SAIF CORPORATION

Financial Statements as of and for the Year Ended December 31, 2002, and Independent Auditors' Report

Overview of SAIF Corporation Financial Reporting
(Prepared by SAIF Corporation)

SAIF Corporation is a public corporation created by an act of the Oregon Legislature. It traces its origins to 1914 when its predecessor organization commenced business.

SAIF is authorized to write workers' compensation and surety coverage in Oregon and certain other jurisdictions as required by the Department of Consumer and Business Services to service accounts in the assigned risk pool.

SAIF Corporation prepares financial statements in conformity with statutory accounting practices, which are prescribed for use in reporting accounting transactions for insurance companies. These practices arise from state laws and from rules adopted by the State Insurance Commissioner and, for Oregon, are the practices promulgated by the National Association of Insurance Commissioners (NAIC). Statutory accounting practices are conservative in nature and are designed to protect policyholders and claimants to ensure that, in the event of liquidation, sufficient amounts will have been set aside to provide for the outstanding claims of injured workers and their dependants, whereas generally accepted accounting principles (GAAP) are based on the going-concern concept and place more emphasis on assigning income and disbursements to their proper period.

At the request of the Oregon Secretary of State's Audits Division, SAIF has prepared the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America. As a component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board. Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as an enterprise fund. Accordingly, SAIF follows the accrual basis of accounting. Revenues are recognized when earned, regardless of when received, and expenses are recognized when incurred, regardless of when paid.

There are significant differences between the statutory statements which SAIF prepares for regulatory and management purposes and the accompanying financial statements. They include:

- Statutory accounting requires the majority of invested assets to be recorded at amortized cost, whereas investments are stated at fair value in the accompanying statements with the corresponding change in the fair value for the year recorded as investment income.

- Statutory accounting does not allow the accrual of policyholder dividends until declared by the Board of Directors. Generally accepted accounting principles require the accrual of estimated policyholder dividends.

- Cash collateral and collateral due to borrowers for securities lending activity are reflected on the accompanying balance sheet. Statutory accounting does not require the reporting of such items as assets and liabilities.

- Acquisition costs, such as commissions and other costs related to acquiring new business, are expensed as incurred for statutory accounting, while under GAAP, they are deferred and amortized to income as premiums are earned or in relation to estimated gross profits.

- Statutory accounting requires that certain assets not readily available for the payment of claims be "non-admitted" and removed from the balance sheet. Those assets, such as property and equipment are included on the GAAP financial statements.

INDEPENDENT AUDITORS' REPORT

The Board of Directors of
SAIF Corporation

The Secretary of State Audits Division,
State of Oregon

We have audited the accompanying balance sheet of SAIF Corporation ("SAIF") as of December 31, 2002, and the related statements of revenues, expenses, and changes in fund equity, and of cash flows for the year then ended. These financial statements are the responsibility of SAIF's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, such financial statements present fairly, in all material respects, the financial position of SAIF as of December 31, 2002, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The Management Discussion and Analysis that precedes the financial statements is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of SAIF's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 20, 2003, on our consideration of SAIF's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Deloitte + Touche LLP

June 20, 2003

SAIF CORPORATION

Management Discussion and Analysis
Unaudited

Management of SAIF Corporation provides Management's Discussion and Analysis for readers of the Company's financial statements and for inclusion in the State of Oregon Comprehensive Annual Financial Report. This narrative overview and analysis of the financial activities of SAIF Corporation is for the calendar year ended December 31, 2002. Readers are encouraged to consider this information in conjunction with the Company's financial statements and footnote disclosures that follow.

Overview

SAIF Corporation is a public corporation created by an act of the Oregon Legislature. It traces its origins to 1914 when its predecessor organization commenced business.

SAIF is authorized to write workers' compensation and surety coverage in Oregon and certain other jurisdictions as required by the Department of Consumer and Business Services to service accounts in the assigned risk pool.

SAIF Corporation prepares financial statements in conformity with statutory accounting practices, which are prescribed for use in reporting accounting transactions for insurance companies. At the request of the Oregon Secretary of State's Audits Division, SAIF has prepared the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America. As a component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board. Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as an enterprise fund.

The Corporation's Board of Directors is appointed by the Governor of the State and consists of prominent Oregonians, three of which represent SAIF policyholders, not otherwise in the employ of the Company. The mission of SAIF Corporation is "to make insurance available to as many Oregon employers as inexpensively as may be consistent with the overall integrity of the Industrial Accident Fund . . . and sound principles of insurance." ORS 656.752.

SAIF fulfills its mission by continuing to make workers' compensation insurance available to a greater number of policyholders at a lower premium rate. The Company's market share, based on direct earned premium in the State of Oregon, increased from 38.4% for 2001 to 40.8% for 2002. In addition, SAIF's claims management practices and loss prevention efforts helped lower the frequency of job related accidents that occurred during the year. Rising medical inflation and weak investment results continued to be a challenge faced during the year.

Condensed Financial Information
(In thousands)
(Unaudited)

Assets			**Increase**
Current Assets	**12/31/02**	**12/31/01**	**(Decrease)**
Cash and Cash Equivalents	$380,439	$182,730	$197,709
Investments	2,179,928	2,322,226	(142,298)
Securities Lending Cash Collateral	151,132	194,413	(43,281)
Accounts and Interest Receivable	149,135	106,573	42,562
Receivable for Securities Sold	30,073	1,581	28,492
Inventories	132	170	(38)
Total Current Assets	2,890,839	2,807,693	83,146
Noncurrent Assets			
Land, Buildings, Property and Equipment	25,185	27,206	(2,021)
Total Assets	$2,916,024	$2,834,899	$81,125

Liabilities and Fund Equity			
Current Liabilities			
Reserve for Loss and Loss Adjustment Expenses	$166,692	$137,036	$29,656
Unearned Premiums	45,781	38,034	7,747
Accounts and Interest Payable	27,273	25,435	1,838
Due to Brokers for Security Purchases	35,876	9,132	26,744
Obligations Under Securities Lending	151,132	194,414	(43,282)
Other Liabilities	29,842	26,105	3,737
Total Current Liabilities	456,596	430,156	26,440
Noncurrent Liabilities			
Reserve for Loss and Loss Adjustment Expenses	2,096,240	1,982,765	113,475
Total Liabilities	2,552,836	2,412,921	139,915
Fund Equity	363,188	421,978	(58,790)
Total Liabilities and Fund Equity	$2,916,024	$2,834,899	$81,125

Operating Revenues			
Net Premiums Earned	$295,092	$246,384	$48,708
Net Investment Income	73,536	19,949	53,587
Other	23,100	18,782	4,318
Total Operating Revenues	391,728	285,115	106,613
Operating Expenses			
Salaries and Wages	54,990	52,575	2,415
Underwriting and Other Expenses	55,294	51,371	3,923
Loss and Dividend Expenses Incurred	335,011	219,365	115,646
Other Expenses	5,223	6,491	(1,268)
Total Operating Expenses	450,518	329,802	120,716
Operating Loss	($58,790)	($44,687)	($14,103)

The unaudited condensed financial information shown above is derived from the audited financial statements for the years ended December 31, 2002, included herein, and 2001, not included herein. We have revised the 2001 financial statements to record TBA securities on a net basis, which resulted in a decrease of investments and due to brokers for security purchases of $288.4 million.

Management's Discussion and Analysis

Financial Position

At the end of 2002, total assets were $81.1 million greater than the prior year. Total liabilities increased $139.9 million for the year, while fund equity declined $58.8 million.

Significant changes include:

Cash and Cash Equivalents – The majority of the Company's cash accounts are made up of short-term investment funds utilized by external investment managers. Cash may fluctuate significantly from period to period as the investment managers trade securities. At the end of 2002, there were significantly more pending security trades than there were at the end of 2001. Also, the core bond managers invest in FNMA and GNMA TBA securities. These securities have monthly settlement dates, and offer investors the ability to finance these transactions rather than taking delivery on a monthly basis. These transactions are commonly referred to as "rolling" and are accomplished by simultaneously selling your position for one month's delivery and buying it for the next month's delivery. This basically postpones the settlement of the transaction until the following month, which explains the increase in the Company's cash position.

Investments – At the end of 2002, investments were $142.3 million less than the end of 2001. The reduction was primarily due to a $112.3 million decline in equity holdings, which was the result of valuation changes rather than acquisitions and disposals.

Early in 2001, the Oregon Investment Council approved a change in the Company's asset allocation target, which lowers the allocation to equity securities and increase the allocation to bonds. Therefore, the reinvestment of investment income is directed toward bond holdings with no new contributions to equity securities. During 2002, the bond market performed relatively well, so the market value adjustment made to the Company's bond holdings was $36.2 million greater than the amount recorded for 2001.

The decline in the value of the Company's equity holdings was primarily due to the decline in market value. The Company's BGI Russell 3000 index holdings had a return of minus 21.5% for the year. Trading activity and market value declines reduced the value of convertible preferred stocks.

Securities Lending Cash Collateral – This line item can fluctuate significantly from period to period depending on the amount of investment securities on loan. The amount of securities on loan will vary depending on market conditions and the demand for certain securities in our portfolio.

Accounts and Interest Receivable – The amount of premium due to SAIF increased in 2002 because of an increase in the Company's book of business and because of increased amounts due on retrospectively rated policies. During 2002, net earned premium for SAIF increased almost 20% as Oregon experienced a "hard" workers' compensation market and several insurance carriers quit writing this line of business in the state. Premiums due on retrospectively rated policies increased approximately $26.0 million as claims costs increased significantly on two large group retro policies, namely the State of Oregon and AGC.

Other receivable amounts went up during 2002 primarily because of a $5.4 million increase in the amount due from the assigned risk pool. The amount of assigned risk premium serviced by SAIF grew 47%, a result of the hard workers' compensation market. Premium assessment due from policyholders also increased with the growth in premium.

Receivable for Securities Sold - The amount receivable for securities sold at the end of 2002 was $28.5 million higher than the prior year due to an increase in pending security trade settlements.

Reserve for Loss and Loss Adjustment Expenses – Current and noncurrent loss reserves increased $129.7 million or 7.3% during 2002 and loss adjustment expense reserves increased $13.5 million or 4.0%. The increase in reserves was due to growth in the book of business as favorable prior year loss development was relatively small at $23.4 million.

The favorable loss reserve development disclosed above was primarily due to fewer serious losses than expected. Prior year loss reserves for indemnity costs declined $18.1 million while medical reserves on permanent partial disability losses declined $13.9 million. As a result of favorable frequency development, the Company lowered its assumption of future permanent total disability claims, which had a favorable impact of $11.2 million on loss reserves.

Rising medical cost throughout the year caused an increase in loss reserves. During the year, actual medical inflation was near 14%, which exceeded the explicit inflation assumption used in the loss reserve estimates. SAIF believes higher levels of medical inflation will continue in the near future and adjusted the inflation assumptions accordingly. This refinement in the assumption increased loss reserves approximately $49.0 million.

Unearned Premiums – The amount of unearned premium for 2002 increased $7.7 million from 2001, or 20.4%, which is consistent with the increase in premium due and earned premium.

Due to Brokers for Security Purchases – The amount reported on this line increased $26.7 million from 2001 because of an increase in the amount of investment trades pending. See comments above regarding pending investment trades.

Obligations Under Securities Lending - This line item can fluctuate significantly from period to period depending on the amount of investment securities on loan. The amount of securities on loan will vary depending on market conditions and the demand for certain securities in our portfolio.

Operations

Significant changes in revenues and expenses includes:

Net Premiums Earned – New sales and policyholder payroll growth outpaced premium rate reductions for 2001 and 2002 that would impact earned premium for the year. New sales were $32.6 million for the year compared to premium lost to competitors of $3.0 million. The retention rate for 2002 was 98.8%. Policyholder payroll grew approximately 8.3% and the number of policyholders grew over 10% during the year. An increase in the amount of retrospectively rated premium due, as noted above, also increased the amount of premium earned.

Investment Income – Investment income for 2002 was $53.6 million greater than the amount recorded for 2001 because of an increase in realized investment gains and a decrease in unrealized losses on invested assets. Realized gains for 2002 were $20.5 million greater than the prior year. Unrealized losses recorded for 2002 were $29.6 million less than the unrealized losses recorded for 2001.

Other Income – Other income for 2002 was greater than the amount recorded for 2001 because of the growth in premium assessment income associated with the growth in premium income.

Loss and Dividend Expense Incurred – Losses incurred for 2002 increased over 2001 because of growth in loss reserves as noted above, and the passage of Senate Bill 485 in 2001 which lowered losses $87.6 million in that year.

Other Required Supplementary Information

At less than 1% of total assets, SAIF's capital assets are minimal, consisting of office buildings primarily occupied by the Company and computer and office equipment. There were no significant changes in capital assets during the year. There are no significant commitments outstanding for capital assets.

Other than accounts payable and amounts due for investment purchases, SAIF has no debt and there are no plans to issue debt.

SAIF develops an annual operating budget for planning and control purposes. It is approved by the Board of Directors and monitored closely by management and the Board.

SAIF Corporation

Balance Sheet

December 31, 2002

(In Thousands)

		2002
ASSETS		
Current Assets		
Cash and Cash Equivalents	$	380,439
Investments		2,179,928
Securities Lending Cash Collateral		151,132
Accounts and Interest Receivable		149,135
Receivable for Securities Sold		30,073
Inventories		132
Total Current Assets		2,890,839
Noncurrent Assets		
Land		2,922
Buildings, Property and Equipment		48,515
Less Accumulated Depreciation and Amortization		(26,252)
Total Noncurrent Assets		25,185
Total Assets	$	2,916,024
LIABILITIES AND FUND EQUITY		
Current Liabilities		
Reserve for Loss and Loss Adjustment Expenses	$	166,692
Unearned Premiums		45,781
Accounts and Interest Payable		27,273
Due to Brokers for Security Purchases		35,876
Obligations Under Securities Lending		151,132
Due to Other Governments		4,876
Deferred Revenue		21,940
Compensated Absences Payable		3,026
Total Current Liabilities		456,596
Noncurrent Liabilities		
Reserve for Loss and Loss Adjustment Expenses		2,096,240
Total Noncurrent Liabilities		2,096,240
Total Liabilities		2,552,836
Fund Equity		
Invested in Capital Assets		25,185
Restricted for Workers' Compensation		338,003
Total Fund Equity		363,188
Total Liabilities and Fund Equity	$	2,916,024

The notes to the financial statements are an integral part of this statement.

SAIF Corporation

Statement of Revenues, Expenses, and Changes in Fund Equity

For the Year ended December 31, 2002

(In Thousands)

		2002
Operating Revenues		
Net Premiums Earned	$	295,092
Net Investment Income		73,536
Other Income		23,100
Total Operating Revenues		391,728
Operating Expenses		
Salaries and Wages		54,990
Underwriting and Other Expenses		55,294
Loss and Dividend Expenses Incurred		335,011
Depreciation and Amortization		3,482
Bad Debt		1,741
Total Operating Expenses		450,518
Operating Loss	$	(58,790)
Change in Fund Equity	$	(58,790)
Fund Equity - Beginning		421,978
Fund Equity - Ending	$	363,188

The notes to the financial statements are an integral part of this statement.

SAIF Corporation

Statement of Cash Flows

For the Year ended December 31, 2002

(In Thousands)

		2002
Cash Flows from Operating Activities:		
Premiums Collected Net of Reinsurance	$	270,986
Payments to Employees for Services		(58,854)
Claims Paid		(192,634)
Other Payments		(33,989)
Net Cash Used in Operating Activities		(14,491)
Cash Flows from Capital and Related Financing Activities:		
Acquisition of Capital Assets		(1,870)
Proceeds from Disposition of Capital Assets		4,159
Net Cash Provided by Capital and Related Financing Activities		2,289
Cash Flows from Investing Activities:		
Purchases of Investments		(6,524,682)
Proceeds from Sales and Maturities of Investments		6,620,989
Interest on Investments and Cash Balances		112,839
Interest Income from Securities Lending		4,567
Interest Expense from Securities Lending		(3,802)
Net Cash Provided by Investing Activities		209,911
Net Increase in Cash and Cash Equivalents		197,709
Cash and Cash Equivalents - Beginning		182,730
Cash and Cash Equivalents - Ending	$	380,439

(continued)

SAIF Corporation

Statement of Cash Flows

For the Year ended December 31, 2002

(In Thousands)

Reconciliation of operating loss to net cash used in operating activities:

		2002
Operating Loss	$	(58,790)
Adjustments to Reconcile Operating Loss to Net Cash		
Provided (Used) by Operating Activities:		
Depreciation and Amortization		3,482
Bad Debt Expense		1,741
Interest Income Reported as Operating Revenue		(73,536)
Net Changes in Assets and Liabilities:		
Accounts and Interest Receivable, net		(43,879)
Inventories		38
Accounts and Interest Payable		1,838
Due to Other Governments		(830)
Reserve for Loss and Loss Adjustment Expenses		143,131
Unearned Premiums		7,747
Deferred Revenue		4,791
Compensated Absences Payable		(224)
Total Adjustments		44,299
Net Cash Used in Operating Activities	$	(14,491)
Noncash Investing and Capital and Related Financing Activities:		
Net Change in Fair Value of Investments (included as a component of Interest Income Reported as Operating Revenue above)	$	50,781

The notes to the financial statements are an integral part of this statement.

SAIF CORPORATION

Notes to the Financial Statements
Year ended December 31, 2002

(1) Description of Business & Regulatory Environment

SAIF Corporation (SAIF) is a public corporation created by an act of the Oregon Legislature. It traces its origins to 1914 when its predecessor organization commenced business.

SAIF is an insurance company authorized to write workers' compensation coverage in Oregon and certain other jurisdictions as required by the Department of Consumer and Business Services and to service accounts in the assigned risk pool. SAIF also provides coverage governed by the Longshoremens' and Harbor Workers' Compensation Act, Jones Act, and Federal Employers Liability Law. SAIF's Board of Directors is appointed by the Governor of the State of Oregon (the State) and consists of prominent Oregon business and community leaders, not otherwise in the employ of SAIF.

SAIF writes business on a direct basis and through agents. Premiums written on a direct basis were 32.4% during 2002.

The Department of Consumer and Business Services enforces workers' compensation laws under Oregon Revised Statutes (ORS).

(2) Summary of Significant Accounting Policies

Basis of Accounting

At the request of the Oregon Secretary of State's Audits Division, SAIF has prepared the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America for governmental entities. As a component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board. Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as an enterprise fund. Accordingly, SAIF follows the accrual basis of accounting. Revenues are recognized when earned, regardless of when received, and expenses are recognized when incurred, regardless of when paid.

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting,* SAIF only follows Statements of the Financial Accounting Standards Board issued prior to November 30, 1989.

Investments

SAIF reports certain investments at fair value in the balance sheet and recognizes the corresponding change in the fair value of investments in the year in which the change occurs as investment income. The custodial agent determines the fair value of debt and equity securities, using recognized pricing services or prices quoted by one or more independent brokers. Equity securities traded on a national exchange are valued at the last reported sales price. Debt securities are generally valued at the midpoint between the bid and asked prices. A small percentage of debt securities cannot be priced in this manner, and for these, a similar "benchmark" security is used. The benchmark has a coupon rate and maturity date comparable to the debt security being valued, and its market risk is similar considering current market conditions. Investments in leveraged buyouts representing private securities are valued at cost, or at fair market value as estimated by a recognized pricing service if a significant event has occurred which affects the value of the investment and warrants an adjustment to cost. Investments in leveraged buyouts representing publicly traded securities are stated at the quoted market price adjusted for a reasonable illiquidity discount. Mortgage loans on real estate and state agency loans are stated at the unpaid principal balance.

Realized investment gains and losses are determined using the specific identification method and are included as a component of net income upon the maturity or disposition of the investment. During 2002, SAIF realized a net gain of $12.8 million from sales of investments. The calculation of realized gains and losses is independent of the calculation of the net change in the fair value of investments. Realized gains and losses on investments held in more than one fiscal year and sold in the current year may have been recognized as a change in the fair value of investments reported in prior years. The net change in the fair value of investments during 2002 was a $50.8 million loss. This takes into account all changes in fair value (including purchases and sales) that occurred during the year. The net unrealized loss on investments at December 31, 2002 was $49.6 million.

Cash and Cash Equivalents

SAIF places its temporary cash investments with the Oregon Short Term Fund. The Oregon Short Term Fund is a cash and investment pool that operates as a demand deposit account. As a result, SAIF's investment is not impacted by changes in the market value of the Oregon Short Term Fund. By statute, the Oregon Short Term Fund may hold securities with maturities no greater than three years. The average maturity of the Oregon Short Term Fund as of December 31, 2002 was 93 days.

Oregon's State Treasurer employs the services of three external investment managers to manage SAIF's funds, one that manages a convertible bond portfolio and two that manage fixed income portfolios. The cash balances of the convertible bond manager are invested in the SSgA Money Market Fund, and the cash of the fixed income managers is invested in the State Street Short Term Investment Fund (STIF). Both funds seek to maximize current income while maintaining a stable $1.00 unit value by investing in high-quality, short maturity securities. The average maturity of the SSgA Money Market Fund as of December 31, 2002 was 55 days. The average maturity of the State Street STIF as of December 31, 2002 was 53 days.

Concentrations of Credit Risk

Financial instruments, which potentially subject SAIF to concentrations of credit risk, consist principally of temporary cash investments and debt securities. SAIF places its investment securities with high-credit quality financial institutions and limits the amounts of credit exposure to any one financial institution. Concentrations of credit risk with respect to investments in debt securities are limited due to the large number of such investments and their distribution among U.S. government bonds, many different industries and geographic regions.

Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation. Maintenance, repairs and minor renovations are charged to expense as costs are incurred. Upon retirement or sale, any resulting gain or loss is included as a component of net income. Property and equipment is capitalized and depreciated using the straight-line method over the estimated useful lives of the assets as follows:

	Capitalization Threshold	Useful Life
Buildings and improvements	all	30 to 40 years
Furniture, equipment, and machinery	$0 - $2,000	3 to 7 years
Data processing software	$500,000	3 to 5 years

Land, property and equipment activity for the year ended December 31, 2002 was as follows (dollars in thousands):

	Beginning Balance	Additions	Disposals	Ending Balance
Land	$ 2,922	$ -	$ -	$ 2,922
Buildings and improvements	25,444	-	-	25,444
Equipment	15,902	1,075	(2,551)	14,426
Data processing software	9,458	796	(1,608)	8,645
Totals at historical cost	53,726	1,870	(4,159)	51,437
Less accumulated depreciation for:				
Buidings and improvements	(6,807)	(722)	-	(7,529)
Equipment	(12,747)	(1,343)	2,479	(11,611)
Data processing software	(6,967)	(1,440)	1,295	(7,112)
Total accumulated depreciation	(26,521)	(3,505)	3,774	(26,252)
Land, property and equipment, net	$ 27,205	$ (1,635)	$ (385)	$ 25,185

Depreciation and amortization expense for the year ended December 31, 2002 was $3.5 million.

Premiums

Premiums are based on individual employers' reported payroll using predetermined insurance rates based on employee risk classifications and are recognized as income on a pro rata basis over the coverage period. Ceded premiums are recognized consistent with the underlying reinsurance agreement. The portion of premiums that will be earned in the future are deferred and reported as unearned premiums.

Policyholders' premiums due to SAIF are recorded as premiums receivable, net of the allowance for uncollectible accounts. Premiums receivable consists of both billed and unbilled amounts. Unbilled premiums receivable primarily represent an estimate of the difference between amounts earned ratably on installment-billed policies and the amount to be billed on the policy. Unbilled premiums receivable also include estimated billings on payroll reporting policies which were earned but not billed prior to year-end. SAIF uses its historical experience to estimate earned but unbilled amounts which are recorded as premiums receivable. These unbilled amounts are estimates, and while SAIF believes such amounts are reasonable, there can be no assurance the amounts ultimately received will equal the recorded unbilled amounts. The ultimate collectibility of the unbilled receivables can be affected by general changes in the economy and the regulatory environment due to the increased time required to determine the billable amount. SAIF considers these factors when estimating the receivable for unbilled premiums. Unbilled premiums receivable at December 31, 2002 were $53.7 million.

Certain policyholders are required to remit deposits which represent premium expected to be payable to SAIF at the end of the month following the reporting period (monthly and quarterly), plus one additional month. Deposits are generally in the form of cash, and are recorded in policyholders' premium deposits. However, policyholders may pledge surety bonds and securities in lieu of cash deposits. At December 31, 2002 there were no pledged bonds and securities.

In addition to its regular premium plans, SAIF offers employers retrospective premium rating plans under which premiums are adjusted annually for up to 4-1/2 years following the plan year based on policyholders' loss experience. Adjustments to the original premiums are paid to or collected from the policyholders six months following the expiration of the policy and annually thereafter for up to 4-1/2 years. The estimate of the net accrued premiums receivable for retrospective rating plans as of December 31, 2002 is as follows (dollars in thousands):

		2002
Accrued retrospective premiums receivable	$	54,107
Reserve for retrospective rating plans		(12,171)

These amounts are included in the accompanying balance sheet.

Reserve for Loss and Loss Adjustment Expenses

The reserve for loss and loss adjustment expenses is generally based on past experience, except for certain awarded claims which are determined on an individual case basis. The liability includes provisions for reported claims, claims incurred but not reported, and claims that are currently closed but which experience indicates will be reopened.

Management believes that the reserve for incurred but unpaid loss and loss adjustment expenses at December 31, 2002 is a reasonable estimate of the ultimate net costs of settling claims and claims expenses incurred. Actual claim costs depend upon such factors as duration of worker disability, medical cost trends, occupational disease and inflation, and other societal and economic factors. As a result, the process used in computing the ultimate cost of settling claims and expense for administering claims is necessarily based on estimates. The amount ultimately paid may be more or less than such estimates. Adjustments resulting from changes in estimates of these liabilities are charged or credited to operations in the period in which they occur (see note 4).

Currently, SAIF discounts the reserve for known unpaid fatal and permanent total disability losses. SAIF does not discount the reserve for unpaid fatal and permanent total disability loss adjustment expenses. Oregon Attorney General Opinion Number 6176 requires SAIF to use the discount rate that reflects the anticipated rate of return on investments taking into consideration the uncertainty inherent in long payout patterns. The discount rate used by SAIF is 3.5% at December 31, 2002. Annually, the Board of Directors reviews the actuarial assumptions and discount rates utilized in determining the liability for such losses. The tabular discounts reflected in the reserve for loss and loss adjustment expenses were $101.1 million at December 31, 2002.

Managed Care Organization Fees

SAIF contracts with managed care organizations (MCOs). MCOs manage claims by arranging to provide medical and health care services. The expense is based on the number of claims accepted and closed while managed by an MCO. During 2002 claims covered by contracts with MCOs were approximately 86% of total claims.

Premium Deficiency

At December 31, 2002, no reserve for premium deficiency was required to be recorded. Premium deficiency is based upon an estimate of the amount by which the sum of anticipated claims costs, claims adjustment expenses and maintenance expenses exceeds expected premium income and earnings on investments.

Policyholders' Dividends

Substantially all of SAIF's business is written under various participating plans wherein a dividend may be returned to the policyholder. Estimated amounts to be returned to policyholders are accrued when the related premium is earned. Dividends may be paid to the extent that a surplus is accumulated from premiums, investment gains, or loss reserve reductions. Activity for 2002 resulted in a net credit of $570 thousand.

Taxes and Assessments

The Oregon Department of Justice has determined that SAIF is exempt from federal taxes, because it is an integral part of the State of Oregon and, alternatively, exempt under either or both sections 501(c)(27)(B) and 115(1) of the Internal Revenue Code.

SAIF is subject to levies by the Oregon Workers' Compensation Division of the Department of Consumer and Business Services. Such assessments constitute an in-lieu-of-tax relative to premiums. Premium assessments were $23.1 million for the year ended December 31, 2002.

Use of Estimates

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

Current Accounting Pronouncements

The GASB has issued Statement No. 39, *Determining Whether Certain Organizations are Component Units*. The impact from adopting this statement did not have a material effect on SAIF's financial position or operations. The requirements of this statement were effective for the fiscal year ended December 31, 2002.

(3) Cash, Cash Equivalents and Investments

Cash and Cash Equivalents

Cash on deposit in state banks is covered by federal deposit insurance or is secured by the State Treasury at a minimum of 25% as required by statutes. Amounts held in the Oregon Short Term Fund are insured or secured by securities held by the State Treasurer or by its agent in the Treasurer's name. Deposits at the custodian bank are neither collateralized nor insured, but are backed by the full faith and credit of the custodian bank. The difference between the carrying amount and bank balance consists primarily of deposits in transit and outstanding checks.

Investments

Oregon's State Treasurer acts as SAIF's investment officer, investing in any instrument in which persons of prudence, discretion and intelligence would invest for their own accounts. The Oregon Investment Council establishes SAIF's investment policy.

SAIF adopted GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and External Investment Pools" effective January 1, 1997. GASB Statement No. 31 requires governmental entities to report certain investments at fair value in the balance sheet and recognize the corresponding change in the fair value of investments in the year in which the change occurred. Changes in the fair value of investments are recorded as investment income (loss) in the current year.

Cash collateral received in respect of securities loans is invested in the custodial agent's short-term fund, an "external investment pool" for purposes of GASB Statement No. 31. SAIF's participation in this fund is voluntary. The fair value of investments held by this fund is based upon valuations provided by a recognized pricing service. This fund is not registered with the Securities and Exchange Commission, but the custodial agent is subject to the oversight of the Federal Reserve Board and the Massachusetts Commissioner of Banks. The fair value of SAIF's position in this fund is not the same as the value of the fund's shares, because unrealized gains and losses on the fund's investments included in fair value are not distributed to fund participants. No income from this fund was assigned to another fund by the custodial agent during the year.

Bond, mortgage-backed, asset-backed, and equity security transactions are recorded on a trade date basis, generally three business days prior to the settlement date. However, the number of days between trade and settlement dates for mortgage-backed securities can be up to 30 days or longer depending on the security. Due from brokers for security sales at December 31, 2002 was $30.1 million. Due to brokers for security purchases at December 31, 2002 was $35.9 million.

Investments in FNMA and GNMA TBA securities are not included in the financial statements, as it is not probable that SAIF will ultimately take delivery of the underlying securities. These investments provide an additional opportunity to invest excess cash and participate in the market movements of the underlying securities. At December 31, 2002, SAIF had entered into TBA contracts totaling $422.1 million. The unrealized gain on these contracts was $2.3 million and is included in investments and net investment income in the accompanying financial statements. The underlying investments will be recorded in future periods if and when SAIF takes delivery of the securities.

The majority of SAIF investments are classified in three categories of credit risk to give an indication of the level of risk assumed by SAIF at December 31, 2002. The three categories of credit risk are:

1. Insured or registered, or securities held by the State of Oregon or its agent in the State of Oregon's name for SAIF;

2. Uninsured and unregistered with securities held by the counterparty's trust department or agent in the State of Oregon's name for SAIF; and

3. Uninsured and unregistered with securities held by the counterparty, or by its trust department or agent but not in the State of Oregon's name for SAIF.

SAIF's investments by category at December 31, 2002 are as follows (dollars in thousands):

	Category I	Not Required to be Categorized	Carrying Amount
Bonds:			
U.S. Government	$ 134,800	$ 94,069	$ 228,869
Corporate Bonds	784,123	39,469	823,592
International Bonds	105,166	12,286	117,452
Asset Backed Securities	676,739	-	676,739
Total Bonds	1,700,828	145,824	1,846,652
Equity Securities:			
Russell 3000 Pooled Equity Fund	-	306,837	306,837
Other Equity Securities	15,035	227	15,262
Total Equity Securities	15,035	307,064	322,099
Other Invested Assets	-	10,084	10,084
Mortgage Loans on Real Estate	-	1,093	1,093
Total Investments	$ 1,715,863	$ 464,065	$ 2,179,928

There were no Category 2 or 3 investments at December 31, 2002.

The amortized cost and fair value of investments at December 31, 2002 is as follows (dollars in thousands):

	Cost or Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Bonds:				
U.S. Treasury securities and Obligations of U.S. Government Corporations and Agencies	$ 209,587	$ 23,143	$ (100)	$ 232,630
International Bonds	193,682	14,495	(6,176)	202,001
Corporate Bonds	748,061	42,716	(25,735)	765,042
Asset Backed Securites	629,007	18,535	(563)	646,979
Total Bonds	1,780,337	98,889	(32,574)	1,846,652
Equity Securities:				
Russell 3000 Pooled Equity Fund	416,844	-	(110,007)	306,837
Other Equity Securities	19,506	16	(4,260)	15,262
Total Equity Securities	436,350	16	(114,267)	322,099
Other Invested Assets	11,736	-	(1,652)	10,084
Mortgage Loans on Real Estate	1,091	2	-	1,093
Total Investments	$ 2,229,514	$ 98,907	$ (148,493)	$ 2,179,928

The amortized cost and fair value of debt securities at December 31, 2002, by contractual maturity, are shown below. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties (dollars in thousands).

	Amortized Cost	Fair Value
Due in one year or less	$ 179,107	$ 182,506
Due after one year through five years	530,449	541,969
Due after five years through ten years	498,197	517,979
Due after ten years	572,584	604,198
Total	$ 1,780,337	$ 1,846,652

Net investment income is comprised of the following for the year ended December 31, 2002 (dollars in thousands):

	2002
Bonds	$ 167,720
Equity securities	(95,644)
Mortgage loans on real estate	120
Other	8,099
Investment income	80,295
Less investment expense	(6,759)
Net investment income	$ 73,536

Net realized gains and losses on sales of investments, which are included in net investment income, consist of the following for the year ended December 31, 2002 (dollars in thousands):

		2002
Gains:		
Bonds	$	69,537
Equity securities		4,424
Other invested assets		17
Total	$	73,978
Losses:		
Bonds	$	(43,706)
Equity securities		(17,432)
Other invested assets		(23)
Total	$	(61,161)
Net:		
Bonds	$	25,831
Equity securities		(13,008)
Other invested assets		(6)
Total	$	12,817

Proceeds from the sales of investments in debt securities for the year ended December 31, 2002 were $6,242.2 million.

Securities Lending

In accordance with State investment policies, SAIF participates in securities lending transactions. The Oregon State Treasury has, through a Securities Lending Agreement, authorized State Street Bank and Trust Company ("State Street") to lend SAIF's securities to broker-dealers and banks pursuant to a form of loan agreement. Both SAIF and the borrowers maintained the right to terminate all securities lending transactions on demand. There have been no significant violations of the provisions of securities lending agreements.

During the year, State Street lent SAIF's fixed income and equity securities and received as collateral U.S. dollar-denominated cash. Borrowers were required to deliver cash collateral for each loan equal to at least 102% of the fair value of the loaned security, or 105% in the case of international equity securities. SAIF did not impose any restrictions during the year on the amount of the loans State Street made on its behalf. SAIF was fully indemnified by State Street against losses due to borrower default, and there were no losses during the year from the failure of borrowers to return loaned securities.

State Street is authorized by the Securities Lending Agreement to invest cash collateral received for securities loans in the State Street Bank and Trust Company Oregon Short-Term Investment Fund ("Fund"). The fair value of SAIF's position in this fund is not the same as the value of the fund's shares, because unrealized gains and losses on the fund's investments included in its fair value are not distributed to fund participants. At December 31, 2002 the Fund had an average weighted maturity of 347 days. Since the securities loans are callable on demand by either the lender or borrower, the life of the loans at December 31, 2002 is effectively one day and consequently does not generally match the life of the investments in the Fund. On December 31, 2002 SAIF had no credit risk exposure to borrowers. The collateral held and the fair value including accrued income of the SAIF securities on loan at December 31, 2002 were $151.1 million and $148.0 million, respectively.

Derivatives

In accordance with the investment policies of the State of Oregon, the Oregon State Treasury has invested through its outside investment managers on behalf of SAIF in the following types of securities which may be considered derivatives: asset-backed securities, including collateralized mortgage obligations, FNMA and GNMA TBA securities, and floating-rate bonds. Derivatives are generally used to enhance the return while managing the overall risk of investment portfolios.

Below is a summary of derivative instruments held by SAIF at December 31, 2002. The credit risk, market risk, and legal risk for these investments were not above and beyond those risks that are apparent in the financial statements or otherwise disclosed in the notes to the financial statements.

Asset-backed securities: The fair values of SAIF's holdings of asset-backed securities at December 31, 2002 are: collateralized mortgage obligations, $121.6 million; securities collateralized by the revenue streams from auto loan portfolios $26.5 million; securities collateralized by credit card receivables, $4.2 million; other asset-backed securities, $184.7 million.

SAIF participates in a short-term investment fund maintained by the custodial agent in which the cash collateral received from securities loans is invested. At December 31, 2002, SAIF's balance in the fund totals $152.2 million at fair value. Investments in asset-backed securities collateralized by the revenue streams from credit card and auto loan portfolios account for 22.2% of the total fair value of the fund at December 31, 2002.

Floating rate bonds: At December 31, 2002, SAIF holds $158.6 million in corporate bonds with floating interest rates. The coupon rates on these bonds are reset either monthly or quarterly with reference to the LIBOR (London Interbank Offered Rate).

Mutual Fund Derivative Holdings: As of December 31, 2002, an equity index fund owned by SAIF held $838 thousand of futures contracts on equity indexes similar to the underlying fund holdings. These contracts represent approximately 0.3% of the market value of the fund.

(4) Reserve for Loss and Loss Adjustment Expenses

SAIF has established a reserve for both reported and unreported insured events, which includes estimates of future payments of losses and related loss adjustment expenses. In estimating the reserve for loss and loss adjustment expenses, SAIF considers prior experience, industry information, currently recognized trends affecting data specific to SAIF and other factors relating to workers' compensation insurance underwritten by SAIF.

The following table provides a reconciliation of the beginning and ending reserve for loss and loss adjustment expenses for the year ended December 31, 2002 (dollars in thousands):

	2002
Reserve for loss and loss adjustment expenses, beginning of year, discounted	$ 2,119,801
Add: Discount of reserve for loss and loss adjustment expenses	91,869
Reserve for loss and loss adjustment expenses, beginning of year, undiscounted	2,211,670
Incurred losses:	
Provision for insured events of the current year	380,413
Provision for insured events of prior year	(13,419)
Total incurred losses	366,994
Loss payments attributable to:	
Insured events of the current year	(78,004)
Insured events of prior year	(136,605)
Total payments	(214,609)
Reserve for loss and loss adjustment expenses, end of year, undiscounted	2,364,055
Less: Discount of reserve for loss and loss adjustment expenses	101,123
Reserve for loss and loss adjustment expenses, end of year, discounted	$ 2,262,932

The favorable loss reserve development disclosed above was primarily due to fewer serious losses than expected. Prior year loss reserves for indemnity costs declined $18.1 million while medical reserves on permanent partial disability losses declined $13.9 million. As a result of favorable frequency development, the Company lowered its assumption of future permanent total disability claims, which had a favorable impact of $11.2 million on loss reserves.

Rising medical cost throughout the year caused an increase in loss reserves and partially offset the favorable development discussed above. During the year, actual medical inflation was near 14%, which exceeded the explicit inflation assumption used in the loss reserve estimates. SAIF believes higher levels of medical inflation will continue in the near future and adjusted the inflation assumptions accordingly. This refinement in the assumption increased loss reserves approximately $49.0 million.

(5) Reinsurance

In the ordinary course of business, SAIF cedes premiums for purposes of risk diversification and limiting maximum loss exposure from catastrophic events through contractual agreements with reinsurers. If such assuming reinsurers are unable to meet the obligations assumed under these reinsurance agreements, SAIF would be liable to pay the obligation. To minimize its exposure to significant losses from reinsurer insolvencies, SAIF evaluates the financial condition of its reinsurers and monitors concentration of credit risk.

Effective October 1, 2002, SAIF acquired reinsurance protection providing limits of $70 million excess of $30 million per occurrence with a $2 million maximum on any one life and a $140 million aggregate limit. This reinsurance protection excludes coverage for nuclear, biological, or chemical terrorist attacks. SAIF has reinsurance protection for 90% of losses in excess of 7% of 2002 direct earned premiums for acts of foreign terrorism through the Federal Reinsurance Act.

The following amounts have been deducted in the accompanying financial statements as a result of reinsurance ceded (dollars in thousands):

		2002
Reserve for loss and loss adjustment expenses	$	17,386
Premiums written and earned		1,063
Loss and loss adjustment expenses incurred		2,395

SAIF is authorized to write business on behalf of the Oregon Workers' Compensation Insurance Plan (the Plan), administered by the National Council on Compensation Insurance through the National Workers' Compensation Reinsurance Pool. The Plan provides a guaranteed source of workers' compensation insurance for employers unable to obtain coverage because of unstable financial condition, poor loss experience, or the inherently dangerous nature of the work. SAIF cedes such business to the Plan. In addition, SAIF is also required to assume its share of premiums and losses from the Plan based on voluntary market share.

The following amounts are included in the accompanying financial statements as a result of participation in the Plan (dollars in thousands):

		2002
Assumed:		
Reserve for loss and loss adjustment expenses	$	42,034
Unearned premiums		1,838
Premiums written		18,680
Premiums earned		18,152
Loss and loss adjustment expenses incurred		16,645
Ceded:		
Reserve for loss and loss adjustment expenses	$	63,629
Unearned premiums		3,820
Premiums written		18,636
Premiums earned		17,062
Loss and loss adjustment expenses incurred		13,839

(6) Lease Commitments

SAIF leases office space in several locations under noncancelable operating leases expiring during various years through 2005. Lease expense was $581 thousand for the year ended December 31, 2002.

SAIF's future minimum lease payments under operating leases at December 31, 2002 is as follows (dollars in thousands):

2003	$	547
2004		380
2005		217
Total minimum lease payments	$	1,144

Certain rental commitments have renewal options extending through the year 2010. Some of these renewals are subject to adjustments in future periods. Total minimum lease payments have not been reduced by minimum sublease rentals of approximately $302 thousand on leases due in the future under noncancelable subleases as of December 31, 2002.

(7) Risk Management

The State of Oregon administers property and casualty insurance programs covering State government agencies through its Insurance Fund. The Insurance Fund services claims for: direct physical loss or damage to State property; tort liability claims brought against the State, its officers, employees, or agents; workers' compensation; and employees, elected officials, and members of commissions and boards for honesty and faithful performance. The Insurance Fund is backed by a commercial excess property policy with limits of $400 million and a blanket commercial excess bond with limits of $10 million.

As a state agency, SAIF participates in the Insurance Fund. The cost of servicing insurance claims and payments is covered by charging an assessment to each State entity based on its share of services provided in a prior period. The total statewide assessment of each coverage is based on independent biennial actuarial forecasts and administrative expenses, less carry-forward or equity in the Insurance Fund. Assessments for the year ended December 31, 2002 were $306 thousand.

(8) Contingencies

During the ordinary course of business, SAIF becomes involved in litigation arising out of matters incident to the conduct of its insurance operations. SAIF is represented in these actions by the Attorney General of the State of Oregon. In the opinion of management, based upon information furnished by counsel, the ultimate disposition of these actions will not have a material adverse effect on SAIF's financial position or results of operations.

(9) Deferred Compensation Plan

A deferred compensation plan (Plan) was authorized under Internal Revenue Code Section 457 and ORS 243.400 to 243.495. The Plan is a benefit available to all SAIF employees wherein they may execute an individual agreement with SAIF to defer a portion of their current income until future years so as to shelter such funds from federal and state taxation until withdrawal. Participants cannot receive the funds until certain circumstances are met. Funds accumulated by SAIF under the Plan have been invested with various financial institutions and insurance companies. Plan assets are held in a custodial account or an annuity contract by the Plan provider for the exclusive benefit of the participants or beneficiary. Participants' rights under the Plan are equal to the fair market value of the deferred account for each participant.

(10) Retirement Plan

SAIF's employees participate in the Oregon Public Employees' Retirement System (PERS); a cost-sharing multiple-employer defined benefit pension plan. PERS is administered by the Public Employees Retirement Board under the guidelines of ORS Chapter 238. The PERS retirement allowance, payable monthly for life, may be selected from twelve retirement benefit options. Options include survivorship benefits and lump sum refunds. The basic benefit formula is 1.67% of a member's final average salary multiplied by the member's number of years of service. Benefits may also be calculated under either a money match or an annuity-plus-pension computation if a greater benefit results. PERS also provides death and disability benefits. A copy of the Oregon Public Employees' Retirement System annual financial report may be obtained from PERS, P.O. Box 23700, Tigard, Oregon 97281-3700.

All SAIF employees are eligible to participate in PERS after completing six months of service. Covered employees are required by state statutes to contribute 6.0% of their salary to the plan. Current law permits employers to pay employee contributions to PERS and SAIF elects to do so. SAIF is required by statute to contribute actuarially computed amounts as determined by PERS. Rates are subject to change as a result of subsequent actuarial valuations. Currently the rate is 9.49% of each covered employee's salary. The amounts contributed by SAIF for the years ended December 31, 2002, 2001, and 2000 were \$6.6 million, \$6.4 million, and \$6.2 million, respectively. SAIF employer contributions for the years ended December 31, 2002, 2001, and 2000 were \$4.1 million, \$3.9 million, and \$3.8 million, respectively, which is equal to the required contributions for the year. Employee contributions paid by SAIF for the years ended December 31, 2002, 2001, and 2000 were \$2.5 million, \$2.5 million, and \$2.4 million, respectively. In accordance with GASB Statement No. 27, no pension liability existed at December 31, 2002.