FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

**QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the quarter ended September 30, 2004

Commission file number 0-24000

ERIE INDEMNITY COMPANY

(Exact name of registrant as specified in its charter)

PENNSYLVANIA	25-0466020
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
100 Erie Insurance Place, Erie, Pennsylvania	16530
(Address of principal executive offices)	(Zip Code)

(814) 870-2000

Registrant's telephone number, including area code

Not applicable

Former name, former address and former fiscal year, if changed since last report

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☑ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes ☑ No o

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Class A Common Stock, no par value, with a stated value of $.0292 per share—63,045,097 shares as of October 15, 2004.

Class B Common Stock, no par value, with a stated value of $70 per share—2,878 shares as of October 15, 2004.

The common stock is the only class of stock the Registrant is presently authorized to issue.

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PART I. FINANCIAL INFORMATION

ERIE INDEMNITY COMPANY

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	(Dollars in thousands)	
	September 30 2004	December 31 2003
	(Unaudited)	
ASSETS		
INVESTMENTS		
Fixed maturities at fair value (amortized cost of $944,585 and $834,649, respectively)	$ 981,989	$ 879,361
Equity securities at fair value (cost of $147,910 and $152,338, respectively)	180,380	189,403
Limited partnerships, under equity method (cost of $110,328 and $105,594, respectively)	122,111	111,218
Real estate mortgage loans	5,079	5,182
Total investments	**1,289,559**	**1,185,164**
Cash and cash equivalents	79,167	87,192
Accrued investment income	13,732	11,119
Premiums receivable from policyholders	295,119	266,957
Reinsurance recoverable from Erie Insurance Exchange on unpaid losses	734,636	687,819
Ceded unearned premiums to Erie Insurance Exchange	122,535	97,249
Notes receivable from Erie Family Life Insurance Company	40,000	40,000
Other receivables from Erie Insurance Exchange and affiliates	222,499	199,078
Reinsurance recoverable non-affiliates	381	480
Deferred policy acquisition costs	17,767	16,761
Property and equipment	13,525	13,868
Equity in Erie Family Life Insurance Company	58,104	56,072
Prepaid pension	53,231	52,666
Other assets	41,742	40,182
Total assets	**$ 2,981,997**	**$ 2,754,607**

See Notes to Consolidated Financial Statements

ERIE INDEMNITY COMPANY

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION (Continued)

	(Dollars in thousands)	
	September 30 2004	December 31 2003
	(Unaudited)	
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES		
Unpaid losses and loss adjustment expenses	$ 905,930	$ 845,536
Unearned premiums	493,313	449,606
Commissions payable and accrued	179,182	152,869
Securities lending collateral	33,430	34,879
Accounts payable and accrued expenses	59,400	46,317
Federal income taxes payable	6,546	117
Deferred income taxes	28,258	27,515
Dividends payable	13,666	13,872
Employee benefit obligations	23,720	19,726
Total liabilities	**1,743,445**	**1,590,437**
SHAREHOLDERS' EQUITY		
Capital Stock		
Class A common, stated value $.0292 per share; authorized 74,996,930 shares; 67,492,800 shares issued; 63,133,176 and 64,089,906 shares outstanding, respectively	1,969	1,969
Class B common, convertible at a rate of 2,400 Class A shares for one Class B share, stated value $70 per share; 2,878 shares authorized, issued and outstanding	201	201
Additional paid-in capital	7,830	7,830
Accumulated other comprehensive income	61,505	66,402
Retained earnings	1,313,473	1,189,628
Total contributed capital and retained earnings	1,384,978	1,266,030
Treasury stock, at cost, 4,359,624 and 3,402,894 shares in 2004 and 2003, respectively	(146,426)	(101,860)
Total shareholders' equity	**1,238,552**	**1,164,170**
Total liabilities and shareholders' equity	**$ 2,981,997**	**$ 2,754,607**

See Notes to Consolidated Financial Statements

ERIE INDEMNITY COMPANY

CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

	Three Months Ended September 30		Nine Months Ended September 30	
	2004	2003	2004	2003
	(Amounts in thousands, except per share data)			
OPERATING REVENUE				
Management fee revenue — net	$ 232,837	$ 219,001	$ 684,539	$ 634,785
Premiums earned	52,862	48,358	154,576	140,759
Service agreement revenue	5,384	6,667	16,207	20,014
Total operating revenue	**291,083**	**274,026**	**855,322**	**795,558**
OPERATING EXPENSES				
Cost of management operations	177,659	160,416	521,599	467,030
Losses and loss expenses incurred	34,602	38,723	112,642	115,587
Policy acquisition and other underwriting expenses	12,153	11,168	35,906	32,302
Total operating expenses	**224,414**	**210,307**	**670,147**	**614,919**
INVESTMENT INCOME — UNAFFILIATED				
Investment income, net of expenses	14,795	14,477	45,048	43,015
Net realized gains on investments	859	1,846	6,743	5,815
Equity in earnings (losses) of limited partnerships	3,845	1,311	5,765	(1,435)
Total investment income — unaffiliated	**19,499**	**17,634**	**57,556**	**47,395**
Income before income taxes and equity in earnings of Erie Family Life Insurance Co.	86,168	81,353	242,731	228,034
Provision for income taxes	29,141	27,124	81,865	76,107
Equity in earnings of Erie Family Life Insurance Company, net of tax	1,539	2,008	4,227	4,668
Net income	**$ 58,566**	**$ 56,237**	**$ 165,093**	**$ 156,595**
Net income per share — basic	**$ 0.83**	**$ 0.79**	**$ 2.34**	**$ 2.21**
Net income per share — diluted	**$ 0.83**	**$ 0.79**	**$ 2.34**	**$ 2.20**
Weighted average shares outstanding	**70,186**	**70,997**	**70,584**	**70,997**
Dividends declared per share:				
Class A	**$ 0.215**	**$ 0.19**	**$ 0.645**	**$ 0.57**
Class B	**32.25**	**28.50**	**96.75**	**85.50**

See Notes to Consolidated Financial Statements

ERIE INDEMNITY COMPANY

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

	Three Months Ended September 30		Nine Months Ended September 30	
	2004	2003	2004	2003
	(Dollars in thousands)			
Net Income	**$ 58,566**	**$ 56,237**	**$ 165,093**	**$ 156,595**
Unrealized gains (losses) on securities:				
Unrealized holding gains (losses) arising during period	24,125	(13,867)	(791)	48,481
Less: Gains included in net income	(859)	(1,846)	(6,743)	(5,815)
Net unrealized holding gains (losses) arising during period	23,266	(15,713)	(7,534)	42,666
Income tax (expense) benefit related to unrealized gains (losses)	(8,143)	5,500	2,637	(14,933)
Net appreciation (depreciation) of investments	15,123	(10,213)	(4,897)	27,733
Comprehensive income	$ **73,689**	$ **46,024**	$ **160,196**	$ **184,328**

See Notes to Consolidated Financial Statements

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ERIE INDEMNITY COMPANY

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Nine Months Ended September 30	
	2004	2003
	(Dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Management fee received	$ 657,176	$ 596,368
Service agreement fee received	16,207	20,014
Premiums collected	150,398	149,536
Net investment income received	45,876	44,607
Dividends received from Erie Family Life	1,349	1,288
Salaries and wages paid	(76,144)	(81,693)
Commissions paid to agents	(383,023)	(342,888)
General operating expenses paid	(51,986)	(50,726)
Losses and loss adjustment expenses paid	(98,966)	(98,055)
Underwriting and acquisition costs paid	(9,654)	(11,058)
Income taxes paid	(73,001)	(61,404)
Net cash provided by operating activities	**178,232**	**165,989**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investments:		
Fixed maturities	(275,490)	(391,390)
Equity securities	(23,937)	(29,780)
Limited partnership investments	(24,047)	(26,433)
Sales/maturities of investments:		
Fixed maturity sales	83,145	149,915
Fixed maturity calls/maturities	86,994	110,872
Equity securities	29,413	44,938
Limited partnership distributions	25,078	16,575
(Decrease) increase in collateral from securities lending	(1,449)	18,769
Purchase of property and equipment	(1,887)	(2,083)
Collections (net of distributions) on agent loans	1,943	780
Net cash used in investing activities	**(100,237)**	**(107,837)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Dividends paid to shareholders	(41,454)	(36,762)
Purchase of treasury stock	(44,566)	0
Issuance of note receivable to Erie Family Life Insurance Company	0	(25,000)
Cash used in financing activities	**(86,020)**	**(61,762)**
Net decrease in cash and cash equivalents	(8,025)	(3,610)
Cash and cash equivalents at beginning of period	87,192	85,712
Cash and cash equivalents at end of period	**$ 79,167**	**$ 82,102**

See Notes to Consolidated Financial Statements

ERIE INDEMNITY COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
(All dollar amounts are in thousands except per share data)

NOTE 1 — BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements, which include the accounts of Erie Indemnity Company and its wholly owned property/casualty insurance subsidiaries, Erie Insurance Company (EIC), Erie Insurance Company of New York (EINY) and Erie Insurance Property & Casualty Company (EIPC), have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles (GAAP) for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the nine-month period ended September 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Form 10-K for the year ended December 31, 2003 as filed with the Securities and Exchange Commission on March 8, 2004.

NOTE 2 — RECLASSIFICATONS

Certain amounts previously reported in the 2003 financial statements have been reclassified to conform to the current period's presentation. Such reclassifications did not impact earnings.

NOTE 3 — EARNINGS PER SHARE

Basic earnings per share is based on the weighted average number of Class A shares outstanding (63,133,176 and 64,089,906 at September 30, 2004 and 2003, respectively), giving effect to the conversion of the weighted average number of Class B shares outstanding (2,878 in 2004 and 2003) at a rate of 2,400 Class A shares for one Class B share. Weighted average equivalent shares outstanding totaled 70,186,222 for the quarter ended September 30, 2004 and 70,997,106 for the same period one year ago. For the nine months ended September 30, 2004 weighted average equivalent shares outstanding were 70,584,070 compared to 70,997,106 for the nine months ended September 30, 2003.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 3 — EARNINGS PER SHARE (Continued)

The following table reconciles the numerators and denominators of the basic and diluted per-share computations.

	Three months ended September 30 (Shares in thousands)			Nine months ended September 30 (Shares in thousands)		
	Net Income (Numerator)	Shares Outstanding (Denominator)	Per-Share Earnings	Net Income (Numerator)	Shares Outstanding (Denominator)	Per-Share Earnings
2004						
Basic earnings per share	$ 58,566	70,186	$ 0.83	$ 165,093	70,584	$ 2.34
Restricted stock awards not yet vested		73			73	
Diluted earnings per share	$ 58,566	70,259	$ 0.83	$ 165,093	70,657	$ 2.34
2003						
Basic earnings per share	$ 56,237	70,997	$ 0.79	$ 156,595	$ 70,997	2.21
Restricted stock awards not yet vested		104			104	
Diluted earnings per share	$ 56,237	71,101	$ 0.79	$ 156,595	71,101	$ 2.20

Included in the restricted stock awards not yet vested are awards of 68,176 and 97,061 for the third quarter and nine months ended September 30, 2004 and 2003, respectively, related to the long-term incentive plan for executive and senior management. Awards not yet vested related to the outside directors stock compensation plan were 4,829 and 6,523 for the third quarters and nine months ended September 30, 2004 and 2003, respectively.

NOTE 4 — INVESTMENTS

Fixed maturities and marketable equity securities are classified as “available-for-sale.” Equity securities consist primarily of common and nonredeemable preferred stocks while fixed maturities consist of bonds, notes and redeemable preferred stock. Available-for-sale securities are stated at fair value, with the unrealized gains and losses, net of deferred tax, reflected in shareholders’ equity in accumulated other comprehensive income. When a decline in the value of an investment is considered to be other-than-temporary by management, the investment is written down to estimated realizable value. Investment impairments are evaluated on an individual security position basis. Adjustments to the carrying value of marketable equity securities and fixed maturities that are considered impaired are recorded as realized losses in the Consolidated Statements of Operations. Adjustments to the carrying value of limited partnerships that are considered impaired are recorded as a component of equity in losses or earnings of limited partnerships in the Consolidated Statements of Operations.

The Company had loaned securities, included as part of its invested assets, with a market value of $32,531 and $33,986 at September 30, 2004 and December 31, 2003, respectively. Securities lending collateral is recorded by the Company as a liability. The proceeds from the collateral are invested in cash and short-term investments and are reported on the Consolidated Statements of Financial Position as cash and cash equivalents. The Company shares a portion of the interest on these short-term investments with the lending agent. The Company has incurred no losses on the loan program since the program’s inception.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 4 — INVESTMENTS (Continued)

The following is a summary of fixed maturities and equity securities:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
September 30, 2004				
Fixed maturities:				
U.S. treasuries & government agencies	$ 15,813	$ 469	$ 55	$ 16,227
States & political subdivisions	81,945	2,833	146	84,632
Special revenue	127,277	3,802	97	130,982
Public utilities	60,951	4,660	52	65,559
U.S. industrial & miscellaneous	424,947	16,283	1,104	440,126
Mortgage-backed securities	52,111	915	332	52,694
Asset-backed securities	22,058	71	223	21,906
Foreign	127,054	8,929	615	135,368
Total bonds	912,156	37,962	2,624	947,494
Redeemable preferred stock	32,429	2,139	73	34,495
Total fixed maturities	944,585	40,101	2,697	981,989
Equity securities:				
Common stock:				
U.S. banks, trusts & insurance companies	1,020	2,866	0	3,886
U.S. industrial & miscellaneous	13,838	19,924	0	33,762
Foreign	1,076	631	0	1,707
Nonredeemable preferred stock:				
Public utilities	23,122	1,770	44	24,848
U.S. banks, trusts & insurance companies	40,346	3,069	429	42,986
U.S. industrial & miscellaneous	56,276	3,598	480	59,394
Foreign	12,232	1,595	30	13,797
Total equity securities	147,910	33,453	983	180,380
Total fixed maturities and equity securities	$ 1,092,495	$ 73,554	$ 3,680	$ 1,162,369

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 4 — INVESTMENTS (Continued)

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2003				
Fixed maturities:				
U.S. treasuries & government agencies	$ 11,912	$ 337	$ 60	$ 12,189
States & political subdivisions	69,330	2,986	44	72,272
Special revenue	95,418	4,120	67	99,471
Public utilities	62,966	4,822	22	67,766
U.S. industrial & miscellaneous	372,705	21,269	886	393,088
Mortgage-backed securities	66,385	909	391	66,903
Asset-backed securities	16,754	26	96	16,684
Foreign	106,313	9,903	536	115,680
Total bonds	801,783	44,372	2,102	844,053
Redeemable preferred stock	32,866	2,480	38	35,308
Total fixed maturities	834,649	46,852	2,140	879,361
Equity securities:				
Common stock:				
U.S. banks, trusts & insurance companies	1,020	2,980	0	4,000
U.S. industrial & miscellaneous	13,843	20,921	0	34,764
Foreign	1,077	610	0	1,687
Nonredeemable preferred stock:				
Public utilities	29,767	2,475	20	32,222
U.S. banks, trusts & insurance companies	41,882	4,674	50	46,506
U.S. industrial & miscellaneous	52,517	4,543	392	56,668
Foreign	12,232	1,356	32	13,556
Total equity securities	152,338	37,559	494	189,403
Total fixed maturities and equity securities	$ 986,987	$ 84,411	$ 2,634	$ 1,068,764

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 4 — INVESTMENTS (Continued)

Fixed maturity and equity securities in a gross unrealized loss position at September 30, 2004, are as follows. Data is provided by length of time securities were in a gross unrealized loss position.

	Amortized Cost	Estimated Fair Value	Gross Unrealized Losses	Number of Holdings
September 30, 2004				
Six months or less	$ 187,770	$ 185,345	$ 2,425	88
Six to twelve months	22,649	21,843	806	9
Twelve to eighteen months	21,106	20,687	419	11
Greater than eighteen months	3,395	3,365	30	2
	$ 234,920	$ 231,240	$ 3,680	110

No investments in an unrealized loss position at September 30, 2004, had experienced a decline in market value that was considered by management to be significant and other-than-temporary. There were no market conditions, industry characteristics or fundamental operating results of a specific issuer that suggested other-than-temporary impairment of any of the investments held at September 30, 2004.

The components of net realized gains on investments as reported in the Consolidated Statements of Operations are included below. There were no impairment charges on fixed maturities or equity securities in the third quarter of 2004 or 2003. There were no impairment charges on fixed maturities or equity securities in the first nine months of 2004. In the first nine months of 2003, impairment charges on fixed maturities and equity securities totaled $6,007.

	Three Months Ended September 30		Nine Months Ended September 30	
	2004	2003	2004	2003
Fixed maturities:				
Gross realized gains	$ 933	$ 2,091	$ 5,803	$ 11,237
Gross realized losses	(63)	(119)	(89)	(3,541)
Net realized gains	870	1,972	5,714	7,696
Equity securities:				
Gross realized gains	480	285	1,912	3,278
Gross realized losses	(491)	(411)	(883)	(5,159)
Net realized (losses) gains	(11)	(126)	1,029	(1,881)
Net realized gains on investments	$ 859	$ 1,846	$ 6,743	$ 5,815

Limited partnerships include U.S. and foreign private equity, real estate and mezzanine debt investments. The private equity limited partnerships invest in small- to medium-sized companies. Limited partnerships are recorded using the equity method. Unrealized gains and losses on limited partnerships are reflected in shareholders’ equity in accumulated other comprehensive income, net of deferred taxes. The Company has not guaranteed any of the partnership liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 4 — INVESTMENTS (Continued)

Limited partnerships that have declined in value below cost and for which the decline is considered to be other-than-temporary by management are written down to realizable value. These impairments are made directly on an individual limited partnership basis and are included as a component of equity in losses or earnings of limited partnerships in the Consolidated Statements of Operations. There were no impairment charges on limited partnerships in the third quarter of 2004. Impairment charges totaling $594 were recorded in the third quarter of 2003, related to private equity limited partnerships. For the first nine months of 2004 and 2003, impairment charges totaled $133 and $2,320, respectively. The components of equity in earnings (losses) of limited partnerships as reported in the Consolidated Statements of Operations are included below.

	Three Months Ended September 30		Nine Months Ended September 30	
	2004	2003	2004	2003
Private equity	$ 3,252	$ (333)	$ 2,597	$ (3,846)
Real estate	296	1,374	1,960	1,937
Mezzanine debt	297	270	1,208	474
Total equity in earnings (losses) of limited partnerships	$ 3,845	$ 1,311	$ 5,765	$ (1,435)

NOTE 5 — SUMMARIZED FINANCIAL STATEMENT INFORMATION OF AFFILIATE

The Company owns 21.6% of Erie Family Life Insurance Company's (EFL) outstanding common shares and accounts for this investment using the equity method of accounting. EFL is a Pennsylvania-domiciled life insurance company operating in 10 states and the District of Columbia.

The following represents unaudited condensed financial statement information for EFL on a GAAP basis:

	Three Months Ended September 30		Nine Months Ended September 30	
	2004	2003	2004	2003
Revenues:	$ 34,778	$ 39,096	$ 111,716	$ 110,001
Benefits and expenses	27,161	24,279	73,776	75,160
Income before income taxes	7,617	14,817	37,940	34,841
Income taxes	2,618	5,140	13,179	12,088
Net income	$ 4,999	$ 9,677	$ 24,761	$ 22,753
Comprehensive income (loss)	$ 25,454	$ (4,379)	$ 19,317	$ 41,450
Dividends paid to shareholders	$ 2,079	$ 1,985	$ 6,143	$ 5,954

	As of	
	September 30 2004	December 31 2003
Total assets	$ 1,685,902	$ 1,629,563
Net unrealized appreciation on investment securities, net of deferred taxes	$ 39,158	$ 44,603
Total shareholders' equity	$ 266,564	$ 255,563

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 6 — BENEFIT PLANS

The Company's pension plans consist of: (1) a noncontributory-defined benefit pension plan covering substantially all employees of the Company, (2) an unfunded supplemental employee retirement plan for its executive management and division officers and (3) an unfunded pension plan (discontinued as of April 1997) for certain of its outside directors. All liabilities for the plans described in this note are presented in total for all employees of the Erie Insurance Group, before allocations to related entities.

Components of Net Periodic Benefit Cost

	Pension Benefits		Postretirement Benefits	
	Three months ended September 30		Three months ended September 30	
	2004	2003	2004	2003
Service cost	$ 3,309	$ 2,511	$ 242	$ 178
Interest cost	3,237	2,774	177	149
Expected return on plan assets	(4,248)	(4,138)	0	0
Amortization of prior service cost	225	221	(13)	(12)
Amortization of net loss	801	203	38	14
Unrecognized initial net asset	0	(58)	0	0
Net periodic benefit cost	$ 3,324	$ 1,513	$ 444	$ 329

	Pension Benefits		Postretirement Benefits	
	Nine months ended September 30		Nine months ended September 30	
	2004	2003	2004	2003
Service cost	$ 9,927	$ 7,534	$ 726	$ 536
Interest cost	9,712	8,322	531	446
Expected return on plan assets	(12,747)	(12,415)	0	0
Amortization of prior service cost	676	608	(40)	(37)
Amortization of net loss	2,404	664	116	40
Unrecognized initial net asset	0	(175)	0	0
Net periodic benefit cost	$ 9,972	$ 4,538	$ 1,333	$ 985

A portion of the net periodic benefit cost is borne by the Erie Insurance Exchange (Exchange) and Erie Family Life Insurance Company (EFL). The Company was reimbursed approximately 54% and 55% from the Exchange and EFL during the first nine months of 2004 and 2003, respectively.

NOTE 7 — NOTES RECEIVABLE FROM ERIE FAMILY LIFE INSURANCE COMPANY

The Company is due $40,000 from EFL in the form of two surplus notes. The notes may be repaid only out of unassigned surplus of EFL and repayment is subject to prior approval by the Pennsylvania Insurance Commissioner. The first note, in the amount of $15,000, bears an annual interest rate of 6.45% and will be payable on demand on or after December 31, 2005. Interest is scheduled to be paid semi-annually. EFL accrued interest of $245 in the third quarters of 2004 and 2003 which is payable to the Company.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 7 — NOTES RECEIVABLE FROM ERIE FAMILY LIFE INSURANCE COMPANY (Continued)

The second note, in the amount of $25,000, bears an annual interest rate of 6.70%. This note, which was issued in August 2003, was issued to further strengthen the surplus of EFL and to support its continued sales growth. The note will be payable on demand on or after December 31, 2018. Interest is scheduled to be paid semi-annually. EFL accrued interest of $423 and $166 to the Company in the third quarters of 2004 and 2003, respectively.

NOTE 8 — STATUTORY INFORMATION

Cash and securities with carrying values of $3,682 and $3,431 were deposited by the Company’s property and casualty insurance subsidiaries with regulatory authorities under statutory requirements as of September 30, 2004 and December 31, 2003, respectively.

NOTE 9 — SUPPLEMENTARY DATA ON CASH FLOWS

A reconciliation of net income to net cash provided by operating activities as presented in the Consolidated Statements of Cash Flows is as follows:

	Nine Months Ended September 30	
	2004	2003
	(Dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	**$ 165,093**	**$ 156,595**
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	27,986	28,812
Deferred income tax expense	2,753	538
Equity in (earnings) losses of limited partnerships	(5,765)	1,435
Net realized gains on investments	(6,743)	(5,815)
Net amortization of bond premium	1,212	778
Undistributed earnings of Erie Family Life Insurance Company	(3,196)	(3,731)
Deferred compensation	1,516	5,662
Increase in receivables and reinsurance recoverable from the Exchange	(123,586)	(193,911)
Increase in prepaid expenses and other assets	(33,443)	(32,672)
Increase in accounts payable and accrued expenses	48,305	30,216
Increase in loss reserves	60,394	107,553
Increase in unearned premiums	43,706	70,529
Net cash provided by operating activities	**$ 178,232**	**$ 165,989**

NOTE 10 — COMMITMENTS

The Company has contractual commitments to invest up to $98,376 additional funds in limited partnership investments at September 30, 2004. These commitments will be funded as required by the partnerships’ agreements through 2010. At September 30, 2004, the total commitment to fund limited partnerships that invest in private equity securities is $49,978, real estate activities is $31,196 and fixed income securities is $17,202. The Company expects to have sufficient cash flows from operations to meet these partnership commitments.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 10 — COMMITMENTS (Continued)

During 2001 and 2002, the Company entered into contracts with various external vendors to provide services related to the eCommerce program. The total outstanding commitment for these contracts at September 30, 2004, was $2,250, of which approximately $1,382 will be reimbursed to the Company by the Erie Insurance Exchange (Exchange). The majority of these committed services are expected to be performed in 2004.

The Company is involved in litigation arising in the ordinary course of business. In the opinion of management, the effects, if any, of such litigation are not expected to be material to the Company's consolidated financial condition, results of operations or cash flows.

NOTE 11 — VARIABLE INTEREST ENTITY

The Exchange is a reciprocal insurance company domiciled in Pennsylvania for which the Company serves as attorney-in-fact. The Company has a significant interest in the financial condition of the Exchange because net management fee revenues, which accounted for 75.0% of the Company's revenues in the third quarter of 2004, are based on the direct written premiums of the Exchange and the other members of the Property and Casualty Group. Additionally, the Company participates in the underwriting results of the Exchange through the pooling arrangement in which the Company's insurance subsidiaries have a 5.5% participation. Finally, a concentration of credit risk exists related to the unsecured receivables due from the Exchange for certain fees, costs and reimbursements.

While the Company has a variable interest in the Exchange due to the attorney-in-fact relationship between the Company and Exchange, the Company does not qualify as the primary beneficiary under Financial Accounting Standards Board Interpretation 46, "Consolidation of Variable Interest Entities." Therefore, the financial position and results of operations of the Exchange are not required to be consolidated with the financial statements of the Company.

NOTE 12 — SEGMENT INFORMATION

The Company operates its business as three reportable segments — management operations, insurance underwriting operations and investment operations. Accounting policies for segments are the same as those described in the summary of significant accounting policies Note 3, of the Company's Annual Report on Form 10-K for the year ended December 31, 2003 as filed with the Securities and Exchange Commission on March 8, 2004, with the exception of the management fee revenues received from the property/casualty insurance subsidiaries. These revenues are not eliminated in the segment detail that follows as management bases its decisions on the segment presentation. Assets are not allocated to the segments and are reviewed in total by management for purposes of decision making. No single customer or agent provides 10% or more of revenues for the Property and Casualty Group. The Property and Casualty Group includes the Exchange and its property and casualty insurance subsidiary, Flagship City Insurance Company, and the Company's three property and casualty insurance subsidiaries, EIC, EINY and EIPC.

The Company's principal operations consist of serving as attorney-in-fact for the Exchange, which constitute its management operations. The Company operates in this capacity solely for the Exchange. The Company's insurance underwriting operations arise through direct business of its property/casualty insurance subsidiaries and by virtue of the pooling agreement between its subsidiaries and the Exchange, which includes assumed reinsurance from non-affiliated domestic and

NOTE 12 — SEGMENT INFORMATION (Continued)

foreign sources. (The Exchange exited the voluntary assumed reinsurance business effective December 31, 2003.) Insurance underwriting operations reflect the results of reinsurance ceded under an excess-of-loss agreement with the Exchange.

Insurance provided in the insurance underwriting operations consists of personal and commercial lines and is sold by independent agents. Personal lines are marketed to individuals and commercial lines are marketed to small and medium-sized businesses. The performance of the personal and commercial lines is evaluated based upon the underwriting results as determined under statutory accounting practices (SAP) for the total pooled business of the Property and Casualty Group.

Company management evaluates profitability of its management operations segment principally on the gross margin from management operations, while profitability of the insurance underwriting operations segment is evaluated principally based on the combined ratio. Investment operations performance is evaluated by Company management based on appreciation of assets, rate of return and overall return. These items are analyzed in the Management's Discussion and Analysis that follows on page 21.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 12 — SEGMENT INFORMATION (Continued)

Summarized financial information for the Company's operating segments is presented below:

	Three Months Ended September 30		Nine Months Ended September 30	
	2004	2003	2004	2003
Management Operations				
Operating revenue				
Management fee revenue	$ 246,388	$ 231,747	$ 724,379	$ 671,730
Service agreement revenue	5,384	6,667	16,207	20,014
Total operating revenue	251,772	238,414	740,586	691,744
Cost of management operations	187,999	169,752	551,957	494,212
Income before taxes	63,773	68,662	188,629	197,532
Net income from management operations	$ 42,207	$ 45,769	$ 125,011	$ 131,605
Insurance Underwriting Operations				
Operating revenue				
Premiums earned:				
Commercial lines	$ 15,895	$ 14,159	$ 46,635	$ 41,662
Personal lines	38,205	34,068	110,559	97,088
Reinsurance — nonaffiliates	(396)	1,281	(94)	4,309
Reinsurance — affiliates	(842)	(1,150)	(2,524)	(2,300)
Total premiums earned	52,862	48,358	154,576	140,759
Operating expenses				
Losses and expenses:				
Commercial lines	13,648	17,847	43,683	49,467
Personal lines	35,117	39,751	106,712	109,815
Reinsurance — nonaffiliates	43	2,777	1,548	5,566
Reinsurance — affiliates	1,159	(7,074)	6,088	(7,196)
Total losses and expenses	49,967	53,301	158,031	157,652
Income (loss) before taxes	2,895	(4,943)	(3,455)	(16,893)
Net income (loss) from insurance underwriting operations	$ 1,916	$ (3,295)	$ (2,289)	$ (11,255)
Investment Operations				
Investment income, net of expenses	$ 14,795	$ 14,477	$ 45,048	$ 43,015
Net realized gains on investments	859	1,846	6,743	5,815
Equity in earnings (losses) of limited partnerships	3,845	1,311	5,765	(1,435)
Income before income taxes and before equity in earnings of EFL	19,499	17,634	57,556	47,395
Net income from investment operations	$ 12,904	$ 11,755	$ 38,144	$ 31,577
Equity in earnings of EFL, net of tax	$ 1,539	$ 2,008	$ 4,227	$ 4,668

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 12 — SEGMENT INFORMATION (Continued)

Reconciliation of reportable segment revenues and operating expenses to the Consolidated Statements of Operations:

	Three months ended September 30		Nine months ended September 30	
	2004	2003	2004	2003
Segment revenues	$ 304,634	$ 286,772	$ 895,163	$ 832,503
Elimination of intersegment management fee revenues	(13,551)	(12,746)	(39,841)	(36,945)
Total operating revenues	$ 291,083	$ 274,026	$ 855,322	$ 795,558
Segment operating expenses	$ 237,965	$ 223,053	$ 709,988	$ 651,864
Elimination of intersegment management fee expense	(13,551)	(12,746)	(39,841)	(36,945)
Total operating expenses	$ 224,414	$ 210,307	$ 670,147	$ 614,919

The intersegment revenues and expenses that are eliminated in the Consolidated Statements of Operations relate to the Company's property/casualty insurance subsidiaries 5.5% share of the intersegment management fees paid to the Company.

The following table presents the management fee revenue by line of business before elimination of the intersegment management fee revenue.

	Three Months Ended September 30		%	Nine Months Ended September 30		%
	2004	2003	Change	2004	2003	Change
Private passenger auto	$ 126,724	$ 121,065	4.7%	$ 362,672	$ 343,820	5.5%
Commercial auto	18,587	18,008	3.2	59,956	57,115	5.0
Homeowner	49,962	42,962	16.3	132,615	110,491	20.0
Commercial multi-peril	25,192	23,127	8.9	80,302	74,573	7.7
Workers' compensation	20,491	18,716	9.5	64,319	61,344	4.8
All other lines of business	10,032	9,169	9.4	30,215	27,087	11.5
Total	250,988	233,047	7.7%	730,079	674,430	8.3%
Allowance for management fee returned on cancelled policies	4,600	1,300		5,700	2,700	
Management fee revenue	$ 246,388	$ 231,747	6.3%	$ 724,379	$ 671,730	7.8%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 12 — SEGMENT INFORMATION (Continued)

The growth rate of policies in force and policy retention trends (the percentage of policyholders eligible for renewals who have renewed their policies measured on a twelve-month rolling basis) directly impact the Company's management operations and property and casualty insurance operating segments. Below is a summary of each by line of business for the Property and Casualty Group's insurance business.

Growth rates of policies in force for Property and Casualty Group insurance operations:

Date	Private passenger auto	12-mth. growth rate	Homeowners	12-mth. growth rate	All other personal lines of business	12-mth. growth rate	Total Personal Lines	12-mth. growth rate
06/30/2003	1,650,225	9.1%	1,293,575	12.8%	264,423	14.0%	3,208,223	11.0%
09/30/2003	1,666,285	7.2%	1,316,775	10.6%	269,640	12.2%	3,252,700	9.0%
12/31/2003	1,672,621	5.1%	1,327,842	7.9%	272,547	9.2%	3,273,010	6.6%
03/31/2004	1,678,496	3.4%	1,335,763	5.8%	275,970	7.2%	3,290,229	4.7%
06/30/2004	1,686,524	2.2%	1,347,409	4.2%	278,547	5.3%	3,312,480	3.3%
09/30/2004	1,682,561	1.0%	1,350,899	2.6%	278,707	3.4%	3,312,167	1.9%

Date	CML* auto	12-mth. growth rate	CML* multi-peril	12-mth. growth rate	Workers' comp.	12-mth. growth rate	All other CML* lines of business	12-mth. growth rate	Total CML* Lines	12-mth. growth rate
06/30/2003	112,911	10.2%	201,614	12.2%	61,932	11.4%	83,826	10.5%	460,283	11.3%
09/30/2003	114,339	8.5%	205,127	10.5%	62,396	8.8%	85,789	9.8%	467,651	9.7%
12/31/2003	115,171	6.6%	206,533	8.3%	62,282	5.7%	86,409	8.3%	470,395	7.5%
03/31/2004	115,760	5.3%	206,937	6.2%	61,378	2.1%	86,344	6.1%	470,419	5.4%
06/30/2004	117,060	3.7%	209,795	4.1%	60,735	(1.9%)	87,172	4.0%	474,762	3.1%
09/30/2004	117,090	2.4%	210,012	2.4%	59,863	(4.1%)	87,921	2.5%	474,886	1.5%

Date	Total All Lines	12-mth. growth rate
06/30/2003	3,668,506	11.0%
09/30/2003	3,720,351	9.0%
12/31/2003	3,743,405	6.7%
03/31/2004	3,760,648	4.7%
06/30/2004	3,787,242	3.2%
09/30/2004	3,787,053	1.8%

Policy retention trends for Property and Casualty Group insurance operations:

Date	Private passenger auto	CML* auto	Homeowners	CML* multi-peril	Workers' comp.	All other lines of business	Total
06/30/2003	92.2%	91.1%	90.5%	88.4%	89.4%	88.4%	91.0%
09/30/2003	91.9	90.4	90.1	88.0	88.9	88.4	90.6
12/31/2003	91.6	89.8	89.5	87.5	88.1	88.2	90.2
03/31/2004	91.2	89.7	89.0	87.6	88.1	87.5	89.8
06/30/2004	90.7	89.0	88.4	86.7	86.7	86.8	89.2
09/30/2004	90.3	88.5	87.9	86.0	86.2	86.0	88.7

*CML = Commercial

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following information should be read in conjunction with the historical financial information and the notes thereto included in Item 1 of this Quarterly Report on Form 10-Q and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Annual Report on Form 10-K for the year ended December 31, 2003 as filed with the Securities and Exchange Commission on March 8, 2004. Preceding the discussion of financial results is an introduction discussing the relationships between the member companies of the Erie Insurance Group. The following discussion of financial results focuses heavily on the Erie Indemnity Company's (the Company) three primary segments: management operations, insurance underwriting operations and investment operations consistent with the presentation in Note 12 in the Notes to Consolidated Financial Statements. That presentation, which management uses internally to monitor and evaluate results, is an alternative presentation of the Company's Consolidated Statements of Operations.

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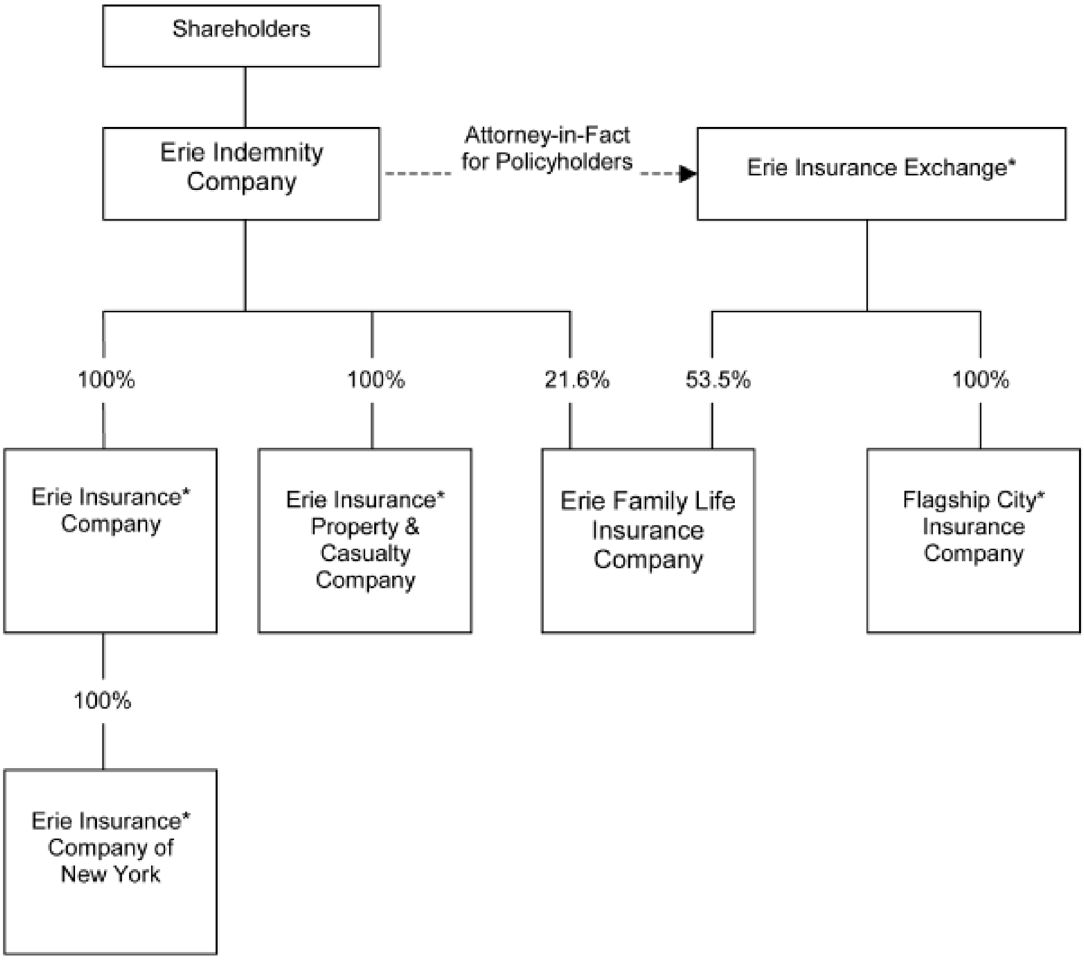
NATURE OF ORGANIZATION

The following organizational chart depicts the organization of the various entities of the Erie Insurance Group:

Erie Insurance Group Organizational Chart



* Denotes a member of the Property and Casualty Group

Erie Indemnity Company (the Company) has served since 1925 as the attorney-in-fact for the policyholders of the Erie Insurance Exchange (Exchange). The Company is a public registrant that operates predominantly as a provider of certain management services to the Exchange. The Company also owns subsidiaries that are property and casualty insurers. Each applicant for insurance to a reciprocal insurance exchange signs a subscriber's agreement, which contains a power-of-attorney appointing an attorney-in-fact. Under the Company's attorney-in-fact arrangement with subscribers to the Exchange, the Company is required to perform services relating to the sales, underwriting and issuance of policies on behalf of the Exchange. The Company also owns a 21.6% interest in Erie Family Life Insurance Company (EFL), a provider of life insurance products. The Exchange owns a 53.5% interest in EFL.

The Exchange and its property/casualty subsidiary, Flagship City Insurance Company, and the Company's three property/casualty subsidiaries, Erie Insurance Company (EIC), Erie Insurance Company of New York (EINY) and Erie Insurance Property & Casualty Company (EIPC), (collectively, the Property and Casualty Group) write personal and commercial lines property and casualty coverage exclusively through approximately 1,750 independent agencies comprising approximately 7,500 licensed independent agents and pool their underwriting results. The financial position or results of operations of the Exchange are not consolidated with those of the Company. The Company, together with the Property and Casualty Group and EFL, operate collectively as the Erie Insurance Group (the Group).

The financial information presented herein reflects the Company's management operations from serving as attorney-in-fact for the Exchange, its insurance underwriting results from its wholly-owned subsidiaries (EIC, EINY and EIPC) and the Company's investment operations.

Results of Operations

	Three Months Ended September 30		Nine Months Ended September 30	
(dollars in thousands, except per share)	**2004**	**2003**	**2004**	**2003**
	(unaudited)		**(unaudited)**	
Income from management operations	$ 63,773	$ 68,662	$ 188,629	$ 197,532
Underwriting income (loss)	2,895	(4,943)	(3,455)	(16,893)
Net revenue from investment operations	21,153	19,794	62,101	52,414
Income before income taxes	87,821	83,513	247,275	233,053
Net income	$ 58,566	$ 56,237	$ 165,093	$ 156,595
Net income per share	$ 0.83	$ 0.79	$ 2.34	$ 2.21

Consolidated net income for the third quarter of 2004 increased 4.1% to $58.6 million compared to $56.2 million during the same period in 2003. Income from management operations for the third quarter of 2004 decreased 7.1% from 2003. Management fee revenue was reduced by $4.6 million and $1.3 million in the third quarters of 2004 and 2003, respectively, due to an increase in the allowance on mid-term policy cancellations. The higher estimated allowance for mid-term cancellations was the result of an increase in mid-term policy cancellation experience for the most recent quarter. After being offset by the change in allowance for returned commissions on mid-term policy cancellations, the impact of the change in cancellation allowance was a reduction to net income of $.02 per share for the third quarter of 2004. Also contributing to the reduction in income from management operations was a reduction in the service fee revenue on voluntary assumed reinsurance as the Company continues to exit the assumed reinsurance business.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Insurance underwriting operations improved as a result of a comprehensive series of initiatives designed to improve property/casualty underwriting profitability. Revenue from investment operations increased 6.9% in the third quarter of 2004 compared to the same period in 2003. This increase is due to improved results in equity in earnings of limited partnerships.

Consolidated net income for the nine months ended September 30, 2004 increased 5.4% to $165.1 million compared to $156.6 million during the same period in 2003. Income from management operations decreased 4.5% during the first nine months of 2004 compared to the first nine months of 2003. The decrease for the year is the result of the lower management fee rate. The rate was 24% for 2003 compared to 23.5% for the first six months of 2004 and 24% for the third quarter of 2004. An increase in the allowance for management fees returned on mid term policy cancellations also caused a decrease in management fee revenue. Insurance underwriting operations losses decreased to $3.5 million from $16.9 million in the first nine months of 2004 and 2003, respectively, principally due to underwriting initiatives designed to improve insurance profitability. Revenue from investment operations increased 18.5% in the first nine months of 2004 compared to the same period in 2003, due to improved equity in earnings on limited partnerships and increased net investment income.

OVERVIEW OF OPERATING SEGMENTS

The following operating segments discussed are those of the Erie Indemnity Company: management operations, insurance underwriting operations and investment operations.

Management Operations

	Three Months Ended September 30		Nine Months Ended September 30	
(dollars in thousands)	**2004**	**2003**	**2004**	**2003**
	(unaudited)		(unaudited)	
Management fee revenue	$ 246,388	$ 231,747	$ 724,379	$ 671,730
Service agreement revenue	5,384	6,667	16,207	20,014
Total revenue from management operations	251,772	238,414	740,586	691,744
Cost of management operations	187,999	169,752	551,957	494,212
Income from management operations	$ 63,773	$ 68,662	$ 188,629	$ 197,532
Gross margin percentage	25.3%	28.8%	25.5%	28.6%

Management fee revenue rose 6.3% for the quarter ended September 30, 2004 compared to the quarter ended September 30, 2003. Management fees from the Exchange represented 75.0% and 75.1% of the Company's total revenues for the third quarter of 2004 and 2003, respectively. For the first nine months of 2004 and 2003, management fees from the Exchange represented 75.0% and 75.3%, respectively, of the Company's total revenues. The management fee rate was increased by the Company's Board of Directors to 24%, effective July 1, 2004, from 23.5% in the first half of 2004. The rate was set at 24% for all of 2003. The lower management fee rate in the first half of the year resulted in $10.2 million less in management fee revenue for the nine months ended September 30, 2004, or a reduction in net income of $.09 per share.

The direct and affiliated assumed premiums of the Exchange, on which the management fee revenue is based, grew 7.7% and 9.8% in the third quarter and first nine months of 2004, respectively. Premiums grew to $1.0 billion from $971.0 million in the third quarter of 2003 and to $3.1 billion for the first nine months of 2004 from $2.8 billion for the first nine months of 2003. Increases in average premium per policy, reflective of rate increases in various lines of business, and high policy retention rates were contributing factors in the growth of direct written premiums. The average premium per policy increased 8.2% to $1,042 for the twelve months ended September 30, 2004 from $964 for the twelve months ended September 30, 2003. The average premium per personal lines policy increased 9.3% while commercial lines average premiums increased 5.8% for the twelve months ended September 30, 2004. The private passenger auto average premium per policy increased 6.6% to $1,174 for the twelve months ended September 30, 2004 from $1,101 for the twelve months ended September 30, 2003.

These factors were offset by a slowdown in new policy sales in 2004. Premium and policy growth has been slower in 2004 relative to 2003 due to the Company's increased emphasis on controlling exposure growth and improving risk selection. Rate increases have also contributed to reduced new policy sales and to reduced policy retention. (See Insurance Underwriting Operations section.)

In August 2004, the Company implemented insurance scoring for underwriting purposes for its private passenger auto and homeowners lines of business in all operating states and territories, except Maryland, in response to changing competitive market conditions. The Company is currently developing a price segmentation model that incorporates insurance scoring, among other risk characteristics, to be deployed during the second quarter of 2005. The pricing model will provide several price tiers to accommodate various risks. This pricing strategy should contribute to an improved competitive position in the marketplace, enhancing agents' sales efforts.

Total new business premium written declined 17.4% to $103.6 million in the third quarter of 2004 from $125.4 million in the third quarter of 2003. Personal lines new business premiums written declined 14.7% to $74.6 million from $87.5 million for the third quarters of 2004 and 2003, respectively. Commercial lines new business premiums declined 23.4% to $29.0 million from $37.9 million for the third quarters of 2004 and 2003, respectively.

Year over year policy retention decreased to 88.7% at September 30, 2004, from 90.6% at September 30, 2003, for all lines of business combined (see Note 12, "Segment Information" which contains policies in force and policy retention trends by line of business.) The combination of new policies written and the decline in policy retention resulted in policies in force increasing 1.8% to 3.8 million at September 30, 2004, from 3.7 million at September 30, 2003.

Management fees are returned to the Exchange when policies are cancelled mid-term and unearned premiums are refunded. The Company records an estimated allowance for management fees returned on mid-term policy cancellations. Third quarter 2004 and 2003 revenues were reduced by $4.6 million and $1.3 million, respectively, due to changes in the allowance. The higher estimated allowance was the result of higher policy cancellation experience in the most recent quarter compared to the previous quarter. This increase in policy cancellations is reflected in the reduced year over year policy retention ratio, which decreased to 88.7% at September 30, 2004 from 89.2% at June 30, 2004. This increase in estimated policy cancellations was partially offset by a change in the allowance for returned commissions on mid-term policy cancellations of $2.3 million in the third quarter of 2004. (See also Note 12 "Segment Information" which details management fee revenue by line of business.) For the first nine months of 2004 and 2003 revenues were reduced $5.7 million and $2.7 million, respectively, by changes in the estimated allowance for management fees returned on mid-term policy cancellations.

Service agreement revenue decreased to $5.4 million for the third quarter of 2004, from $6.7 million for the same period in 2003. Included in service agreement revenue are service charges the Company collects from policyholders for providing multiple payment plans on policies written by the Property and Casualty Group. The service charge revenue for the third quarter of 2004 was $5.3 million compared to $5.0 million for the third quarter of 2003.

Also included in service agreement revenue is service income received from the Exchange as compensation for the management and administration of voluntary assumed reinsurance from non-affiliated insurers. As the Exchange's assumed reinsurance business runs off, the service agreement revenue received by the Company will continue to decrease. The minimal third quarter 2004 voluntary assumed premium revenues yielded revenues to the Company of approximately $43

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thousand. Service fee revenue from voluntary assumed reinsurance business for the third quarter of 2003 was $1.7 million. The non-affiliated voluntary assumed reinsurance premium written in the first nine months of 2004 was $12.4 million compared to $92.2 million in the same period in 2003.

The cost of management operations increased 10.7% for the third quarter of 2004 to $188.0 million from $169.8 million during the third quarter of 2003, primarily due to an increase in commission costs. For the nine months ended September 30, 2004 the cost of management operations grew by 11.7% to $552.0 million, compared to $494.2 million for the same period a year ago.

Commission costs totaled $140.2 million for the third quarter of 2004, a 12.0% increase over the $125.2 million reported in the third quarter of 2003. 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, accelerated commissions and Agency contingency awards as follows:

	Three months ended September 30			Nine months ended September 30		
(dollars in thousands)	**2004**	**2003**	**Percent Change**	**2004**	**2003**	**Percent Change**
Scheduled commissions	$ 120,828	$ 111,407	8.5%	$ 359,107	$ 322,670	11.3%
Accelerated commissions	5,586	7,342	(23.9)	17,908	22,038	(18.7)
Agency contingency awards	13,807	6,393	116.0	32,260	16,693	93.3
Total commissions	$ 140,221	$ 125,142	12.0%	$ 409,275	$ 361,400	13.2%

Scheduled commissions increased to $120.8 million for the quarter ended September 30, 2004 driven by the corresponding increase in premiums written by the Property and Casualty Group of 7.7%. Scheduled commission expense was reduced by $2.3 million and $.8 million in the third quarters of 2004 and 2003, respectively, related to the changes in the allowance for management fees returned on mid-term policy cancellations discussed previously. Accelerated commissions are offered to newly recruited agents in addition to normal commission schedules. Accelerated commissions were lower in the first nine months of 2004 as new agency appointments were curtailed for the latter part of 2003 in conjunction with the Company's emphasis on controlling exposure growth.

Agency contingency awards are based upon the 36-month underwriting profitability of the direct business written within the Property and Casualty Group by the Company's independent agency force. The estimate for the contingency award 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. Company estimates use projected underwriting data for the remainder of the current year in order to model the 36-month underwriting results by agency.

Changes were made to the agent contingency award program effective January 1, 2004. The changes to the program place more emphasis on underwriting profitability and quality growth in an agency's book of business. These changes and improved underwriting results in 2004 are expected to increase annual agency contingency award expense by approximately $20 million in 2004 as compared to 2003. Of the estimated increase, about $5.8 million is related to the one time special transition rules for the bonus.

The cost of management operations excluding commission costs, increased 7.1% for the three months ended September 30, 2004 to $47.8 million from $44.6 million recorded in the third quarter of

2003. Personnel and benefit related costs are the second largest component in cost of management operations. The Company’s personnel costs, principally salaries, totaled $29.4 million for the three months ended September 30, 2004, compared to $25.6 million for the same period in 2003, an increase of 14.7%. Contributing to the increase in salaries was a 4.3% increase in staffing levels as well as about 4% to 5% normal merit pay rate increases. Total employee benefit costs increased 12.4% in the third quarter of 2004 compared to the third quarter of 2003. Health plan benefit costs, which the Company self insures, rose 11.4% to $3.7 million in the third quarter of 2004 from $3.4 million in the third quarter of 2003 due to increased plan enrollment and increases in medical costs within the various plans offered by the Company. Retirement plan benefit costs increased 28.6% to $2.3 million in the third quarter of 2004 compared to $1.8 million in the third quarter of 2003 driven by the change in the discount rate assumption used to calculate the Statement of Financial Accounting Standard (FAS) 87, “Employers’ Accounting for Pensions,” pension expense decreasing from 6.75% in 2003 to 6.00% in 2004. FAS 87 pension costs were expected to increase by about $.8 million per quarter in 2004 over 2003 levels as a result of the discount rate change.

The gross margins from management operations were 25.3% and 28.8% in the third quarters of 2004 and 2003, respectively. Gross margins were 25.5% and 28.6% for the first nine months of 2004 and 2003, respectively. If the management fee rate had been 24% for all nine months of 2004, the gross margin would have been 26.5%

Insurance Underwriting Operations

	Three Months Ended September 30		Nine Months Ended September 30	
(dollars in thousands)	**2004**	**2003**	**2004**	**2003**
	(unaudited)		**(unaudited)**	
Premiums earned	$ 52,862	$ 48,358	$ 154,576	$ 140,759
Losses and loss adjustment expenses incurred	34,602	38,723	112,642	115,587
Policy acquisition and other underwriting expenses	15,365	14,578	45,389	42,065
Total losses and expenses	$ 49,967	$ 53,301	$ 158,031	$ 157,652
Underwriting loss	$ 2,895	$ (4,943)	$ (3,455)	$ (16,893)
GAAP combined ratio	94.5	110.2	102.2	112.0

The GAAP combined ratio represents the ratio of losses, loss adjustment, acquisition and other underwriting expenses incurred to premiums earned. The GAAP combined ratios of the Company are different than the results of the Property and Casualty Group due to differences between GAAP and statutory accounting bases and the effects of the excess-of-loss reinsurance agreement between the Company’s property/casualty subsidiaries and the Exchange. The statutory combined ratio for the Property and Casualty Group was 88.6 and 117.0 for the quarters ended September 30, 2004 and 2003 and 93.9 and 112.0 for the nine months ended September 30, 2004 and 2003, respectively. After being adjusted for the profit component paid to the Company, the adjusted statutory combined ratio was 83.0 and 110.7 for the quarters ended September 30, 2004 and 2003 and 88.3 and 105.7 for the nine months ended September 30, 2004 and 2003, respectively.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

The Company's insurance subsidiaries' share of the Property and Casualty Group's direct business generated underwriting income of $5.3 million in the third quarter of 2004 compared to underwriting losses of $9.4 million in the third quarter of 2003. The reported statutory combined ratio of the direct business of the Property and Casualty Group was 87.9 and 114.5 for the third quarters of 2004 and 2003, respectively. The reported statutory combined ratio of the direct business of the Property and Casualty Group was 92.9 and 111.4 for the nine months ended 2004 and 2003, respectively. The improvement in 2004 underwriting results on direct business reflects the impact of the underwriting profitability initiatives implemented in 2003 to help offset severity increases and control exposure growth. Additionally, the Property and Casualty Group has experienced positive development on losses of prior accident years through the first nine months of 2004 of approximately $120 million, compared to adverse development on losses of prior accident years experience of approximately $30 million in the same period a year ago. The impact on the Company of the positive development of prior accident years, net of changes in recoverables under the excess-of-loss reinsurance agreement, resulted in a $.5 million positive impact on year to date 2004 underwriting results.

Underwriting practices affect the number of new policyholders eligible for coverage with the Property and Casualty Group as well as the number eligible to renew and the terms of renewal. The acceptability of risks written by the Property and Casualty Group is an important element of underwriting profitability. Underwriting profitability is also affected by loss cost inflation and changes in the average loss per claim. Management's efforts to improve underwriting profitability include programs to control loss severity, exposure growth and improve risk selection, obtain additional premium on risks through rate increases, exit the assumed reinsurance business, relax the timeframe to begin operations in Minnesota and modify the agency contingency award program. Together, the Property and Casualty Group's pricing actions, underwriting and claims initiatives are designed to improve the overall underwriting results of the Property and Casualty Group.

These actions may continue to reduce the growth rate of the Property and Casualty Group's new and renewal premium and policy retention rates of the Property and Casualty Group. To the extent premium growth rate of the Property and Casualty Group direct written premiums is impacted by these actions, the growth in the Company's management fee revenue will be proportionally affected. Offsetting the potential negative impacts on growth and policy retention from more rigorous underwriting practices are the beneficial impacts to underwriting profitability. As the quality of business improves, underwriting profitability should continue to improve, and premium increases can be minimized, making the Property and Casualty Group's products more attractive to potential customers and more desirable to existing customers. In addition to impacting the management fee, improvements in underwriting profitability directly affect the Company by virtue of its 5.5% share of the intercompany pooling agreement.

In 2003 and 2004 substantial rate increases were filed by the Property and Casualty Group for certain lines of business in various states to offset the growing loss costs. The Property and Casualty Group writes one-year policies; therefore, rate increases take 24 months to be reflected fully in earned premiums as it takes 12 months to implement rate increases to all policyholders and 12 months more to earn fully the increased premiums. The Company continuously evaluates pricing actions and management estimates that those approved through September 30, 2004 could generate up to approximately $62 million in additional written premiums of the Property and Casualty Group in the remainder of 2004. Premium rate increases are not expected to continue at the level experienced in recent years as the Property and Casualty Group's underwriting results improve and the general market conditions change.

In August 2004, subject to regulatory approval in the various jurisdictions where the Company operates, the Property and Casualty Group implemented the use of insurance scoring in underwriting to maintain and enhance underwriting fundamentals and risk selection capabilities for private passenger auto and homeowners lines of business. Insurance scoring is being used during agents' underwriting, giving agents increased flexibility in applying the Company's underwriting guidelines. Insurance scoring is used by many property/casualty insurers to more accurately predict the likelihood of future claims. Insurance scores are being used by the Company to improve risk selection. The Company anticipates the cost of obtaining insurance scores on new applications for the next twelve months will be approximately $2.0 million.

Catastrophes are an inherent risk of the property/casualty insurance business and can have a material impact on the Company's insurance underwriting results. In addressing this risk, the Company employs what it believes are reasonable underwriting standards and monitors its exposure by geographic region. The Property and Casualty Group maintains catastrophe reinsurance coverage from unaffiliated insurers (see p. 42). During the third quarters of 2004 and 2003, the Company's share of catastrophe losses, as defined by the Property and Casualty Group, amounted to $2.0 million and $6.1 million, respectively and contributed 3.7 points and 12.5 points to the GAAP combined ratio respectively. The third quarter 2004 catastrophe losses included the effects of Hurricane Ivan on North Carolina, West Virginia, Virginia and Pennsylvania. The third quarter 2003 catastrophe losses included the effects of Hurricane Isabel on North Carolina, Virginia, Maryland, Pennsylvania and the District of Columbia. Catastrophe losses were $3.6 million and $9.2 million for the first nine months of 2004 and 2003, respectively.

The Company's property/casualty insurance subsidiaries' nonaffiliated reinsurance business includes its share of the Property and Casualty Group's voluntary and involuntary assumed reinsurance business and unaffiliated ceded business. The Exchange exited the voluntary assumed reinsurance business as of December 31, 2003 to allow the Property and Casualty Group to focus on its core business and lessen its underwriting exposure.

The Company's property/casualty insurance subsidiaries' also maintain an all lines excess-of-loss reinsurance agreement with the Exchange which limits their retained share of ultimate net losses in any applicable accident year. EIC's and EINY's aggregate excess-of-loss reinsurance agreement with the Exchange provides that once EIC and EINY have sustained ultimate net losses, excluding losses from terrorism, nuclear, biological and chemical events, in any applicable accident year that exceed an amount equal to 72.5% of EIC's and EINY's net premiums earned in that period, 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 EIC's and EINY's net premium earned. Losses equal to 5% of the ultimate net loss in excess of the retention under the contract are retained by EIC and EINY. The contract only requires reimbursement when claims are paid. The contract also requires that any unpaid loss recoverables will be commuted 60 months after an annual period expires. The premium for this coverage was 1.29% of EIC's and EINY's net premium earned in 2003 and was increased to 1.70% in 2004 to reflect current market conditions. The premium paid to the Exchange for this agreement in the third quarters of 2004 and 2003 was $1.6 million and $1.2 million, respectively. The portion of this premium recorded as expense was $.8 million in the third quarter of 2004 compared to $1.2 million in the third quarter of 2003. For the first nine months of 2004 and 2003, premium recorded as expense totaled $2.5 million and $2.3 million, respectively.

In the third quarter of 2004, the Company's property/casualty insurance subsidiaries recorded charges under the excess-of-loss reinsurance agreement with the Exchange of $1.2 million. This is the result of the positive loss development experience on prior accident years, especially the 2003 accident year.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

During the third quarter of 2003, the Company's property/casualty insurance subsidiaries recorded recoveries of $7.1 million under the excess-of-loss reinsurance agreement. Contributing to these recoveries were the impact of Hurricane Isabel on the 2003 accident year results and adverse development of prior accident years. As reimbursement occurs only when claims are paid, no cash payments have been made between the companies in 2004 or 2003 for recoveries. An increase in the recoverable in any given year reduces the Company's losses and loss adjustment expenses on the Consolidated Statements of Operations while a decrease in the recoverable results in an increase in the Company's losses and loss adjustments expenses.

The Company's policy acquisition and other underwriting expenses includes the property/casualty insurance subsidiaries' share of costs related to the eCommerce initiative. Costs associated with the eCommerce initiative totaled $.3 million and $.5 million for the third quarters of 2004 and 2003, respectively. These costs relate to application development expenses associated with the eCommerce initiative covered under an intercompany technology cost-sharing agreement ("Agreement"). The 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 Group in a manner consistent with the sharing of property/casualty underwriting results under the existing intercompany pooling agreement. Since the amounts are pooled within the Exchange and ceded to members of the pooling agreement at their participation levels, the Company, by way of its insurance subsidiaries, incurs a 5.5% share of these costs. These technology costs are included in the policy acquisition and other underwriting expenses in the Company's Consolidated Statements of Operations.

Investment Operations

	Three Months Ended September 30		Nine Months Ended September 30	
(dollars in thousands)	**2004**	**2003**	**2004**	**2003**
	(unaudited)		**(unaudited)**	
Net investment income	$ 14,795	$ 14,477	$ 45,048	$ 43,015
Net realized gains on investments	859	1,846	6,743	5,815
Equity in earnings of EFL	1,654	2,160	4,545	5,019
Equity in earnings (losses) of limited partnerships	3,845	1,311	5,765	(1,435)
Net revenue from investment operations	$ 21,153	$ 19,794	$ 62,101	$ 52,414

The increase in net revenue from investment operations in 2004 is primarily due to equity in earnings of limited partnerships of $3.8 million in the third quarter of 2004, compared to $1.3 million in the third quarter of 2003. There were no impairment charges included in net realized gains or losses on fixed maturity and equity investments in the third quarter of 2004 or 2003. Net revenue from investment operations increased 18.5% for the nine months ended September 30, 2004 to $62.1 million compared to $52.4 million for the same period of 2003, with the increase primarily attributable to improved equity in earnings of limited partnerships.

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The Company's performance of its fixed maturities and equity securities compared to selected market indices is presented below.

	Pre-tax annualized returns **Two year period ended September 30, 2004**
Erie Indemnity Company Indices:	
Fixed maturities — corporate	8.35%
Fixed maturities — municipal	3.88(1)
Preferred stock	8.06(1)
Common stock	16.88
Market indices:	
Lehman Brothers U.S. Aggregate	4.54%
S&P500 Composite Index	18.97

(1) Returns on municipal fixed maturities and preferred stocks have tax-equivalent yields of 6.53% and 9.97%, respectively.

Equity in earnings of limited partnerships was $3.8 million and $1.3 million for the quarters ended September 30, 2004 and 2003, respectively. Private equity and fixed income limited partnerships generated earnings of $3.5 million for the three months ended September 30, 2004 compared to losses of $.1 million for the same period of 2003. Real estate limited partnerships reflected earnings of $.3 million for the third quarter of 2004 compared to earnings of $1.4 million for the same period of 2003. There were no impairment charges on limited partnerships in the third quarter of 2004. In the third quarter of 2003, there were impairment charges related to private equity limited partnerships of $.6 million.

FINANCIAL CONDITION

Investments

The Company's investment strategy takes a long-term perspective emphasizing investment quality, diversification and superior investment returns. Investments are managed on a total return approach that focuses on current income and capital appreciation. The Company's investment strategy also provides for liquidity to meet the short- and long-term commitments of the Company. At September 30, 2004, the Company's investment portfolio of investment-grade bonds and preferred stock, common stock and cash and cash equivalents represents $1.2 billion, or 39.9%, of total assets. These investments provide the liquidity the Company requires to meet the demands on its funds.

The Company continually reviews the investment portfolio to evaluate positions that might incur other-than-temporary declines in value. For all investment holdings, general economic conditions and/or conditions specifically affecting the underlying issuer or its industry, including downgrades by the major rating agencies, are considered in evaluating impairment in value. In addition to specific factors, other factors considered in the Company's review of investment valuation are the length of time the market value is below cost and the amount the market value is below cost.

There is a presumption of impairment for common equity securities and equity limited partnerships when the decline is, in management's opinion significant and of an extended duration. The Company considers market conditions, industry characteristics and the fundamental operating results of the issuer to determine if sufficient objective evidence exists to refute the presumption of impairment. When the presumption of impairment is confirmed, the Company will recognize an impairment charge to operations. Common stock impairments are included in realized losses in the Consolidated Statements of Operations.

For limited partnerships, the impairment charge is included as a component of equity in losses or earnings of limited partnerships in the Consolidated Statements of Operations. No impairment charges were recorded on equity securities in the third quarter of 2004 or 2003. There were no impairment charges on equity securities in the first nine months of 2004. In the first nine months of 2003, impairment charges on equity securities were $.2 million. There were no impairment charges on limited partnerships in the third quarter of 2004. There was a $.5 million impairment charge on equity limited partnerships for the third quarter of 2003. Impairment charges on equity limited partnerships were $.1 million and $2.3 million for the nine months ended 2004 and 2003, respectively.

For fixed maturity and preferred stock investments, the Company individually analyzes all positions with emphasis on those that have, in management's opinion, declined significantly below cost. The Company considers market conditions, industry characteristics and the fundamental operating results of the issuer to determine if the decline is due to changes in interest rates, changes relating to a decline in credit quality, or other issues affecting the investment. A charge is recorded in the Consolidated Statements of Operations for positions that have experienced other-than-temporary impairments due to credit quality or other factors, or for which it is not the intent or ability of the Company to hold the position until recovery has occurred. There were no impairments recognized in the third quarter of 2004 or 2003 related to fixed maturity and preferred stock investments. (See "Analysis of Investment Operations" section). For the nine months ended September 30, 2004 there were no impairment charges on fixed maturities and preferred stock investments. For the first nine months of 2003 there were impairment charges of $3.5 million on fixed maturities and $2.3 million on preferred stock investments.

If the Company's policy for determining the recognition of impaired positions were different, the Company's Consolidated 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.

The Company's investments are subject to certain risks, including interest rate and price risk. The Company's exposure to interest rates is concentrated in the fixed maturities portfolio. The fixed maturities portfolio comprises 76.1% and 74.2% of invested assets at September 30, 2004 and December 31, 2003, respectively. The Company calculates the duration and convexity of fixed maturities portfolio each month to measure the price sensitivity of the portfolio to interest rate changes. Duration measures the relative sensitivity of the fair value of an investment to changes in interest rates. Convexity measures the rate of change of duration with respect to changes in interest rates. These factors are analyzed monthly to ensure that both the duration and convexity remain in the targeted ranges established by management.

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 does not hedge its exposure to equity price risk inherent in its equity investments. The Company's objective is to earn competitive relative returns by investing in a diverse portfolio of high-quality, liquid securities. Portfolio holdings are diversified across industries and among exchange traded mid- to large-cap stocks. The Company measures risk by comparing the performance of the marketable equity portfolio to benchmark returns such as the S&P 500.

The Company's portfolio of limited partnership investments has exposure to market risks, primarily relating to the financial performance of the various entities in which they invested. The limited partnership portfolio comprises 9.5% and 9.4% of invested assets at September 30, 2004 and

December 31, 2003, respectively. These investments consist primarily of equity investments in small and medium-sized companies and in real estate. The Company achieves diversification within the limited partnership portfolio by investing in approximately 70 partnerships that have approximately 1,428 distinct investments. The Company reviews at least quarterly the limited partnership investments by sector, geography and vintage year. These limited partnership investments are diversified to avoid concentration in a particular industry. The Company performs extensive research prior to investment in these partnerships.

Property/casualty insurance liabilities

Reserves for property/casualty insurance unpaid losses and loss adjustment expenses include estimates of 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 different than original estimates. Management has factored these changes in trends into the Company's loss estimates. Due to the nature of these liabilities, actual results ultimately could vary significantly from the amounts recorded.

Multiple actuarial methods are used in estimating unpaid loss and loss adjustment expense liabilities. Each methodology utilizes unique assumptions and variables. A range of reasonable estimates is developed utilizing these methods for each product line or product coverage analyzed. The presence or absence and magnitude of underlying variables, their interaction, and their recognition in estimation methods will cause the width of the range to vary for different product segments and over time for the same product segment. The final estimate recorded by management is a function of detailed analyses of historical trends, adjusted to reflect any new, perceived actionable data, adjusted as new emerging data indicates.

The factors which may potentially cause the greatest variation between current reserve estimates and the actual future paid amounts are: unforeseen changes in statutory or case law altering the amounts to be paid on existing claim obligations, new medical procedures and/or drugs whose cost is significantly different from that seen in the past, and claims patterns on current business that differ significantly from historical claims patterns.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Loss and loss adjustment expense reserves are presented on the Company's Statements of Financial Position on a gross basis. Under the terms of the Property and Casualty Group's intercompany pooling arrangement, a significant portion of these reserve liabilities are recoverable. Recoverable amounts are reflected as an asset on the Company's Statements of Financial Position. Gross loss and loss adjustment expense reserves by major line of business and the related amount recoverable under the intercompany pooling arrangement are as follows:

Property & Casualty Loss and Loss Adjustment Expense Reserve Liabilities:

	As of September 30, 2004	As of December 31, 2003
Gross Reserve Liability:		
Private Passenger Auto	$ 467,722	$ 445,141
Homeowners	25,067	22,433
Workers' Compensation	202,827	190,018
Commercial Auto	76,927	69,016
Commercial Multi-Peril	62,713	57,996
Other Direct	21,771	17,202
Reinsurance	48,903	43,730
Total Gross Reserves	905,930	845,536
Reinsurance Recoverables	734,636	687,819
Net Reserve Liability	$ 171,294	$ 157,717

At September 30, 2004, the Property and Casualty Group's estimated total loss exposure related to the events of September 11th remained at $150 million. At September 30, 2004, total paid claims and case reserves on reported claims total $78.0 million with an additional exposure to adverse development of $53.5 million if every claim ultimately develops into the full layer limit loss. These estimates are based on the September 11th attack being considered one event. If the attack comes to be considered two events, the Company anticipates an additional loss of approximately $22 million. Recent court proceedings have ruled that the September 11th attack was a single event under certain reinsurance treaties. If this ruling is upheld in the courts, the Property and Casualty Group's World Trade Center reserve could be reduced. Until this issue is definitively decided, the Company believes the $150 million total loss estimate remains appropriate and should be sufficient to absorb any potential development that may occur regardless of the determination of the occurrence as one or two events. The Company's property and casualty insurance subsidiaries share of losses related to the World Trade Center attack amounted to $5.8 million in 2001 net of recoveries under the excess-of-loss reinsurance agreement with the Exchange. No losses were recognized by the Company's property and casualty insurance subsidiaries in 2002, 2003 or 2004 related to the World Trade Center attack.

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 has a rating from A.M. Best of A+ ("Superior", the second highest A.M. Best rating). The A+ rating places the members of the Property and Casualty Group in the top 10% of approximately 3,000 property/casualty insurers rated and represents a superior ability to meet ongoing obligations to policyholders. Each member of the Property and Casualty Group also has a rating of Api ("strong") from Standard & Poors. A rating of "A" means that the insurer has strong financial security characteristics. The subscript "pi" means the rating was based on publicly available information.

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 upgraded in June 2004. The Erie Insurance Exchange was upgraded from a C (Fair) to a B- (Good) and the Erie Insurance Company was upgraded from a B- to a B. The remaining members of the Property and Casualty Group maintained B ratings (Good). Management believes that financial ratings are among many important factors in marketing the Property and Casualty Group's products to its agents and customers.

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. The Company's major sources of funds from operations are the net cash flow generated from the Company's management operations, the net cash flow from EIC's and EINY's 5.5% participation in the underwriting results of the reinsurance pool with the Exchange, and the Company's investment income from affiliated and non-affiliated investments. With respect to the management fee, funds are generally received from the Exchange on a premiums collected basis. The Company has a receivable from the Exchange and affiliates related to the management fee receivable from premiums written, but not yet collected, as well as the management fee receivable on premiums collected in the current month. The Company pays nearly all general and administrative expenses on behalf of the Exchange and other affiliated companies. The Exchange generally reimburses the Company for these expenses on a paid basis each month.

Management fee and other cash settlements due from the Exchange were $220.3 million at September 30, 2004, and $195.6 million at December 31, 2003. A receivable from EFL for cash settlements totaled $2.2 million at September 30, 2004, compared to $3.4 million at December 31, 2003. The receivable due from the Exchange for reinsurance recoverable from unpaid loss and loss adjustment expenses and unearned premium balances ceded to the intercompany reinsurance pool rose 9.2% to $857.2 million at September 30, 2004 from $785.1 million at December 31, 2003. The increases are the result of corresponding increases in direct loss reserves, loss adjustment expense reserves and unearned premium reserves of the Company's property/casualty insurance subsidiaries that are ceded to the Exchange under the intercompany pooling agreement. The increase in the property/casualty insurance subsidiaries reserves ceded to the Exchange is a result of a corresponding increase in direct premium written by the Company's property/casualty insurance subsidiaries. The increase in the property/casualty insurance subsidiaries direct written premium was 4.6% and 17.8% for the nine month period ended September 30, 2004 and 2003, respectively.

The Company's receivables from the Exchange represented 12.8% of the Exchange's assets at September 30, 2004, and 12.2% at December 31, 2003.

Cash outflows are variable because settlement dates for claim payments vary and cannot be predicted with absolute certainty. While volatility in claims payments could be significant for the Property and Casualty Group, the effect on the Company of this volatility is mitigated by the intercompany reinsurance pooling arrangement. The exposure for large loss payments is also mitigated by the Company's excess-of-loss reinsurance agreement with the Exchange. The cash flow requirements for claims have not historically been significant to the Company's liquidity. Based on a historical 15 year average, about 50% of losses and loss adjustment expenses included in the reserve are paid out in the subsequent 12-month period and approximately 89% is paid out within a five-year period. Such payments are reduced by recoveries under the intercompany reinsurance pooling agreement.

The Company has certain obligations and commitments to make future payments under various contracts. As of September 30, 2004, the payment periods are estimated for the aggregate obligations as follows:

	Payments Due By Period				
(dollars in thousands)	**Total**	**Less than 1year**	**1-3 years**	**3-5 years**	**Thereafter**
Fixed Obligations:					
Limited partnership commitments	$ 98,376	$ 26,536	$ 42,123	$ 21,717	$ 8,000
Operating leases-other	18,697	8,701	8,731	1,265	—
Operating leases-real estate	8,819	2,768	4,498	1,553	—
Operating leases-computer	3,900	2,689	1,211	—	—
Financing arrangements	1,134	543	591	—	—
eCommerce Program consulting arrangements	224	224	—	—	—
Fixed contractual obligations	131,150	41,461	57,154	24,535	8,000
Gross loss and loss expense reserves	905,930	452,965	266,343	88,781	97,841
Gross contractual obligations	1,037,080	494,426	323,497	113,316	105,841
Estimated reinsurance recoverables	734,636	367,318	215,983	71,994	79,341
Net contractual obligations	$ 302,444	$ 127,108	$ 107,514	$ 41,322	$ 26,500

For a complete discussion of the fixed contractual obligations see Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Annual Report on Form 10-K for the year ended December 31, 2003 as filed with the Securities and Exchange Commission on March 8, 2004.The Company has historically generated sufficient net positive cash flow from its operations to fund its commitments and build the investment portfolio. The Company also maintains a high degree of liquidity in its investment portfolio in the form of readily marketable fixed maturities, equity securities and short-term investments. Net cash flows provided by operating activities were $178.2 million and $166.0 million for the nine months ended September 30, 2004 and 2003, respectively.

Dividends declared and paid to shareholders for the nine months ended September 30, 2004 and 2003, totaled $41.5 million and $36.8 million, respectively. There are no regulatory restrictions on the payment of dividends to the Company's shareholders, although there are state law restrictions on the payment of dividends from the Company's insurance subsidiaries to the Company. Dividends from insurance subsidiaries are not material to the Company's cash flows.

During the third quarter of 2004, the Company repurchased 338,656 shares of its outstanding Class A common stock in conjunction with the stock repurchase plan that was authorized in December 2003. The shares were purchased at a total cost of $16.1 million, or an average price per share of $47.65. (See table at Part II. Item 2., Issuer Repurchases of Equity Securities.) During the first nine months of 2004, the Company repurchased 956,730 shares at a total cost of $44.6 million, or an average price per share of $46.58. The plan allows the Company to repurchase up to $250 million of its outstanding Class A common stock through December 31, 2006.

FACTORS THAT MAY AFFECT FUTURE RESULTS

Financial Condition of the Exchange

Erie Insurance Exchange was organized in Pennsylvania as a reciprocal insurance exchange. A reciprocal insurance exchange is an unincorporated association that consists of individuals, corporations or entities who, as subscribers, exchange contracts of insurance (policies) and share insurance risks among themselves, and whose affairs are managed by an attorney-in-fact appointed at the time of application for insurance. The subscribers pay premiums for insurance coverage that are intended to be sufficient to cover all of the costs of operating the reciprocal insurance exchange, including the payments of losses covered by the insurance policies issued by the reciprocal insurance exchange and the payment of the management fees of the attorney-in-fact, and generate a profit that is retained by the reciprocal insurance exchange as surplus. The purpose of the surplus is to increase the financial strength of the reciprocal insurance exchange so that it has greater capacity to pay the insurance losses incurred by its subscribers. In March of 2004, the Exchange's A.M. Best rating of A+ (superior) was reaffirmed with a stable outlook.

The subscribers' agreements between the policyholders and the Company, which is included in each insurance policy issued by the Company, permits the Company to retain up to 25% of the direct and affiliated assumed written premiums of the Exchange. In consideration for this payment, the Company performs certain services related to the sales, underwriting and issuance of policies on behalf of the Exchange.

Under the agreement between the Exchange and the other members of the Property and Casualty Group governing participation in the pooling arrangement whereby all property and casualty business is ceded to the Exchange. This pooling arrangement provides for EIC and EINY to share proportionately through retrocession in the results of the Property and Casualty Group, except for the provisions of the excess of loss reinsurance agreement discussed below. EIC's and EINY's proportionate share of the reinsurance pool is 5.0% and 0.5%, respectively.

The Company has a direct interest in the financial condition of the Exchange because management fee revenues are based on the direct written premiums of the Exchange and the other members of the Property and Casualty Group. Additionally, the Company's profitability is affected by its' participation in the underwriting results of the Exchange through the pooling arrangement in which the Company's insurance subsidiaries have a 5.5% participation. The Company's property/casualty insurance subsidiaries have in effect an all-lines aggregate excess-of-loss reinsurance agreement with the Exchange to reduce potential exposure to catastrophe losses and variations in long-term underwriting results. Additionally, a concentration of credit risk exists related to the unsecured receivables due from the Exchange for certain fees, costs and reimbursements.

To the extent that the Exchange incurs underwriting losses or investment losses resulting from declines in the value of its marketable securities, the Exchange's policyholders' surplus would be adversely affected. If the surplus of the Exchange were to decline significantly, 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 Exchange would have an adverse effect on the amount of the management fees the Company receives. Declining business could also adversely affect underwriting results of the Property and Casualty Group in which the Company has a 5.5% participation. In addition, a significant decline in the surplus of the Exchange could effect the management fee rate.

The selected financial data of the Exchange presented below is prepared in accordance with Statutory Accounting Principles (SAP) required by the NAIC Accounting Practices and Procedures Manual, as modified to include prescribed or permitted practices of the Commonwealth of Pennsylvania. The Exchange does not, nor is it required to, prepare financial statements in accordance with Generally Accepted Accounting Principles (GAAP). Financial statements prepared under SAP generally provide a more conservative approach than under GAAP. Under SAP, the principal focus is on the solvency of the insurer in order to protect the interests of the policyholders. Some significant differences between SAP and GAAP and state prescribed or permitted practices include the following:

- Bonds and short-term investments are valued at amortized cost or the lower of amortized cost or market under SAP. Nonredeemable preferred stocks are valued at fair value as determined by the Securities Valuation Office (SVO) or the lower of cost or SVO fair value. Redeemable preferred stocks are valued at cost or amortized cost or the lower of cost or SVO fair value. The SAP valuations are dependent upon the designation prescribed to the investment by the National Association of Insurance Commissioners. GAAP requires these investment securities be valued at fair value.

- SAP recognizes expenses when incurred and does not allow for the establishment of deferred policy acquisition cost assets that is required by GAAP;

- SAP deferred tax calculations follow GAAP with certain modifications for the realization criteria of deferred tax assets and the recording of the impact of changes in its deferred tax balances;

- GAAP requires the establishment of an asset for the estimated salvage and subrogation that will be recovered in the future. Under SAP, a company may establish this recoverable but is not required to do so. The Exchange does not establish estimated salvage and subrogation recoveries;

- As prescribed by the Insurance Department of the Commonwealth of Pennsylvania, the Exchange records in its statutory basis financial statements, unearned subscriber fees (fees to Attorney-In-Fact) as deductions from unearned premium reserve and charges current operations on a pro-rata basis over the periods covered by the policies;

- As permitted by the Insurance Department of the Commonwealth of Pennsylvania, the Exchange discounts workers' compensation case and IBNR liabilities at a rate of 2.5% on a non-tabular basis in their statutory basis financial statements.

The selected financial data below as of and for the three and nine months ended September 30, 2004 and 2003 is 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 condensed summarized financial data set forth below represents the Exchange's share of underwriting results after accounting for intercompany pool transactions.

Selected financial data of the Exchange
Condensed Statements of Operations
(Statutory Accounting Basis)

	Three Months Ended September 30		**Nine Months Ended September 30**	
(dollars in thousands)	**2004**	**2003**	**2004**	**2003**
	(unaudited)		**(unaudited)**	
Premiums earned	$ 937,357	$ 866,860	$ 2,741,960	$ 2,501,654
Losses and loss adjustment expenses	573,469	793,945	1,830,851	2,116,828
Insurance underwriting and other expenses*	271,123	247,732	790,223	756,597
Net underwriting income (loss)	92,765	(174,817)	120,886	(371,771)
Net investment income	70,685	61,138	202,179	172,313
Net realized gain	45,371	76,693	76,550	154,907
Federal income tax expense (benefit)	63,525	(12,858)	119,725	(59,539)
Net income	$ 145,296	$ (24,128)	$ 279,890	$ 14,988

** Includes management fees incurred*

The Exchange recorded net income of $145.3 million in the third quarter of 2004 compared to income of $24.1 million for the same period in 2003. Net written premiums grew in the third quarter of 2004, but at a slower pace than in 2003. Losses and loss adjustment expenses were lower in the third quarter of 2004, reflective of the initiatives implemented in 2003 to focus on underwriting profitability and reduced catastrophe losses.

Net premiums written of the Exchange increased 4.3% in the third quarter of 2004 compared to the third quarter of 2003, a slower growth rate than the 12.7% increase that occurred in the third quarter of 2003 compared to 2002. The changes in the Exchange's net written premium directly correlate to the changes of the Property and Casualty Group's premiums taken as a whole, and have been affected by the Company's focus on underwriting profitability through increased emphasis on controlling exposure growth and loss severity and improving risk selection and exiting the assumed reinsurance business.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Continued)

Losses and loss adjustment expenses decreased 27.8% in the third quarter of 2004 compared to 2003, compared to an increase of 30.3% in the third quarter of 2003 compared to 2002. The decrease in 2004 can partly be attributed to the impact of the focus on underwriting and reunderwriting standards to control exposure growth and loss severity and improve risk selection. Catastrophe losses or weather related events in the third quarters of 2004 and 2003 that impacted direct losses and loss adjustment expenses totaled $34.0 million and $104.0 million, respectively. The 2004 catastrophe losses included the effects of Hurricane Ivan. The 2003 catastrophe losses included approximately $70 million related to Hurricane Isabel. For the nine months ended September 30, 2003, eCommerce expenses were $10.5 million and $16.2 million, respectively.

The Exchange exited the voluntary assumed reinsurance business effective December 31, 2003. In the third quarter of 2004, nominal premiums received by the Exchange for voluntary assumed reinsurance business were offset by premium cancellation fees and a settlement amount upon the expiration of a treaty. The voluntary assumed business generated income of $9.3 million and $7.8 million in the first nine months of 2004 and 2003, respectively.

The reported statutory combined ratio of the Exchange was 93.6% and 112.1% for the nine months ended September 30, 2004 and 2003, respectively. The impact of the underwriting profitability initiatives and positive development of prior year results contributed to the improvement in the statutory combined ratio.

Net investment income of the Exchange increased 15.6% in the third quarter of 2004 compared to 2003. Realized gains totaled $45.4 million and $76.7 million in the third quarters of 2004 and 2003, respectively. Impairment charges of $.1 million were recorded on equity securities in the third quarter of 2004. In the third quarter of 2003, there were impairment charges on limited partnerships of $4.1 million.

Condensed Statements of Financial Condition
(Statutory Accounting Basis)

(dollars in thousands)	As of September 30 2004	As of December 31 2003
	(unaudited)	
Cash and invested assets	$ 7,223,864	$ 7,024,796
Other assets	1,180,043	1,020,830
Total assets	$ 8,403,907	$ 8,045,626
Claims and unearned premium reserves	$ 4,916,395	$ 4,616,687
Other liabilities	835,380	999,854
Total liabilities	5,751,775	5,616,541
Policyholders' surplus	2,652,132	2,429,085
Total liabilities and policyholders' surplus	$ 8,403,907	$ 8,045,626

The Exchange's policyholders' surplus increased 9.2% as of September 30, 2004 compared to December 31, 2003, as a result of net investment income and underwriting profitability.

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The Exchange's cash and invested assets consist of:

(Statutory Accounting Basis) (dollars in thousands)	Carrying value at September 30 2004 (unaudited)	%	December 31 2003	%
Equity securities:				
Common stock (fair value)	$ 1,339,877	18.6%	$ 1,258,685	17.9%
Preferred stock (fair value)	530,405	7.3	562,973	8.0
Bonds (amortized cost)	4,431,491	61.4	4,028,556	57.3
Limited partnerships, (under equity method)	540,626	7.5	485,174	6.9
Real estate mortgage loans	10,937	.1	11,161	.2
Properties occupied by the Exchange	36,610	.5	37,822	.5
Cash and cash equivalents	333,918	4.6	640,425	9.2
Total invested assets	$ 7,223,864	100.0%	$ 7,024,796	100.0%

Common equity securities historically represented a significant portion of the Exchange's investment portfolio and surplus that was exposed to price risk, volatility of the capital markets and general economic conditions. During 2003, the Exchange initiated a planned re-allocation of its invested assets with the intent of lessening its exposure to common stock investments. The goal of the reallocation of the common stock portfolio was to reduce the Exchange's equity investments to no more than 60% of surplus. At September 30, 2004 common stock investments of the Exchange were $1.3 billion, approximately 50.5% of the Exchange's surplus at September 30, 2004. During the third quarter of 2004, the Exchange had realized and unrealized capital losses of $65.6 million on its common stock portfolio. The weighted average current price to trailing twelve months earnings ratio of the Exchange's common stock portfolio was 28.3 and 22.21 at September 30, 2004 and 2003, respectively. The Standard & Poor's composite price to trailing twelve months earnings ratio was 24.75 at September 30, 2004 and 27.69 at September 30, 2003. Bonds are recorded at amortized cost in accordance with SAP. The fair value of bonds was $4.5 billion at September 30, 2004.

Insurance Premium Rate Increases

The premium growth attributable to rate increases of the Property and Casualty Group bears directly on underwriting profitability of the Property and Casualty Group and the Exchange. In recent years, prices for commercial and personal lines insurance have increased considerably in the industry. The property/casualty insurers of the Property and Casualty Group also increased prices considerably during 2003 and into 2004. Pricing actions contemplated or taken by the Property and Casualty Group are subject to various regulatory requirements of the states in which these insurers operate. The pricing actions already implemented, or to be implemented through 2004, will also have an effect on the market competitiveness of the Property and Casualty Group's insurance products. Such pricing actions, and those of our competitors, could affect the ability of our agents to sell and/or renew business.

Rate increases filed by the Property and Casualty Group for certain lines of business in various states were sought to offset growing loss costs in those lines. In the first nine months of 2004 these rate increases accounted for approximately $236 million in increased written premiums. Premium increases anticipated due to pricing actions approved through September 30, 2004, could amount to approximately $62 million in additional written premium for the Property and Casualty Group in the remainder of 2004. There is also the potential for an additional $2 million in written premium for the Property and Casualty Group in 2004 resulting from pricing actions contemplated or filed and awaiting approval. The majority of the anticipated increase stems from the private passenger auto, commercial multiple-peril, workers' compensation and the homeowners line of business. Price increases can reduce the Property and Casualty Group's ability to attract new policyholders and to retain existing policyholders because of the possibility of acquiring coverage at more competitive prices from other insurers.

Rate increases filed or anticipated to be filed at this time are estimated to increase 2005 written premiums by approximately $77 million.

Insurance Scoring

Underwriting: In August 2004, the Company implemented insurance scoring for underwriting purposes for its private passenger auto and homeowners lines of business in all operating states and territories, except Maryland, in response to changing competitive market conditions. Many insurance companies currently utilize insurance scoring to provide a better initial assessment of the acceptability of a risk and to develop a pricing strategy commensurate with the risk. Initially, insurance scoring will be used by the Company as a tool to distinguish between acceptable and unacceptable risks. Employing insurance scoring for underwriting should result in a more desirable pool of risks for the Property and Casualty Group. The impact the implementation of insurance scoring will have on the number of policies that are accepted or retained is not known. However, having a more desirable pool of risks will lend itself to better experience in the long term, which should positively impact underwriting profitability.

Pricing Segmentation: The Company is developing a comprehensive rating plan for the Property and Casualty Group's private passenger auto and homeowners lines of business. The rating plan will introduce significantly more rating tiers, providing the Company greater flexibility in pricing policies with varying degrees of risk. Insurance scores will be among the most significant risk factors the Company will incorporate into the rating plan. Expanded pricing segmentation, incorporating insurance scoring, should enable the Company to provide more competitive rates to policyholders with varying risk characteristics. The long-term effects of pricing segmentation using insurance scoring cannot currently be determined.

Catastrophe Risk

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 the 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 or destructive weather pattern could materially adversely affect the results of operations and surplus position of the members of the Property and Casualty Group. Common catastrophe events include hurricanes, earthquakes, tornadoes, wind and hail storms, fires and explosions. Catastrophe insurance had not been acquired since 1993. The Property and Casualty Group entered into a reinsurance treaty in 2003 covering the 2003 accident year, and renewed the treaty to cover accident year 2004, to mitigate the future potential catastrophe loss exposure. The 2004 agreement is a property catastrophe reinsurance treaty that provides coverage of up to 95.0% of a loss of $460 million in excess of the Property and Casualty Group's loss retention of $140 million per occurrence. No loss recoverables were recorded under this treaty at September 30, 2004.

Information Technology Costs

In 2001, the 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 over the long-term.

The Erie Insurance Group has incurred approximately $171.2 million on the technology effort through the third quarter of 2004. In addition to this amount, $2.0 million has been committed for computer and equipment leases. Target delivery dates originally established in 2002 have generally not been met as management has devoted increased effort to quality assurance efforts to ensure that the rollout creates only minimal business disruption. Revised target dates and program costs continue to be developed and will extend beyond originally estimated target delivery dates and exceed costs.

As of September 30, 2004, the Company had deployed *ErieConnection*, the insurance application and policy processing system being developed in the eCommerce program, to approximately 48 agencies in Ohio, Illinois, Indiana and Wisconsin and a total of about 1,000 Erie employees in the home and branch office locations. The system has generally not met Company or agency expectations for functionality or performance. Management is taking action to enhance *ErieConnection*, to correct deficiencies and improve usability and will not continue deployment beyond the current installed base until such remedial actions are suitably completed. The cost and timing of such actions are not determinable at this time.

In addition to the cost impact of eCommerce, the implementation of this new system will require a significant investment in training and orientation for the independent agency force. During implementation, as agency resources are dedicated to learning the new system, new business sales may decline over the short term. The amount of lost sales will correlate to the timing and duration of the rollout effort as well as the number and types of issues encountered. Measurement of this impact on sales can not yet be estimated.

Terrorism

The World Trade Center terrorist attack resulted in significant losses for the insurance industry and has caused uncertainty in the insurance and reinsurance markets. The Property and Casualty Group recorded a loss of $150 million in 2001 related to this attack.

The Company's 5.5% share of this incurred loss was $5.8 million, after consideration of recoveries under the excess-of-loss reinsurance agreement. Accordingly, the industry was 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/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 initially excluded or limited some coverages and exposures where permitted by state regulators prior to enactment of the Terrorism Risk Insurance Act of 2002, discussed below.

On November 26, 2002, President Bush signed the Terrorism Risk Insurance Act of 2002 ("Act"), establishing a program for commercial property/casualty losses, including workers' compensation, resulting from foreign acts of terrorism. The Act required commercial insurers to make terrorism coverage available immediately through at least December 31, 2004 and provided 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 second year to $15 billion in the third year of the program. The federal government will pay 90% of covered terrorism losses that exceed retention levels. On June 18, 2004, the Department of Treasury announced its decision to require insurers to continue to make terrorism coverage available under the Act in program year three. The Act is scheduled to expire on December 31, 2005. Personal lines are not included under the protection of the Act, and state regulators have not approved exclusions for acts of terrorism on personal lines policies. The Property and Casualty Group is exposed to terrorism losses for personal and commercial lines and workers' compensation, although commercial lines are afforded a backstop above certain retention levels for foreign acts of terrorism under the federal program. The Property and Casualty Group could incur large losses if future terrorist attacks occur.

The Erie Insurance Group has taken the steps necessary to comply with the Act by providing notices to all commercial policyholders, disclosing the premium, if any, attributable to coverage for acts of terrorism, as defined in the Act, and disclosing federal participation in payment of terrorism losses. The Act pre-empted any exclusion or provision in place prior to November 26, 2002 that excluded or limited coverage for losses from foreign acts of terrorism. Insurers may exclude coverage for foreign acts of terrorism under the Act if the policyholder accepts an exclusion and rejects coverage or fails to pay additional premium charges after notice is given. Exclusions are not allowed under workers' compensation policies and rates for terrorism coverage are applied in accordance with state laws.

The Erie Insurance Group continues to evaluate procedures that have been established to comply with the Act. Terrorism coverage is not excluded under the majority of Erie Insurance Group commercial property and casualty policies. Other than workers' compensation policies which incur charges consistent with state law, premium charges for terrorism coverage are currently applied only for a small number of new and renewal commercial policies where deemed appropriate based upon individual risk factors and characteristics. Appropriate disclosure notices and the opportunity to reject coverage are provided to such policyholders in accordance with the Act.

Sarbanes-Oxley Act of 2002

The Company is currently undergoing a comprehensive effort to comply with Section 404 of the Sarbanes-Oxley Act of 2002. Compliance is required for the Company's December 31, 2004 fiscal year end. Substantial testing of the internal control procedures has been completed to date and has identified certain potential deficiencies. These potential deficiencies if uncorrected, individually or when aggregated, may amount to significant deficiencies or material weaknesses in internal controls over financial reporting under definitions established by the Securities and Exchange Commission and Public Company Accounting Oversight Board. Management has adopted a remediation plan to resolve these known deficiencies. The planned improvements include additional information technology system controls, further formalization of policies and procedures, improved segregation of duties and additional monitoring controls. While the Company's review continues with the goal of completion by the specified deadline, and management reasonably expects to complete this evaluation by this deadline, there is a chance that unforeseen circumstances may impede the Company's ability to complete all phases of testing by December 31, 2004.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's exposure to market risk is primarily related to fluctuations in prices and interest rates. Quantitative and qualitative disclosures about market risk resulting from changes in prices and interest rates are included in Item 7A. in the Company's 2003 Annual Report on Form 10-K. There have been no material changes in such risks or the Company's periodic reviews of asset and liability positions during the nine months ended September 30, 2004. The information contained in the investments section of Management's Discussion and Analysis of Financial Condition and Results of Operations is incorporated herein by reference.

The Company's objective is to earn competitive returns by investing in a diversified portfolio of securities. The Company is exposed to credit risk through its portfolios of fixed maturity securities, nonredeemable preferred stock, mortgage loans and to a lesser extent short-term investments. This risk is defined as the potential loss in 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 ongoing reviews of credit quality by position and for the fixed maturity portfolio in total. The Company does not hedge credit risk inherent in its fixed maturity investments.

The Company has significant receivables from the Exchange, which are subject to credit risk. Company results are directly related to the financial strength of the Exchange. Credit risks related to the receivables from the Exchange are evaluated periodically by Company management. Since the Company's inception, it has collected all amounts due from the Exchange in a timely manner (generally within 120 days).

ITEM 4. CONTROLS AND PROCEDURES

As of September 30, 2004, the Company carried out an evaluation, under the supervision and with the participation of the Company’s management, including its Chief Executive Officer and its Chief Financial Officer, of the design and operation of the Company’s disclosure controls and procedures. Based on this evaluation, the Company’s Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures are effective for gathering, analyzing and disclosing the information the Company is required to disclose in the reports it files under the Securities Exchange Act of 1934, within the time periods specified in the SEC’s rules and forms. There have been no significant changes in the Company’s internal controls or in other factors that could significantly affect internal controls subsequent to the date of this evaluation.

PART II. OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES, AND USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased	Average Price Paid Per share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plan
July 1 - 31, 2004	64,890	$ 46.71	63,195	
August 1 - 31, 2004	265,461	47.74	265,461	
September 1 - 30, 2004	10,000	50.74	10,000	
Total	340,351	$ 47.63	338,656	$ 205,430,000

The month of July 2004 includes shares that vested under the stock compensation plan for the Company’s outside directors of 1,695. Included in this amount are the vesting of 1,610 of awards previously granted and 85 dividend equivalent shares that vest as they are granted (as dividends are declared by the Company).

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PART II. OTHER INFORMATION (Continued)

ITEM 6. EXHIBITS

Exhibit Number	Description of Exhibit
31.1	Certifications of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certifications of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Reports on Form 8-K

On July 28, 2004, the Company filed a report on Form 8-K reporting under Item 5, the Company’s results for the second quarter of 2004. The results were discussed for the period based on the three primary segments, management operations, insurance underwriting operations and investment operations. The Company’s Consolidated Statements of Operations, Consolidated Statements of Operations Segment Basis, Consolidated Statements of Financial Position, Segment Information and Selected Financial Data of the Erie Insurance Exchange were included in the filing.

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SIGNATURES

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

Erie Indemnity Company
(Registrant)

Date: October 27, 2004

/s/ Jeffrey A. Ludrof
Jeffrey A. Ludrof, President & CEO

/s/ Philip A. Garcia
Philip A. Garcia, Executive Vice President & CFO

EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002

I, Jeffrey A. Ludrof, Chief Executive Officer of Erie Indemnity Company, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Erie Indemnity Company;

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

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

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

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

   b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors:

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 27, 2004

/s/ Jeffrey A. Ludrof

Jeffrey A. Ludrof, President & CEO

EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002

I, Philip A. Garcia, Chief Financial Officer of Erie Indemnity Company, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Erie Indemnity Company;

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

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

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

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

    b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors:

    a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: October 27, 2004

/s/ Philip A. Garcia

Philip A. Garcia, Executive Vice President & CFO

EXHIBIT 32

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

We, Jeffrey A. Ludrof, Chief Executive Officer of the Company, and Philip A. Garcia, Chief Financial Officer of the Company, certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. § 1350, that:

(1) The Quarterly Report on Form 10-Q of the Company for the quarterly period September 30, 2004 (the "Report") fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Jeffrey A. Ludrof

Jeffrey A. Ludrof
President and Chief Executive Officer

/s/ Philip A. Garcia

Philip A. Garcia
Executive Vice President and Chief Financial Officer

October 27, 2004

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to Erie Indemnity Company and will be retained by Erie Indemnity Company and furnished to the Securities and Exchange Commission or its staff upon request.