SAIF Corporation

(A Component Unit of the State of Oregon)

Financial Statements as of and for the Years Ended December 31, 2008 and 2007, and Independent Auditors' Report

SAIF CORPORATION

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OVERVIEW OF SAIF CORPORATION FINANCIAL REPORTING

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 dependents, whereas generally accepted accounting principles (GAAP) are based on the going-concern concept and recognize revenues when earned and expenses when incurred.

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 discrete component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board (GASB). Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as a special purpose government engaged solely in business-type activities. 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. GAAP requires 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 if the collateral received is not available for the general use of the transferor.

- 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 "nonadmitted" and removed from the balance sheet. Those assets, such as property and equipment, are included on the GAAP financial statements.

KPMG LLP
Suite 3800
1300 South West Fifth Avenue
Portland, OR 97201

Independent Auditors' Report

The Board of Directors of
SAIF Corporation:

The Secretary of State Audits Division of
the State of Oregon:

We have audited the accompanying financial statements of SAIF Corporation (SAIF), a component unit of the State of Oregon, as of and for the years ended December 31, 2008 and 2007, as listed in the table of contents. These financial statements are the responsibility of SAIF's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of SAIF's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of SAIF Corporation as of December 31, 2008 and 2007, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 18, 2009 on our consideration of SAIF's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

KPMG

Management's discussion and analysis and postemployment healthcare benefit plan schedule of funding progress on pages 4 through 11 and page 35, respectively, are not a required part of the basic financial statements but are supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

KPMG LLP

August 18, 2009

SAIF CORPORATION
Management's Discussion and Analysis
December 31, 2008 and 2007

Management of SAIF Corporation (SAIF) prepares Management's Discussion and Analysis for readers of SAIF's financial statements. This narrative overview and analysis of the financial activities of SAIF is as of and for the years ended December 31, 2008 and 2007. Readers are encouraged to consider this information in conjunction with SAIF's financial statements and notes that follow.

Financial Statements

This discussion and analysis is intended to serve as an introduction to SAIF's financial statements: the Balance Sheet; the Statement of Revenues, Expenses, and Changes in Fund Equity; and the Statement of Cash Flows. The financial statements are designed to provide the readers with an overview of SAIF's financial position and activities.

The Balance Sheet presents information on SAIF's assets and liabilities, with the difference between the two reported as fund equity. Assets and liabilities are classified as either current or noncurrent.

The Statement of Revenues, Expenses, and Changes in Fund Equity is SAIF's income statement. Revenues earned and expenses incurred during the year are classified as either operating or nonoperating.

The Statement of Cash Flows presents the changes in SAIF's cash and cash equivalents during the year. This statement is prepared using the direct method of cash flows. The statement breaks out the sources and uses of SAIF's cash and cash equivalents into the following categories: operating activities, investing activities, and capital and related financing activities.

Condensed Financial Information
(In thousands)

Condensed Balance Sheet Information

	December 31, 2008	December 31, 2007	December 31, 2006	2007 to 2008 Increase (Decrease)	2006 to 2007 Increase (Decrease)
ASSETS					
CURRENT ASSETS:					
Cash and cash equivalents	$ 39,478	$ 39,862	$ 53,301	$ (384)	$ (13,439)
Investments	3,398,861	3,597,781	3,402,120	(198,920)	195,661
Securities lending cash collateral	439,181	570,060	648,185	(130,879)	(78,125)
Accounts and interest receivable, net	371,001	377,502	229,813	(6,501)	147,689
Receivable for securities sold	132	280	959	(148)	(679)
Other assets	8,354	8,246	2,075	108	6,171
Total current assets	4,257,007	4,593,731	4,336,453	(336,724)	257,278
NONCURRENT ASSETS—Capital assets	19,345	19,666	19,797	(321)	(131)
TOTAL ASSETS	$ 4,276,352	$ 4,613,397	$ 4,356,250	$ (337,045)	$ 257,147
LIABILITIES AND FUND EQUITY					
CURRENT LIABILITIES:					
Reserve for losses and loss adjustment expenses	$ 209,139	$ 213,498	$ 218,910	$ (4,359)	$ (5,412)
Unearned premiums	198,736	207,800	76,570	(9,064)	131,230
Accounts payable	52,090	58,024	42,609	(5,934)	15,415
Due to brokers for security purchases	5	5	2	-	3
Obligations under securities lending	465,208	570,060	648,185	(104,852)	(78,125)
Other liabilities and deposits	54,200	46,802	50,386	7,398	(3,584)
Total current liabilities	979,378	1,096,189	1,036,662	(116,811)	59,527
NONCURRENT LIABILITIES:					
Reserve for losses and loss adjustment expenses	2,702,170	2,591,867	2,467,491	110,303	124,376
Other noncurrent liabilities	472	244	1,247	228	(1,003)
Total noncurrent liabilities	2,702,642	2,592,111	2,468,738	110,531	123,373
Total liabilities	3,682,020	3,688,300	3,505,400	(6,280)	182,900
FUND EQUITY:					
Invested in capital assets	19,345	19,666	19,797	(321)	(131)
Unrestricted	574,987	905,431	831,053	(330,444)	74,378
Total fund equity	594,332	925,097	850,850	(330,765)	74,247
TOTAL LIABILITIES AND FUND EQUITY	$ 4,276,352	$ 4,613,397	$ 4,356,250	$ (337,045)	$ 257,147

Condensed Revenues, Expenses, and Changes in Fund Equity Information

	Years Ended December 31, 2008	2007	2006	2007 to 2008 Increase (Decrease)	2006 to 2007 Increase (Decrease)
OPERATING REVENUES:					
Net premiums earned	$ 416,016	$ 459,977	$ 437,984	$ (43,961)	$ 21,993
Other income	23,553	20,267	25,519	3,286	(5,252)
Total operating revenues	439,569	480,244	463,503	(40,675)	16,741
OPERATING EXPENSES:					
Net losses and loss adjustment expenses incurred	436,079	435,297	407,854	782	27,443
Policyholders' dividends	-	59,979	-	(59,979)	59,979
Underwriting expenses	89,459	88,972	92,322	487	(3,350)
Other expenses	2,300	-	856	2,300	(856)
Total operating expenses	527,838	584,248	501,032	(56,410)	83,216
OPERATING LOSS	(88,269)	(104,004)	(37,529)	15,735	(66,475)
NONOPERATING REVENUES:					
Net investment income (loss)	(242,496)	178,251	208,242	(420,747)	(29,991)
INCREASE (DECREASE) IN FUND EQUITY	$ (330,765)	$ 74,247	$ 170,713	$ (405,012)	$ (96,466)
FUND EQUITY—Beginning of year	925,097	850,850	680,137	74,247	170,713
FUND EQUITY—End of year	$ 594,332	$ 925,097	$ 850,850	$ (330,765)	$ 74,247

Financial Position as of December 31, 2008

At the end of 2008, total assets decreased $337.1 million from the prior year. Total liabilities decreased $6.3 million for the year, and fund equity decreased $330.8 million.

Significant changes include:

Cash and Cash Equivalents—The majority of SAIF's cash accounts consist of short-term investments and funds utilized by external investment managers. Cash and cash equivalents decreased $0.4 million from December 31, 2007 to December 31, 2008.

Investments—At the end of 2008, investments were $198.9 million or 5.5 percent less than at the end of 2007. The decrease was due to significant declines in market values. While investment holdings (principal and cost) increased $125.1 million for bonds and $17.9 million for equities due to positive cash flow from operations and the reinvestment of investment income, this was offset by declines in market values of $127.1 million for bonds and $214.8 million for equities. SAIF's Russell 3000 pooled equity fund investment had a negative return of 37.1 percent for the year.

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 SAIF's portfolio.

Accounts and Interest Receivable—The balance in this line is comprised of investment income receivable, net premiums receivable, accrued retrospective premiums receivable, and other accounts receivable. This balance decreased $6.5 million or 1.7 percent from December 31, 2007 to December 31, 2008.

Accrued investment income increased $3.3 million or 9.3 percent from December 31, 2007 to December 31, 2008, due to growth in principal and increasing bond yields.

Premiums receivable increased $16.2 million or 6.5 percent in 2008, primarily due to the completion of the migration of accounts from the installment method to the annualized method during 2007. This increase was partially offset by a decline in written premium during the current year. The migration resulted in a $28.8 million increase in the earned but unbilled premiums receivable balance in 2008 primarily related to retrospectively rated policies. The current year was the first year all policies were accounted for using the annualized method. The annualized method records written premium up front (at policy inception) for the entire policy term. Under the annualized method, the entire premium is recorded as premiums receivable – deferred and not yet due (asset) and unearned premium (liability) at policy inception.

Accrued retrospective premiums receivable decreased $23.0 million or 30.7 percent due to favorable loss development for certain retrospectively rated policies.

Other accounts receivable decreased $3.0 million or 18.5 percent, primarily due to a $2.2 million reduction in the amount due from the assigned risk pool.

Reserve for Losses and Loss Adjustment Expenses—The total (current and non-current) reserve for losses and loss adjustment expenses (LAE) increased $105.9 million or 3.8 percent from the prior year. Loss reserves increased $81.6 million or 3.2 percent and LAE reserves increased $24.3 million or 8.5 percent during 2008. Loss reserves for the 2008 accident year were offset somewhat by favorable loss reserve development of $37.3 million related to prior accident years.

The favorable development from prior years recognized in 2008 can be attributed to a number of factors. Claim count development was lower than expected. The methods used to estimate ultimate settlement fees and vocational rehabilitation expenses were revised, resulting in lower tail factors. Prior year development for indemnity reserves was unfavorable due to case reserve strengthening, partially offsetting the favorable loss development. This was offset by unfavorable LAE development largely attributed to an update of SAIF's internal expense allocation in 2008. Additional resources have been allocated to the loss adjustment function, resulting in a reserve increase.

Unearned Premiums—The amount of unearned premium for 2008 decreased $9.1 million or 4.4 percent due to the decline in written premium.

Accounts Payable—The balance in this line is comprised of commissions payable, reinsurance payable, accrued premium assessment, and other accounts payables. The $5.9 million decrease in this line item is due primarily to a $4.6 million reduction in reinsurance payable. The decrease is the result of a reduction in the liability for premiums ceded to the assigned risk pool. A decline in written premium resulted in a $660 thousand decrease in commissions payable, and a $2.7 million or 18.0 percent decrease in premium assessment payable. This reduction is offset by a $2.1 million increase in other accounts payable, primarily from policyholder credit balances.

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 SAIF's portfolio.

Other Liabilities and Deposits—The balance in this line is comprised of accrued retrospective premiums payable, premium deposits, amounts due to other governments, and compensated absences payable. This balance increased $7.4 million or 15.8 percent from the prior year due primarily to a $9.8 million increase in the estimated amount of return premium payable on retrospectively rated policies, because of favorable loss development experience for certain retrospectively rated policies. This increase was partially offset by a $2.2 million decrease in premium deposits.

Operations - Year Ended December 31, 2008

Significant changes in revenues and expenses include:

Net Premiums Earned—Net premiums earned decreased $44.0 million or 9.6 percent compared to 2007 as a result of the faltering economy and a pure premium rate reduction averaging 2.3 percent in 2008. For the first time in at least 15 years, the amount of payroll reported by policyholders declined from the prior year.

Other Income—Other income increased $3.3 million or 16.2 percent from 2007 to 2008. This is primarily due to an increase in earned but unbilled premium assessment income and an increase in employer interest and penalties.

Net Losses and Loss Adjustment Expenses Incurred—Net losses incurred for 2008 decreased by $36.8 million from 2007 while net LAE incurred increased $37.6 million for a total net increase of $0.8 million. Incurred losses declined from the prior year as favorable loss reserve development related to prior accident years partially offset losses incurred for the current accident year. LAE incurred increased $37.6 million due to unfavorable reserve development largely attributed to an update of SAIF's internal expense allocation in 2008. Additional resources were allocated to the loss adjustment function, resulting in an increase to both the reserve and paid loss adjustment expenses.

Policyholders' Dividends—Substantially all of SAIF's business is written under various participating plans wherein a dividend may be returned to the policyholder. Dividends may be paid to the extent that a surplus is accumulated from premiums, investment gains, or loss reserve reductions. No policyholder dividends were declared or paid in 2008. A $60.0 million dividend was declared and paid during 2007.

Underwriting Expense—This line increased by $0.5 million or 0.6 percent in 2008.

Net Investment Income—Investment income for 2008 was $420.7 million less than the amount recorded for 2007, primarily due to significant declines in both bond and equity market values. The change in fair value of investments recorded for 2008 was a negative $368.0 million compared to a positive $14.1 million for 2007. Interest income from bonds increased $11.5 million from the prior year due to growth in principal and increasing yields.

Financial Position as of December 31, 2007

At the end of 2007, total assets were $257.1 million greater than the prior year. Total liabilities increased $182.9 million for the year, while fund equity increased $74.2 million.

Significant changes include:

Cash and Cash Equivalents—The majority of SAIF's cash accounts consist of short-term investments and funds utilized by external investment managers. Cash and cash equivalents may fluctuate significantly from period to period as the investment managers trade securities or anticipate changing market conditions. Cash and cash equivalents decreased $13.4 million from December 31, 2006 to December 31, 2007.

Investments—At the end of 2007, investments were $195.7 million greater than at the end of 2006. The increase was primarily due to an increase of $191.5 million in bond investments and a $4.2 million increase in equity investments. Investments grew due to a positive cash flow from operations, the reinvestment of investment income, and an increase in the net unrealized gain on investments. The net unrealized gain on the bond holdings was $232.9 thousand less than the amount recorded for 2006. The net unrealized gain on the equity holdings was $14.3 million more in 2007 than in 2006. SAIF's Russell 3000 index holdings had a positive return of 3.3 percent for the year.

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 SAIF's portfolio.

Accounts and Interest Receivable—The balance in this line is comprised of investment income receivable, net premiums receivable, accrued retrospective premiums receivable, and other accounts receivable. This balance increased 64.3 percent from December 31, 2006 to December 31, 2007. Premiums receivable, including retrospective premiums receivable, increased 75.1 percent in 2007 due primarily to the continued migration of accounts from the installment method to the annualized method. The installment method records written premium in installments over the policy term as premiums are billed. The annualized method records written premium up front (at policy inception) for the entire policy term. Under the annualized method, the entire premium is recorded as premiums receivable – deferred and not yet due (asset) and unearned premium (liability) at policy inception.

Accrued investment income increased 11.9 percent from December 31, 2006 to December 31, 2007, due to the increase in the size of the bond portfolio and improving bond yields.

Receivable for Securities Sold—The amount receivable for securities sold at the end of 2007 was $679 thousand less than the prior year due to a decrease in pending security trade settlements at year-end 2007.

Other Assets—The amount reported for other assets was $8.2 million and $2.1 million at December 31, 2007 and 2006, respectively. Deferred acquisition costs increased $6.2 million as a result of an increase in unearned premiums.

Reserve for Losses and Loss Adjustment Expenses—Loss reserves increased $125.7 million or 5.3 percent and loss adjustment expense (LAE) reserves decreased $6.7 million or 2.3 percent during 2007. Loss reserves increased primarily due to growth in SAIF's book of business as both the number of policyholders and premium amount grew during the year.

Several loss reserve assumptions were refined, which produced favorable loss reserve development for prior accident years. The favorable loss development in 2007 can be attributed to a number of factors. Medical cost escalation for 2007 was lower than expected, and the explicit assumption for medical cost escalation for the next three years was lowered to recognize the current short-term trend. Development for indemnity reserves related to prior accident years was also favorable due to lower tail factors for permanent total disability and fatal awards. The favorable LAE development was largely attributed to a reduction in the number of payments and reserve changes performed by claims adjusters during 2007.

Unearned Premiums—The amount of unearned premium for 2007 increased $131.2 million due to the continued migration of policies from the installment accounting method to the annualized method as discussed previously.

Accounts Payable—The balance in this line is comprised of commissions payable, reinsurance payable, accrued premium assessment, and other accounts payables. The $15.4 million increase in this line item is due primarily to a $5.9 million increase in commissions payable and a $4.7 million increase in premium assessment payable due to an increase in premiums written.

Due to Brokers for Security Purchases—The amount payable for pending settlement of investment purchases can fluctuate significantly from period to period depending on the amount of investment activity near the end of the period.

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 SAIF's portfolio.

Other Liabilities and Deposits—The balance in this line is comprised of accrued retrospective premiums payable, premium deposits, amounts due to other governments, and compensated absences payable. The decrease in this line item is due primarily to a decline in the estimated amount of return premium payable on retrospectively rated policies, because of unfavorable loss development experience for certain retrospectively rated policies.

Operations - Year Ended December 31, 2007

Significant changes in revenues and expenses include:

Net Premiums Earned—Despite an average 2.1 percent decline in pure premium rates in 2007, net earned premiums increased $22.0 million or 5.0 percent compared to 2006. However, the growth in premium for 2007 slowed somewhat compared to the growth experienced during

2006 and 2005, when net earned premiums increased 6.0 percent and 10.6 percent, respectively.

Other Income—Other income decreased $5.3 million from 2006 to 2007. This is due to a continued declined in premium assessment rates.

Net Losses and Loss Adjustment Expenses Incurred—Losses incurred for 2007 decreased by $1.6 million from 2006 while loss expenses incurred increased $29.0 million for a net increase of $27.4 million. Incurred losses for the current year are comparable to the prior year as favorable loss reserve development for prior accident years offset a portion of losses incurred for the current accident year. LAE for 2007 were greater than the prior year, because the amount of favorable reserve development recorded during 2006 was higher than the favorable development recorded during the current year.

Policyholders' Dividends—On November 9, 2007, SAIF's Board of Directors declared a policyholder dividend of $60.0 million for all eligible policyholders with policy expiration dates during calendar year 2006. After careful evaluation of SAIF's reserve adequacy, risk-based capital and surplus requirements, and pure premium rate changes, the Board determined that it was appropriate to declare this dividend and that the remaining surplus was adequate to protect against an unanticipated downturn in the investment markets, adverse loss reserve development, or other catastrophic events. The declared dividend was paid during December, 2007.

Underwriting Expense—This line decreased $3.4 million due primarily to a decrease in premium assessment expense as a result of a continued declined in premium assessment rates.

Net Investment Income—Investment income for 2007 was $30.0 million less than the amount recorded for 2006, primarily due to a decrease in the market value adjustment for invested assets. The change in fair value of investments recorded for 2007 was $44.7 million less than the change recorded for 2006. Interest income from bonds increased $7.4 million from the prior year due to growth in bond holdings.

SAIF CORPORATION

BALANCE SHEETS
AS OF DECEMBER 31, 2008 AND 2007
(In thousands)

	2008	2007
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 39,478	$ 39,862
Investments	3,398,861	3,597,781
Securities lending cash collateral	439,181	570,060
Investment income receivable	38,485	35,210
Premiums receivable, net of allowance of $1,692 and $1,138	267,482	251,264
Accrued retrospective premiums receivable	51,867	74,881
Accounts receivable	13,167	16,147
Receivable for securities sold	132	280
Other assets	8,354	8,246
Total current assets	4,257,007	4,593,731
NONCURRENT ASSETS:		
Capital assets:		
Land	3,029	3,029
Buildings, property, and equipment	45,237	46,260
Less accumulated depreciation and amortization	(28,921)	(29,623)
Total noncurrent assets	19,345	19,666
TOTAL	$ 4,276,352	$ 4,613,397
LIABILITIES AND FUND EQUITY		
CURRENT LIABILITIES:		
Reserve for losses and loss adjustment expenses	$ 209,139	$ 213,498
Unearned premiums	198,736	207,800
Accrued retrospective premiums payable	35,337	25,536
Commissions payable	10,687	11,347
Reinsurance payable	6,330	10,975
Accrued premium assessment payable	12,380	15,088
Premium deposits	12,495	14,698
Accounts payable	22,693	20,614
Due to brokers for security purchases	5	5
Obligations under securities lending	465,208	570,060
Due to other governments	3,256	3,755
Compensated absences payable	3,112	2,813
Total current liabilities	979,378	1,096,189
NONCURRENT LIABILITIES:		
Reserve for losses and loss adjustment expenses	2,702,170	2,591,867
Other postemployment benefits obligation	472	244
Total noncurrent liabilities	2,702,642	2,592,111
Total liabilities	3,682,020	3,688,300
FUND EQUITY:		
Invested in capital assets	19,345	19,666
Unrestricted	574,987	905,431
Total fund equity	594,332	925,097
TOTAL	$ 4,276,352	$ 4,613,397

See notes to financial statements.

SAIF CORPORATION

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN FUND EQUITY FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007 (In thousands)

	2008	2007
OPERATING REVENUES:		
Net premiums earned	$ 416,016	$ 459,977
Other income	23,553	20,267
Total operating revenues	439,569	480,244
OPERATING EXPENSES:		
Net losses and loss adjustment expenses incurred	436,079	435,297
Policyholders' dividends	-	59,979
Underwriting expenses	89,459	88,972
Other expenses	2,300	-
Total operating expenses	527,838	584,248
OPERATING LOSS	(88,269)	(104,004)
NONOPERATING REVENUES:		
Investment income (loss)	(225,392)	216,404
Investment expenses	(17,104)	(38,153)
Net investment income (loss)	(242,496)	178,251
INCREASE (DECREASE) IN FUND EQUITY	$ (330,765)	$ 74,247
FUND EQUITY—Beginning of year	925,097	850,850
FUND EQUITY—End of year	$ 594,332	$ 925,097

See notes to financial statements.

SAIF CORPORATION

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007
(In thousands)

	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES:		
Premiums collected, net of reinsurance	$ 416,703	$ 448,725
Loss and loss adjustment expenses paid	(330,135)	(316,333)
Underwriting expenses paid	(89,459)	(98,692)
Policyholder dividends paid	-	(59,979)
Other receipts	24,327	34,865
Net cash provided by operating activities	21,436	8,586
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investments	(795,922)	(2,014,095)
Proceeds from sales and maturities of investments	596,928	1,834,030
Interest received on investments and cash balances	174,363	157,320
Interest received from securities lending	15,202	34,104
Interest paid for securities lending	(11,218)	(32,109)
Net cash used in investing activities	(20,647)	(20,750)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition of capital assets	(1,173)	(1,614)
Proceeds from disposition of capital assets	-	339
Net cash used in capital and related financing activities	(1,173)	(1,275)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(384)	(13,439)
CASH AND CASH EQUIVALENTS—Beginning of year	39,862	53,301
CASH AND CASH EQUIVALENTS—End of year	$ 39,478	$ 39,862

(Continued)

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007
(In thousands)

	2008	2007
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating loss	$ (88,269)	$ (104,004)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation and amortization	1,464	1,679
Bad debt provision	2,300	(264)
Net changes in assets and liabilities:		
Premiums receivable, net	(18,517)	(142,863)
Accrued retrospective premiums receivable	23,015	3,238
Accounts receivable	2,979	(4,051)
Other assets	(107)	(6,171)
Reserve for losses and loss adjustment expenses	105,943	118,964
Unearned premiums	(9,064)	131,230
Accrued retrospective premiums payable	9,800	(4,397)
Commissions payable	(660)	5,994
Reinsurance payable	(4,645)	790
Accrued premium assessment payable	(2,708)	4,693
Premium deposits	(2,202)	1,015
Accounts payable	2,078	2,691
Due to other governments	(499)	(311)
Compensated absences payable	299	109
Other postemployment benefits obligation	229	244
Total adjustments	109,705	112,590
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 21,436	$ 8,586
SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING ACTIVITIES: Investments acquired and sold through conversions and tax free exchange transactions	$ 50,347	$ 41,332

See notes to financial statements.

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 is a servicing carrier for accounts in the assigned risk pool. SAIF also provides coverage governed by the Longshore 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 Oregon business and community leaders not otherwise in the employ of SAIF. Three members of SAIF's board of directors are employed with policyholders of SAIF. The transactions between SAIF and these policyholders were within SAIF's standard terms and conditions.

SAIF writes business on a direct basis as well as through agents. Premiums written on a direct basis were 32.0 percent and 30.5 percent of standard premium during 2008 and 2007, respectively. SAIF issues workers' compensation insurance policies to individual Oregon employers including state agencies.

The Oregon Department of Consumer and Business Services (DCBS) enforces workers' compensation laws under the Oregon Revised Statutes (ORS). Under the reporting requirements of the DCBS, Insurance Division, SAIF is subject to Risk Based Capital (RBC) requirements of the National Association of Insurance Commissioners (NAIC), which establishes that certain amounts of capital and surplus be maintained. SAIF's RBC calculated minimum capital and surplus amount on the statutory basis of accounting was $229.5 million and $340.5 million at December 31, 2008 and 2007, respectively. At December 31, 2008 and 2007, the statutory capital and surplus of SAIF exceeded the minimum RBC requirements.

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 discretely presented component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board (GASB). Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as a special purpose government engaged solely in business-type activities. Accordingly, SAIF follows the economic resources measurement focus and 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 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 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 fair value of debt and equity securities is determined 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. For some debt securities, fair value cannot be determined in this manner. For these securities, a similar "benchmark" security is used. The benchmark security has a coupon rate and maturity date comparable to the debt security being valued, and its market risk is similar considering current market conditions. As of December 31, 2008, 14.3 percent of SAIF's debt securities were priced using the benchmark method. Mortgage loans on real estate are stated at the unpaid principal balance.

Cash and Cash Equivalents—SAIF places its temporary cash investments with the Oregon Short Term Fund, an external cash and investment pool. SAIF's participation in this fund is involuntary. This fund is not registered with the Securities and Exchange Commission and is not rated. 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, 2008 and 2007, was 160 days and 168 days, respectively. As of December 31, 2008 and 2007, SAIF's balance in the Oregon Short Term Fund was $17.4 million and $20.0 million, respectively.

Oregon's State Treasurer employs the services of two external investment managers to manage SAIF's fixed income portfolios. The cash balances of the fixed income managers are invested in the SSgA Prime Money Market Fund which had an average credit quality rating of A1+/P-1. This fund's stated objectives are 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 Prime Money Market Fund as of December 31, 2008 and 2007, was 31 days and 28 days, respectively.

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 amount 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 many different industries and geographic regions.

Capital Assets—Capital assets are stated at historical 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 recorded as other income.

Internal and external costs incurred to develop internal-use computer software and web sites during the application development stage are capitalized; costs incurred during the preliminary project stage and post-implementation/operation stage are expensed as incurred.

Capital assets are 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	30–40 years
Furniture, equipment, and machinery	$0–$5,000	3–7 years
Data processing software	$500,000	3 years

Capital assets activity for the years ended December 31, 2008 and 2007, were as follows (dollars in thousands):

	2008			
	Beginning Balance	Additions	Disposals	Ending Balance
Nondepreciable capital assets - land	$ 3,029	$ -	$ -	$ 3,029
Buildings and improvements	25,930	147	-	26,077
Equipment	11,287	1,026	(2,196)	10,117
Data processing software	9,043	-	-	9,043
Total depreciable capital assets	46,260	1,173	(2,196)	45,237
Total	49,289	1,173	(2,196)	48,266
Less accumulated depreciation for:				
Buildings and improvements	(11,162)	(753)	-	(11,915)
Equipment	(9,417)	(741)	2,196	(7,962)
Data processing software	(9,044)	-	-	(9,044)
Total accumulated depreciation	(29,623)	(1,494)	2,196	(28,921)
Capital assets—net	$ 19,666	$ (321)	$ -	$ 19,345

	2007			
	Beginning Balance	Additions	Disposals	Ending Balance
Nondepreciable capital assets - land	$ 2,922	$ 107	$ -	$ 3,029
Buildings and improvements	25,502	428	-	25,930
Equipment	11,381	1,079	(1,173)	11,287
Data processing software	9,043	-	-	9,043
Total depreciable capital assets	45,926	1,507	(1,173)	46,260
Total	48,848	1,614	(1,173)	49,289
Less accumulated depreciation for:				
Buildings and improvements	(10,425)	(737)	-	(11,162)
Equipment	(9,880)	(676)	1,139	(9,417)
Data processing software	(8,746)	(298)	-	(9,044)
Total accumulated depreciation	(29,051)	(1,711)	1,139	(29,623)
Capital assets—net	$ 19,797	$ (97)	$ (34)	$ 19,666

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 which is generally one year. Ceded premiums are recognized consistent with the underlying policies. 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 premiums recorded as written at the policy inception date and not yet billed, as well as an estimate of the difference between amounts earned ratably on installment-billed policies and the amount 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 premiums receivable 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 premium receivable for unbilled premiums. Unbilled premiums receivable at December 31, 2008 and 2007, were $260.5 million and $242.9 million, respectively.

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 as policyholders' premium deposits. However, policyholders may pledge surety bonds and securities in lieu of cash deposits. Premium deposits were $12.5 million and $14.7 million as of December 31, 2008 and 2007, respectively.

In addition to its regular premium plans, SAIF offers employers retrospective premium rating plans under which premiums are adjusted annually for up to 10½ 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 10½ years. The estimate of the net accrued premiums receivable for retrospective rating plans as of December 31, 2008 and 2007, is as follows (dollars in thousands):

	2008	**2007**
Accrued retrospective premiums receivable	$ 51,867	$ 74,881
Reserve for retrospective rating plans	(35,337)	(25,536)
Net	$ 16,530	$ 49,345

SAIF estimates accrued retrospective premiums receivable and payable by reviewing historical loss and premium development patterns at various stages of maturity and using these historical patterns to arrive at the best estimate of return and additional retrospective premiums on all open retrospectively rated policies. Premiums written on retrospective workers' compensation policies for 2008 and 2007 were $119.8 million and $137.0 million, respectively, or 29.4 percent and 23.2 percent of net premiums written, respectively.

Reserve for Losses and Loss Adjustment Expenses—The reserve for losses and loss adjustment expenses is generally based on past experience. 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 losses and loss adjustment expenses at December 31, 2008 and 2007, are a reasonable estimate of the ultimate net costs of settling claims and claims expenses incurred. Annually, the board of directors reviews the actuarial assumptions utilized in determining the liability for such losses. Actual claim costs depend upon such factors as duration of worker disability, medical cost trends, occupational disease, 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).

Premium Deficiency—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. At December 31, 2008 and 2007, no reserve for premium deficiency was required to be recorded.

Policyholders' Dividends—Substantially all of SAIF's business is written under various participating plans wherein a dividend may be returned to the policyholder. Dividends may be paid to the extent that a surplus is accumulated from premiums, investment gains, or loss reserve reductions. No policyholder dividends were declared or paid in 2008. In 2007, SAIF's Board of Directors declared and paid a policyholder dividend of $60.0 million.

Taxes and Assessments—The Oregon Department of Justice has determined that SAIF is exempt from federal and state 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 DCBS. Such assessments constitute an in-lieu-of-tax relative to premiums. Premium assessments were $18.9 million and $17.6 million, including $12.4 million and $15.1 million of accrued premium assessments, for the years ended December 31, 2008 and 2007, respectively.

Deferred Acquisition Costs—Acquisition costs such as commissions and other costs related to acquiring new business are deferred and amortized to income as premiums are earned. As of December 31, 2008 and 2007, deferred acquisition costs were $8.3 million and $8.2 million, respectively, and were recorded as other assets on the balance sheet. Amortization expense for the years ended December 31, 2008 and 2007, was $601 thousand and $4.6 million, respectively and is recorded as a component of underwriting expenses.

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 the reported amounts of revenues and expenses during the reporting period and disclosures of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

New Accounting Pronouncements—In November 2006, the GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations.* This statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. SAIF implemented this statement for the fiscal year ended December 31, 2008. There was no significant impact on the financial statements.

In June 2007, the GASB issued Statement No. 51, *Accounting and Financial Reporting for Intangible Assets.* This statement requires that all intangible assets not specifically excluded by its scope provisions be classified as capital assets. Accordingly, existing authoritative guidance related to the accounting and financial reporting for capital assets should be applied to these intangible assets, as applicable. This statement requires that an intangible asset be recognized in the statement of net assets only if it is considered identifiable. This statement also provides guidance on recognizing internally generated computer software as an intangible asset. The requirements of this statement are effective for SAIF's 2010 financial statements.

In November 2007, the GASB issued Statement No. 52, *Land and Other Real Estate Held as Investments by Endowments*. This statement establishes standards for accounting and financial reporting for land and other real estate held as investments by endowments. Endowments include permanent and term endowments and permanent funds. This statement does not apply to lands granted by the Federal government in connection with a state being admitted to the United States. It also does not apply to quasi-endowments. This statement applies to all state and local governments. The requirements of this statement are effective for SAIF's 2009 financial statements.

In June 2008, the GASB issued Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*. This statement establishes accounting and financial reporting standards for all state and local governments that enter into derivative instruments as defined in this statement. The requirements of this statement are effective for SAIF's 2010 financial statements.

In February 2009, the GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*. This statement establishes accounting and financial reporting standards for all governments that report governmental funds. It establishes criteria for classifying fund balances into specifically defined classifications and clarifies definitions for governmental fund types. The requirements of this statement are effective for SAIF's 2011 financial statements.

In April 2009, the GASB issued Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This statement identifies the sources of accounting principles and the framework for selecting the principles used in the preparation of financial statements of state and local governmental entities that are presented in conformity with generally accepted accounting principles (the GAAP hierarchy). This statement applies to the financial statements of all state and local governments that are presented in conformity with GAAP. The requirements of this statement are effective for SAIF's 2009 financial statements.

In April 2009, the GASB issued Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*. This statement establishes accounting and financial reporting standards for related party transactions, subsequent events, and going concern considerations. This statement applies to all state and local governments. The requirements of this statement are effective for SAIF's 2009 financial statements.

Reclassifications—Certain reclassifications have been made to prior year amounts in order to conform with current year presentation.

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 Oregon State Treasury (State Treasury) at a minimum of 25 percent as required by statute.

SAIF's cash and cash equivalents totaled $39.5 million and $39.9 million as of December 31, 2008 and 2007, respectively, and are composed of the following (dollars in thousands):

	2008	**2007**
Cash balances	$ 23,373	$ 26,575
SSgA prime money market fund	16,105	13,287
Total cash and cash equivalents	$ 39,478	$ 39,862

As of December 31, 2008 and 2007, the cash balances are on deposit in the Oregon Short Term Fund ($17.4 million and $20.0 million, respectively), U.S. Bank ($4.8 million and $4.7 million, respectively), and in State Street Bank and Trust Company (State Street) ($1.2 million and $1.9 million, respectively).

Custodial Credit Risk for Cash and Cash Equivalents (Deposits)—Custodial credit risk for deposits is the risk that in the event of a bank failure, SAIF will not be able to recover the value of its deposits or collateral securities that are in possession of an outside party.

As of December 31, 2008, the cash held in U.S. Bank ($4.8 million) is FDIC insured for up to $250 thousand.

Investments—SAIF's investment policies are governed by statute and the Oregon Investment Council (Council). The State Treasurer (Treasurer) is the investment officer for the Council and is responsible for the funds on deposit in the State Treasury. In accordance with ORS 293.726, the investment funds are to be invested, and the investments of those funds managed, as a prudent investor would do, exercising reasonable care, skill, and caution. While the Treasurer is authorized to use demand deposit accounts and fixed-income investments, equity investment transactions must be directed by external investment managers that are under contract with the Council. Equity investments are limited to not more than 50 percent of the monies contributed to the Industrial Accident Fund (SAIF Corporation). However, SAIF's adopted investment policy as approved by the Council limits equity holdings to a range of 10 to 20 percent of the market value of invested assets with a target allocation of 15 percent.

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, 2008 and 2007, were $132 thousand and $280 thousand, respectively. Due to brokers for security purchases were $5 thousand as of December 31, 2008 and 2007.

Interest Rate Risk—Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. SAIF's policy for fixed income investments effective January 1, 2005, provides that a duration target be used to manage interest rate risk. The policy calls for the portfolio duration to be within 20 percent of the benchmark duration. The benchmark duration as of December 31, 2008, was 7.08 years, with an acceptable range of 5.66 to 8.50 years. As of that date, the fixed income portfolio's duration was 6.74 years.

The following 2008 maturity distribution schedule includes $787.2 million in interest-rate sensitive securities. As of December 31, 2008, SAIF held $591.6 million of U.S. Federal Agency mortgage-backed securities and $161.1 million of commercial mortgage obligations (CMOs). These securities are based on cash flows from principal and interest payments on underlying mortgages. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates. As of December 31, 2008, SAIF held $34.5 million of asset-backed securities which consist primarily of sequential-pay tranches of utility, student loan, and equipment lease receivables, and callable pass-through certificates issued by airlines and railroads. The value of these securities can be volatile as interest rates fluctuate. Additional risk inherent with these securities is the unpredictability of default on loans that are the collateral for the debt.

The following schedule represents the fixed income investments by maturity date as of December 31, 2008 and 2007, using the segmented time distribution method. 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):

2008	**Less Than 1 Year**	**1–5 Years**	**6–10 Years**	**More Than 10 Years**	**Fair Value**
Bonds:					
U.S. Treasury obligations	$ -	$ 8,176	$ -	$ 287,689	$ 295,865
U.S. Treasury obligations—STRIPS	-	-	-	80,362	80,362
U.S. federal agency mortgage securities	80,458	191,570	132,187	187,432	591,647
U.S. federal agency debt	47,335	-	59,176	57,660	164,171
Corporate bonds	35,649	296,876	460,519	600,370	1,393,414
Municipal bonds	-	-	1,269	17,897	19,166
Collateralized mortgage obligations	23,631	44,858	85,591	7,050	161,130
Asset-backed securities	6,806	18,310	8,358	1,005	34,479
International debt securities	70	62,193	46,801	168,671	277,735
Total bonds	$ 193,949	$ 621,983	$ 793,901	$ 1,408,136	$ 3,017,969
Equity securities:					
Domestic equity securities					$ 212
Russell 3000 pooled equity fund					380,588
Total equity securities					380,800
Other invested assets					86
Mortgage loans on real estate					6
Total investments					$ 3,398,861

2007	Less Than 1 Year	1–5 Years	6–10 Years	More Than 10 Years	Fair Value
Bonds:					
U.S. Treasury obligations	$ 7,560	$ 99,343	$ 5,121	$ 293,592	$ 405,616
U.S. Treasury obligations—TIPS	-	-	-	22,269	22,269
U.S. Treasury obligations—STRIPS	-	-	-	53,534	53,534
U.S. federal agency mortgage securities	84,992	216,303	132,363	167,072	600,730
U.S. federal agency debt	2,313	110,832	15,074	49,134	177,353
Corporate bonds	9,079	268,574	336,442	523,463	1,137,558
Municipal bonds	-	-	1,418	26,268	27,686
Collateralized mortgage obligations	23,313	67,689	123,553	18,745	233,300
Asset-backed securities	29,913	27,311	7,684	417	65,325
International debt securities	5,568	50,228	50,091	190,664	296,551
Total bonds	$ 162,738	$ 840,280	$ 671,746	$ 1,345,158	$ 3,019,922
Equity securities:					
Domestic equity securities					$ 306
Russell 3000 pooled equity fund					577,223
Total equity securities					577,529
Other invested assets					308
Mortgage loans on real estate					22
Total investments					$ 3,597,781

Credit Risk—Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. SAIF's credit risk policy is to maintain a well-diversified investment portfolio. Fixed income holdings shall be the largest component of the portfolio. The policy seeks to maintain an overall fixed income portfolio quality of at least "AA-" or higher.

The majority of SAIF's debt securities as of December 31, 2008 and 2007, were rated by Moody's and Standard & Poor's, which are nationally recognized statistical rating organizations. The following schedule represents the ratings of debt securities by investment type as of December 31, 2008 and 2007, using the Standard & Poor's rating scale (dollars in thousands):

2008 — **Quality Ratings**

	AAA	AA	A	BBB	BB	B	CCC	CC	C	D	Unrated	Fair Value
Bonds:												
U.S. Treasury obligations	$ 295,865	-	-	-	-	-	-	-	-	-	-	$ 295,865
U.S. Treasury obligations - TIPS	-	-	-	-	-	-	-	-	-	-	-	-
U.S. Treasury obligations - STRIPS	80,362	-	-	-	-	-	-	-	-	-	-	80,362
U.S. federal agency mortgage securities	472,584	7,153	58,178	27,390	8,019	13,292	3,690	1,094	-	26	221	591,647
U.S. federal agency debt	89,614	7,852	5,235	-	-	-	-	39,066	18,862	-	3,542	164,171
Corporate bonds	75,835	158,688	670,545	408,249	39,728	13,776	18,179	3,486	669	-	4,259	1,393,414
Municipal bonds	376	13,090	-	5,700	-	-	-	-	-	-	-	19,166
Collaterized mortgage obligations	111,205	3,768	4,558	93	-	-	161	-	-	-	41,345	161,130
Asset-backed securities	24,044	1,227	1,550	-	-	-	-	-	-	-	7,658	34,479
International debt securities	2,988	12,476	76,537	182,678	3,014	-	42	-	-	-	-	277,735
Total bonds	$ 1,152,873	$ 204,254	$ 816,603	$ 624,110	$ 50,761	$ 27,068	$ 22,072	$ 43,646	$ 19,531	$ 26	$ 57,025	$ 3,017,969

2007 — **Quality Ratings**

	AAA	AA	A	BBB	BB	B	CCC	CC	C	D	Unrated	Fair Value
Bonds:												
U.S. Treasury obligations	$ 405,616	-	-	-	-	-	-	-	-	-	-	$ 405,616
U.S. Treasury obligations - TIPS	22,269	-	-	-	-	-	-	-	-	-	-	22,269
U.S. Treasury obligations - STRIPS	53,534	-	-	-	-	-	-	-	-	-	-	53,534
U.S. federal agency mortgage securities	600,189	-	-	-	-	-	-	-	-	-	541	600,730
U.S. federal agency debt	173,108	999	-	-	-	-	-	-	-	-	3,246	177,353
Corporate bonds	61,905	172,797	434,075	355,486	54,205	47,177	8,248	-	-	-	3,665	1,137,558
Municipal bonds	9,748	8,441	-	9,497	-	-	-	-	-	-	-	27,686
Collaterized mortgage obligations	168,451	3,556	-	-	-	-	-	-	-	-	61,293	233,300
Asset-backed securities	45,366	2,716	2,470	3,338	-	-	-	-	-	-	11,435	65,325
International debt securities	5,412	11,507	80,503	191,118	3,317	4,694	-	-	-	-	-	296,551
Total bonds	$ 1,545,598	$ 200,016	$ 517,048	$ 559,439	$ 57,522	$ 51,871	$ 8,248	$ -	$ -	$ -	$ 80,180	$ 3,019,922

Concentration of Credit Risk—Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. SAIF's investment policy places limitations on the amount that may be invested in any one issuer. The following specific limitations reflect, in part, the Oregon Investment Council's current investment philosophy regarding diversification.

- No fixed income investment in any one issue shall be in excess of 5 percent of the outstanding fixed income obligations of the issuer.

- Not more than 3 percent of the total fair value of SAIF's fixed income portfolio shall be invested in fixed income securities of any one issuer, except U.S. government and agency obligations (no limit) and private mortgage-backed and asset-backed securities which shall be limited to 10 percent per issuer.

- Obligations of other national governments are limited to 10 percent per issuer.

As of December 31, 2008 and 2007, SAIF did not have a concentration of credit risk in any one issuer that represented 5 percent or more of total investments.

Securities on Deposit—U.S. Treasury obligations with a fair value of $8.2 million and $15.4 million at December 31, 2008 and 2007, respectively, were on deposit with the Federal Reserve as required by the U.S. Department of Labor under the Longshore and Harbor Workers' Compensation Act. In addition, U.S. Bank certificates of deposit with a fair value of $200 thousand and $300 thousand at December 31, 2008 and 2007, respectively, were on deposit at U.S. Bank as required by the DCBS.

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

During 2008 and 2007, State Street loaned 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 percent of the fair value of the loaned security. SAIF did not impose any restrictions 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.

Cash collateral received in respect of securities loaned is invested in the State Street Bank and Trust Company Oregon Short-Term Investment Fund (the 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. No income from the Fund was assigned to another fund by the custodial agent during 2008 and 2007. At December 31, 2008 and 2007, the Fund had an average-weighted maturity of 339 days and 315 days, respectively. As of December 31, 2008 and 2007, Standard and Poor's weighted average credit quality for the Fund was AA.

At December 31, 2008 and 2007, the collateral held was $439.2 million and $570.1 million, respectively. At December 31, 2008 and 2007, the fair value, including accrued investment income related to the securities on loan, was $448.7 million and $558.6 million, respectively. For 2008 and 2007, securities lending income was $15.2 million and $34.3 million and securities lending expense was $11.2 million and $32.1 million, respectively.

4. RESERVE FOR LOSSES 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 (LAE). In estimating the reserve for loss and LAE, 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 losses and LAE (dollars in thousands):

	2008	2007	2006
Gross reserve for losses and loss adjustment expenses—beginning of year	$ 2,960,635	$ 2,841,103	$ 2,737,022
Less reinsurance recoverable—beginning of year	(155,270)	(154,702)	(149,017)
Net reserve for losses and loss adjustment expenses—beginning of year	2,805,365	2,686,401	2,588,005
Incurred losses and loss adjustment expenses:			
Provision for insured events of the current year	473,348	509,690	516,726
Provision for insured events of prior years	(37,269)	(74,393)	(108,872)
Total incurred losses	436,079	435,297	407,854
Loss and loss adjustment expense payments attributable to:			
Insured events of the current year	106,974	106,674	106,452
Insured events of prior years	223,161	209,659	203,006
Total payments	330,135	316,333	309,458
Net reserve for losses and loss adjustment expenses—end of year	2,911,309	2,805,365	2,686,401
Plus reinsurance recoverable—end of year	158,827	155,270	154,702
Gross reserve for losses and loss adjustment expenses—end of year	$ 3,070,136	$ 2,960,635	$ 2,841,103

The reserve for losses and LAE increased $105.9 million in 2008, which was somewhat offset by favorable loss reserve development related to prior accident years. The favorable development of $37.3 million is attributed to a number of factors. Claim count development was lower than expected. The methods used to estimate ultimate settlement fees and vocational rehabilitation expenses were revised, resulting in lower tail factors. Prior year development for indemnity reserves was unfavorable due to case reserve strengthening, partially offsetting the overall favorable loss development. The unfavorable LAE development was largely attributed to an update of SAIF's internal expense allocation in 2008. Additional resources have been allocated to the loss adjustment function, resulting in a reserve increase.

For 2007, the reserve for losses and LAE increased primarily due to growth in SAIF's book of business as both the number of policyholders and premium amount grew during the year. There was favorable development of $74.4 million related to prior accident years, which is attributed to a number of factors. Medical cost escalation for 2007 was lower than expected, and the explicit assumption for medical cost escalation for the next three years was lowered to recognize the current short-term trend. Development for indemnity reserves related to prior accident years was also favorable due to lower tail factors for permanent total disability and fatal awards. The favorable LAE development was largely attributed to a reduction in the number of payments and reserve changes performed by claims adjusters during 2007.

SAIF discounts its case unpaid losses on a tabular basis using the 1999 United States Life Tables, the 1980 United States of America Railroad Retirement Board Remarriage Table, and a discount rate of 3.5 percent. SAIF does not discount any incurred but not reported reserves, medical unpaid losses, or unpaid LAE. Discounted reserves include known unpaid fatal and permanent total disability losses. Gross reserves subject to tabular discounting were $277.2 million and $275.7 million for 2008 and 2007, respectively. The discounts were $97.0 million and $99.2 million as of December 31, 2008 and 2007, respectively.

Anticipated salvage and subrogation of $21.5 million and $19.5 million was included as a reduction of the reserve for losses and LAE at December 31, 2008 and 2007, respectively.

SAIF's exposure to asbestos claims arose from the sale of workers' compensation policies. Reserves of $24.5 million and $22.8 million for losses and LAE are related to asbestos claims as of December 31, 2008 and 2007, respectively. Amounts paid for asbestos related claims were $527 thousand and $488 thousand for the years ended December 31, 2008 and 2007, respectively.

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.

SAIF maintains reinsurance protection providing limits of $60 million excess of $40 million per occurrence with a $10 million maximum on any one life and a $120 million aggregate limit. This reinsurance protection excludes coverage for nuclear, biological, chemical, or radiological events in some or all instances. During 2008, SAIF had reinsurance protection for 85 percent of losses in excess of 20 percent of 2007 direct earned premium for acts of terrorism through the Terrorism Risk Insurance Program Reauthorization Act.

The following amounts have been deducted (added) in the accompanying financial statements as a result of reinsurance ceded for 2008 and 2007 (dollars in thousands):

	2008	**2007**
Reserve for losses and loss adjustment expenses	$ 56,397	$ 54,213
Premiums earned	1,234	1,390
Losses and loss adjustment expenses incurred	2,640	(3,045)

Of the $56.4 and $54.2 million recoverable, SAIF had a reinsurance recoverable from an individual reinsurer of $29.4 million and $25.8 million, respectively as of December 31, 2008 and 2007.

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 (NWCRP). The Plan provides a guaranteed source of workers' compensation insurance for employers unable to obtain coverage because of unstable financial conditions, poor loss experience, or the inherently dangerous nature of the work. SAIF cedes such business to the Plan. In addition, SAIF is 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 in 2008 and 2007 (dollars in thousands):

	2008	2007
Assumed:		
Reserve for losses and loss adjustment expenses	$ 76,875	$ 75,853
Unearned premiums	2,871	3,517
Premiums written	24,942	33,780
Premiums earned	25,588	37,893
Losses and loss adjustment expenses incurred	18,218	22,117
Commission expense	8,008	10,625
Ceded:		
Reserve for losses and loss adjustment expenses	$ 102,430	$ 101,057
Unearned premiums	7,409	11,254
Premiums written	19,177	30,203
Premiums earned	23,022	30,283
Losses and loss adjustment expenses incurred	16,797	17,975
Commission expense	6,115	8,498

6. LEASE COMMITMENTS

SAIF leases office space in several locations under non-cancellable operating leases expiring during various years through 2019. Lease expense was $730 thousand and $671 thousand for the years ended December 31, 2008 and 2007, respectively.

SAIF's future minimum lease payments under operating leases at December 31, 2008, are as follows (dollars in thousands):

2009	$ 815
2010	941
2011	878
2012	887
2013	914
Total minimum payments	$ 4,435

Certain rental commitments have renewal options extending through the year 2024. 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 $204 thousand and $411 thousand on leases due in the future under non-cancellable subleases as of December 31, 2008 and 2007, respectively.

7. RISK MANAGEMENT

The State of Oregon administers property and casualty insurance programs covering state government agencies through its Insurance Fund, an internal service 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 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 $20 million.

SAIF participates in the Insurance Fund. The cost of servicing insurance claims and payments is covered by charging an assessment to each participating 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 any available fund balance of the Insurance Fund from the prior biennium. SAIF's assessment was $260 thousand as of December 31, 2008 and 2007.

SAIF's employees do not participate in the State of Oregon's health insurance plans.

8. CONTINGENCIES

SAIF has entered into structured settlements wherein SAIF has purchased annuities for which the claimant is payee, but for which SAIF is contingently liable. The amount of the contingent liability is the amount of the liability due to the various claimants that has been offset by the purchase of the annuity. Contingent liabilities arising from these settlements were $6.5 million and $6.7 million at December 31, 2008 and 2007, respectively.

During the normal 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 Oregon Department of Justice. Some of these potential liabilities become actual liabilities when one or more future events occur or fail to occur. To the extent that the future event is likely to occur or fail to occur, and a reasonable estimate of the loss can be made, an estimated liability would be recorded on SAIF's financial statements. Management believes that these matters do not materially impact the financial statements.

9. DEFERRED COMPENSATION PLAN

A deferred compensation plan was authorized under Internal Revenue Code Section 457(b) 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 withheld from employees and remitted to 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. SAIF does not perform the investing function and has no fiduciary accountability for the plan. Thus, plan assets and any related liability to plan participants have been excluded from the financial statements.

10. RETIREMENT PLAN

The majority of SAIF's employees participate in the Oregon Public Employees' Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan. The PERS Board of Trustees under the guidelines of ORS Chapter 238 administers PERS. The PERS retirement allowance, payable monthly for life, may be selected from thirteen retirement benefit options. Options include survivorship benefits and lump-sum refunds. The basic benefit formula is 1.67 percent 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, Fiscal Services, 11410 SW 68th Parkway, Tigard, Oregon 97223.

Beginning January 1, 2004, all covered employees are required by state statute to contribute 6.0 percent of their salary to the Individual Account Program (IAP), a defined contribution plan. Current law permits employers to pay employees' contributions to PERS, which SAIF has elected to do. Additionally, SAIF is required by statute to contribute a percentage of each covered employee's salary to fund the PERS program. For the year ended December 31, 2008, SAIF's contribution rate of each covered employee's salary was 6.54 percent. Rates are subject to change as a result of subsequent actuarial valuations.

SAIF employees hired after August 29, 2003, participate in the Oregon Public Service Retirement Plan (OPSRP) after completing six months of service. OPSRP is a hybrid pension plan (cost sharing multiple-employer plan) administered by the PERS Board of Trustees under the guidelines of ORS Chapter 238A with two components: the Pension Program (defined benefit) and the Individual Account Program (defined contribution). SAIF currently contributes 8.03 percent of each covered employee's salary to the Pension Program and 6.0 percent to the Individual Account Program. Rates are subject to change as a result of subsequent actuarial valuations.

SAIF participates, along with other State of Oregon agencies, in paying the debt service for State of Oregon general obligation bonds issued in October 2003 to reduce an unfunded PERS liability. The bonds are scheduled to mature 25 years after the date of issuance. Currently, the repayment rate is 5.95 percent of payroll each month. The payment rate is recalculated each state fiscal biennium.

The total amount contributed by SAIF for all plans for the years ended December 31, 2008, 2007, and 2006, consist of the following (dollars in thousands):

	2008	2007	2006
Employer contributions:			
Debt service	$ 3,211	$ 3,114	$ 3,025
PERS-Pension Program	2,785	3,072	3,622
OPSRP-Pension Program	904	501	328
Total employer contributions	6,900	6,687	6,975
Employee contributions paid by SAIF:			
PERS-IAP	2,555	2,517	2,501
OPSRP-IAP	676	497	379
Total employee contributions	3,231	3,014	2,880
Total contributions	$ 10,131	$ 9,701	$ 9,855

For the years ended December 31, 2008, 2007, and 2006, SAIF's employer contributions were equal to the annual required contributions.

11. OTHER POSTEMPLOYMENT BENEFIT PLAN

Plan Description—SAIF administers a single-employer defined benefit healthcare plan. SAIF employees retiring under Oregon PERS are eligible to receive medical coverage for self and eligible dependents until age 65. Retirees must pay the premium for the coverage elected. Premiums for coverage are identical for active and retired employees, except to the extent that SAIF pays all or a portion of its active employees' premiums. Participating retirees pay their own monthly premiums based on a blended premium rate since retirees are pooled together with active employees for insurance rating purposes. Benefit provisions are established by SAIF.

Funding Policy—SAIF's funding policy provides for contributions at amounts sufficient to fund benefits on a pay-as-you-go basis. For the years ended December 31, 2008 and 2007, respectively, retired plan members contributed $541 thousand and $498 thousand through their required contributions and the required contribution rate per member is an average of $586 and $488 per month.

Annual OPEB Cost and Net OPEB Obligation—SAIF's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of SAIF's annual OPEB cost for the years ended December 31, 2008 and 2007, the amount actually contributed, and changes in SAIF's net OPEB obligation to the plan (dollars in thousands):

	2008	**2007**
Annual required contribution	$ 408	$ 391
Interest on net OPEB obligation	13	-
Adjustment to ARC	(19)	-
Annual OPEB cost (expense)	402	391
Contributions made	174	147
Increase in net OPEB obligation	228	244
Net OPEB obligation - beginning of year	244	-
Net OPEB obligation - end of year	$ 472	$ 244
Percent of annual OPEB cost contributed	43.3%	37.6%

Actuarial Methods and Assumptions—Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress shown as required supplementary information presents multiyear trend information about whether the actuarial value of assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and participating members to that point. Actuarial calculations reflect a long-term perspective and include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

The postemployment healthcare benefit obligation was determined as part of the actuarial valuation prepared by a consulting actuary as of January 1, 2007, using the projected unit credit cost method. Significant assumptions used in the actuarial valuation include a 5.5 percent investment rate of return and an annual medical healthcare cost trend rate of 9 percent initially, reduced by 1 percent decrements annually to an ultimate rate of 5 percent in 2011. The unfunded actuarial accrued liability (UAAL) is being amortized as a level percentage of projected payroll on an open basis for 15 years. As GASB Statement 45 was implemented prospectively, there was no net OPEB liability at transition on January 1, 2007.

Funding Progress Information—The funded status as of the most recent actuarial valuation date is a follows (dollars in thousands):

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Annual Covered Payroll ((b-a)/c)
01/01/2007	$0	$2,973	$2,973	0.0%	$50,229	5.9%

(Unaudited)

REQUIRED SUPPLEMENTARY INFORMATION

POSTEMPLOYMENT HEALTHCARE BENEFIT PLAN

SCHEDULE OF FUNDING PROGRESS

(In thousands)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (b)	Unfunded Actuarial Accrued Liability (UAAL) (b-a)	Funded Ratio (a/b)	Annual Covered Payroll (c)	UAAL as a Percentage of Annual Covered Payroll ((b-a)/c)
01/01/2007	$0	$2,973	$2,973	0.0%	$50,229	5.9%

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