ERIE INDEMNITY CO
Form 424B1
January 30, 2003
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Filed Pursuant to Rule 424(b)(1)
File Number 333-99943

3,000,000 Shares

Erie Indemnity Company

Class A Common Stock

Shares of Erie Indemnity Company Class A common stock, which are non-voting, are being offered by the selling shareholder named in this prospectus. Erie Indemnity Company will not receive any proceeds from the sale of shares.

The Class A common stock is quoted on the NASDAQ Stock Market[SM] under the symbol ERIE . The last reported sale price of the Class A common stock on January 29, 2003 was $35.27 per share.

See Risk Factors beginning on page 8 to read about factors you should consider before buying shares of the Class A common stock.

Neither the Securities and Exchange Commission nor any other regulatory body has approved or disapproved of these securities or passed upon the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per Share	Total
Initial price to public	$ 34.50	$ 103,500,000
Underwriting discount	$ 1.81	$ 5,430,000
Proceeds, before expenses, to selling shareholder	$ 32.69	$ 98,070,000

To the extent the underwriters sell more than 3,000,000 shares of Class A common stock, the underwriters have the option to purchase up to an additional 450,000 shares of Class A common stock from the selling shareholder at the public offering price, less the underwriting discount.

The underwriters expect to deliver the shares against payment in New York, New York on or about February 4, 2003.

Goldman, Sachs & Co. **Credit Suisse First Boston**

Advest, Inc.

Cochran, Caronia & Co.

Legg Mason Wood Walker
Incorporated

Prospectus dated January 29, 2003.

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PROSPECTUS SUMMARY

This summary highlights the information contained in this prospectus that we believe is the most important regarding us and this offering. However, you should read the entire prospectus carefully before investing in our Class A common stock. All financial information, operating statistics and ratios in this prospectus are based on generally accepted accounting principles unless otherwise noted. Unless the context indicates otherwise, all references in this prospectus to we , us , our or the Company include Erie Indemnity Company and its wholly owned subsidiaries, Erie Insurance Company, Erie Insurance Company of New York and Erie Insurance Property & Casualty Company. As used in this prospectus, the Exchange refers to Erie Insurance Exchange, and Erie Insurance Group refers to the Company, the Exchange, its subsidiary, Flagship City Insurance Company, and its affiliate, Erie Family Life Insurance Company.

Our Company

We operate predominantly as a provider of management services to Erie Insurance Exchange (the Exchange). We also operate as a property and casualty insurer through our subsidiaries. We have served since 1925 as the attorney-in-fact for the policyholders of the Exchange. The Exchange is a reciprocal insurance exchange, which is an unincorporated association of individuals, partnerships and corporations that agree to insure one another. Each applicant for insurance to a reciprocal insurance exchange signs a subscriber s agreement, which contains an appointment of an attorney-in-fact. As attorney-in-fact, the Company is required to perform certain services relating to the sales, underwriting and issuance of policies on behalf of the Exchange.

The Exchange and its property and casualty subsidiary and our three property and casualty subsidiaries (collectively, the Property and Casualty Group) write personal and commercial lines property and casualty coverages exclusively through approximately 8,000 independent agents and pool their underwriting results. The financial results of the Exchange are not consolidated with ours.

For our services as attorney-in-fact, we charge the Exchange a management fee calculated as a percentage, limited to 25%, of the direct written premiums of the Property and Casualty Group. Management fees accounted for approximately 78% of our revenues for the nine months ended September 30, 2002. For the first nine months of 2002, 70% of the direct premiums written by the Property and Casualty Group were personal lines, while 30% were commercial lines. We also own 21.6% of the common stock of Erie Family Life Insurance Company, an affiliated life insurance company, of which the Exchange owns 53.5% and public shareholders, including certain of our directors, own 24.9%. At September 30, 2002, we had total assets of $2.2 billion, total liabilities of $1.2 billion and shareholders equity of $958 million. Our net income was $138.2 million for the nine months ended September 30, 2002 and $122.3 million for the year ended December 31, 2001.

We believe we are the only publicly-traded attorney-in-fact for a reciprocal insurance exchange in the country. Several other private property and casualty companies, such as USAA and Farmers Insurance Group (owned by Zurich Financial Services Group), are reciprocal insurance exchanges that operate with separate management arrangements**.** Our earnings are largely generated by fees based on premiums written directly by the underwriting pool of the Property and Casualty Group, in which the Exchange has a 94.5% participation. We therefore have a direct incentive to protect the financial condition of the Exchange. As a result of the Exchange s 94.5% participation in the underwriting results of the Property and Casualty Group, the underwriting risk of the Property and Casualty Group s business is largely borne by the Exchange, which had $2.1 billion of statutory surplus at September 30, 2002. The surplus of the Exchange was $4.8 billion at December 31, 1999 and has declined primarily

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from marketable security investment declines and underwriting losses. Through the pool, our property and casualty subsidiaries currently assume 5.5% of the Property and Casualty Group s underwriting results, and therefore we also have a direct incentive to manage the overall underwriting business as effectively as possible.

The Property and Casualty Group seeks to insure standard and preferred risks in primarily private passenger automobile, homeowners and small commercial lines, including workers compensation policies. We believe the Property and Casualty Group has differentiated its products from standard industry products by providing additional coverages, which enhance agents marketing efforts. The Property and Casualty Group s agency force consists of over 1,700 independent agencies comprised of approximately 8,000 agents in 11 Midwestern, Mid-Atlantic and Southeastern states (Illinois, Indiana, Maryland, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and Wisconsin) and the District of Columbia. These independent agents play a significant role as underwriters and are major contributors to the Property and Casualty Group s success.

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The Company has reported increasing net operating income for 14 consecutive years. The increases in net operating income have been driven by the premium growth of the Property and Casualty Group that resulted in a corresponding increase in the amount of the management fee. The premium growth of the Property and Casualty Group has resulted primarily from an expansion of its business into new territories, the appointment of new agencies, high policy and agency retention rates and, recently, increased premium rates.

Since 1997, the Property and Casualty Group has entered Illinois and Wisconsin and expects to begin operating in Minnesota in the third quarter of 2004.

In 2001, we continued the planned expansion of the Property and Casualty Group s independent agency force by appointing 247 agencies. Since 1997, we have increased the overall number of agencies representing the Property and Casualty Group by 60%.

The Property and Casualty Group has a very stable base of policyholders. The Property and Casualty Group s retention rate of 90.9% in 2001 compared favorably to an average of 82.6% for a core benchmark group consisting largely of regional property and casualty insurers, according to a 2001 Ward Group benchmark study.

The Property and Casualty Group is achieving premium rate increases as a result of the current favorable market conditions in both commercial and personal property and casualty lines, which are generally referred to within the industry as hard market conditions . Hard market conditions are characterized by increasing premium rates, more stringent underwriting standards and a need for additional capital. The Property and Casualty Group and the Company have benefited from these hard market conditions and for the twelve months ended September 30, 2002 experienced average premium per policy increases of 7.2% for personal automobile insurance policies, 17.6% for commercial lines policies and 9.5% across all lines. Management believes increases in premium rates are likely to continue in 2002 and 2003. Generally, the Company s profit margins from management operations have increased during periods of premium rate increases.

As a result of these growth initiatives and market conditions, the Property and Casualty Group had over 3.4 million insurance policies in force as of September 30, 2002, an 11.9% increase from September 30, 2001. Personal lines policies in force grew by 11.8% during the twelve months ended September 30, 2002, while commercial lines policies increased 13.0% over the same period.

The Property and Casualty Group has incurred underwriting losses in recent years, primarily as a result of reducing premium rates in 1998 and 1999 in response to competitive conditions, due to increasing loss severity and due to reinsurance losses, including losses from the terrorist attack on the World Trade Center. Because we have a 5.5% participation in the underwriting results of the Property and Casualty Group, 5.5% of its underwriting losses are reflected in our results of operations. Our share of these underwriting losses, which includes the reinsurance losses, were $3.5 million in 1999, $10.4 million in 2000 and $20.5 million in 2001, respectively.

Each member of the Property and Casualty Group is rated A++ (Superior) by A.M. Best Company, Inc. (A.M. Best), its highest financial strength rating, which was held by only 2.8% of the property and casualty insurance groups rated by A.M. Best as of July 11, 2002.

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Strategy

The Erie Insurance Group s overall strategy includes providing attractive property and casualty insurance products at competitive prices, coupled with high-quality service. The Erie Insurance Group distributes these products exclusively through independent insurance agents whose insurance and underwriting expertise, local market knowledge and commitment to service have been key drivers of Erie Insurance Group s growth. The Erie Insurance Group s strategy includes:

Growth by expansion of existing operations, rather than through acquisition, including by (i) a careful agency selection process in which the Property and Casualty Group seeks to be the primary property and casualty underwriter for each agency, (ii) a thoughtful expansion into favorable states and (iii) increased market penetration in existing operating territories.

Quality service to policyholders in claims handling, underwriting and other service activities.

Achieving underwriting profits for the Property and Casualty Group by focusing on standard and preferred risks and by setting and adhering to consistent underwriting standards.

A business model designed to provide the advantages of localized marketing and claims servicing with the economies of scale derived from centralized management and administration.

Recent Developments

At its meeting on December 10, 2002, our board of directors approved:

the reduction of the management fee rate for 2003 from its previous rate of 25% to 24%, which would have reduced the Company s net income by $15.4 million and net income per share by $0.22, or 11.2%, had such reduction been effective for the nine months ended September 30, 2002;

an increase in the regular quarterly dividend from $0.17 to $0.19 on each share of Class A common stock and from $25.50 to $28.50 on each share of Class B common stock; and

the reduction of the service agreement rate, which relates to the management and administration by us of the Exchange s voluntary assumed reinsurance business from non-affiliated insurers, for 2003 from its previous rate of 7% to 6%, which would have reduced the Company s net income by $891,000 and net income per share by $0.01, or less than 1%, had such reduction been effective for the nine months ended September 30, 2002.

In determining whether to reduce the management fee rate and the service agreement rate, the Company s board of directors considered the relative financial position of the Exchange and the Company, including the surplus levels and underwriting results of the Exchange and the management fee and earnings growth prospects of the Company.

The Company recorded in the fourth quarter of 2002 a one-time charge to net income of $3.9 million, or $.06 per share, to establish an estimated allowance for returned management fees, rather than continuing to make adjustments upon return. This charge recognizes the management fee anticipated to be returned to the Exchange based on historical cancellation rates. The Company did not restate prior period financial statements because the Company believes this adjustment is not material to the trend of earnings for the Company nor any related financial statement amount. Future changes in this allowance will be reflected in the Company s statement of operations and are not expected to be material. Cash flows will not be affected.

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Members of the Property and Casualty Group increased their loss and loss adjustment reserves by approximately $184 million in the fourth quarter of 2002. Approximately $3.1 million to $6.2 million of these increases were for our subsidiaries, which will result in after tax charges to us of approximately $.03 to $.06 in the fourth quarter. The increases in reserves were taken in response to adverse loss experience in the group s automobile, homeowners and workers compensation lines, which was primarily attributable to increased loss severity from automobile bodily injury and catastrophic medical claims in the workers compensation lines.

The Company recognized realized capital losses during the fourth quarter of 2002 of approximately $8.4 million. These losses resulted from the sale of certain securities and from charges for impairments based on the Company s regular periodic review of equity, debt and limited partnership investments held by the Company. The losses will reduce fourth quarter net income by approximately $5.5 million or $.08 per share.

The Offering

Class A common stock offered	3,000,000 shares of our Class A common stock, which is non-voting, are being offered by the Selling Shareholder named below.
Class A common stock outstanding after this offering	64,037,106 shares
Class B common stock outstanding after this offering	2,900 shares
Class B common stock conversion ratio	One share of Class B common stock may be converted into 2,400 shares of Class A common stock.
Class A common stock outstanding after this offering assuming conversion	70,997,106 shares
Dividend history	We declared and paid cash dividends of $0.17 per share of Class A common stock for each of the first three quarters of 2002 and $25.50 per share of Class B common stock for each of the first three quarters of 2002. We declared and paid a cash dividend of $0.19 per share of Class A common stock for the fourth quarter of 2002 and $28.50 per share of Class B common stock for the fourth quarter of 2002.

We have paid regular quarterly cash dividends since 1942. Our board of directors considers the declaration of cash dividends on a quarterly basis. The payment of future dividends, if any, will be at the discretion of our board of directors and will depend upon many factors, including:

- our earnings;
- our financial position;

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our capital requirements and those of our subsidiaries; and

our ability to receive dividends from our subsidiaries, which is subject to regulatory limitations.

There can be no assurance as to the declaration of future dividends.

Use of proceeds	We will not receive any of the proceeds from this offering of our Class A common stock. The Selling Shareholder identified below will receive all the net proceeds from the sale of these shares.
NASDAQ Stock Market[SM] symbol	ERIE

The above information assumes that the option covering an additional 450,000 shares granted by the Selling Shareholder to the underwriters will not be exercised.

The above information is based on the number of shares outstanding as of January 1, 2003.

Selling Shareholder

Black Interests Limited Partnership (the Selling Shareholder) is offering 3.0 million shares of the Company s Class A common stock. The Selling Shareholder has also granted the underwriters a 30-day option to purchase up to an additional 450,000 shares of the Company s Class A common stock. Samuel P. Black, III is the managing general partner of the Selling Shareholder and has the right to vote the shares held by it. Mr. Black has been a director of the Company since 1997 and succeeded his father, who served as a director during various periods from 1930 to 1997. Mr. Black is also an officer and principal shareholder of an insurance agency that receives insurance commissions in the ordinary course of business from the insurance companies we manage, in accordance with the insurance companies standard commission schedules and agents contracts.

A majority of the proceeds of the shares being offered as described in this prospectus will be used by the Selling Shareholder to pay estate taxes and other estate-related expenses arising from the recent death of Mr. Black s mother and to make a charitable bequest.

Corporate Information

We were incorporated in Pennsylvania in 1925. Our principal executive offices are located at 100 Erie Insurance Place, Erie, Pennsylvania 16530, and our telephone number is (814) 870-2000. Our website is located at www.erieinsurance.com. The information on this website is not a part of this prospectus.

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Summary Historical Financial Information

The summary consolidated financial data presented below as of or for the years ended December 31, 1997 through 2001 is derived from our audited financial statements. Our consolidated financial statements as of December 31, 2000 and 2001 and for each of the years in the three-year period ended December 31, 2001, and our independent auditors report thereon, are included elsewhere in this prospectus and incorporated by reference herein. See Where To Find More Information/Incorporation by Reference . The summary consolidated financial data presented below as of or for the nine-month periods ended September 30, 2001 and 2002 is derived from our unaudited consolidated financial statements included elsewhere in this prospectus and incorporated by reference herein. See Where To Find More Information/Incorporation by Reference . Our results of operations for the nine months ended September 30, 2002 are not necessarily indicative of our results of operations that may be expected for the year ended December 31, 2002. In the opinion of our management, all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation have been included. The financial data set forth below is only a summary and should be read in conjunction with our consolidated financial statements and related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations included elsewhere herein.

(amounts in thousands, except per share data)	Nine Months Ended September 30, (unaudited)		Year Ended December 31,				
	2002	2001	2001	2000	1999	1998	1997
Statements of Operations Data:							
Operating revenue	$ 730,029	$ 602,001	$ 799,861	$ 698,016	$ 646,040	$ 615,965	$ 581,979
Operating expense	556,871	466,566	635,756	549,672	501,061	470,155	450,037
Total other income and expenses	33,187	35,408	17,998	70,102	58,731	45,770	38,747
Equity in earnings of Erie Family Life Insurance Company, net of tax	1,015	2,337	719	5,108	4,692	4,443	3,935
Federal income tax expense	69,171	56,835	60,561	71,161	65,296	61,472	56,043
Net income	$ 138,189	$ 116,345	$ 122,261	$ 152,393	$ 143,106	$ 134,551	$ 118,581
Per Share Data:							
Net income per share	$ 1.94	$ 1.63	$ 1.71	$ 2.12	$ 1.95	$ 1.81	$ 1.59
Book value per share	13.50	12.01	12.15	10.91	9.62	8.81	7.25
Weighted average shares outstanding	71,109	71,380	71,342	71,954	73,487	74,400	74,400
Financial Position:							
Investments(1)	$ 969,898	$ 884,599	$ 885,650	$ 853,146	$ 785,258	$ 709,417	$ 566,118
Receivables from the Exchange and affiliates	761,295	650,091	640,655	532,009	470,969	467,794	469,708
Total assets	2,194,690	1,897,077	1,935,566	1,680,599	1,518,794	1,454,062	1,292,544
Shareholders equity	958,274	855,755	865,255	779,015	697,599	655,223	539,383

(1) Includes investment in Erie Family Life Insurance Company.

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RISK FACTORS

You should consider carefully the risks and uncertainties described below and the other information in this prospectus, including our consolidated financial statements and related notes, before deciding to invest in shares of our Class A common stock. If any of the following risks or uncertainties actually occur, our business, financial condition and operating results would likely suffer. In that event, the market price of our Class A common stock could decline and you could lose all or part of the money you paid to buy our Class A common stock.

Risks Relating to Our Business and Our Relationships with Third Parties

If the management fee rate paid to us by the Exchange is further reduced, if there is a significant decrease in the amount of premiums written by the Exchange or if we do not control the costs of providing services to the Exchange, our revenues and profitability could be materially adversely affected.

We are dependent upon management fees paid to us by the Exchange, which represent our principal source of revenue. Management fees from the Exchange constituted 78% of our revenues for the first nine months of 2002, 78% of our revenues for 2001, and 74% of our revenues during the three years ended December 31, 2001. The management fee rate we receive is determined by our board of directors and may not exceed 25% of the direct written premiums of the Property and Casualty Group. Since 1999, the management fee rate has been 25%. In 1998 and 1997, the management fee rate was 24.25% and 24%, respectively.

Our board of directors generally sets the management fee rate each December for the following year. However, at their discretion, the rate can be changed at any time. The factors our board of directors consider in setting the management fee rate include our financial position in relation to the Exchange and the long-term needs of the Exchange for capital and surplus to support its continued growth and competitiveness. The Exchange s capital and surplus could become impaired due to a number of factors, including those discussed under Risks Relating to the Business of the Property and Casualty Group and Risks Relating to the Property and Casualty Insurance Industry below. In light of factors including the strong growth of the Exchange s premium base and the decline in the policyholders surplus of the Exchange from $4.8 billion at December 31, 1999 to $2.1 billion at September 30, 2002, the management fee rate for 2003 was reduced to 24% at our board s December 2002 meeting.

If our board of directors were to determine that the management fee rate should be further reduced, our revenues and profitability could be materially adversely affected. For example, a 1% reduction in the management fee rate during the nine months ended September 30, 2002 would have resulted in a reduction in our net revenues of $23.8 million, or 12.6%, and a reduction in our net income per share of $0.22, or 11.2%. A similar decrease of 1% during 2001 would have resulted in a reduction in our net revenues of $25.4 million, or 13.8%, and a reduction in our net income per share of $0.23, or 13.5%.

Our management fee revenue from the Exchange is calculated by multiplying the management fee rate by the direct premiums written by the Exchange and the direct premiums written by the other members of the Property and Casualty Group, which are initially assumed by the Exchange. Accordingly, any reduction in direct premiums written by the Property and Casualty Group would have a proportional negative effect on our revenues and net income.

Pursuant to the attorney-in-fact agreements with the policyholders of the Exchange, the Company is appointed to perform certain services, regardless of the cost to the Company of providing those

services. These services relate to the sales, underwriting and issuance of policies on behalf of the Exchange. We could lose money or be less profitable if our cost of providing those services increases significantly.

Our board of directors faces certain conflicts of interest because it must balance fiduciary obligations to policyholders of the Exchange and to our shareholders; thus our board of directors must make decisions that are not solely in the interests of our shareholders.

The Exchange has no board of directors or governing body of its own. In our capacity as attorney-in-fact, we have a fiduciary duty to the policyholders of the Exchange to protect their interests. Likewise, we have a fiduciary duty to our shareholders. Certain conflicts of interest arise from these separate fiduciary duties. Among these conflicts of interest are:

- Our board of directors sets the management fee rate paid by the Exchange to us and decides the percentage participation rate of our property and casualty subsidiaries in the pool.
- We make judgments about the allocation of shared costs between the Exchange and the Company in accordance with intercompany agreements and the attorney-in-fact agreements with the policyholders of the Exchange, including costs relating to the eCommerce program.
- The Exchange may enter into other transactions and contractual relationships with the Company and its subsidiaries.

As a consequence, our board of directors must make decisions or take actions that are not solely in the interests of our shareholders. If, for example, there should be a need to strengthen the surplus of the Exchange, our board of directors may decide to reduce the management fee rate and/or that we should make a capital contribution to the Exchange in the form of a surplus note or some other form. Under such circumstances, we may be required to provide such capital to the Exchange at a lower rate of return than would be available with other investments or at no return at all. Payments of interest and repayment of principal on a surplus note are subject to prior approval of the Pennsylvania Department of Insurance, which may not approve such payments. We may also find it necessary to fund additional surplus for the Exchange by issuing additional shares of our capital stock, resulting in dilution of existing shareholders interest. In addition, state regulators could challenge the reasonableness of the transactions between us and the Exchange.

We are subject to credit risk to the Exchange because our management fees from the Exchange are not paid immediately when earned and our insurance subsidiaries are subject to credit risk to the Exchange because the Exchange assumes a higher insurance risk under an intercompany pooling arrangement than is proportional to its direct business contribution to the pool.

We recognize management fees due from the Exchange as income when the premiums are written because at that time we have performed substantially all of the services we are required to perform, including sales, underwriting and policy issuance activities, but currently such fees are not paid to us by the Exchange until it collects the premiums. As a result, we hold receivables for management fees due us for premiums written but not yet collected by the Exchange. In addition, we hold receivables from the Exchange for costs we pay on its behalf and for reinsurance under the intercompany pooling arrangement. Our total receivables from the Exchange, including the management fee, costs we pay on behalf of the Exchange and reinsurance recoverables, totaled $759.6 million, or 34.6% of our total assets at September 30, 2002, and $638.4 million, or 33.0% of our total assets at December 31, 2001. The receivables represented 12.3% of the Exchange s assets at September 30, 2002 and 9.1% at December 31, 2001.

The Exchange and two of our wholly owned subsidiaries, Erie Insurance Company and Erie Insurance Company of New York, are parties to an intercompany pooling arrangement. Under this pooling arrangement, our insurance subsidiaries cede 100% of their property and casualty underwriting business to the Exchange, which retrocedes 5% of the pooled business to Erie Insurance Company and 0.5% to Erie Insurance Company of New York. In 2001, only approximately 81.4% of the pooled direct property and casualty business was originally generated by the Exchange and its subsidiary, while 94.5% of the pooled business is retroceded to the Exchange under the intercompany pooling arrangement. Accordingly, the Exchange assumes a higher insurance risk than is proportional to the insurance business it contributes to the pool. In 2001, our subsidiaries wrote 18.6% of the direct premiums, while assuming only 5.5% of the risk. This poses a credit risk to our subsidiaries participating in the pool because they are still responsible ultimately to the policyholders for policies they have written if the Exchange is unable to meet its obligations.

Our financial condition may suffer because of declines in the value of the marketable securities that constitute a significant portion of our assets.

At September 30, 2002, we had investments in marketable securities of approximately $828 million and investments in limited partnerships of approximately $89 million. In addition, we are obligated to invest up to an additional $116 million in limited partnerships, including in partnerships for U.S. and foreign private equity, real estate and fixed income investments. All of our marketable security investments are subject to market volatility. Our fixed income securities investments are exposed to price risk and to risk from changes in interest rates as well as credit risk related to the issuer. Generally, we do not hedge our exposure to interest rate risk as we have the ability to hold fixed income securities to maturity. Our marketable securities have exposure to price risk and the volatility of the equity markets and general economic conditions. The stock market decline in 2002 has reduced the value of our marketable securities by $6.8 million during the first nine months of 2002, compared to $3.4 million during the first nine months of 2001. To the extent that future market volatility negatively impacts our investments, our results of operations will be negatively impacted.

The two individual trustees of our controlling shareholders, the H.O. Hirt Trusts, have significantly differing views on a number of matters relating to the Company; such disagreements may have an adverse effect on our business and on the value of our Class A common stock.

Two trusts established by our founder, H.O. Hirt (the H.O. Hirt Trusts), own 80.7% of our Class B common stock, which is the only class of stock that can vote for the election of directors and has the ability to determine the outcome of all other matters that require shareholder approval, except those matters pertaining only to the rights of the holders of our Class A common stock. The corporate trustee of the H.O. Hirt Trusts is Bankers Trust Company of New York (Bankers Trust) and the two individual trustees of the H.O. Hirt Trusts are F. William Hirt and Susan Hirt Hagen, who are brother and sister and the children of H.O. Hirt. Any determination by the H.O. Hirt Trusts requires a vote of two of the three trustees and, because the H.O. Hirt Trusts control 80.7% of our Class B common stock, any such determination will be controlling in a shareholder vote. Mrs. Hagen and Mr. Hirt disagree on a number of matters relating to corporate governance, the appointment of a successor corporate trustee and the financial condition of the Exchange.

Mrs. Hagen has recently raised concerns regarding a number of such matters, including: the role of the H.O. Hirt Trusts as controlling shareholders in the governance of the Company; the propriety of a corporate trustee of the H.O. Hirt Trusts engaging in insurance brokerage activities; the restructuring of our board of directors so that a majority of the directors are independent of management; the restructuring of the committees of our board of directors to provide a more meaningful role for directors who do not have ongoing business relationships with us; the desirability of more liquidity and increased

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institutional investor interest in the Company and the allocation of expenses between the Exchange and us.

Mrs. Hagen on one occasion commenced litigation against us in connection with corporate governance matters and has participated in litigation involving the H.O. Hirt Trusts brought by each of the trustees of the H.O. Hirt Trusts and by other beneficiaries of the H.O. Hirt Trusts. On two occasions in the recent past, Mr. Hirt brought a suit, which was subsequently withdrawn without prejudice, seeking the removal of Mrs. Hagen as an individual trustee. The effect of these disagreements and concerns and possible future disagreements between Mrs. Hagen and Mr. Hirt on us and the value of our Class A common stock cannot be predicted.

Mrs. Hagen, who is a member of our board of directors, a trustee and a beneficiary of the H.O. Hirt Trusts and a beneficial owner of approximately 26.2% of our Class A common stock, is opposed to our participation in this offering because she believes there may be a better alternative for us and may take additional actions to oppose this offering.

The concerns that Mrs. Hagen has expressed to our board of directors about this offering include:

- the amount of time and effort required of our officers to prepare a registration statement relating to this offering and to assist in the marketing of the shares offered hereby instead of fully concentrating their efforts on business and financial issues confronting Erie Insurance Group;
- the liability of our directors and the H.O. Hirt Trusts if the registration statement, including this prospectus, were determined to contain a material misstatement or a material omission and the indemnification by us of the underwriters for certain potential liabilities under federal securities laws related to this offering;
- the need for the Company to consider retention of a national auditing firm;
- the impact of the offering on our ability to attract independent director candidates during this offering because of the potential liability associated therewith;
- doubts whether a public offering would unlock any long-term value for our shareholders;
- concerns that increased public holdings of our Class A common stock will attract institutional investors; and
- her opinion that a below-market purchase by us of the shares being offered by the Selling Shareholder would be more advantageous to us.

Our board of directors considered Mrs. Hagen s concerns at meetings held on August 16, 2002 and September 9, 2002. At each meeting, Mrs. Hagen was the only member of our board of directors present to vote against proceeding with this offering. We are unable to predict whether Mrs. Hagen or any other trustee or any other beneficiary of the H.O. Hirt Trusts may take additional actions to oppose this offering.

Mrs. Hagen has also recently proposed five amendments to the Company s Bylaws for consideration by the voting shareholders at the Company s annual meeting of shareholders for 2003. These amendments concern (i) revising the existing advance notice bylaw to provide that direct nomination by voting shareholders of candidates for director are not due until after our nominating committee announces its proposed slate rather than generally not less than 90 calendar days nor more than 120 calendar days before the first anniversary of the date on which the Company first mailed its proxy statement to shareholders for the immediately preceding year s annual meeting of shareholders as currently provided; (ii) revising the advance notice bylaw to provide that other shareholder proposals for annual meetings must be submitted not less than 60 nor more than 120 days prior to the first anniversary of the prior year s annual meeting rather than generally not less than 90 calendar days nor more than 120 calendar days before the first anniversary of the date on which the

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Company first mailed its proxy statement to shareholders for the immediately preceding year s annual meeting of shareholders as currently provided; (iii) fixing the size of our board of directors at 13 members rather than not less than 7 members nor more than 16 members as determined from time to time by our board of directors as currently provided; (iv) providing that vacancies on our board of directors only may be filled by the voting shareholders rather than by a majority vote of remaining members of our board of directors or the voting shareholders as currently provided and (v) providing that the bylaw provisions containing the foregoing may not be amended without a vote of the voting shareholders rather than by a majority vote of our board of directors or the voting shareholders as currently provided.

Mrs. Hagen s proposals to amend the Company s Bylaws were timely submitted in accordance with the Company s Bylaws applicable to shareholder proposals other than the nomination of directors. If these proposals are presented by Mrs. Hagen at the Company s 2003 annual meeting of shareholders, approval of the proposals would require the affirmative vote of a majority of the shares of the Company s Class B common stock voting at the annual meeting. Under the provisions of the H.O. Hirt Trusts, which have the power to vote 80.7% of the outstanding Class B common stock, the shares of Class B common stock held by the H.O. Hirt Trusts are to be voted as directed by a majority of the trustees then in office. The current trustees are Mrs. Hagen, Mr. Hirt and Bankers Trust. The Company has not been advised to date by the trustees of the H.O. Hirt Trusts as to how they intend to vote on Mrs. Hagen s proposals.

In addition, Mrs. Hagen has sent the Company a notice requesting that the Company s nominating committee consider a slate of director nominees proposed by her for election at the 2003 annual meeting of shareholders. Mr. Hirt has sent the Company a notice requesting that the Company s nominating committee consider certain other persons as director nominees. At the Company s 2000 annual meeting of shareholders, five nominees nominated by Mrs. Hagen and who were not nominated by our nominating committee were elected as directors of the Company and seven nominees nominated by our nominating committee were elected as directors of the Company. At the Company s 2001 and 2002 annual meetings of shareholders, all of the nominees nominated by our nominating committee, who were the same as the directors elected in 2000, were elected as directors of the Company and no nominees other than those nominated by our nominating committee were elected as directors. The Company has not been advised to date by the trustees of the H.O. Hirt Trusts as to the director nominees for whom they intend to vote at the 2003 annual meeting of shareholders.

Laurel A. Hirt, a beneficiary of the H.O. Hirt Trusts and the daughter of Mr. Hirt, the chairman of our board of directors, has requested that the trustees of the H.O. Hirt Trusts take appropriate actions to stop this offering and may take additional actions to oppose this offering.

On January 24, 2003, Laurel A. Hirt addressed a letter to the trustees of the H.O. Hirt Trusts, who are Mr. Hirt, Mrs. Hagen and Bankers Trust, and copied our board of directors, requesting that the trustees direct our board of directors to withdraw their support for this offering and direct management of the Company to withdraw this offering. Ms. Hirt expressed the view that permitting the Company to engage in an offering that would expand the base of shareholders to possibly include more investors whose interests may be adverse to the H.O. Hirt Trusts creates an undue and unacceptable risk for the H.O. Hirt Trusts and could make the H.O. Hirt Trusts more vulnerable to lawsuits. Ms. Hirt also cited certain passages of this prospectus that she felt could be considered material and misleading to potential investors and that could create liability to the H.O. Hirt Trusts as a controlling person. Ms. Hirt indicated she would consider initiating legal actions against the trustees of the H.O. Hirt Trusts, our directors and our management if this offering is not stopped and harm comes to the H.O. Hirt Trusts, the Exchange or the Company as a result of this offering.

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We have evaluated Ms. Hirt s concerns regarding disclosure in this prospectus and do not believe that any of her concerns indicates that there is any material misstatement or omission in this prospectus. There can be no assurance that Ms. Hirt will not take additional actions to oppose this offering or initiate litigation as a result of this offering. The effect of any such actions on us and the value of our Class A common stock cannot be predicted.

Decisions by the corporate trustee of the H.O. Hirt Trusts or a successor to either of the individual trustees could materially alter our management, strategic direction, operating philosophy or other matters material to us.

Bankers Trust tendered its resignation as corporate trustee of the H.O. Hirt Trusts on March 3, 1999, 36 days after it had been appointed as a result of conflicts of interest that Bankers Trust believed existed from certain insurance operations of its parent company and affiliates. Also, an affiliate of Bankers Trust, Deutsche Bank, is one of the largest market makers in the Company s stock. The selection of a new corporate trustee of the H.O. Hirt Trusts to replace Bankers Trust is pending before Orphan s Court in Erie County, Pennsylvania. We cannot predict or estimate when a replacement corporate trustee will be chosen to replace Bankers Trust or who it will be. Because any action of the H.O. Hirt Trusts requires a vote of two of the three trustees and because Mrs. Hagen and Mr. Hirt have significantly differing views, the vote of the corporate trustee has been, and will likely continue to be, determinative of the actions of the H.O. Hirt Trusts. There are a number of circumstances in which a successor to one of the individual trustees would be appointed, including the death of an individual trustee. If an individual trustee is to be appointed, under the terms of the H.O. Hirt Trusts, the remaining individual trustee, the corporate trustee and our board of directors may select a replacement individual trustee or, if no successor is selected within 30 days, the remaining trustees and the Company shall petition the Court of Common Pleas of Erie County, Pennsylvania to fill said vacancy under the trust agreement. Mr. Hirt is 77 years old and Mrs. Hagen is 67 years old. Decisions by the existing trustees or successor trustees, including supporting a slate of directors put forth by Mrs. Hagen or another shareholder, could materially alter our management, strategic direction, operating philosophy or other matters material to us. It is impossible to determine how these decisions may affect the value of the Company and therefore our Class A common stock.

Risks Relating to the Business of the Property and Casualty Group

The Property and Casualty Group conducts business in only 11 states and the District of Columbia, with a concentration of business in Ohio, Maryland, Virginia and, particularly, Pennsylvania. Any single catastrophe occurrence or other condition disproportionately affecting losses in these states could adversely affect the results of operations of members of the Property and Casualty Group.

The Property and Casualty Group conducts business in only 11 states and the District of Columbia, primarily in the Mid-Atlantic, Midwestern and Southeastern portions of the United States. A substantial portion of this business is private passenger and commercial automobile, homeowners and workers compensation insurance in Ohio, Maryland, Virginia and, particularly, Pennsylvania. As a result, a single catastrophe occurrence, destructive weather pattern, general economic trend, terrorist attack, regulatory development or other condition disproportionately affecting one or more of the states in which the Property and Casualty Group conducts substantial business could materially adversely affect the results of operations of members of the Property and Casualty Group. Common catastrophe events include hurricanes, earthquakes, tornadoes, wind and hail storms, fires and explosions. Recent ice storms in North Carolina and tornadoes and hail in Ohio and Pennsylvania during November and December 2002 are examples of the type of event that can negatively impact underwriting results. The Property and Casualty Group estimates the combined exposure from the approximately 4,500 damage claims from these storms will result in incurred losses of approximately $21 million to $24 million, our share of which will be approximately $1.3 million or $.01 per share after taxes. Effective January 1, 2003, the Property and Casualty Group entered into a property catastrophe reinsurance treaty that provides coverage of 95% of a loss up to $415 million in excess of the Property and Casualty Group s loss retention of $115 million per occurrence.

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The operating results of the Exchange are subject to greater variability because the Property and Casualty Group generally did not maintain reinsurance coverage after 1993 through 2002.

The Property and Casualty Group did not purchase treaty reinsurance, including catastrophe reinsurance, after 1993 through 2002, because management concluded, during our periodic assessments of the Property and Casualty Group s catastrophe exposure, that the benefits of such coverage were outweighed by the costs of the coverage in light of the Exchange s substantial surplus and its ratio of net premiums written to surplus. The Property and Casualty Group did obtain property catastrophe treaty reinsurance to protect its 2003 accident year underwriting results from catastrophes. The lower surplus levels of the Exchange, along with increasing catastrophe risk exposure as a result of accelerating policy growth, have resulted in management s decision to purchase property catastrophe treaty reinsurance coverage. The Exchange s reported surplus totaled $2.1 billion at September 30, 2002 compared to $4.8 billion at December 31, 1999, a reduction of 56%.

We cannot determine whether the Exchange s profitability could have been improved in years after 1993 through 2002 if the Exchange had purchased treaty reinsurance because it is impossible to establish the terms on which the Exchange might have obtained such reinsurance. If the recently purchased property catastrophe treaty reinsurance had been in effect during 2002, there would have been no recoveries and the profitability of the Exchange would not have been affected except by the cost of such reinsurance. The risk of not maintaining reinsurance coverage in the event of a significant catastrophe or a series of moderate catastrophes in the same year means that surplus levels could be exposed to dramatic decline should such catastrophes occur. Reinsurance for catastrophe exposure protects the balance sheet and income statement against large and infrequent events and reduces the variability of earnings. A dramatic decline in the surplus levels would result in pressure to reduce premium writings, and thereby, curtail growth of our property and casualty subsidiaries. Without the benefit of higher surplus levels, the ability of the Exchange to write additional premium would be reduced and so would be the Company s opportunity to grow.

Variability in the Exchange s financial results can affect our financial results in several ways. The management fee rate charged to the Exchange by us is set based in substantial part on a review of the relative financial condition and operating results of the Exchange and us. Deterioration in the financial condition and operating results of the Exchange could result in a reduction in the management fee rate paid to us or could constrain the capacity of the Exchange to write additional premium, which would reduce management fees paid to us. In addition, if the Exchange s financial condition worsened considerably we could be subject to greater credit risk related to our large accounts receivable balance due from the Exchange.

The business and results of operations of the Property and Casualty Group will be adversely affected if the independent agents that market the Property and Casualty Group s products do not maintain their current levels of premium writing, fail to comply with established underwriting guidelines or otherwise improperly market our products.

The Property and Casualty Group markets its insurance products solely through a network of over 1,700 independent insurance agencies. As a result, the Property and Casualty Group is wholly dependent upon these agencies, each of which has the authority to bind the Property and Casualty Group to insurance contracts. To the extent that these agencies marketing efforts cannot be maintained at their current levels of volume and quality or they bind the Property and Casualty Group to unacceptable insurance risks, fail to comply with established underwriting guidelines or otherwise improperly market our products, the results of operations and business of the Property and Casualty Group will suffer.

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The business of the Property and Casualty Group may not continue to grow and may be materially adversely affected if the Company cannot retain existing, and attract new, independent agencies or if insurance consumers increase use of other insurance delivery systems.

The continued growth of the business of members of the Property and Casualty Group is partially dependent upon the Company s ability to retain existing, and attract new, independent agencies for the Property and Casualty Group. The following factors are among those that may cause the growth and retention in the number of independent agencies of the Property and Casualty Group, and thereby growth in revenue of its members, to be slower than it otherwise would have been:

- There is significant competition to attract independent agencies;
- Our process to select a new independent agency is intensive and typically requires from six to nine months;
- The Company has stringent criteria for new independent agencies and requires adherence by independent agencies to consistent underwriting standards; and
- The Company may be required to reduce agents commissions, bonuses and other incentives, thereby reducing our attractiveness to agencies.

The Property and Casualty Group sells insurance solely through its network of independent agencies. The Property and Casualty Group s competitors sell insurance through a variety of delivery methods, including independent agencies, captive agencies, the Internet and direct sales. To the extent that business migrates to a delivery system other than independent agencies because of changing consumer preferences, the business of the Property and Casualty Group will be adversely affected.

The Property and Casualty Group has incurred underwriting losses in recent years primarily as a result of reducing premium rates in 1998 and 1999 in response to competitive conditions, due to increased loss severity and due to reinsurance losses, including losses from the terrorist attack on the World Trade Center. To the extent underwriting losses continue, the management fee revenues we receive may be reduced, in addition to the continuing adverse effect on our operating results from our subsidiaries 5.5% participation in the underwriting results of the Property and Casualty Group.

In 1997 and 1998, the property and casualty insurance market was marked by soft market conditions, which are characterized by decreased revenues, less stringent underwriting standards and an excess of surplus in the industry. These conditions created severe price competition in commercial and personal lines of insurance, including private passenger automobile, the Property and Casualty Group s largest line of business. These competitive conditions resulted in slower new policy growth and declines in policy retention rates for the Property and Casualty Group. Management viewed these competitive effects as a serious threat to the well-being of the Property and Casualty Group. In 1998, following discussions with our board of directors, management decided to reduce premium rates in 1998 and 1999 in order to retain the Property and Casualty Group s most profitable customers. The 1998 and 1999 premium rate reductions, coupled with a general trend of increasing loss severity, negatively affected the Property and Casualty Group s underwriting results, which increased from underwriting losses of $49.8 million in 1999 to $189.7 million in 2000 and $517.3 million in 2001. In 1999, 2000 and 2001, the Property and Casualty Group also incurred significant underwriting losses from its non-affiliated assumed reinsurance business, including $55 million in losses from wind storms in Western Europe in late December 1999 and $150 million from the World Trade Center terrorist attack in September 2001, assuming that attack is treated as one occurrence.

The Property and Casualty Group and the Company have responded to underwriting losses in a number of ways, including adopting stricter underwriting requirements; restricting policy coverages; increasing the emphasis on reviewing existing policies and accounts to determine which risks continue

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to meet underwriting guidelines and taking appropriate action regarding those policies and accounts that do not; continuing the focus on claims strategies to reduce claims severity, such as reducing claims fraud; raising premium rates on its direct lines of insurance; reunderwriting all of its assumed reinsurance treaties, resulting in the cancellation of a significant number of treaties and the reduction in total aggregate limits for other treaties; significantly raising reinsurance premium rates; and excluding terrorism coverage from all reinsurance treaties entered into in 2002. However, there can be no assurance that the measures taken or that may be taken by the Property and Casualty Group and the Company will meet or exceed increases in loss costs or restore the Property and Casualty Group s underwriting profitability.

To the extent underwriting losses continue, our operating results will suffer from our subsidiaries 5.5% participation in the pooling arrangement. In addition, the Exchange s policyholders surplus will be further adversely affected. If the surplus of the Exchange were to decline significantly from its current level, the Property and Casualty Group could find it more difficult to retain its existing business and attract new business. A decline in the business of the Property and Casualty Group would have an adverse effect on the amount of the management fees we receive and the underwriting results of the Property and Casualty Group in which we have a 5.5% participation. In addition, a decline in the surplus of the Exchange from its current level would make it more likely that the management fee rate received by us would be further reduced.

The surplus of the Exchange has decreased from $4.8 billion at December 31, 1999 to $2.1 billion at September 30, 2002. Of this decrease, approximately $1.6 billion was because of declines in the market value of marketable securities investments, including the significant portfolio of common equity securities. To the extent these declines in market value continue and the Exchange s surplus continues to decrease, the management fee rate we receive may be further reduced and the underwriting results of our property and casualty subsidiaries may suffer.

In 1985, the Exchange increased its investments in common equity securities as a core element of its investment strategy. At December 31, 1999, when the Exchange s surplus was $4.8 billion, the Exchange s portfolio of marketable securities investments included common equity securities that had appreciated in value by $2.6 billion, to a market value of $3.8 billion. However, as a result of the downturn in common equity markets since 1999, the Exchange s portfolio of common equity securities has experienced a decline in value of $1.8 billion and the value of the portfolio was $2.0 billion at September 30, 2002. The common equity portfolio of the Exchange represents 32.8% of its admitted assets at September 30, 2002 while the entire portfolio of marketable securities investments represents 76.0% of its admitted assets at that date.

All marketable securities held by the Exchange are subject to market volatility. The Exchange s marketable securities have exposure to price risk and the volatility of capital markets. The stock market decline in 2002 has reduced the value of the Exchange s marketable securities by $1.3 billion during the first nine months of 2002 compared to the decrease of $1.0 billion during the first nine months of 2001.

To the extent that the Exchange incurs additional investment losses resulting from declines in the value of its marketable securities, the Exchange s policyholders surplus will be further adversely affected. If the surplus of the Exchange were to decline significantly from its current level, the Property and Casualty Group could find it more difficult to retain its existing business and attract new business. A decline in the business of the Property and Casualty Group would have an adverse effect on the amount of the management fees we receive and the underwriting results of the Property and Casualty Group in which we have a 5.5% participation. In addition, a decline in the surplus of the Exchange from its current level would make it more likely that the management fee rate received by us would be further reduced.

Erie Insurance Group s recent efforts to develop technology, including Internet capabilities, to enhance policy administration and to improve interaction with agents may be more costly than we anticipate, may not be completed due to cost or technology considerations and may increase our exposure to breaches of privacy or security.

Customers and agents expect rapid turnaround of quotes and endorsements and efficient services. Failure to meet these service expectations could place the Erie Insurance Group at a competitive disadvantage. To remain competitive, the Erie Insurance Group has undertaken an initiative, called ERIEConnection SM , to utilize technology, including the Internet, to automate certain functions to facilitate quoting, underwriting and the issuing of policies and provide these services directly to its agents via the Internet. Such an upgrading of technology requires a sizable financial investment. Moreover, the effectiveness of certain areas of technology remain unproven. Erie Insurance Group completed the first major component of the program during the second quarter of 2002. Through September 30, 2002, the Erie Insurance Group has spent $87 million on its current technology development efforts. The timing, scope and level of spending for remaining deliverables under the program are uncertain. Actual costs to complete the technology initiatives may exceed anticipated costs and lead to a reduction in profits or the termination of these technology initiatives. In addition, use of Internet technology to connect directly with the Property and Casualty Group s agents increases the risk of security breaches, which may cause short-term or long-term disruptions to the Property and Casualty Group s business operations and could lead to further and currently unanticipated technology costs to prevent and mitigate the effects of such security breaches.

If ratings for financial strength assigned to members of the Property and Casualty Group by industry rating organizations were significantly downgraded, the Property and Casualty Group s competitive position in the insurance industry would be adversely affected.

Ratings are a factor in establishing the competitive position of insurance companies. Members of the Property and Casualty Group receive ratings from A.M. Best and Standard & Poor s, which are industry-accepted measures of an insurance company s financial strength and are specifically designed to provide an independent opinion of an insurance company s financial health and ability to meet ongoing obligations to policyholders. Members of the Property and Casualty Group are also rated by Weiss Ratings, Inc., which is a consumer-oriented rating company that issues ratings designed to provide an independent opinion of an insurance company s financial strength. The ratings by Weiss Ratings, Inc. for the Exchange and Erie Insurance Company were downgraded in July 2002. In addition, in January 2003, the Company was notified by Standard & Poor s that the ratings for members of the Property and Casualty Group were under review and may be downgraded. Ratings are not recommendations to buy, sell or hold our common stock and are subject to change. A description of the Company s recent ratings appears under Business Financial Ratings beginning on page 63.

If the Exchange or any other member of the Property and Casualty Group were to incur underwriting losses or reductions in surplus for an extended period of time, the ratings of such entity may be downgraded. While management of the Company believes that recent downgrades by Weiss Ratings, Inc. have not impacted any member of the Property and Casualty Group, a significant future downgrade in these or other ratings would reduce the competitive position of the affected member by making it more difficult to attract profitable business in the highly competitive property and casualty insurance market.

Risks Relating to the Property and Casualty Insurance Industry

The Property and Casualty Group faces significant exposure to terrorism.

The tragic World Trade Center terrorist attack resulted in staggering losses for the insurance industry and has caused uncertainty in the insurance and reinsurance markets. The Property and Casualty Group incurred a loss of $150 million in this attack assuming it continues to be considered

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one occurrence, and it estimates it would incur an additional loss of $50 to $75 million if the attack is considered two occurrences. The Company s 5.5% share of this incurred loss was $5.8 million. Accordingly, the industry has been compelled to re-examine policy language and to address the potential for future threats of terrorist events and losses. The Property and Casualty Group s personal and commercial property and casualty insurance policies were not priced to cover the risk of terrorist attacks and losses such as those suffered in the World Trade Center terrorist attack. The Property and Casualty Group has withdrawn from some coverages and exposures, including terrorism, where permitted by state regulators. However, even in states where withdrawal has been permitted, the Property and Casualty Group is still exposed to terrorism under several lines, including personal lines and workers compensation, and, in most states, losses caused by an ensuing fire. On November 26, 2002, President Bush signed the Terrorism Risk Insurance Act of 2002, establishing a program for commercial property and casualty losses, including workers compensation, resulting from foreign acts of terrorism. The Terrorism Risk Insurance Act requires commercial insurers to make terrorism coverage available immediately and provides limited federal protection above individual company retention levels, based upon a percentage of direct earned premium, and above aggregate industry retention levels that range from $10 billion in the first year to $15 billion in the third year. The federal government will pay 90% of covered terrorism losses that exceed retention levels. The Terrorism Risk Insurance Act is scheduled to expire on December 31, 2005. Personal lines are not included under the protection of the Terrorism Risk Insurance Act, and state regulators have not approved exclusions for acts of terrorism on personal lines policies. The Property and Casualty Group could incur large unexpected losses if future terrorist attacks occur.

Even excluding terrorism exposure, the Property and Casualty Group faces the threat of substantial catastrophe losses and did not maintain treaty reinsurance coverage for catastrophe losses after 1993 through 2002.

The Property and Casualty Group has experienced, and can be expected in the future to experience, catastrophe losses that may have a material adverse impact on our results of operations and financial condition. The Property and Casualty Group did not maintain treaty reinsurance coverage to mitigate the impact of catastrophe losses after 1993 through 2002; however, effective January 1, 2003, the Property and Casualty Group has obtained property catastrophe reinsurance coverage. Catastrophes can be caused by various events, including hurricanes, earthquakes, tornadoes, wind, hail, fires, explosions and man-made disasters. The incidence and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of two factors: the total amount of insured exposure in the area affected by the event and the severity of the event. Most catastrophes are localized to small geographic areas; however, events such as hurricanes, hail and ice storms have the potential to produce significant damage in large, heavily populated areas.

For the Property and Casualty Group, areas of major potential hurricane loss include major metropolitan centers in the eastern United States and areas of major potential ice storm or hail loss include major metropolitan centers in the Mid-Atlantic and Midwestern states. Although catastrophes can cause losses in a variety of property and casualty lines, homeowners insurance has in the past generated the vast majority of catastrophe-related claims. At December 31, 2001, 76% of the Property and Casualty Group s total homeowners insurance exposure was comprised of risks in Mid-Atlantic states, which exposes the Property and Casualty Group to significant risk of loss from catastrophes in that region.

Increased litigation against the industry, willingness of courts to expand covered causes of loss, rising jury awards, increasing medical costs and the escalation of loss severity may contribute to increased costs and to the deterioration of reserve positions of the Property and Casualty Group.

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Loss severity for the Property and Casualty Group continues to increase, principally driven by larger court judgments and increasing medical costs in recent years. In addition, many legal actions and proceedings have been brought on behalf of classes of complainants, which can increase the size of judgments. The propensity of policyholders to litigate and the willingness of courts to expand causes of loss and the size of awards may render loss reserves inadequate for current and future losses. Loss reserves are liabilities established by insurers and reinsurers to reflect the estimated cost of loss payments and the related loss adjustment expenses that the insurer or reinsurer will ultimately be required to pay in respect of insurance or reinsurance it has written.

The Property and Casualty Group has exposure to mold claims for which there has recently been a sharp increase in the industry generally. Sometimes referred to as sick building syndrome , tenants claiming to suffer illnesses caused by mold may seek financial compensation from building owners. Businesses also may claim loss-of-use business income interruption losses. Homeowners have also been submitting claims based on mold that has occurred from water damage. The Property and Casualty Group s exposure to date, including known and expected claims, has been insignificant.

Members of the Property and Casualty Group increased their loss and loss adjustment reserves by approximately $184 million in the fourth quarter of 2002 in response to adverse loss experience in the group s automobile, homeowners and workers compensation lines. To the extent that adverse trends continue, including expansion by courts of covered causes of loss, rising jury awards, increasing medical costs and the escalation of loss severity, the Property and Casualty Group may need to further increase reserves and its profitability may be adversely affected.

Changes in applicable insurance laws, regulations or changes in the way regulators administer those laws or regulations could materially adversely change the Property and Casualty Group s operating environment and increase its exposure to loss or put it at a competitive disadvantage.

Property and casualty insurers are subject to extensive supervision in the states in which they do business. This regulatory oversight includes, by way of example, matters relating to licensing and examination, rate setting, market conduct, policy forms, limitations on the nature and amount of certain investments, claims practices, mandated participation in involuntary markets and guaranty funds, reserve adequacy, insurer solvency, transactions between affiliates, the amount of dividends that may be paid and restrictions on underwriting standards. Such regulation and supervision are primarily for the benefit and protection of policyholders and not for the benefit of shareholders. For instance, members of the Property and Casualty Group are subject to involuntary participation in specified markets in various states in which it operates, and the rate levels the Property and Casualty Group is permitted to charge do not always correspond with the underlying costs associated with the coverage issued.

The National Association of Insurance Commissioners (NAIC) and state insurance regulators are re-examining existing laws and regulations, specifically focusing on insurance company investments, issues relating to the solvency of insurance companies, risk-based capital guidelines, interpretations of existing laws and the development of new laws. Changes in state laws and regulations, as well as changes in the way state regulators view related party transactions in particular, could materially change the operating environment for the Property and Casualty Group and significantly increase the amount of loss to which the Property and Casualty Group is exposed after an insurance policy has been issued.

The state insurance regulatory framework recently has come under increased federal scrutiny. Congress is considering legislation that would create an optional federal charter for insurers. Federal chartering has the potential to create an uneven playing field for insurers. Federally chartered

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companies could be subject to different regulatory requirements than state chartered insurers in areas such as market conduct oversight, solvency regulation, guaranty fund participation and premium tax burdens. If this occurs, federally chartered insurers may obtain a competitive advantage over state licensed carriers. Federal chartering also raises the specter of a matrix of regulation and costly duplicative, or conflicting, federal and state requirements. Specific federal regulatory developments include the potential repeal of the McCarran-Ferguson Act. The repeal of the McCarran-Ferguson Act and its partial exemption for the insurance industry from federal antitrust laws would make it extremely difficult for insurers to compile and share loss data, develop standard policy forms and manuals and predict future loss costs. The ability of the industry, under the exemption permitted in the McCarran-Ferguson Act, to collect loss cost data and build a credible database as a means of predicting future loss costs is an extremely important part of cost-based pricing. If the ability to collect this data were removed, then the predictability of future loss costs, and hence, the reliability of pricing would be greatly undermined.

If certain state regulators, legislators and special interest groups are successful in attempts to reduce, freeze or set rates for insurance policies, especially automobile policies, at levels that do not, in our management s view, correspond with underlying costs, the results of operations of the Property and Casualty Group will be adversely affected.

From time to time, the automobile insurance industry in particular has been under pressure from certain state regulators, legislators and special interest groups to reduce, freeze or set rates at levels that do not, in our management s view, correspond with underlying costs, including initiatives to roll back automobile and other personal lines rates. For example, in recent years, certain rate increase requests by the Property and Casualty Group for automobile coverage that management believed were necessary were rejected in New York and Maryland. This activity has adversely affected, and may in the future adversely affect, the profitability of the Property and Casualty Group s automobile insurance line of business in various states because increasing costs of litigation and medical treatment, combined with rising automobile repair costs, continue to increase the costs of providing automobile insurance coverage. Adverse legislative and regulatory activity constraining the Property and Casualty Group s ability to price automobile insurance coverage adequately may occur in the future. The impact of the automobile insurance regulatory environment on the results of operations of members of the Property and Casualty Group in the future is not predictable.

The Property and Casualty Group is subject to assessment, depending upon its market share of a given line of business, to assist in the payment of unpaid claims and related costs of insolvent insurance companies; such assessments could significantly affect the financial condition of any assessed member.

The Property and Casualty Group is obligated to pay assessments under the guaranty fund laws of the various states in which they are licensed. These assessments were $0.6 million for the year ended December 31, 1999, $0.8 million for the year ended December 31, 2000 and $30.9 million for the year ended December 31, 2001. Generally, under these laws, an insurer is subject to assessment, depending upon its market share of a given line of business, to assist in the payment of unpaid claims and related costs of insolvent insurance companies. The number and magnitude of future insurance company failures in the states in which the Property and Casualty Group does business cannot be predicted, but resulting assessments levied on members of the Property and Casualty Group could significantly affect the financial condition of members of the Property and Casualty Group. The Property and Casualty Group believes that it is likely to receive an assessment in the next year relating to the insolvency of The Pennsylvania Hospital Insurance Company (PHICO), the amount of which we cannot currently estimate.

Premium rates and reserves must be established for members of the Property and Casualty Group from forecasts of the ultimate costs expected to arise from risks underwritten

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during the policy period; a member s profitability could be adversely affected to the extent such premium rates or reserves are too low.

One of the distinguishing features of the property and casualty insurance industry in general is that its products are priced before its costs are known, as premium rates are generally determined before losses are reported. Accordingly, premium rates must be established from forecasts of the ultimate costs expected to arise from risks underwritten during the policy period and may not prove to be adequate. Further, property and casualty insurers establish reserves for losses and loss adjustment expenses based upon estimates, and it is possible that the ultimate liability will exceed these estimates because of the future development of known losses, the existence of losses that have occurred but are currently unreported and larger than historical settlements on pending and unreported claims. The process of estimating reserves is inherently judgmental and can be influenced by factors that are subject to variation. If pricing or reserves established by a member of the Property and Casualty Group are not sufficient, such member s profitability may be adversely impacted.

The Property and Casualty Group experienced adverse loss development relating to losses from prior accident years of $107 million for calendar year 2000, or 5.6% of loss reserves at year-end 2000, and $117 million for calendar year 2001, or 5.0% of loss reserves at year-end 2001. Adverse development of losses from prior accident years results in higher calendar year loss ratios and reduced calendar year underwriting results. To the extent prior year reserve deficiencies are indicative of deteriorating underlying loss trends and are material, the Property and Casualty Group s pricing of affected lines of business would be increased to the extent permitted by state departments of insurance.

Substantial premium rate increases are drawing new entrants and new capital to the reinsurance markets, which may increase competition among property and casualty insurers and may cause a reduction in our revenues.

Property and casualty market conditions in the wake of the World Trade Center terrorist attack have been characterized by closer adherence to underwriting standards, higher deductibles, reduced coverages and limits, more restrictive terms and conditions and higher premium rates. As a result of these changes in the industry, substantial new capital has entered the property and casualty insurance market. A substantial portion of the new capital is dedicated to building the capacity of new offshore reinsurers. This increased capital could result in lower prices for reinsurance, which in turn would allow primary insurers to offer more competitive prices or more favorable insurance terms and conditions or increase capacity. Increased competition among insurers and reinsurers could also allow the Property and Casualty Group s competitors to relax their underwriting standards. If substantial premium rate increases were to continue, additional new capital would likely be attracted, which would further promote the effects of increased competition.

Risks Relating to Our Class A Common Stock

The price of our Class A common stock may be adversely affected by its low trading volume.

The trading market for our Class A common stock is marked by limited liquidity. Reported average daily trading volume in our Class A common stock for the period January 1, 2002 through October 31, 2002 was approximately 32,000 shares. Of our 63.7 million shares of Class A common stock outstanding at September 30, 2002, approximately 23 million shares are available for public sale, with the remainder held by a small number of significant shareholders. Since 1999, we have had a stock repurchase program that authorized us to repurchase up to $120 million of our outstanding Class A common stock through December 31, 2002. Approximately $101.9 million of Class A common stock has been repurchased under the program to date. We believe the repurchase program had the effect of stabilizing the price of our Class A common stock notwithstanding that the variability of the price of our Class A common stock had been declining every year in the three years prior to our stock

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repurchase program. The program, however, has been suspended in connection with this offering of Class A common stock, and as a result, there may be an adverse effect on the market price of our Class A common stock.

The market price of our Class A common stock may be adversely affected by future sales of a substantial number of shares of our Class A common stock by our existing shareholders in the public market, or the availability of such shares for sale.

In connection with this offering, the Company, certain of its directors and officers, the Selling Shareholder and certain other shareholders have indicated that they will enter into lock-up agreements under which they will generally agree not to dispose of or hedge any of their shares or securities convertible into or exchangeable for shares of common stock of the Company during the 90-day period from the date of this prospectus without prior written approval of the underwriters. Certain of our existing shareholders and directors, however, have indicated that they will not agree to enter into lock-up agreements, including Susan Hirt Hagen, who is a member of our board of directors and a trustee and a beneficiary of the H.O. Hirt Trusts, Thomas B. Hagen, who is Mrs. Hagen s husband, and Henry N. Nassau, who is a member of our board of directors. Also, Audrey C. Hirt and Laurel A. Hirt have indicated that they will not agree to enter into lock-up agreements. Audrey Hirt is the wife and Laurel Hirt is a daughter of F. William Hirt, the chairman of our board of directors. Mr. Hirt is also a trustee and a beneficiary of the H.O. Hirt Trusts. Although we have not received any indication that Mr. and Mrs. Hagen, Mr. Nassau, Audrey Hirt or Laurel Hirt are planning to sell shares of Class A common stock during the 90-day period from the date of this prospectus, Mr. and Mrs. Hagen, Mr. Nassau, Audrey Hirt and Laurel Hirt, if they do not execute lock-up agreements, may have available for sale up to 34.74% of the outstanding shares of Class A common stock (based on the number of shares of Class A common stock outstanding as of December 31, 2002), assuming no further conversion of Class B shares into Class A shares. Sales, or the availability for sale, by these shareholders following the consummation of this offering of a substantial number of shares of our Class A common stock that are not subject to lock-up agreements may have an adverse effect on the market price of our Class A common stock.

Holders of Class A common stock have limited voting rights, and two shareholders of our Class B common stock, the H.O. Hirt Trusts, have the ability to determine the outcome of all matters submitted for shareholder approval, except those matters pertaining only to the rights of the holders of Class A common stock.

Our Class A common stock cannot vote for the election of directors and generally can only vote on matters pertaining to the rights of holders of Class A common stock. Generally, voting control of the Company is vested in the 2,900 outstanding shares of Class B common stock. The H.O. Hirt Trusts together own 2,340 shares, or 80.7%, of the outstanding Class B common stock and can therefore together elect the entire board of directors and determine the outcome of all matters submitted for approval of our shareholders, except those matters pertaining only to the rights of the holders of Class A common stock.

The value of our Class A common stock may be adversely affected because the ability of our principal shareholders to vote in favor of a transaction that would result in a change of control is limited.

The vote of the H.O. Hirt Trusts will determine the outcome of any matter submitted for shareholder approval, except those matters pertaining only to the rights of the holders of Class A common stock. The trust agreement governing the H.O. Hirt Trusts provide that at least two of the three trustees, including the corporate trustee, would be required to vote in favor of a transaction under which we would be acquired and such action, by the terms of the trust agreements, would be permitted only if required to maintain the health of the Exchange. This may prevent anyone from acquiring us in a transaction that shareholders, other than the H.O. Hirt Trusts, may consider to be in their best interests and may consequently have a negative effect on the price of our Class A common stock.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus and the documents incorporated by reference into this prospectus contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements include certain discussions relating to underwriting, premium and investment income volume, business strategies, profitability and business relationships and our other business activities during 2002 and beyond. In some cases, you can identify forward-looking statements by terms such as may , will , should , could , would , expect , plan , intend , anticipate , believe , estimate , potential and similar expressions. These forward-looking statements reflect our current views about future events, are based on assumptions and are subject to known and unknown risks and uncertainties that may cause results to differ materially from those anticipated in those statements. Many of the factors that will determine future events or achievements are beyond our ability to control or predict. Such factors may include those described under Risk Factors beginning on page 8.

The forward-looking statements contained in this prospectus reflect our views and assumptions only as of the date of this prospectus. Except as required by law, we assume no responsibility for updating any forward-looking statements. You should read this prospectus and the documents that we reference in this prospectus and have filed as exhibits to the registration statement of which this prospectus is a part, completely and with the understanding that our actual future results may be materially different from what we expect.

We qualify all of our forward-looking statements by these cautionary statements.

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PRICE RANGE OF OUR CLASS A COMMON STOCK AND DIVIDEND HISTORY

Prices for our Class A common stock are quoted on the NASDAQ Stock Market[SM] under the symbol ERIE . The following table presents for the periods indicated the high and low closing prices for our Class A common stock as reported by the NASDAQ Stock Market[SM] and the cash dividends declared.

	Price Range		Cash Dividends Declared
	High	Low	
2000:			
First Quarter	$ 32.44	$ 26.50	$ 0.1350
Second Quarter	32.50	27.50	0.1350
Third Quarter	32.00	29.19	0.1350
Fourth Quarter	30.00	24.00	0.1525

	Price Range		Cash Dividends Declared
	High	Low	
2001:			
First Quarter	$ 30.00	$ 26.50	$ 0.1525
Second Quarter	36.12	27.54	0.1525
Third Quarter	39.55	32.70	0.1525
Fourth Quarter	40.63	36.91	0.1700

	Price Range		Cash Dividends Declared
	High	Low	
2002:			
First Quarter	$ 40.82	$ 37.65	$ 0.1700
Second Quarter	45.49	40.44	0.1700
Third Quarter	44.50	37.45	0.1700
Fourth Quarter	42.39	35.90	0.1900

	Price Range		Cash Dividends Declared
	High	Low	
2003:			
First Quarter (through January 29)	$ 36.58	$ 35.27	

The last reported sale price of our Class A common stock on January 29, 2003 was $35.27. As of September 30, 2002, there were 1,061 holders of record of our Class A common stock.

We have paid regular quarterly cash dividends since 1942. Our board of directors considers the declaration of cash dividends on a quarterly basis. The payment of future dividends, if any, will be at the discretion of our board of directors and will depend upon many factors, including:

- our earnings;
- our financial position;
- our capital requirements and those of our subsidiaries; and
- our ability to receive dividends from our subsidiaries, which is subject to regulatory limitations.

Therefore, there can be no assurance as to the declaration of future dividends.

Although a potential source of cash for the payment of dividends to our shareholders is dividends from our insurance subsidiaries, our insurance subsidiaries have never paid us a dividend. Our insurance subsidiaries are subject to state laws that restrict their ability to pay dividends.

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CAPITALIZATION

The following table sets forth our capitalization as of September 30, 2002. We will not receive any proceeds from the sale of the shares of Class A common stock being offered hereby.

(amounts in thousands)	September 30, 2002
Long-term debt	
Shareholders equity:	
Class A common stock, stated value $0.0292 per share; authorized 74,996,930 shares; issued 67,080,000 shares and outstanding 63,677,106 shares	$ 1,957
Class B common stock, stated value $70 per share; authorized 3,070 shares; issued and outstanding 3,050 shares	213
Additional paid-in capital	7,830
Accumulated other comprehensive income	31,266
Retained earnings	1,018,868
Contributed capital and retained earnings	$ 1,060,134
Treasury stock, at cost (3,402,894 shares)	(101,860)
Total capitalization	$ 958,274

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SELECTED HISTORICAL FINANCIAL INFORMATION OF THE COMPANY

The selected consolidated financial data presented below as of or for the years ended December 31, 1997 through 2001 is derived from our audited financial statements. Our consolidated financial statements as of December 31, 2000 and 2001 and for each of the years in the three-year period ended December 31, 2001, and our independent auditors report thereon, are included elsewhere in this prospectus and incorporated by reference herein. See Where To Find More Information/Incorporation by Reference . The selected consolidated financial data presented below as of or for the nine-month periods ended September 30, 2001 and 2002 are derived from our unaudited consolidated financial statements included elsewhere in this prospectus and incorporated by reference herein. See Where To Find More Information/Incorporation by Reference . Our results of operations for the nine months ended September 30, 2002 are not necessarily indicative of our results of operations that may be expected for the year ended December 31, 2002. In the opinion of our management, all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation have been included. The financial data set forth below is only a summary and should be read in conjunction with our consolidated financial statements and related notes and Management s Discussion and Analysis of Financial Condition and Results of Operations included elsewhere herein.

(amounts in thousands, except per share data)	Nine Months Ended September 30,		Year Ended December 31,				
	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Statements of Operations Data:							
Operating revenue	$ 730,029	$ 602,001	$ 799,861	$ 698,016	$ 646,040	$ 615,965	$ 581,979
Operating expense	556,871	466,566	635,756	549,672	501,061	470,155	450,037
Total other income and expenses	33,187	35,408	17,998	70,102	58,731	45,770	38,747
Equity in earnings of Erie Family Life Insurance Company, net of tax	1,015	2,337	719	5,108	4,692	4,443	3,935
Federal income tax expense	69,171	56,835	60,561	71,161	65,296	61,472	56,043
Net income	$ 138,189	$ 116,345	$ 122,261	$ 152,393	$ 143,106	$ 134,551	$ 118,581
Per Share Data:							
Net income per share	$ 1.94	$ 1.63	$ 1.71	$ 2.12	$ 1.95	$ 1.81	$ 1.59
Dividends declared per Class A share	0.51	0.4575	0.6275	0.5575	0.4950	0.4425	0.3925
Dividends declared per Class B share	76.50	68.625	94.125	83.625	74.250	66.375	58.875
Book value per share	13.50	12.01	12.15	10.91	9.62	8.81	7.25
Weighted average shares outstanding	71,109	71,380	71,342	71,954	73,487	74,400	74,400
Financial Position:							
Investments(1)	$ 969,898	$ 884,599	$ 885,650	$ 853,146	$ 785,258	$ 709,417	$ 566,118
Receivables from the Exchange and affiliates	761,295	650,091	640,655	532,009	470,969	467,794	469,708
Total assets	2,194,690	1,897,077	1,935,566	1,680,599	1,518,794	1,454,062	1,292,544
Shareholders equity	958,274	855,755	865,255	779,015	697,599	655,223	539,383
Cumulative shares repurchased at December 31/September 30	3,403	3,170	3,196	2,976	1,900	0	0

(1) Includes investment in Erie Family Life Insurance Company.

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SELECTED HISTORICAL FINANCIAL INFORMATION OF THE EXCHANGE
(Statutory Accounting Principles)

The selected financial data of the Exchange presented below as of and for the years ended December 31, 1997 through 2001 is derived from financial statements prepared in accordance with statutory accounting principles (SAP) that were audited by our independent auditors. The selected financial data below as of and for the nine months ended September 30, 2001 and 2002 are derived from the Exchange s unaudited financial statements prepared in accordance with SAP. In the opinion of management, all adjustments consisting only of normal recurring accruals, considered necessary for a fair presentation have been included. The financial data set forth below is only a summary. More information about the Exchange, including the reasons why the Company believes the financial data set forth below is meaningful to a reader of this prospectus, can be found in Erie Insurance Exchange . The Annual Statements filed by the Exchange with the Insurance Department of the Commonwealth of Pennsylvania are available for inspection without charge at the Department s offices at Strawberry Square, Harrisburg, Pennsylvania. The financial statements of the Exchange included in these annual statements are prepared in accordance with SAP required by the NAIC Accounting Practices and Procedures Manual, as modified to include prescribed or permitted practices of the Commonwealth of Pennsylvania. See Erie Insurance Exchange General on page 78 for a discussion of significant differences between SAP and generally accepted accounting principles (GAAP). The Exchange does not, nor is it required to, prepare financial statements in accordance with GAAP.

	Nine Months Ended September 30,		Year Ended December 31,				
(amounts in thousands)	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Operating Data:							
Premiums earned	$ 2,140,526	$ 1,792,450	$ 2,422,600	$ 2,161,034	$ 2,039,791	$ 1,971,525	$ 1,877,270
Loss and loss adjustment expenses	1,727,052	1,568,896	2,150,749	1,714,487	1,509,895	1,372,705	1,375,643
Insurance underwriting and other expenses	718,881	551,623	766,304	624,622	576,031	568,149	520,648
Net underwriting (loss) income	$ (305,407)	$ (328,069)	$ (494,453)	$ (178,075)	$ (46,135)	$ 30,671	$ (19,021)
Investment income (loss), net	48,237	(32,489)	(421,754)	347,582	428,874	378,845	365,393
Federal income tax expense (benefit)	(68,925)	(43,230)	(300,257)	42,433	102,339	102,917	86,627
Net income (loss)	$ (188,245)	$ (317,328)	$ (615,950)	$ 127,074	$ 280,400	$ 306,599	$ 259,745
Financial Position:							
Cash and invested assets	$ 5,238,660	$ 5,563,420	$ 5,990,511	$ 6,357,658	$ 6,860,008	$ 5,604,496	$ 4,670,320
Total assets	6,190,240	6,317,728	6,998,794	6,969,746	7,415,176	6,174,590	5,204,856
Claims and unearned premium reserves	3,663,000	3,084,067	3,200,836	2,654,300	2,463,806	2,388,958	2,328,230
Total liabilities	4,042,623	3,418,368	3,953,243	2,847,861	2,660,713	2,582,998	2,490,465
Policyholders surplus(1)(2)	2,147,617	2,899,360	3,045,551	4,121,885	4,754,462	3,591,592	2,714,391

(1) Periods beginning after January 1, 2001 are computed taking into consideration changes in SAP required by the NAIC Accounting Practices and Procedures Manual. An adjustment made on January 1, 2001 as a result of such changes decreased policyholders surplus by $523.8 million.

(2) Under a practice prescribed by the Commonwealth of Pennsylvania, unearned premium reserves are reduced (and policyholders surplus increased) by the amount of the management fee ultimately payable by the Exchange to us correlating to premiums not yet earned at the respective financial statement date. At December 31, 2001, this amount was $240.9 million.

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MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis of our financial condition and results of operations in conjunction with the Selected Historical Financial Information of the Company and the consolidated financial statements, and the related notes, included elsewhere in this prospectus and incorporated by reference herein. In addition to this information, the table entitled Management Evaluation of Operating Results on the next page directly reflects measurements used by management in evaluating operating results. This table, which management uses internally to monitor and evaluate results, is an alternative presentation of the Company s Consolidated Statements of Operations. You should refer to this table in conjunction with reading those portions of the following discussions relating to operating results and measurements.

General

We operate predominantly as a provider of management services to Erie Insurance Exchange (the Exchange) and also as an underwriter of insurance through our subsidiaries. We have served since 1925 as the attorney-in-fact, or management company, for the policyholders of the Exchange. The Exchange and its property and casualty subsidiary and our three property and casualty subsidiaries (collectively, the Property and Casualty Group) write personal and commercial lines property and casualty coverages exclusively through approximately 8,000 independent agents and pool their underwriting results. The financial results of the Exchange are not consolidated with ours. For our services as attorney-in-fact in providing sales, underwriting and policy issuance services to the Exchange, we charge the Exchange a management fee calculated as a percentage, limited to 25%, of the direct written premiums of the Property and Casualty Group.

Under the pooling arrangement, all property and casualty insurance business of the five property and casualty insurance companies that comprise the Property and Casualty Group is pooled within the Exchange as the pooling entity. Our insurance subsidiaries, Erie Insurance Company and Erie Insurance Company of New York, share in the underwriting results of the pool through retrocession. Erie Insurance Company has a 5.0% participation, Erie Insurance Company of New York has a 0.5% participation and the Exchange has a 94.5% participation in the pooled underwriting results. These participation percentages are determined by our board of directors. We also own 21.6% of the common stock of Erie Family Life Insurance Company, an affiliated life insurance company, of which the Exchange owns 53.5% and public shareholders, including its officers and directors, own 24.9%.

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Erie Indemnity Company
Management Evaluation of Operating Results

(amounts in thousands)	Nine Months Ended September 30, 2002	Nine Months Ended September 30, 2001	Year Ended December 31, 2001	Year Ended December 31, 2000	Year Ended December 31, 1999
	(unaudited)				
Management Operations:					
Management fee revenue	$ 593,895	$ 480,805	$ 634,966	$ 551,646	$ 513,375
Service agreement revenue	16,310	20,339	27,247	22,662	15,441
Cost of management operations	(421,097)	(349,796)	(477,645)	(415,562)	(380,298)
Income from management operations	$ 189,108	$ 151,348	$ 184,568	$ 158,746	$ 148,518
Insurance Underwriting Operations:					
Premiums earned	$ 119,824	$ 100,857	$ 137,648	$ 123,708	$ 117,224
Losses and loss adjustment expenses incurred	(98,431)	(88,074)	(117,201)	(99,564)	(87,719)
Policy acquisition and other underwriting expenses	(37,343)	(28,696)	(40,910)	(34,546)	(33,044)
Underwriting loss	$ (15,950)	$ (15,913)	$ (20,463)	$ (10,402)	$ (3,539)
Investment Operations:					
Net investment income	$ 40,705	$ 36,855	$ 49,884	$ 48,401	$ 43,344
Net realized (losses) gains on investments	(8,628)	(2,726)	(31,879)	16,968	14,746
Equity in earnings of EFL	1,091	2,513	773	5,492	5,045
Equity in earnings (losses) of limited partnerships	1,110	1,279	(7)	4,733	641
Net revenue from investment operations	$ 34,278	$ 37,921	$ 18,771	$ 75,594	$ 63,776
Income before income taxes	207,436	173,356	182,876	223,938	208,755
Provision for income taxes	(69,247)	(57,011)	(60,615)	(71,545)	(65,649)
Net income	$ 138,189	$ 116,345	$ 122,261	$ 152,393	$ 143,106
Operating income(1)	$ 143,797	$ 118,117	$ 142,983	$ 141,364	$ 133,521
Per Share Data:					
Net income	$ 1.94	$ 1.63	$ 1.71	$ 2.12	$ 1.95

(1) Operating income excludes net realized gain (loss) on investments and related federal income taxes.

Critical Accounting Estimates

We make estimates and assumptions that can have a significant effect on amounts and disclosures we report in our financial statements. The most significant estimates relate to our reserves for property and casualty insurance unpaid losses and loss adjustment expenses, valuation of investments and guaranty fund liability accruals. While management believes its estimates are appropriate, the ultimate amounts may differ from the estimates provided. The methods for making these estimates are continually reviewed, and any adjustments considered necessary are reflected in current earnings.

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With respect to reserves for property and casualty unpaid losses and loss adjustment expenses, significant components of estimates include a variety of factors such as medical inflation trends, regulatory and judicial rulings, legal settlements, property replacements and repair cost trends, and losses for assumed reinsurance activities. In recent years, certain of these component costs such as medical inflation trends and legal settlements have experienced significant volatility and resulted in incurred amounts higher than our original estimates. We have factored these changes in trends into our loss estimates. However, due to the nature of these liabilities, actual results could ultimately vary significantly from the amounts recorded. If the ultimate liability for unpaid losses and loss adjustment expenses were 10% more than the recorded amount at December 31, 2001, the effect would be a reduction in the Company s pre-tax income of approximately $12 million or $0.17 per share.

We make estimates concerning the valuation of our investments and the recognition of other than temporary declines in value of these investments. When the decline in value of an individual investment is considered by management to be other than temporary, the investment is written down to its estimated net realizable value and reflected as a realized loss in the statement of operations. All investments are individually monitored for other than temporary declines in value. Management makes judgments about when there are other than temporary declines in its investments. Generally, if an individual security has depreciated in value by more than 20% of original cost, and has been in such unrealized loss position for more than six months, we assume there has been an other than temporary decline in value. In addition, the Company may write-down other securities in an unrealized loss position depending on the existence of certain other factors. These other factors we consider include: the significance of the fair value below cost, whether there has been a deterioration in financial condition of the issuer, whether there have been specific events adversely affecting an investment, debt security downgrades and specific industry or geographic events. If we had determined there was an other than temporary decline in value in 2001 for 10% of our investments with unrealized losses, then the Company would have recorded an additional realized loss of $480,000 in our 2001 statement of operations. Our evaluation of the need for write-downs due to other than temporary declines in value is also applied to our investment in limited partnerships and mortgage loans.

Our investments in fixed maturity and marketable equity securities are presented at estimated fair value, which generally represents quoted market prices. Our investments in limited partnerships are recorded using the equity method, which approximates the Company s proportionate share of the partnership s reported net equity. Because of their illiquidity relative to our other investments, there is increased risk in valuation of limited partnerships. The recorded value of limited partnerships includes the valuation of investments held by these partnerships, which include U.S. and foreign private equity, real estate and fixed income investments. These valuations are determined by the general partner. We consider the reasonableness of these valuations based on various information, including: audited and unaudited financial statements from these partnerships, and other information provided by the general partner. The carrying value of limited partnership investments totaled $81.6 million at December 31, 2001.

Estimates are also made by the Company s insurance subsidiaries of liabilities for guaranty fund and other assessments. Our insurance subsidiaries are sometimes required to pay assessments to states in which the subsidiaries are licensed because of insurance company insolvencies. The liability for the assessments is recorded when the insolvency event has occurred and can be reasonably estimated. We commonly become aware of insolvencies that will affect us prior to obtaining specific assessment amounts from state guaranty associations to estimate our share of the liability. It is often a long process before state guaranty associations know of the ultimate amount of assessment needed to cover the insolvency. We initiate communication with the state insurance departments and guaranty associations when we learn of an insolvency. Although the insurance departments and guaranty associations may not be able to provide specifics on the ultimate assessment amounts, they will sometimes provide us with information from which we develop an estimated range of the future

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assessment. We generally record a liability at the mid-point of the range. In these cases, the mid-point of the range we develop represents our best estimate of the ultimate loss to be incurred due to the assessment. We adjust our estimated liability as the guaranty association provides us with more up to date assessment amounts. For example in 2001, the insolvency of Reliance Insurance Company was significant. Although we had not received definitive notices of assessment amounts as of December 31, 2001 from the guaranty funds, we recorded an estimated liability of $2.0 million at December 31, 2001. This liability was recorded based on the mid-point of the range of estimated assessment amounts. Additional future information may result in adjustments to our estimated liability.

Results of Operations

Nine Months Ended September 30, 2002 and September 30, 2001

Financial Overview

Our consolidated net income for the nine months ended September 30, 2002 increased 18.8% to $138.2 million, from $116.3 million during the same period in 2001. Income from management operations grew as a result of a 23.5% increase in direct written premiums of the Property and Casualty Group. Results of our insurance underwriting operations were about the same in the first nine months of 2002 compared to the same period in 2001 as a result of wind storm-related catastrophe losses and increased technology spending related to the eCommerce initiative in 2002 and World Trade Center losses in 2001. In addition, charges of $17.7 million and $5.7 million were taken for impaired investments contributing to net realized losses on investments in the first nine months of 2002 and 2001, respectively. The board of directors voted to reduce the management fee rate from 25% to 24% for 2003 at its December 10, 2002 meeting.

For the nine months ended September 30, 2002, operating income (net income excluding net realized (losses) gains and related federal income taxes) increased 21.7% to $143.8 million, from $118.1 million reported for the same period in 2001.

We have benefited during this period, and expect to continue to benefit, from premium increases by the Property and Casualty Group that have resulted from pricing actions approved by regulators through September 30, 2002. These premiums accounted for $48.4 million in increased premiums from the Property and Casualty Group for the nine months ended September 30, 2002. These increases were primarily related to private passenger automobile, workers compensation and homeowners lines of business premium rate increases realized in the states of Pennsylvania, Maryland and Ohio. The remaining anticipated premium rate increases to be recognized in future periods are in the private passenger automobile, commercial multiple peril and homeowners lines of business in the states of Pennsylvania, Ohio and West Virginia.

Analysis of Management Operations

Our management fee revenue increased 23.5% to $593.9 million for the nine months ended September 30, 2002, from $480.8 million for the same period in 2001.

The direct written premium of the Property and Casualty Group upon which our management fee revenue is calculated grew 23.5% to $2,375.6 million during the first nine months of 2002, from $1,923.2 million for the same period in 2001. Increases in average premium per policy, improvements in new policy growth and continuing favorable policy retention rates were all contributing factors in the growth of direct written premium.

The average premium per policy increased 9.5% to $877 for the rolling twelve months ended September 30, 2002, from $801 for the same period ended September 30, 2001. In private passenger automobile, which accounted for 53.1% of the direct written premiums of the Property and Casualty

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Group and over 1.5 million policies in force, the average premium per policy increased 7.2% to $1,023 for the rolling twelve months ended September 30, 2002, from $954 during the same period ended September 30, 2001.

Continued growth in the number of new policies also drove the gains experienced in the Property and Casualty Group s direct written premium. Personal lines new business premium grew 45.3% for the first nine months of 2002 to $270.6 million, from $186.2 million, while commercial lines new premium grew 56.8% to $164.6 million, from $104.9 million, during the same period in 2001. Policies in force increased at an annualized rate of 11.9% to 3,411,953 at September 30, 2002, from 3,048,808 at September 30, 2001.

Policy retention remained strong at 91.1% and 90.9% for the periods ended September 30, 2002 and 2001, respectively, for all lines of business combined.

Changes in the management fee rate can affect our revenue and net income significantly. If our board of directors had reduced the management fee rate 1% (from 25% to 24%) for the nine-month periods ended September 30, 2002 and 2001, the decrease would have resulted in a reduction of our management fee revenue of $23.8 million and $19.2 million, respectively. The net income per share impact would have been a reduction of $0.22 and $0.18 for the nine-month periods ended September 30, 2002 and 2001, respectively. The board of directors voted to reduce the management fee rate from 25% to 24% for 2003 at its December 10, 2002 meeting.

Service agreement revenue decreased by 19.8% to $16.3 million for the nine months ended September 30, 2002, from $20.3 million for the same period in 2001. Service agreement revenue includes service charges the Company collects from policyholders for providing extended payment plans on policies written by the Property and Casualty Group. During the third quarter of 2002, the Company determined service charges were incorrectly being recognized in full as billing installments were created at the time of policy issuance instead of at the time the billings were rendered. The Company recorded a one-time adjustment reducing service charge income by $7.4 million. The effect on 2002 net income per share after taxes and other adjustments was $.06 per share. The Company did not restate prior period financial statements because the Company believes this adjustment is not material to the trend of earnings for the Company nor any related financial statement amount.

Service agreement revenue also includes service income received from the Exchange as compensation for the management and administration of voluntary assumed reinsurance from non-affiliated insurers. These fees totaled $9.6 million and $8.3 million for the nine months ended September 30, 2002 and 2001 on net voluntary assumed reinsurance premiums of $137.1 million and $118.7 million, respectively. During the 2002 reinsurance renewal season, the Exchange obtained significant price increases on treaties it renewed. In addition, the Exchange reduced its aggregate exposure in non-affiliated assumed voluntary reinsurance by non-renewing unprofitable business, generally excluding terrorism coverage and restricting its exposure on certain types of risks. These factors impact the level of service income received from the Exchange since this fee is based on a percentage of non-affiliated assumed reinsurance premiums.

The cost of management operations increased 20.4% for the first nine months of 2002 to $421.1 million, from $349.8 million during the same period in 2001. Commissions to independent agents are the largest component of the cost of management operations, and include scheduled commissions earned by independent agents on premiums written, as well as promotional incentives for agents and agent contingency awards. Commission costs totaled $302.6 million for the first nine months of 2002, a 23.9% increase over the $244.1 million reported in the same period of 2001. Growth in commission costs was slightly greater than the growth in direct premium written in the first nine months of 2002, primarily due to increased accelerated commissions as well as an accrual for a promotional incentive contest for agents that ran through 2002.

Accelerated commissions are offered to newly recruited agents in addition to normal commission schedules. For the nine months ended September 30, 2002, additional charges for accelerated commission costs totaled $6.8 million, compared to $5.0 million for the same period one year ago due to an increase in the number of agents. For the nine months ended September 30, 2002, the accrual recorded for a sales incentive contest was $1.8 million. There was no similar sales contest in 2001.

The cost of management operations, excluding commission costs, increased 12.2% for the nine months ended September 30, 2002 to $118.5 million, from $105.6 million for the same period in 2001. These costs include amounts related to information technology hardware and infrastructure from the eCommerce initiative launched in September 2001. For the first nine months of 2002, these costs totaled $2.5 million, compared to $0.5 million in the same period in 2001.

Personnel costs also increased as employment grew by 8.4%, driven by strong policy sales growth. In addition, temporary labor costs were incurred to assist with a company-wide rollout of personal computers. As a result, salaries, wages, benefits and payroll taxes for the first nine months of 2002 increased 10.2% to $68.8 million, from $62.5 million for the same period in 2001.

Our gross margin from management operations (net revenue divided by total revenue) increased to 31.0% in the first nine months of 2002, compared to the gross margin of 30.2% reported in the same period of 2001.

Analysis of Insurance Underwriting Operations

The underwriting loss from the insurance underwriting operations of Erie Insurance Company and Erie Insurance Company of New York, which together assume a 5.5% share of the direct and non-affiliate assumed underwriting results of the Property and Casualty Group under the intercompany pooling arrangement, was $16.0 million during the first nine months of 2002 compared to an underwriting loss of $15.9 million during the same period in 2001. Losses of $4.4 million resulting from spring storm-related catastrophes were partly responsible for the underwriting loss in 2002. The per share impact, after federal income taxes, was about $0.04 per share for the first nine months of 2002. The underwriting results for the first nine months of 2002 also reflect increased underwriting expenses related to the eCommerce technology program and assigned risk buyout program costs. In addition, our share of catastrophe losses was $5.4 million for the nine months ended September 30, 2002, compared to $1.5 million for the same period in 2001.

Our insurance subsidiaries share of the Property and Casualty Group s direct business generated net underwriting losses was $16.4 million and $8.7 million for the nine months ended September 30, 2002 and 2001, respectively. The increase in the underwriting loss of $7.7 million was primarily attributable to two factors: (i) increased incurred underwriting losses of $5.4 million resulting from catastrophes in our underwriting territories and increased loss severity and (ii) increased underwriting expenses related to the eCommerce technology initiatives, which amounted to $3.0 million, and to the assigned risk buyout program costs, which amounted to $0.8 million. The firming of automobile insurance pricing in 2001 by the industry in response to deteriorating loss cost trends allowed the Property and Casualty Group to begin raising automobile insurance prices in order to improve underwriting profitability. The Property and Casualty Group only writes one-year policies; therefore, rate increases take 24 months to be reflected fully in earned premium because it takes 12 months to implement the rate increase as to all policyholders and 12 months thereafter to earn fully the increased premiums.

In late 2001, we took measures to improve the underwriting results from our non-affiliated voluntary assumed reinsurance book of business. The effect of these measures was to lower the Property and Casualty Group s exposure to loss by excluding terrorism coverage on certain contracts,

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not renewing unprofitable contracts and, at the same time, raising pricing substantially. Pricing in the reinsurance marketplace has firmed considerably since the World Trade Center terrorist attack and we have obtained significant price increases in our 2002 contract renewals.

Our insurance subsidiaries share of the Property and Casualty Group s unaffiliated voluntary net assumed reinsurance business generated net underwriting income of $0.5 million and a net underwriting loss of $7.2 million in the first nine months of 2002 and 2001, respectively. The 2001 losses include the Company s 5.5% share of the Property and Casualty Group s estimated incurred losses from the terrorist attack on the World Trade Center. These losses, net of recoveries under the excess of loss agreement with the Exchange, totaled $5.8 million. There was no additional reserve development in 2002 relating to our insurance subsidiaries 5.5% share of the Property and Casualty Group s estimated incurred reinsurance loss of $150 million from the World Trade Center terrorist attack. Through September 30, 2002, loss payments made by the Property and Casualty Group related to the terrorist attack have totaled $35.6 million with an additional $114.4 million established as reserves for case and incurred but not reported claims. Incurred but not reported claims are claims for indemnity against losses that have been incurred by an insurer or reinsurer that have not yet been reported to the insurer or reinsurer and include future developments on losses that have been reported to the insurer or reinsurer.

A dispute concerning whether the World Trade Center terrorist attack should be considered one or two insurable events is currently being litigated. The Property and Casualty Group s $150 million estimated incurred loss, which was recorded in the third quarter of 2001, assumes that the World Trade Center terrorist attack will continue to be considered one event. If the attack is considered as two events, the total potential exposure for the Property and Casualty Group would increase between $50 million and $75 million. The effect on us, as a result, would be an additional loss of between $2.7 million and $4.1 million out of this amount. Taking into consideration the excess of loss reinsurance agreement, the net impact of such potential additional losses would be minimal to our results of operations or financial condition.

An all-lines aggregate excess of loss reinsurance agreement with the Exchange limits the ultimate net losses of Erie Insurance Company and Erie Insurance Company of New York. Under the reinsurance agreement, once Erie Insurance Company and Erie Insurance Company of New York sustain ultimate net losses and allocated loss expenses in an accident year that exceed an amount equal to 72.5% of Erie Insurance Company s and Erie Insurance Company of New York s net premiums earned, the Exchange will be liable for 95% of the amount of such excess up to, but not exceeding, an amount equal to 95% of 15% of Erie Insurance Company s and Erie Insurance Company of New York s net premium earned. Erie Insurance Company and Erie Insurance Company of New York retain the remaining 5% of such layer as well as ultimate net losses and allocated loss expenses in excess of 87.5% of Erie Insurance Company s and Erie Insurance Company of New York s net premiums earned. Erie Insurance Company and Erie Insurance Company of New York pay a premium to the Exchange equal to 1.01% of their net premium earned, subject to a minimum premium of $800,000 for each annual period. Net premiums means gross premiums net of reinsurance premiums. The premium paid to the Exchange for the agreement totaled $1.4 million for each of the nine-month periods ended September 30, 2002 and 2001. Recoveries during the first nine months of 2002 amounted to $2.0 million, compared to recoveries of $3.1 million for the same period one year ago. No cash payments have been made between the companies in 2002 for recoveries under this agreement since the recoveries are recorded based on reserved but not yet paid losses.

During 2001, we and the Property and Casualty Group entered into a cost-sharing agreement for information technology development. This agreement describes how member companies of the Property and Casualty Group will share the costs to be incurred for the development of new customer relationship management and Internet-enabled property and casualty policy administration systems.

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This agreement provides that the application development costs and the related enabling technology costs, such as technical infrastructure and architectural tools, will be shared among the property and casualty insurance companies in a manner consistent with the sharing of insurance transactions under the existing intercompany pooling arrangement. These technology costs are included in the Property and Casualty Group s policy acquisition and other underwriting expenses. Our share of eCommerce initiative expenses covered under the cost sharing agreement amounted to $3.0 million and $0.6 million for the nine-month periods ended September 30, 2002 and 2001, respectively. These shared costs will continue to be incurred in future periods as the program proceeds.

As part of the eCommerce initiative, a significant portion of Erie Insurance Group s information technology staff have been deployed to work on the eCommerce program. As such, certain personnel costs are currently being allocated to the Property and Casualty Group as part of the eCommerce project. However, once the eCommerce program is completed, some of these personnel costs will again be included in our cost of management operations. Approximately 60 full time equivalent staff, or 15% of the Erie Insurance Group information technology staff, are currently deployed to work on the eCommerce program. We expect the cost of operations to increase by as much as $8.0 million per year when the staff is reassigned to non-eCommerce tasks.

The Property and Casualty Group experienced an increase in costs associated with assigned risk buyout programs during the first nine months of 2002. Under a buyout program, one insurer pays another insurer to assume the first insurer s obligations to participate in a state-mandated involuntary coverage program, such as an assigned risk plan, for those who are unable to obtain automobile insurance in the voluntary market because of underwriting considerations. Our share of these costs in the first nine months of 2002 was $0.8 million, compared to $0.2 million for the same period in 2001. The buyout programs consist of Limited Assignment Distribution (LAD) agreements, which cover personal automobile risks, and Commercial Limited Assignment Distribution (CLAD) agreements, which cover commercial automobile risks. The Property and Casualty Group has a CLAD program in Pennsylvania and both LAD and CLAD programs in New York, Illinois, Virginia, West Virginia and Tennessee. These programs provide that a servicing carrier perform all administrative functions relative to the assigned risk policies, including collecting premiums and making payments for losses and loss adjustment expenses. The Property and Casualty Group makes payments to the servicing carrier, which includes an administrative fee, as well as a fee for rate inadequacy costs above the collected premium.

The increase in LAD/CLAD expense is almost exclusively attributable to the buy-out program in the State of New York, which had costs of $0.8 million, compared to $0.2 million during the first nine months of 2002 and 2001, respectively. The rise in costs in New York State is the result of significant increases in both the population of assigned risk policies and the deteriorating rate adequacy of the New York State residual market. A residual market consists of consumers who are unable to purchase insurance in the voluntary market due to a variety of factors. In addition, the Property and Casualty Group s market share in the state has increased, resulting in additional assigned risk policies being allocated to the Property and Casualty Group.

The combined ratio computed under GAAP for our property and casualty insurance underwriting operations was 113.3% and 115.8% for the nine months ended September 30, 2002 and 2001, respectively. The GAAP combined ratio represents the ratio of loss, loss adjustment, acquisition and other underwriting expenses and dividends incurred to premiums earned. The 2002 ratio was affected by 2.5 combined ratio points related to eCommerce expenses and by 4.5 combined ratio points related to catastrophe losses and increased loss severity in the first nine months of 2002. The GAAP combined ratio for our property/casualty operations, excluding eCommerce costs and catastrophe losses, was 106.3% for the nine months ended September 30, 2002.

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Analysis of Investment Operations

Our net revenue from investment operations is comprised of four major elements, (1) equity in earnings (losses) of Erie Family Life Insurance Company; (2) equity in the earnings (losses) of limited partnerships; (3) net realized capital gains (losses); and (4) net investment income that is comprised of interest, dividend and rental income from our invested assets less investment expenses incurred.

Our net revenue from investment operations for the first nine months of 2002 declined 9.6% to $34.3 million, from $37.9 million in the same period of 2001. As a result of impairment charges taken in the first nine months of 2002, we realized net losses on investments of $8.6 million, compared to losses of $2.7 million in the same period of 2001. The impairment charges were for fixed maturity, non-redeemable preferred stock and common stock, which totaled $17.7 million. Net realized losses included charges related to the WorldCom Group securities totaling $5.7 million.

For the nine months ended September 30, 2002, our net investment income increased 10.4% to $40.7 million, compared to $36.9 million for the same period one year ago. Increases in investments in taxable bonds contributed to the growth in net investment income for the first nine months of 2002. The following table compares the performance of our equities portfolio to selected indices:

Erie Indemnity Company
Portfolio Performance

	Two Years Ended September 30, 2002 (Pre-Tax Annualized Returns)
Erie Indemnity Company:	
Fixed Maturities Corporate	8.43%
Fixed Maturities Municipal	7.40(1)
Preferred Stock	9.42(1)
Common Stock	(27.90)
Other Indices:	
Lehman Brothers Global Aggregate Bond Index Unhedged	8.67%
S&P 500 Composite Index	(23.57)

(1) Returns on municipal fixed maturities and preferred stocks have tax-equivalent yields of 10.47% and 11.27%, respectively.

Our equity in earnings of limited partnerships totaled $1.1 million and $1.3 million for the nine months ended September 30, 2002 and 2001, respectively. Private equity and fixed income limited partnerships realized losses of $2.6 million for the nine months ended September 30, 2002, compared to losses of $39,000 for the same period in 2001. Our earnings from real estate limited partnerships were $3.7 million for the nine months ended September 30, 2002, compared to earnings of $1.3 million for the same period in 2001. Our September 30, 2002 earnings included impairment charges totaling almost $1.4 million in private equity limited partnerships where we considered declines in value to be other than temporary.

Our share of the earnings of Erie Family Life Insurance Company totaled $1.1 million during the first nine months of September 30, 2002, down from the $2.5 million recorded for the same period in 2001. The decrease in the level of earnings from our investment in Erie Family Life Insurance Company is related to impairment charges recorded on investments by Erie Family Life Insurance Company totaling $17.2 million, which resulted in net realized losses for Erie Family Life Insurance Company. Our investment in Erie Family Life Insurance Company is accounted for under the equity method of accounting.

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Years Ended December 31, 2001, 2000 and 1999

Financial Overview

Our consolidated net income in 2001 was $122.3 million, a decrease of 19.8% from net income of $152.4 million in 2000, which in turn represented an increase of 6.5% from net income of $143.1 million in 1999. Gains made in our management operations, including a 15.1% increase in management fee revenue in 2001 over 2000 and a 7.5% increase in 2000 over 1999, were outpaced by losses experienced in our insurance underwriting operations and reduced levels of income from investment operations in 2001. In 2000, gains in our management and investment operations outpaced losses experienced in our insurance underwriting operations. Our 2001 underwriting loss resulted from increased losses in the direct business of our property and casualty subsidiaries, primarily in private passenger and commercial automobile and workers compensation insurance, as well as assumed reinsurance losses, some of which relate to the World Trade Center terrorist attack. We recognized $31.9 million in net realized losses from investments in 2001 on the sale of securities and related charges for other than temporary impairments of equity securities and limited partnerships. There were no similar impairments in 2000 or 1999. Our 2000 underwriting loss stemmed from increased losses in private passenger automobile and several commercial lines of business. Revenue from our investment operations increased 18.5% in 2000 from 1999 as our cash flows were reinvested for higher returns and our equity earnings in limited partnerships grew substantially over 1999.

Our operating income (net income excluding realized gains/losses and related federal income taxes) increased by 1.1% in 2001, to $143.0 million from $141.4 million in 2000, and 5.9% in 2000 from $133.5 million in 1999. Operating income in 2001 reflected a third quarter after-tax charge of $3.8 million, or $0.06 per share, from the World Trade Center terrorist attack and a fourth quarter after-tax charge of $6.9 million, or almost $0.10 a share, for severance charges related to the retirement of our chief executive officer. Our operating income in 2000 reflected adverse developments on assumed reinsurance losses from the catastrophic wind storms that devastated Europe in December 1999, which resulted in a loss of $1.4 million, or $0.01 per share, after federal income taxes.

Analysis of Management Operations

Our income from management operations rose 16.3% to $184.6 million in 2001 from $158.7 million in 2000 and 6.9% in 2000 from $148.5 million in 1999. Gross margins from management operations were 27.9% in 2001 compared to gross margins of 27.6% in 2000 and 28.1% in 1999.

Our management fee revenue rose $83.3 million, or 15.1%, to $635.0 million in 2001 from $551.6 million in 2000 and $38.3 million, or 7.5%, in 2000 from $513.4 million in 1999. The direct and affiliated assumed premiums of the Exchange grew 15.1% in 2001 to $2,539.9 million from $2,206.6 million in 2000 and grew by 7.5% in 2000 from $2,053.5 million in 1999. Increases in average premium per policy, improvements in new policy growth and favorable policy retention rates were all contributing factors in the growth. Firming pricing in 2001 for commercial and personal insurance allowed the Property and Casualty Group to price its products more favorably while maintaining their competitive advantage in the marketplace. The year-to-year growth rate of direct written premium in the fourth quarter was 18.9%, up from 14.8% growth in the third quarter, 14.0% growth in the second quarter and 12.8% growth in the first quarter of 2001.

The Property and Casualty Group s average premium per policy increased 6.1% to $817 in 2001 from $770 in 2000, and 0.9% in 2000 from $763 in 1999. For private passenger automobile (which accounted for 54.6% of the direct written premiums of the Property and Casualty Group during 2001 with over 1.4 million policies in force), the average premium per policy increased 3.1% to $967 in 2001 from $938 in 2000, and decreased 1.6% in 2000 from $954 in 1999.

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Continued improvement in new policy growth also drove the gains experienced in the Property and Casualty Group s direct written premiums. Policies in force increased 8.5% to 3.1 million in 2001 from 2.9 million in 2000, and 6.5% in 2000, from 2.7 million in 1999. Policy retention of the Property and Casualty Group remained strong at 90.9%, 91.0% and 90.5% during 2001, 2000 and 1999, respectively, for all lines of business combined.

Changes in the management fee rate can affect our revenue and net income significantly. If our board of directors had decreased the management fee rate 1% (from 25% to 24%) for 2001, 2000 and 1999, the decrease would have resulted in a reduction of our management fee revenues of $25.4 million, $22.1 million and $20.5 million, respectively, and a per share reduction in net income of $0.23, $0.20 and $0.18, respectively. At our December 2001 board of directors meeting, the board voted to maintain the management fee rate at 25% for 2002.

Our service agreement revenue grew 20.2% to $27.2 million in 2001 from $22.7 million in 2000, and 46.8% in 2000 from $15.4 million in 1999. Service agreement revenue earned for the management and administration of the Exchange s voluntary assumed reinsurance from non-affiliated insurers, totaled $11.3 million, $10.1 million and $8.2 million on net voluntary assumed reinsurance premiums of $160.7 million, $145.0 million and $116.6 million for 2001, 2000 and 1999, respectively.

Service charges we collect from policyholders who pay premiums in installments on policies written by the Property and Casualty Group amounted to $16.0 million, $12.5 million and $7.3 million in 2001, 2000 and 1999, respectively. The 2001 and 2000 growth was positively affected by service charge increases from $2 to $3 per installment for policies renewing in most states beginning in the second quarter of 2000.

The cost of management operations rose 14.9% to $477.6 million in 2001, from $415.6 million in 2000, and 9.3% in 2000 from $380.3 million in 1999. Commissions to independent agents, which are the largest component of the cost of management operations, include scheduled commissions earned by independent agents on premiums written, as well as promotional incentives for agents and agent contingency awards. Agent contingency awards are based upon a three-year average of the underwriting profitability of the direct business written and serviced within the Property and Casualty Group by the independent agent. The estimate for the agent contingency awards is modeled on a monthly basis using the two prior years actual underwriting data by agency combined with the current year to date actual data. The Company uses projected underwriting data for the remainder of the current year in order to model the 36-month underwriting results by agency. Commission costs rose 14.3% to $323.1 million in 2001, from $282.7 million in 2000, and 7.5% in 2000 from $263.1 million in 1999. Commission costs grew at a slower rate relative to the growth in direct premiums written in 2001 as a result of lower accruals for agent contingency awards compared to 2000. The provision for agent contingency awards totaled $15.7 million, $18.3 million and $19.9 million in 2001, 2000 and 1999, respectively. Commission costs, excluding agent contingency awards, increased 16.2% in 2001 compared to 2000, and 9.0% in 2000 compared to 1999, which is in line with the increase in direct written premiums.

Cost of our management operations, excluding commission costs, increased 16.4% in 2001 to $154.6 million, from $132.8 million in 2000, and increased 13.3% in 2000 from $117.2 million in 1999, due primarily to increases in personnel costs. Our personnel costs totaled $94.4 million, $79.3 million and $69.5 million in 2001, 2000 and 1999, respectively. A portion of the 2001 increase in personnel costs resulted from recognition of the severance obligation related to the retirement of our president and chief executive officer on January 18, 2002. We recorded a severance charge in the fourth quarter of 2001 of $10.7 million. Personnel costs, excluding the severance charge, rose 5.5% in 2001 due to increases in employee pay rates and staffing levels. Increases in 2000 over 1999 were attributable to pay rate increases and the introduction of an incentive compensation program for branch sales employees.

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During 2001, we also incurred information technology infrastructure expenditures related to the eCommerce program that were not subject to the cost-sharing agreement for information technology. These eCommerce program costs were included in the cost of management operations and totaled $1.6 million in 2001.

Analysis of Insurance Underwriting Operations

We recorded underwriting losses of $20.5 million, $10.4 million and $3.5 million in 2001, 2000 and 1999, respectively. The underwriting results in 2001 reflect higher losses experienced in private passenger automobile, and commercial automobile and workers compensation lines of business, as well as losses from assumed reinsurance.

Premiums earned increased 11.3% to $137.6 million in 2001, from $123.7 million in 2000, and 5.5% in 2000 from $117.2 million in 1999. The average premium per policy of the Property and Casualty Group was $817, $770 and $763 in 2001, 2000 and 1999, respectively. Losses and loss adjustment expenses incurred increased 17.7%, to $117.2 million in 2001 from $99.6 million in 2000, and 13.5% in 2000 from $87.7 million in 1999.

Our property and casualty insurance subsidiaries share of the Property and Casualty Group s direct business generated net underwriting losses of $16.4 million, $6.1 million and $0.5 million in 2001, 2000 and 1999, respectively. In 2001, the Property and Casualty Group continued to experience a decrease in loss frequency, although loss severity continued to rise. The higher loss costs in 2001 also include adverse development of prior accident year losses amounting to $5.9 million, net of reinsurance recoveries. In 1998 and 1999, the Property and Casualty Group lowered prices in the private passenger automobile lines of insurance in response to extremely competitive market conditions and improving loss trends in automobile insurance. The firming of automobile pricing in 2001 by the industry in response to deteriorating loss cost trends allowed the Property and Casualty Group to begin raising automobile insurance prices in order to improve underwriting profitability. Because all policies issued by the Property and Casualty Group are for a one-year term, it will take 24 months before the full impact of 2001 rate increases are recognized in earned premiums of Erie Insurance Group.

Our insurance subsidiaries unaffiliated voluntary assumed reinsurance business generated net underwriting losses of $4.1 million, $4.3 million and $3.0 million in 2001, 2000 and 1999, respectively. Our 5.5% share of the Property and Casualty Group s estimated incurred reinsurance losses of $150 million from the World Trade Center terrorist attack contributed to the increased loss in 2001. Our share of these losses totaled $8.3 million in 2001.

During 2001, our property and casualty insurance subsidiaries, Erie Insurance Company and Erie Insurance Company of New York, recorded $7.2 million in reinsurance recoveries under the excess of loss reinsurance agreement with the Exchange. Of the total recoveries in 2001, $6.5 million related to accident year 2001, including the losses related to the World Trade Center terrorist attack, with the balance pertaining to the 1999 accident year. The total recoverable reduced our loss and loss adjustment expenses in 2001. No cash payments were made between the companies in 2001 for these recoveries since the recoveries were recorded based on reserved but yet unpaid losses. No such recoveries were recognized in calendar years 2000 or 1999.

Under the cost sharing agreement for information technology development, our policy acquisition and other underwriting expenses include our property and casualty insurance subsidiaries share of costs related to the eCommerce initiative totaling $1.3 million for 2001. No such costs were incurred in 2000 or 1999.

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The 2001 combined ratio for our property and casualty insurance underwriting operations calculated under GAAP was 114.9%, compared to 108.4% in 2000 and 103.0% in 1999. During 2001, 2000 and 1999, the Company s share of catastrophe losses from direct business amounted to $1.6 million, $2.1 million and $4.4 million, respectively. The GAAP combined ratio for 2001, 2000 and 1999, excluding catastrophe losses on direct business, was 113.7, 106.7 and 99.3, respectively.

During 2001, we received notification of the insolvency of the Reliance Insurance Group. As a result, the Property and Casualty Group companies recorded an estimated assessment of $36.8 million, before consideration of potential premium tax recoveries of $5.9 million. Our share of this assessment was $1.7 million and was recorded in the policy acquisition and other underwriting expenses during the fourth quarter of 2001. This estimate was based upon preliminary data relating to this insolvency and is subject to change as more information becomes available.

Analysis of Investment Operations

Our net revenue from investment operations in 2001 decreased by 75.2% to $18.8 million, compared to $75.6 million in 2000, compared to an increase of 18.5% in 2000 from $63.8 million in 1999. In 2001, the equity markets declined and recovery was further slowed by the World Trade Center terrorist attack. As a result, we experienced declines in value in our investment portfolios over the past year. Net realized losses totaled $31.9 million in 2001 compared to realized gains of $17.0 million in 2000 and $14.7 million in 1999. We recognized realized losses in 2001 as a result of the sale of securities and charges for other than temporary impairments of preferred stock and limited partnerships. The sale of investments in a loss position in 2001 was part of a proactive year-end tax selling strategy. Included in the 2001 realized loss was $4.5 million related to sales of securities of Enron Corporation and its related legal entities. The period of time that various securities held by the Company had been continuously in an unrealized loss position varied. The table below lists the quarter in which any equity securities sold during the fourth quarter of 2001 were first in an unrealized loss position of any amount:

Erie Indemnity Company
Quarter When Equity Issues Sold in the Fourth Quarter of 2001
Were First in Unrealized Loss Position

Quarter	Number of Issues
Third Quarter 2001	12
Second Quarter 2001	15
First Quarter 2001	16
Fourth Quarter 2000	12
Third Quarter 2000	5
Second Quarter 2000	2
First Quarter 2000	6
Fourth Quarter 1999	3
Third Quarter 1999	3
Second Quarter 1999	1
First Quarter 1999	
Fourth Quarter 1998	1
Third Quarter 1998	1

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Impairment charges of investments with declines in value considered by management to be other than temporary totaled $12.1 million in 2001, including charges of $5.7 million in the third quarter of 2001 and $6.4 million in the fourth quarter of 2001. Additionally, $1.3 million of impairment charges were incurred in the fourth quarter of 2000. There were no such impairment charges recorded in 1999. See Business Investments beginning on page 64 for a description of the Company s impairment policy for equity securities.

Net investment income rose 3.1% to $49.9 million in 2001 and 11.7% to $48.4 million in 2000 from $43.3 million in 1999. The growth in investment income for 2001, 2000 and 1999 was offset by cash outflows we used to repurchase $93.4 million of our Class A common stock through December 31, 2001.

Our equity in losses of limited partnerships was $7,000 in 2001, compared to earnings of $4.7 million and $0.6 million in 2000 and 1999, respectively. Private equity and fixed income limited partnerships investments we held realized losses of $1.4 million in 2001 compared to earnings of $2.8 million in 2000 and losses of $0.3 million in 1999. Earnings on our real estate limited partnerships were $1.4 million in 2001, compared to $1.9 million in 2000 and $0.9 million in 1999.

Our share of the earnings of Erie Family Life Insurance Company totaled $0.8 million in 2001, down from $5.5 million in 2000 and $5.0 million in 1999. The decrease in level of earnings from our investment in Erie Family Life Insurance Company is related to Erie Family Life Insurance Company s sales of investments in 2001 resulting in net realized losses on that company s statement of operations.

Financial Condition

September 30, 2002 and 2001

At September 30, 2002 and 2001, our investment portfolio of investment-grade bonds, common stock, preferred stock and cash and cash equivalents totaled $889 million and $792 million, respectively, representing 40.6% and 41.7% of our total assets.

At September 30, 2002 and 2001, the carrying value of our fixed maturity investments represented 70.0% and 65.1%, respectively, of our total invested assets. Our fixed maturity investments consisted of 97.6% and 96.1% of high-quality marketable bonds and redeemable preferred stock, all of which were rated at investment-grade levels (above Ba/BB), at September 30, 2002 and 2001, respectively. Included in this investment-grade category at September 30, 2002 were $244 million, or 37.8%, and at September 30, 2001 were $224 million, or 41.3%, respectively, of the highest quality bonds and redeemable preferred stock rated Aaa/AAA or Aa/AA or bonds issued by the United States government.

At September 30, 2002, the net unrealized gain on fixed maturities, net of deferred taxes, amounted to $16.8 million, compared to $13.5 million at September 30, 2001.

At September 30, 2002 and 2001, equity securities held by the Company included net unrealized gains of $10.5 million and $2.6 million, respectively, net of deferred taxes.

At September 30, 2002, our limited partnership investments increased to $89.0 million from $77.5 million at September 30, 2001. Fixed income and real estate limited partnerships comprised 42.1% and 31.8% of the total limited partnerships at September 30, 2002 and 2001, respectively, while private equity limited partnerships comprised 57.9% and 68.2%, respectively.

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December 31, 2001, 2000 and 1999

At December 31, 2001, 2000 and 1999, our investment portfolio of investment-grade bonds, common stock, preferred stock and cash and cash equivalents totaled $824.6 million, $758.4 million and $714.5 million respectively, representing 42.6%, 46.1% and 47.1%, respectively, of our total assets.

At December 31, 2001, 2000 and 1999, the carrying value of our fixed maturity investments represented 66.6%, 65.6% and 64.9% of our total invested assets, respectively.

Our fixed maturity investments consisted of 96.9%, 96.9% and 97.9% of high-quality, marketable bonds and redeemable preferred stock, all of which were rated at investment-grade levels (above Ba/BB), at December 31, 2001, 2000 and 1999, respectively. Included in this investment-grade category at December 31, 2001 were $230.2 million, or 41.1%, at December 31, 2000, $220.8 million or 41.5%, and at December 31, 1999, $225.7 million or 46.5%, of the highest quality bonds and redeemable preferred stock rated Aaa/AAA or Aa/AA or bonds issued by the United States government.

At December 31, 2001, the net unrealized gain on fixed maturities, net of deferred taxes, amounted to $10.7 million, compared to $4.8 million at December 31, 2000 and a net realized loss of $2.5 million at December 31, 1999.

At December 31, 2001, 2000 and 1999, equity securities held by the Company included net unrealized gains of $22.1 million, $12.7 million and $28.5 million, respectively, net of deferred taxes.

During 2001, limited partnership investments increased to $81.6 million from $68.2 million at December 31, 2000 and $39.1 million at December 31, 1999. Fixed income and real estate limited partnerships, which comprised 34.5%, 28.6% and 49.9% of the total limited partnerships at December 31, 2001, 2000 and 1999, respectively, produced a predictable earnings stream while private equity limited partnerships, which comprised 65.5%, 71.4% and 50.1% of the total limited partnerships, tend to provide a less predictable earnings stream but the potential for greater long-term returns.

Covered Losses and Loss Reserves

Loss reserves are set at full expected cost, except for loss reserves for workers compensation that were discounted at 2.5% in 2001 and 2000. Inflation is implicitly provided for in the reserving function through analysis of costs, trends and reviews of historical reserving results.

The Property and Casualty Group is exposed to new claims on files previously closed (e.g., covered losses not detected during original claim settlement) and to larger than historical settlements (due to changes in law, precedent or underlying inflation) on pending and unreported claims. We are exposed to increased losses by virtue of our 5.5% participation in the intercompany reinsurance pooling arrangement with the Exchange.

Adverse development of losses from prior accident years results in higher calendar year loss ratios and reduced calendar year underwriting results. To the extent prior year reserve deficiencies are indicative of deteriorating underlying loss trends and are material, the Property and Casualty Group s pricing of affected lines of business would be increased to the extent permitted by state departments of insurance. Management also reviews trends in loss developments in order to determine if adjustments, such as reserve strengthening, are appropriate. Any adjustments considered necessary are reflected in current results of operations.

The Property and Casualty Group s $150 million loss estimate anticipates that the World Trade Center terrorist attack is considered one event. If the attack comes to be considered two events, the

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total potential exposure for the Property and Casualty Group would increase between $50 million and $75 million. The effect on the Company, as a result, would be additional losses between $2.7 million and $4.1 million. Taking into consideration the excess of loss reinsurance agreement, the net impact of such potential additional losses to us would be minimal.

Quantitative and Qualitative Disclosures About Market Risk

The Company is exposed to the impact of interest rate changes, changes in market values of investments and to credit risk.

In the normal course of business, the Company employs established policies and procedures to manage its exposure to changes in interest rates, fluctuations in the value of the fair market value of its debt and equity securities and credit risk. The Company seeks to mitigate these risks by various actions described below.

Interest Rate Risk

The Company s exposure to market risk for a change in interest rates is concentrated in the investment portfolio. The Company monitors this exposure through periodic reviews of asset and liability positions. Estimates of cash flows and the impact of interest rate fluctuations relating to the investment portfolio are monitored regularly. Generally, the Company does not hedge its exposure to interest rate risk because it has the capacity to, and does, hold fixed maturity investments to maturity.

Principal cash flows and related weighted-average interest rates by expected maturity dates for financial instruments sensitive to interest rates are as follows:

Erie Indemnity Company
Principal Cash Flows/Weighted Average Interest Rates

(amounts in thousands)	As of December 31, 2001	
	Principal cash flows	Weighted-average interest rate
Fixed maturities:		
2002	$ 37,245	6.5%
2003	35,245	6.5
2004	37,978	7.0
2005	49,515	6.3
2006	55,340	6.5
Thereafter	$ 330,872	7.5
Total	$ 546,195	
Market Value	$ 574,874	

	As of December 31, 2000	
	Principal cash flows	Weighted-average interest rate
Fixed maturities and short-term bonds:		
2001	$ 54,677	6.5%
2002	55,203	6.6
2003	49,720	6.7
2004	47,852	7.0
2005	59,775	6.5
Thereafter	$ 289,077	7.2
Total	$ 556,304	

Market Value	$ 561,502

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The following pro forma information is presented assuming a 100 basis point increase in interest rates at December 31 of each year, and reflects the estimated effect on the fair value of the Company s fixed maturity investment portfolio. The Company used the modified duration of its fixed maturity investment portfolio to model the pro forma effect of a change in interest rates at December 31, 2001 and 2000.

Erie Indemnity Company
Fixed Maturity Interest Rate Sensitivity Analysis

(amounts in thousands)	As of December 31, 2001	As of December 31, 2000
Market value	$ 574,874	$ 561,502
Change in market value(1)	(24,145)	(22,460)
Pro forma market value	550,729	539,042
Modified duration(2)	4.2	4.0

(1) The change in market value is calculated by taking the negative of the product obtained by multiplying (i) modified duration by (ii) change in interest rates by (iii) market value of the portfolio.
(2) Modified duration is a measure of a portfolio s sensitivity to changes in interest rates. It is interpreted as the approximate percentage change in the market value of a portfolio for a certain basis point change in interest rates.

Equity Price Risk

The Company s portfolio of marketable equity securities, which is carried on the Consolidated Statements of Financial Position at estimated fair value, has exposure to price risk, the risk of potential loss in estimated fair value resulting from an adverse change in prices. The Company s objective is to earn competitive relative returns by investing in a diverse portfolio of high-quality, liquid securities.

Portfolio characteristics are analyzed regularly, and market risk is actively managed through a variety of techniques. Portfolio holdings are diversified across industries; concentrations in any one company or industry are limited by parameters established by management and the Company s board of directors. The Company s marketable equity security portfolio is well diversified among primarily actively traded mid- to large-cap stocks. The value of the Company s marketable equity portfolio generally moves with the broad market indices such as the S&P 500. If market prices were to decrease by 10%, the fair value of the Company s marketable equity securities would have had a corresponding decrease of approximately $19 million at December 31, 2001 compared to approximately $20 million at December 31, 2000.

The Company s portfolio of limited partnership investments has exposure to market risks, primarily relating to the viability of the various entities in which they invested. These investments consist primarily of equity investments in small and medium sized companies, and in real estate. These investments involve risk related to changes in the equity and real estate markets. The market value of these limited partnership investments equaled 10% of total invested assets. We actively manage these risks in a variety of ways. These limited partnership investments are diversified to avoid concentration in a particular industry. We perform extensive research, including consideration of the identity of other potential investors, prior to investment in these partnerships.

Credit Risk

The Company s objective is to earn competitive returns by investing in a diversified portfolio of securities. The Company s portfolios of fixed maturity securities, mortgage loans and, to a lesser extent, short-term investments are subject to credit risk. This risk is defined as the potential loss in

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market value resulting from adverse changes in the borrower s ability to repay the debt. The Company manages this risk by performing up front underwriting analysis and through regular reviews by the Company s investment staff. The fixed maturity investments are also maintained between minimum and maximum percentages of invested assets.

The Company s results of operations are directly related to the financial strength of the Exchange. Credit risks related to the receivables from the Exchange are evaluated monthly. Since the Company s inception, it has collected its other receivables from the Exchange in a timely manner (generally within 120 days). Other receivables include amounts due for the management fee and costs paid by the Company on behalf of the Exchange. Other receivables from the Exchange equaled 8.7% and 7.7% of total Company assets as of September 30, 2002 and December 31, 2001, respectively. An additional receivable from the Exchange as relates to reinsurance recoverable amounted to $570.1 million and $491.1 million at September 30, 2002 and December 31, 2001, respectively, or 26.0% and 25.4% of assets, respectively. This receivable relates primarily to unpaid losses ceded to the Exchange as part of the pooling agreement between the Exchange and the Company s property and casualty subsidiaries. The Company collects its reinsurance recoverable receivable generally within 30 days of actual settlement of losses. Reinsurance contracts do not relieve the Company from its primary obligations to policyholders. A contingent liability exists with respect to reinsurance receivables from the Exchange in the event the Exchange would be unable to meet its obligations under its reinsurance agreement with the Exchange. The aggregate of these receivables from the Exchange at September 30, 2002 and December 31, 2001 equaled $761.3 million and $640.7 million, respectively, or 34.7% and 33.1%, respectively, of the Company s total assets. Because of the Company s attorney-in-fact agreements with the subscribers to the Exchange and its pooling agreement with the Exchange, the Company s existence and performance is dependent on the existence and financial stability of the Exchange.

Liquidity and Capital Resources

Liquidity is a measure of an entity s ability to secure enough cash to meet its contractual obligations and operating needs as they arise. Our major sources of funds from operations are the net cash flow generated from management operations, the net cash flow from our property and casualty insurance subsidiaries 5.5% participation in the underwriting results of the Property and Casualty Group and investment income from affiliated and nonaffiliated investments.

We generate sufficient net positive cash flow from our operations to fund our commitments and build our investment portfolio, thereby increasing future investment returns. We maintain a high degree of liquidity in our investment portfolio in the form of readily marketable fixed maturities, equity securities and short-term investments. Net cash flows provided by operating activities in 2001, 2000 and 1999 were $148.6 million, $130.6 million and $137.0 million, respectively.

Management fee and other cash settlements due at December 31 from the Exchange were $147.3 million, $118.0 million and $104.3 million in 2001, 2000 and 1999, respectively. A receivable from Erie Family Life Insurance Company for cash settlements totaled $2.3 million at December 31, 2001, compared to $2.0 million at December 31, 2000 and $1.5 million at December 31, 1999. We also have a receivable due from the Exchange for reinsurance recoverable from losses and unearned premium balances ceded to the intercompany reinsurance pool.

The reinsurance recoverable from the Exchange rose 19.2% to $491.1 million at December 31, 2001 from the $412.0 million at December 31, 2000 and 12.8% from $365.2 million at December 31, 1999. These increases are the result of corresponding increases in direct loss reserves, loss adjustment expense reserves and unearned premium reserves of the Company s property and

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casualty insurance subsidiaries that are ceded to the Exchange under the intercompany pooling arrangement. The increase in direct loss reserves, loss adjustment expense reserves and unearned premium reserves ceded to the Exchange is a result of a corresponding increase in direct premium written by the Company s property and casualty insurance subsidiaries. The increase in direct written premium of the subsidiaries of the Company that is ceded to the Exchange was 18.3% and 11.4% for the years ended December 31, 2001 and 2000, respectively. Total receivables from the Exchange represented 12.3% of the Exchange s assets at September 30, 2002, 9.1% at December 31, 2001, 7.6% at December 31, 2000 and 6.3% at December 31, 1999.

We established a stock repurchase program in 1999 pursuant to which we may have repurchased as much as $120 million of our Class A common stock through December 31, 2002. In 2001, 220,000 shares were repurchased at a total cost of $7.7 million. During the first nine months of 2002, 207,217 shares were repurchased at a total cost of $8.5 million. From its inception through September 30, 2002, 3,402,894 shares have been repurchased at a total cost of $101.9 million. We suspended the stock repurchase program in connection with this offering of Class A common stock because we did not believe it was appropriate to buy Class A common stock in the market while a registered offering was pending and considering the repurchase program was expiring at the end of 2002.

Dividends declared to shareholders totaled $40.4 million, $36.2 million and $32.8 million in 2001, 2000 and 1999, respectively. There are no regulatory restrictions on the payment of dividends to our shareholders, although there are state law restrictions on the payment of dividends from our insurance subsidiaries to us.

Temporary differences between the financial statement carrying amounts and tax bases of assets and liabilities that give rise to deferred tax assets and liabilities resulted in net deferred tax liabilities at December 31, 2001, 2000 and 1999 of $12.9 million, $7.2 million and $11.8 million, respectively. The primary reason for the increase in the deferred tax liability in 2001 is an increase in unrealized gains from available-for-sale securities and limited partnerships in 2001 of $18.0 million resulting in an increase in deferred tax liability of $6.3 million. Management believes it is likely that we will have sufficient taxable income in future years to realize the benefits of the gross deferred tax assets.

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BUSINESS

We operate predominantly as a provider of sales, underwriting and policy issuance services to the Exchange. We also operate as a property and casualty insurer through our subsidiaries. We have served since 1925 as the attorney-in-fact for the policyholders of the Exchange. The Property and Casualty Group writes personal and commercial lines property and casualty coverages exclusively through approximately 8,000 independent agents and pool their underwriting results. The financial results of the Exchange are not consolidated with ours.

For our services as attorney-in-fact, we charge the Exchange a management fee calculated as a percentage, limited to 25%, of the direct written premiums of the Exchange in addition to the direct written premiums of the other members of the Property and Casualty Group, all of which are initially assumed by the Exchange under the pooling agreement. Management fees accounted for approximately 78% of our revenues for the nine months ended September 30, 2002. For the first nine months of 2002, 70% of direct premiums written by the Property and Casualty Group were personal lines, while 30% were commercial lines. We also own 21.6% of the common stock of Erie Family Life Insurance Company, an affiliated life insurance company, of which the Exchange owns 53.5% and public shareholders, including our directors, own 24.9%. At September 30, 2002, we had total assets of $2.2 billion and shareholders equity of $958 million. Our net income was $138.2 million for the nine months ended September 30, 2002 and $122.3 million for the year ended December 31, 2001.

We believe we are the only publicly-traded attorney-in-fact for a reciprocal insurance exchange in the country. Several other private property and casualty companies, such as USAA and Farmers Insurance Group (owned by Zurich Financial Services Group), also operate as reciprocals with separate management arrangements. Our earnings are largely generated from fees based on the direct written premium of the Exchange in addition to the direct written premiums of the other members of the Property and Casualty Group. As such, we have an interest in the growth and financial condition of the Exchange.

In addition to our interest in the growth in premium of the Exchange, our property and casualty insurance subsidiaries also participate in the underwriting results of the Exchange. Our property and casualty insurance subsidiaries share in the underwriting results of the Exchange via a pooling arrangement under which the Exchange has a 94.5% participation in the underwriting results of the Property and Casualty Group and our insurance subsidiaries, Erie Insurance Company and Erie Insurance Company of New York, have a 5.5% participation. As such, we have an interest in the underwriting profitability of the business written as well as the volume of premium written. The Property and Casualty Group wrote approximately $3.0 billion in premium during the twelve months ended September 30, 2002. Of the net underwriting risk for this $3.0 billion, $2.8 billion in premium, or 94.5%, is borne by the Exchange. The remaining $165 million, or 5.5%, of the net underwriting risk is borne by our property and casualty insurance subsidiaries via the pooling arrangement with the Exchange.

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The Property and Casualty Group seeks to insure standard and preferred risks in primarily private passenger automobile, homeowners and small commercial lines, including workers compensation policies. We believe the Property and Casualty Group has differentiated its products from standard industry products by providing additional coverages, which enhance agents marketing efforts. The Property and Casualty Group is represented by an agency force consisting of over 1,700 independent agencies comprised of approximately 8,000 agents in 11 Midwestern, Mid-Atlantic and Southeastern states (Illinois, Indiana, Maryland, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and Wisconsin) and the District of Columbia. These independent agents play a significant role as underwriters and are major contributors to our success.

We have reported increasing net operating income for 14 consecutive years. Our growth has primarily been driven by an expansion of the Property and Casualty Group s business into new territories, the appointment of new agencies, high policy and agency retention rates and, recently, increased premium rates.

Since 1997, the Property and Casualty Group has entered Illinois and Wisconsin and expects to begin operating in Minnesota in the third quarter of 2004.

In 2001, we continued the planned expansion of the Property and Casualty Group s independent agency force by appointing 247 agencies. Since 1997, we have increased the overall number of agencies representing the Property and Casualty Group by 60%.

The Property and Casualty Group has a very stable base of policyholders. The Property and Casualty Group s retention rate (the percentage of existing policyholders who renew their policies) of 90.9% in 2001 compared favorably to an average of 82.6% for a core benchmark group consisting largely of regional property and casualty carriers, according to a 2001 Ward Group benchmark study.

The Property and Casualty Group is achieving premium rate increases as a result of the current favorable market conditions in both commercial and personal property and casualty lines, which are generally referred to within the industry as hard market conditions . Hard market conditions are characterized by increasing premium rates, more stringent underwriting standards and a need for additional capital in the industry. The Property and Casualty Group and the Company have benefited from these hard market conditions and for the twelve months ended September 30, 2002 experienced average premium per policy increases of 7.2% for personal automobile insurance policies, 17.6% for commercial lines policies and 9.5% across all lines. Management believes increases in premium rates are likely to continue in 2002 and 2003 because of the industry s need to improve underwriting results and to achieve adequate operating returns in light of the reduced investment yields resulting from low interest rates and poor returns in the equity markets. Premium rates approved by regulators that will be realized in the fourth quarter of 2002 and in 2003 totaled $46.9 million and $96.6 million, respectively. These premium increases were primarily related to private passenger automobile, homeowners and commercial multiple peril lines of business in the states of Pennsylvania, Ohio and West Virginia. Generally, the Company s profit margins from management operations have increased during periods of premium rate increases.

As a result of these growth initiatives and market conditions, the Property and Casualty Group had over 3.4 million insurance policies in force as of September 30, 2002, an 11.9% increase from September 30, 2001. Personal lines policies in force grew by 11.8% during the twelve months ended September 30, 2002, while commercial lines policies increased 13.0% over the same period.

The Erie Insurance Group built its reputation in the industry and among insurance consumers, agents and others on its commitment to be Above all in sERvIcE[SM] . Customer satisfaction surveys independently conducted by a nationally recognized research firm have ranked the Property and Casualty Group:

No. 2 for homeowners insurance in 2002 and No. 1 for homeowners insurance in 2001;

No. 3 for private passenger automobile insurance in 2002 and No. 2 for private passenger automobile insurance in 2001 and 2000; and

No. 1 for automobile collision repair in 2002, the first year this survey was conducted.

Each member of the Property and Casualty Group is rated A++ (Superior) by A.M. Best, its highest financial strength rating, which was held by only 2.8% of the property and casualty insurance groups rated by A.M. Best as of July 11, 2002.

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Our Competitive Advantages

We believe that our competitive advantages come from:

Committed, loyal and productive independent agency force. We seek to develop long-term business relationships with high-quality independent agencies. Prior to allowing an agency to represent the Property and Casualty Group, we undertake a rigorous selection process that seeks agency principals who meet our high standards and operate their agencies in line with Erie Insurance Group s business philosophy. We believe the independent agency force has been loyal and that the Property and Casualty Group is the preferred carrier for most of the independent agencies that represent it. Average annual written premium volume per agency is approximately $1.7 million for these agencies.

Focus on quality service. Service to the policyholder and agent has been a tradition of the Erie Insurance Group since its founding more than 77 years ago. Erie Insurance Group has consistently been recognized as a provider of quality service. Customer satisfaction surveys independently conducted by a nationally recognized research firm ranked the Property and Casualty Group No. 2 for homeowners insurance in 2002 and No. 1 in 2001, No. 3 for private passenger automobile insurance in 2002 and No. 2 in 2001 and 2000 and No. 1 for automobile collision repair in 2002, the first year that survey was conducted. The claims force is comprised predominantly of personnel trained in Erie Insurance Group s service-oriented claims settlement philosophy.

Competitive products and pricing. A key to attracting a highly effective sales force of independent agents and enhancing the Property and Casualty Group s ability to attract customers is a portfolio of competitively priced products. These products include many additional coverages that we believe differentiate the Property and Casualty Group s products in the marketplace.

Cost-efficient operation. Expense management is one of Erie Insurance Group s founding traditions and is an important part of its culture. We believe the Erie Insurance Group s operations are cost-efficient. In addition, Erie Insurance Group s organizational structure is relatively flat and combines the advantages of centralized common services with field marketing and claims services. Average agency annual written premium volume of $1.7 million allows us to keep agency training, marketing and support costs low. The Property and Casualty Group s five-year statutory average loss adjustment and underwriting expense ratio for the period from 1997 to 2001 is 37.2%, which compares favorably to A.M. Best s property and casualty industry composite average of 40.3%. The loss adjustment expense ratio is the ratio of loss adjustment expenses (the expenses incurred in settling a claim) incurred, including estimates thereof for claims incurred but not reported, to net premiums earned, and an underwriting expense ratio is the ratio of underwriting expenses incurred to net premiums earned. The Property and Casualty Group s underwriting expense ratio includes the management fee paid to us of 25% of direct premiums written, which was reduced to 24% for 2003. The actual cost of management operations is less than the management fee, which results in a profit for our shareholders. If the actual cost of management operations were used to compute the underwriting expense ratio, consistent with industry-reported results, the loss adjustment and underwriting expense ratio would be 30.7%, which compares even more favorably to industry averages. In a 2001 benchmarking study completed by Ward Group, productivity of the Company and the Property and Casualty Group, as measured by the ratio of full time equivalent employees to gross premiums written (total insurance premiums written during a given period), is over 40% better than the core benchmark group.

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Unique corporate structure. The Erie Insurance Group s operating structure allows for:

A long-term management approach to business. Erie Insurance Group aims to nurture its relationships with policyholders, agents and employees to create long-term value. Each of our principal executive officers has been with Erie Insurance Group for over 20 years and is committed to this long-term view of the business.

Lower earnings volatility. Since the bulk of the insurance risk of the Property and Casualty Group remains with the Exchange, we do not experience the same earnings volatility as competing property and casualty insurance carriers.

A long-term investment horizon. Since most of the capital and reserves necessary to support the Property and Casualty Group s insurance underwriting business are held by the Exchange, which is not a publicly-owned entity, a long-term total return strategy is used in investing the Exchange s assets. Though recent equity market results have had a significant negative effect on the value of the Exchange s investment portfolio, the Exchange s investment strategy of investing in equity securities has created substantial surplus capacity over an extended period of time. From January 1, 1995 to September 30, 2002, the Exchange s equity investments generated a pre-tax compound annual return of 10.8% compared to a pre-tax compound annual return of 9.5% for the Standard & Poor s 500 Index.

Strategy

The Erie Insurance Group s overall strategy includes providing attractive property and casualty insurance products at competitive prices, coupled with high-quality service. The Erie Insurance Group distributes these products exclusively through independent insurance agents whose insurance and underwriting expertise, local market knowledge and commitment to service have been key drivers of Erie Insurance Group s growth. The Erie Insurance Group s strategy includes:

Growth by expansion of existing operations, rather than through acquisitions, including by (i) a careful agency selection process in which the Property and Casualty Group seeks to be the primary property and casualty underwriter for each agency, (ii) a thoughtful expansion into favorable states and (iii) increased market penetration in existing operating territories.

Quality service to policyholders in claims handling, underwriting and other service activities.

Achieving underwriting profits for the Property and Casualty Group by focusing on standard and preferred risks and by setting and adhering to consistent underwriting standards.

A business model designed to provide the advantages of localized marketing and claims servicing with the economies of scale derived from centralized management and administration.

Our Operating Segments

Our financial results are segmented into management operations, insurance underwriting operations and investment operations. As attorney-in-fact for the subscribers to the Exchange, we provide sales, underwriting and policy issuance services on behalf of the Exchange and take no underwriting risk. This segment is the largest contributor to our earnings, providing pre-tax income of $189.1 million for the nine months ended September 30, 2002 and $184.6 million for 2001. In the property and casualty insurance underwriting operations, we take underwriting risk through our insurance subsidiaries. This segment had a pre-tax loss of $16.0 million for the nine months ended September 30, 2002 and $20.5 million for 2001. Investment operations include investment income and realized gains and losses generated by assets of our management and insurance underwriting operations. This segment had pre-tax income of $33.2 million for the nine months ended September 30, 2002 and $18.0 million for 2001.

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The following table summarizes the revenue we receive and the costs we incur in connection with these three segments:

Erie Indemnity Company
Operating Segment Summary

(amounts in thousands)

Segment	Income Statement Item	Description	Nine Months Ended September 30, 2002	Year Ended December 31, 2001
			(unaudited)	
Management Operations	Management fee revenue +	Direct premium written by the Property and Casualty Group x management fee rate (25% for 2002 and 24% for 2003)	$ 593,895	$ 634,966
	Service agreement revenue -	Reinsurance premiums assumed from non-affiliates x service agreement rate (7% for 2002 and 6% for 2003) and per installment charge for premiums billed on an installment basis (currently $3)	16,310	27,247
	Cost of management operations	Cost of sales, including commissions, underwriting, policy issuance and administration	(421,097)	(477,645)
	= Segment income before income taxes		$ 189,108	$ 184,568
Insurance Underwriting Operations(1)	Premiums earned -	5.5% of the Property and Casualty Group earned premiums	$ 119,824	$ 137,648
	Losses and loss adjustment expense -	5.5% of the Property and Casualty Group losses and loss adjustment expense	(98,431)	(117,201)
	Policy acquisition and other underwriting expense	5.5% of the Property and Casualty Group policy acquisition and other underwriting expense	(37,343)	(40,910)
	= Segment (loss) before income taxes		$ (15,950)	$ (20,463)
Investment Operations	Net investment revenue from management operations(2) +	Investment income and realized gains (losses) generated by assets retained in management operations	$ 24,882	$ 927
	Net investment revenue from insurance underwriting operations(3)	Investment income and realized gains (losses) generated by assets of our property and casualty subsidiaries	8,305	17,071
	= Segment income before income taxes		$ 33,187	$ 17,998
Total	Total income before income taxes		$ 206,345	$ 182,103

(1) Includes the effect of the all-lines aggregate excess of loss agreement currently in place with the Exchange.
(2) Includes realized capital losses of $3.4 million for the nine months ended September 30, 2002 and $30.7 million for 2001.
(3) Includes realized capital losses of $5.2 million for the nine months ended September 30, 2002 and $1.1 million for 2001.

Our Management Operations

We recognize management fees due from the Exchange as income when the premiums are written because at that time we have performed substantially all of the services we are required to perform, including sales, underwriting and policy issuance activities, but currently such fees are not paid to us by the Exchange until it collects the premiums. Management fees received from the Exchange accounted for 78% of our revenues for the nine months ended September 30, 2002 and 78% of our revenues in 2001. The management fee rate charged to the Exchange is set by and may be changed at the discretion of our board of directors. The fee has been at its maximum permitted level of 25% since 1999 and was 24.25% in 1998 and 24% in 1997. Our board of directors generally sets the management fee rate each December for the following year. At our December 10, 2002 board of directors meeting, the board voted to reduce the management fee for 2003 to 24%.

Since 1995, we have received a service agreement fee from the Exchange, at the rate of 7% of voluntary assumed written premium as compensation for the management and administration of its voluntary assumed reinsurance business from non-affiliated insurers. Reinsurance is an arrangement in which an assuming company indemnifies an insurer or reinsurer (a ceding company) against all or a portion of the insurance or reinsurance risks underwritten by the ceding company under one or more policies. At our December 10, 2002 board of directors meeting, the board voted to reduce the service agreement rate for 2003 to 6%. Service agreement revenue is earned when reinsurance premiums are earned because the services we are required to perform are completed over the terms of the related treaties. We also collect service charges from policyholders who pay their premiums in installments on policies written by the Property and Casualty Group. The service agreement rate and service charge amount are periodically evaluated and are subject to change.

Erie Indemnity Company
Management Operations Financial Results

(amounts in thousands, except percentages)	Nine Months Ended September 30,		Year Ended December 31,				
	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Direct premium written by Property and Casualty Group	$ 2,375,579	$ 1,923,219	$ 2,539,863	$ 2,206,583	$ 2,053,501	$ 2,017,103	$ 1,948,343
Management fee rate	*25.00%*	*25.00%*	*25.00%*	*25.00%*	*25.00%*	*24.25%*	*24.00%*
Management fee revenue	$ 593,895	$ 480,805	$ 634,966	$ 551,646	$ 513,375	$ 489,147	$ 467,603
Service agreement revenue	16,310	20,339	27,247	22,662	15,441	13,879	7,026
Total revenue from management operations	$ 610,205	$ 501,144	$ 662,213	$ 574,308	$ 528,816	$ 503,026	$ 474,629
Cost of management operations	421,097	349,796	477,645	415,562	380,298	357,783	340,428
Net investment revenue from management operations(1)	24,882	20,474	927	51,721	41,966	28,883	25,179
Income before income taxes	$ 213,990	$ 171,822	$ 185,495	$ 210,467	$ 190,484	$ 174,126	$ 159,380
(1) Includes realized (losses) gains of:	$ (3,467)	$ (4,099)	$ (30,735)	$ 16,469	$ 14,408	$ 6,363	$ 5,551

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The direct written premiums of the Property and Casualty Group have a direct impact on the Company s management fee revenue and, consequently, the Company s management operations. The following table sets forth our management fee revenue by state and by line of business for the year ended December 31, 2001:

Erie Indemnity Company
Management Fee Revenue By State and Line of Business for 2001

(amounts in thousands)

State	Private Passenger	Commercial Auto	Homeowners	Commercial Multi Peril	Workers Compensation	All other Lines of Business	Total
Pennsylvania	$ 193,280	$ 23,004	$ 50,042	$ 27,319	$ 26,801	$ 7,806	$ 328,252
Maryland	40,521	6,869	12,689	6,383	6,311	2,671	75,444
Ohio	29,094	4,312	9,619	7,123	0	1,697	51,845
Virginia	22,413	5,404	7,695	6,254	6,993	1,958	50,717
North Carolina	11,948	4,718	6,171	5,255	3,993	1,384	33,469
West Virginia	18,070	2,644	4,115	2,757	0	838	28,424
Indiana	13,309	1,721	5,742	2,846	2,041	845	26,504
New York	10,319	1,887	2,654	3,010	1,645	494	20,009
Tennessee	3,712	1,378	1,450	1,830	1,278	386	10,034
Illinois	3,075	645	1,048	1,667	1,010	223	7,668
District of Columbia	548	108	247	510	595	117	2,125
Wisconsin	191	52	68	63	78	23	475
Total	$ 346,480	$ 52,742	$ 101,540	$ 65,017	$ 50,745	$ 18,442	$ 634,966

The following table sets forth our management fee revenue by line of business and percentage growth for each of the five years ended December 31, 2001:

Erie Indemnity Company
Management Fee Revenue By Line of Business 2001-1997

(amounts in thousands, except percentages)

Year	Private Passenger	Commercial Auto	Homeowners	Commercial Multi Peril	Workers Compensation	All other Lines of Business	Total	Percent Increase
2001	$ 346,480	$ 52,742	$ 101,540	$ 65,017	$ 50,745	$ 18,442	$ 634,966	15.1%
2000	313,703	43,318	88,743	50,401	39,914	15,567	551,646	7.5
1999	305,346	37,663	80,377	42,646	33,363	13,980	513,375	5.0
1998	304,026	33,555	69,845	36,096	31,409	14,216	489,147	4.6
1997	295,424	32,796	60,443	31,384	32,906	14,649	467,602	5.6

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The following table sets forth the Property and Casualty Group s percentage of management fees by state for each of the five years ended December 31, 2001.

Erie Indemnity Company
Percentage of Management Fees By State 2001-1997

State	2001	2000	1999	1998	1997
Pennsylvania	51.7%	53.9%	55.6%	58.1%	59.3%
Maryland	11.9	11.9	11.9	11.7	12.0
Ohio	8.2	8.0	7.9	7.6	7.4
Virginia	8.0	8.0	8.1	8.1	8.3
North Carolina	5.3	4.6	4.1	3.3	2.7
West Virginia	4.4	4.6	4.6	4.6	4.6
Indiana	4.2	4.0	3.9	3.8	3.7
New York	3.1	2.7	2.2	1.4	0.8
Tennessee	1.6	1.4	1.3	1.2	1.0
Illinois	1.2	0.6	0.2	0.0	0.0
District of Columbia	0.3	0.3	0.2	0.2	0.2
Wisconsin	0.1	0.0	0.0	0.0	0.0
Total direct premiums written	100.0%	100.0%	100.0%	100.0%	100.0%

The cost of management operations includes all independent agent commission expenses as well as personnel and benefit costs, underwriting and policy issuance costs and other administrative expenses of the Company.

The largest component of the cost of management operations is the cost of our independent agent commissions and other incentives to our independent agents. Included in commission costs is the cost of scheduled commissions earned on premiums written, agency contingency awards based on the three-year average underwriting profitability of the business written with us, accelerated commissions earned by start-up agencies and promotional incentives to agents.

Personnel and benefit costs related to the sales, underwriting and issuance of policies and the administrative staff of the Company are the second largest cost of management operations. Expenses other than personnel and benefit costs related to the underwriting and issuance of new business vary with the number of new policies. Underwriting reports, printing, postage and other cost of materials necessary for the underwriting and issuance of policies are included in the cost of management operations.

Additional costs are incurred for general administrative expenses of the Company including the cost of office facilities, travel, telephone and communication costs, the cost of data processing and information technology and other miscellaneous expenses. Beginning in 2001, Erie Insurance Group initiated the eCommerce program and committed to new information technology infrastructure expenditures as part of the program. Our share of these eCommerce infrastructure expenditures are included in the cost of management operations. Non-infrastructure costs of the eCommerce program which are subject to the technology cost-sharing agreement are included in the insurance underwriting segment.

We also earn investment income in this business segment on the cash flow from management operations, which is invested in our investment portfolio. We also report our share of earnings from our 21.6% investment in Erie Family Life Insurance Company as part of the investment income of our management operations segment.

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Insurance Underwriting Operations

Our insurance underwriting operations consist of our three property and casualty insurance subsidiaries that participate in an intercompany pooling arrangement with the Exchange. The pool also includes reinsurance assumed by the Exchange from non-affiliated entities. The table below presents a financial summary of results of the property and casualty insurance operations of the Property and Casualty Group.

Erie Indemnity Company
Insurance Underwriting Operations Financial Results

	Nine Months Ended September 30,		Year Ended December 31,				
(amounts in thousands)	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Premiums earned	$ 119,824	$ 100,857	$ 137,648	$ 123,708	$ 117,224	$ 112,939	$ 107,350
Net investment revenue from insurance underwriting operations(1)	8,305	14,934	17,071	18,381	16,765	16,887	13,569
Total revenues	$ 128,129	$ 115,791	$ 154,719	$ 142,089	$ 133,989	$ 129,826	$ 120,919
Losses and loss adjustment expenses	98,431	88,074	117,201	99,564	87,719	79,881	79,970
Policy acquisition and underwriting expenses	37,343	28,696	40,910	34,546	33,044	32,491	29,639
Total losses and expenses	$ 135,774	$ 116,770	$ 158,111	$ 134,110	$ 120,763	$ 112,372	$ 109,609
(Loss) income before income taxes	$ (7,645)	$ (979)	$ (3,392)	$ 7,979	$ 13,226	$ 17,454	$ 11,310

(1) Includes realized (losses) gains of:	$ (5,160)	$ 1,374	$ (1,144)	$ 499	$ 337	$ 800	$ 264

Under the pooling arrangement, all property and casualty insurance business of the five property and casualty insurance companies that comprise the Property and Casualty Group is pooled within the Exchange as the pooling entity. Our insurance subsidiaries, Erie Insurance Company and Erie Insurance Company of New York, share in the underwriting results of the pool through retrocession. Erie Insurance Company has a 5.0% participation, Erie Insurance Company of New York has a 0.5% participation and the Exchange has a 94.5% participation in the pooled underwriting results. These participation percentages are determined by our board of directors. Pooling participation percentages have not changed since 1995.

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Erie Insurance Company and Erie Insurance Company of New York have an all-lines aggregate excess of loss reinsurance agreement with the Exchange that limits the amount of their annual net losses. Excess of loss reinsurance is reinsurance that indemnifies the reinsured against all or a specified portion of losses on underlying insurance policies in excess of a specified amount. Under the reinsurance agreement, once Erie Insurance Company and Erie Insurance Company of New York sustain ultimate net losses and allocated loss expenses in an accident year that exceed an amount equal to 72.5% of Erie Insurance Company s and Erie Insurance Company of New York s net premiums earned, the Exchange will be liable for 95% of the amount of such excess up to, but not exceeding, an amount equal to 95% of 15% of Erie Insurance Company s and Erie Insurance Company of New York s net premium earned. Erie Insurance Company and Erie Insurance Company of New York retain the remaining 5% of such layer as well as ultimate net losses and allocated loss expenses in excess of 87.5% of Erie Insurance Company s and Erie Insurance Company of New York s net premiums earned.

The Property and Casualty Group sells personal and commercial lines policies through independent agencies. Commercial lines policies are marketed to small- and medium-sized businesses. Premium revenues from our property and casualty insurance underwriting operations accounted for approximately 16% of our revenues in the nine months ended September 30, 2002 and 17% of our revenues in 2001.

The Property and Casualty Group has exposure to reinsurance that the Exchange assumes from unaffiliated insurers, placed principally through unaffiliated brokers. The Exchange engages in this

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assumed reinsurance business, which represented net premiums written of $131.3 million for the nine months ended September 30, 2002 and $158.1 million for the year ended December 31, 2001, in each case net of retrocessions, in order to geographically diversify the overall insurance risk to the Property and Casualty Group. The assumed business, which is included in the pooling arrangement, consists predominately of property lines excess of loss treaties. In 2002, management tightened underwriting standards, limited coverages, excluded terrorism coverage and, consistent with market conditions, increased rates for this business. Treaties are generally renewed annually and management evaluates each treaty for profitability and continuing desirability of the customer relationship during the renewal process.

We also earn investment income in this business segment on the cash flow from property and casualty insurance underwriting operations, which is invested in our investment portfolio.

The following table sets forth certain data for the Property and Casualty Group compared to industry composites for the five years ended December 31, 2001.

Property and Casualty Group
Five-Year Comparison vs. Industry Composite

	Net Premiums Written Growth		Loss Ratio		Operating Expense Ratio(2)		Policyholder Dividend Ratio		Combined Ratio	
	Erie	Industry(1)	Erie	Industry(1)	Erie	Industry(1)	Erie	Industry(1)	Erie	Industry(1)
2001	14.8%	9.1%	78.1%	75.4%	39.7%	39.7%	0.6%	0.8%	118.4%	115.9%
2000	8.3	5.7	69.8	68.5	36.8	40.4	0.8	1.5	107.4	110.3
1999	2.6	2.0	65.5	65.4	36.1	41.1	0.4	1.3	102.0	107.8
1998	4.4	1.6	59.2	63.4	38.2	40.7	0.6	1.9	98.0	106.0
1997	5.6	3.0	65.1	60.6	34.6	39.4	0.9	1.8	100.6	101.9
5-year compound annual growth rate or average	7.2%	4.2%	68.0%	66.9%	37.2%	40.3%	0.7%	1.4%	105.9%	108.6%

(1) A.M. Best s Aggregates and Averages, 2002 Edition.
(2) Includes loss adjustment and underwriting expenses.

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Distribution

The Property and Casualty Group s insurance products are marketed primarily in the Midwest, Mid-Atlantic and Southeast regions through over 1,700 insurance agencies that are comprised of approximately 8,000 agents. The Property and Casualty Group is licensed to do business in 16 states and in the District of Columbia and, at September 30, 2002, operated in 11 states (Illinois, Indiana, Maryland, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and Wisconsin) and the District of Columbia. The Property and Casualty Group maintains branch offices throughout these states. The Property and Casualty Group expects to begin operating in Minnesota in the third quarter of 2004.

Property and Casualty Group
States of Operation

State	Year Began Writing	% of Total
Pennsylvania	1925	52%
Maryland	1953	12
Ohio	1968	8
Virginia	1955	8
North Carolina	1991	5
West Virginia	1963	4
Indiana	1978	4
New York	1995	3
Tennessee	1987	2
Illinois	1999	1
District of Columbia	1953	Less than 1%
Wisconsin	2001	Less than 1%

In 2001, we continued our ongoing expansion of the independent agency force by appointing 247 agencies. Since 1997, we have increased the overall number of agencies representing the Property and Casualty Group by 60%. Partially due to growth in the number of agents, the Property and Casualty Group has achieved rapid growth in premiums. As of September 30, 2002, the Property and Casualty Group had over 3.4 million insurance policies in force, an 11.9% increase from September 30, 2001. Personal lines policies in force grew by 11.8% during the twelve months ended September 30, 2002, while commercial lines increased 13.0% over the same period.

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Property and Casualty Group
12-Month Rolling Average Policy Growth Rates by Line of Business

	Twelve Months Ended						
	September 30, 2002	June 30, 2002	March 31, 2002	December 31, 2001	September 30, 2001	June 30, 2001	March 31, 2001
Personal lines:							
Private passenger auto	10.4%	9.4%	8.3%	7.1%	6.3%	5.9%	5.3%
Homeowners	13.1	11.4	10.1	9.0	8.4	8.1	7.7
All other personal lines	14.4	13.4	12.2	11.5	11.4	10.9	10.7
Total personal lines	11.8	10.5	9.3	8.2	7.5	7.1	6.6
Commercial lines:							
Commercial auto	11.8	11.6	10.7	9.7	8.8	7.9	7.0
Commercial multi-peril	14.4	13.9	12.5	11.6	11.1	10.8	10.6
Workers compensation	12.5	11.9	10.8	10.3	9.6	9.5	8.7
All other commercial lines	11.5	11.7	10.7	9.9	9.0	8.9	8.0
Total commercial lines	13.0	12.6	11.5	10.7	9.9	9.5	8.9
Total	11.9	10.8	9.6	8.5	7.8	7.4	6.9

In addition, the Property and Casualty Group experiences above average retention rates. Based upon an annual best practices benchmark study conducted by the Ward Group, an independent financial services consulting company, the Property and Casualty Group s policy retention rate of 90.9% is among the highest of all the property and casualty companies benchmarked by the Ward Group.

Property and Casualty Group
12-Month Rolling Average Policy Retention Rates by Line of Business

	Twelve Months Ended						
	September 30, 2002	June 30, 2002	March 31, 2002	December 31, 2001	September 30, 2001	June 30, 2001	March 31, 2001
Private passenger automobile	92.50%	92.35%	92.26%	92.24%	92.22%	92.25%	92.24%
Commercial automobile	90.79	91.12	90.86	90.53	90.16	90.35	90.29
Homeowners	90.54	90.35	90.24	90.24	90.38	90.63	90.66
Commercial multi-peril	88.69	88.95	88.77	88.03	88.18	88.36	88.58
Workers compensation	89.51	89.46	89.34	88.43	88.53	88.76	89.06
All other lines	88.15	88.30	88.11	88.15	88.16	88.18	88.03
Total	91.12	91.02	90.91	90.85	90.89	91.01	91.03

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Careful selection of independent agencies to represent the Property and Casualty Group is a key strategy of our Company. The Property and Casualty Group strives to be the primary writing company with the agents. In order to enhance agency relationships and the likelihood of receiving the most desirable underwriting opportunities, we have ongoing, direct communications with the agency force. We believe the independent agency force has been loyal and that the Property and Casualty Group is the preferred carrier for most of these independent agencies. Average agency annual written premium volume is $1.7 million for all of these agencies. Agents have access to a number of Company-sponsored venues designed to promote sharing of ideas, concerns and suggestions with the senior management of Erie Insurance Group with the goal of improving communications and service. These efforts have resulted in outstanding agency penetration and the ability to sustain long-term agency partnerships.

Agents receive commissions for premiums written, as well as promotional incentives and contingency awards. Agent contingency awards are based upon a three-year average of the underwriting profitability of the direct business written and serviced within the Erie Insurance Group by the independent agent. Commission costs rose 14.3% to $323.1 million in 2001 from $282.7 million in 2000 and 7.5% in 2000 from $263.1 million in 1999. Commission costs grew at a slower rate relative to the growth in direct premiums written in 2001 as a result of lower accruals for agent contingency awards compared to 2000. The provision for agent contingency awards totaled $15.7 million, $18.3 million and $19.9 million in 2001, 2000 and 1999, respectively. Commission costs, excluding agent contingency awards, increased 16.2% in 2001, in line with the increase in direct written premiums.

Products

The Property and Casualty Group underwrites a broad range of insurance for risks. In 2001, personal lines comprised 72.6% of direct and affiliated assumed premium revenue while commercial lines constituted the remaining 27.4%. The core products in the personal lines are private passenger automobile (75.2%) and homeowners (22.0%) while the core commercial lines consist principally of multi-peril (37.0%), automobile (30.3%) and workers compensation (29.2%).

The insurance policies of the Property and Casualty Group contain many features not offered as standard coverages by many of our competitors. These extras are a major selling feature for agents. Some examples of these features include:

- full replacement cost coverage with no loss cap on the percentage of insured value in the Property and Casualty Group s full-cost replacement homeowners policy;
- waiver of collision deductible in an automobile claim involving two insureds of the Property and Casualty Group;
- coverage for transportation expense that begins immediately after a collision;
- coverage for locksmith services for keys locked in cars;
- coverage for cost of replacing a deployed airbag;
- coverage for losses due to theft, loss or other unauthorized use of a credit card; and
- coverage for theft, misplacement or loss of jewelry.

The growth rate of policies in force and policy retention trends impact the Company s management and property and casualty operating segments.

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Property and Casualty Group
Policies in Force and 12-Month Rolling Average Policy Retention Rate by Line of Business

	At September 30,		At December 31,				
(amounts in thousands, except percentages)	2002	2001	2001	2000	1999	1998	1997
Policies in Force:							
Personal lines	2,985	2,671	2,724	2,517	2,368	2,255	2,174
Commercial lines	426	377	386	349	322	304	291
Total policies in force	3,411	3,048	3,110	2,866	2,690	2,559	2,465
Policy Retention Percentages:							
Personal policy retention percentages	91.5%	91.4%	91.3%	91.5%	91.0%	90.4%	90.9%
Commercial policy retention percentages	88.1	87.5	87.7	87.3	86.5	85.6	85.6
Total policy retention percentages	91.1	90.9	90.9	91.0	90.5	89.4	89.7

Underwriting

Our Commercial Underwriting Division (Commercial Property and Commercial Automobile Underwriting and Risk Management) and our Personal Lines Underwriting Division (Personal Property and Personal Automobile Underwriting) perform underwriting and processing functions, provide advice, instruction and guidance to the agency force regarding underwriting philosophy and assist other divisions in developing quality products at competitive prices to promote growth and profitability.

We strive toward underwriting profitability by: (1) assessing and selecting quality standard and preferred risks; (2) by adhering to underwriting and re-underwriting guidelines; (3) by providing loss control services with in house loss control specialists and (4) by offering risk management services such as hazard identification loss control program development, risk management training programs and the establishment of safety committees. The Company evaluates and selects those policies believed to be good quality risks. The Company reunderwrites by reviewing existing policies and accounts to determine which risks continue to meet underwriting qualifications and taking appropriate action regarding these policies or accounts. Loss control services are offered to policyholders via the Company s dedicated team of loss control personnel. Risk management services offered to policyholders include hazard identification and analysis, loss control program development, and establishment of safety committees and risk management training programs.

To assure maintenance of acceptable underwriting results, we conduct an annual review of agencies to identify those that do not meet our underwriting performance expectations. Agencies failing to meet our profitability criteria are subject to a detailed review. This review focuses on the factors affecting the property and casualty underwriting results for the agency. The review process includes an evaluation of the underwriting and reunderwriting practices of the agency, completeness and accuracy of applications submitted, staffing levels and adequacy of training of agency staff and adherence by the agency to the business practice, underwriting and service standards of Erie Insurance Group. The review team and the agency jointly develop an action plan to improve agency processes and procedures designed to improve the underwriting profitability of the agency. We then monitor the agency s progress and underwriting performance and may take additional measures, including reducing commissions, and/or terminating the agency if underwriting profitability continues to be unacceptable.

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Claims

The Property and Casualty Group realizes that an insurance policy is also a promise of service. The Property and Casualty Group uses its own trained adjusters wherever possible, to assure that claims are settled quickly and fairly by personnel who know the coverages in the Property and Casualty Group s policies and understand the Erie Insurance Group s service philosophy.

The Property and Casualty Group claims services include:

- Prompt response standards, generally the same day, for contact with an insured after a loss is reported;
- A toll-free number for claims call center where Erie Insurance Group trained personnel handle reporting of losses after normal business hours and on weekends and holidays;
- An automobile glass repair and replacement program for automobile claims designed to simplify and speed the claims process and permit the insured to decide who should do the repair or replacement; and
- A direct repair program for automobile claims that allows insureds to select their own body shop and use one of numerous participating body shops that bill the Property and Casualty Group directly for the repair costs less any deductible.

These and other claims services the Property and Casualty Group offers have resulted in a reputation for fast, fair and courteous claim services and the service awards received from independent consumer organizations.

Technology

In 2001, Erie Insurance Group began a comprehensive program of eCommerce initiatives in support of the Erie Insurance Group s agency force and back office policy underwriting, issuance and administration. The eCommerce program is intended to improve service and efficiency, as well as result in increased sales. The first major component of the eCommerce program (network and desktop hardware deployment) was completed during the second quarter of 2002. Also, the Erie Insurance Group completed the release of the new web interface to a limited number of agents and employees in July 2002. In August 2002, the eCommerce program took advantage of a significant business opportunity to work with a well-known provider of information technology services and solutions to develop the Erie Insurance Group s eCommerce system called ERIEConnection℠. The Erie Insurance Group is now working with that service provider, who is the chief integrator and manager of the eCommerce program and provides software applications that meet the Company s needs. Management of Erie Insurance Group believes this approach will allow the eCommerce program to meet its established budget goals. The Company estimates its share of eCommerce costs in 2003 will amount to approximately $.09 to $.12 per share after income taxes.

Financial Ratings

Insurance companies are rated by rating agencies to provide insurance consumers and investors with meaningful information on the rated companies. Higher ratings generally indicate financial stability and a stronger ability to pay claims. The ratings are generally based upon factors relevant to policyholders and are not directed toward return to investors.

Each member of the Property and Casualty Group currently has an A++ (superior) rating from A.M. Best. A++ is the highest rating that A.M. Best gives to insurance companies, and represents a

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superior ability to meet ongoing obligations to policyholders. Each member of the Property and Casualty Group also has a rating of AA_{pi} (very strong) from Standard & Poor s. A rating of AA means that the insurer has very strong financial security characteristics, differing only slightly from those with the highest rating, AAA. The subscript pi means the rating was based on publicly available information of the Exchange. Standard & Poor s has recently advised the Company that these ratings are being reviewed and may be downgraded. The Exchange s rating from Weiss Ratings, Inc. was downgraded from A (excellent, the highest Weiss rating) to B (lower end of the good rating) in July 2002, while Erie Insurance Company s rating was downgraded from B+ (higher end of good rating) to B (good). At that time, our other insurance subsidiaries maintained their B ratings from Weiss Ratings, Inc. A Weiss rating of B means that the rated company has the financial strength to deal with a variety of adverse economic conditions, but should be reassessed in the event of a severe economic downturn.

Investments

Our investment strategy takes a long-term perspective emphasizing investment quality, diversification and investment returns providing liquidity for our short and long-term commitments. Investments are managed on a total return approach that focuses on both current income and capital appreciation. At September 30, 2002, our investment portfolio increased to $923 million, representing 42.0% of total assets. For the nine months ended September 30, 2002, net investment income was $40.7 million. Net investment income totaled $49.9 million in 2001, compared to $48.4 million in 2000, and $43.3 million in 1999.

Erie Indemnity Company
Total Investments at Market Value

(amounts in thousands)	At September 30,		At December 31,				
	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Investments:							
Fixed maturities	$ 646,172	$ 545,700	$ 559,873	$ 531,546	$ 485,522	$ 441,353	$ 349,973
Equity securities							
Preferred stock	146,955	132,682	130,007	109,081	99,584	112,574	84,963
Common stock	34,964	76,984	63,791	95,365	115,799	90,230	80,170
Limited partnerships	88,952	77,546	81,596	68,242	39,116	17,494	7,932
Real estate mortgage loans	5,601	5,731	5,700	6,581	8,230	8,287	8,392
Total Investments	$ 922,644	$ 838,643	$ 840,967	$ 810,815	$ 748,251	$ 669,938	$ 531,430

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Erie Indemnity Company
Total Investments at Cost

(amounts in thousands)	At September 30,		At December 31,				
	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Investments:							
Fixed maturities	$ 620,274	$ 524,929	$ 543,423	$ 524,172	$ 489,394	$ 421,102	$ 333,136
Equity securities							
Preferred stock	143,732	131,875	127,725	110,555	106,625	109,355	79,361
Common stock	22,040	73,793	32,002	74,413	64,870	60,622	64,762
Limited partnerships	93,197	76,725	79,668	60,661	37,402	17,494	7,932
Real estate mortgage loans	5,601	5,731	5,700	6,581	8,230	8,287	8,392
Total Investments	$ 884,844	$ 813,053	$ 788,518	$ 776,382	$ 706,521	$ 616,860	$ 493,583

Management considers all fixed maturities and marketable equity securities available-for-sale. These securities are stated at fair value, with the unrealized gains and losses, net of deferred tax, reported as a separate component of accumulated other comprehensive income in shareholders equity. When a decline in the value of investments is considered to be other than temporary by management, the investments are written down in the Consolidated Statements of Operations to their realizable value.

For common equity securities (including equity limited partnerships) where the decline in market value is more than 20% below cost for a period exceeding six months, there is a presumption of impairment. Management considers market conditions, industry characteristics and the fundamental operating results of the issuer before deciding to sell the investment at a loss or to recognize an impairment charge to operations. For common equity securities that have declined more than 20% below cost for a period exceeding twelve months, the position is either sold or recognized as impaired and a charge to operations is recognized as realized losses through the Consolidated Statements of Operations. If a security s market value is at least 80% of cost, there is a presumption that the security s decline is temporary regardless if the decline in value is material either individually or in the aggregate unless there are conditions specifically affecting the underlying issuer or its industry that would lead us to believe the security s decline is other than temporary.

Prior to the fourth quarter of 2001, the Company s impairment policy for common equity securities, which was based on existing GAAP guidance, was based primarily on judgments by management as to whether declines in value were other than temporary. The policy considered such factors as the underlying financial condition of the issuer, the short- and long-range prospects of the issuer and other risk factors such as corporate actions and events affecting the issuer. If the Company had used the criteria established for common equity securities in the amended impairment policy it adopted in the fourth quarter of 2001 in earlier periods, approximately $1.8 million (pre-tax) in realized capital losses recognized in the fourth quarter of 2001 would have been recognized over various earlier periods.

For fixed maturity investments, our management analyzes all positions individually whose market value have declined below cost for a period exceeding six months. Management considers market conditions, industry characteristics and the fundamental operating results of the issuer to determine if

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the decline is due to changes in interest rates, changes relating to a decline in credit quality, or other issues specifically affecting the investment. Positions that have incurred market price decline of over 20% for a period greater than six months where the creditworthiness of the issuer indicates a decline that is other than temporary are either sold or recognized as impaired and reflected as a charge to the Company s operations.

If the Company s policy for determining the recognition of impaired positions were different, the Company s Consolidated Statements of Financial Position and results of operations could be significantly impacted. Management believes its investment valuation philosophy and accounting practices result in appropriate and timely measurement of value and recognition of impairment.

Our investments include a 21.6% common stock interest in Erie Family Life Insurance Company of $47.3 million at September 30, 2002, which is accounted for under the equity method of accounting. Dividends paid to us for the nine months ended September 30, 2002 and 2001 totaled over $1.2 million and $1.1 million, respectively. Related to this investment, we are also due $15 million in principal in the form of a surplus note. The note bears an annual interest rate of 6.45% and all payments of interest and principal on the note may be repaid only out of unassigned surplus of Erie Family Life Insurance Company and are subject to prior approval by the Pennsylvania Insurance Commissioner. Interest of the surplus note is scheduled to be paid semi-annually. The note will be payable on demand on or after December 31, 2005.

Fixed Income Securities

At September 30, 2002, the carrying value of fixed income securities accounted for 70.0% of total invested assets. The Company s investment strategy achieves a balanced maturity schedule in order to moderate the effect on investment income in the event of interest rate declines in a year in which a large amount of securities are scheduled to be redeemed or mature.

Erie Indemnity Company
Fixed Maturity Securities at Market Value

(amounts in thousands)	At September 30,		At December 31,				
	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Fixed Maturities:							
U.S. treasuries and government agencies	$ 8,926	$ 11,844	$ 11,713	$ 11,612	$ 11,051	$ 13,707	$ 13,200
State and political subdivisions	55,442	40,801	44,121	51,959	53,118	51,600	44,771
Special revenue	101,574	114,393	113,418	114,566	122,096	139,235	123,901
Public utilities	43,356	28,340	26,270	23,564	20,318	13,416	7,331
U.S. industrial and miscellaneous	376,382	303,143	319,308	266,061	227,176	203,695	156,582
Foreign	46,556	28,579	27,476	29,914	20,743	7,047	4,188
Total bonds	$ 632,236	$ 527,100	$ 542,306	$ 497,676	$ 454,502	$ 428,700	$ 349,973
Redeemable preferred stock	13,936	18,600	17,567	33,870	31,020	12,653	
Total fixed maturities	$ 646,172	$ 545,700	$ 559,873	$ 531,546	$ 485,522	$ 441,353	$ 349,973

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Erie Indemnity Company
Fixed Maturity Securities at Amortized Cost

(amounts in thousands)	At September 30, 2002 (unaudited)	At September 30, 2001 (unaudited)	At December 31, 2001	At December 31, 2000	At December 31, 1999	At December 31, 1998	At December 31, 1997
Fixed Maturities:							
U.S. treasuries and government agencies	$ 8,281	$ 11,211	$ 11,211	$ 11,216	$ 11,029	$ 13,018	$ 12,771
State and political subdivisions	52,071	38,511	42,392	50,337	52,064	48,307	41,931
Special revenue	96,068	110,046	110,267	110,855	120,170	132,025	116,052
Public utilities	42,820	27,286	25,150	23,221	20,909	13,116	7,171
U.S. industrial and miscellaneous	360,806	292,729	311,757	267,231	232,458	195,296	150,666
Foreign	47,177	27,584	26,634	30,082	21,593	7,149	4,545
Total bonds	$ 607,223	$ 507,367	$ 527,411	$ 492,942	$ 458,223	$ 408,911	$ 333,136
Redeemable preferred stock	13,051	17,562	16,012	31,230	31,171	12,191	
Total fixed maturities	$ 620,274	$ 524,929	$ 543,423	$ 524,172	$ 489,394	$ 421,102	$ 333,136

At September 30, 2002, the Company s fixed maturity investments consist of 97.6% of high-quality, marketable bonds and redeemable preferred stock, all of which were rated at investment-grade levels (above Ba/BB). Included in this investment-grade category are $244.3 million or 37.8% of the highest quality bonds and redeemable preferred stock rated Aaa/AAA or Aa/AA or bonds issued by the United States government. Generally, the fixed maturities in the Company s portfolio are rated by external agencies. Management classifies all fixed maturities as available-for-sale securities, allowing the Company to meet its liquidity needs and provide greater flexibility for its investment managers to appropriately respond to changes in market conditions or strategic direction.

Erie Indemnity Company
Fixed Maturity Securities by Credit Quality

(amounts in thousands, except percentages)

Moody s Equivalent Description	At September 30, 2002 Amortized Cost	At September 30, 2002 Estimated Fair Market Value	At September 30, 2002 % of Carry
Aaa/Aa/A	$ 381,508	$ 408,320	63.2%
Baa	223,267	222,525	34.4
Ba/BB	3,929	3,837	0.6
B	5,750	6,775	1.1
In or near default	5,820	4,715	0.7
Total	$ 620,274	$ 646,172	100.0%

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Erie Indemnity Company
Fixed Maturity Securities Term to Maturity

(amounts in thousands, except percentages)	At September 30, 2002		
Term to Maturity	Amortized Cost	Estimated Fair Market Value	% of Carry
Due in less than one year	$ 30,328	$ 30,608	4.7%
Due in 1-5 years	174,835	182,964	28.3
Due in 5-10 years	241,914	251,941	39.0
Due after 10 years	173,197	180,659	28.0
Total	$ 620,274	$ 646,172	100.0%

Equity Securities

Equity securities (common stock and non-redeemable preferred stock) are carried on the Consolidated Statements of Financial Position at market value. The Company s non-redeemable preferred stock portfolio provides a source of highly predictable current income that is competitive with investment-grade bonds. Non-redeemable preferred stocks generally provide for fixed rates of return that, while not guaranteed, resemble fixed income securities and are paid before common stock dividends. Common stock provides capital appreciation potential within the portfolio. Common stock investments inherently provide no assurance of producing income because dividends are not guaranteed.

Erie Indemnity Company
Equity Securities at Market Value

	At September 30,		At December 31,				
(amounts in thousands)	2002	2001	2001	2000	1999	1998	1997
	(unaudited)						
Common stock:							
U.S. industrials and miscellaneous	$ 32,168	$ 68,846	$ 59,709	$ 86,605	$ 103,132	$ 83,563	$ 71,191
U.S. banks, trusts and insurance	2,146	4,445	4,082	3,798	7,156	3,488	6,517
Foreign	650	3,693		4,962	5,511	3,179	2,462
Nonredeemable preferred stock:							
U.S. industrial and miscellaneous	90,032	90,792	91,647	61,134	56,662	60,463	27,914
U.S. banks, trusts and insurance	23,181	16,396	15,565	22,125	36,694	45,338	50,248
Foreign	21,829	25,494	20,416	25,822	6,228	6,773	4,155
Public utilities	11,913		2,379				2,646
Total	$ 181,919	$ 209,666	$ 193,798	$ 204,446	$ 215,383	$ 202,804	$ 165,133

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Erie Indemnity Company
Equity Securities at Cost

(amounts in thousands)	At September 30, 2002 (unaudited)	At September 30, 2001 (unaudited)	At December 31, 2001	At December 31, 2000	At December 31, 1999	At December 31, 1998	At December 31, 1997
Common stock:							
U.S. industrials and miscellaneous	$ 19,777	$ 65,206	$ 28,718	$ 63,662	$ 56,035	$ 53,914	$ 58,415
U.S. banks, trusts and insurance	1,846	3,651	3,284	3,651	3,887	3,522	3,138
Foreign	417	4,936		7,100	4,948	3,186	3,209
Nonredeemable preferred stock:							
U.S. industrial and miscellaneous	89,166	91,593	91,185	62,266	61,109	59,858	25,909
U.S. banks, trusts and insurance	22,189	15,684	14,685	22,094	38,708	42,807	46,901
Foreign	20,475	24,598	19,485	26,195	6,808	6,690	3,932
Public utilities	11,902		2,370				2,619
Total	$ 165,772	$ 205,668	$ 159,727	$ 184,968	$ 171,495	$ 169,977	$ 144,123

Limited Partnerships

The Company s limited partnership investments include U.S. and foreign private equity, real estate and fixed income investments. During the first nine months of 2002, limited partnership investments increased $7.4 million to $89.0 million. Fixed income and real estate limited partnerships, which comprise 42.1% of the total limited partnerships, produce a predictable earnings stream while private equity partnerships, which comprise 57.9% of the total limited partnerships, tend to provide a less predictable earnings stream but the potential for greater long-term returns.

At September 30, 2002, the Company had contractual commitments to invest up to $116 million related to these limited partnership investments. The Company is required to fund these commitments as required by the partnership agreements through September 2007. These represented commitments by the Company to these limited partnerships to fund investments of up to $80 million in private equity securities, $20 million in real estate activities and $16 million in fixed income securities. The Company expects to have sufficient cash flows from operations to meet these limited partnership commitments.

Derivatives

During 2001, we entered into several foreign currency forward contracts that are by definition derivatives. The purpose of these contracts is to partially hedge future capital calls related to our limited partnership commitments. However, under accounting rules, these contracts are not considered hedges. The forward contracts have no cash requirements at the inception of the arrangement. At September 30, 2002, there were no contracts outstanding. For the quarter ended September 30, 2002, changes in value totaling $85,000 were recognized currently in earnings as realized gains in the Consolidated Statements of Operations. Gains on these contracts totaled $214,000 for the nine months ended September 30, 2002 and $50,000 in 2001.

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Securities Lending Program

The Company participates in a securities lending program whereby certain securities from its portfolio are loaned to other institutions for short periods of time through a lending agent. A fee is paid to us by the borrower. Collateral, comprised of cash and government securities, is maintained by the lending agent. The Company has an indemnification agreement with the lending agent in the event a borrower becomes insolvent or fails to return securities. The Company had loaned securities with a market value of $37.4 million and $38.5 million secured by collateral of $39.1 million and $39.6 million at September 30, 2002 and 2001, respectively. The loaned securities are maintained on the Consolidated Statements of Financial Position as a part of invested assets. We have incurred no losses on the loan program since its inception.

Reserves for Our Property and Casualty Subsidiaries

Loss reserves are established to account for the estimated ultimate costs of loss and loss adjustment expenses for claims that have been reported but not yet settled and claims that have been incurred but not yet reported. The estimated loss reserve for reported claims is based primarily upon a case-by-case evaluation of the type of risk involved and knowledge of the circumstances surrounding each claim and the insurance policy provisions relating to the type of loss. Estimates of reserves for unreported claims and loss settlement expenses are determined on the basis of historical information by line of business as adjusted to current conditions. Inflation is implicitly provided for in the reserving function through analysis of historical loss development patterns that reflect the impact of inflation as well as other factors such as changes in claims handling practices, changes in laws and changes in allowable expenses among other things.

The Property and Casualty Group establishes loss and loss expense reserves for the Property and Casualty Group and for all states as a whole for various lines of business groupings. Bulk and incurred but not reported reserves are allocated to each company, state, and line of business. The Property and Casualty Group reviews the insurance laws of all states in which it operates, not just domiciliary states, to ensure that carried loss and loss adjustment expense reserves meet requirements. The statutory annual statements filed by the companies comprising the Property and Casualty Group contain actuarial opinions as to reserve adequacy as required by the states in which the Property and Casualty Group does business.

The loss and loss adjustment expense reserves are computed in accordance with accepted loss reserving standards and principles for the purpose of making a reasonable provision for all unpaid loss and loss expense obligations under the terms of the Property and Casualty Group s policies and agreements. However, the process of estimating the liability for unpaid losses and loss adjustment expenses is inherently judgmental and can be influenced by factors subject to variation. Possible sources of variation include claim frequency and severity, changing rates of inflation as well as changes in other economic conditions, judicial trends and legislative changes. It is unlikely that future losses and loss adjustment expenses will develop exactly as projected. The Property and Casualty Group continually refines reserves as experience develops and new information becomes known. The Property and Casualty Group reflects adjustments to reserves in the results of operations in the periods in which the estimates are changed. With the exception of reserves relating to certain workers compensation cases, which have been discounted at 2.5% since 1998, loss reserves are not discounted.

The Property and Casualty Group continuously reevaluates reserve estimates and retrospectively reviews past reserve estimates. The Property and Casualty Group modifies our selections when we observe current development diverging from our selected development pattern. The Property and Casualty Group also performs various reasonability checks. Historical variation between actual and

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estimated development has not been material in relation to policyholder surplus as of the year ended December 31, 2001.

The following table sets forth the development of our property and casualty subsidiaries reserves for unpaid losses and loss adjustment expense from 1992 through 2001, the period that our property and casualty subsidiaries have assumed underwriting activity under the intercompany pool.

Property and Casualty Subsidiaries of Erie Indemnity Company
Reserves for Unpaid Losses and Loss Adjustment Expenses

	Year Ended December 31,									
	2001	**2000**	**1999**	**1998**	**1997**	**1996**	**1995**	**1994**	**1993**	**1992**
(amounts in millions)										
Net liability for unpaid losses and loss adjustment expense (LAE)	$ 118.7	$ 102.3	$ 95.0	$ 91.4	$ 89.5	$ 84.9	$ 79.0	$ 68.9	$ 65.4	$ 61.0
Net liability re-estimated as of:										
One year later		110.4	103.0	91.3	88.9	87.2	78.4	65.7	61.8	59.0
Two years later			103.9	93.2	85.3	86.6	79.4	65.3	58.5	55.2
Three years later				94.1	87.6	83.4	80.2	68.6	60.1	53.4
Four years later					87.5	84.4	78.2	69.4	65.7	56.1
Five years later						84.5	78.9	68.2	67.3	60.9
Six years later							79.8	68.8	68.8	62.9
Seven years later								69.7	68.2	64.3
Eight years later									69.3	63.8
Nine years later										64.8
Cumulative (deficiency) redundancy		(8.1)	(8.9)	(2.7)	2.0	0.4	(0.8)	(0.8)	(3.9)	(3.8)
Net liability for unpaid losses and LAE	$ 118.7	$ 102.3	$ 95.0	$ 91.4	$ 89.5	$ 84.9	$ 79.0	$ 68.9	$ 65.4	$ 61.0
Reinsurance recoverable on unpaid losses	438.6	375.6	337.9	334.8	323.9	301.5	278.3	275.9	288.5	293.0
Gross liability for unpaid losses and LAE	$ 557.3	$ 477.9	$ 432.9	$ 426.2	$ 413.4	$ 386.4	$ 357.3	$ 344.8	$ 353.9	$ 354.0
Gross re-estimated liability as of:										
One year later		$ 500.4	$ 463.2	$ 414.3	$ 410.6	$ 394.2	$ 351.0	$ 327.3	$ 323.2	$ 408.4
Two years later			464.9	429.0	398.4	398.2	362.3	332.7	322.8	312.6
Three years later				426.9	406.0	388.0	373.0	351.6	332.7	