surrender of stock to successor

The successor is not required to pay for the stock of an objecting stockholder or to pay a judgment rendered against it in a proceeding for an appraisal unless, simultaneously with payment:

(1) The certificates representing the stock are surrendered to it, indorsed in blank, and in proper form for transfer; or

(2) Satisfactory evidence of the loss or destruction of the certificates and sufficient indemnity bond are furnished.

§ 3-213. Rights of successor

(a) A successor which acquires the stock of an objecting stockholder is entitled to any dividends or distributions payable to holders of record of that stock on a record date after the close of business on the day as at which fair value is to be determined under § 3-202 of this subtitle.

(b) After acquiring the stock of an objecting stockholder, a successor in a transfer of assets may exercise all the rights of an owner of the stock.

(c) Unless the articles provide otherwise, stock in the successor of a consolidation, merger, or share exchange otherwise deliverable in exchange for the stock of an objecting stockholder has the status of authorized but unissued stock of the successor. However, a proceeding for reduction of the capital of the successor is not necessary to retire the stock or to reduce the capital of the successor represented by the stock.

Appendix D
Form 10-KSB

Appendix E
Form 10-QSB

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-QSB

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2006.

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _________ to _________

Commission File Number 0-20990

HARBOR BANKSHARES CORPORATION

(Exact name of registrant as specified in its charter)

Maryland	**52-1786341**
(State of other jurisdiction of incorporation or organization)	(IRS Employer identification No.)
25 W. Fayette Street, Baltimore, Maryland	**21201**
(Address of principal executive office)	(Zip code)

Registrants telephone number, including area code: (410) 528-1800

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 such shorter period that the registrant was required to file such reports); and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a shell company (as defined in rule 12b-2 of the Exchange Act). Yes No

APPLICABLE ONLY TO CORPORATE ISSUERS: Indicate the number of shares outstanding of each of the issuers classes of common stock, as of the latest practicable date.

Common stock, non-voting, $.01 Par value 33,795 shares as of May 1, 2006.

Common stock, $.01 Par value -641,784 shares as of May 1, 2006.

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

INDEX

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

	March 31, 2006	December 31, 2005
	(Unaudited) Dollars in Thousands	
ASSETS		
Cash and Due from Banks	$ 5,287	$ 7,334
Federal Funds Sold		15,625
Investment Securities:		
Held to maturity at amortized cost (fair value of $24 as of March 31, 2006 and $30 as of December 31, 2005)	24	30
Available for Sale, at fair value	26,043	26,117
Total Investment Securities	26,067	26,147
Loans Held for Sale		716
Loans	202,650	190,279
Allowance for Loan Losses	(2,105)	(2,059)
Net Loans	200,545	188,220
Property and Equipment Net	7,556	7,526
Goodwill	2,506	2,506
Intangible Assets	443	463
Bank-owned Life Insurance	4,217	4,179
Accrued Interest Receivable and Other Assets	4,334	3,920
TOTAL ASSETS	$ 250,955	$ 256,636
LIABILITIES AND STOCKHOLDERS EQUITY		
Deposits:		
Non-Interest Bearing Demand	$ 46,964	$ 50,433
Interest Bearing Transaction Accounts	22,622	25,562
Savings	85,743	87,499
Time, $100,000 or more	33,387	32,810
Other Time	33,201	33,540
Total Deposits	221,917	229,844
Short Term Brrowings	3,000	
Junior Subordinated Debentures	7,217	7,217
Accrued Interest and Other Liabilities	2,056	2,621
TOTAL LIABILITIES	234,190	239,682
STOCKHOLDERS EQUITY		
Common stock, par value $.01 per share: Authorized 10,000,000 shares; issued and outstanding 641,784 at March 31, 2006 and 651,784 at December 31, 2005 and 33,795 common non-voting at March 31, 2006 and December 31, 2005.	6	7

Paid in Capital	6,366	6,616
Retained Earnings	10,958	10,853
Accumulated other comprehensive loss	(565)	(522)
TOTAL STOCKHOLDERS and EQUITY	16,765	16,954
TOTAL LIABILITIES and STOCKHOLDERS EQUITY	$ 250,955	$ 256,636

See Notes to Unaudited Consolidated Financial Statements

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

	Three Months Ended March 31 2006	2005
	(Unaudited) Dollars in Thousands Except Per Share Data	
INTEREST INCOME		
Interest and Fees on Loans	$ 3,777	$ 3,167
Interest on Investment Securities (Taxable)	207	219
Interest on Deposits in Other Banks	1	9
Interest on Federal Funds Sold	151	26
Other Interest Income	8	7
TOTAL INTEREST INCOME	4,144	3,428
INTEREST EXPENSE		
Interest on Deposits:		
Savings	609	263
Interest Bearing Transaction Accounts	13	14
Time $100,000 or More	259	135
Other Time	334	230
Interest Other Borrowed Money	1	4
Interest on Junior Subordinated Debentures	130	97
TOTAL INTEREST EXPENSE	1,346	743
NET INTEREST INCOME	2,798	2,685
Provision for Loan Losses	55	120
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	2,743	2,565
NON-INTEREST INCOME		
Service Charges on Deposit Accounts	168	238
Other Income	209	254
Loss on Sale of Loans	(2)	—
TOTAL NON-INTEREST INCOME	375	492
NON-INTEREST EXPENSE		
Salaries and Employee Benefits	1,186	1,121
Advertising	89	87
Occupancy Expense of Premises	330	214
Equipment Expense	86	87
Professional Cost	55	188
Data Processing Expense	274	261
ATM Loss	—	225
Other Expenses	395	415

TOTAL NON-INTEREST EXPENSES	2,415	2,598
INCOME BEFORE INCOME TAXES	703	459
Applicable Income Taxes	256	165
NET INCOME	$ 447	$ 294
BASIC EARNINGS PER SHARE	**$ 0.66**	**$ 0.42**
DILUTED EARNINGS PER SHARE	$ 0.62	$ 0.39
Dividends Declared per Share	$ 0.50	$ 0.40

See notes to unaudited consolidated Financial Statements

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended March 31 2006	2005
	(Unaudited) Dollars in Thousands	
OPERATING ACTIVITIES		
Net Income	$ 447	$ 294
Adjustments to Reconcile Net Income to Net Cash And Cash Equivalents Provided by Operating Activities:		
Origination of Loans Held for Sale	—	(152)
Proceeds from the Sale of Loans Held for Sale	714	—
Increase in bank-owned life insurance policies	(40)	(38)
Loss on sale of loans	2	—
Provisions for loan losses	55	120
Depreciation and Amortization	237	151
(Increase) Decrease in Interest Receivable and Other Assets	(412)	360
Decrease in Interest Payable and Other Liabilities	(565)	(189)
Net Cash Provided by Operating Activities	$ 438	$ 546
INVESTING ACTIVITIES		
Net decrease in Deposits at Other Banks	—	12
Proceeds from Matured Securities and Principal Payments	—	2,002
Net Increase in Loans	(12,344)	(6,236)
Purchase of Premises and Equipment	(246)	(967)
Net Cash Used in Investing Activities	(12,590)	(5,189)
FINANCING ACTIVITIES		
Net Decrease in Non-Interest Bearing Transaction Accounts	(3,469)	(7,115)
Net (Decrease) Increase in Interest Bearing Transaction Accounts	(2,940)	2,398
Net (Decrease) Increase in Savings Deposits	(1,756)	3,679
Net Increase in Time Deposits	238	1,044
Short Term Borrowings	3,000	—
Payment of Cash Dividends	(343)	(282)
Retirement of Common Stock	(250)	(275)
Proceeds from the Sale of Common Stock	—	63
Net Cash Used by Financing Activities	(5,520)	(488)
Decrease in Cash and Cash Equivalents	(17,672)	(5,131)
Cash and Cash Equivalents at Beginning of Period	22,959	16,714
Cash and Cash Equivalents at End of Period	$ 5,287	$ 11,583

See notes to unaudited consolidated Financial Statements

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

Notes to Unaudited Consolidated Financial Statements
For the Three Months Ended March 31, 2006

Note A: Basis of Presentation

The accompanying unaudited consolidated financial statements of Harbor Bankshares Corporation and subsidiaries (The Company) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10 QSB. Certain reclassifications have been made to amounts previously reported to conform to the classifications made in 2006. Accordingly, they do not include all the information required for complete financial statements. In the opinion of management, all adjustments and reclassifications considered necessary for a fair presentation have been included. All such adjustments are of a normal renewable nature. Operating results for the three month period ended March 31, 2006, are not necessarily indicative of the results that may be expected for the year ending December 31, 2006. The enclosed unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes thereto incorporated by reference in the Companys Annual Report on Form 10 KSB for the year ended December 31, 2005.

Note B: Comprehensive Income

The Companys comprehensive income consists of its net income and unrealized holding losses on its available for sale securities, net of taxes.

Presented below is a reconciliation of net income to comprehensive income.

	Three Months Ended March 31	
	2006	**2005**
	(In Thousands)	
Net Income	$ 447	$ 294
Unrealized (loss) gains on securities Available-for-sale	(71)	(409)
Related Income Tax (benefit) expense	(28)	(165)
	(43)	(244)
Total Comprehensive Income	$ 404	$ 50

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HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

EARNINGS PER SHARE

Note C: Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding for the period. Basic earnings per share does not include the effect of potentially dilutive transactions or conversions. This computation of diluted earnings per share reflects the potential dilution of earnings per share under the treasury stock method, which could occur if contracts to issue common stock, such as stock options, were exercised and shared in corporate earnings. At March 31, 2006 and 2005, there were no antidilutive options to purchase common shares.

The following table presents a summary of per share data and amounts for the period indicated:

	Three Months Ended	
	2006	**2005**
	(amount in thousands except per-share data)	
Basic:		
Net income applicable to common stock	$ 447	$ 294
Average common shares outstanding	680	697
Basic net income per share	$ .66	$ .42
Diluted:		
Net income applicable to common stock	$ 447	$ 294
Average common shares outstanding	680	697
Stock option adjustment	41	55
Diluted average common shares outstanding	721	752
Diluted net income per share	$ .62	$ .39

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HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

Note D: EMPLOYEE STOCK-BASED COMPENSATION

Effective on January 1, 2006, the Company adopted Financial Accounting Standards Board Statement No. 123R, "Share-Based Payment" (Statement 123R), which requires an entity to measure the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. Previously, the Company accounted for stock-based compensation plans and the employee stock purchase plan in accordance with Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees" and related Interpretations and provided the required pro forma disclosures of Financial Accounting Standards Board Statement No. 123, "Accounting for Stock-Based Compensation". The Company elected to adopt the modified prospective-transition method as provided by Statement 123R. Under this transition method, compensation cost recognized during 2006 includes (a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006 based on the grant-date fair value estimated in accordance with the original provisions of Statement 123, and (b) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of Statement 123R. The effect of applying Statement 123R was a decrease to net income of $10 thousand for the quarter ended March 31, 2006, or $0.01 per basic and diluted share. Results for prior periods have not been restated.

The following table illustrates the effect on net loss and loss per share as if the Company had applied the fair value recognition provisions of Statement 123R to stock-based employee compensation for the period ended March 31, 2005:

	Three months Ended 3/31/05
Net income, as reported	$ 294
Add: Stock-based compensation cost included in net loss, net of taxes	—
Deduct: Total stock-based compensation expense determined under fair value based method for all awards, net of taxes	(12)
Pro forma net income	
Pro forma net income attributable to common stockholders	$ 282
Net income attributable to common stockholders:	
Basic — as reported	$ 0.42
Diluted — as reported	$ 0.39
Basic — pro forma	$ 0.40
Diluted — pro forma	$ 0.37

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

The following are the assumptions made in computing the fair value of stock-based awards:

	Three months ended March 31,	
	2006	**2005**
Average risk-free interest rate	4.36%	5.00%
Dividend yield	1.50%	1.50%
Expected term	10	10
Average expected volatility	20%	20%
Weighted average fair value of granted options	7.44	6.78

Expected volatilities are based on historical volatility of the Companys stock. The expected term of options granted represents the period of time that options granted are expected to be outstanding. The Company uses historical data to estimate option exercise and employee termination within the valuation model. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

A summary of stock option activity during the three months ended March 31, 2006 and related information is included in the table below:

	Options	**Weighted-Average Exercise Price**	**Aggregate Intrinsic Value**
Outstanding at January 1, 2006	132,741	16.24	$ 2,159,300
Granted	6,043	25.00	151,075
Exercised			
Forfeited	(15,500)	16.19	(250,945)
Outstanding at March 31, 2006	123,284	16.70	2,059,430
Exercisable at March 31, 2006	123,284	16.70	2,059,430
Weighted-average remaining contractual life	7.6		

The weighted average grant date fair value of options granted during the quarter ended March 31, 2006 was $25.00 per share. All options granted have an exercise price equal to the fair value of the Companys common stock on the date of grant. Exercise prices for options outstanding as of March 31, 2006 ranged from $15.24 to $25.00 as follows:

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

Range of Exercise Prices	Options Outstanding	Weighted Average Exercise Prices of Options Outstanding	Weighted Average Remaining Contractual Life of Options Outstanding
$15.24 $17.35	99,853	$ 15.45	5.35
$18.00 $21.69	12,497	$ 20.24	7.65
$23.04 $25.00	10,934	$ 24.44	9.73
	123,284		

Assuming that no additional share-based payments are granted after March 31, 2006, unamortized stock compensation expense of $40,614 will be recognized in the statement of operations over a weighted average period of 1.73 years.

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

Part I. FINANCIAL INFORMATION

Item 2. Managements Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements. This management's discussion and analysis of financial condition and results of operations and other portions of this report include forward-looking statements such as: statements of the Company's goals, intentions, and expectations; estimates of risks and of future costs and benefits; assessments of loan quality, and probable loan losses, liquidity, and interest risk; and statements of the Company's ability to achieve financial and other goals. These forward-looking statements are subject to significant uncertainties because they are based upon: the amount and timing of future changes in interest rates, market behaviors, and other economic conditions; future laws and regulations; and a variety of other matters. Because of these uncertainties, the actual future results may be materially different from the results indicated by these forward-looking statements. In addition, the Company's past growth and performance do not necessarily indicate its future results.

Harbor Bankshares Corporation's earnings for the first quarter of 2006 totaled $447 thousand, reflecting an increase of $153 thousand or 52.0 percent when compared to the first quarter of 2005. For the first quarter of 2006, the annualized return on average assets (ROAA) and average stockholders equity (ROAE) were .70 percent and 10.64 percent respectively, compared to .50 percent and 7.29 percent respectively achieved during the first quarter of 2005.

For the first quarter of 2006, net interest income increased by $113 thousand or 4.2 percent. Interest and fees on loans increased by $610 thousand or 19.3 percent as a result of the growth in the portfolio and rate increases. Investment income decreased by $12 thousand or 5.5 percent. Interest on Federal Funds sold increased by $125 thousand or 480.7 percent. Interest expense increased by $603 thousand or 81.2 percent. Interest on time deposits increased by $228 thousand or 62.4 percent. Interest expense on saving accounts increased by $346 thousand or 131.5 percent. Although, deposits as of March 31, 2006 decreased when compared to December 31, 2005, higher interest rates led to an overall interest expense increase in deposits. The interest expense of borrowed funds for the quarter was $1 thousand. The interest expense for the junior subordinated debentures increased by $33 thousand or 34.0 percent due to higher interest rates, since the debentures are tied to floating rates.

For the quarter ended March 31, 2006, the provision for loan losses was $55 thousand compared to $120 thousand for the same period of 2005. Charge-offs totaled $10 thousand reflecting a decrease of $3 thousand when compared to the $13 thousand charged-off during the same period for 2005. Recoveries for the period were $2 thousand, compared to $38 thousand recovered during the first quarter of 2005.

Future provisions for loan losses will continue to be based upon our assessment of the overall loan portfolio and its underlying collateral, the mix of loans within the portfolio, delinquency trends, economic conditions, current and prospective trends in real estate values, and other relevant factors under our allowance methodology.

Our allowance for loan loss methodology is a loan classification-based system. We base the required allowance on a percentage of the loan balance for each type of loan classification level. Allowance percentages are based on each individual lending program, its loss history and underwriting characteristics including loan value, credit score, debt coverage, collateral, and capacity to service debt.

This analysis is used to validate the loan loss reserve matrix as well as assist in establishing overall lending direction. In Management's opinion, the allowance for loan losses as of March 31, 2006 is adequate. There

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

were no changes in estimation methods or assumptions that affected the methodology for assessing the appropriateness of the allowance during the period.

Non-performing assets consist of non-accruing loans, loans past due 90 days or more but still accruing, restructured loans, and foreclosed real estate.

The following table shows the non-performing assets as of March 31, 2006 compared to December 31, 2005.

	March 31, 2006	December 31, 2005
	(In Thousands)	
Non-accruing Loans	$ 200	$ 558
Past Due 90 days or more	46	18
Restructured loans	—	—
Total non-performing loans	246	576
Foreclosed real estate	—	—
Total non-performing assets	$ 246	$ 576
Non-performing loans to total loans	0.12%	0.30%
Non-performing assets to total assets	0.45%	0.22%
Allowance for loan losses to non-performing loans	855.69%	357.50%

Non-interest income decreased by $117 thousand or 23.8 percent. Service charges on deposit accounts decreased by $70 thousand or 29.4 percent, mainly related to decreases in the returned check fees charges. Other income decreased by $45 thousand or 17.7 percent. There was a loss of $2 thousand on the sale of loans during the first quarter of 2006. Salary and employee benefits at $1.2 million increased by $65 thousand when compared to the same period of 2005. Advertising cost of $89 thousand increased slightly by $2 thousand. Occupancy expense increased by $116 thousand or 54.2 percent reflecting the cost associated with the renovation of the Corporation’s headquarter building and a de-novo branch facility opened during the last quarter of 2005. Equipment expenses decreased by $1 thousand or 1.1 percent. Professional cost decreased by $133 thousand or 70.7 percent mainly due to a decrease in legal cost associated with the ATM shortage settlement. Data processing fees increased by $13 thousand or 5.0 percent. Included in non-interest expenses for the quarter ending March 31, 2005 was a $225 thousand expense related to a final settlement of the ATM shortage. On April 8, 2005, the Bank settled this matter in return for the payment of $575 thousand. All other expenses decreased by $20 thousand or 4.8 percent.

As of March 31, 2006, total deposits were $222 million, reflecting a decrease of $7.9 million when compared to deposits as of December 31, 2005. Non-interest bearing deposits decreased by $3.5 million or 6.9 percent. Interest bearing transaction accounts decreased by $2.9 million or 11.5 percent. Savings accounts which included money market accounts decreased by $1.8 million or 2.0 percent and time deposits increased by $238 thousand or 0.4 percent. There was $3.0 million of other short term borrowings outstanding as of the quarter end.

Total loans, increased by $12.4 million or 6.5 percent. The increase was mainly reflected in the commercial loans and commercial real estate categories. Stockholder’s equity decreased by $189 thousand or 1.1 percent, resulting from an increase of $43 thousand of unrealized losses on available-for-sale securities, cash dividend paid in the amount of $343 thousand, retirement of 10,000 shares or $250 thousand of common stock, offset by earnings of $447 thousand. Primary and risk based capital were 7.2 percent and 11.14 percent, respectively.

As of March 31, 2006, based on borrowing arrangements with the Federal Home Loan Bank there was unused credit availability of $22.0 million, the Corporation has sufficient liquidity to withstand any unusual demand of funds without the liquidation of its securities.

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

The Harbor Bank CDC (CDC) and The Harbor Bank of Baltimore LLC (LLC) were established in 2003. The Harbor Bank CDC is a non-profit company established with the purpose of bringing financial assistance to underserved areas in the City of Baltimore. The Corporation has no investments in this company. The Harbor Bank of Maryland, one of the Corporations subsidiaries has a $1.8 million loan to the CDC. As of March 31, 2005, the CDC had $4 thousand in operating income and a $25 thousand loss since inception. These numbers exclude any tax benefit that may be available.

The Harbor Bank of Baltimore LLC was established with the purpose of taking advantage of the New Markets Tax Credit program offered by the U.S. Treasury Department for the development of certain targeted markets in the country. In the case of the LLC, the targeted market is the City of Baltimore. The LLC received a $50 million New Market Tax Credit award in September 2004. The LLC funded a $25.0 million loan through a partnership with General Motors Corporation. The Corporation has no investment in this company.

The financial data from these companies is not included in the Corporations financial statements.

The Corporations stock is traded over the counter. During the first three months of 2006, only one trade was registered at $25.00 per share.

Recent Development
On May 2, 2006, the Corporation filed a preliminary proxy statement with the Securities and Exchange Commission with respect to the 2006 annual shareholders meeting, at which shareholders would be asked (i) to approve a merger designed to allow the Corporation to no longer be subject to periodic and other reporting obligations under the Securities Exchange Act of 1934, and (ii) to reelect four Class II directors. The proxy statement has not been finalized.

ITEM 3. Controls and Procedures
The Companys management, under the supervision and with the participation of its Chief Executive Officer and the Treasurer, evaluated as of the last day of the period covered by this report, the effectiveness of the design and operation of the Companys disclosure controls and procedures, as defined in Rule 13a 15 under the Securities Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and Treasurer concluded that the Companys disclosure controls and procedures were adequate. There were no significant changes in the Companys internal controls over financial reporting (as defined in Rule 13a 15 under the Securities Act of 1934) for the period ending March 31, 2006 that have materially affected, or are reasonably likely to materially affect, the Companys internal control over financial reporting.

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

Part II. **OTHER INFORMATION**

Item 1. Legal Proceedings

The Company and its Bank subsidiary, at times and in the ordinary course of business, are subject to various pending and threatened legal actions. The relief or damages sought in some of these actions may be substantial. Management considers that the outcome of such actions will not have a material adverse effect on the Company's financial position; however, the Company is not able to predict whether the outcome of such actions may or may not have a material adverse effect on results of operations in a particular future period as the timing and amount of any resolution of such actions and relationship to the future results of operations are not known.

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

Issuer Purchases of Equity Securities (1)

Period	(a) Total Number of Shares Purchased	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number that May Yet Be Purchased Under the Plans or Programs
January 2006	10,000	$25.00	10,000	0
February 2006	0			
March 2006	0			

(1) Includes purchases of the Company's stock made by or on behalf of the Company or any affiliated purchasers of the Company as defined in Securities and Exchange Commission Rule 10b-18.

Item 3. Defaults Upon Senior Securities

None

Item 4. Matters Submitted to a Vote of Security Holders

None

Item 5. Other Information

None

Item 6. Exhibits

Exhibit 31(a),(b), Rule 13a-14(a)/15d-14(a) Certifications

Exhibit 32(a), (b), 18 U.S.C Section 1350 Certifications

HARBOR BANKSHARES CORPORATION AND SUBSIDIARIES

SIGNATURES

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

HARBOR BANKSHARES CORPORATION

Date: May 12, 2006

/s/ Joseph Haskins, Jr.
Joseph Haskins, Jr.
Chairman and Chief Executive Officer

Date: May 12, 2006

/s/ Teodoro J. Hernandez
Teodoro J. Hernandez
Vice President and Treasurer

Exhibit (c)(iii) to Schedule 13E-3

HARBOR BANKSHARES CORPORATION

Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

HARBOR BANKSHARES CORPORATION

Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

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Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

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HARBOR BANKSHARES CORPORATION

Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

Set forth herein is Danielson Associates Inc. s (Danielson Associates) independent appraisal of the fair market value of the common stock of Harbor Bankshares Corporation (Harbor or the Bank) of Baltimore, Maryland as of December 8, 2005. Market value is defined as the price at which the common stock would change hands between a willing seller and a willing buyer, each having reasonable knowledge of relevant facts and assuming a significant amount of stock changing hands daily to assure a true reflection of market forces.

This fairness opinion is based on data supplied by Harbor to Danielson Associates and its regulators, but relies on some public information, all of which is believed to be reliable, but the accuracy or completeness of such information cannot be guaranteed. In particular, this fairness opinion assumes that there are no significant loan quality problems beyond what has been stated in Harbor s quarterly reports to the Federal Deposit Insurance Corporation (FDIC).

In determining the fair value of the common stock of Harbor, primary emphasis has been given to the stock prices of publicly-traded banks that have comparable financial, market and structural characteristics, and the relationship of these prices to earnings.

Based on these comparisons, an analysis of Harbor s past performance and future potential and by applying discounts for market, stock liquidity and its minority ownership, it has been established that the fair value of its common stock as of December 8, 2005 is between $28.23 and $29.63 per share with the midpoint being $28.88 per share. Any price in this range would be fair to current shareholders.

Respectfully submitted,

/s/ David G. Danielson

David G. Danielson
President
Danielson Associates Inc.

DESCRIPTION

Harbor Bankshares Corporation (Harbor or the Bank) was formed in 1992 and is based in Baltimore, Maryland. Its wholly owned subsidiary, Harbor Bank of Maryland (Harbor or also the Bank) is regulated by the Federal Deposit Insurance Corporation. The holding company is regulated by the Federal Reserve.

The Bank was formed in 1982 and currently has six full-service offices, of which four are in the City of Baltimore. The other two branches are in Baltimore and Prince George s counties. Additionally, the Bank plans to open a branch in the University of Maryland s biotechnology park which would bring its total branch network up to seven. Its services include checking, savings and time deposits; home and commercial mortgages; and commercial and consumer loans. The lending emphasis is on commercial real estate and commercial loans. The Bank is also a member of a local and national ATM network

Market

The markets served by the Bank s six offices typically have a majority African-American population. The Baltimore City branches are in areas with negative population growth rates and are median household income of less than $33,000. The branches in Baltimore and Prince George s counties have good population growth rates and median household income of $56,000 and $62,000, respectively. Currently, the Bank does the majority of its business in the City of Baltimore with 75% of the deposits located within its four branches (see Tables 1 and 2).

Harbor is a relatively small factor in its primary market of Baltimore City and Baltimore County, but it has managed to keep its share of deposits. On June 30, 2005, it had deposits of $195 million, or .6% of the area s total. It ranked nineteenth in overall deposit size, and twelfth when compared to locally-based institutions (see Table 3).

Financial Performance

Since its inception, Harbor has been a slow growing bank. This, though, is still considered good growth as its primary market has a declining population base and comparatively low income levels. In 1990, its eighth year of operations, the Bank had assets of $38 million and grew these assets to $62 million by the end of 1993. In 1994, the Bank purchased 2 branches from the Resolution Trust Corporation, which moved assets above $100 million for the first time. From he beginning of 1998 through the end of 2001 a four year period Harbor s growth stalled as assets hovered around $184 million. Growth picked up again in 2002 when Harbor purchased a branch in Randallstown from Carrollton Bancorp. With the purchase of this branch, the Bank s assets in 2002 surpassed $200 million and as of September 30, 2005 it had assets of $247 million (see Table 4).

Harbor has earned in excess of $1 million annually since 2002, and annualized earnings for the nine months ended September 30, 2005 are just under $1.8 million. These earnings produced returns on equity in the 8% to 12% range during this period and while these are good results, they were helped by capital that was less than 7% of assets. Returns on assets were not as good, ranging from a low of .54% to a high of .84% during this same period.

On the asset side of the balance sheet the Bank has shown some good underlying momentum. The Bank has consistently added about $20 million in loans per year since 2001 and as of September 30, 2005, the Bank had loans outstanding of $194 million. This growth in loans has allowed Harbor to reduce its securities position from $52 million at the end of 2001, to $26 million as of September 30, 2005 a reduction of 50% (see Table 5).

The growth of the loan portfolio has had a positive impact on Harbor s margins. In a period when margin decline is an industry-wide problem, the Bank generally went against industry trends. The net result was net interest income rose from 3.85% of average assets in 2001 to better then 4.40% of average assets in 2003 and 2004. In the first nine months of 2005, net interest income was 4.59% of average assets, well above the regional average (see Table 6).

Harbor has not translated these above-average margins into above-average earnings because of its high overhead. Its operating expense of 3.98% of average assets through the first nine months of 2005 was more than one percentage point higher than the regional average of 2.79% (see Table 6).

The reasons for the good margins can be readily seen in the Bank s deposit mix. As of June 30, 2005, about 23% of its deposits were non-interest-bearing and 48% were savings and other transactions accounts. Only 29% were CDs, which normally are the most expensive type of deposits (see Table 7).

As a result of the loan growth discussed earlier, Harbor, as of June 30, 2005, had 78% of its assets committed to loans, compared to only 61% in 2000. More then half of these loans were secured by real estate 16% were residential mortgages and 39% by commercial real estate. The other large loan type was commercial loans not secured by real estate, which comprised 40% of the loan portfolio (see Table 7).

The Bank s asset quality continues be adequate with non-performing assets (NPAs) at .38% of assets as of September 30, 2005. The only concern would be the low level of reserves as a percentage of loans. As of September, 30, 2005 reserves as a percentage of loans was only 1.01%, which is low considering the large amount of non-secured commercial loans and an equity-to-assets ratio of only 6.66%. The median reserve to loans of its regional peers was 1.11% (see Table 8).

What do all these numbers say about Harbor? They describe a good, small bank that has decent earnings and grown steadily over the years, both internally and through branch acquisitions, but that has not maximized its earnings potential. In order to do this it either has to reduce overhead or grow into the existing overhead. The latter may require additional capital.

4

COMPARISONS WITH OTHER

PUBLICLY-TRADED COMMERCIAL BANKS

Overview

In determining a fair price for the outstanding shares of Harbor s common stock, the Bank has been compared with four groups of publicly-traded banks. The initial comparisons are to three groups of non-minority banks in urban areas, but the primary comparison on which Harbor s valuation is based is to a group comprised of other minority-owned banks. In the first three groups, the term urban has no solid definition but simply means a metropolitan area like Jacksonville, Florida or Charlotte, North Carolina, or a smaller city like Annapolis, Maryland.

Urban exchange group Comprised of fourteen commercial banks based in urban areas along the east coast with assets between $150 and $500 million, returns on average assets above .50% and trade on a national exchange. The stocks of these banks, with three exceptions trade, on average more than 2,000 shares each day (see Table 9a).
Urban OTC group - Consists of eleven commercial banks with the same restrictions as the urban exchange group but trade instead on the over-the-counter bulletin board market. The stocks of most of these banks are less liquid than the urban exchange group and trade on average a little over 900 shares each day (see Table 10a).
Urban most applicable group Since these first two groups contained several newly-formed banks and banks with much better performance than Harbor, a third group was created from the banks in the urban exchange group and the urban OTC group which eliminated those less comparable banks. The remaining seven banks are the banks most applicable to Harbor based on location, performance and history (the urban most applicable group) (see Table 11a).
Minority-owned group Comprised of the seventeen minority-owned banks and thrifts that are publicly-traded. There are several different minorities represented African-American, Hispanic, Asian and women. This group was condensed further as those banks with assets over $900 million or other attributes that would make them incomparable to Harbor were excluded (see Table 12 and 13a).

The first two groups of urban comparables, and the third group which is a mix of the first two, provides a good base from which to view the pricing of a non-minority-owned bank located in a city. As will be discussed later, minority-owned banks tend to serve larger more densely populated urban areas and typically have a lower valuation.

Urban Comparables

The urban exchange group s financial performance was comparable to Harbor. The urban exchange group s median returns on average assets and equity of .78% and 9.74% were similar to Harbor s .74% and 10.94%, respectively. Additionally, NPAs as a percent of assets were .38% for Harbor which was higher, but not much higher, than the .22% for the comparable group. The urban exchange group had equity-to-assets of 8.24% while Harbor s was 6.66% (see Table 9b).

Harbor s net interest income of 4.59% of average assets in the nine months ending September 30, 2005 was much higher than the urban exchange group median of 3.65%, but this was more than offset by net operating expense that was about one and a half times the comparative group s median (see Table 9c).

The urban exchange group s stock price multiples were diverse. The price times earnings multiples for the fourteen banks, ranged from 12.8 to 34.0 times earnings, with a median of 22.7 times earnings. The price-to-book ratios also had a wide range with a low of 143%, a high of 288% and the median was 178% (see Table 9d).

The urban OTC group performed much better than Harbor with median returns on average assets and equity of 1.12% and 14.18%, respectively, compared to .74% and 10.94%, respectively, for Harbor. Equity-to-assets was similar with the urban OTC group having a median of 6.53% to Harbor s 6.66%. Once again the NPAs of the comparable group were lower with the urban OTC group but at .23% of assets versus .38% of assets for Harbor the difference was negligible.

In comparing income and expense ratios, Harbor outperformed the OTC group in terms of net interest income but gave away its advantage with higher net operating expense. Harbor had net interest income to average assets of 4.59% for the first nine months ended September 30, 2005 versus a median of 3.96% for the urban OTC group. Net operating expense was the opposite with Harbor having a much higher net operating expense to average assets of 3.23% compared to 2.12% for the comparable group. As a result Harbor s net operating as a percent of assets was lower than that of the comparable group s median 1.36% to 2.04% (see Tables 10b and 10c).

The pricing ratios for the urban OTC group were just as wide as the urban exchange group. Price-to-earnings multiples ranged from 11.6 to 30.7, with a median of 17.8. Price-to-book multiples ranged from 159% to 296% of book with a median of 223% (see Table 10d).

Using the pricing multiples of the urban exchange group and the urban OTC group, the pricing multiples applied to Harbor would be in the range of 18 to 23 times earnings and 170% to 230% of book. These ratios, though, are high because the groups contain several newly formed banks and a few banks with far superior performance that are valued at high multiples. Thus, a third group was formed the urban most applicable group using banks from the first two groups but eliminating new or high performing banks. This newly formed group is comprised of seven banks.

The urban most applicable group s seven banks had median returns on average assets and equity of .91% and 11.30%, respectively. While this was higher than Harbor s .74% and 10.94%, respectively, both are in the range of moderate performing banks (see Tables 11b and 11c).

The urban most applicable group had pricing multiples based on earnings much tighter than the other two groups if one outlier is ignored. Price times earnings multiples ranged from 11.6 to 32.1 with five of the seven between 12.8 and 18.7. Price-to-book ranged from 143% to 237% with five of the seven between 145% and 212%. The median price times earnings was 15.5 and the median price-to-book was 186% (see Table 11d).

Minority-Owned Comparables

There are seventeen publicly traded minority-owned institutions as defined by the Federal Reserve Bank. These banks represent African-American, Hispanic, Asian and women minorities. Some of these banks are comparable to Harbor but others because of their size, performance or minority orientation are not comparable and have been excluded. The remaining four banks that are most comparable to Harbor provide the best basis on which to value its stock (see Table 12 and 13a).

The minority-owned institutions that were non-comparable were excluded based on size, performance or minority orientation. The five banks with assets over $900 million were so much larger than Harbor that they were not comparable. In terms of performance there were three banks whose performance was too far above Harbor s to be comparable and five banks whose performance was too far below Harbor s to be comparable. The three top performers all had returns on equity near 14% or more and the five poor performing banks all had returns on equity below 4%. In addition two of these poor performers were too small to be comparable with assets under $100 million and a third had high NPAs which might add another reason that it would be incomparable. One of the top performers Abigail Adams has performance that could be considered comparable but it was also eliminated based on being a women s owned bank, rather than an African-American owned bank, and it does not market itself as a minority-owned institution (see Table 13a and 13b).

Financial Performance Comparisons*

	Equity/ Assets	NPAs/ Assets	Return on Average Assets	Return on Average Equity
Comparable groups				
Urban exchange group	8.24 %	.22 %	.78 %	9.74 %
Urban OTC group	6.53	.23	1.12	14.18
Urban most applicable group	6.78 %	.42 %	.91 %	11.30 %
Minority-owned group	7.87	.57	.59	7.24
Harbor**	6.66 %	.38 %	.74 %	10.94 %

* For the twelve months ended September 30, 2005 or September 30, 2005, or most recent available.

** Nine months ended September 30, 2005 or September 30, 2005.

Source: SNL Financial, Charlottesville, Virginia and internal reports.

The remaining four minority-owned institutions (the minority-owned group) were all African-American owned, three of which were banks and the other a thrift. The largest in the group was the New York City based thrift Carver Bancorp, Inc. (Carver) with assets of $648 million and the smallest the Miami, Florida based PanAmerican Bancorp (PanAmerican) with assets of $244 million The other two banks were the Atlanta, Georgia based Citizens Bancshares Corporation (Citizens) and the Washington, D.C. based IBW Financial Corporation (IBW). Harbor with assets of $247 million was nearly identical in assets to PanAmerican.

Equity as a percent of assets was similar for three of the banks, but the fourth was substantially higher. The three with similar capital-to-asset ratios Carver, Citizens and IBW all had ratios between 7.33% and 8.29%. Harbor had capital-to-assets of 6.66%. The fourth bank PanAmerican had capital-to-assets of 17.59% but it just raised about $15 million in new equity in the third quarter of 2005.

In terms of performance the four banks in the minority-owned group had performance comparable but below that of Harbor. Returns on average equity ranged from 5.93% to 8.66% with a median of 7.24%. Harbor s return on average equity was 10.94% but it was aided by its low capital ratio. Returns on average assets were closer with the four banks posting returns of .45%, .48%, .69% and .99%. Harbor had a return on average assets of .74%, above all but one of the minority owned group.

In terms on NPAs none of the four banks in the minority-owned group has significant NPAs. The bank with the lowest NPAs-to-assets was PanAmerican at .02% and the highest was Citizens with 1.23%. Harbor had NPAs-to-assets of .38%.

Harbor s net interest income and net operating expense as a percent of average assets was similar to that of three of the four banks in the minority-owned group. Harbor s net interest income to average assets of 4.59% was inside the range of 4.48% to 4.65% posted by Citizens, IBW and PanAmerican. In terms on net operating expense to average assets Harbor s 3.23% was again inside the range of the same three banks 3.16% to 3.87%. The fourth bank Carver posted net interest income and net operating income as a percent of average assets of 3.05% and 2.29%, respectively.

The pricing of three of the four banks in the minority-owned group were similar. Citizens, Carver and IBW all had price times earnings multiples in a fairly tight range with multiples of 9.8, 14.0 and 14.0 times earnings, respectively. These same banks had price-to-book ratios of 82%, 80% and 90%, respectively. The fourth bank, PanAmerican had a price times earnings multiple of 22.2 and price-to-book of 141%. The pricing of PanAmerican can be discounted as it recently raised a substantial amount of new capital after years of losses and its stock trades for less than $5.00.

Stock Pricing Comparisons*

	Price			
	Times Earnings	Percent of Book	Avg. Shares Traded Daily**	No. in Group
Comparable groups				
Urban exchange group	22.7X	178%	2,615	14
Urban OTC group	17.8	223	920	11
Urban most applicable group	15.5X	186%	1,359	7
Minority-owned group	14.0	86	1,836	4

* December 8, 2005 stock price and financial data for the year ended September 30, 2005 or September 30, 2005 or most recent available.

** For the past year.

Source: SNL Financial, Charlottesville, Virginia and internal reports.

MARKET VALUE ADJUSTMENTS

In order to determine a fair price for shares of Harbor s common stock, it is necessary to consider how it differs from the most applicable group and the minority-owned group and make the adjustments reflecting the differences, if needed. These adjustments should consider such items as profitability, capital, growth momentum, market, deposit mix, asset mix and quality, management, liquidity of stock as well as any unique circumstances. Background information on these items appears in the preceding section or in the tables at the end of the report.

Profitability

Earnings, when they are normal, are the primary determinant of the value of a stock, but relationships based on earnings have to consider their sustainability. Harbor s earnings have been consistent over the last three years, and its overall financial condition make it likely that it can, and will, sustain similar earnings and earnings growth going forward. Thus, in an earnings-determined valuation, there is no cause for an adjustment based on profitability.

Capital

Harbor s capital-to-asset ratio is low but so were several banks in the comparable groups. The current amount of capital is sufficient to continue to grow at historical rates and should not have an impact on restraining earnings growth. Thus, there is no cause for a value adjustment based on capital.

In the beginning of 2006, the Bank s going private transaction will cause the holding company to purchase, approximately, 14,000 shares of Harbor common stock for an amount less than $420,000. This will reduce Harbor s capital ratios, but not enough to cause a value adjustment.

Growth

Harbor s growth has been adequate. Some of this growth was fueled by branch acquisitions, but this has helped Harbor hold onto its current local market share. Thus, growth is not a reason for a value adjustment.

Market

The Bank has continued to look for branches in growing areas within its market, but the majority of its branches and deposits are in Baltimore City, a declining market. This is particularly important in a valuation since part of the value of a bank is its growth opportunities and the likelihood that it will be acquired. Harbor s market limits both its potential growth and is likely to deter most potential acquirers. Thus, market is a reason for a downward value adjustment in comparison to the urban most applicable group, which generally served better markets, but not the minority-owned group, which served similar large urban markets.

Size

The comparable banks take into account Harbor s size. As a result, size is not a reason for a value adjustment.

Asset Mix and Quality

Harbor s asset mix is good and contributes toward the Bank s profitability. Thus, since asset mix is factored into an earnings-determined value, a value adjustment is not necessary.

Asset quality is also good and is comparable to the asset quality of the comparable groups. Thus, asset quality is not a reason for a value adjustment.

Deposit Mix

Harbor s deposit mix is excellent, but these good deposits are a major part of the determination of profits. Thus, deposit mix is factored into an earnings-determined value and is not a reason for a value adjustment.

Management

Since there has not been any substantial change in management for many years, the impact of management on value is reflected in all of the above value-determining categories. Thus, management also is not a reason for a value adjustment.

Stock Liquidity

Harbor differs from the comparable banks in the illiquidity of its stock. The banks in the comparable groups, generally, do not trade extensively, but they are listed on either a national exchange or trade over-the-counter. Harbor is not listed on any exchange, and its stock trades very sporadically. Thus, stock liquidity is a reason for a value discount in relation to the comparable groups.

Unique Characteristics

The only unique characteristic of Harbor that is not addressed above is Harbor s minority-ownership. This characteristic is reflected in the minority-owned group, but not in the urban most applicable group. This minority-ownership impacts the value of the stock by decreasing the likelihood the bank will be sold, and thus its potential sale value. Investors do not consider minority banks likely to sell, and, thus, no acquisition premium is normally included in the value. The reason for this perception is that minority banks seldom are sold willingly because there is a stronger community commitment than for most non-minority urban banks and non-minority banks, which represent the bulk of possible buyers, have minimal interest in acquiring minority banks because of the poor economic dynamics of the urban markets they normally serve and the potential run-off of customers after a merger. A non-minority bank will buy a minority bank, but it will not pay a full premium. Harbor s status as a minority-owned bank is a reason for a value discount relative to the urban most applicable group.

Conclusion

When all of the elements of possible adjustment to the value of Harbor s value are considered, it merits discounts to the urban most applicable group based on market, stock liquidity and minority ownership. In relation to the minority-owned group which are all African-American owned the only discount would be for the illiquidity of its stock.

VALUATION

In establishing a fair price for shares of an unlisted stock, there are numerous methodologies that can be used including a) sale prices of similar companies, b) liquidation value, c) discounted dividends analysis under certain earnings and growth assumptions and d) comparisons with stock prices of similar companies that are publicly-traded. The latter is by far the most commonly-used method, and the first three are primarily utilized when there is either a likely sale of the company; a possibility of failing; and/or adequate comparisons do not exist. For Harbor there are applicable market comparables, and comparisons have been made to urban and minority-owned banks with similar size, performance and market characteristics.

Earnings derived Valuation

The best method of valuation when earnings are normal, or can be normalized, is earnings. As Harbor s earnings are normal and have been sustained for several years a valuation will be determined based on earnings.

The first two groups considered were the urban exchange group and the urban OTC group. While many of the banks in these two groups were eliminated to form a single group with more similarities to Harbor, it is helpful to consider their pricing multiples as each is a much larger group than the final two comparative groups. The urban exchange group had fourteen banks and a median price times earnings multiple of 22.7. The urban OTC group had eleven banks and had a median price times earnings multiple of 17.8.

When the new banks and high performers in the urban exchange group and the OTC group were eliminated there were seven banks remaining. These seven banks comprise the urban most applicable group and had financial conditions and performance quite similar to Harbor. The median price times earnings of this group was 15.5. That the price times earnings multiple fell is not surprising as new banks are often valued based on anticipated future performance and high performing banks may merit a higher multiple.

The final comparative group and the most relevant to Harbor is the minority-owned group. These four banks all are African-American owned and serve large urban areas like Harbor. In addition, they all have similarities in financial condition and performance. The median price times earnings for this group is 14.0.

Stock Transactions

The Bank had two known stock transactions so far in 2005. In April there were two trades in which 77 and 308 shares were exchanged for $25 per share. The total value of these two transactions was only $9,625. At this price based on current financial data, the Bank trades for 10.4 times fully-diluted earnings and 112% of book. These are too few shares traded on which to base a valuation and they are not considered in this valuation (see Table 14).

Discounted Dividends

Using the discounted dividends investment calculation and price times earnings of 12 and 14, Harbor s price per share varies from $24.54 to $33.72. The low price of $24.54 per share is under a 12% discount rate and 12 times earnings and the high price of $33.72 per share is under a 10% discount rate and 14 times earnings (see Table 15).

Application of earnings multiples

Using the earnings multiple from the urban most applicable group of 15.5 times earnings, a value of $27.4 million, or $35.86 per fully-diluted share is reached. Since the majority of banks in this group are located in better urban markets and thus have better growth opportunities a downward adjustment in value is necessary. Further adjustments take into account that these banks all have some liquidity in their stock which exceeds the few trades in Harbor s stock. Finally, an adjustment should be made to because the minority-ownership of Harbor limits the potential sale value of the Bank, and thus makes its stock less attractive.

It is our opinion that a discount of 20% to 30% would be appropriate to account for the poor market dynamics, illiquidity of stock and minority-ownership of Harbor. When these discounts are applied to a 15.5 times earnings multiple the value is 10.9 to 12.4 times earnings, $19.2 to $21.9 million, or $25.88 to $29.20 per fully-diluted share. The midpoint is $20.6 million, or $27.54 per fully-diluted share, which is 11.6 times earnings, or 125% of book.

In using the minority-owned group the price times earnings multiple is 14.0 and discounts would only be taken for the illiquidity of stock since the other minority-owned banks are all African American owned banks and are located in similar urban markets. At 14.0 times earnings, these minority-owned financial institutions suggest an unadjusted value of $24.8 million, or $32.63 per fully-diluted share.

It is our opinion that a discount of 5% to 15% would be appropriate to account for the illiquidity of Harbor s stock. When this discount is applied, the resulting value is 11.9 times earnings to 13.3 times earnings, $21.0 to $23.5 million; or $28.13 to $31.13 per fully-diluted share. The midpoint is $22.3 million or $29.63 per fully-diluted share, which is 12.6 times earnings, or 136% of book.

In our opinion, the best guide as to the value of Harbor s stock is the price times earnings multiples of other African-American banks having similar size and performance, and being located in similar urban markets. The value determined by the urban most applicable group which is slightly lower should also be considered, but only to determine that the value is to the lower half of the range determined by the minority-owned group. This range is $21.0 to $22.3 million, or $28.13 to $29.63 per fully diluted share. This is 128% to 136% of book value. Any price in this range would be a fair price at which to exchange stock (see Tables 16 and 17).

Table 1

Harbor Branch Locations

Address	Deposits June 30, 2005	Percent of Deposits	County
	(In thous.)		
25 West Fayette Street	$95,532	43.8 %	Baltimore City
1000 Lancaster Street	39,199	18.0	Baltimore City
8725 Liberty Road	31,079	14.3	Baltimore
6812 Riverdale Road	22,745	10.4	Prince George s
3420 Belair Road	15,894	7.3	Baltimore City
5000 Park Heights Avenue	13,456	6.2	Baltimore City
Total deposits	$217,905	100.0 %	

Source: SNL Financial, Charlottesville, Virginia.

Table 2

Harbor s Market Demographics*

	Population		2004			
Markets by Zip Code	2004*	Estimated Annual Gr. Rate 2000-04*	Median Household Income	Number of Business	Number of Empl.	2004 Percent African American
Baltimore City	625,867	(.9)%	$32,715	21,409	290,693	67.0%
21201 Main Office	13,976	(.2)%	$18,709	2,366	57,283	67.9%
21213 Erdman Ave.	36,645	(1.0)	30,000	565	4,748	90.1
21215 Pimlico Office	63,232	(.6)	31,298	1,855	22,917	83.2
Baltimore County	775,960	.7%	$56,135	27,704	301,934	22.3%
21133 Randallstown	28,616	1.3%	$62,352	806	6,266	72.0%
Prince George s County	836,416	1.0%	$61,518	24,636	295,184	64.2%
20737 Riverdale	20,636	1.0%	$50,564	456	3,944	50.7%

*2004 and growth rates estimated by ERSI.

Source: ERSI, Sourcebook America 2004 Edition, Vienna, Virginia.

Table 3

Deposit Share

Harbor s Primary Market*

	Deposits 2005	Market Share June 30, 2005	2004	2003	2002	2000
	(In millions)					
Large Banks						
Bank of America	$8,816	28.5%	26.8%	22.4%	20.9%	17.6%
M&T	3,865	12.5	12.2	14.6	17.0	19.6
Wachovia	2,332	7.5	7.1	7.1	6.5	8.6
SunTrust	759	2.4	2.6	3.0	3.2	3.1
BB&T	274	.9	1.0	.8	.9	.9
Subtotal	$16,046	51.8%	49.7%	47.9%	48.5%	49.8%
Leading Locals						
Mercantile	$3,546	11.4%	11.5%	12.8%	11.1%	9.6%
Provident	2,028	6.5	6.9	7.2	8.6	13.0
First Mariner	606	2.0	1.9	1.9	1.9	1.3
Susquehanna	556	1.8	1.9	1.9	1.8	1.9
K Capital	304	1.0	.9	.8	.7	.6
Carrollton	204	.7	.6	.7	.8	.9
Harbor	195	.6	.6	.6	.6	.6
Subtotal	$7,439	24.0%	24.3%	25.9%	25.5%	27.9%
Leading Thrifts						
Eastern	$524	1.7%	1.8%	1.9%	1.9%	1.8%
BCSB	471	1.5	1.6	1.6	1.6	1.3
Rosedale	376	1.2	1.4	1.4	1.3	1.2
Northwest	313	1.0	1.3	1.3	1.4	1.2
Bradford	264	.9	.9	1.0	1.0	1.0
Hopkins Savings	218	.7	.7	.7	.7	.5
Hamilton	203	.7	.7	.8	.8	.7
Subtotal	$2,369	7.7%	8.4%	8.7%	8.7%	7.7%
Other banks	$888	2.9%	2.7%	2.5%	2.4%	2.2%
Other thrifts	1,663	5.4	5.8	5.9	6.1	5.2
Credit Unions	2,559	8.2	9.1	9.1	8.8	7.2
Total	$30,964	100.0%	100.0%	100.0%	100.0%	100.0%

* Baltimore County and the City of Baltimore.

Source: SNL Financial, Charlottesville, Virginia.

Table 4

Harbor

Financial History

	Assets	Equity	Net Income	Percent of Assets Capital	Percent of Assets Net Income	Return on Avg. Equity
	(In millions)		(In thous.)			
2005*	$247	$16.4	$1,768	6.66%	.74%	10.94%
2004	235	16.2	1,462	6.90	.63	9.33
2003	220	15.3	1,785	6.96	.84	12.22
2002	210	14.1	1,077	6.73	.54	8.22
2001	187	12.2	730	6.56	.37	6.24
2000	185	10.2	565	5.55	.32	7.03
1999	178	7.5	1	4.20		.01
1998**	184	16.4	1,009	8.91	.70	6.21
1997	136	16.0	905	11.77	.69	5.99
1996	130	14.5	777	11.21	.67	5.90
1995	113	11.3	901	10.00	.84	8.14
1994	106	10.9	703	10.26	.79	8.92
1993	62	4.5	475	7.25	.78	11.18
1992	57	4.1	346	7.15	.67	8.99
1991	45	3.7	107	8.24	.25	2.95
1990	38	3.5	149	9.35	.40	

* September 30, 2005 or nine months annualized.
** Bank level data for 1998 and proceeding years.
Source: SNL Financial, Charlottesville, Virginia.

Table 5

Harbor

Balance Sheet Growth

	Loans	Securities	Deposits	Borrowings
	(In millions)			
2005*	$194	$26	$218	$10
2004	174	29	210	7
2003	151	38	196	7
2002	122	56	193	2
2001	107	52	172	2
2000	112	55	169	4
1999	103	50	166	4
1998	86	72	167	
1997	78	30	119	
1996	85	17	114	

* September 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 6

Harbor

Income and Expense

	Percent of Average Assets				
	Interest Income	**Interest Expense**	**Net Int. Income**	**Nonint. Income**	**Oper. Income**
2005*	6.05 %	1.46 %	4.59 %	.75 %	5.34 %
2004	5.45	.98	4.47	.65	5.12
2003	5.57	1.13	4.44	1.07	5.51
2002	5.88	1.72	4.16	1.01	5.17
2001	6.86	3.01	3.85	1.08	4.93
2000	7.81	3.54	4.27	1.05	5.32
1999	7.23	3.35	3.88	.80	4.68
Regional average***	5.50 %	1.59 %	3.91 %	.68 %	4.59 %

	Oper. Expense	**Net Oper. Expense**	**Contr. to Reserves**	**Other****	**Net Income**
2005*	3.98 %	1.36 %	.20 %		.74 %
2004	4.01	1.11	.16	.01 %	.63
2003	4.04	1.47	.35	.11	.84
2002	4.33	.84	.17	.11	.54
2001	4.30	.63	.20	.10	.37
2000	4.64	.68	.20		.32
1999	4.20	.48	.47		
Regional average***	2.79 %	1.80 %	.14 %		1.14 %

* Nine months ended September 30th, annualized.

** Gains (loss) on securities.

*** Commercial banks in the District of Columbia, Maryland, New Jersey and Virginia with assets between $200 and $500 million, noninterest income less than 2% of assets for the six months ended June 30, 2005 annualized or June 30, 2005 in this and the following tables.

Source: SNL Financial, Charlottesville, Virginia.

Table 7

Harbor

Loan and Deposit Mix

	Percent of Deposits					
			CDs			
	Nonint. Bearing	Other Trans.*	Consumer	Jumbo	Total	Deposits/ Assets
2005**	23%	48%	16%	13%	100%	88%
2004	23	49	16	12	100	89
2002	14	58	15	13	100	92
2000	11	55	17	17	100	92
Regional average	15%	42%	29%	14%	100%	85%

	Loans					
	Res. Mtge.	Comm. R.E.	Comm.	Consumer	Total	Loans/ Assets
2005**	16%	39%	40%	5%	100%	78%
2004	18	36	40	6	100	73
2002	32	31	26	11	100	58
2000	29	33	29	9	100	61
Regional average	26%	49%	14%	11%	100%	71%

* Includes other savings.
** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 8

Harbor

Capital and Asset Quality Comparison

	Percent of Assets			
	Capital	**Reserves**	**NPAs***	**Reserves/ Loans**
2005**	6.66 %	.79 %	.38 %	1.01 %
2004	6.90	.68	.34	.93
2003	6.96	.68	.33	.98
2002	6.73	.50	.58	.86
2001	6.56	.51	.41	.90
2000	5.55	.40	.17	.65
1999	4.20	.38	.71	.66
1998	8.91	.34	1.24	.74
1997	11.77	.48	2.00	.84
1996	11.21	.69	.43	1.04
Regional median	9.89 %	.78 %	.50 %	1.11 %

* Includes loans 90 days past due.
** September 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 9a

Urban Exchange Group*

Description

Full Name	**City, State**	**Assets**** (In mill.)
American Community Bancshares, Inc.	Charlotte, N.C.	$443
Annapolis Bancorp, Inc.	Annapolis, Md.	322
Bank of Wilmington Corporation	Wilmington, N.C.	312
Cardinal State Bank	Durham, N.C.	152
Carolina Bank Holdings, Inc.	Greensboro, N.C.	331
Cornerstone Bancorp, Inc.	Stamford, Ct.	221
Crescent Financial Corporation	Cary, N.C.	405
First National Bancshares, Inc.	Spartanburg, S.C.	303
Glen Burnie Bancorp	Glen Burnie, Md.	319
Greenville First Bancshares, Inc.	Greenville, S.C.	375
Jacksonville Bancorp, Inc.	Jacksonville, Fla.	262
Millennium Bankshares Corporation	Reston, Va.	428
Monarch Bank	Chesapeake, Va.	300
Valley Bancorp	Las Vegas, Nev.	373
Harbor	Baltimore, Md.	$247

* Non-minority urban banks on the east coast with assets between $150 and $500 million and returns on average assets over .50%.

** September 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 9b

Urban Exchange Group

Financial Performance*

		As a Percent of Assets or Avg. Assets			
	Assets	Equity	NPAs**	Net Income	Return on Avg. Equity
	(In mill.)				
American Community	$443	11.31%	.73%	.98%	9.64%
Annapolis	322	6.29	.96	.91	14.16
Bank of Wilmington	312	7.78	.25	.61	6.16
Cardinal State	152	12.46	.30	.56	4.24
Carolina Bank	331	6.78	1.77	.63	9.10
Cornerstone	221	11.40	.56	.69	6.39
Crescent Financial	405	7.20	.05	.79	10.19
First National	303	5.21	.09	1.03	18.34
Glen Burnie	319	8.35	.07	.95	11.30
Greenville First	375	8.12	.32	.91	10.73
Jacksonville	262	7.35	.19	.76	9.84
Millennium	428	11.28	.15	.61	5.02
Monarch	300	9.68	.00	.70	6.75
Valley	373	10.80	.04	1.63	13.18
Median	$320	8.24%	.22%	.78%	9.74%
Harbor***	$247	6.66%	.38%	.74%	10.94%

* September 30, 2005 or the twelve months ended September 30, 2005.

** Includes loans 90 days past due.

*** September 30, 2005 or the nine months ended September 30, 2005, annualized.

Source: SNL Financial, Charlottesville, Virginia.

Table 9c

Urban Exchange Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. to Reserves**	**Other**	**Net Income**
American Community	3.81%	1.94%	1.87%	.17%	(.14)%	.98%
Annapolis	3.71	2.15	1.56	.13		.91
Bank of Wilmington	3.46	2.04	1.42	.59		.61
Cardinal State	3.66	2.91	.75	.18		.56
Carolina Bank	3.12	1.76	1.36	.38		.63
Cornerstone**	4.47	3.07	1.40	.11	(.13)	.69
Crescent Financial	3.64	2.20	1.44	.25	.03	.79
First National	3.38	1.61	1.77	.23		1.03
Glen Burnie	3.88	2.81	1.07	(.02)	.06	.95
Greenville First	3.31	1.51	1.80	.33		.91
Jacksonville	3.62	2.24	1.38	.16	(.03)	.76
Millennium	3.15	2.10	1.05	.15		.61
Monarch	3.80	2.39	1.41	.33		.70
Valley	4.84	2.13	2.71	.24		1.63
Median	3.65%	2.14%	1.42%	.21%		.78%
Harbor**	4.59%	3.23%	1.36%	.20%		.74%

* Twelve months ended September 30, 2005.

** September 30, 2005 or the nine months ended September 30, 2005, annualized.

Source: SNL Financial, Charlottesville, Virginia.

Table 9d

Urban Exchange Group

Stock Performance

	Stock Price*	Price* Times Earnings		Price* Percent of Book		Avg. Shares Traded Daily**
American Community	$18.46	18.5	X***	167	%	4,755
Annapolis	9.28	14.3		186		2,136
Bank of Wilmington	10.55	24.5		149		4,613
Cardinal State	11.56	34.0		138		2,763
Carolina Bank	11.95	15.5	***	145		2,471
Cornerstone	36.31	32.1		194		2,758
Crescent Financial	15.01	23.1		214		5,014
First National	24.01	20.2		275		405
Glen Burnie	18.50	12.8		143		633
Greenville First	23.88	22.3		209		2,209
Jacksonville	32.40	32.4		288		1,308
Millennium	8.34	29.8		152		23,724
Monarch	15.66	28.0		170		2,320
Valley	34.96	20.7		245		16,029
Median		22.7	X	178	%	2,615

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelve months ended September 30, 2005, unless otherwise noted.

** One year.

*** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

Table 10a

Urban OTC Group*

Description

Full Name	**City, State**	**Assets****	
		(In mill.)	
BCB Bancorp, Inc.***	Bayonne, N.J.	$447	
Business Bank Corporation	Las Vegas, Nev.	410	
Capital Bancorp, Inc.	Nashville, Tenn.	445	
First South Bancorp, Inc.	Spartanburg, S.C.	312	
First Trust Bank***	Charlotte, N.C.	292	
Grandsouth Bancorporation***	Greenville, S.C.	236	
Greater Sacramento Bancorp	Sacramento, Calif.	256	
Hampton Roads Bankshares, Inc.	Chesapeake, Va.	393	
North State Bancorp***	Raleigh, N.C.	373	
Summit Bancshares, Inc.	Oakland, Calif.	166	****
VSB Bancorp, Inc.	Staten Island, N.Y.	228	
Harbor	Baltimore, Md.	$247	

* Non-minority urban banks on the east coast with assets between $150 and $500 million and returns on average assets above .50%.

** September 30, 2005 unless otherwise noted.

*** De novo bank.

**** June 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 10b

Urban OTC Group

Financial Performance*

		As a Percent of Assets or Avg. Assets			Return on Avg.
	Assets	Equity	NPAs**	Income	Equity
	(In mill.)				
BCB	$447	6.53%	.26%	1.18%	17.20%
Business Bank	410	8.04	.23	1.23	16.04
Capital	445	6.30	.19	.89	13.41
First South	312	9.49	.60	.92	10.10
First Trust	292	9.28	.03	1.16	14.18
Grandsouth	236	6.26	1.01	.98	18.69
Greater Sacramento	256	6.23	.16	.99	14.89
Hampton Roads	393	11.67	.56	1.40	11.66
North State	373	5.53	.00	.69	11.04
Summit***	166	11.21	.11	1.12	9.94
VSB	228	6.31	.42	1.18	19.26
Median	$312	6.53%	.23%	1.12%	14.18%
Harbor	$247	6.66%	.38%	.74%	10.94%

* September 30, 2005 or the twelve months ended September 30, 2005, unless otherwise noted.

** Includes loans 90 days past due.

*** June 30, 2005 or the twelve months ended June 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 10c

Urban OTC Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. To Reserves**	**Other**	**Net Income**
BCB	3.90 %	1.77 %	2.13 %	.26 %	.01 %	1.18 %
Business Bank	4.86	2.82	2.04	.10	(.05)	1.23
Capital	3.69	2.07	1.62	.46		.89
First South	3.93	1.68	2.25	.27	(.55)	.92
First Trust	3.96	1.93	2.03	.16		1.16
Grandsouth	3.93	1.93	2.00	.45	.01	.98
Greater Sacramento	4.08	2.44	1.64	.04	.03	.99
Hampton Roads	4.68	2.37	2.31	.17		1.40
North State	3.60	2.25	1.35	.26		.69
Summit**	5.00	2.86	2.14	.18	(.06)	1.12
VSB	4.25	2.12	2.13	(.03)	.05	1.18
Median	3.96 %	2.12 %	2.04 %	.18 %		1.12 %
Harbor***	4.59 %	3.23 %	1.36 %	.20 %		.74 %

* Twelve months ended September 30, 2005.
** Twelve months ended June 30, 2005.
*** September 30, 2005 or the nine months ended September 30, 2005, annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 10d

Urban OTC Group

Stock Performance

	Stock Price*	Price* Times Earnings	Price* Percent of Book	Avg. Shares Traded Daily**
BCB	$17.50	14.6X	223%	1,320
Business Bank	42.15	21.0	267	1,305
Capital	19.10	18.7	237	663
First South	32.75	15.7****	193	595
First Trust	19.00	18.5	209	1,358
Grandsouth	12.00	17.1	235	221
Greater Sacramento	28.95	18.4****	235	920
Hampton Roads	10.85	17.8	193	1,738
North State	21.50	30.7	296	469
Summit***	17.65	15.8	159	1,359
VSB	20.25	11.6	212	241
Median		17.8X	223%	920

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelvemonths ended September 30, 2005, unless otherwise noted.

** One year.

*** December 8, 2005 stock price and financial data as of June30, 2005 or the twelvemonths ended June 30, 2005.

**** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

Table 11a

Urban Most Applicable Group*

Description

Full Name	**City, State**	**Assets****	
		(In mill.)	
Annapolis Bancorp, Inc.	Annapolis, Md.	$322	
Capital Bancorp, Inc.	Nashville, Tenn.	445	
Carolina Bank Holdings, Inc.	Greensboro, N.C.	331	
Cornerstone Bancorp, Inc.	Stamford, Ct.	221	
Glen Burnie Bancorp	Glen Burnie, Md.	319	
Summit Bancshares, Inc.	Oakland, Calif.	166	***
VSB Bancorp, Inc.	Staten Island, N.Y.	228	
Harbor	Baltimore, Md.	$247	

* Non-minority urban banks with assets between $150 and $500 million and returns on average assets above .50% excluding banks established on or after 1998 and top performing banks with a return on average assets over 1.20%.

** September 30, 2005.

*** June 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 11b

Urban Most Applicable Group

Financial Performance*

		As a Percent of Assets or Avg. Assets			
	Assets	**Equity**	**NPAs****	**Net Income**	**Return on Avg. Equity**
	(In mill.)				
Annapolis	$322	6.29%	.96%	.91%	14.16%
Capital	445	6.30	.19	.89	13.41
Carolina Bank	331	6.78	1.77	.63	9.10
Cornerstone	221	11.40	.56	.69	6.39
Glen Burnie	319	8.35	.07	.95	11.30
Summit***	166	11.21	.11	1.12	9.94
VSB	228	6.31	.42	1.18	19.26
Median	$319	6.78%	.42%	.91%	11.30%
Harbor	$247	6.66%	.38%	.74%	10.94%

* September 30, 2005 or the twelve months ended September 30, 2005.

** Includes loans 90 days past due. Excludes new banks and high performing banks.

*** June 30, 2005 or the twelve months ended June 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 11c

Urban-Most Applicable Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. to Reserves**	**Other**	**Net Income**
Annapolis	3.71%	2.15%	1.56%	.13%		.91%
Capital	3.69	2.07	1.62	.46		.89
Carolina Bank	3.12	1.76	1.36	.38		.63
Cornerstone	4.47	3.07	1.40	.11	(.13)%	.69
Glen Burnie	3.88	2.81	1.07	(.02)	.06	.95
Summit**	5.00	2.86	2.14	.18	(.06)	1.12
VSB	4.25	2.12	2.13	(.03)	.05	1.18
Median	3.88%	2.15%	1.56%	.13%		.91%
Harbor***	4.59%	3.23%	1.36%	.20%		.74%

* Twelve months ended September 30, 2005.
** Twelve months ended June 30, 2005.
*** September 30, 2005 or the nine months ended September 30, 2005, annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 11d

Urban-Most Applicable Group

Stock Performance

	Stock Price*	Price* Times Earnings		Price* Percent of Book		Avg. Shares Traded Daily**
Annapolis	$9.28	14.3	X	186	%	2,136
Capital	19.10	18.7		237		663
Carolina Bank	11.95	15.5	****	145		2,471
Cornerstone	36.31	32.1		194		2,758
Glen Burnie	18.50	12.8		143		633
Summit***	17.65	15.8		159		1,359
VSB	20.25	11.6		212		241
Median		15.5	X	186	%	1,359

* December 8 2005 stock price and financial data as of September 30, 2005 or the twelvemonths ended September 30, 2005, unless otherwise noted.

** One year.

*** December 8, 2005 stock price and financial data as of June 30, 2005 or the twelvemonths ended June 30, 2005.

**** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

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Table 12

Publicly-Traded Minority-Owned Banks and Thrifts

Description

Full Name	City, State	Assets*	
		(In mill.)	
Banks - over $900 million			
Cathay General Bancorp, Inc.	Los Angeles, Calif.	$6,157	
East West Bancorp, Inc.	San Marino, Calif.	7,938	
International Bancshares Corporation	Laredo, Texas	10,310	
MetroCorp Bancshares, Inc.**	Houston, Texas	935	
Preferred Bank	Los Angeles, Calif.	1,097	
Banks - under $900 million			
Abigail Adams National Bancorp, Inc.	Washington, D.C.	$333	
Albina Community Bancorp	Portland, Org.	120	
Canyon National Bank	Palm Springs, Calif.	232	
Citizens Bancshares Corporation**	Atlanta, Ga.	324	
IBW Financial Corporation**	Washington, D.C.	339	***
M&F Bancorp, Inc.**	Durham, N.C.	246	
Pan American Bancorp	Los Angeles, Calif.	42	
Pan American Bancorp	Miami, Fla.	243	
Saehan Bancorp	Los Angeles, Calif.	494	
Thrifts			
Carver Bancorp, Inc.**	New York, N.Y.	$648	
Independence Federal Savings Bank**	Washington, D.C.	160	
Mutual Community Savings Bank, Inc.**	Durham, N.C.	91	
Harbor**	Baltimore, Md.	$247	

* September 30, 2005.
** African-American owned banks.
*** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 13a

Minority-Owned Group*

Description

Full Name	**City, State**	**Assets****	
		(In mill.)	
Carver***	New York, N.Y.	$648	
Citizens***	Atlanta, Ga.	324	
IBW***	Washington, D.C.	339	****
PanAmerican	Miami, Fla.	243	
Median		$332	
Harbor***	Baltimore, Md.	$247	

* Minority owned with assets under $900 million.
** September 30, 2005.
*** African-American owned banks.
**** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 13b

Minority-Owned Group

Financial Performance*

	Assets	Equity	NPAs**	Net Income	Return on Avg. Equity
		As a Percent of Assets or Avg. Assets			
	(In mill.)				
Comparable					
Carver	$648	7.33 %	.42 %	.45 %	5.93 %
Citizens	324	8.29	1.23	.69	8.66
IBW***	339	7.45	.72	.48	6.31
PanAmerican	244	17.59	.02	.99	8.16
Median	$332	7.87 %	.57 %	.59 %	7.24 %
Harbor****	$247	6.66 %	.38 %	.74 %	10.94 %
Non-comparable					
Abigail Adams	$334	8.39 %	.21 %	1.36 %	**13.96 %**
Albina Community	120	5.69	1.92	.30	**3.71**
Canyon National	232	7.93	.10	1.55	**20.86**
Independence	160	10.14	.34	.16	**1.59**
M&F	246	8.26	**2.08**	.25	**2.86**
Mutual Community	**91**	8.11	1.22	.01	**.09**
Pan American	**42**	13.67		.18	**1.29**
Saehan	494	8.55	.16	1.52	**16.02**

NOTE: Bolded numbers are reason for exclusion.

* September 30, 2005 or the twelve months ended September 30, 2005.
** Includes loans 90 days past due.
*** June 30, 2005 or the twelve months ended June 30, 2005.
**** September 30, 2005 or the nine months ended September 30, 2005 annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 13c

Minority-Owned Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. To Reserves**	**Other**	**Net Income**
Carver	3.05 %	2.29 %	.76 %		(.07) %	.45 %
Citizens	4.48	3.44	1.04	.09 %	(.11)	.69
IBW**	4.53	3.87	.66	.05	.12	.48
PanAmerican	4.65	3.16	1.49	.50		.99
Median	4.51 %	3.30 %	.90 %	.07 %	(.03) %	.59 %
Harbor***	4.59 %	3.23 %	1.36 %	.20 %		.74 %

* Twelve months ended September 30, 2005.

** Twelve months ended June 30, 2005.

*** September 30, 2005 or the nine months ended September 30, 2005, annualized.

Source: SNL Financial, Charlottesville, Virginia.

Table 13d

Minority-Owned Group

Stock Performance

	Stock Price*	Price* Times Earnings		Price* Percent of Book		Avg. Shares Traded Daily***
Carver	$15.10	14.0	X	80	%	2,486
Citizens	10.50	9.8		82		1,186
IBW**	34.00	14.0		90		133
PanAmerican	4.21	22.2		141		8,162
Median		14.0	X	86	%	1,836

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelve months ended September 30, 2005.

** December 8, 2005 stock price and financial data as of June 30, 2005 or the twelve months ended June 30,2005.

*** One Year.

**** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

Table 14

Stock Trades in 2005

	Shares	Price
April 19	77	$25.00
April 21	308	25.00

Source: Internal report.

Table 15

Discounted Dividends Applied to Harbor*

	Discount Rate		
	10%	11%	12%
	Value (in millions)		
12 times earnings***	$21.6	$19.0	$16.8
14 times earnings***	23.1	20.3	17.9
	Per Share**		
12 times earnings***	$31.46	$27.71	$24.54
14 times earnings***	33.72	29.58	26.09
	Times Earnings		
12 times earnings***	12.2X	10.7X	9.5X
14 times earnings***	13.1	11.5	10.1
	Price-to-Book****		
12 times earnings***	131%	116%	102%
14 times earnings***	141	123	109

* Assumes 6% earnings growth, capital in excess of 6.50% dividended out and a tax rate of 36%.
** Shares outstanding of 685,579.
*** Earnings of $1,768,000.
**** Equity of $16,435,000.

Table 16

Summary of Valuation Multiples*

Comparable groups	Price: Times Earnings	Price: Percent of Book	Number in Group
Urban exchange group	22.7 X	178 %	14
Urban OTC group	17.8	223	11
Urban most applicable	15.5 X	186 %	7
Minority-owned group	14.0	86	4
Stock trades	10.4 X	112 %	
Discounted Dividends**	10.7 X	116 %	

* December 8, 2005 stock price and financial data for the year ended September 30, 2005 or September 30, 2005 or most recent available.

** Based on a 11% discount rate and a terminal value of 12 times earnings.

Table 17

Pricing Applied to Harbor

Based on urban most applicable group		**Discount All***		
		20%	**25%**	**30%**
P/E**	15.5 X	12.4 X	11.6 X	10.9 X
Value (in mill.)	$27.4	$21.9	$20.6	$19.2
Per share***	$39.97	$31.98	$29.98	$27.98
Per Share Diluted***	$35.86	$29.20	**$27.54**	$25.88
Price-to-book****	167 %	133 %	125 %	117 %

Based on minority-owned group		**Discount for illiquidity**		
		5%	**10%**	**15%**
P/E**	14.0 X	13.3 X	12.6 X	11.9 X
Value (in mill.)	$24.8	$23.5	$22.3	$21.0
Per share***	$36.10	$34.30	$32.49	$30.69
Per Share Diluted***	$32.63	$31.13	**$29.63**	$28.13
Price-to-book****	151 %	143 %	136 %	128 %

* Discount for poor market dynamics, illiquidity of stock and minority-ownership.

** Earnings of $1,768,000.

*** Shares outstanding of 685,579; options outstanding of 132,741 with a weighted strike price of $16.27.

**** Equity of $16,435,000.

HARBOR BANKSHARES CORPORATION

Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

HARBOR BANKSHARES CORPORATION

Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

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HARBOR BANKSHARES CORPORATION

Baltimore, Maryland

FAIRNESS OPINION

As of December 8, 2005

Set forth herein is Danielson Associates Inc. s (Danielson Associates) independent appraisal of the fair market value of the common stock of Harbor Bankshares Corporation (Harbor or the Bank) of Baltimore, Maryland as of December 8, 2005. Market value is defined as the price at which the common stock would change hands between a willing seller and a willing buyer, each having reasonable knowledge of relevant facts and assuming a significant amount of stock changing hands daily to assure a true reflection of market forces.

This fairness opinion is provided in connection with a proposed going private transaction, in the form of a merger in which Harbor common stock owned by shareholders who own 100 or fewer shares would be exchanged for cash. Record holders of more than 100 shares of Harbor common stock would not receive cash for their shares in the merger and would remain Harbor shareholders. Harbor would be the surviving company in the merger.

This fairness opinion is based on data supplied by Harbor to Danielson Associates and its regulators, but relies on some public information, all of which is believed to be reliable, but the accuracy or completeness of such information cannot be guaranteed. In particular, this fairness opinion assumes that there are no significant loan quality problems beyond what has been stated in Harbor s quarterly reports to the Federal Deposit Insurance Corporation (FDIC).

In determining the fair value of the common stock of Harbor, primary emphasis has been given to the stock prices of publicly-traded banks that have comparable financial, market and structural characteristics, and the relationship of these prices to earnings.

Based on these comparisons, an analysis of Harbor s past performance and future potential and by applying discounts for market, stock liquidity and its minority ownership, it has been established that the fair value of its common stock as of December 8, 2005 is between $28.13 and $29.63 per share with the midpoint being $28.88 per share. Any price in this range would be fair to current shareholders, including shareholders who would be cashed out in the merger and shareholders who would not be cashed out in the merger.

Respectfully submitted,

David G. Danielson
President
Danielson Associates Inc.

DESCRIPTION

Harbor Bankshares Corporation (Harbor or the Bank) was formed in 1992 and is based in Baltimore, Maryland. Its wholly owned subsidiary, Harbor Bank of Maryland (Harbor or also the Bank) is regulated by the Federal Deposit Insurance Corporation. The holding company is regulated by the Federal Reserve.

The Bank was formed in 1982 and currently has six full-service offices, of which four are in the City of Baltimore. The other two branches are in Baltimore and Prince George s counties. Additionally, the Bank plans to open a branch in the University of Maryland s biotechnology park which would bring its total branch network up to seven. Its services include checking, savings and time deposits; home and commercial mortgages; and commercial and consumer loans. The lending emphasis is on commercial real estate and commercial loans. The Bank is also a member of a local and national ATM network

Market

The markets served by the Bank s six offices typically have a majority African-American population. The Baltimore City branches are in areas with negative population growth rates and are median household income of less than $33,000. The branches in Baltimore and Prince George s counties have good population growth rates and median household income of $56,000 and $62,000, respectively. Currently, the Bank does the majority of its business in the City of Baltimore with 75% of the deposits located within its four branches (see Tables 1 and 2).

Harbor is a relatively small factor in its primary market of Baltimore City and Baltimore County, but it has managed to keep its share of deposits. On June 30, 2005, it had deposits of $195 million, or .6% of the area s total. It ranked nineteenth in overall deposit size, and twelfth when compared to locally-based institutions (see Table 3).

Financial Performance

Since its inception, Harbor has been a slow growing bank. This, though, is still considered good growth as its primary market has a declining population base and comparatively low income levels. In 1990, its eighth year of operations, the Bank had assets of $38 million and grew these assets to $62 million by the end of 1993. In 1994, the Bank purchased 2 branches from the Resolution Trust Corporation, which moved assets above $100 million for the first time. From he beginning of 1998 through the end of 2001 a four year period Harbor s growth stalled as assets hovered around $184 million. Growth picked up again in 2002 when Harbor purchased a branch in Randallstown from Carrollton Bancorp. With the purchase of this branch, the Bank s assets in 2002 surpassed $200 million and as of September 30, 2005 it had assets of $247 million (see Table 4).

Harbor has earned in excess of $1 million annually since 2002, and annualized earnings for the nine months ended September 30, 2005 are just under $1.8 million. These earnings produced returns on equity in the 8% to 12% range during this period and while these are good results, they were helped by capital that was less than 7% of assets. Returns on assets were not as good, ranging from a low of .54% to a high of .84% during this same period.

On the asset side of the balance sheet the Bank has shown some good underlying momentum. The Bank has consistently added about $20 million in loans per year since 2001 and as of September 30, 2005, the Bank had loans outstanding of $194 million. This growth in loans has allowed Harbor to reduce its securities position from $52 million at the end of 2001, to $26 million as of September 30, 2005 a reduction of 50% (see Table 5).

The growth of the loan portfolio has had a positive impact on Harbor s margins. In a period when margin decline is an industry-wide problem, the Bank generally went against industry trends. The net result was net interest income rose from 3.85% of average assets in 2001 to better then 4.40% of average assets in 2003 and 2004. In the first nine months of 2005, net interest income was 4.59% of average assets, well above the regional average (see Table 6).

Harbor has not translated these above-average margins into above-average earnings because of its high overhead. Its operating expense of 3.98% of average assets through the first nine months of 2005 was more than one percentage point higher than the regional average of 2.79% (see Table 6).

The reasons for the good margins can be readily seen in the Bank s deposit mix. As of June 30, 2005, about 23% of its deposits were non-interest-bearing and 48% were savings and other transactions accounts. Only 29% were CDs, which normally are the most expensive type of deposits (see Table 7).

As a result of the loan growth discussed earlier, Harbor, as of June 30, 2005, had 78% of its assets committed to loans, compared to only 61% in 2000. More then half of these loans were secured by real estate 16% were residential mortgages and 39% by commercial real estate. The other large loan type was commercial loans not secured by real estate, which comprised 40% of the loan portfolio (see Table 7).

The Bank s asset quality continues be adequate with non-performing assets (NPAs) at .38% of assets as of September 30, 2005. The only concern would be the low level of reserves as a percentage of loans. As of September, 30, 2005 reserves as a percentage of loans was only 1.01%, which is low considering the large amount of non-secured commercial loans and an equity-to-assets ratio of only 6.66%. The median reserve to loans of its regional peers was 1.11% (see Table 8).

What do all these numbers say about Harbor? They describe a good, small bank that has decent earnings and grown steadily over the years, both internally and through branch acquisitions, but that has not maximized its earnings potential. In order to do this it either has to reduce overhead or grow into the existing overhead. The latter may require additional capital.

COMPARISONS WITH OTHER

PUBLICLY-TRADED COMMERCIAL BANKS

Overview

In determining a fair price for the outstanding shares of Harbor s common stock, the Bank has been compared with four groups of banks that trade publicly or over-the counter. The banks in these groups are either small urban banks or minority-owned banks. This analysis is complicated by the fact that very few small urban banks or banks that are minority-owned have a stock that trades. However, the banks in these four groups are similar to Harbor and provide the best measurement of Harbor s stock value.

The initial comparisons are to three groups of non-minority banks in urban areas, but the primary comparison on which Harbor s valuation is based is to a group comprised of other minority-owned banks. In the first three groups, the term urban has no solid definition but simply means a metropolitan area like Jacksonville, Florida or Charlotte, North Carolina, or a smaller city like Annapolis, Maryland.

- Urban exchange group Comprised of fourteen commercial banks based in urban areas along the east coast with assets between $150 and $500 million, returns on average assets above .50% and trade on a national exchange. The stocks of these banks, with three exceptions trade, on average more than 2,000 shares each day (see Table 9a).
- Urban OTC group - Consists of eleven commercial banks with the same restrictions as the urban exchange group but trade instead on the over-the-counter bulletin board market. The stocks of most of these banks are less liquid than the urban exchange group and trade on average a little over 900 shares each day (see Table 10a).
- Urban most applicable group Since these first two groups contained several newly-formed banks and banks with much better performance than Harbor, a third group was created from the banks in the urban exchange group and the urban OTC group which eliminated those less comparable banks. The remaining seven banks are the banks most applicable to Harbor based on location, performance and history (the urban most applicable group) (see Table 11a).

Minority-owned group   Comprised of the seventeen minority-owned banks and thrifts that are publicly-traded. There are several different minorities represented   African-American, Hispanic, Asian and women. This group was condensed further as those banks with assets over $900 million or other attributes that would make them incomparable to Harbor were excluded (see Table 12 and 13a).

The first two groups of   urban   comparables, and the third group which is a mix of the first two, provides a good base from which to view the pricing of a non-minority-owned bank located in a city. As will be discussed later, minority-owned banks tend to serve larger more densely populated   urban   areas and typically have a lower valuation.

Urban Comparables

The urban exchange group s financial performance was comparable to Harbor. The urban exchange group s median returns on average assets and equity of .78% and 9.74% were similar to Harbor s .74% and 10.94%, respectively. Additionally, NPAs as a percent of assets were .38% for Harbor which was higher, but not much higher, than the .22% for the comparable group. The urban exchange group had equity-to-assets of 8.24% while Harbor s was 6.66% (see Table 9b).

Harbor s net interest income of 4.59% of average assets in the nine months ending September 30, 2005 was much higher than the urban exchange group median of 3.65%, but this was more than offset by net operating expense that was about one and a half times the comparative group s median (see Table 9c).

The urban exchange group s stock price multiples were diverse. The price times earnings multiples for the fourteen banks, ranged from 12.8 to 34.0 times earnings, with a median of 22.7 times earnings. The price-to-book ratios also had a wide range with a low of 143%, a high of 288% and the median was 178% (see Table 9d).

The urban OTC group performed much better than Harbor with median returns on average assets and equity of 1.12% and 14.18%, respectively, compared to .74% and 10.94%, respectively, for Harbor. Equity-to-assets was similar with the urban OTC group having a median of 6.53% to Harbor s 6.66%. Once again the NPAs of the comparable group were lower with the urban OTC group but at .23% of assets versus .38% of assets for Harbor the difference was negligible.

In comparing income and expense ratios, Harbor outperformed the OTC group in terms of net interest income but gave away its advantage with higher net operating expense. Harbor had net interest income to average assets of 4.59% for the first nine months ended September 30, 2005 versus a median of 3.96% for the urban OTC group. Net operating expense was the opposite with Harbor having a much higher net operating expense to average assets of 3.23% compared to 2.12% for the comparable group. As a result Harbor s net operating as a percent of assets was lower than that of the comparable group s median 1.36% to 2.04% (see Tables 10b and 10c).

The pricing ratios for the urban OTC group were just as wide as the urban exchange group. Price-to-earnings multiples ranged from 11.6 to 30.7, with a median of 17.8. Price-to-book multiples ranged from 159% to 296% of book with a median of 223% (see Table 10d).

Using the pricing multiples of the urban exchange group and the urban OTC group, the pricing multiples applied to Harbor would be in the range of 18 to 23 times earnings and 170% to 230% of book. These ratios, though, are high because the groups contain several newly formed banks and a few banks with far superior performance that are valued at high multiples. Thus, since Harbor is not a new bank or a high performing bank, a third group was formed the urban most applicable group using banks from the first two groups but eliminating new or high performing banks. This newly formed group is comprised of seven banks.

The urban most applicable group s seven banks had median returns on average assets and equity of .91% and 11.30%, respectively. While this was higher than Harbor s .74% and 10.94%, respectively, both are in the range of moderate performing banks (see Tables 11b and 11c).

The urban most applicable group had pricing multiples based on earnings much tighter than the other two groups if one outlier is ignored. Price times earnings multiples ranged from 11.6 to 32.1 with five of the seven between 12.8 and 18.7. Price-to-book ranged from 143% to 237% with five of the seven between 145% and 212%. The median price times earnings was 15.5 and the median price-to-book was 186% (see Table 11d).

Minority-Owned Comparables

Since Harbor is a minority-owned institution, the trading value of other minority-owned institutions provides a good indication as to the value of its stock. There are seventeen publicly traded minority-owned institutions as defined by the Federal Reserve Bank. These banks represent African-American, Hispanic, Asian and women minorities. Some of these banks are comparable to Harbor but others because of their size, performance or minority orientation are not comparable and have been excluded. The remaining four minority-owned banks are most comparable to Harbor and provide the best basis on which to value its stock (see Table 12 and 13a).

The minority-owned institutions that were non-comparable were excluded based on size, performance or minority orientation. The five banks with assets over $900 million were so much larger than Harbor that they were not comparable. In terms of performance there were three banks whose performance was too far above Harbor s to be comparable and five banks whose performance was too far below Harbor s to be comparable. The three top performers all had returns on equity near 14% or more and the five poor performing banks all had returns on equity below 4%. In addition two of these poor performers were too small to be comparable with assets under $100 million and a third had high NPAs which might add another reason that it would be incomparable. One of the top performers Abigail Adams has performance that could be considered comparable but it was also eliminated based on being a women s owned bank, rather than an African-American owned bank, and it does not market itself as a minority-owned institution (see Table 13a and 13b).

Financial Performance Comparisons*

	Equity/ Assets	NPAs/ Assets	Return on Average Assets	Return on Average Equity
Comparable groups				
Urban exchange group	8.24 %	.22 %	.78 %	9.74 %
Urban OTC group	6.53	.23	1.12	14.18
Urban most applicable group	6.78 %	.42 %	.91 %	11.30 %
Minority-owned group	7.87	.57	.59	7.24
Harbor**	6.66 %	.38 %	.74 %	10.94 %

* For the twelve months ended September 30, 2005 or September 30, 2005, or most recent available.

** Nine months ended September 30, 2005 or September 30, 2005.

Source: SNL Financial, Charlottesville, Virginia and internal reports.

The remaining four minority-owned institutions (the minority-owned group) were all African-American owned, three of which were banks and the other a thrift. The largest in the group was the New York City based thrift Carver Bancorp, Inc. (Carver) with assets of $648 million and the smallest the Miami, Florida based PanAmerican Bancorp (PanAmerican) with assets of $244 million The other two banks were the Atlanta, Georgia based Citizens Bancshares Corporation (Citizens) and the Washington, D.C. based IBW Financial Corporation (IBW). Harbor with assets of $247 million was nearly identical in assets to PanAmerican.

Equity as a percent of assets was similar for three of the banks, but the fourth was substantially higher. The three with similar capital-to-asset ratios Carver, Citizens and IBW all had ratios between 7.33% and 8.29%. Harbor had capital-to-assets of 6.66%. The fourth bank PanAmerican had capital-to-assets of 17.59% but it just raised about $15 million in new equity in the third quarter of 2005.

In terms of performance the four banks in the minority-owned group had performance comparable but below that of Harbor. Returns on average equity ranged from 5.93% to 8.66% with a median of 7.24%. Harbor s return on average equity was 10.94% but it was aided by its low capital ratio. Returns on average assets were closer with the four banks posting returns of .45%, .48%, .69% and .99%. Harbor had a return on average assets of .74%, above all but one of the minority owned group.

In terms on NPAs none of the four banks in the minority-owned group has significant NPAs. The bank with the lowest NPAs-to-assets was PanAmerican at .02% and the highest was Citizens with 1.23%. Harbor had NPAs-to-assets of .38%.

Harbor s net interest income and net operating expense as a percent of average assets was similar to that of three of the four banks in the minority-owned group. Harbor s net interest income to average assets of 4.59% was inside the range of 4.48% to 4.65% posted by Citizens, IBW and PanAmerican. In terms on net operating expense to average assets Harbor s 3.23% was again inside the range of the same three banks 3.16% to 3.87%. The fourth bank Carver posted net interest income and net operating income as a percent of average assets of 3.05% and 2.29%, respectively.

The pricing of three of the four banks in the minority-owned group were similar. Citizens, Carver and IBW all had price times earnings multiples in a fairly tight range with multiples of 9.8, 14.0 and 14.0 times earnings, respectively. These same banks had price-to-book ratios of 82%, 80% and 90%, respectively. The fourth bank, PanAmerican had a price times earnings multiple of 22.2 and price-to-book of 141%. The pricing of PanAmerican can be discounted as it recently raised a substantial amount of new capital after years of losses and its stock trades for less than $5.00.

Stock Pricing Comparisons*

	Price		**Avg. Shares**	
	Times Earnings	**Percent of Book**	**Traded Daily****	**No. in Group**
Comparable groups				
Urban exchange group	22.7 X	178 %	2,615	14
Urban OTC group	17.8	223	920	11
Urban most applicable group	15.5 X	186 %	1,359	7
Minority-owned group	14.0	86	1,836	4

* December 8, 2005 stock price and financial data for the year ended September 30, 2005 or September 30, 2005 or most recent available.

** For the past year.

Source: SNL Financial, Charlottesville, Virginia and internal reports.

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MARKET VALUE ADJUSTMENTS

In order to determine a fair price for shares of Harbor s common stock, it is necessary to consider how it differs from the urban most applicable group and the minority-owned group and make the adjustments reflecting the differences, if needed. These adjustments should consider such items as profitability, capital, growth momentum, market, deposit mix, asset mix and quality, management, liquidity of stock as well as any unique circumstances. Background information on these items appears in the preceding section or in the tables at the end of the report.

Profitability

Earnings, when they are normal, are the primary determinant of the value of a stock, but relationships based on earnings have to consider their sustainability. Harbor s earnings have been consistent over the last three years, and its overall financial condition make it likely that it can, and will, sustain similar earnings and earnings growth going forward. Thus, in an earnings-determined valuation, there is no cause for an adjustment based on profitability.

Capital

Harbor s capital-to-asset ratio is low but so were several banks in the comparable groups. The current amount of capital is sufficient to continue to grow at historical rates and should not have an impact on restraining earnings growth. Thus, there is no cause for a value adjustment based on capital.

In the beginning of 2006, the Bank s going private transaction will cause the holding company to purchase, approximately, 14,000 shares of Harbor common stock for an amount less than $420,000. This will reduce Harbor s capital ratios, but not enough to cause a value adjustment.

Growth

Harbor s growth has been adequate. Some of this growth was fueled by branch acquisitions, but this has helped Harbor hold onto its current local market share. Thus, growth is not a reason for a value adjustment.

Market

The Bank has continued to look for branches in growing areas within its market, but the majority of its branches and deposits are in Baltimore City, a declining market. This is particularly important in a valuation since part of the value of a bank is its growth opportunities and the likelihood that it will be acquired. Harbor s market limits both its potential growth and is likely to deter most potential acquirersThus, market is a reason for a downward value adjustment in comparison to the urban most applicable group, which generally served better markets, but not the minority-owned group, which served similar large urban markets.

Size

The comparable banks take into account Harbor s size. As a result, size is not a reason for a value adjustment.

Asset Mix and Quality

Harbor s asset mix is good and contributes toward the Bank s profitability. Thus, since asset mix is factored into an earnings-determined value, a value adjustment is not necessary.

Asset quality is also good and is comparable to the asset quality of the comparable groups. Thus, asset quality is not a reason for a value adjustment.

Deposit Mix

Harbor s deposit mix is excellent, but these good deposits are a major part of the determination of profits. Thus, deposit mix is factored into an earnings-determined value and is not a reason for a value adjustment.

Management

Since there has not been any substantial change in management for many years, the impact of management on value is reflected in all of the above value-determining categories. Thus, management also is not a reason for a value adjustment.

Stock Liquidity

Harbor differs from the comparable banks in the illiquidity of its stock. The banks in the comparable groups, generally, do not trade extensively, but they are listed on either a national exchange or trade over-the-counter. Harbor is not listed on any exchange, and its stock trades very sporadically. Thus, stock liquidity is a reason for a value discount in relation to the comparable groups.

Unique Characteristics

The only unique characteristic of Harbor that is not addressed above is Harbor s minority-ownership. This characteristic is reflected in the minority-owned group, but not in the urban most applicable group. This minority-ownership impacts the value of the stock by decreasing the likelihood the bank will be sold, and thus its potential sale value. Investors do not consider minority banks likely to sell, and, thus, no acquisition premium is normally included in the value. The reason for this perception is that minority banks seldom are sold willingly because there is a stronger community commitment than for most non-minority urban banks and non-minority banks, which represent the bulk of possible buyers, have minimal interest in acquiring minority banks because of the poor economic dynamics of the urban markets they normally serve and the potential run-off of customers after a merger. A non-minority bank will buy a minority bank, but it will not pay a full premium. Harbor s status as a minority-owned bank is a reason for a value discount relative to the urban most applicable group.

Conclusion

When all of the elements of possible adjustment to the value of Harbor s value are considered, it merits discounts to the urban most applicable group based on market, stock liquidity and minority ownership. In relation to the minority-owned group which are all African-American owned the only discount would be for the illiquidity of its stock.

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VALUATION

In establishing a fair price for shares of an unlisted stock, there are numerous methodologies that can be used including a) sale prices of similar companies, b) liquidation value, c) discounted dividends analysis under certain earnings and growth assumptions and d) comparisons with stock prices of similar companies that are publicly-traded. The latter is by far the most commonly-used method and is the best method by which to value Harbor s stock. The first three methods are primarily utilized when there is either a likely sale of the company, a possibility of failing, and/or adequate comparisons do not exist. These methods have not been used because Harbor is not considering a sale, it is not in danger of failing and there are applicable market comparables on which to base a valuation of its stock. Thus, Harbor s value has been established by comparisons to urban and minority-owned banks with similar size, performance and market characteristics after which certain discounts were applied.

Earnings derived Valuation

There are several methods by which bank stocks are normally valued. Price times earnings, price-to-book and price-to-assets. The best method of valuation when earnings are normal , or can be normalized , is earnings. Price-to-book is used when price times earnings cannot be used because earnings are not normal or cannot easily be normalized . Price-to-assets is used when price-to book does not provide a meaningful valuation. Thus, as Harbor s earnings are normal and have been sustained for several years the best method of a valuation is one determined based on earnings.

The first two groups considered were the urban exchange group and the urban OTC group. While many of the banks in these two groups were eliminated to form a single group with more similarities to Harbor, it is helpful to consider their pricing multiples as each is a much larger group than the final two comparative groups. The urban exchange group had fourteen banks and a median price times earnings multiple of 22.7. The urban OTC group had eleven banks and had a median price times earnings multiple of 17.8.

When the new banks and high performers in the urban exchange group and the OTC group were eliminated there were seven banks remaining. These seven banks comprise the urban most applicable group and had financial conditions and performance quite similar to Harbor. The median price times earnings of this group was 15.5. That the price times earnings multiple fell is not surprising as new banks are often valued based on anticipated future performance and high performing banks may merit a higher multiple.

The final comparative group and the most relevant to Harbor is the minority-owned group. These four banks all are African-American owned and serve large urban areas like Harbor. In addition, they all have similarities in financial condition and performance. The median price times earnings for this group is 14.0.

The price times earnings multiples for the four comparables groups were 22.7X, 17.8X, 15.5X and 14.0X. The latter two multiples for the urban most applicable and the minority-owned group are the most comparable.

Stock Transactions

The Bank had two known stock transactions so far in 2005. In April there were two trades in which 77 and 308 shares were exchanged for $25 per share. The total value of these two transactions was only $9,625. At this price based on current financial data, the Bank trades for 10.4 times fully-diluted earnings and 112% of book. These are too few shares traded on which to base a valuation and they are not considered in this valuation (see Table 14).

Discounted Dividends

Using the discounted dividends investment calculation and price times earnings of 12 and 14, Harbor s price per share varies from $24.54 to $33.72. The low price of $24.54 per share is under a 12% discount rate and 12 times earnings and the high price of $33.72 per share is under a 10% discount rate and 14 times earnings (see Table 15).

Application of earnings multiples

Using the earnings multiple from the urban most applicable group of 15.5 times earnings, a value of $27.4 million, or $35.86 per fully-diluted share is reached. Since the majority of banks in this group are located in better urban markets and thus have better growth opportunities a downward adjustment in value is necessary. Further adjustments take into account that these banks all have some

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liquidity in their stock which exceeds the few trades in Harbor s stock. Finally, an adjustment should be made because the minority-ownership of Harbor limits the potential sale value of the Bank, and thus makes its stock less attractive.

It is our opinion that a discount of 20% to 30% would be appropriate to account for the poor market dynamics, illiquidity of stock and minority-ownership of Harbor. When these discounts are applied to a 15.5 times earnings multiple the value is 10.9 to 12.4 times earnings, $19.2 to $21.9 million, or $25.88 to $29.20 per fully-diluted share. The midpoint is $20.6 million, or $27.54 per fully-diluted share, which is 11.6 times earnings, or 125% of book.

In using the minority-owned group the price times earnings multiple is 14.0 and discounts would only be taken for the illiquidity of stock since the other minority-owned banks are all African American owned banks and are located in similar urban markets. At 14.0 times earnings, these minority-owned financial institutions suggest an unadjusted value of $24.8 million, or $32.63 per fully-diluted share.

It is our opinion that a discount of 5% to 15% would be appropriate to account for the illiquidity of Harbor s stock. When this discount is applied, the resulting value is 11.9 times earnings to 13.3 times earnings, $21.0 to $23.5 million; or $28.13 to $31.13 per fully-diluted share. The midpoint is $22.3 million or $29.63 per fully-diluted share, which is 12.6 times earnings, or 136% of book.

In our opinion, the best guide as to the value of Harbor s stock is the price times earnings multiples of other African-American owned banks having similar size and performance, and being located in similar urban markets. The value determined by the urban most applicable group which is slightly lower should also be considered, but only to determine that the value is toward the lower half of the range determined by the minority-owned group. This range is $21.0 to $22.3 million, or $28.13 to $29.63 per fully diluted share. This is 128% to 136% of book value. Any price in this range would be a fair price at which to exchange stock (see Tables 16 and 17).

This fairness opinion is provided in connection with a proposed going private transaction, in the form of a merger in which Harbor common stock owned by shareholders who own 100 or fewer shares would be exchanged for cash.. Record holders of more than 100 shares of Harbor common stock would not receive cash for their shares in the merger and would remain Harbor shareholders. Harbor would be the surviving company in the merger. Any price in the indicated range would be fair to current Harbor shareholders, including shareholders who would be cashed out in the merger and shareholders who would not be cashed out in the merger

Table 1

Harbor Branch Locations

Address	Deposits June 30, 2005	Percent of Deposits	County
	(In thous.)		
25 West Fayette Street	$ 95,532	43.8 %	Baltimore City
1000 Lancaster Street	39,199	18.0	Baltimore City
8725 Liberty Road	31,079	14.3	Baltimore
6812 Riverdale Road	22,745	10.4	Prince George s
3420 Belair Road	15,894	7.3	Baltimore City
5000 Park Heights Avenue	13,456	6.2	Baltimore City
Total deposits	$ 217,905	100.0 %	

Source: SNL Financial, Charlottesville, Virginia.

Table 2

Harbor s Market Demographics*

Markets by Zip Code	Population 2004*	Estimated Annual Gr. Rate 2000-04*	2004 Median Household Income	Number of Business	Number of Empl.	2004 Percent African American
Baltimore City	625,867	(.9)%	$ 32,715	21,409	290,693	67.0 %
21201 Main Office	13,976	(.2)%	$ 18,709	2,366	57,283	67.9 %
21213 Erdman Ave.	36,645	(1.0)	30,000	565	4,748	90.1
21215 Pimlico Office	63,232	(.6)	31,298	1,855	22,917	83.2
Baltimore County	775,960	.7%	$ 56,135	27,704	301,934	22.3 %
21133 Randallstown	28,616	1.3%	$ 62,352	806	6,266	72.0 %
Prince George s County	836,416	1.0%	$ 61,518	24,636	295,184	64.2 %
20737 Riverdale	20,636	1.0%	$ 50,564	456	3,944	50.7 %

*2004 and growth rates estimated by ERSI.

Source: ERSI, Sourcebook America 2004 Edition, Vienna, Virginia.

Table 3

Deposit Share

Harbor s Primary Market*

	Deposits 2005	Market Share June 30, 2005	2004	2003	2002	2000
	(In millions)					
Large Banks						
Bank of America	$ 8,816	28.5 %	26.8 %	22.4 %	20.9 %	17.6 %
M&T	3,865	12.5	12.2	14.6	17.0	19.6
Wachovia	2,332	7.5	7.1	7.1	6.5	8.6
SunTrust	759	2.4	2.6	3.0	3.2	3.1
BB&T	274	.9	1.0	.8	.9	.9
Subtotal	$ 16,046	51.8 %	49.7 %	47.9 %	48.5 %	49.8 %
Leading Locals						
Mercantile	$ 3,546	11.4 %	11.5 %	12.8 %	11.1 %	9.6 %
Provident	2,028	6.5	6.9	7.2	8.6	13.0
First Mariner	606	2.0	1.9	1.9	1.9	1.3
Susquehanna	556	1.8	1.9	1.9	1.8	1.9
K Capital	304	1.0	.9	.8	.7	.6
Carrollton	204	.7	.6	.7	.8	.9
Harbor	195	.6	.6	.6	.6	.6
Subtotal	$ 7,439	24.0 %	24.3 %	25.9 %	25.5 %	27.9 %
Leading Thrifts						
Eastern	$ 524	1.7 %	1.8 %	1.9 %	1.9 %	1.8 %
BCSB	471	1.5	1.6	1.6	1.6	1.3
Rosedale	376	1.2	1.4	1.4	1.3	1.2
Northwest	313	1.0	1.3	1.3	1.4	1.2
Bradford	264	.9	.9	1.0	1.0	1.0
Hopkins Savings	218	.7	.7	.7	.7	.5
Hamilton	203	.7	.7	.8	.8	.7
Subtotal	$ 2,369	7.7 %	8.4 %	8.7 %	8.7 %	7.7 %
Other banks	$ 888	2.9 %	2.7 %	2.5 %	2.4 %	2.2 %
Other thrifts	1,663	5.4	5.8	5.9	6.1	5.2
Credit Unions	2,559	8.2	9.1	9.1	8.8	7.2
Total	$ 30,964	100.0 %	100.0 %	100.0 %	100.0 %	100.0 %

*Baltimore County and the City of Baltimore.

Source: SNL Financial, Charlottesville, Virginia.

Table 4

Harbor

Financial History

	Assets	Equity	Net Income	Percent of Assets: Capital	Percent of Assets: Net Income	Return on Avg. Equity
	(In millions)		(In thous.)			
2005*	$ 247	$ 16.4	$ 1,768	6.66 %	.74 %	10.94 %
2004	235	16.2	1,462	6.90	.63	9.33
2003	220	15.3	1,785	6.96	.84	12.22
2002	210	14.1	1,077	6.73	.54	8.22
2001	187	12.2	730	6.56	.37	6.24
2000	185	10.2	565	5.55	.32	7.03
1999	178	7.5	1	4.20		.01
1998**	184	16.4	1,009	8.91	.70	6.21
1997	136	16.0	905	11.77	.69	5.99
1996	130	14.5	777	11.21	.67	5.90
1995	113	11.3	901	10.00	.84	8.14
1994	106	10.9	703	10.26	.79	8.92
1993	62	4.5	475	7.25	.78	11.18
1992	57	4.1	346	7.15	.67	8.99
1991	45	3.7	107	8.24	.25	2.95
1990	38	3.5	149	9.35	.40	

* September 30, 2005 or nine months annualized.

** Bank level data for 1998 and proceeding years.

Source: SNL Financial, Charlottesville, Virginia.

Table 5

Harbor

Balance Sheet Growth

	Loans	Securities	Deposits	Borrowings
	(In millions)			
2005*	$194	$26	$218	$10
2004	174	29	210	7
2003	151	38	196	7
2002	122	56	193	2
2001	107	52	172	2
2000	112	55	169	4
1999	103	50	166	4
1998	86	72	167	
1997	78	30	119	
1996	85	17	114	

* September 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 6

Harbor

Income and Expense

	Percent of Average Assets				
	Interest Income	**Interest Expense**	**Net Int. Income**	**Nonint. Income**	**Oper. Income**
2005*	6.05 %	1.46 %	4.59 %	.75 %	5.34 %
2004	5.45	.98	4.47	.65	5.12
2003	5.57	1.13	4.44	1.07	5.51
2002	5.88	1.72	4.16	1.01	5.17
2001	6.86	3.01	3.85	1.08	4.93
2000	7.81	3.54	4.27	1.05	5.32
1999	7.23	3.35	3.88	.80	4.68
Regional average***	5.50 %	1.59 %	3.91 %	.68 %	4.59 %
	Oper. Expense	**Net Oper. Expense**	**Contr. to Reserves**	**Other****	**Net Income**
2005*	3.98 %	1.36 %	.20 %		.74 %
2004	4.01	1.11	.16	.01 %	.63
2003	4.04	1.47	.35	.11	.84
2002	4.33	.84	.17	.11	.54
2001	4.30	.63	.20	.10	.37
2000	4.64	.68	.20		.32
1999	4.20	.48	.47		
Regional average***	2.79 %	1.80 %	.14 %		1.14 %

* Nine months ended September 30th, annualized.

** Gains (loss) on securities.

*** Commercial banks in the District of Columbia, Maryland, New Jersey and Virginia with assets between $200 and $500 million, noninterest income less than 2% of assets for the six months ended June 30, 2005 annualized or June 30, 2005 in this and the following tables.

Source: SNL Financial, Charlottesville, Virginia.

Table 7

Harbor

Loan and Deposit Mix

	Percent of Deposits					
			CDs			
	Nonint. Bearing	Other Trans.*	Consumer	Jumbo	Total	Deposits/ Assets
2005**	23 %	48 %	16 %	13 %	100 %	88 %
2004	23	49	16	12	100	89
2002	14	58	15	13	100	92
2000	11	55	17	17	100	92
Regional average	15 %	42 %	29 %	14 %	100 %	85 %

	Loans					
	Res. Mtge.	Comm. R.E.	Comm.	Consumer	Total	Loans/ Assets
2005**	16 %	39 %	40 %	5 %	100 %	78 %
2004	18	36	40	6	100	73
2002	32	31	26	11	100	58
2000	29	33	29	9	100	61
Regional average	26 %	49 %	14 %	11 %	100 %	71 %

* Includes other savings.
** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 8

Harbor

Capital and Asset Quality Comparison

	Percent of Assets			
	Capital	**Reserves**	**NPAs***	**Reserves/ Loans**
2005**	6.66 %	.79 %	.38 %	1.01 %
2004	6.90	.68	.34	.93
2003	6.96	.68	.33	.98
2002	6.73	.50	.58	.86
2001	6.56	.51	.41	.90
2000	5.55	.40	.17	.65
1999	4.20	.38	.71	.66
1998	8.91	.34	1.24	.74
1997	11.77	.48	2.00	.84
1996	11.21	.69	.43	1.04
Regional median	9.89 %	.78 %	.50 %	1.11 %

* Includes loans 90 days past due.
** September 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 9a

Urban Exchange Group*

Description

Full Name	**City, State**	**Assets****
		(In mill.)
American Community Bancshares, Inc.	Charlotte, N.C.	$443
Annapolis Bancorp, Inc.	Annapolis, Md.	322
Bank of Wilmington Corporation	Wilmington, N.C.	312
Cardinal State Bank	Durham, N.C.	152
Carolina Bank Holdings, Inc.	Greensboro, N.C.	331
Cornerstone Bancorp, Inc.	Stamford, Ct.	221
Crescent Financial Corporation	Cary, N.C.	405
First National Bancshares, Inc.	Spartanburg, S.C.	303
Glen Burnie Bancorp	Glen Burnie, Md.	319
Greenville First Bancshares, Inc.	Greenville, S.C.	375
Jacksonville Bancorp, Inc.	Jacksonville, Fla.	262
Millennium Bankshares Corporation	Reston, Va.	428
Monarch Bank	Chesapeake, Va.	300
Valley Bancorp	Las Vegas, Nev.	373
Harbor	Baltimore, Md.	$247

* Non-minority urban banks on the east coast with assets between $150 and $500 million and returns on average assets over .50%.
** September 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 9b

Urban Exchange Group

Financial Performance*

	Assets	As a Percent of Assets or Avg. Assets			Return on Avg. Equity
		Equity	NPAs**	Net Income	
	(In mill.)				
American Community	$443	11.31%	.73%	.98%	9.64%
Annapolis	322	6.29	.96	.91	14.16
Bank of Wilmington	312	7.78	.25	.61	6.16
Cardinal State	152	12.46	.30	.56	4.24
Carolina Bank	331	6.78	1.77	.63	9.10
Cornerstone	221	11.40	.56	.69	6.39
Crescent Financial	405	7.20	.05	.79	10.19
First National	303	5.21	.09	1.03	18.34
Glen Burnie	319	8.35	.07	.95	11.30
Greenville First	375	8.12	.32	.91	10.73
Jacksonville	262	7.35	.19	.76	9.84
Millennium	428	11.28	.15	.61	5.02
Monarch	300	9.68	.00	.70	6.75
Valley	373	10.80	.04	1.63	13.18
Median	$320	8.24%	.22%	.78%	9.74%
Harbor***	$247	6.66%	.38%	.74%	10.94%

* September 30, 2005 or the twelve months ended September 30, 2005.
** Includes loans 90 days past due.
*** September 30, 2005 or the nine months ended September 30, 2005, annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 9c

Urban Exchange Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. to Reserves**	**Other**	**Net Income**
American Community	3.81%	1.94%	1.87%	.17%	(.14)%	.98%
Annapolis	3.71	2.15	1.56	.13		.91
Bank of Wilmington	3.46	2.04	1.42	.59		.61
Cardinal State	3.66	2.91	.75	.18		.56
Carolina Bank	3.12	1.76	1.36	.38		.63
Cornerstone**	4.47	3.07	1.40	.11	(.13)	.69
Crescent Financial	3.64	2.20	1.44	.25	.03	.79
First National	3.38	1.61	1.77	.23		1.03
Glen Burnie	3.88	2.81	1.07	(.02)	.06	.95
Greenville First	3.31	1.51	1.80	.33		.91
Jacksonville	3.62	2.24	1.38	.16	(.03)	.76
Millennium	3.15	2.10	1.05	.15		.61
Monarch	3.80	2.39	1.41	.33		.70
Valley	4.84	2.13	2.71	.24		1.63
Median	3.65%	2.14%	1.42%	.21%		.78%
Harbor**	4.59%	3.23%	1.36%	.20%		.74%

* Twelve months ended September 30, 2005.
** September 30, 2005 or the nine months ended September 30, 2005, annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 9d

Urban Exchange Group

Stock Performance

	Stock Price*	Price* Times Earnings		Price* Percent of Book		Avg. Shares Traded Daily**
American Community	$18.46	18.5	X***	167	%	4,755
Annapolis	9.28	14.3		186		2,136
Bank of Wilmington	10.55	24.5		149		4,613
Cardinal State	11.56	34.0		138		2,763
Carolina Bank	11.95	15.5	***	145		2,471
Cornerstone	36.31	32.1		194		2,758
Crescent Financial	15.01	23.1		214		5,014
First National	24.01	20.2		275		405
Glen Burnie	18.50	12.8		143		633
Greenville First	23.88	22.3		209		2,209
Jacksonville	32.40	32.4		288		1,308
Millennium	8.34	29.8		152		23,724
Monarch	15.66	28.0		170		2,320
Valley	34.96	20.7		245		16,029
Median		22.7	X	178	%	2,615

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelve months ended September 30, 2005, unless otherwise noted.

** One year.

*** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

Table 10a

Urban OTC Group*

Description

Full Name	City, State	Assets**	
		(In mill.)	
BCB Bancorp, Inc.***	Bayonne, N.J.	$447	
Business Bank Corporation	Las Vegas, Nev.	410	
Capital Bancorp, Inc.	Nashville, Tenn.	445	
First South Bancorp, Inc.	Spartanburg, S.C.	312	
First Trust Bank***	Charlotte, N.C.	292	
Grandsouth Bancorporation***	Greenville, S.C.	236	
Greater Sacramento Bancorp	Sacramento, Calif.	256	
Hampton Roads Bankshares, Inc.	Chesapeake, Va.	393	
North State Bancorp***	Raleigh, N.C.	373	
Summit Bancshares, Inc.	Oakland, Calif.	166	****
VSB Bancorp, Inc.	Staten Island, N.Y.	228	
Harbor	Baltimore, Md.	$247	

* Non-minority urban banks on the east coast with assets between $150 and $500 million and returns on average assets above .50%.

** September 30, 2005 unless otherwise noted.
*** De novo bank.
**** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

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Table 10b

Urban OTC Group

Financial Performance*

		As a Percent of Assets or Avg. Assets			
	Assets	Equity	NPAs**	Net Income	Return on Avg. Equity
	(In mill.)				
BCB	$447	6.53%	.26%	1.18%	17.20%
Business Bank	410	8.04	.23	1.23	16.04
Capital	445	6.30	.19	.89	13.41
First South	312	9.49	.60	.92	10.10
First Trust	292	9.28	.03	1.16	14.18
Grandsouth	236	6.26	1.01	.98	18.69
Greater Sacramento	256	6.23	.16	.99	14.89
Hampton Roads	393	11.67	.56	1.40	11.66
North State	373	5.53	.00	.69	11.04
Summit***	166	11.21	.11	1.12	9.94
VSB	228	6.31	.42	1.18	19.26
Median	$312	6.53%	.23%	1.12%	14.18%
Harbor	$247	6.66%	.38%	.74%	10.94%

* September 30, 2005 or the twelve months ended September 30, 2005, unless otherwise noted.
** Includes loans 90 days past due.
*** June 30, 2005 or the twelve months ended June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 10c

Urban OTC Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. To Reserves**	**Other**	**Net Income**
BCB	3.90 %	1.77 %	2.13 %	.26 %	.01 %	1.18 %
Business Bank	4.86	2.82	2.04	.10	(.05)	1.23
Capital	3.69	2.07	1.62	.46		.89
First South	3.93	1.68	2.25	.27	(.55)	.92
First Trust	3.96	1.93	2.03	.16		1.16
Grandsouth	3.93	1.93	2.00	.45	.01	.98
Greater Sacramento	4.08	2.44	1.64	.04	.03	.99
Hampton Roads	4.68	2.37	2.31	.17		1.40
North State	3.60	2.25	1.35	.26		.69
Summit**	5.00	2.86	2.14	.18	(.06)	1.12
VSB	4.25	2.12	2.13	(.03)	.05	1.18
Median	3.96 %	2.12 %	2.04 %	.18 %		1.12 %
Harbor***	4.59 %	3.23 %	1.36 %	.20 %		.74 %

* Twelve months ended September 30, 2005.
** Twelve months ended June 30, 2005.
*** September 30, 2005 or the nine months ended September 30, 2005, annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 10d

Urban OTC Group

Stock Performance

		Price*				
	Stock Price*	Times Earnings		Percent of Book		Avg. Shares Traded Daily**
BCB	$17.50	14.6	X	223	%	1,320
Business Bank	42.15	21.0		267		1,305
Capital	19.10	18.7		237		663
First South	32.75	15.7	****	193		595
First Trust	19.00	18.5		209		1,358
Grandsouth	12.00	17.1		235		221
Greater Sacramento	28.95	18.4	****	235		920
Hampton Roads	10.85	17.8		193		1,738
North State	21.50	30.7		296		469
Summit***	17.65	15.8		159		1,359
VSB	20.25	11.6		212		241
Median		17.8	X	223	%	920

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelvemonths ended September 30, 2005, unless otherwise noted.

** One year.

*** December 8, 2005 stock price and financial data as of June30, 2005 or the twelvemonths ended June 30, 2005.

**** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

Table 11a

Urban Most Applicable Group*

Description

Full Name	**City, State**	**Assets****	
		(In mill.)	
Annapolis Bancorp, Inc.	Annapolis, Md.	$322	
Capital Bancorp, Inc.	Nashville, Tenn.	445	
Carolina Bank Holdings, Inc.	Greensboro, N.C.	331	
Cornerstone Bancorp, Inc.	Stamford, Ct.	221	
Glen Burnie Bancorp	Glen Burnie, Md.	319	
Summit Bancshares, Inc.	Oakland, Calif.	166	***
VSB Bancorp, Inc.	Staten Island, N.Y.	228	
Harbor	Baltimore, Md.	$247	

* Non-minority urban banks with assets between $150 and $500 million and returns on average assets above .50% excluding banks established on or after 1998 and top performing banks with a return on average assets over 1.20%.

** September 30, 2005.

*** June 30, 2005.

Source: SNL Financial, Charlottesville, Virginia.

Table 11b

Urban Most Applicable Group

Financial Performance*

		As a Percent of Assets or Avg. Assets			
	Assets	Equity	NPAs**	Net Income	Return on Avg Equity
	(In mill.)				
Annapolis	$322	6.29%	.96%	.91%	14.16%
Capital	445	6.30	.19	.89	13.41
Carolina Bank	331	6.78	1.77	.63	9.10
Cornerstone	221	11.40	.56	.69	6.39
Glen Burnie	319	8.35	.07	.95	11.30
Summit***	166	11.21	.11	1.12	9.94
VSB	228	6.31	.42	1.18	19.26
Median	$319	6.78%	.42%	.91%	11.30%
Harbor	$247	6.66%	.38%	.74%	10.94%

* September 30, 2005 or the twelve months ended September 30, 2005.
** Includes loans 90 days past due. Excludes new banks and high performing banks.
*** June 30, 2005 or the twelve months ended June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 11c

Urban-Most Applicable Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. to Reserves**	**Other**	**Net Income**
Annapolis	3.71%	2.15%	1.56%	.13%		.91%
Capital	3.69	2.07	1.62	.46		.89
Carolina Bank	3.12	1.76	1.36	.38		.63
Cornerstone	4.47	3.07	1.40	.11	(.13)%	.69
Glen Burnie	3.88	2.81	1.07	(.02)	.06	.95
Summit**	5.00	2.86	2.14	.18	(.06)	1.12
VSB	4.25	2.12	2.13	(.03)	.05	1.18
Median	3.88%	2.15%	1.56%	.13%		.91%
Harbor***	4.59%	3.23%	1.36%	.20%		.74%

* Twelve months ended September 30, 2005.

** Twelve months ended June 30, 2005.

*** September 30, 2005 or the nine months ended September 30, 2005, annualized.

Source: SNL Financial, Charlottesville, Virginia.

Table 11d

Urban-Most Applicable Group

Stock Performance

		Price*				
	Stock Price*	Times Earnings		Percent of Book		Avg. Shares Traded Daily**
Annapolis	$9.28	14.3	X	186	%	2,136
Capital	19.10	18.7		237		663
Carolina Bank	11.95	15.5	****	145		2,471
Cornerstone	36.31	32.1		194		2,758
Glen Burnie	18.50	12.8		143		633
Summit***	17.65	15.8		159		1,359
VSB	20.25	11.6		212		241
Median		15.5	X	186	%	1,359

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelve months ended September 30, 2005, unless otherwise noted.

** One year.

*** December 8, 2005 stock price and financial data as of June 30, 2005 or the twelve months ended June 30, 2005.

**** Adjusted to remove unusual quarters.

Source: SNL Financial, Charlottesville, Virginia.

Table 12

Publicly-Traded Minority-Owned Banks and Thrifts

Description

Full Name	City, State	Assets*	
		(In mill.)	
Banks - over $900 million			
Cathay General Bancorp, Inc.	Los Angeles, Calif.	$6,157	
East West Bancorp, Inc.	San Marino, Calif.	7,938	
International Bancshares Corporation	Laredo, Texas	10,310	
MetroCorp Bancshares, Inc.**	Houston, Texas	935	
Preferred Bank	Los Angeles, Calif.	1,097	
Banks - under $900 million			
Abigail Adams National Bancorp, Inc.	Washington, D.C.	$333	
Albina Community Bancorp	Portland, Org.	120	
Canyon National Bank	Palm Springs, Calif.	232	
Citizens Bancshares Corporation**	Atlanta, Ga.	324	
IBW Financial Corporation**	Washington, D.C.	339	***
M&F Bancorp, Inc.**	Durham, N.C.	246	
Pan American Bancorp	Los Angeles, Calif.	42	
PanAmerican Bancorp	Miami, Fla.	243	
Saehan Bancorp	Los Angeles, Calif.	494	
Thrifts			
Carver Bancorp, Inc.**	New York, N.Y.	$648	
Independence Federal Savings Bank**	Washington, D.C.	160	
Mutual Community Savings Bank, Inc.**	Durham, N.C.	91	
Harbor**	Baltimore, Md.	$247	

* September 30, 2005.
** African-American owned banks.
*** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 13a

Minority-Owned Group*

Description

Full Name	**City, State**	**Assets****	
		(In mill.)	
Carver***	New York, N.Y.	$ 648	
Citizens***	Atlanta, Ga.	324	
IBW***	Washington, D.C.	339	****
PanAmerican	Miami, Fla.	243	
Median		$ 332	
Harbor***	Baltimore, Md.	$ 247	

* Minority owned with assets under $900 million.
** September 30, 2005.
*** African-American owned banks.
**** June 30, 2005.
Source: SNL Financial, Charlottesville, Virginia.

Table 13b

Minority-Owned Group

Financial Performance*

		As a Percent of Assets or Avg. Assets			
	Assets	**Equity**	**NPAs****	**Net Income**	**Return on Avg. Equity**
	(In mill.)				
Comparable					
Carver	$648	7.33 %	.42 %	.45 %	5.93 %
Citizens	324	8.29	1.23	.69	8.66
IBW***	339	7.45	.72	.48	6.31
PanAmerican	244	17.59	.02	.99	8.16
Median	$332	7.87 %	.57 %	.59 %	7.24 %
Harbor****	$247	6.66 %	.38 %	.74 %	10.94 %
Non-comparable					
Abigail Adams	$334	8.39 %	.21 %	1.36 %	**13.96 %**
Albina Community	120	5.69	1.92	.30	**3.71**
Canyon National	232	7.93	.10	1.55	**20.86**
Independence	160	10.14	.34	.16	**1.59**
M&F	246	8.26	**2.08**	.25	**2.86**
Mutual Community	**91**	8.11	1.22	.01	**.09**
Pan American	**42**	13.67		.18	**1.29**
Saehan	494	8.55	.16	1.52	**16.02**

NOTE: Bolded numbers are reason for exclusion.

* September 30, 2005 or the twelve months ended September 30, 2005.
** Includes loans 90 days past due.
*** June 30, 2005 or the twelve months ended June 30, 2005.
**** September 30, 2005 or the nine months ended September 30, 2005 annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 13c

Minority-Owned Group

Income and Expense Comparison*

	Percent of Average Assets					
	Net Int. Income	**Net Oper. Expense**	**Net Oper. Income**	**Contr. to Reserves**	**Other**	**Net Income**
Carver	3.05 %	2.29 %	.76 %		(.07) %	.45 %
Citizens	4.48	3.44	1.04	.09 %	(.11)	.69
IBW**	4.53	3.87	.66	.05	.12	.48
PanAmerican	4.65	3.16	1.49	.50		.99
Median	4.51 %	3.30 %	.90 %	.07 %	(.03) %	.59 %
Harbor***	4.59 %	3.23 %	1.36 %	.20 %		.74 %

* Twelve months ended September 30, 2005.
** Twelve months ended June 30, 2005.
*** September 30, 2005 or the nine months ended September 30, 2005, annualized.
Source: SNL Financial, Charlottesville, Virginia.

Table 13d

Minority-Owned Group

Stock Performance

	Stock Price*	Price* Times Earnings		Price* Percent of Book		Avg. Shares Traded Daily***
Carver	$ 15.10	14.0	X	80	%	2,486
Citizens	10.50	9.8		82		1,186
IBW**	34.00	14.0		90		133
PanAmerican	4.21	22.2		141		8,162
Median		14.0	X	86	%	1,836

* December 8, 2005 stock price and financial data as of September 30, 2005 or the twelve months ended September 30, 2005.
** December 8, 2005 stock price and financial data as of June 30, 2005 or the twelve months ended June 30, 2005.
*** One Year.
**** Adjusted to remove unusual quarters.
Source: SNL Financial, Charlottesville, Virginia.

Table 14

Stock Trades in 2005

	Shares	Price
April 19	77	$25.00
April 21	308	25.00

Source: Internal report.

Table 15

Discounted Dividends Applied to Harbor*

	Discount Rate					
	10%		11%		12%	
	Value (in millions)					
12 times earnings***	$ 21.6		$ 19.0		$ 16.8	
14 times earnings***	23.1		20.3		17.9	
	Per Share**					
12 times earnings***	$ 31.46		$ 27.71		$ 24.54	
14 times earnings***	33.72		29.58		26.09	
	Times Earnings					
12 times earnings***	12.2	X	10.7	X	9.5	X
14 times earnings***	13.1		11.5		10.1	
	Price-to-Book****					
12 times earnings***	131	%	116	%	102	%
14 times earnings***	141		123		109	

* Assumes 6% earnings growth, capital in excess of 6.50% dividended out and a tax rate of 36%.
** Shares outstanding of 685,579.
*** Earnings of $1,768,000.
**** Equity of $16,435,000.

Table 16

Summary of Valuation Multiples*

	Price		
Comparable groups	**Times Earnings**	**Percent of Book**	**Number in Group**
Urban exchange group	22.7 X	178 %	14
Urban OTC group	17.8	223	11
Urban most applicable	15.5 X	186 %	7
Minority-owned group	14.0	86	4
Stock trades	10.4 X	112 %	
Discounted Dividends**	10.7 X	116 %	

* December 8, 2005 stock price and financial data for the year ended September 30, 2005 or September 30, 2005 or most recent available.

** Based on a 11% discount rate and a terminal value of 12 times earnings.

Table 17

Pricing Applied to Harbor

			Discount All*					
Based on urban most applicable group			**20%**		**25%**		**30%**	
P/E**	15.	5X	12.	4X	11.	6X	10.	9X
Value (in mill.)	$27.	4	$21.	9	$20.	6	$19.	2
Per share***	$39.	97	$31.	98	$29.	98	$27.	98
Per Share Diluted***	$35.	86	$29.	20	**$27.**	**54**	$25.	88
Price-to-book****	167	%	133	%	125	%	117	%

			Discount for illiquidity					
Based on minority-owned group			**5%**		**10%**		**15%**	
P/E**	14.0	X	13.	3X	12.	6X	11.	9X
Value (in mill.)	$24.	8	$23.	5	$22.	3	$21.	0
Per share***	$36.	10	$34.	30	$32.	49	$30.	69
Per Share Diluted***	$32.	63	$31.	13	**$29.**	**63**	$28.	13
Price-to-book****	151	%	143	%	136	%	128	%

* Discount for poor market dynamics, illiquidity of stock and minority-ownership.
** Earnings of $1,768,000.
*** Shares outstanding of 685,579; options outstanding of 132,741 with a weighted strike price of $16.27.
**** Equity of $16,435,000.

Exhibit (f) to Schedule 13E-3
Form of Proxy

PRELIMINARY
-FORM OF PROXY-

REVOCABLE PROXY
HARBOR BANKSHARES CORPORATION
ANNUAL MEETING OF SHAREHOLDERS
_____________, 2006

The undersigned hereby constitutes and appoints Joseph Haskins, Jr. and George F. Vaeth, Jr. and each of them the proxies of the undersigned, with full power of substitution, to attend the annual meeting of shareholders (the "Annual Meeting") of Harbor Bankshares Corporation (the "Company") to be held at the offices of the Company at 25 West Fayette Street, Baltimore, Maryland 21201 on Wednesday,________ 2006, at 12:00 noon Eastern Time, or at any adjournment thereof, and to vote all the shares of stock of the Company that the undersigned may be entitled to vote, upon the following matters:

THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR' APPROVAL OF THE AGREEMENT AND PLAN OF MERGER, “FOR” ADJOURNMENT OF THE ANNUAL MEETING IF NECESSARY TO SOLICIT ADDITIONAL VOTES FOR APPROVAL OF THE AGREEMENT AND PLAN OF MERGER, AND “FOR” THE ELECTION OF ALL DIRECTOR NOMINEES. PLEASE SIGN, DATE AND RETURN PROMPTLY IN THE ENCLOSED ENVELOPE. PLEASE MARK YOUR VOTE IN BLUE OR BLACK INK

1. Approval of the Agreement and Plan of Merger, dated as of ________, 2006, by and between Harbor Bankshares Corporation and Harbor Merger Corporation, a Maryland corporation and wholly-owned subsidiary of Harbor Bankshares Corporation (the “merger subsidiary”), pursuant to which the merger subsidiary will merge with and into Harbor Bankshares Corporation, with Harbor Bankshares Corporation being the surviving corporation.

   FOR ______ AGAINST ______ ABSTAIN ______

2. The adjournment of the Annual Meeting to solicit additional votes for approval of the Agreement and Plan of Merger, if necessary.

   FOR ______ AGAINST ______ ABSTAIN ______

3. The election of four Class II Directors, each to serve for a three-year term.

   _____ For all nominees listed below (except as marked to the contrary below).
   _____ Withhold authority to vote for all nominees listed below.

Nominees: Nathaniel Higgs, Delores G. Kelley, Erich March, and Stanley W. Tucker

(To withhold authority to vote for any individual nominee, strike out the nominee’s name.)

4. The transaction of such other matters as may properly come before the Annual Meeting or any adjournments or postponements thereof.

THIS PROXY WILL BE VOTED IN ACCORDANCE WITH THE INSTRUCTIONS MARKED HEREIN. IF NO INSTRUCTIONS TO THE CONTRARY ARE MARKED HEREIN, THIS PROXY WILL BE VOTED FOR APPROVAL OF THE AGREEMENT AND PLAN OF MERGER, FOR ADJOURNMENT OF THE ANNUAL MEETING, IF NECESSARY, AND FOR THE ELECTION OF DIRECTORS, AND AS DETERMINED BY A MAJORITY OF THE BOARD OF DIRECTORS AS TO OTHER MATTERS.

THIS PROXY IS SOLICITED BY THE BOARD OF DIRECTORS.

The undersigned shareholder hereby acknowledges receipt of a copy of the accompanying Notice of Annual Meeting of Shareholders and Proxy Statement and hereby revokes any proxy or proxies previously given. This proxy may be revoked at any time prior to its exercise.

PLEASE COMPLETE, DATE, SIGN, AND MAIL THIS PROXY PROMPTLY IN THE ENCLOSED POSTAGE-PREPAID ENVELOPE.

To change the address on your account, please check the box at right and indicate your new address in the address space above. Please note that changes to the registered name(s) on the account may not be submitted via this method.

Signature of Shareholder	Date:
Signature of Shareholder	Date:

Note: Please sign exactly as your name or names appear on this Proxy. When shares are held jointly, each holder should sign. When signing as executor, administrator, attorney, trustee, or guardian, please give full title as such. If the signer is a corporation, please sign full corporate name by duly authorized officer, giving full title as such. If signer is a partnership, please sign in partnership name by authorized person.