

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Form 10-K  
[X] Annual Report Pursuant to Section 13 or 15(d) of  
The Securities Exchange Act of 1934

For the fiscal year ended December 31, 1996  
Commission File Number 0-21886

BARRETT BUSINESS SERVICES, INC.  
(Exact name of registrant as specified in its charter)

Maryland 52-0812977  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

4724 S.W. Macadam Avenue 97201  
Portland, Oregon (Zip Code)  
(Address of principal executive offices)

Registrant's telephone number, including area code: (503) 220-0988

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section  
12(g) of the Act:

Common Stock, Par Value \$.01 Per Share  
(Title of class)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

State the aggregate market value of the voting stock held by non-affiliates of the Registrant.  
\$90,027,225 at February 28, 1997

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date.  
Class Outstanding at February 28, 1997  
Common Stock, Par Value \$.01 Per Share 6,825,827 Shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive Proxy Statement for the 1997 Annual Meeting of Stockholders are hereby incorporated by reference into Part III of Form 10-K.

<TABLE>

INDEX

Page	<S>	<C>	<C>
PART I	.....		
3			
	ITEM 1.	BUSINESS.....	
3			
	ITEM 2.	PROPERTIES.....	
15			

15	ITEM 3.	LEGAL PROCEEDINGS.....
16	ITEM 4.	SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.....
16		EXECUTIVE OFFICERS OF THE REGISTRANT.....
18	PART II.....	
18	ITEM 5.	MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS.....
19	ITEM 6.	SELECTED FINANCIAL DATA.....
20	ITEM 7.	MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.....
28	ITEM 8.	FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.....
52	ITEM 9.	CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.....
52	PART III.....	
52	ITEM 10.	DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT.....
52	ITEM 11.	EXECUTIVE COMPENSATION.....
52	ITEM 12.	SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT.....
52	ITEM 13.	CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS.....
53	PART IV.....	
53	ITEM 14.	EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K.....
54	SIGNATURES	.....
55	EXHIBIT INDEX	.....

</TABLE>

PART I

Item 1. BUSINESS

General

Barrett Business Services, Inc. ("Barrett" or the "Company"), was incorporated in the state of Maryland in 1965. Barrett is a leading human resource management company. The Company provides comprehensive outsourced solutions addressing the costs and complexities of a broad array of employment-related issues for small and mid-sized businesses. Employers are faced with increasing complexities in employment laws and regulations, employee benefits and administration, federal, state and local payroll tax compliance, and mandatory workers' compensation coverage, as well as the recruitment and retention of quality employees. The Company believes that outsourcing the management of various employer and human resource responsibilities, which are considered non-core functions, enables organizations to focus on their core competencies, thereby improving operating efficiencies.

Barrett's range of services and expertise in human resource management

encompasses five major categories: payroll processing, employee benefits and administration, workers' compensation coverage, aggressive risk management and workplace safety programs, and human resource administration, which includes functions such as recruiting, interviewing, drug testing, hiring, placement, training, and regulatory compliance. These services are typically provided through a variety of contractual arrangements, as part of either a traditional staffing service or a professional employer organization ("PEO") service. Staffing services include on-demand or short-term staffing assignments, long-term or indefinite-term contract staffing, and comprehensive on-site personnel management responsibilities. In a PEO arrangement, the Company enters into a contract to become a co-employer of the client company's existing workforce and assumes responsibility for some or all personnel-related matters. The Company's target PEO clients typically have limited resources available to effectively manage these matters. The Company believes that its ability to offer clients a broad mix of staffing and PEO services differentiates it from its competitors and benefits its clients through (i) lower recruiting and personnel administration costs, (ii) decreases in payroll expenses due to lower workers' compensation and health insurance costs, (iii) improvements in workplace safety and employee benefits, (iv) lower employee turnover, and (v) reductions in management time and energy expended in labor-related regulatory compliance. For 1996, Barrett's staffing services revenues represented 52.6% of total revenues, compared to 47.4% for PEO services revenues.

Barrett provides services to a diverse array of customers, including, among others, electronics manufacturers, various light-manufacturing industries, forest products and agriculture-based companies, transportation and shipping enterprises, general contractors in numerous construction-related fields and various professional services firms. During 1996, the Company provided staffing services to approximately 5,000 customers. Although a majority of the Company's staffing customers are small to mid-sized businesses, during 1996 approximately 55 of the Company's customers have each utilized Barrett employees in a number ranging from at least 200 employees to as many as 1,400 employees through various staffing services arrangements. In addition, Barrett had approximately 780 PEO clients at December 31, 1996, compared to 530 at December 31, 1995.

The Company operates through a network of 24 branch offices in Oregon, California, Washington, Maryland, Delaware, Idaho, Arizona and Michigan. Barrett also has 21 smaller recruiting and staffing offices in its general market areas under the direction of a branch office.

#### Operating Strategies

The Company's principal operating strategies are to: (i) promote a decentralized and autonomous management philosophy, (ii) motivate employees through wealth sharing, (iii) operate successfully in smaller geographic markets, (iv) leverage branch level economies of scale, (v) provide a unique and efficient blend of staffing and PEO services and (vi) control costs through effective risk management.

#### Growth Strategies

The Company's principal growth strategies are to: (i) expand through acquisitions of human resource-related businesses in new and existing geographic markets, (ii) expand into new geographic markets, (iii) increase revenues in existing branches through enhanced marketing and sales initiatives, (iv) accelerate the growth of PEO services and (v) enhance management information systems to support continued growth and to improve customer services.

#### Recent Acquisitions

On April 1, 1996, the Company acquired certain assets and the business of StaffAmerica, Inc., pursuant to a Plan and Agreement of Reorganization. StaffAmerica provides both temporary staffing and PEO services through its two offices located in Goleta and Oxnard, California. In 1995, StaffAmerica had revenues of approximately \$6.7 million. In exchange for the StaffAmerica assets and business operations, the Company issued 157,464 shares of its common stock valued at \$2,795,000, assumed a StaffAmerica liability of \$50,000 for customer deposits and issued to each of the two owners of StaffAmerica 845 shares of Company common stock for their covenants not to compete.

On April 8, 1996, the Company acquired certain assets and the business of JobWorks Agency, Inc. by way of a Plan and Agreement of Reorganization. JobWorks provides both temporary staffing and PEO services through its two offices located in Hood River and The Dalles, Oregon. JobWorks had revenues of approximately \$1.2 million in 1995. The Company issued 20,446 shares of its

common stock with a then-fair value of \$380,000 for the assets and business of JobWorks, assumed a customer deposit liability of \$2,000 and paid \$20,000 in cash for the selling shareholder's agreement of noncompetition.

Effective August 26, 1996, the Company acquired certain assets of Cascade Technical Staffing for \$550,000 in cash. Cascade, which had 1995 revenues of approximately \$3.5 million, provides technical and light industrial staffing services primarily in the electronics industry through its Tigard, Oregon office.

Effective November 4, 1996, the Company acquired the PEO division of California Employer Services, Inc., an Orange County, California staffing services company. The Company paid \$624,000 in cash for the division and assumed a customer deposit liability of \$36,000. The division generated revenues of approximately \$10.5 million for the fiscal year ended September 30, 1996.

Effective November 25, 1996, the Company acquired certain assets of Professional Personnel, Inc. ("PPI"), a provider of PEO services located in Downey, California. The Company paid \$176,000 in cash for the division and assumed a customer deposit liability of \$19,000. For the fiscal year ended September 30, 1996, PPI had revenues of approximately \$2.4 million.

4

Subsequent to year end, effective February 1, 1997, the Company acquired D&L Personnel Department Specialists, Inc., dba HR Only, a staffing services company which specializes in human resource professionals with offices in Los Angeles and Orange County, California. The Company paid \$1,800,000 in cash for all of the outstanding common stock of HR Only and \$1,200,000 in cash for noncompete agreements with certain individuals, of which \$1,000,000 will be deferred for five years and then be paid ratably over the succeeding five-year period. HR Only's revenues for the fiscal year ended January 31, 1997 were approximately \$4.3 million.

The Company reviews acquisition opportunities on an ongoing basis. While growth through acquisition is a major element of the Company's overall strategic growth plan, there can be no assurance that any additional acquisitions will be completed in the foreseeable future, or that any future acquisitions will have a positive effect on the Company's performance. Acquisitions involve a number of potential risks, including the diversion of management's attention to the assimilation of the operations and personnel of the acquired companies, exposure to workers' compensation and other costs in differing regulatory environments, adverse short-term effects on the Company's operating results, integration of management information systems and the amortization of acquired intangible assets.

#### The Company's Services

Overview of Services. The Company offers a continuum of human resource management services to its clients. While some services are more frequently associated with Barrett's co-employer arrangements, the Company's expertise in such areas as safety services and personnel-related regulatory compliance may also be utilized by its staffing services customers through the Company's human resource management services. The Company's range of services and expertise in human resource management encompasses five major categories:

- o Payroll Processing. For both the Company's PEO and staffing services employees, the Company performs all functions associated with payroll administration, including preparing and delivering paychecks, computing tax withholding and payroll deductions, handling garnishments, computing vacation and sick pay, and preparing W-2 forms and accounting reports through centralized operations at its headquarters in Portland, Oregon.
- o Employee Benefits and Administration. As a result of its size, Barrett is able to offer employee benefits which are not available at an affordable cost to many of its customers, particularly those with fewer than 100 employees. These benefits include health care insurance, a 401(k) savings plan, a Section 125 cafeteria plan, life and disability insurance, and claims administration.
- o Safety Services. Barrett offers safety services to both its staffing services and PEO customers in keeping with its corporate philosophy of "making the workplace safer." The Company has at least one risk manager available at each branch office to perform workplace safety assessments for each of its customers and to recommend actions to achieve safer operations. The Company's

services include safety training and safety manuals for both workers and supervisors, job-site visits and meetings, improvements in workplace procedures and equipment to further reduce the risk of injury, compliance with OSHA requirements, environmental regulations, and workplace regulation by the U.S. Department of Labor and state agencies, and accident investigations. As discussed under "Self-Insured Workers' Compensation Program" below, the Company also pays safety incentives to its customers who achieve improvements in workplace safety.

5

- o Workers' Compensation Coverage. Beginning in 1987, the Company acquired self-insured employer status for workers' compensation coverage in Oregon and is currently a qualified self-insured employer in many of the state and federal jurisdictions in which it operates. Through its third-party administrators, Barrett provides claims management services to its PEO customers. As discussed under "Self-Insured Workers' Compensation Program" below, the Company aggressively manages job injury claims, including identifying fraudulent claims and utilizing its staffing services to return workers to active employment earlier. As a result of its enhanced ability to manage workers' compensation costs, the Company is often able to reduce its clients' overall expenses arising out of job-related injuries and insurance.
- o Human Resource Administration. Barrett offers its clients the opportunity to leverage the Company's experience in personnel-related regulatory compliance. For both its PEO clients and for staffing services employees, the Company handles the burdens of advertising, recruitment, skills testing, checking job applications and references, drug screening, criminal and motor vehicle records checks, hiring, and compliance with such employment regulatory areas as immigration, the Americans with Disabilities Act, and federal and state labor regulations.

Staffing Services. Barrett's staffing services include on-demand or short-term staffing assignments, contract staffing, long-term or indefinite-term on-site management, and human resource administration. Short-term staffing involves employee demands caused by such factors as seasonality, fluctuations in customer demand, vacations, illnesses, parental leave, and special projects without incurring the ongoing expense and administrative responsibilities associated with recruiting, hiring, and retaining additional permanent employees. As more and more U.S. companies focus on cost-cutting and reducing overhead, the use of employees on a short-term basis allows firms to utilize the "just-in-time" approach to their personnel needs, converting a portion of their fixed personnel costs to variable expense.

Contract staffing refers to the Company's responsibilities for the placement of employees for a period of more than three months or an indefinite period. This type of arrangement often involves outsourcing an entire department in a large corporation or providing the manpower for a large project.

In an on-site management arrangement, Barrett places an experienced manager on site at a customer's place of business. The manager is responsible for conducting all recruiting, screening, interviewing, testing, hiring, and employee placement functions at the customer's facility for a long-term or indefinite period.

The Company's staffing services customers operate in a broad range of businesses, including forest products and agriculture-based companies, electronic manufacturers, transportation and shipping companies, food processors, professional firms, and construction contractors. Such customers range in size from small local firms to large national companies which use Barrett's services on a local basis. None of the Company's staffing services customers individually accounted for more than 10% of its total 1996 revenues.

In 1996, light industrial workers generated approximately 73% of the Company's staffing services revenues, while technical personnel accounted for 17% of such revenues and clerical staff represented the balance of 10%. Light industrial workers in the Company's employ perform such tasks as operation of machinery, manufacturing, loading and shipping, site preparation for special events, construction-site cleanup and janitorial services. Technical personnel include electronic parts

6

assembly workers and designers and drafters of electronic parts. Clerical workers include primarily secretaries, receptionists and office clerks.

Barrett emphasizes prompt, personalized service in assigning quality, trained, drug-free personnel at competitive rates to users of its staffing services. The Company uses internally developed computer databases of employee skills and availability at each of its branches to match customer needs with available qualified employees. The Company emphasizes the development of an understanding of the unique requirements of its clientele by its account managers. Customers are offered a "money-back" guarantee if dissatisfied with staffing employees placed by Barrett.

The Company utilizes a variety of methods to recruit its workforce for staffing services, including among others, referrals by existing employees, newspaper advertising and marketing brochures distributed at colleges and vocational schools. The employee application process includes an interview, skills assessment test, reference verification and drug screening. The recruiting of qualified employees requires more effort when unemployment rates are low.

Barrett's staffing services employees are not under its direct control while placed at a customer's worksite. Barrett has not experienced any significant liability due to claims arising out of negligent acts or misconduct by its staffing services employees. The possibility exists, however, of claims being asserted against the Company which may exceed the Company's liability insurance coverage, which could have a material adverse effect on the Company's business, financial condition, and results of operations.

PEO Services. Many businesses, particularly those with a limited number of employees, find personnel administration requirements to be unduly complex and time consuming. These businesses often cannot justify the expense of a full-time human resources staff. In addition, the escalating costs of health and workers' compensation insurance in recent years, coupled with the increased complexity of laws and regulations affecting the workplace, have created a compelling motivation for small to mid-sized businesses to outsource these managerial burdens. The outsourcing of non-core business functions, such as human resource administration, enables small enterprises to devote their limited resources to their core competencies.

In a PEO services arrangement, Barrett enters into a contract to become a co-employer of the client company's existing workforce. Pursuant to this contract, Barrett assumes responsibility for some or all personnel-related matters, including payroll and payroll taxes, employee benefits, health insurance, workers' compensation coverage, workplace safety programs, compliance with federal and state employment laws, labor and workplace regulatory requirements, and related administrative responsibilities. Barrett also hires and fires its PEO employees, although the client company remains responsible for day-to-day assignments, supervision and training and, in most cases, recruiting.

The Company began offering PEO services to Oregon customers in 1990 and expanded these services to Maryland and Washington in the first and third quarters, respectively, of 1994, to Delaware and California in the second quarter of 1995, to Idaho and Arizona in 1996. The Company has entered into co-employer arrangements with a wide variety of clients, including companies involved in reforestation, moving and shipping, professional firms, construction, retail, manufacturing and distribution businesses. PEO clients are typically small to mid-sized businesses with up to 100 employees. None of the Company's PEO clients individually accounted for more than 5% of its total annual revenues during 1996.

Prior to entering into a co-employer arrangement, the Company performs an analysis of the potential client's actual personnel and workers' compensation costs based on information provided by the customer. Barrett introduces its workplace safety program and recommends improvements in procedures and equipment following a safety inspection of the customer's facilities which the potential client must agree to implement as part of the co-employer arrangement. Barrett also offers significant financial incentives to PEO clients to maintain a safe work environment.

The Company's standard PEO services agreement provides for services for an indefinite term, until notice of termination is given by either party. The agreement permits cancellation by either party upon 30 days' written notice. In addition, the Company may terminate the agreement at any time for specified reasons, including nonpayment or failure to follow Barrett's workplace safety program.

The form of agreement also provides for indemnification of the Company by the client against losses arising out of any default by the client under the agreement, including failure to comply with any employment-related, health and safety or immigration laws or regulations. The Company also requires the client to maintain comprehensive liability coverage in the amount of \$1,000,000 for acts of its worksite employees. In addition, the Company has excess liability insurance coverage in the amount of \$2,000,000 per occurrence and policy limits of \$5,000,000 in the aggregate. Although no claims exceeding such policy limits have been paid by the Company to date, the possibility exists that claims for amounts in excess of sums available to the Company through indemnification or insurance may be asserted in the future, which could have a material adverse effect on the Company's business, financial condition, and results of operations.

#### Sales and Marketing

The Company markets its services primarily through direct sales presentations by its branch office account managers. The Company also obtains referrals from existing clients and other third parties, and places radio commercials and advertisements in various publications, including local newspapers and the Yellow Pages. Barrett believes that it is able to offer its services at competitive rates due to the lower costs associated with its self-insured workers' compensation program when compared to the cost of workers' compensation insurance. See "Self-Insured Workers' Compensation Program" below.

#### Billing

Through centralized operations at the Company's headquarters in Portland, Oregon, the Company prepares invoices weekly for its staffing services customers and following the end of each payroll period for PEO clients. The costs of health insurance coverage and Barrett's cafeteria plan are passed through to its PEO clients based on the number of participating employees. The Company often requires a deposit from its PEO clients to cover a portion of the anticipated billing for one payroll period. The Company has generally had favorable results with collecting accounts receivable, which it attributes to customer satisfaction, its analysis of potential clients' credit histories, and weekly monitoring of account aging by each branch manager.

#### Self-Insured Workers' Compensation Program

A principal service provided by Barrett to its customers, particularly its PEO clients, is workers' compensation coverage. As the employer of record, Barrett is responsible for complying with applicable statutory requirements for workers' compensation coverage. The Company's

workplace safety services, also described under "Overview of Services," are closely tied to its approach to the management of workers' compensation risk.

Elements of Workers' Compensation System. State law (and, for certain types of employees, federal law) generally mandates that an employer reimburse its employees for the costs of medical care and other specified benefits for injuries or illnesses incurred in the course and scope of employment. The benefits payable for various categories of claims are determined by state regulation and vary with the severity and nature of the injury or illness and other specified factors. In return for this guaranteed protection, workers' compensation is an exclusive remedy and employees are generally precluded from seeking other damages from their employer for workplace injuries. Most states require employers to maintain workers' compensation insurance or otherwise demonstrate financial responsibility to meet workers' compensation obligations to employees. In many states, employers who meet certain financial and other requirements are permitted to self-insure.

Self Insurance for Workers' Compensation. In August 1987, Barrett became a self-insured employer for workers' compensation coverage in Oregon. The Company has subsequently obtained self-insured employer status for workers' compensation in four additional states, Maryland, Washington, Delaware, and California. In addition, in May 1995, the Company was granted self-insured employer status by the U.S. Department of Labor for longshore and harbor ("USL&H") workers' compensation coverage. Regulations governing self-insured

employers in each jurisdiction typically require the employer to maintain surety deposits of cash, government securities or other financial instruments to cover workers' claims in the event the employer is unable to pay for such claims.

Barrett also maintains excess workers' compensation insurance for single occurrences exceeding \$350,000 (except for \$300,000 in Maryland and \$500,000 for USL&H coverage) with statutory limits (i.e., in unlimited amounts) pursuant to annual policies with major insurance companies. The excess-insurance policies contain standard exclusions from coverage, including punitive damages, fines or penalties in connection with violation of any statute or regulation and losses covered by other insurance or indemnity provisions.

In addition, the Company has implemented an insured large-deductible program which allows it to become insured for workers' compensation coverage in nearly all states where the extent of the Company's operations does not yet warrant the investment to become a self-insured employer.

Claims Management. Pursuant to its self-insured status, the Company's workers' compensation expense is tied directly to the incidence and severity of workplace injuries to its employees. Barrett seeks to contain its workers' compensation costs through an aggressive approach to claims management. The Company uses managed-care systems to reduce medical costs and keeps time-loss costs to a minimum by assigning injured workers, whenever possible, to short-term assignments which accommodate the workers' physical limitations. The Company believes that these assignments minimize both time actually lost from work and covered time-loss costs. Barrett has also engaged third-party administrators ("TPAs") to provide additional claims management expertise. Typical management procedures include performing thorough and prompt on-site investigations of claims filed by employees, working with physicians to encourage efficient medical management of cases, denying questionable claims and negotiating early settlements to eliminate future case development and costs. Barrett also maintains a mandatory corporate-wide pre-employment drug testing program. The program is believed to have resulted in a reduction in the frequency of fraudulent claims and in accidents in which the use of illegal drugs appears to have been a contributing factor.

Elements of Self-Insurance Costs. The costs associated with the Company's self-insured workers' compensation program include case reserves for reported claims, an additional expense provision (referred to as the "IBNR reserve") for unanticipated increases in the cost of open injury claims (known as "adverse loss development") and for claims incurred in prior periods but not reported, fees payable to the Company's TPAs, additional claims administration expenses, administrative fees payable to state and federal workers' compensation regulatory agencies, premiums for excess workers' compensation insurance, legal fees, and safety incentive payments. Although not directly related to the size of the Company's payroll, the number of claims and correlative loss payments may be expected to increase with growth in the total number of employees. TPA fees also vary with the number of claims administered. The state assessments are typically based on payroll amounts and, to a limited extent, the amount of permanent disability awards during the previous year. Excess insurance premiums are also based in part on the size of the Company's payroll. Safety incentives expense may increase as the number of the Company's PEO employees rises, although increases will only occur for any given PEO client if such client's claims costs are below agreed-upon amounts.

#### Workers' Compensation Claims Experience and Reserves

The Company recognizes its liability for the ultimate payment of incurred claims and claims adjustment expenses by accruing liabilities which represent estimates of future amounts necessary to pay claims and related expenses with respect to covered events that have occurred. When a claim involving a probable loss is reported, the Company's TPA establishes a case reserve for the estimated amount of ultimate loss. The estimate reflects an informed judgment based on established case reserving practices and the experience and knowledge of the TPA regarding the nature and expected value of the claim, as well as the estimated expense of settling the claim, including legal and other fees and expenses of administering claims. The adequacy of such case reserves depends on the professional judgment of each TPA to properly and comprehensively evaluate the economic consequences of each claim. Additionally, on an aggregate basis, the Company has established an additional expense reserve for both future adverse loss development in excess of initial case reserves on open claims and for claims incurred but not reported, referred to as the IBNR reserve.

As part of the case reserving process, historical data is reviewed and consideration is given to the anticipated effect of various factors, including



known and anticipated legal developments, inflation and economic conditions. Reserve amounts are necessarily based on management's estimates, and as other data becomes available, these estimates are revised, which may result in increases or decreases in existing case reserves. Barrett has engaged a nationally-recognized, independent actuary to periodically review the Company's total workers' compensation claims liability and reserving practices. Based in part on such review, the Company believes its total accrued workers' compensation claims liabilities are adequate. There can, however, be no assurance that the Company's actual future workers' compensation obligations will not exceed the amount of its accrued liabilities, with a corresponding negative effect on future earnings, due to such factors as unanticipated adverse loss development of known claims, and the effect, if any, of claims incurred but not reported.

Approximately one-third of the Company's payroll exposure associated with staffing or PEO services is in relatively high-risk industries with respect to workplace injuries, including trucking, logging, construction, and reforestation. A failure to successfully manage the severity and frequency of workers' compensation injuries will have a negative impact on the Company. In early 1995, the Company experienced a noticeable increase in workers' compensation costs arising out of the failure of some PEO clients to adhere to the Company's workplace safety policies. In response

10

to this increase, the Company hired additional workers' compensation loss control branch personnel. Also, management instituted clear guidelines for its branch managers, account managers, and loss control specialists directly tying their continued employment with the Company to their diligence in understanding and addressing the risks of accident or injury associated with the industries in which client companies operated and in monitoring the compliance by client with workplace safety requirements. The adoption of this policy of "zero tolerance" for avoidable workplace injuries resulted in the termination of more than 100 PEO client accounts.

#### Management Information System

The Company performs all functions associated with payroll administration through its internal management information system. Each branch performs payroll data entry functions and maintains an independent database of employees and customers, as well as payroll and invoicing records. All processing functions are centralized at Barrett's corporate headquarters in Portland, Oregon. Although the current system employed by the Company satisfactorily meets its current needs, the Company perceives an opportunity to significantly expand the capacity and capabilities necessary to accommodate its anticipated growth through the utilization of new software technologies. Accordingly, management has recently initiated a project to convert to new technologies which it anticipates will enable the Company to more effectively accommodate its anticipated growth, maintain a cost-effective and efficient processing structure, improve functionality, meet expected customer requirements for expanded communication capabilities, and provide additional customer services and information reporting. The Company's new system will utilize client-server technology, an existing software product from an independent software development company and a relational database environment. Management estimates the cost of implementing this project at approximately \$2.0 million. The new system is currently expected to be operational in late 1997.

#### Employees and Employee Benefits

At December 31, 1996, the Company had approximately 17,775 employees, including approximately 11,400 staffing services employees, approximately 6,100 PEO employees and approximately 275 managerial, sales and administrative employees. The number of employees at any given time may vary significantly due to business conditions at customer or client companies. Approximately 1% of the Company's employees are covered by a collective bargaining agreement. Each of Barrett's managerial, sales and administrative employees has entered into a standard form of employment agreement which, among other things, contains covenants not to engage in certain activities in competition with the Company for 18 months following termination of employment and to maintain the confidentiality of certain proprietary information. Barrett believes its employee relations are good.

Benefits offered to Barrett's staffing services employees include group health insurance, a Section 125 cafeteria plan which permits employees to use pretax earnings to fund various services, including medical, dental and childcare, and a Section 401(k) savings plan pursuant to which employees may begin making contributions upon reaching 21 years of age and completing 1,000 hours of service in any consecutive 12-month period. The Company may also make contributions to the savings plan, which vest over seven years and are subject

to certain legal limits, at the sole discretion of the Company's Board of Directors. Employees subject to a co-employer arrangement may participate in the Company's benefit plans, provided that the group health insurance premiums may, at the client's option, be paid by payroll deduction. See "Regulatory and Legislative Issues--Employee Benefit Plans".

## Regulatory and Legislative Issues

**Business Operations.** The Company is subject to the laws and regulations of the jurisdiction within which it operates, including those governing self-insured employers under the workers' compensation systems in Oregon, Washington, Maryland, Delaware, California, and the U.S. Department of Labor for USL&H workers. An Oregon PEO company, such as Barrett, is required to be licensed as a worker leasing company by the Workers' Compensation Division of the Oregon Department of Consumer and Business Services. Temporary staffing companies are expressly exempt from the Oregon licensing requirement. Oregon PEO companies are also required to ensure that each PEO client provides adequate training and supervision for its employees to comply with statutory requirements for workplace safety and to give 30 days' written notice in the event of a termination of its obligation to provide workers' compensation coverage for PEO employees and other subject employees of a PEO client. Although compliance with these requirements has caused Barrett to make certain changes in its PEO operations and contracts in Oregon, resulting in additional financial risk, particularly with respect to those clients who breach their payment obligation to the Company, such compliance has not had a material impact on Barrett's business, financial condition, or results of operations.

**Employee Benefit Plans.** The Company's operations are affected by numerous federal and state laws relating to labor, tax and employment matters. By entering into a co-employer relationship with employees who are assigned to work at client locations (sometimes referred to as "worksites employees"), the Company assumes certain obligations and responsibilities of an employer under these federal and state laws. Because many of these federal and state laws were enacted prior to the development of nontraditional employment relationships, such as professional employer, temporary employment, and outsourcing arrangements, many of these laws do not specifically address the obligations and responsibilities of nontraditional employers. In addition, the definition of "employer" under these laws is not uniform.

As an employer, the Company is subject to all federal statutes and regulations governing its employer-employee relationships. Subject to the issues discussed below, the Company believes that its operations are in compliance in all material respects with all applicable federal statutes and regulations.

The Company offers various employee benefit plans to its employees, including its worksite employees. These employee benefit plans include a savings plan (the "401(k) plan") under Section 401(k) of the Internal Revenue Code (the "Code"), a cafeteria plan under Code Section 125, a group health plan, a group life insurance plan, a group disability insurance plan and an employee assistance plan. Generally, employee benefit plans are subject to provisions of both the Code and the Employee Retirement Income Security Act ("ERISA"). In order to qualify for favorable tax treatment under the Code, qualified plans must be established and maintained by an employer for the exclusive benefit of its employees.

A definitive judicial interpretation of "employer" in the context of a PEO arrangement has not been established. The tax-exempt status of the Company's 401(k) plan and cafeteria plan is subject to continuing scrutiny and approval by the IRS and depends upon the Company's ability to establish the Company's employer-employee relationship with PEO employees. The issue of whether the Company's tax-qualified benefit plans can legitimately include worksite employees under their coverage has not yet been resolved. If the worksite employees cannot be covered by the plans, then the exclusive benefit requirement imposed by the Code would not be met by the plans as currently administered and the plans could be disqualified.

Leasing for the stated purpose of examining whether PEOs, such as the Company, are the employers of worksite employees under the Code provisions applicable to employee benefit plans and are, therefore, able to offer to worksite employees benefit plans that qualify for favorable tax treatment. The IRS Study Group is reportedly also examining whether the owners of client companies are employees of PEO companies under Code provisions applicable to employee benefit plans. To the best of the Company's knowledge, the Market Segment Study Group has not issued a report.

A PEO company headquartered in Texas has stated publicly that the IRS National Office is being requested by the IRS Houston District to issue a Technical Advice Memorandum ("TAM") on the PEO worksite employee issue in connection with an ongoing audit of a plan of the Texas PEO company. The stated purpose of TAMs is to help IRS personnel in closing cases and to establish and maintain consistent holdings. The IRS's position is that TAMs are not precedential; that is, they are limited to the particular taxpayer involved and that taxpayer's set of facts. The draft request for a TAM by the IRS Houston District reportedly states its determination that the Texas PEO company's Code Section 401(k) plan should be disqualified for the reason, among others, that it covers worksite employees who are not employees of the PEO company.

The timing and nature of the issuance and contents of any TAM regarding the worksite employee issue or any report of the Market Segment Study Group regarding Employee Leasing is unknown at this time. There has also been public discussion of the possibility that the Treasury Department may propose some form of administrative relief or that Congress may provide legislative resolution or clarification regarding this issue.

In the event the tax exempt status of the Company's benefit plans were to be discontinued and the benefit plans were to be disqualified, such actions could have a material adverse effect on the Company's business, financial condition, and results of operations. The Company is not presently able to predict the likelihood of disqualification nor the resulting range of loss, in light of the lack of public direction from the IRS or Congress.

#### Competition

The PEO and staffing services businesses are characterized by rapid growth and intense competition. The staffing services market includes competitors of all sizes, including several, such as Manpower, Inc., Kelly Services, Inc., The Olsten Corporation, Interim Services, Inc., and Adia Services, Inc., which are national in scope and have substantially greater financial, marketing, and other resources than the Company. In addition to national companies, Barrett competes with numerous regional and local firms for both customers and employees. The Company estimates that at least 100 firms provide staffing services in Oregon. There are relatively few barriers to entry into the staffing services business. The principal competitive factors in the staffing services industry are price, the ability to provide qualified workers in a timely manner and the monitoring of job performance. The Company attributes its internal growth in staffing services revenues to the cost-efficiency of its operations which permits the Company to price its services competitively, and to its ability through its branch office network to understand and satisfy the needs of its customers with competent personnel.

Although there are believed to be approximately 2,200 companies currently offering PEO service in the U.S., many of these potential competitors are located in states in which the Company presently does not operate. Barrett believes that there are at least 30 firms offering PEO services in Oregon, but the Company has the largest presence in the state. The Company may face additional competition in the future from new entrants to the field, including other staffing services companies,

payroll processing companies and insurance companies. Certain PEO companies operating in areas in which Barrett does not now, but may in the future, offer its services have greater financial and marketing resources than the Company, such as YourStaff, a subsidiary of Kelly Services, Inc., The Vincam Group Inc., Administaff, Inc. and Paychex, Inc., among others. Competition in the PEO industry is based largely on price, although service and quality are also important. Barrett believes that its growth in PEO services revenues is attributable to its ability to provide small and mid-sized companies with the opportunity to provide enhanced benefits to their employees while reducing their overall personnel administration and workers' compensation costs. The Company's competitive advantage may be adversely affected by a substantial increase in the costs of maintaining its self-insured workers' compensation program. A general market decrease in the level of workers' compensation insurance premiums may also decrease demand for PEO services.

## Item 2. PROPERTIES

The Company provides staffing and PEO services through all 24 of its branch offices. The following table shows the locations of the Company's branch offices and the year in which each branch was opened or acquired. The Company's Oregon branches accounted for 66% of its total revenues in 1996. The Company also leases office space in 21 other locations in its market areas which it uses to recruit and place employees.

<TABLE>  
<CAPTION>

Opened	Year Opened		Year or Acquired
	Oregon Locations -----	or Acquired -----	
--	<S>	<C>	<C>
	Portland (Industrial)	1984	Tucson, Arizona 1996
	Portland (Bridgeport)	1988	Sacramento, California 1988
	Bend	1990	Santa Clara, California 1994
	Medford	1990	Brea, California 1996
	Salem	1990	Goleta, California 1996
	Albany	1991	Ontario, California 1996
	Eugene	1991	Oxnard, California 1996
	Portland (Leasing)	1993	Los Angeles, California 1997
	Pendleton	1994	Boise, Idaho 1996
	Hood River	1996	Lutherville, Maryland 1951
	Tigard	1996	Easton, Maryland 1994
			Flint, Michigan 1997
			Spokane, Washington 1994

</TABLE>

The Company's corporate headquarters are located in an office building in Portland, Oregon, with approximately 9,200 square feet of office space. The building is subject to a mortgage loan with a principal balance of approximately \$598,000 at December 31, 1996.

The Company also owns another office building in Portland, Oregon, which houses its Portland/Bridgeport branch office. The building is subject to a mortgage loan with a principal balance at December 31, 1996, of approximately \$276,000 and has approximately 7,000 square feet of office space.

Barrett leases office space for its other branch offices. At December 31, 1996, such leases had expiration dates ranging from less than one year to seven years, with total minimum payments through 2001 of approximately \$2,205,000.

## Item 3. LEGAL PROCEEDINGS

A lawsuit was filed in the Circuit Court of the State of Oregon for the County of Multnomah on February 5, 1997, by Javier and Ester Munoz, husband and wife, against Asger M. Nielson, doing business as Nielson and Son ("Nielson"), Rain-Master Roofing, Inc. ("Rain-Master"), and the Company. Mr. Munoz was employed by the Company under a PEO arrangement with Rain-Master, which is in the roofing business. On February 1, 1995, Rain-Master was providing roofing services at a construction site for which Nielson was serving as general contractor. Mr. Munoz fell from the roof at the site in the course of his employment and is now a paraplegic as a result of the injuries he suffered. Until the filing of the lawsuit referred to above, Mr. Munoz's claim was being defended as a workers' compensation claim.

In the lawsuit, the plaintiffs are seeking damages in the amount of \$10,000,000 pursuant to claims for relief based on employer liability, intentional injury, product liability, negligence, breach of implied warranty and loss of consortium. Defense of the lawsuit has been tendered to the

umbrella liability insurance carriers; acceptance of the defense to the claim has not yet been received. Management intends to vigorously defend this action on the basis, among others, that workers' compensation is the exclusive remedy for employees injured in the course of employment. Under appropriate circumstances, the Company also may seek to enforce its contractual right to indemnification from Rain-Master pursuant to its PEO leasing arrangement. Based upon its investigation and analysis to date, management believes that the outcome of this proceeding will not have a materially adverse effect on the Company's financial position or results of operations.

On March 12, 1997, a Notice of Intent to Revoke Farm/Forest Labor Contractor License and to Assess Civil Penalties (the "Notice") was served on the Company by the Bureau of Labor and Industries of the State of Oregon (the "Bureau"). The Notice also names Daniel A. Hatfield, an employee of the Company. The Notice proposes to assess civil penalties in the amount of \$488,000, based on the numbers of workers allegedly affected, for alleged noncompliance with various duties imposed on farm labor contractors by Oregon law, including licensing violations, failure to comply with wage payment laws, and failure to maintain and to provide workers and the Bureau with required documentation. Management intends to vigorously contest the claims asserted in the Notice and is in the process of collecting and analyzing data necessary to defend its position and to evaluate the probable outcome of the proceedings.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of the Company's stockholders during the fourth quarter of 1996.

EXECUTIVE OFFICERS OF THE REGISTRANT

The following table identifies, as of February 28, 1997, each executive officer of the Company. Executive officers are elected annually and serve at the discretion of the Board of Directors.

<TABLE>  
<CAPTION>

Name	Age	Principal Positions and Business Experience	Officer Since
<S> William W. Sherertz	<C> 51	<C> President; Chief Executive Officer; Director	<C> 1980
Michael D. Mulholland	45	Vice President-Finance and Secretary; Chief Financial Officer	1994
Michael K. Barrett	33	Vice President-Business Development	1995
K. Risa Olsen	46	Vice President	1997
James D. Miller	33	Controller, Principal Accounting Officer	1994

</TABLE>

William W. Sherertz has acted as Chief Executive Officer of the Company since 1980. He has also been a director of the Company since 1980, and was appointed President of the Company in March 1993. Mr. Sherertz also serves as Chairman of the Board of Directors.

Michael D. Mulholland joined the Company in August 1994 as Vice President-Finance and Secretary. From 1988 to 1994, Mr. Mulholland was employed by Sprouse-Reitz Stores Inc., a former Nasdaq-listed retail company, serving as its Executive Vice President, Chief Financial Officer and Secretary. In November 1991, Sprouse-Reitz filed a voluntary petition under Chapter 11 of the U.S. Bankruptcy Code. Its plan of

reorganization was confirmed by the Bankruptcy Court in June 1992. Subsequently, Mr. Mulholland was appointed to the additional position of Acting Chief Executive Officer prior to Sprouse's filing of a voluntary petition in connection with a prepackaged liquidating Chapter 11 in November 1993. He is a certified public accountant on inactive status.

Michael K. Barrett joined the Company as Vice President-Business Development in December 1995. Prior to joining the Company, Mr. Barrett was Vice President of Marketing for YourStaff, Inc., a PEO subsidiary of Kelly Services,

Inc., from May 1994 to December 1995. From November 1989 to May 1994, Mr. Barrett owned and operated an advertising firm.

K. Risa Olsen rejoined the Company in April 1996 as National Accounts Manager. Ms. Olsen was elected Vice President in January 1997. Prior to rejoining Barrett, she was a self-employed Area Director for The Worth Collection, Ltd., a national privately-held direct marketer of women's apparel, from November 1994 to March 1996. From January 1993 to October 1994, Ms. Olsen owned and operated a marketing organization for various manufacturers of women's apparel. Prior to 1993, Ms. Olsen was employed by The John H. Harland Co., a publicly-held provider of checks, forms, and business documents to financial institutions, as a District Manager. Ms. Olsen was previously employed by the Company from 1976 to 1981.

James D. Miller joined the Company in January 1994 as Controller. From 1991 to 1994, he was the Corporate Accounting Manager for Christensen Motor Yacht Corporation. Mr. Miller, a certified public accountant on inactive status, was employed by Price Waterhouse LLP from 1987 to 1991.

There are no family relationships among any of the above listed officers.

PART II

Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's common stock (the "Common Stock") trades on the Nasdaq National Market tier of The Nasdaq Stock Market under the symbol "BBSI." At February 28, 1997, there were 70 stockholders of record and approximately 2,200 beneficial owners of the Common Stock. The Company has not declared or paid any cash dividends since the closing of its initial public offering of Common Stock on June 18, 1993, and has no present plan to pay any cash dividends in the foreseeable future. The following table presents the high and low sales prices of the Common Stock for each quarterly period during the last two fiscal years, as reported by The Nasdaq Stock Market:

1995	High	Low
----	-----	----
First Quarter	\$19.50	\$13.50
Second Quarter	15.00	10.50
Third Quarter	15.75	13.50
Fourth Quarter	15.50	12.25
1996		
----		
First Quarter	\$20.75	\$14.50
Second Quarter	20.00	16.25
Third Quarter	22.25	14.00
Fourth Quarter	17.50	13.50

During 1996, the Company issued equity securities without registration under the Securities Act of 1933, in each case in reliance upon the exemption from registration set forth in Section 4(2) of the Securities Act of 1933 regarding transactions by an issuer not involving a public offering, as follows:

On April 1, 1996, the Company issued 157,464 shares of Common Stock to the seller in connection with its purchase of certain assets and the business of StaffAmerica, Inc., valued at \$2,795,000, as well as 1,690 shares of Common Stock valued at \$17.75 per share to the two owners of StaffAmerica, Inc., in exchange for their covenants not to compete.

On April 8, 1996, the Company issued 20,446 shares of Common Stock to the seller in connection with the Company's purchase of certain assets and the business of JobWorks Agency, Inc., valued at \$380,000.

Item 6. SELECTED FINANCIAL DATA

The following selected financial data should be read in conjunction with the Company's financial statements and the accompanying notes presented in Item 8 of this report.

<TABLE>  
<CAPTION>

Years Ended December 31,

	1996	1995	1994	1993
1992				
(In thousands, except per share data)				
Statement of Operations Data:				
Revenues:				
<S> <C>	<C>	<C>	<C>	<C>
<C>				
Staffing services.....	\$ 113,539	\$ 99,233	\$ 71,148	\$ 41,755
\$ 34,681				
Professional employer services.....	102,277	80,572	69,404	58,512
45,444				
Total.....	215,816	179,805	140,552	100,267
80,125				
Cost of revenues:				
Direct payroll costs.....	164,180	136,174	105,515	75,171
59,820				
Payroll taxes and benefits.....	19,913	16,088	12,758	9,911
7,826				
Workers' compensation.....	5,938	6,073	5,069	4,591
3,233				
Safety incentives.....	1,532	981	1,103	598
651				
Total.....	191,563	159,316	124,445	90,271
71,530				
Gross margin.....	24,253	20,489	16,107	9,996
8,595				
Selling, general, and administrative expenses...	16,034	13,657	10,302	6,450
6,003				
Amortization of intangibles.....	820	564	430	370
336				
Income from operations.....	7,399	6,268	5,375	3,176
2,256				
Other (expense) income:				
Interest expense.....	(82)	(75)	(106)	(86)
(77)				
Interest income.....	534	400	224	161
70				
Other, net.....	--	32	78	133
26				
Total.....	452	357	196	208
19				
Income before provision for income taxes.....	7,851	6,625	5,571	3,384
2,275				
Provision for income taxes(1).....	2,815	2,507	2,105	437
--				
Net income.....	\$ 5,036	\$ 4,118	\$ 3,466	\$ 2,947
\$ 2,275				
Net income per share.....	\$ .73	\$ .62	\$ .53	
Unaudited pro forma data(1):				
Net income.....				\$ 2,060
\$ 1,385				
Net income per share(2).....				\$ .39
\$ .35				

Weighted average common shares outstanding(2)...	6,935	6,680	6,591	5,260
4,000	=====	=====	=====	=====

-----  
As of December 31,  
-----

	1996	1995	1994	1993
1992	-----	-----	-----	-----

	(In thousands)			
Selected Balance Sheet Data:				
Working capital (deficit).....	\$ 11,557	\$ 8,417	\$ 4,889	\$ 7,017
\$ (678)				
Total assets.....	42,646	31,273	24,665	18,425
7,219				
Long-term debt, net of current portion.....	838	875	908	946
292				
Stockholders' equity.....	25,562	20,034	14,455	10,480
1,574				

</TABLE>

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- (1) Effective July 1, 1987, the Company elected to be treated as a corporation subject to taxation under Subchapter S of the Internal Revenue Code, pursuant to which the net earnings of the Company were taxed directly to the Company's stockholders rather than to the Company. The Company terminated its election on April 30, 1993, and recognized a cumulative net deferred tax asset of \$505,000. The amounts shown reflect a pro forma tax provision as if the Company had been a Subchapter C corporation subject to income taxes for all periods presented.
- (2) All share and per share amounts have been restated to reflect the 2-for-1 stock split effective May 23, 1994.

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

The Company's revenues consist of staffing services and professional employer organization ("PEO") services. Staffing services revenues consist of short-term staffing, contract staffing, payrolling and on-site management. PEO services refer exclusively to co-employer contractual agreements with PEO clients. The Company's revenues represent all amounts billed to customers for direct payroll, related employment taxes, workers' compensation coverage, all other pass-through costs such as health care insurance, and a service fee (equivalent to a mark-up percentage). The Company's Oregon branches accounted for 66% of its total revenues in 1996, and an additional 22% was derived from its branches in California and Washington. Consequently, weakness in economic conditions on the West Coast could have a material adverse effect on the Company's financial results.

The Company's cost of revenues is comprised of direct payroll costs, payroll taxes and benefits, workers' compensation and safety incentives. Direct payroll costs represent the gross payroll earned by employees based on salary or hourly wages. Payroll taxes and benefits consist of the employer's portion of Social Security and Medicare taxes, federal unemployment taxes, state unemployment taxes, health care insurance and employee reimbursements for materials, supplies and other expenses which are passed through to the customer. Workers' compensation expense consists primarily of the costs associated with the Company's self-insured workers' compensation program, such as claims reserves, claims administration fees, legal fees, state and federal administrative agency fees and reinsurance costs for catastrophic injuries. The Company also maintains a large-deductible workers' compensation insurance policy for employees working in states where the Company is not currently self-insured. Safety incentives represent cash incentives paid to certain PEO client companies as a reward for maintaining safe work practices in order to minimize workplace injuries. The incentive is based on a percentage of annual payroll and is paid annually to customers who meet prearranged loss parameters.

The largest portion of workers' compensation expense is the cost of workplace injury claims. When an injury occurs and is reported to the Company, the Company's respective independent third-party claims administrator ("TPA") analyzes the details of the injury and develops a case reserve, which is the



TPA's estimate of the cost of the claim based on similar injuries and its professional judgment. The Company then records, or accrues, an expense and a corresponding liability based upon the TPA's estimates for claims reserves. As cash payments are made by the Company's TPA against specific case reserves, the accrued liability is reduced by the corresponding payment amount. The TPA also reviews existing injury claims on an on-going basis and adjusts the case reserves as new or additional information for each claim becomes available. The Company has established an additional IBNR reserve to provide for future unanticipated increases in expenses ("adverse loss development") of the claims reserves for open injury claims and for claims incurred but not reported related to prior and current periods. Management believes that the Company's internal claims reporting system minimizes the occurrence of unreported incurred claims.

Selling, general and administrative expenses represent both branch and corporate operating expenses. Branch operating expenses consist primarily of branch office staff payroll and payroll related costs, advertising, rent, office supplies, depreciation and branch incentive compensation. Branch incentive compensation represents a combined 15% of branch pre-tax profits, of which 10% is paid to the branch manager and 5% is shared among the office staff. Corporate operating

20

expenses consist primarily of executive and office staff payroll and payroll related costs, professional and legal fees, travel, depreciation, advertising and executive and corporate staff incentive bonuses.

Amortization of intangibles consists primarily of the amortization of the costs of acquisitions in excess of the fair value of net assets acquired (goodwill). The Company uses a 15-year estimate as the useful life of goodwill, as compared to the 40-year maximum permitted by generally accepted accounting principles, and amortizes such cost using the straight-line method. Other intangible assets, such as customer lists and covenants not to compete, are amortized using the straight-line method over their estimated useful lives, which range from two to 15 years.

#### Forward-Looking Information

Statements in this Item or in Item 1 of this report which are not historical in nature, including discussion of economic conditions in the Company's market areas, the potential for and effect of future acquisitions, the effect of changes in the Company's mix of services on gross margin, the adequacy of the Company's workers' compensation reserves, the tax-qualified status of the Company's 401(k) savings plan, and the availability of financing and working capital to meet the Company's funding requirements, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors with respect to the Company include difficulties associated with integrating acquired businesses and clients into the Company's operations, economic trends in the Company's service areas, uncertainties regarding government regulation of PEOs, including the possible adoption by the IRS of an unfavorable position as to the tax-qualified status of employee benefit plans maintained by PEOs, future workers' compensation claims experience, and the availability of and costs associated with potential sources of financing. The Company disclaims any obligation to update any such factors or to publicly announce the result of any revisions to any of the forward-looking statements contained herein to reflect future events or developments.

#### Results of Operations

The following table sets forth the percentages of total revenues represented by selected items in the Company's Statements of Operations for the years ended December 31, 1996, 1995 and 1994, included in Item 8 of this report. References to the Notes to Financial Statements appearing below are to the notes to the Company's financial statements included in Item 8 of this report.

21

<TABLE>  
<CAPTION>

Percentage of Total Revenues

	Years Ended December 31,		
	1996	1995	
1994	-----	-----	---
<S>	<C>	<C>	<C>
Revenues:			
Staffing services.....	52.6%	55.2%	
50.6% Professional employer services.....	47.4	44.8	49.4
	-----	-----	---
Total revenues.....	100.0	100.0	
	-----	-----	---
Cost of revenues:			
Direct payroll costs.....	76.1	75.7	75.1
Payroll taxes and benefits.....	9.2	8.9	9.1
Workers' compensation.....	2.8	3.4	3.6
Safety incentives.....	.7	.6	
.8	-----	-----	---
Total cost of revenues.....	88.8	88.6	
	-----	-----	---
Gross margin.....	11.2	11.4	11.4
Selling, general and administrative expenses.....	7.4	7.6	7.3
Amortization of intangibles.....	.4	.3	.3
	-----	-----	---
Income from operations.....	3.4	3.5	3.8
Other income (expense).....	.2	.2	.2
	-----	-----	---
Pretax income.....	3.6	3.7	4.0
Provision for income taxes.....	1.3	1.4	1.5
	-----	-----	---
Net income.....	2.3	2.3	2.5
	=====	=====	
=====			
</TABLE>			

Years Ended December 31, 1996 and 1995

Net income for 1996 amounted to \$5,036,000, an increase of \$918,000 or 22.3% over 1995 net income of \$4,118,000. The increase in 1996 net income over 1995 was primarily due to continued growth in revenues and gross margin, which was offset in part by increased selling, general and administrative expenses. Net income per share for 1996 was \$.73 as compared to \$.62 for 1995.

Total 1996 revenues were \$215,816,000, which represented an increase of \$36,011,000 or 20.0% over 1995 revenues of \$179,805,000. The increase in revenues over 1995 was primarily due to a 1996 internal growth rate of 10.6%, coupled with the acquisition of five staffing and PEO businesses during 1996. Professional employer (staff leasing) services revenue increased 26.9% over 1995 due to the growth in the number of new PEO clients, primarily in Oregon and California. The growth in PEO services revenue was a result of internal sales efforts coupled with the acquisitions made during the year. These factors contributed to the increased mix of PEO services for 1996 to 47.4% of total revenues, up from 44.8% of total revenues for 1995. Revenues from staffing services, as a percent of total revenues, declined in 1996 to 52.6% as compared to 55.2% of total revenues in 1995, despite a 14.4% growth rate over 1995.

Subsequent to December 31, 1996, the Company closed its branch offices in Seattle, Washington and Phoenix, Arizona. Management expects to relocate the Seattle operations to Tacoma, Washington in connection with a new customer base in the south Puget Sound area. The Phoenix office, which opened during the third quarter of 1996 and represented the Company's first office in Arizona, has recently been transferred to the expanding operations of the Company's Tucson, Arizona office opened shortly thereafter. During the first quarter of 1997, the Company opened an office in Flint, Michigan to support a new large contract staffing arrangement involving two processing facilities of an existing customer.

Gross margin for 1996 totaled \$24,253,000, representing an increase of \$3,764,000 or 18.4% over 1995. The gross margin rate of 11.2% of revenues represents a 20 basis point decrease from 1995 due to slight increases in direct payroll costs and payroll taxes and benefits offset in part by a decrease in workers' compensation expense as a percentage of revenues. The Company expects gross margin to continue to decline as a percentage of revenues due to the continued growth in PEO services, contract staffing and on-site management in the Company's service mix and the Company's decision to maintain its workers' compensation IBNR reserve at a higher level relative to claims, as discussed below.

The following table summarizes certain indicators of performance regarding the Company's self-insured workers' compensation program by quarter for 1996 and 1995.

<TABLE>  
<CAPTION>

Self-Insured Workers' Compensation Profile

Reserve" (1)	No. of Injury Claims		Total Workers' Comp Expense (in thousands)		Total Workers' Comp Expense as a % of Total Payroll		"IBNR as a % of "At Risk
	1996	1995	1996	1995	1996	1995	1996
1995							
<S>	<C>	<C>	<C>	<C>	<C>	<C>	<C>
Q1	193	266	\$ 770	\$2,307	2.4%	7.8%	41.0%
33.0%							
Q2	312	309	1,213	1,707	3.1	5.1	41.0
40.6							
Q3	401	287	2,161	1,160	4.7	3.1	41.0
40.9							
Q4	422	270	1,794	899	3.9	2.5	55.9
41.0							
For the Year	1,328	1,132	\$5,938	\$6,073	3.6	4.5	
	=====	=====	=====	=====			

- (1) "IBNR Reserve" in this context is defined as an additional expense provision for both the unexpected future adverse loss development of open claims and for claims incurred but not reported.
- (2) "At Risk Claims" are defined as the dollar amount of all injury claims submitted under self-insured payroll less amounts covered by excess reinsurance.

</TABLE>

Although workers' compensation expense for the third and fourth quarters of 1996 was higher than in the comparable quarters of 1995, the preceding table illustrates the 1996 improvement over 1995 in the Company's total workers' compensation expense both in terms of total dollars and as a percent of total payroll dollars. Concurrent with the improved expense level and percentage of workers' compensation expense, expressed as a percent of total payroll, the Company has increased its IBNR reserve to 55.9% of "at risk claims" as of December 31, 1996. It is management's objective to continue to increase the dollar value of the Company's IBNR reserve, which is a component of the total accrued workers' compensation claims liabilities recorded on the balance sheet. The IBNR reserve expressed as a percentage reflects the relationship between the dollar value of the IBNR reserve and the dollar value of all reserves for open or at risk claims less reserve amounts covered by excess reinsurance policies. Costs attributable to adverse loss development of open claims, claims incurred in a prior period but reported currently, and catastrophic events may be shifted from the IBNR reserve to a specific case reserve, thereby reducing the IBNR reserve level. Accordingly, there can be no assurance that the IBNR reserve will remain at its present level or at any future level.

Selling, general and administrative expenses consist of compensation and other expenses incident to the operation of the Company's headquarters and branch offices and marketing of its services. These expenses (excluding the amortization of intangibles) amounted to \$16,034,000 or 7.4% of revenues for 1996, as compared to \$13,657,000 or 7.6% of revenues for 1995. The increase in total dollars for 1996 was primarily due to additional branch office staff resulting from the five acquisitions made during the year.

Amortization of intangibles totaled \$820,000 for 1996 or .4% of revenues which compares to \$564,000 or .3% of revenues for 1995. The increased amortization expense for 1996 was primarily attributable to amortization arising from the five acquisitions made during the year.

The Company offers various employee benefit plans to its employees, including its worksite employees. These employee benefit plans include a savings plan (the "401(k) plan") under Section 401(k) of the Internal Revenue Code (the "Code"), a cafeteria plan under Code Section 125, a group health plan, a group life insurance plan, a group disability insurance plan and an employee assistance plan. Generally, employee benefit plans are subject to provisions of both the Code and the Employee Retirement Income Security Act ("ERISA"). In order to qualify for favorable tax treatment under the Code, qualified plans must be established and maintained by an employer for the exclusive benefit of its employees.

A definitive judicial interpretation of "employer" in the context of a PEO arrangement has not been established. The tax-exempt status of the Company's 401(k) plan and cafeteria plan is subject to continuing scrutiny and approval by the IRS and depends upon the Company's ability to establish the Company's employer-employee relationship with PEO employees. The issue of whether the Company's tax-qualified benefit plans can legitimately include worksite employees under their coverage has not yet been resolved. If the worksite employees cannot be covered by the plans, then the exclusive benefit requirement imposed by the Code would not be met by the plans as currently administered and the plans could be disqualified.

The IRS has established a Market Segment Study Group regarding Employee Leasing for the stated purpose of examining whether PEOs, such as the Company, are the employers of worksite employees under the Code provisions applicable to employee benefit plans and are, therefore, able to offer to worksite employees benefit plans that qualify for favorable tax treatment. The IRS Study Group is reportedly also examining whether the owners of client companies are employees of PEO companies under Code provisions applicable to employee benefit plans. To the best of the Company's knowledge, the Market Segment Study Group has not issued a report.

A PEO company headquartered in Texas has stated publicly that the IRS National Office is being requested by the IRS Houston District to issue a Technical Advice Memorandum ("TAM") on the PEO worksite employee issue in connection with an ongoing audit of a plan of the Texas PEO company. The stated purpose of TAMs is to help IRS personnel in closing cases and to establish and maintain consistent holdings. The IRS's position is that TAMs are not precedential; that is, they are limited to the particular taxpayer involved and that taxpayer's set of facts. The draft request for a TAM by the IRS Houston District reportedly states its determination that the Texas PEO company's Code Section 401(k) plan should be disqualified for the reason, among others, that it covers worksite employees who are not employees of the PEO company.

The timing and nature of the issuance and contents of any TAM regarding the worksite employee issue or any report of the Market Segment Study Group regarding Employee Leasing is unknown at this time. There has also been public discussion of the possibility that the Treasury Department may propose some form of administrative relief or that Congress may provide legislative resolution or clarification regarding this issue.

In the event the tax exempt status of the Company's benefit plans were to be discontinued and the benefit plans were to be disqualified, such actions could have a material adverse effect on the Company's business, financial condition, and results of operations. The Company is not presently able to predict the likelihood of disqualification nor the resulting range of loss, in light of the lack of public direction from the IRS or Congress.

Years Ended December 31, 1995 and 1994

Net income for 1995 amounted to \$4,118,000, an increase of \$652,000 or 18.8% over 1994 net income of \$3,466,000. The increase in 1995 net income over 1994 was primarily due to continued growth in revenues and gross margin, which

was offset in part by increased selling, general and administrative expenses. Net income per share for 1995 was \$.62 as compared to \$.53 for 1994.

Total 1995 revenues were \$179,805,000, which represented an increase of \$39,253,000 or 27.9% over 1994 revenues of \$140,552,000. The increase in revenues in 1995 over 1994 was primarily due to a 1995 internal growth rate of 20.3%, coupled with the acquisition of four staffing services businesses during the 1995 third quarter. Such acquisitions and continued growth of staffing services in northern California were the principal factors which contributed to the increased mix of staffing services for 1995 to 55.2% of total revenues, up from 50.6% of total revenues for 1994. Revenues from PEO services, as a percent of total revenues, declined in 1995 to 44.8% as compared to 49.4% of total revenues in 1994, despite a 16.1% growth rate over 1994.

Gross margin for 1995 totaled \$20,489,000, representing an increase of \$4,382,000 or 27.2% over 1994. The gross margin rate of 11.4% of revenues, however, remained unchanged from 1994 due to a slight increase in direct payroll costs, offset by decreases in payroll taxes and benefits, workers' compensation and safety incentive expenses, as a percent of revenues.

Workers' compensation expense was lower in terms of total dollars and, more importantly, as a percent of total payroll dollars in the second half of 1995 compared to the prior year, as a result of actions taken by management in early 1995 to enhance the Company's monitoring of safe-work practices and to terminate its co-employer relationship with client companies that did not conform to Barrett's business philosophies and operating standards. Concurrent with the improved expense level and percentage of workers' compensation expense, expressed as a percent of total payroll, the Company increased its IBNR reserve for future adverse claim development and claims incurred but not reported from 37.0% of "at risk claims" at December 31, 1994, to 41.0% at December 31, 1995.

Selling, general and administrative expenses (excluding the amortization of intangibles) amounted to \$13,657,000 or 7.6% of revenues for 1995, as compared to \$10,302,000 or 7.3% of revenues for 1994. The increase for 1995 was primarily due to additional branch office staff added to support the increased business activity and additional workers' compensation loss control branch personnel to enhance the administration of the Company's self-insured workers' compensation program.

Amortization of intangibles totaled \$564,000 or .3% of revenues for 1995 which compares to \$430,000 or .3% of revenues for 1994. The increase in amortization in 1995 was attributable to the two acquisitions made during the year.

#### Fluctuations in Quarterly Operating Results

The Company has historically experienced significant fluctuations in its quarterly operating results and expects such fluctuations to continue in the future. The Company's operating results may fluctuate due to a number of factors such as seasonality, wage limits on payroll taxes, claims experience for workers' compensation, demand and competition for the Company's services, and the effect of acquisitions. The Company's revenue levels fluctuate from quarter to quarter primarily

due to the impact of seasonality in its staffing services business and on certain of its PEO clients in the agriculture and forest products-related industries. As a result, the Company may have greater revenues and net income in the third and fourth quarters of its fiscal year. Payroll taxes and benefits fluctuate with the level of direct payroll costs but may tend to represent a smaller percentage of revenues later in the Company's fiscal year as federal and state statutory wage limits for unemployment and social security taxes are exceeded by employees. Workers' compensation expense varies with both the frequency and severity of workplace injury claims reported during a quarter, as well as adverse loss development of prior period claims during the current quarter.

#### Liquidity and Capital Resources

The Company's net cash position of \$1,901,000 at December 31, 1996 decreased \$1,317,000 from year-end 1995. The decrease was primarily due to cash used to acquire five staffing and PEO businesses and funds used for net purchases of restricted marketable securities, offset in part by cash provided by operating activities.

Net cash provided by operating activities for 1996 amounted to \$2,208,000 as compared to \$2,496,000 for 1995. For 1996, the cash flow generated by net income and increases in accrued payroll and related benefits was offset

in part by a \$5,834,000 increase in accounts receivable. The increase in 1996 year-end accounts receivable over 1995 was the result of higher sales levels, the acquisition of five staffing and PEO businesses and an increase in the number of days' sales in receivables from 28 days in 1995 to 29 days at December 31, 1996.

Net cash used by investing activities totaled \$3,603,000 for 1996, which compares to \$2,011,000 for 1995. During 1996, the Company paid \$1,519,000 in cash in connection with five acquisitions and had net purchases of \$1,026,000 of restricted marketable securities to satisfy various state and federal self-insured workers' compensation surety deposit requirements. During 1995, the Company paid \$1,199,000 in cash in connection with two acquisitions and purchased \$443,000 in marketable securities. Capital expenditures for 1996, consisting principally of office equipment and software, totaled \$1,058,000. The Company presently has no material long-term capital commitments.

Net cash provided by financing activities for 1996 totaled \$78,000 which compares to \$519,000 for 1995. The principal source of cash provided by financing activities in 1996 arose from the exercise of employee incentive stock options. During 1995, warrants were exercised by underwriters to purchase 110,000 shares of the Company's Common Stock at \$4.20 per share. Such warrants were received by the Company's underwriters in connection with its June, 1993 initial public offering of Common Stock. As of the date of this filing, an underwriter continues to hold warrants to purchase 90,000 shares of Common Stock at \$4.20 per share. The unexercised warrants expire on June 10, 1998.

The Company has an unsecured \$4.0 million revolving credit facility of which there was no outstanding balance at December 31, 1996. See Note 7 of the Notes to Financial Statements. Management believes that the credit facility and other potential sources of financing, together with anticipated funds generated from operations, will be sufficient in the aggregate to fund the Company's working capital needs for the foreseeable future.

#### Inflation

Inflation generally has not been a significant factor in the Company's operations during the periods discussed above. The Company has taken into account the impact of escalating medical and other costs in establishing reserves for future expenses for self-insured workers' compensation claims.

#### Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

(a) The following audited financial statements of Barrett Business Services, Inc., and related documents are set forth herein on the pages indicated:

<TABLE>  
<CAPTION>

#### Page

<S>	
<C>	
Report of Independent Accountants.....	29
Balance Sheets at December 31, 1996 and 1995.....	30
Statements of Operations for the years ended December 31, 1996, 1995, and 1994.....	31
Statements of Redeemable Common Stock and Nonredeemable Stockholders' Equity for the years ended December 31, 1996, 1995, and 1994.....	32

Statements of Cash Flows for the years ended  
December 31, 1996, 1995, and 1994 .....  
33

Notes to Financial Statements .....  
34

</TABLE>

Other financial statement schedules are omitted because they are not applicable or not required.

REPORT OF INDEPENDENT ACCOUNTANTS

February 4, 1997

To the Stockholders and Board of Directors of  
Barrett Business Services, Inc.

In our opinion, the accompanying balance sheets and the related statements of operations, of redeemable common stock and nonredeemable stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Barrett Business Services, Inc. at December 31, 1996 and 1995, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1996 in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

/s/ Price Waterhouse LLP

Portland, Oregon

BARRETT BUSINESS SERVICES, INC.  
BALANCE SHEETS  
(IN THOUSANDS)

<TABLE>  
<CAPTION>

	DECEMBER 31,	
	1996	1995
	-----	-----
ASSETS		
<S>	<C>	<C>
Current assets:		
Cash and cash equivalents	\$ 1,901	\$ 3,218
Trade accounts receivable, net	19,057	13,151
Note receivable (Note 2)	324	-
Prepaid expenses and other	914	478
Deferred tax assets (Note 12)	1,279	937
	-----	-----
Total current assets	23,475	17,784
Intangibles, net (Note 4)	10,226	6,452
Property and equipment, net (Notes 5 and 8)	3,111	2,261

Restricted marketable securities and workers' compensation deposits (Note 6)	5,707	4,681
Other assets	127	95
	-----	-----
	\$ 42,646	\$ 31,273
	=====	=====
LIABILITIES, REDEEMABLE COMMON STOCK AND NONREDEEMABLE STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt (Notes 8 and 11)	\$ 36	\$ 33
Accounts payable	667	378
Accrued payroll, payroll taxes and related benefits	7,960	5,797
Accrued workers' compensation claim liabilities (Note 6)	2,240	2,383
Customer safety incentives payable	1,015	776
	-----	-----
Total current liabilities	11,918	9,367
Long-term debt, net of current portion (Notes 8 and 11)	838	875
Customer deposits	890	675
Long-term workers' compensation liabilities (Note 6)	613	322
	-----	-----
	14,259	11,239
Commitments and contingencies (Notes 9, 10 and 15)		
Redeemable common stock, \$.01 par value; 159 shares issued and outstanding at December 31, 1996 (Note 13)	2,825	-
	-----	-----
Nonredeemable stockholders' equity:		
Common stock, \$.01 par value; 20,500 shares authorized, 6,625 and 6,551 shares issued and outstanding (Notes 13 and 14)	66	66
Additional paid-in capital	10,929	10,437
Retained earnings	14,567	9,531
	-----	-----
	25,562	20,034
	-----	-----
	\$ 42,646	\$ 31,273
	=====	=====

The accompanying notes are an integral part of these financial statements.

</TABLE>

BARRETT BUSINESS SERVICES, INC.  
STATEMENTS OF OPERATIONS  
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

<TABLE>  
<CAPTION>

	YEAR ENDED DECEMBER 31,		
	1996	1995	1994
	-----	-----	-----
<S>	<C>	<C>	<C>
Revenues:			
Staffing services	\$ 113,539	\$ 99,233	\$ 71,148
Professional employer services	102,277	80,572	69,404
	-----	-----	-----
	215,816	179,805	140,552
	-----	-----	-----
Cost of revenues:			
Direct payroll costs	164,180	136,174	105,515
Payroll taxes and benefits	19,913	16,088	12,758
Workers' compensation (Note 6)	5,938	6,073	5,069
Safety incentives	1,532	981	1,103
	-----	-----	-----
	191,563	159,316	124,445
	-----	-----	-----
Gross margin	24,253	20,489	16,107
Selling, general and administrative expenses	16,034	13,657	10,302



Amortization of intangibles (Note 4)	820	564	430
Income from operations	7,399	6,268	5,375
Other (expense) income:			
Interest expense	(82)	(75)	(106)
Interest income	534	400	224
Other, net	-	32	78
	452	357	196
Income before provision for income taxes	7,851	6,625	5,571
Provision for income taxes (Note 12)	2,815	2,507	2,105
Net income	\$ 5,036	\$ 4,118	\$ 3,466
Net income per share	\$ .73	\$ .62	\$ .53
Weighted average number of shares outstanding	6,935	6,680	6,591

The accompanying notes are an integral part of these financial statements.

</TABLE>

31

BARRETT BUSINESS SERVICES, INC.  
STATEMENTS OF REDEEMABLE COMMON STOCK AND  
NONREDEEMABLE STOCKHOLDERS' EQUITY  
(IN THOUSANDS)

<TABLE>  
<CAPTION>

	NONREDEEMABLE STOCKHOLDERS' EQUITY					
	REDEEMABLE COMMON STOCK		COMMON STOCK		ADDITIONAL	RETAINED
TOTAL	SHARES	AMOUNT	SHARES	AMOUNT	PAID-IN CAPITAL	EARNINGS
	-----	-----	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>	<C>	<C>
<C>						
Balance, December 31, 1993	-	\$ -	3,152	\$ 32	\$ 8,469	\$ 1,979
\$ 10,480						
Common stock issued for acquisitions			29		468	
468						
Common stock issued on exercise						
of options			22		41	
41						
Net income						3,466
3,466						
Reclassification of retained earnings						
for stock split	-			3,164	32	
(32)						
	-----	-----	-----	-----	-----	-----
- -						
Balance, December 31, 1994	-	-	6,367	64	8,978	5,413
14,455						
Common stock issued for acquisitions			67	1	910	
911						
Common stock issued on exercise						
of options and warrants			124	1	549	

550						
Net income						4,118
4,118						
Contribution of common stock (Note 11)			(7)			
-						
-----						
Balance, December 31, 1995 20,034	-	-	6,551	66	10,437	9,531
Common stock issued for acquisitions 380	159	2,825	20		380	
Common stock issued on exercise of options, net 112			54		112	
Net income 5,036						5,036
-----						
Balance, December 31, 1996 \$ 25,562	159	\$ 2,825	6,625	\$ 66	\$ 10,929	\$ 14,567
=====						

The accompanying notes are an integral part of these financial statements.

</TABLE>

BARRETT BUSINESS SERVICES, INC.  
STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)

<TABLE>  
<CAPTION>

	YEAR ENDED DECEMBER 31,		
	1996	1995	1994
	<C>	<C>	<C>
<S>			
Cash flows from operating activities:			
Net income \$	5,036	\$ 4,118	\$ 3,466
Reconciliation of net income to net cash provided by operating activities:			
Depreciation and amortization	1,126	812	637
Gain on sales of marketable securities	-	(42)	-
Deferred taxes	(342)	(23)	(20)
Changes in certain assets and liabilities, net of amounts purchased in acquisitions:			
Trade accounts receivable, net	(5,834)	(3,520)	(4,677)
Prepaid expenses and other	(436)	121	(454)
Income taxes payable	-	-	(79)
Accounts payable	289	160	127
Accrued payroll, payroll taxes and related benefits	2,163	740	1,834
Accrued workers' compensation claim liabilities	148	183	88
Customer safety incentives payable	239	(29)	278
Customer deposits, other liabilities and other assets, net	(181)	(24)	115
Net cash provided by operating activities	2,208	2,496	1,315
Cash flows from investing activities:			
Cash paid for acquisitions, including other direct costs	(1,519)	(1,199)	(4,870)
Purchases of fixed assets, net of amounts purchased in acquisitions	(1,058)	(369)	(175)
Proceeds from sales of marketable securities	7,025	1,862	8,619
Purchases of marketable securities	(8,051)	(2,305)	(3,713)
Net cash used by investing activities	(3,603)	(2,011)	(139)
Cash flows from financing activities:			
Payments on long-term debt	(34)	(31)	(130)
Proceeds from the exercise of stock options and warrants	112	550	41

Net cash provided (used) by financing activities	78	519	(89)
	-----	-----	-----
Net (decrease) increase in cash and cash equivalents	(1,317)	1,004	1,087
Cash and cash equivalents, beginning of year	3,218	2,214	1,127
	-----	-----	-----
Cash and cash equivalents, end of year	\$ 1,901	\$ 3,218	\$ 2,214
	=====	=====	=====

Supplemental schedule of noncash activities:

Acquisition of other businesses:			
Cost of acquisitions in excess of fair market value of net assets acquired	\$ 4,337	\$ 2,080	\$ 5,205
Tangible assets acquired	494	30	133
Liabilities assumed	107	-	-
Common stock issued in connection with acquisitions	3,205	911	468

The accompanying notes are an integral part of these financial statements.

</TABLE>

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

NATURE OF OPERATIONS

Barrett Business Services, Inc. ("Barrett" or "the Company"), a Maryland corporation, is engaged in providing staffing and professional employer organization ("PEO") services to a diversified group of customers through a network of branch offices throughout Oregon, Washington, Idaho, California, Arizona, Maryland, and Delaware. Approximately 66%, 68%, and 78%, respectively, of the Company's revenues during 1996, 1995, and 1994 were attributable to its Oregon operations.

REVENUE RECOGNITION

The Company recognizes revenue as the services are rendered by its work force. Staffing services are engaged by customers to meet short-term fluctuations in personnel needs. Professional employer services are normally used by organizations to satisfy ongoing personnel needs and typically involve contracts with an indefinite term, until notice of termination is given by either party, which cover all employees at a particular work site.

CASH AND CASH EQUIVALENTS

The Company considers nonrestricted short-term investments which are highly liquid, readily convertible into cash, and have original maturities of less than three months to be cash equivalents for purposes of the statements of cash flows.

ALLOWANCE FOR DOUBTFUL ACCOUNTS

The Company had an allowance for doubtful accounts of \$25,000 at December 31, 1996 and 1995.

MARKETABLE SECURITIES

The Company adopted Statement of Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities," effective December 31, 1994. At December 31, 1996 and 1995, marketable securities consisted primarily of governmental debt instruments with maturities generally from 90 days to 30 years (see Note 6). Marketable equity and debt securities have been categorized as held-to-maturity and, as a result, are stated at amortized cost. Realized gains and losses on sales of marketable securities are included in other (expense) income on the Company's statements of operations.

INTANGIBLES

Intangible assets consist primarily of identifiable intangible assets acquired and the cost of acquisition in excess of the fair value of net assets acquired ("goodwill"). Intangible assets acquired are recorded at their estimated fair value at the acquisition date.

The Company uses a 15-year estimate as the useful life of goodwill. This life is based on an analysis of industry practice and the factors influencing the acquisition decision. Other intangible assets are amortized on the straight-line method over their estimated useful lives, ranging from 2 to 15 years. (See Note 4.)

## BARRETT BUSINESS SERVICES, INC.

## NOTES TO FINANCIAL STATEMENTS

## 1. SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

## INTANGIBLES (CONTINUED)

The Company reviews for asset impairment at the end of each quarter or more frequently when events or changes in circumstances indicate that the carrying amount of intangible assets may not be recoverable. To perform that review, the Company estimates the sum of expected future undiscounted net cash flows from the intangible assets. If the estimated net cash flows are less than the carrying amount of the intangible asset, the Company recognizes an impairment loss in an amount necessary to write down the intangible asset to a fair value as determined from expected future discounted cash flows. No write-down for impairment loss was recorded for the years ended December 31, 1996, 1995, and 1994.

## PROPERTY AND EQUIPMENT

Property and equipment are stated at cost. Expenditures for maintenance and repairs are charged to operating expense as incurred, and expenditures for additions and betterments are capitalized. The cost of assets sold or otherwise disposed of and the related accumulated depreciation are eliminated from the accounts, and any resulting gain or loss is reflected in the statements of operations.

Depreciation of property and equipment is calculated using either straight-line or accelerated methods over estimated useful lives which range from 3 years to 31.5 years.

## CUSTOMER SAFETY INCENTIVES PAYABLE

Safety incentives are paid annually to professional employer services clients if the cost of workers' compensation claims is less than agreed upon amounts; amounts paid are based on a percentage of payroll. The Company accrues the amounts payable under this program on a monthly basis.

## CUSTOMER DEPOSITS

The Company requires deposits from certain professional employer services customers to cover a portion of its accounts receivable due from such customers in event of default of payment.

## COMMON STOCK SPLIT AND CHANGE IN AUTHORIZED SHARES

On April 20, 1994, the Company's board of directors approved a 2-for-1 stock split in the form of a stock dividend, paid May 23, 1994, to holders of record of its common stock at the close of business on May 2, 1994 (the "Record Date"), at the rate of one new share for each share outstanding on the Record Date.

All earnings per share amounts have been adjusted to reflect these transactions for all periods presented.

A special meeting of stockholders was held on August 10, 1994, pursuant to which the stockholders approved an amendment to the Company's charter to increase the number of authorized shares of common stock from 7,500,000 shares to 20,500,000 shares.

## BARRETT BUSINESS SERVICES, INC.

## NOTES TO FINANCIAL STATEMENTS

## 1. SUMMARY OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

## STATEMENTS OF CASH FLOWS

The Company has recorded the following non-cash transactions:

During 1995, the President and Chief Executive Officer of the Company contributed 7,400 shares of common stock of the Company with a then-fair market value of \$111,000 to the Company in settlement of a personal guarantee of a receivable from an insolvent customer (see Note 11).

Interest paid during 1996, 1995, and 1994 did not materially differ from interest expense.

Income taxes paid by the Company in 1996 and 1995 totaled \$2,939,900 and \$2,510,700, respectively.

#### NET INCOME PER SHARE

Net income per share for the years ended December 31, 1996, 1995, and 1994 is computed based on the weighted average number of common stock and common stock equivalents outstanding during the periods. Outstanding stock options and warrants, net of assumed buy-back, are considered common stock equivalents.

#### RECLASSIFICATIONS

Certain prior year amounts have been reclassified to conform with the 1996 presentation. Such reclassifications had no impact on net income or stockholders' equity.

#### ACCOUNTING ESTIMATES

The preparation of the Company's financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results may differ from those estimates.

## 2. ACQUISITIONS

#### PERSONNEL MANAGEMENT & CONSULTING, INC.

On February 27, 1994, the Company purchased substantially all of the assets of Personnel Management & Consulting, Inc., a company engaged in the temporary staffing business in Maryland and Delaware. Of the \$270,000 purchase price, the Company paid \$42,000 in cash and issued 12,000 shares of its common stock with a then-fair market value of \$228,000. The acquisition was accounted for under the purchase method of accounting, which resulted in approximately \$241,000 of intangible assets and \$29,000 of fixed assets.

36

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

## 2. ACQUISITIONS (CONTINUED)

#### GOLDEN WEST TEMPORARY SERVICES

On March 7, 1994, the Company purchased certain assets of Golden West Temporary Services ("Golden West"), a company in the temporary staffing business with four offices in northern California. The cash purchase price of \$4,514,000 was paid by liquidating a portion of the Company's short-term marketable securities. The Company accounted for the acquisition under the purchase method of accounting, which resulted in approximately \$4,425,000 of intangible assets and \$89,000 of fixed assets.

#### CONSTRUCTION WORKFORCE

On December 26, 1994, the Company purchased certain assets of Max Johnson Enterprises, Inc., operating as Construction Workforce, a company located in Spokane, Washington, which specializes in providing highly skilled temporary craftsmen to the commercial construction industry. Of the \$300,000 purchase price, the Company paid \$60,000 in cash and issued 17,142 shares of its common stock with a then-fair market value of \$240,000. The acquisition was accounted for under the purchase method of accounting, which resulted in \$285,000 of intangible assets and \$15,000 of fixed assets.

#### ADVANCED TEMPORARY SYSTEMS, INC.

On December 29, 1994, the Company purchased, for \$51,000 in cash, certain assets of Advanced Temporary Systems, Inc., a company engaged in the temporary staffing business in Kent, Washington. The Company accounted for the acquisition under the purchase method of accounting, which resulted in \$51,000 of intangible assets.

MID-DEL EMPLOYMENT SERVICE, INC.; SUSSEX EMPLOYMENT SERVICES, INC.; PPI (PRESTIGE PERSONNEL) -SALISBURY, INC.; AND DEL-MAR-VA NURSES-ON-CALL INC. On July 17, 1995, the Company purchased certain assets of Mid-Del Employment Service, Inc.; Sussex Employment Services, Inc.; PPI (Prestige

Personnel) - Salisbury, Inc.; and Del-Mar-Va Nurses-On-Call Inc. (collectively, "the Maryland and Delaware companies"). These companies are engaged in the temporary staffing business in eastern Maryland and Delaware. The all-cash purchase price of \$969,000 (inclusive of acquisition-related costs of \$19,000) was accounted for under the purchase method of accounting, which resulted in \$944,000 of intangible assets and \$25,000 of fixed assets.

#### STREGE & ASSOCIATES, INC.

Effective December 11, 1995, the Company purchased certain assets of Strege & Associates, Inc., a company specializing in providing highly skilled tradesmen to various industries for maintenance and supplemental labor purposes in Portland, Oregon. Of the \$1,141,000 purchase price (inclusive of acquisition-related costs of \$4,000), the Company paid \$230,000 in cash and issued 67,443 shares of its common stock with a then-fair market value of \$911,000. The acquisition was accounted for under the purchase method of accounting, which resulted in \$1,136,000 of intangible assets and \$5,000 of fixed assets.

37

#### BARRETT BUSINESS SERVICES, INC.

##### NOTES TO FINANCIAL STATEMENTS

## 2. ACQUISITIONS (CONTINUED)

#### STAFFAMERICA, INC.

On April 1, 1996, the Company acquired certain assets and the business of StaffAmerica, Inc., pursuant to a Plan and Agreement of Reorganization. StaffAmerica provides both temporary staffing and PEO services through its two offices located in Santa Barbara and Oxnard, California. In 1995, StaffAmerica had revenues of approximately \$6.7 million. In exchange for the StaffAmerica assets and business operations, the Company issued 157,464 shares of its common stock valued at \$2,795,000, assumed a StaffAmerica liability of \$50,000 for customer deposits, issued to each of the two owners of StaffAmerica 845 shares of Company common stock for their covenants not to compete, and incurred \$102,000 in acquisition-related costs. The acquisition was accounted for under the purchase method of accounting, which resulted in \$2,597,000 of intangible assets, a promissory note receivable of \$324,000 from the seller, and \$56,000 in fixed assets. The \$324,000 promissory note is due and payable no later than March 31, 1997.

The Plan and Agreement of Reorganization between StaffAmerica and the Company allows StaffAmerica and the former owners to require the Company to repurchase the shares issued to them in the acquisition. There are certain conditions and restrictions imposed on StaffAmerica and the former owners with regard to the Company's obligation to repurchase its stock. The Company's obligation to repurchase such shares commenced on May 1, 1996 and expires on March 31, 1997. Upon redemption, and to the extent the note receivable from the seller remains outstanding, the price per share shall be the lower of \$17.75 per share or the then-fair market value of the common stock. If the note receivable has been fully retired, then the price per share of the common stock for redemption purposes shall be \$17.75. The total 159,154 shares of common stock is shown as redeemable common stock in the accompanying balance sheet at its recorded value of \$2,825,000.

#### JOBWORKS AGENCY, INC.

On April 8, 1996, the Company acquired certain assets and the business of JobWorks Agency, Inc. (JobWorks) by way of a Plan and Agreement of Reorganization. JobWorks provides both temporary staffing and PEO services through its two offices located in Hood River and The Dalles, Oregon. JobWorks had revenues of approximately \$1.2 million (unaudited) in 1995. The Company issued 20,446 shares of its common stock with a then-fair value of \$380,000 for the assets and business of JobWorks, assumed a customer deposit liability of \$2,000, and incurred \$14,000 in acquisition-related costs. The Company paid \$20,000 in cash for the selling shareholder's agreement of noncompetition. The acquisition was accounted for under the purchase method of accounting, which resulted in \$324,000 of intangible assets, \$72,000 in accounts receivable, and \$20,000 in fixed assets.

#### CASCADE TECHNICAL STAFFING

Effective August 26, 1996, the Company acquired certain assets of Cascade Technical Staffing (Cascade). Cascade provides technical and light industrial staffing services primarily in the electronics industry through its Beaverton, Oregon office. Cascade had revenues of approximately \$3.5 million (unaudited) in 1995. The Company paid \$550,000 in cash for the assets and incurred \$6,000 in acquisition-related costs. The acquisition was accounted for under the purchase method of accounting, which resulted

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

2. ACQUISITIONS (CONTINUED)

CALIFORNIA EMPLOYER SERVICES, INC.

Effective November 4, 1996, the Company acquired the PEO division of California Employer Services, Inc. (CES), an Orange County, California staffing services company. The CES division had revenues of approximately \$10.5 million (unaudited) for the fiscal year ended September 30, 1996. The Company paid \$624,000 in cash for the division, assumed a customer deposit liability of \$36,000, and incurred \$25,000 in acquisition-related costs. The transaction was accounted for under the purchase method of accounting, which resulted in \$685,000 of intangible assets.

PROFESSIONAL PERSONNEL, INC.

Effective November 25, 1996, the Company acquired certain assets of Professional Personnel, Inc. (PPI), a provider of PEO services located in Downey, California. PPI had revenues of approximately \$2.4 million (unaudited) for the year ended September 30, 1996. The Company paid \$176,000 in cash for the division, assumed a customer deposit liability of \$19,000, and incurred \$2,000 in acquisition-related costs. The transaction was accounted for under the purchase method of accounting, which resulted in \$195,000 of intangible assets and \$2,000 of fixed assets.

PRO FORMA RESULTS OF OPERATIONS (UNAUDITED)

The operating results of each of the above acquisitions are included in the Company's results of operations from the respective date of acquisition. The following unaudited pro forma summary presents the combined results of operations as if the Maryland and Delaware companies, Strege & Associates, StaffAmerica, Cascade Technical Staffing, and CES acquisitions had occurred at the beginning of 1995, after giving effect to certain adjustments for the amortization of intangible assets, taxation and cost of capital. The other acquisitions made since January 1, 1995 are not included in the pro forma information as their effect is not material.

	Year ended December 31,	
	1996	1995
	-----	-----
	(in thousands, except per share amounts)	
Revenue	\$ 229,877	\$ 204,426
	=====	=====
Net income	\$ 5,248	\$ 4,631
	=====	=====
Net income per share	\$ .75	\$ .67
	=====	=====

The unaudited pro forma results above have been prepared for comparative purposes only and do not purport to be indicative of what would have occurred had the acquisitions been made as of that date or of results which may occur in the future.

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

3. FAIR VALUE OF FINANCIAL INSTRUMENTS AND CONCENTRATION OF CREDIT RISK

All of the Company's significant financial instruments are recognized in its balance sheet. Carrying values approximate fair market value of most financial assets and liabilities. The fair market value of certain financial instruments was estimated as follows:

- Marketable securities - Marketable securities primarily consist of U.S.

Treasury bills and municipal bonds. The interest rates on the Company's marketable security investments approximate current market rates for these types of investments; therefore, the recorded value of the marketable securities approximates fair market value.

- Long-term debt - The interest rates on the Company's long-term debt approximate current market rates, based upon similar obligations with like maturities; therefore, the recorded value of long-term debt approximates the fair market value.

Financial instruments that potentially subject the Company to concentration of credit risk consist primarily of temporary cash investments, marketable securities, and trade accounts receivables. The Company restricts investment of temporary cash investments and marketable securities to financial institutions with high credit ratings and to investments in governmental debt instruments. Credit risk on trade receivables is minimized as a result of the large and diverse nature of the Company's customer base. At December 31, 1996, the Company had significant concentrations of credit risk as follows:

- Marketable securities - \$2,170,000 of marketable securities at December 31, 1996 consisted of Oregon State Housing & Community Service Bonds.
- Trade receivables - \$2,426,000 of trade receivables were with two customers at December 31, 1996 (13% of trade receivables outstanding at December 31, 1996).

4. INTANGIBLES

Intangibles consist of the following (in thousands):

	December 31,	
	1996	1995
Covenants not to compete	\$ 2,049	\$ 1,614
Goodwill	10,985	6,826
Customer lists	358	358
	-----	-----
	13,392	8,798
Less accumulated amortization	3,166	2,346
	-----	-----
	\$ 10,226	\$ 6,452
	=====	=====

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

5. PROPERTY AND EQUIPMENT

Property and equipment consist of the following (in thousands):

	December 31,	
	1996	1995
Office furniture and fixtures	\$ 3,037	\$ 1,908
Buildings	1,183	1,175
Vehicles	60	41
	-----	-----
	4,280	3,124
Less accumulated depreciation	1,477	1,171
	-----	-----
	2,803	1,953
Land	308	308
	-----	-----
	\$ 3,111	\$ 2,261
	=====	=====

6. ACCRUED WORKERS' COMPENSATION CLAIM LIABILITIES

In August 1987, the Company became a self-insured employer with respect to workers' compensation coverage for all its employees working or living in



Oregon. The Company also became a self-insured employer for workers' compensation coverage in the states of Maryland effective November 1993, Washington effective July 1994, Delaware effective January 1995, and California effective March 1995. Effective May 1995, the Company also became self-insured for workers' compensation purposes by the United States Department of Labor for longshore and harbor ("USL&H") workers' coverage.

The Company has provided \$2,853,000 and \$2,705,000 at December 31, 1996 and 1995, respectively, as an estimated liability for unsettled workers' compensation claims. This estimated liability represents management's best estimate which includes, in part, an evaluation of information provided by the Company's third-party administrators and its independent actuary. Included in the claims liabilities are case reserve estimates for reported losses, plus additional amounts based on projections for incurred but not reported claims, anticipated increases in case reserve estimates, and additional claims administration expenses. These estimates are continually reviewed and adjustments to liabilities are reflected in current operations as they become known. The Company believes that the difference between amounts recorded at December 31, 1996 for its estimated liability and the possible range of costs of settling related claims is not material to results of operations; nevertheless, it is reasonably possible that adjustments required in future periods may be material to results of operations.

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

6. ACCRUED WORKERS' COMPENSATION CLAIM LIABILITIES (CONTINUED)

The United States Department of Labor and the States of Oregon, Maryland, Washington, and California require the Company to maintain specified investment balances or other financial instruments, totaling \$7,151,000 at December 31, 1996 and \$5,974,000 at December 31, 1995, to cover potential claims losses. In partial satisfaction of these requirements, at December 31, 1996 and 1995, the Company has provided a letter of credit in the amount of \$1,572,000 and a \$300,000 surety bond guaranteed by an irrevocable standby letter of credit. The investments are included in restricted marketable securities and workers' compensation deposits in the accompanying balance sheets.

Liabilities incurred for work-related employee fatalities are recorded either at an agreed lump-sum settlement amount or the net present value of future fixed and determinable payments over the actuarially determined remaining life of the beneficiary, discounted at a rate that approximates a long-term, high-quality corporate bond rate. The Company has obtained excess workers' compensation insurance to limit its self-insurance exposure to \$350,000 per occurrence in all states, except for \$300,000 in Maryland and \$500,000 per occurrence for USL&H exposure. The excess insurance provides unlimited coverage above the aforementioned exposures. At December 31, 1996, the Company has recorded \$613,000 for work-related catastrophic injuries and fatalities in long-term workers' compensation liabilities in the accompanying balance sheets.

The workers' compensation expense in the accompanying statements of operations consists of \$5,799,000, \$5,802,000, and \$4,254,000 for self-insurance expense for 1996, 1995, and 1994, respectively. Premiums in the insured states were \$139,000, \$271,000, and \$815,000 for 1996, 1995, and 1994, respectively.

7. CREDIT FACILITY

On August 12, 1993, the Company entered into a loan agreement ("the Agreement") with a major bank, which provides for (a) an unsecured revolving credit facility for working capital purposes and (b) a term real estate loan (see Note 8). The Agreement, as amended, expires on May 30, 1997 and currently permits total borrowings of up to \$4,000,000 under the revolving credit facility. The interest rates available on outstanding balances under the revolving credit facility include Prime Rate, Federal Funds Rate plus 1.75%, or Adjusted Eurodollar Rate plus 1.25%. Under the amended loan agreement, the Company is required to maintain a zero outstanding balance against the revolving credit facility for a minimum of 60 consecutive days during each year. The Company is also prohibited from pledging any of its assets other than existing mortgages on its real property.

There were no borrowings on the revolving credit facility during 1996 and

1995. During the year ended December 31, 1994, the maximum balance outstanding under the revolving credit facility was \$1,500,069, the average balance outstanding was \$165,000, and the weighted average interest rate during the period was 6.9%. The weighted average interest rate during 1994 was calculated using daily weighted averages.

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

8. LONG-TERM DEBT

Long-term debt consists of the following:

<TABLE>

	December 31,	
	1996	1995
	(in thousands)	
<S>	<C>	<C>
Mortgage note payable in monthly installments of \$2,784, including interest at 11% per annum through 1998, with a principal payment of \$269,485 due in 1998, secured by land and building	\$ 276	\$ 279
Mortgage note payable in monthly installments of \$6,730, including interest at 8.15% per annum through 2003, with a principal payment of \$366,900 due in 2003, secured by land and building (Note 7)	598	629
	-----	-----
	874	908
Less portion due within one year	36	33
	-----	-----
	\$ 838	\$ 875
	=====	=====

</TABLE>

Maturities on long-term debt are summarized as follows at December 31, 1996 (in thousands):

Year ending	
December 31,	
1997	\$ 36
1998	309
1999	39
2000	42
2001	45
Thereafter	403
	-----
	\$ 874
	=====

9. SAVINGS PLAN

On April 1, 1990, the Company established a Section 401(k) employee savings plan for the benefit of its eligible employees. All employees 21 years of age or older, except those covered under a co-employer (PEO) contract, become eligible to participate in the savings plan upon completion of 1,000 hours of service in any consecutive 12-month period following the initial date of employment. Employees covered under a co-employer (PEO) contract are eligible to participate in the savings plan beginning with their respective dates of employment. The determination of Company contributions to the plan, if any, is subject to the sole discretion of the Company. Participants' interests in Company contributions to the plan vest over a seven-year period. Company contributions to the plan were \$134,000, \$142,000, and \$103,000 for the years ended December 31, 1996, 1995, and 1994, respectively.

9. SAVINGS PLAN (CONTINUED)

Recent attention has been placed by the Internal Revenue Service ("the IRS") and the PEO industry on IRC Section 401(k) plans sponsored by PEO companies. As such, the tax-exempt status of the Company's plan is subject to continuing scrutiny and approval by the IRS and to the Company's ability to support to the IRS the Company's employer-employee relationship with leased employees. In the event the tax-exempt status were to be discontinued and the plan were to be disqualified, the operations of the Company could be adversely affected. The Company has not recorded any provision for this potential contingency, as the Company and its legal counsel cannot presently estimate either the likelihood of disqualification nor the resulting range of loss, if any.

10. COMMITMENTS

LEASE COMMITMENTS

The Company leases its branch offices under operating lease agreements which require minimum annual payments as follows (in thousands):

Year ending December 31,	
1997	\$ 806
1998	591
1999	428
2000	201
2001	179
	-----
Total minimum payments	\$ 2,205 =====

Rent expense for the years ended December 31, 1996, 1995, and 1994 was approximately \$799,000, \$607,000, and \$423,000, respectively.

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

11. RELATED PARTY TRANSACTIONS

During 1996, 1995, and 1994, the Company recorded revenues of \$4,086,000, \$3,753,000, and \$3,261,000, respectively, and cost of revenues of \$3,768,000, \$3,408,000, and \$2,958,000, respectively, for providing services to a company of which a director of the Company is president and majority stockholder. At December 31, 1996 and 1995, Barrett had trade receivables from this company of \$126,000 and \$160,000, respectively.

During 1994, the Company recorded revenues of \$119,000 and cost of revenues of \$110,000 for providing professional employer services to a company owned by Barrett's President and Chief Executive Officer.

At December 31, 1993, the President and Chief Executive Officer of the Company, pursuant to the approval of a majority of the disinterested outside directors, agreed to personally guarantee, at no cost to the Company, the repayment of a \$111,000 receivable from an unrelated, insolvent customer. During 1995, pursuant to this agreement, the Company exercised its right to the personal guarantee provided by the Company's Chief Executive Officer. Accordingly, the Chief Executive Officer surrendered to the Company 7,400 shares of common stock of the Company with a then-fair market value of \$111,000 or \$15.00 per share, in satisfaction of the guarantee. The Company subsequently retired the shares, and the par value of the shares was reclassified to additional paid-in capital. The uncollectible account was included in the Company's provisions for doubtful accounts during 1993 and 1994.

Through June 1995, a director of the Company was Vice Chairman of the board of directors of the bank that provides the Company's unsecured revolving credit facility and certain mortgage financing. See Notes 7 and 8.

12. INCOME TAXES

The provisions for income taxes are as follows (in thousands):

	Year ended December 31,		
	1996	1995	1994
Current:			
Federal	\$ 2,681	\$ 2,067	\$ 1,750
State	476	463	375
	3,157	2,530	2,125
Deferred:			
Federal	(283)	(19)	(17)
State	(59)	(4)	(3)
	(342)	(23)	(20)
Total provision	\$ 2,815	\$ 2,507	\$ 2,105

45

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

12. INCOME TAXES (CONTINUED)

Deferred tax assets (liabilities) are comprised of the following components (in thousands):

<TABLE>  
<CAPTION>

	December 31,	
	1996	1995
<S>	<C>	<C>
Accrued workers' compensation claim liabilities	\$ 1,113	\$ 1,053
Allowance for doubtful accounts	10	10
Tax depreciation in excess of book depreciation	(154)	(126)
Safety incentives	281	
Amortization of intangibles	29	
	\$ 1,279	\$ 937

</TABLE>

The effective tax rate differed from the U.S. statutory federal tax rate due to the following:

<TABLE>  
<CAPTION>

	Year ended December 31,		
	1996	1995	1994
<S>	<C>	<C>	<C>
Statutory federal tax rate	34.0%	34.0%	34.0%
State taxes, net of federal benefit	3.5	4.6	4.4
Nondeductible amortization of intangibles	.1	.1	.2
Federal tax-exempt interest income	(1.4)	(1.3)	(1.1)
Other, net	(.3)	.6	.3
	35.9%	38.0%	37.8%

</TABLE>

During 1996, the Company recognized a State of Oregon surplus tax refund of approximately \$145,000 related to tax years 1993 through 1995.

13. REDEEMABLE COMMON STOCK AND NONREDEEMABLE STOCKHOLDERS' EQUITY

REDEEMABLE COMMON STOCK

As part of the 1996 acquisition of StaffAmerica discussed in Note 2, the Company granted "put rights" to certain shareholders that may require the Company to redeem 159,154 shares of its common stock at a maximum redemption price of \$17.75 per share subject to certain contingencies as described in Note 2. If all shareholders with such "put rights" exercise their options, the Company would be required to

repurchase the above shares of common stock at a maximum amount of \$2,825,000. The redemption period began April 1, 1996 and continues through March 31, 1997. If such shareholders do not place a redemption request during the redemption period, the "put right" will expire on the stated expiration date.

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

13. REDEEMABLE COMMON STOCK AND NONREDEEMABLE STOCKHOLDERS' EQUITY (CONTINUED)

The shares of common stock subject to the "put rights" are presented in the accompanying balance sheets as redeemable common stock. Such shares have been recorded at their fair market value as of the dates of acquisition. Such fair market value equals the maximum redemption amount.

PUBLIC STOCK OFFERING

In June 1993, the Company completed an initial public offering of 1,000,000 shares of common stock at \$7.00 per share. In July 1993, the underwriters exercised an option to purchase 150,000 additional shares at \$7.00 per share to cover over-allotments. Total net proceeds to the Company were \$6,828,000 after deducting the underwriting discount and offering expenses.

14. STOCK INCENTIVE PLAN

As of March 1, 1993, the Company adopted the 1993 Stock Incentive Plan ("the Plan") which provides for stock-based awards to the Company's employees, non-employee directors, and outside consultants or advisers. As of April 20, 1994, the Company increased the number of shares of common stock reserved for issuance under the Plan from 500,000 to 800,000.

Options granted under the Plan generally become exercisable in four equal annual installments beginning one year after the date of grant, and expire ten years after the date of grant. Under the terms of the Plan, the exercise price of the options must not be less than the fair market value of the Company's stock on the date of grant. The number of options and the price per share have been restated to reflect the 2-for-1 stock split effective May 23, 1994.

In connection with the initial public offering, the Company issued 200,000 warrants to its underwriters and related parties for the purchase of shares of the Company's common stock exercisable in whole at any time or in part from time to time commencing June 11, 1994 at \$4.20 per share, after giving effect to the 2-for-1 stock split. A total of 110,000 warrants were exercised in January 1995 for proceeds of \$462,000. The remaining unexercised warrants expire on June 10, 1998.

A summary of the status of the options granted under the Plan at December 31, 1996, 1995, and 1994, together with changes during the period then ended, are presented below. The numbers of options exercisable at December 31, 1996, 1995, and 1994 were 126,500, 94,375, and 10,450, respectively.

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

14. STOCK INCENTIVE PLAN (CONTINUED)

<TABLE>  
<CAPTION>

Options	Weighted average exercise price
-----	-----

<S>	<C>	<C>
Outstanding at December 31, 1993	160,500	\$ 3.50
Options granted at market price	233,500	9.67
Options exercised	(22,175)	3.50
Options canceled or expired	(65,250)	7.45
	-----	
Outstanding at December 31, 1994	306,575	7.36
Options granted at market price	151,500	14.31
Options granted above market price	70,000	16.36
Options exercised	(13,950)	6.19
Options canceled or expired	(17,500)	7.52
	-----	
Outstanding at December 31, 1995	496,625	10.78
Options granted at market price	137,498	16.63
Options exercised	(83,625)	6.77
Options canceled or expired	(58,500)	17.70
	-----	
Outstanding at December 31, 1996	491,998	12.27
	=====	
Available for grant at December 31, 1996	184,252	
	=====	

</TABLE>

The Company applies APB Opinion 25 and related interpretations in accounting for the Plan. Accordingly, no compensation cost has been recognized for options granted under the Plan. Had compensation cost associated with the Plan been determined based on the fair market value at the grant date for options granted under the Plan, consistent with the methodology of Statement of Financial Accounting Standards (SFAS) No. 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

	1996	1995
	-----	-----
	(in thousands)	
Net income, as reported	\$ 5,036	\$ 4,118
Net income, pro forma	4,664	3,857
Earnings per share, as reported	.73	.62
Earnings per share, pro forma	.67	.58

The effects of applying SFAS No. 123 to pro forma disclosures for 1996 and 1995 are not likely to be representative of the effects on reported net income for future years, because options vest over several years and additional awards generally are made each year.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants in 1996 and 1995: expected volatility of 41%, expected dividend yield 0%, risk-free rate of return of 6.1%, and expected lives of seven years.

48

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

14. STOCK INCENTIVE PLAN (CONTINUED)

Total fair value of options granted at market price was computed to be \$1,227,834 and \$1,165,925 for the years ended December 31, 1996 and 1995, respectively. Total fair value of options granted at 110% above market price was computed to be \$531,300 for the year ended December 31, 1995. Such options were granted to the chief executive officer in 1995.

The following table summarizes information about options outstanding at December 31, 1996:

<S>	Exercise price range	Number of shares	Weighted average price	Weighted average remaining contractual life
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
	\$ 3.50 - \$10.00	159,000	\$ 7.41	7.0

\$10.50 - \$13.00	30,000	\$ 11.08	7.9
\$13.50 - \$19.00	302,833	\$ 15.19	8.9

</TABLE>

#### 15. LITIGATION

The Company is subject to legal proceedings and claims which arise in the ordinary course of its business. In the opinion of management, the amount of ultimate liability with respect to currently pending or threatened actions are not expected to materially affect the financial position or results of operations of the Company except as discussed below in Note 16.

#### 16. SUBSEQUENT EVENTS

A lawsuit was filed in the Circuit Court of the State of Oregon for the County of Multnomah on February 5, 1997, by Javier and Ester Munoz, husband and wife, against Asger M. Nielson, doing business as Nielson and Son ("Nielson"), Rain-Master Roofing, Inc. ("Rain-Master"), and the Company. Mr. Munoz was employed by the Company under a PEO arrangement with Rain-Master, which is in the roofing business. On February 1, 1995, Rain-Master was providing roofing services at a construction site for which Nielson was serving as general contractor. Mr. Munoz fell from the roof at the site in the course of his employment and is now a paraplegic as a result of the injuries he suffered. Until the filing of the lawsuit referred to above, Mr. Munoz's claim was being defended as a workers' compensation claim.

In the lawsuit, the plaintiffs are seeking damages in the amount of \$10,000,000 pursuant to claims for relief based on employer liability, intentional injury, product liability, negligence, breach of implied warranty and loss of consortium. Defense of the lawsuit has been tendered to the Company's excess workers' compensation, commercial general liability and umbrella liability insurance carriers; acceptance of the defense to the claim has not yet been received. Management intends to vigorously defend this action on the basis, among others, that workers' compensation is the exclusive remedy for employees injured in the course of employment. Under appropriate circumstances, the Company also may seek to enforce its contractual right to indemnification from Rain-Master pursuant to its PEO leasing arrangement. Based upon its investigation and analysis to date, management believes that the outcome of

49

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

this proceeding will not have a materially adverse effect on the Company's financial position or results of operations.

On March 12, 1997, a Notice of Intent to Revoke Farm/Forest Labor Contractor License and to Assess Civil Penalties (the "Notice") was served on the Company by the Bureau of Labor and Industries of the State of Oregon (the "Bureau"). The Notice also names Daniel A. Hatfield, an employee of the Company. The Notice proposes to assess civil penalties in the amount of \$488,000, based on the numbers of workers allegedly affected, for alleged noncompliance with various duties imposed on farm labor contractors by Oregon law, including licensing violations, failure to comply with wage payment laws, and failure to maintain and to provide workers and the Bureau with required documentation. Management intends to vigorously contest the claims asserted in the Notice and is in the process of collecting and analyzing data necessary to defend its position and to evaluate the probable outcome of the proceedings.

Effective February 1, 1997, the Company acquired D&L Personnel Department Specialists, Inc., dba HR Only, a staffing services company which specializes in human resource professionals with offices in Los Angeles and Orange County, California. The Company paid \$1,800,000 in cash for all of the outstanding common stock of HR Only and \$1,200,000 in cash for noncompete agreements with certain individuals, of which \$1,000,000 will be deferred for five years and then be paid ratably over the succeeding five-year period. HR Only's revenues for the fiscal year ended January 31, 1997 were approximately \$4.3 million. The transaction was accounted for under the purchase method of accounting, which resulted in \$3,021,000 of intangible assets, including an estimated \$85,000 for acquisition-related costs, and \$64,000 of net tangible assets.

50

BARRETT BUSINESS SERVICES, INC.

NOTES TO FINANCIAL STATEMENTS

17. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

<TABLE>  
<CAPTION>

	First quarter -----	Second quarter -----	Third quarter -----	Fourth quarter -----
	(in thousands, except per share amounts)			
<S>	<C>	<C>	<C>	<C>
Year ended December 31, 1994:				
Revenues	\$ 27,067	\$ 35,136	\$ 41,149	\$ 37,200
Cost of revenues	24,096	31,217	36,107	33,025
Net income	608	765	1,235	858
Net income per share	.09	.12	.19	.13
Year ended December 31, 1995:				
Revenues	39,298	44,564	49,636	46,306
Cost of revenues	35,819	39,645	43,378	40,474
Net income	344	1,039	1,513	1,223
Net income per share	.05	.16	.23	.18
Year ended December 31, 1996:				
Revenues	43,185	51,871	60,252	60,508
Cost of revenues	38,169	45,724	53,659	54,011
Net income	827	1,305	1,661	1,243
Net income per share	.12	.19	.24	.18

</TABLE>

51

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

PART III

Item 10. INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

The information required by Item 10, Directors and Executive Officers of the Registrant, is incorporated herein by reference to the Company's definitive Proxy Statement for the 1997 Annual Meeting of Stockholders ("Proxy Statement"), under the headings "Election of Directors" and "Stock Ownership by Principal Stockholders and Management--Section 16(a) Beneficial Ownership Reporting Compliance" or appears under the heading "Executive Officers of the Registrant" on pages 16-17 of this report. The information required by Item 11, Executive Compensation, is incorporated herein by reference to the Proxy Statement, under the headings "Executive Compensation" and "Election of Directors--Compensation Committee Interlocks and Insider Participation." The information required by Item 12, Security Ownership of Certain Beneficial Owners and Management, is incorporated herein by reference to the Proxy Statement, under the heading "Stock Ownership by Principal Stockholders and Management--Beneficial Ownership Table." The information required by Item 13, Certain Relationships and Related Transactions, is incorporated herein by reference to the Proxy Statement, under the heading "Election of Directors--Compensation Committee Interlocks and Insider Participation."

52

PART IV





## EXHIBIT INDEX

## Exhibits

- 3.1 Charter of the registrant, as amended. Incorporated by reference to Exhibit 3 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1994.
- 3.2 Bylaws of the registrant, as amended.
- 4.1 Loan Agreement between the registrant and First Interstate Bank of Oregon, N.A., dated August 12, 1993 ("Loan Agreement"). Incorporated by reference to Exhibit 10 to the registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1993.
- 4.2 First Amendment to Loan Agreement dated March 29, 1994. Incorporated by reference to Exhibit 4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 1994.
- 4.3 Second Amendment to Loan Agreement dated May 31, 1994, together with Optional Advance Note dated May 31, 1994. Incorporated by reference to Exhibit 4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1994.
- 4.4 Third Amendment to Loan Agreement dated January 3, 1995, together with Optional Advance Note dated January 3, 1995. Incorporated by reference to Exhibit 4.4 to the registrant's Annual Report of Form 10-K for the year ended December 31, 1994.
- 4.5 Fourth Amendment to Loan Agreement dated June 1, 1995, together with Optional Advance Note dated June 1, 1995 and Interest Rate Option Agreement dated June 1, 1995. Incorporated by reference to Exhibit 4.4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1995.
- 4.6 Fifth Amendment to Loan Agreement dated May 31, 1996. Incorporated by reference to Exhibit 4.4 to the registrant's Quarterly Report on Form 10-Q for the quarter ended June 30, 1996.

The registrant has incurred other long-term indebtedness as to which the amount involved is less than 10 percent of the registrant's total assets. The registrant agrees to furnish copies of the instruments relating to such indebtedness to the Commission upon request.

- 10 Executive Compensation Plans and Arrangements and Other Management Contracts.
- 10.1 1993 Stock Incentive Plan of the registrant as amended.
- 10.2 Form of Indemnification Agreement with each director of the registrant. Incorporated by reference to Exhibit 10.8 to the registrant's Registration Statement on Form S-1 (No. 33- 61804).
- 11 Statement of Calculation of Average Common Shares Outstanding.
- 23 Consent of Price Waterhouse LLP, independent accountants.
- 24 Power of attorney of certain officers and directors.

- 27 Financial Data Schedule.

Other exhibits listed in Item 601 of Regulation S-K are not applicable.



ARTICLE I. STOCKHOLDERS

Section 1. Annual Meeting. The annual meeting of the stockholders shall be held during the third week of May of each year on the date and time or at such other date and time in May of each year as the board of directors may establish, for the purpose of electing directors and for the transaction of such other business as may come before the meeting. The board of directors shall timely establish the annual meeting date and time in conjunction with the notice of meeting requirements of Article I, Section 4, of these Bylaws.

Section 2. Special Meetings. Special meetings of the stockholders, for any purpose or purposes, may be called by the president or by the board of directors, and shall be called by the secretary upon written request by stockholders entitled to cast 25 percent of all votes entitled to be cast at the meeting stating the purpose of the meeting and the matters proposed to be acted upon at the meeting and upon payment by such stockholders to the corporation of the costs of the notice of the meeting. Notwithstanding the foregoing, a special meeting need not be called by the secretary to consider any matter which is substantially the same as a matter voted on at any special meeting of the stockholders held during the preceding 12 months unless requested by stockholders entitled to cast a majority of all votes entitled to be cast at the meeting.

Section 3. Place of Meeting. The place of meeting for all annual and special meetings of the stockholders shall be such place within the United States as shall be determined by the board of directors. In the absence of any such determination, all meetings of stockholders shall be held at the principal office of the corporation in the state of Oregon.

Section 4. Notice of Meeting; Waiver. Written or printed notice stating the place, day, and hour of the meeting and, in case of a special meeting or if otherwise required by law, the purpose or purposes for which the meeting is called, shall be given by the secretary not earlier than 90 nor less than 10 days before the date of the meeting, either personally or by mail, to each stockholder of record entitled to vote at or to receive notice of such meeting. If given personally, such notice shall be effective when delivered to the stockholder or when left at the stockholder's residence or usual place of business. If given by mail, such notice shall be effective when deposited in the United States mail, addressed to the stockholder at his or her address as shown in the corporation's current record of stockholders, with postage thereon prepaid. A stockholder entitled to notice of a meeting waives such notice if he or she is present at the meeting in person or by proxy. A written waiver of notice of a meeting signed by a stockholder entitled to such notice, whether before or after the time stated therein, which is filed with the records of stockholders meetings, shall be equivalent to the giving of such notice. A meeting of stockholders convened on the date for which it was called may be adjourned from time to time without further notice to a date not more than 120 days after the original record date for the meeting.

Section 5. Quorum; Manner of Acting. The presence in person or by proxy of stockholders entitled to cast a majority of all the votes entitled to be cast at the meeting shall constitute a quorum. If a quorum is present, a majority of all the votes cast at the meeting is sufficient to approve any matter which properly comes before the meeting unless

- 1 -

the vote of a greater proportion of all the votes cast or voting by classes is required by the Maryland General Corporation Law or the charter.

Section 6. Proxies. At all meetings of stockholders, a stockholder may vote by proxy executed in writing by the stockholder or by his or her duly authorized attorney-in-fact. Such proxy shall be filed with the secretary of the corporation before or at the time of the meeting. No proxy shall be valid after 11 months from the date of its execution unless otherwise expressly provided in the proxy.

Section 7. Voting of Shares. Each outstanding share of the corporation's common stock shall be entitled to one vote upon each matter submitted to a vote at a meeting of the stockholders except that shares owned, directly or indirectly, by another corporation in which the corporation owns, directly or indirectly, shares entitled to cast a majority of all the votes entitled to be cast by all shares of such other corporation shall not be voted at any meeting or counted in determining the total number of outstanding shares at any given time.

Section 8. Acceptance of Votes. If the name signed on a vote,

consent, waiver, or proxy appointment corresponds to the name of a stockholder, the corporation shall be entitled to accept the vote, consent, waiver, or proxy appointment and give it effect as the act of the stockholder.

If the name signed on a vote, consent, waiver, or proxy appointment does not correspond to the name of its stockholder, the corporation shall nevertheless be entitled to accept the vote, consent, waiver, or proxy appointment and give it effect as the act of the stockholder if:

a. The stockholder is a corporation, and the name signed purports to be that of the president, a vice-president, or a proxy appointed by either of them or by another person appointed under a bylaw or resolution of the board of directors of such stockholder, a certified copy of which is presented to the corporation.

b. The stockholder is an entity, other than a corporation, and the name signed purports to be that of an officer or agent of the entity.

c. The name signed purports to be that of an administrator, executor, guardian, or conservator representing the stockholder.

d. The name signed purports to be that of a receiver or trustee in bankruptcy of the stockholder.

e. The name signed purports to be that of a pledgee, beneficial owner, or attorney-in-fact of the stockholder.

f. Two or more persons are the stockholder whether as fiduciaries, members of a partnership, joint tenants, tenants in common, tenants by the

- 2 -

entirety, or otherwise, and the name signed purports to be the name of at least one of the co-owners.

The corporation shall be entitled to reject a vote, consent, waiver, or proxy if the secretary or other officer or agent authorized to tabulate votes, acting in good faith, has reasonable basis for doubt about the validity of the signature on it or about the signatory's authority to sign for the stockholder.

Section 9. Action Without Meeting. Any action required or permitted by the Maryland General Corporation Law to be taken at a meeting of the stockholders may be taken without a meeting if there are filed with the records of stockholders meetings a consent in writing which sets forth the action so taken signed by each stockholder entitled to vote on the matter and a written waiver of any right to dissent signed by each stockholder entitled to notice of the meeting but not entitled to vote at the meeting.

## ARTICLE II. BOARD OF DIRECTORS

Section 1. General Powers. The business and affairs of the corporation shall be managed under the direction of its board of directors.

Section 2. Number, Tenure, and Qualifications. The board of directors shall consist of not more than nine persons and not less than three persons, the exact number within such specified limits to be fixed from time to time by resolution of a majority of the entire board, provided that so long as there are less than three stockholders the number of directors may be fixed at less than three but not less than the number of stockholders. Each director shall hold office until the next annual meeting of the stockholders and until his or her successor shall have been elected and qualified unless sooner removed from office as hereinafter provided. Directors need not be residents of the state of Maryland or stockholders of the corporation.

Section 3. Regular Meetings. A regular meeting of the board of directors shall be held without other notice than this bylaw immediately after, and at the same place as, the annual meeting of stockholders. The board of directors may provide by resolution the time and place, either within or without the state of Maryland, for the holding of additional regular meetings without other notice than such resolution.

Section 4. Special Meetings. Special meetings of the board of directors may be called by or at the request of the president or any two directors. The person or persons authorized to call special meetings of the board of directors may fix any place, either within or without the state of Maryland, as the place for holding any special meeting of the board of directors called by them.

Section 5. Notice; Waiver. Notice of the date, time, and place of any special meeting shall be given at least 36 hours previously thereto by written notice delivered personally or given by facsimile transmission, teletype, or other form of wire communication, or by mail or private carrier, to each director at his or her business address.

- 3 -

Such notice shall be deemed effective at the earliest of the following: (a) when received, (b) three days after its deposit in the United States mail, as evidenced by the postmark, if mailed postpaid and correctly addressed, and (c) on the date shown on the return receipt, if sent by registered or certified mail, return receipt requested, and the receipt is signed by or on behalf of the director. A director's attendance at, or participation in, a meeting shall constitute a waiver of notice of such meeting, except where a director at the beginning of the meeting, or promptly upon the director's arrival, objects to holding of the meeting or the transacting of business at the meeting and does not thereafter vote for or assent to action taken at the meeting. A written waiver of notice of a meeting signed by a director entitled to such notice, whether before or after the time stated therein, which specifies the meeting for which notice is waived and which is filed with the records of the meeting shall be equivalent to the giving of such notice. Neither the business to be transacted at, nor the purpose of, any regular or special meeting of the board of directors need be specified in the notice or waiver of notice of such meeting.

Section 6. Quorum. A majority of the number of directors fixed from time to time pursuant to Section 2 of this Article II shall constitute a quorum for the transaction of business at any meeting of the board of directors, but, if less than such majority is present at a meeting, a majority of the directors present may adjourn the meeting from time to time without further notice.

Section 7. Manner of Acting. The action of a majority of the directors present at a meeting at which a quorum is present shall be the act of the board of directors.

Section 8. Vacancies. Any vacancy occurring in the board of directors, except a vacancy resulting from an increase in the number of directors, may be filled by the affirmative vote of a majority of the remaining directors, whether or not sufficient to constitute a quorum. A vacancy resulting from an increase in the number of directors may be filled by the affirmative vote of a majority of the entire board of directors.

Section 9. Presumption of Assent. A director who is present at a meeting of the board of directors when corporate action is taken shall be presumed to have assented to the action taken unless the director announces his or her dissent at the meeting and (a) the director's dissent is entered in the minutes of the meeting; or (b) the director files his or her written dissent with the secretary of the meeting before its adjournment; or (c) the director forwards his or her written dissent within 24 hours after the meeting is adjourned, by registered or certified mail, to the secretary of the meeting or of the corporation. Such right to dissent shall not apply to a director who voted in favor of such action.

Section 10. Removal of Directors. All or any number of the directors may be removed by the stockholders with or without cause at a meeting expressly called for that purpose by the affirmative vote of a majority of all votes entitled to be cast for the election of directors. The notice of such meeting shall state that the purpose or one of the purposes of the meeting is the removal of the director or directors.

Section 11. Compensation. By resolution of the board of directors, each director may be paid an annual fee as director and, in addition thereto, a fixed sum for

- 4 -

attendance at each meeting of the board of directors and executive committee or other committees and his expenses, if any, of attendance at any such meeting. No such payment shall preclude any director from serving the corporation in any other capacity and receiving compensation therefor.

Section 12. Action Without Meeting. Any action required or permitted by the Maryland General Corporation Law to be taken at a meeting of the board of directors may be taken without a meeting if a consent in writing which sets forth the action so taken is signed by each member of the board of directors and filed with the minutes of proceedings of the board of directors.

Section 13. Meetings By Telephone. Meetings of the board of directors may be held by means of conference telephone or similar communications equipment if all persons participating in the meeting can hear each other at the same time, and such participation shall constitute presence in person at the meeting. Section 14. Chairman and Vice Chairman. The board of directors shall appoint from among its members a chairman and a vice chairman who shall serve at the pleasure of the board of directors. The chairman, or in his absence the vice chairman, shall preside at the meetings of the board of directors.

### ARTICLE III.

#### EXECUTIVE COMMITTEE AND OTHER COMMITTEES

Section 1. Appointment. The board of directors may appoint from among its members an executive committee to consist of a chairman and one or more other directors. The appointment of such committee, the delegation of authority to it or action by it under that authority shall not constitute of itself compliance by any director not a member of the committee with the standard provided in the Maryland General Corporation Law for the performance of duties by directors.

Section 2. Authority. The executive committee, when the board of directors is not in session, shall have and may exercise all the authority of the board of directors except to the extent, if any, that such authority shall be limited by the resolution appointing the executive committee and except also that neither the executive committee nor any other committee of the board of directors appointed pursuant to Section 9 of this Article III shall have the authority to (a) declare dividends or distributions on stock; (b) fix the terms of stock subject to classification or reclassification or the terms on which any stock may be issued except according to a general formula or method specified by the board of directors by resolution or by adoption of a stock option or other plan; (c) recommend to the stockholders any action which requires stockholder approval; (d) amend the bylaws; or (e) approve a merger or share exchange which does not require stockholder approval.

Section 3. Tenure. Each member of the executive committee shall hold office until the next regular annual meeting of the board of directors following his or her

- 5 -

appointment and until his or her successor is appointed as a member of the executive committee.

Section 4. Meetings; Notice; Waiver. Regular meetings of the executive committee or any other committee of the board of directors appointed pursuant to Section 9 of this Article III may be held without notice at such times and places as the committee may fix from time to time by resolution. Special meetings of the executive committee or any such other committee may be called by any member thereof upon not less than 24 hours' notice stating the place, date and hour of the meeting. The provisions of Section 5 of Article II shall apply to the method for giving notice of special meetings of the executive committee or any such other committee and to the waiver of notice of any such meetings. The notice of a meeting of the executive committee or any such other committee need not state the business proposed to be transacted at the meeting.

Section 5. Quorum; Manner of Acting. A majority of the members of the executive committee or any such other committee shall constitute a quorum for the transaction of business at any meeting thereof, and the act of a majority of the members present at a meeting at which a quorum is present shall be the act of the committee.

Section 6. Vacancies. Any vacancy in the executive committee or any such other committee may be filled by the board of directors.

Section 7. Resignations and Removal. Any member of the executive committee or any such other committee may be removed at any time with or without cause by the board of directors. Any member of the executive committee or any such other committee may resign as a member of the committee at any time by giving written notice to the chairman of the board or secretary of the corporation, and, unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective.

Section 8. Procedure. The chairman of the executive committee shall be the presiding officer of the executive committee. The executive committee and any such other committee shall fix its own rules of procedure which shall not be inconsistent with these bylaws. The committee shall keep regular minutes of its proceedings and report the same to the board of directors for its information at the meeting thereof held next after the proceedings shall have been taken.

Section 9. Appointment of Other Committees of the Board of Directors. The board of directors may from time to time create any other committee or committees of the board of directors and appoint members of the board of directors to serve thereon. Each member of any such committee shall hold office until the next regular annual meeting of the board of directors following his or her appointment and until his or her successor is appointed as a member of such committee. Each committee shall have two or more members and, to the extent specified by the board of directors, may exercise the powers of the board subject to the limitations set forth in Section 2 of this Article III.

Section 10. Action Without a Meeting. Any action that may be taken by the executive committee or any such other committee at a meeting may be taken without a

- 6 -

meeting if a consent in writing which sets forth the action so taken is signed by each member of the committee and filed with the minutes of proceedings of the committee.

Section 11. Meetings By Telephone. Meetings of any committee of the board of directors may be held by means of conference telephone or similar communications equipment if all persons participating in the meeting can hear each other at the same time, and such participation shall constitute presence in person at the meeting.

#### ARTICLE IV. OFFICERS

Section 1. Number. The officers of the corporation shall be a president, a secretary and a treasurer, each of whom shall be elected by the board of directors. The board of directors may elect one or more vice presidents (the number thereof to be determined by the board of directors) and such other officers and assistant officers as may be deemed necessary.

Section 2. Election and Term of Office. The officers of the corporation shall be elected annually at the first meeting of the board of directors held after each annual meeting of the stockholders. A person may hold more than one office but may not serve concurrently as both president and vice president of the corporation. Each officer shall hold office until his or her successor shall have been duly elected, or until his or her death, or until he or she shall resign or shall have been removed in the manner hereinafter provided.

Section 3. Removal. The board of directors may remove any officer at any time. The election of an officer shall not of itself create contract rights, and the resignation or removal of an officer shall not affect the contract rights, if any, of the corporation or the officer.

Section 4. Vacancies. A vacancy in any office because of death, resignation, removal, or otherwise may be filled by the board of directors for the unexpired portion of the term.

Section 5. President. The president shall be the chief executive officer of the corporation and, subject to the control of the board of directors, shall in general supervise and control all the business and affairs of the corporation. He or she shall preside at all meetings of the stockholders and, in the absence of the chairman or vice chairman, at all meetings of the board of directors. He or she may sign, with the secretary or any other proper officer of the corporation thereunto authorized by the board of directors, certificates for shares of stock of the corporation and any deeds, mortgages, bonds, contracts, or other instruments which the board of directors has authorized to be executed, except in cases where the signing and execution thereof shall be expressly delegated by the board of directors, or by these bylaws to some other officer or agent of the corporation, or shall be required by law to be otherwise signed or executed; and in general he or she shall perform all duties incident to the office of president and such other duties as may be prescribed by the board of directors from time to time.

- 7 -

Section 6. Vice Presidents. In the absence of the president, or in the event of his or her death, inability, or refusal to act, the vice president (or, in the event there be more than one vice president, the vice presidents in the order designated at the time of their election, or, in the absence of any designation, then in the order of their election) shall perform the duties of the president and, when so acting, shall have all the powers of and be subject to all the restrictions upon the president. Any vice president



may sign, with the secretary or an assistant secretary, certificates for shares of stock of the corporation; and shall perform such other duties as from time to time may be assigned to him or her by the president or by the board of directors.

Section 7. Secretary. The secretary shall (a) keep the minutes of the stockholders' and of the board of directors' meetings in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provisions of these bylaws or as required by law; (c) be custodian of the corporate records and responsible for the authentication of such records; (d) keep or cause to be kept a register of the post office address of each stockholder which shall be furnished to the secretary by such stockholder; (e) sign, with the president or a vice president, certificates for shares of stock of the corporation, the issuance of which shall have been authorized by the board of directors; (f) have general charge of the stock transfer books of the corporation; and (g) in general perform all duties incident to the office of secretary and such other duties as from time to time may be assigned to him or her by the president or by the board of directors.

Section 8. Treasurer. If required by the board of directors, the treasurer shall give a bond for the faithful discharge of his or her duties in such sum and with such surety or sureties as the board of directors shall determine. He or she shall (a) have charge and custody of and be responsible for all funds and securities of the corporation, receive and give receipts for moneys due and payable to the corporation from any source whatsoever, and deposit all such moneys in the name of the corporation in such banks, trust companies, or other depositories as shall be selected in accordance with the provisions of Article V of these bylaws; and (b) in general perform all the duties incident to the office of treasurer and such other duties as from time to time may be assigned to him or her by the president or by the board of directors.

Section 9. Assistant Secretaries and Assistant Treasurers. The assistant secretaries, when authorized by the board of directors, may sign, with the president or a vice president, certificates for shares of stock of the corporation, the issuance of which shall have been authorized by the board of directors. The assistant treasurers shall, respectively, if required by the board of directors, give bonds for the faithful discharge of their duties in such sums and with such sureties as the board of directors shall determine. The assistant secretaries and assistant treasurers, in general, shall perform such duties as shall be assigned to them by the secretary or the treasurer, respectively, or by the president or the board of directors.

Section 10. Salaries. The salaries of the officers shall be fixed from time to time by the board of directors and no officer shall be prevented from receiving such salary by reason of the fact that he or she is also a director of the corporation.

- 8 -

#### ARTICLE V. CONTRACTS, LOANS, CHECKS, AND DEPOSITS

Section 1. Contracts. The board of directors may authorize any officer or officers, agent or agents, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the corporation; and such authority may be general or confined to specific instances.

Section 2. Loans. No loans shall be contracted on behalf of the corporation and no evidences of indebtedness shall be issued in its name unless authorized by a resolution of the board of directors. Such authority may be general or confined to specific instances.

Section 3. Checks, Drafts, Etc. All checks, drafts, or other orders for the payment of money, notes, or other evidences of indebtedness issued in the name of the corporation shall be signed by such officer or officers, agent or agents, of the corporation and in such manner as shall from time to time be determined by resolution of the board of directors.

Section 4. Deposits. All funds of the corporation not otherwise employed shall be deposited from time to time to the credit of the corporation in such banks, trust companies, or other depositories as selected by the officer or officers authorized by the board of directors to make such selection.

#### ARTICLE VI. CERTIFICATES FOR SHARES AND THEIR TRANSFER

Section 1. Certificates for Shares. Certificates representing shares of stock of the corporation shall be in such form as shall be determined

by the board of directors. Such certificates shall be signed manually by the president or a vice president and by the secretary or an assistant secretary and may be sealed with the corporate seal or a facsimile thereof. The signatures of such officers on a certificate may be facsimiles if the certificate is countersigned by a transfer agent, or registered by a registrar, other than the corporation itself or an employee of the corporation. All certificates for shares or stock shall be consecutively numbered or otherwise identified. The name and address of the person to whom the shares represented thereby are issued, with the number of shares and date of issue, shall be entered on the stock transfer books of the corporation. All certificates surrendered to the corporation for transfer shall be canceled and no new certificates shall be issued until the former certificate for a like number of shares shall have been surrendered and canceled, except that in case of a lost, stolen, destroyed, or mutilated certificate a new certificate may be issued therefor on such terms and indemnity to the corporation as the board of directors may prescribe.

Section 2. Transfer of Shares. Transfer of shares of stock of the corporation shall be made only on the stock transfer books of the corporation by the holder of record thereof or by his or her legal representative, who shall furnish proper evidence of authority to transfer, or by his or her attorney thereunto authorized by power of attorney duly executed and filed with the secretary of the corporation, and on surrender for cancellation of the

- 9 -

certificate for such shares. The person in whose name shares of stock stand on the books of the corporation shall be deemed by the corporation to be the owner thereof for all purposes.

#### ARTICLE VII. AMENDMENTS

The bylaws may be adopted, altered, or repealed solely by the board of directors.

- 10 -

BARRETT BUSINESS SERVICES, INC.  
AMENDED AND RESTATED 1993 STOCK INCENTIVE PLAN

ARTICLE 1  
ESTABLISHMENT AND PURPOSE

1.1 Establishment. Barrett Business Services, Inc. ("Corporation"), hereby establishes the Barrett Business Services, Inc., 1993 Stock Incentive Plan (the "Plan"), effective as of March 1, 1993, subject to shareholder approval as provided in Article 18. The Plan was previously amended effective March 8, 1994, and is further amended and restated as set forth herein effective March 12, 1997, subject to shareholder approval as provided in Article 16.

1.2 Purpose. The purpose of the Plan is to promote and advance the interests of Corporation and its shareholders by enabling Corporation to attract, retain, and reward key employees, directors, and outside consultants of Corporation and its subsidiaries. It is also intended to strengthen the mutuality of interests between such employees, directors, and consultants and Corporation's shareholders. The Plan is designed to serve these purposes by offering stock options and other equity-based incentive awards, thereby providing a proprietary interest in pursuing the long-term growth, profitability, and financial success of Corporation.

ARTICLE 2  
DEFINITIONS

2.1 Defined Terms. For purposes of the Plan, the following terms shall have the meanings set forth below:

"AWARD" means an award or grant made to a Participant of Options, Stock Appreciation Rights, Restricted Awards, Performance Awards, or Other Stock-Based Awards pursuant to the Plan.

"AWARD AGREEMENT" means an agreement as described in Section 6.4.

"BOARD" means the Board of Directors of Corporation.

"CODE" means the Internal Revenue Code of 1986, as amended and in effect from time to time, or any successor thereto, together with rules, regulations, and interpretations promulgated thereunder. Where the context so requires, any reference to a particular Code section shall be construed to refer to the successor provision to such Code section.

"COMMITTEE" means the committee appointed by the Board to administer the Plan

- 1 -

as provided in Article 3 of the Plan.

"COMMON STOCK" means the \$.01 par value Common Stock of Corporation or any security of Corporation issued in substitution, exchange, or lieu thereof.

"CONSULTANT" means any consultant or adviser to Corporation or a Subsidiary selected by the Committee, who is not an employee of Corporation or a Subsidiary.

"CONTINUING RESTRICTION" means a Restriction contained in Sections 6.5(i), 17.4, 17.5, and 17.7 of the Plan and any other Restrictions expressly designated by the Committee in an Award Agreement as a Continuing Restriction.

"CORPORATION" means Barrett Business Services, Inc., a Maryland corporation, or any successor corporation.

"DEFERRED COMPENSATION OPTION" means a Nonqualified Option granted in lieu of a specified amount of other compensation pursuant to Section 7.8 of the Plan.

"DIRECTOR OPTIONS" means options granted to Non-Employee Board Directors pursuant to Article 14 of the Plan, including Initial Director Options and Annual Director Options.

"DISABILITY" means the condition of being permanently "disabled" within the meaning of Section 22(e)(3) of the Code, namely being

unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months. However, the Committee may change the foregoing definition of "Disability" or may adopt a different definition for purposes of specific Awards.

"EXCHANGE ACT" means the Securities Exchange Act of 1934, as amended and in effect from time to time, or any successor statute. Where the context so requires, any reference to a particular section of the Exchange Act, or to any rule promulgated under the Exchange Act, shall be construed to refer to successor provisions to such section or rule.

"FAIR MARKET VALUE" means on any given date, the fair market value per share of the Common Stock determined as follows:

(a) If the Common Stock is traded on an established securities exchange, the mean between the reported high and low sale prices of Common Stock as reported for such day by the principal exchange on which Common Stock is traded (as determined by the Committee) or, if Common Stock was not traded on such date, on the next preceding day on which Common Stock was traded;

- 2 -

(b) If trading activity in Common Stock is reported in the NASDAQ National Market System, the mean between the reported high and low sale prices of Common Stock as reported for such day by the NASDAQ or, if Common Stock trades were not reported on such date, on the next preceding day on which Common Stock trades were reported by the NASDAQ;

(c) If trading activity in Common Stock is reported in the NASDAQ Bid and Asked Quotations, the mean between the bid price and asked price quote for such day as reported by the NASDAQ or, if there are no such quotes for Common Stock for such date, on the next preceding day for which bid and asked price quotes for Common Stock were reported by NASDAQ; or

(d) If there is no market for Common Stock or if trading activities for Common Stock are not reported in one of the manners described above, the fair market value shall be as determined by the Committee.

"INCENTIVE STOCK OPTION" or "ISO" means any Option granted pursuant to the Plan that is intended to be and is specifically designated in its Award Agreement as an "incentive stock option" within the meaning of Section 422 of the Code.

"NON-EMPLOYEE BOARD DIRECTOR" means a member of the Board who is not an employee of Corporation or any Subsidiary.

"NON-EMPLOYEE SUBSIDIARY DIRECTOR" means a member of the board of directors of a Subsidiary who is neither an employee of Corporation or a Subsidiary nor a member of the Board.

"NONQUALIFIED OPTION" or "NQO" means any Option, including a Deferred Compensation Option, granted pursuant to the Plan that is not an Incentive Stock Option.

"OPTION" means an ISO, an NQO, a Deferred Compensation Option, or a Director Option.

"OTHER STOCK-BASED AWARD" means an Award as defined in Section 11.1.

"PARTICIPANT" means an employee or a Consultant of Corporation or a Subsidiary, a Non-Employee Board Director, or a Non-Employee Subsidiary Director who is granted an Award under the Plan.

"PERFORMANCE AWARD" means an Award granted pursuant to the provisions of Article 10 of the Plan, the Vesting of which is contingent on performance attainment.

- 3 -

"PERFORMANCE CYCLE" means a designated performance period pursuant to the provisions of Section 10.3 of the Plan.

"PERFORMANCE GOAL" means a designated performance objective pursuant to the provisions of Section 10.4 of the Plan.

"PLAN" means this Barrett Business Services, Inc., 1993 Stock Incentive Plan, as set forth herein and as it may be hereafter amended and from time to time.

"REPORTING PERSON" means a Participant who is subject to the reporting requirements of Section 16(a) of the Exchange Act.

"RESTRICTED AWARD" means a Restricted Share or a Restricted Unit granted pursuant to Article 9 of the Plan.

"RESTRICTED SHARE" means an Award described in Section 9.1(a) of the Plan.

"RESTRICTED UNIT" means an Award of units representing Shares described in Section 9.1(b) of the Plan.

"RESTRICTION" means a provision in the Plan or in an Award Agreement which limits the exercisability or transferability, or which governs the forfeiture, of an Award or the Shares, cash, or other property payable pursuant to an Award.

"RETIREMENT" means:

(a) For Participants who are employees, retirement from active employment with Corporation and its Subsidiaries on or after age 65, or such earlier retirement date as approved by the Committee for purposes of the Plan;

(b) For Participants who are Non-Employee Board Directors or Non-Employee Subsidiary Directors, retirement from the applicable board of directors after attaining the maximum age (if any) specified in the articles of incorporation or bylaws of the applicable corporation; or

(c) For Participants who are Consultants, termination of service as a Consultant after attaining a retirement age specified by the Committee for purposes of an Award to such Consultant.

However, the Committee may change the foregoing definition of "Retirement" or may adopt a different definition for purposes of specific Awards.

- 4 -

"SHARE" means a share of Common Stock.

"STOCK APPRECIATION RIGHT" or "SAR" means an Award to benefit from the appreciation of Common Stock granted pursuant to the provisions of Article 8 of the Plan.

"SUBSIDIARY" means a "subsidiary corporation" of Corporation, within the meaning of Section 425 of the Code, namely any corporation in which Corporation directly or indirectly controls 50 percent or more of the total combined voting power of all classes of stock having voting power.

"VEST" or "VESTED" means:

(a) In the case of an Award that requires exercise, to be or to become immediately and fully exercisable and free of all Restrictions (other than Continuing Restrictions);

(b) In the case of an Award that is subject to forfeiture, to be or to become nonforfeitable, freely transferable, and free of all Restrictions (other than Continuing Restrictions);

(c) In the case of an Award that is required to be earned by attaining specified Performance Goals, to be or to become earned and nonforfeitable, freely transferable, and free of all Restrictions (other than Continuing Restrictions); or

(d) In the case of any other Award as to which payment is not dependent solely upon the exercise of a right, election, exercise, or option, to be or to become immediately payable and free of all

Restrictions (except Continuing Restrictions).

2.2 Gender and Number. Except where otherwise indicated by the context, any masculine or feminine terminology used in the Plan shall also include the opposite gender; and the definition of any term in Section 2.1 in the singular shall also include the plural, and vice versa.

ARTICLE 3  
ADMINISTRATION

3.1 General. The Plan shall be administered by a Committee composed as described in Section 3.2.

3.2 Composition of the Committee. The Committee shall be appointed by the Board and shall consist of not less than a sufficient number of Non-Employee Board Directors

- 5 -

so as to qualify the Committee to administer the Plan as contemplated by Rule 16b-3 under the Exchange Act. The Board may from time to time remove members from, or add members to, the Committee. Vacancies on the Committee, however caused, shall be filled by the Board. In the event that the Committee shall cease to satisfy the requirements of Rule 16b-3, the Board shall appoint another Committee satisfying such requirements.

3.3 Authority of the Committee. The Committee shall have full power and authority (subject to such orders or resolutions as may be issued or adopted from time to time by the Board) to administer the Plan in its sole discretion, including the authority to:

- (a) Construe and interpret the Plan and any Award Agreement;
- (b) Promulgate, amend, and rescind rules and procedures relating to the implementation of the Plan;
- (c) Select the employees, Non-Employee Subsidiary Directors, and Consultants who shall be granted Awards;
- (d) Determine the number and types of Awards to be granted to each such Participant;
- (e) Determine the number of Shares, or Share equivalents, to be subject to each Award;
- (f) Determine the option price, purchase price, base price, or similar feature for any Award; and
- (g) Determine all the terms and conditions of all Award Agreements, consistent with the requirements of the Plan.

Decisions of the Committee, or any delegate as permitted by the Plan, shall be final, conclusive, and binding on all Participants.

3.4 Action by the Committee. A majority of the members of the Committee shall constitute a quorum for the transaction of business. Action approved by a majority of the members present at any meeting at which a quorum is present, or action in writing by a majority of the members of the Committee, shall be the valid acts of the Committee.

3.5 Delegation. Notwithstanding the foregoing, the Committee may delegate to one or more officers of Corporation the authority to determine the recipients, types, amounts, and terms of Awards granted to Participants who are not Reporting Persons.

- 6 -

3.6 Liability of Committee Members. No member of the Committee shall be liable for any action or determination made in good faith with respect to the Plan, any Award, or any Participant.

3.7 Costs of Plan. The costs and expenses of administering the Plan shall be borne by Corporation.

ARTICLE 4  
DURATION OF THE PLAN AND SHARES SUBJECT TO THE PLAN

4.1 Duration of the Plan. The Plan is effective March 1, 1993, subject to approval by Corporation's shareholders as provided in Article 18. The Plan shall remain in effect until Awards have been granted covering all the available Shares or the Plan is otherwise terminated by the Board. Termination of the Plan shall not affect outstanding Awards.

4.2 Shares Subject to the Plan. The shares which may be made subject to Awards under the Plan shall be Shares of Common Stock, which may be either authorized and unissued Shares or reacquired Shares. No fractional Shares shall be issued under the Plan. Subject to adjustment pursuant to Article 15, the maximum number of Shares for which Awards may be granted under the Plan shall be 1,300,000. If an Award under the Plan is canceled or expires for any reason prior to having been fully Vested or exercised by a Participant or is settled in cash in lieu of Shares or is exchanged for other Awards, all Shares covered by such Awards shall be made available for future Awards under the Plan.

ARTICLE 5  
ELIGIBILITY

5.1 Employees and Non-Employee Subsidiary Directors. Officers and other key employees of Corporation and its Subsidiaries (including employees who may also be directors of Corporation or a Subsidiary), Consultants, and Non-Employee Subsidiary Directors who, in the Committee's judgment, are or will be contributors to the long-term success of Corporation shall be eligible to receive Awards under the Plan.

5.2 Non-Employee Board Directors. All Non-Employee Board Directors shall be eligible to receive Director Options pursuant to Article 14 of the Plan.

ARTICLE 6  
AWARDS

6.1 Types of Awards. The types of Awards that may be granted under the Plan are:

- 7 -

- (a) Options governed by Article 7 of the Plan;
- (b) Stock Appreciation Rights governed by Article 8 of the Plan;
- (c) Restricted Awards governed by Article 9 of the Plan;
- (d) Performance Awards governed by Article 10 of the Plan;
- (e) Other Stock-Based Awards or combination awards governed by Article 11 of the Plan; and
- (f) Director Options governed by Article 14 of the Plan.

In the discretion of the Committee, any Award (other than a Director Option) may be granted alone, in addition to, or in tandem with other Awards under the Plan.

6.2 General. Subject to the limitations of the Plan, the Committee may cause Corporation to grant Awards to such Participants, at such times, of such types, in such amounts, for such periods, with such option prices, purchase prices, or base prices, and subject to such terms, conditions, limitations, and restrictions as the Committee, in its discretion, shall deem appropriate. Awards may be granted as additional compensation to a Participant or in lieu of other compensation to such Participant. A Participant may receive more than one Award and more than one type of Award under the Plan.

6.3 Nonuniform Determinations. The Committee's determinations under the Plan or under one or more Award Agreements, including without limitation, (a) the selection of Participants to receive Awards, (b) the type, form, amount, and timing of Awards, (c) the terms of specific Award Agreements, and (d) elections and determinations made by the Committee with respect to exercise or payments of Awards, need not be uniform and may be made by the Committee selectively among Participants and Awards, whether or not Participants are similarly situated.

6.4 Award Agreements. Each Award shall be evidenced by a written Award Agreement between Corporation and the Participant. Award Agreements may, subject to the provisions of the Plan, contain any provision

approved by the Committee.

6.5 Provisions Governing All Awards. All Awards shall be subject to the following provisions:

(a) Alternative Awards. If any Awards are designated in their Award Agreements as alternative to each other, the exercise of all or part of one Award automatically shall cause an immediate equal (or pro rata) corresponding

- 8 -

termination of the other alternative Award or Awards.

(b) Rights as Shareholders. No Participant shall have any rights of a shareholder with respect to Shares subject to an Award until such Shares are issued in the name of the Participant.

(c) Employment Rights. Neither the adoption of the Plan nor the granting of any Award shall confer on any person the right to continued employment with Corporation or any Subsidiary or the right to remain as a director of or a Consultant to Corporation or any Subsidiary, as the case may be, nor shall it interfere in any way with the right of Corporation or a Subsidiary to terminate such person's employment or to remove such person as a Consultant or as a director at any time for any reason, with or without cause.

(d) Nontransferable. Each Award (other than Restricted Shares after they Vest) shall not be transferable otherwise than by will or the laws of descent and distribution and shall be exercisable (if exercise is required) during the lifetime of the Participant, only by the Participant or, in the event the Participant becomes legally incompetent, by the Participant's guardian or legal representative.

(e) Termination Of Employment. The terms and conditions under which an Award may be exercised, if at all, after a Participant's termination of employment or service as a Non-Employee Subsidiary Director or a Consultant shall be determined by the Committee and specified in the applicable Award Agreement.

(f) Change in Control. The Committee, in its discretion, may provide in any Award Agreement that in the event of a change in control of Corporation (as the Committee may define such term in the Award Agreement), as of the date of such change in control:

(i) All, or a specified portion of, Awards requiring exercise shall become fully and immediately exercisable, notwithstanding any other limitations on exercise;

(ii) All, or a specified portion of, Awards subject to Restrictions shall become fully Vested; and

(iii) All, or a specified portion of, Awards subject to Performance Goals shall be deemed to have been fully earned.

Unless the Committee specifically provides otherwise in the change in control

- 9 -

provision for a specific Award Agreement, Awards shall become exercisable, become Vested, or become earned as of a change in control date only if, or to the extent, such acceleration in the exercisability, Vesting, or becoming earned of the Awards does not result in an "excess parachute payment" within the meaning of Section 280G(b) of the Code. The Committee, in its discretion, may include change in control provisions in some Award Agreements and not in others, may include different change in control provisions in different Award Agreements, and may include change in control provisions for some Awards or some Participants and not for others.

(g) Conditioning or Accelerating Benefits. The Committee, in its discretion, may include in any Award Agreement a provision conditioning or accelerating the Vesting of an Award or the receipt of



benefits pursuant to an Award, either automatically or in the discretion of the Committee, upon the occurrence of specified events including, without limitation, a change in control of Corporation (subject to the foregoing paragraph (f)), a sale of all or substantially all the property and assets of Corporation, or an event of the type described in Section 15 of this Plan.

(h) Payment of Purchase Price and Withholding. The Committee, in its discretion, may include in any Award Agreement a provision permitting the Participant to pay the purchase or option price, if any, for the Shares or other property issuable pursuant to the Award, or the Participant's federal, state, or local tax, or tax withholding, obligation with respect to such issuance in whole or in part by any one or more of the following:

(i) By delivering previously owned Shares (including Restricted Shares, whether or not vested);

(ii) By surrendering outstanding other Vested Awards under the Plan denominated in Shares or in Share equivalent units;

(iii) By reducing the number of Shares or other property otherwise Vested and issuable pursuant to the Award;

(iv) By delivering to Corporation a promissory note payable on such terms and over such period as the Committee shall determine;

(v) By delivery (in a form approved by the Committee) of an irrevocable direction to a securities broker acceptable to the Committee:

- 10 -

(A) To sell Shares subject to the Option and to deliver all or a part of the sales proceeds to Corporation in payment of all or a part of the option price and taxes or withholding taxes attributable to the issuance; or

(B) To pledge Shares subject to the Option to the broker as security for a loan and to deliver all or a part of the loan proceeds to Corporation in payment of all or a part of the option price and taxes or withholding taxes attributable to the issuance; or

(vi) In any combination of the foregoing or in any other form approved by the Committee.

If Restricted Shares are surrendered in full or partial payment of the purchase or option price of Shares issuable under an Award, a corresponding number of the Shares issued upon exercise of the Award shall be Restricted Shares subject to the same Restrictions as the surrendered Restricted Shares. Shares withheld or surrendered as described above shall be valued based on their Fair Market Value on the date of the transaction. Any Shares withheld or surrendered with respect to a Reporting Person shall be subject to such additional conditions and limitations as the Committee may impose to comply with the requirements of the Exchange Act.

(i) Reporting Persons. With respect to all Awards granted to Reporting Persons:

(i) Awards requiring exercise shall not be exercisable until at least six months after the date the Award was granted, except in the case of the death or Disability of the Participant; and

(ii) Shares issued pursuant to any other Award may not be sold by the Participant for at least six months after acquisition, except in the case of the death or Disability of the Participant;

provided, however, that (unless an Award Agreement provides otherwise) the limitation of this Section 6.5(i) shall apply only if or to the extent required by Rule 16b-3 under the Exchange Act. Award Agreements for Awards to Reporting Persons shall also comply with any future

(j) Service Periods. At the time of granting Awards, the Committee may specify, by resolution or in the Award Agreement, the period or periods of service performed or to be performed by the Participant in connection with the grant of the Award.

ARTICLE 7  
OPTIONS

7.1 Types of Options. Options granted under the Plan may be in the form of Incentive Stock Options or Nonqualified Options (including Deferred Compensation Options and Director Options). The grant of each Option and the Award Agreement governing each Option shall identify the Option as an ISO or an NQO. In the event the Code is amended to provide for tax-favored forms of stock options other than or in addition to Incentive Stock Options, the Committee may grant Options under the Plan meeting the requirements of such forms of options.

7.2 General. Options shall be subject to the terms and conditions set forth in Article 6 and this Article 7 and Award Agreements governing Options shall contain such additional terms and conditions, not inconsistent with the express provisions of the Plan, as the Committee shall deem desirable.

7.3 Option Price. Each Award Agreement for Options shall state the option exercise price per Share of Common Stock purchasable under the Option, which shall not be less than:

(a) \$.01 per share in the case of a Deferred Compensation Option;

(b) 75 percent of the Fair Market Value of a Share on the date of grant for all other Nonqualified Options (except Director Options); or

(c) 100 percent of the Fair Market Value of a Share on the date of grant for all Incentive Stock Options.

7.4 Option Term. The Award Agreement for each Option shall specify the term of each Option, which may be unlimited or may have a specified period during which the Option may be exercised, as determined by the Committee.

7.5 Time of Exercise. The Award Agreement for each Option shall specify, as determined by the Committee:

(a) The time or times when the Option shall become exercisable and whether the Option shall become exercisable in full or in graduated amounts based on: (i) continuation of employment over a period specified in the Award

Agreement, (ii) satisfaction of performance goals or criteria specified in the Award Agreement, or (iii) a combination of continuation of employment and satisfaction of performance goals or criteria;

(b) Such other terms, conditions, and restrictions as to when the Option may be exercised as shall be determined by the Committee; and

(c) The extent, if any, that the Option shall remain exercisable after the Participant ceases to be an employee, Consultant, or director of Corporation or a Subsidiary.

An Award Agreement for an Option may, in the discretion of the Committee, provide whether, and to what extent, the time when an Option becomes exercisable shall be accelerated or otherwise modified (i) in the event of the death, Disability, or Retirement of the Participant, or (ii) upon the occurrence of a change in control of Corporation. The Committee may, at any time in its discretion, accelerate the time when all or any portion of an outstanding Option becomes exercisable.

7.6 Special Rules for Incentive Stock Options. In the case of an Option designated as an Incentive Stock Option, the terms of the Option and the Award Agreement shall conform with the statutory and regulatory requirements specified pursuant to Section 422 of the Code, as in effect on the date such ISO is granted. ISOs may be granted only to employees of Corporation or a Subsidiary. ISOs may not be granted under the Plan after ten years following the date specified in Section 4.1, unless the ten-year limitation of Section 422(b)(2) of the Code is removed or extended.

7.7 Restricted Shares. In the discretion of the Committee, the Shares issuable upon exercise of an Option may be Restricted Shares if so provided in the Award Agreement for the Option.

7.8 Deferred Compensation Options. The Committee may, in its discretion, grant Deferred Compensation Options with an option price less than Fair Market Value to provide a means for deferral to future dates of compensation otherwise payable to a Participant. The option price shall be determined by the Committee subject to Section 7.3(a) of the Plan. The number of Shares subject to a Deferred Compensation Option shall be determined by the Committee, in its discretion, by dividing the amount of compensation to be deferred by the difference between the Fair Market Value of a Share on the date of grant and the option price of the Deferred Compensation Option. Amounts of compensation deferred with Deferred Compensation Options may include amounts payable under Awards granted under the Plan or under any other compensation program or arrangement of Corporation as permitted by the Committee. The Committee shall grant Deferred Compensation Options only if it reasonably determines that the recipient of such an Option is not likely to be deemed to be in constructive

- 13 -

receipt for income tax purposes of the income being deferred.

7.9 Reload Options. The Committee, in its discretion, may provide in an Award Agreement for an Option that in the event all or a portion of the Option is exercised by the Participant using previously acquired Shares, the Participant shall automatically be granted (subject to the available pool of Shares subject to grants of Awards as specified in Section 4.2 of the Plan) a replacement Option (with an option price equal to the Fair Market Value of a Share on the date of such exercise) for a number of Shares equal to (or equal to a portion of) the number of shares surrendered upon exercise of the Option. Such reload Option features may be subject to such terms and conditions as the Committee shall determine, including without limitation, a condition that the Participant retain the Shares issued upon exercise of the Option for a specified period of time.

7.10 Limitation on Number of Shares Subject to Options. In no event may Options for more than 200,000 Shares be granted to any individual under the Plan during any calendar year.

#### ARTICLE 8 STOCK APPRECIATION RIGHTS

8.1 General. Stock Appreciation Rights shall be subject to the terms and conditions set forth in Article 6 and this Article 8 and Award Agreements governing Stock Appreciation Rights shall contain such additional terms and conditions, not inconsistent with the express terms of the Plan, as the Committee shall deem desirable.

8.2 Nature of Stock Appreciation Right. A Stock Appreciation Right is an Award entitling a Participant to receive an amount equal to the excess (or, if the Committee shall determine at the time of grant, a portion of the excess) of the Fair Market Value of a Share of Common Stock on the date of exercise of the SAR over the base price, as described below, on the date of grant of the SAR, multiplied by the number of Shares with respect to which the SAR shall have been exercised. The base price shall be designated by the Committee in the Award Agreement for the SAR and may be the Fair Market Value of a Share on the grant date of the SAR or such other higher or lower price as the Committee shall determine.

8.3 Exercise. A Stock Appreciation Right may be exercised by a Participant in accordance with procedures established by the Committee. The Committee may also provide that a SAR shall be automatically exercised on one or more specified dates or upon the satisfaction of one or more specified conditions. In the case of SARs granted to Reporting Persons, exercise of the SAR shall be limited by the Committee to the extent required to comply with the applicable requirements of Rule 16b-3 under the Exchange Act.

8.4 Form of Payment. Payment upon exercise of a Stock Appreciation Right may be made in cash, in installments, in Shares, by issuance of a Deferred Compensation Option, or in any combination of the foregoing, or in any other form as the Committee shall determine.

8.5 Limitation on Number of Stock Appreciation Rights. In no event may more than 200,000 Stock Appreciation Rights be granted to any individual under the Plan during any calendar year.

ARTICLE 9  
RESTRICTED AWARDS

9.1 Types of Restricted Awards. Restricted Awards granted under the Plan may be in the form of either Restricted Shares or Restricted Units.

(a) Restricted Shares. A Restricted Share is an Award of Shares transferred to a Participant subject to such terms and conditions as the Committee deems appropriate, including, without limitation, restrictions on the sale, assignment, transfer, or other disposition of such Restricted Shares and may include a requirement that the Participant forfeit such Restricted Shares back to Corporation upon termination of Participant's employment (or service as a Non-Employee Subsidiary Director or a Consultant) for specified reasons within a specified period of time or upon other conditions, as set forth in the Award Agreement for such Restricted Shares. Each Participant receiving a Restricted Share shall be issued a stock certificate in respect of such Shares, registered in the name of such Participant, and shall execute a stock power in blank with respect to the Shares evidenced by such certificate. The certificate evidencing such Restricted Shares and the stock power shall be held in custody by Corporation until the Restrictions thereon shall have lapsed.

(b) Restricted Units. A Restricted Unit is an Award of units (with each unit having a value equivalent to one Share) granted to a Participant subject to such terms and conditions as the Committee deems appropriate, and may include a requirement that the Participant forfeit such Restricted Units upon termination of Participant's employment (or service as a Non-Employee Subsidiary Director or a Consultant) for specified reasons within a specified period of time or upon other conditions, as set forth in the Award Agreement for such Restricted Units.

9.2 General. Restricted Awards shall be subject to the terms and conditions of Article 6 and this Article 9 and Award Agreements governing Restricted Awards shall contain such additional terms and conditions, not inconsistent with the express provisions of the Plan, as the Committee shall deem desirable.

9.3 Restriction Period. Award Agreements for Restricted Awards shall provide that Restricted Awards, and the Shares subject to Restricted Awards, may not be transferred, and may provide that, in order for a Participant to Vest in such Restricted Awards, the Participant must remain in the employment (or remain as a Non-Employee Subsidiary Director or a Consultant) of Corporation or its Subsidiaries, subject to relief for reasons specified in the Award Agreement, for a period commencing on the grant date of the Award and ending on such later date or dates as the Committee may designate at the time of the Award (the "Restriction Period"). During the Restriction Period, a Participant may not sell, assign, transfer, pledge, encumber, or otherwise dispose of Shares received under or governed by a Restricted Award grant. The Committee, in its sole discretion, may provide for the lapse of restrictions in installments during the Restriction Period. Upon expiration of the applicable Restriction Period (or lapse of Restrictions during the Restriction Period where the Restrictions lapse in installments) the Participant shall be entitled to settlement of the Restricted Award or portion thereof, as the case may be. Although Restricted Awards shall usually Vest based on continued employment (or service as a Non-Employee Subsidiary Director or a Consultant) and Performance Awards under Article 10 shall usually Vest based on attainment of Performance Goals, the Committee, in its discretion, may condition Vesting of Restricted Awards on attainment of Performance Goals as well as continued employment (or service as a Non-Employee Subsidiary Director or a Consultant). In such case,

the Restriction Period for such a Restricted Award shall include the period prior to satisfaction of the Performance Goals.

9.4 Forfeiture. If a Participant ceases to be an employee (or Consultant or Non-Employee Subsidiary Director) of Corporation or a Subsidiary during the Restriction Period for any reason other than reasons which may be specified in an Award Agreement (such as death, Disability, or Retirement) the Award Agreement may require that all non-Vested Restricted Awards previously granted to the Participant be forfeited and returned to Corporation.

#### 9.5 Settlement of Restricted Awards.

(a) Restricted Shares. Upon Vesting of a Restricted Share Award, the legend on such Shares will be removed and the Participant's stock power will be returned and the Shares will no longer be Restricted Shares. The Committee may also, in its discretion, permit a Participant to receive, in lieu of unrestricted Shares at the conclusion of the Restriction Period, payment in cash, installments, or by issuance of a Deferred Compensation Option equal to the Fair Market Value of the Restricted Shares as of the date the Restrictions lapse.

(b) Restricted Units. Upon Vesting of a Restricted Unit Award, a Participant shall be entitled to receive payment for Restricted Units in an amount equal to the aggregate Fair Market Value of the Shares covered by such Restricted Units at the expiration of the Applicable Restriction Period. Payment in settlement of a Restricted Unit shall be made as soon as practicable following the conclusion of the applicable Restriction Period in cash, in installments, in Shares equal to the number of Restricted Units, by issuance of a Deferred Compensation

- 16 -

Option, or in any other manner or combination of such methods as the Committee, in its sole discretion, shall determine.

9.6 Rights as a Shareholder. A Participant shall have, with respect to unforfeited Shares received under a grant of Restricted Shares, all the rights of a shareholder of Corporation, including the right to vote the shares, and the right to receive any cash dividends. Stock dividends issued with respect to Restricted Shares shall be treated as additional Shares covered by the grant of Restricted Shares and shall be subject to the same Restrictions.

### ARTICLE 10 PERFORMANCE AWARDS

10.1 General. Performance Awards shall be subject to the terms and conditions set forth in Article 6 and this Article 10 and Award Agreements governing Performance Awards shall contain such other terms and conditions not inconsistent with the express provisions of the Plan, as the Committee shall deem desirable.

10.2 Nature of Performance Awards. A Performance Award is an Award of units (with each unit having a value equivalent to one Share) granted to a Participant subject to such terms and conditions as the Committee deems appropriate, including, without limitation, the requirement that the Participant forfeit such Performance Award or a portion thereof in the event specified performance criteria are not met within a designated period of time.

10.3 Performance Cycles. For each Performance Award, the Committee shall designate a performance period (the "Performance Cycle") with a duration to be determined by the Committee in its discretion within which specified Performance Goals are to be attained. There may be several Performance Cycles in existence at any one time and the duration of Performance Cycles may differ from each other.

10.4 Performance Goals. The Committee shall establish Performance Goals for each Performance Cycle on the basis of such criteria and to accomplish such objectives as the Committee may from time to time select. Performance Goals may be based on (i) performance criteria for Corporation, a Subsidiary, or an operating group, (ii) a Participant's individual performance, or (iii) a combination of both. Performance Goals may include objective and subjective criteria. During any Performance Cycle, the Committee may adjust the Performance Goals for such Performance Cycle as it deems equitable in recognition of unusual or nonrecurring events affecting Corporation, changes in applicable tax laws or accounting principles, or such other factors as the Committee may determine.

10.5 Determination of Awards. As soon as practicable after the end of a Performance Cycle, the Committee shall determine the extent to which Performance Awards have been earned on the basis of performance in relation to

10.6 Timing and Form of Payment. Settlement of earned Performance Awards shall be made to the Participant as soon as practicable after the expiration of the Performance Cycle and the Committee's determination under Section 10.5, in the form of cash, installments, Shares, Deferred Compensation Options, or any combination of the foregoing or in any other form as the Committee shall determine.

ARTICLE 11  
OTHER STOCK BASED AND COMBINATION AWARDS

11.1 Other Stock-Based Awards. The Committee may grant other Awards under the Plan pursuant to which Shares are or may in the future be acquired, or Awards denominated in or measured by Share equivalent units, including Awards valued using measures other than the market value of Shares. Other Stock-Based Awards are not restricted to any specified form or structure and may include, without limitation, Share purchase warrants, other rights to acquire Shares, and securities convertible into or redeemable for Shares. Such Other Stock-Based Awards may be granted either alone, in addition to, or in tandem with, any other type of Award granted under the Plan.

11.2 Combination Awards. The Committee may also grant Awards under the Plan in tandem or combination with other Awards or in exchange of Awards, or in tandem or combination with, or as alternatives to, grants or rights under any other employee plan of Corporation, including the plan of any acquired entity. No action authorized by this section shall reduce the amount of any existing benefits or change the terms and conditions thereof without the Participant's consent.

ARTICLE 12  
DEFERRAL ELECTIONS

The Committee may permit a Participant to elect to defer receipt of the payment of cash or the delivery of Shares that would otherwise be due to such Participant by virtue of the exercise, earn out, or Vesting of an Award made under the Plan. If any such election is permitted, the Committee shall establish rules and procedures for such payment deferrals, including, but not limited to: (a) payment or crediting of reasonable interest or other growth or earnings factor on such deferred amounts credited in cash, (b) the payment or crediting of dividend equivalents in respect of deferrals credited in Share equivalent units, or (c) granting of Deferred Compensation Options.

ARTICLE 13  
DIVIDEND EQUIVALENTS

Any Awards may, at the discretion of the Committee, earn dividend equivalents. In respect of any such Award which is outstanding on a dividend record date for Common

Stock, the Participant may be credited with an amount equal to the amount of cash or stock dividends that would have been paid on the Shares covered by such Award, had such covered Shares been issued and outstanding on such dividend record date. The Committee shall establish such rules and procedures governing the crediting of dividend equivalents, including the timing, form of payment, and payment contingencies of such dividend equivalents, as it deems are appropriate or necessary.

ARTICLE 14  
NON-EMPLOYEE BOARD DIRECTORS

14.1 General. Awards shall be made to Non-Employee Board Directors only pursuant to this Article 14. All Non-Employee Board Directors shall receive Initial Director Options and Annual Director Options. No person, including the members of the Board or the Committee, shall have any discretion as to the selection of eligible recipients or the determination of the type, amount, or terms of Awards pursuant to this Article 14.

14.2 Eligibility. The persons eligible to receive Awards pursuant to this Article 14 are all Non-Employee Board Directors of Corporation.

14.3 Definitions. For purposes of this Article 14, the following terms shall have the meanings set forth below:

"ANNUAL MEETING DATE" means the date of Corporation's regular annual meeting of shareholders.

"OFFERING DATE" means the closing date of Corporation's initial public offering of Shares pursuant to a registration statement which has become effective under the Securities Act of 1933.

#### 14.4 Initial Director Options.

(a) Grant of Initial Director Options. As of the Offering Date, each Non-Employee Board Director who is a member of the Board on the Offering Date shall be granted automatically an Initial Director Option to purchase 1,500 Shares.

(b) Option Price. The option purchase price for each Initial Director Option shall be equal to the public offering price of a Share.

(c) Terms of Initial Director Option. Each Initial Director Option shall have the terms and conditions specified in the form of Award Agreement attached to this Plan as Appendix A.

- 19 -

#### 14.5 Annual Director Options.

(a) Grant of Annual Director Options. As of each Annual Meeting Date, each Non-Employee Board Director whose term begins on or continues after that Annual Meeting Date shall be granted automatically an Annual Director Option to purchase 500 Shares.

(b) Option Price. The option exercise price for each Annual Director Option shall be equal to the Fair Market Value of a Share as of the Annual Meeting Date.

(c) Terms of Annual Director Options. Each Annual Director Option shall have the terms and conditions specified in the form of Award Agreement attached to this Plan as Appendix A.

### ARTICLE 15 ADJUSTMENTS UPON CHANGES IN CAPITALIZATION, ETC.

15.1 Plan Does Not Restrict Corporation. The existence of the Plan and the Awards granted under the Plan shall not affect or restrict in any way the right or power of the Board or the shareholders of Corporation to make or authorize any adjustment, recapitalization, reorganization, or other change in Corporation's capital structure or its business, any merger or consolidation of the Corporation, any issue of bonds, debentures, preferred or prior preference stocks ahead of or affecting Corporation's capital stock or the rights thereof, the dissolution or liquidation of Corporation or any sale or transfer of all or any part of its assets or business, or any other corporate act or proceeding.

15.2 Adjustments by the Committee. In the event of any change in capitalization affecting the Common Stock of Corporation, such as a stock dividend, stock split, recapitalization, merger, consolidation, split-up, combination or exchange of shares or other form of reorganization, or any other change affecting the Common Stock, such proportionate adjustments, if any, as the Committee, in its sole discretion, may deem appropriate to reflect such change, shall be made with respect to the aggregate number of Shares for which Awards in respect thereof may be granted under the Plan, the maximum number of Shares which may be sold or awarded to any Participant, the number of Shares covered by each outstanding Award, and the base price or purchase price per Share in respect of outstanding Awards. The Committee may also make such adjustments in the number of Shares covered by, and price or other value of any outstanding Awards in the event of a spin-off or other distribution (other than normal cash dividends), of Corporation assets to shareholders.

- 20 -

ARTICLE 16  
AMENDMENT AND TERMINATION

Without further approval of Corporation's shareholders, the Board may at any time terminate the Plan, or may amend it from time to time in such respects as the Board may deem advisable, except that the Board may not, without approval of the shareholders, make any amendment which would (i) materially increase the benefits accruing to Participants under the Plan, (ii) materially increase the aggregate number of shares of Common Stock which may be issued under the Plan (except for adjustments pursuant to Article 15 of the Plan), or (iii) materially modify the requirements as to eligibility for participation in the Plan. Without further shareholder approval, the Board may amend the Plan to take into account changes in applicable securities, federal income tax laws, and other applicable laws. Further, should the provisions of Rule 16b-3, or any successor rule, under the Exchange Act be amended, the Board, without further shareholder approval, may amend the Plan as necessary to comply with any modifications to such rule. The provisions of Article 14 may not be amended more than once every six months, other than to conform with changes in the Code or in Rule 16b-3 under the Exchange Act.

ARTICLE 17  
MISCELLANEOUS

17.1 Tax Withholding. Corporation shall have the right to deduct from any settlement of any Award under the Plan, including the delivery or vesting of Shares, any federal, state, or local taxes of any kind required by law to be withheld with respect to such payments or to take such other action as may be necessary in the opinion of Corporation to satisfy all obligations for the payment of such taxes. The recipient of any payment or distribution under the Plan shall make arrangements satisfactory to Corporation for the satisfaction of any such withholding tax obligations. Corporation shall not be required to make any such payment or distribution under the Plan until such obligations are satisfied.

17.2 Unfunded Plan. The Plan shall be unfunded and Corporation shall not be required to segregate any assets that may at any time be represented by Awards under the Plan. Any liability of Corporation to any person with respect to any Award under the Plan shall be based solely upon any contractual obligations that may be effected pursuant to the Plan. No such obligation of Corporation shall be deemed to be secured by any pledge of, or other encumbrance on, any property of Corporation.

17.3 Payments to Trust. The Committee is authorized to cause to be established a trust agreement or several trust agreements whereunder the Committee may make payments of amounts due or to become due to Participants in the Plan.

17.4 Annulment of Awards. Any Award Agreement may provide that the grant

- 21 -

of an Award payable in cash is revocable until cash is paid in settlement thereof or that grant of an Award payable in Shares is revocable until the Participant becomes entitled to the certificate in settlement thereof. In the event the employment (or service as a Non-Employee Subsidiary Director or a Consultant) of a Participant is terminated for cause (as defined below), any Award which is revocable shall be annulled as of the date of such termination for cause. For the purpose of this Section 17.4, the term "for cause" shall have the meaning set forth in the Participant's employment agreement, if any, or otherwise means any discharge (or removal) for material or flagrant violation of the policies and procedures of Corporation or for other job performance or conduct which is materially detrimental to the best interests of Corporation, as determined by the Committee.

17.5 Engaging in Competition With the Corporation. Any Award Agreement may provide that, if a Participant terminates employment (or service as a Non-Employee Subsidiary Director or a Consultant) with Corporation or a Subsidiary for any reason whatsoever, and within a period of time (as specified in the Award Agreement) after the date thereof accepts employment with any competitor of (or otherwise engages in competition with) Corporation, the Committee, in its sole discretion, may require such Participant to return to Corporation the economic value of any Award that is realized or obtained (measured at the date of exercise, Vesting, or payment) by such Participant at any time during the period beginning on the date that is six months prior to the date of such Participant's termination of employment (or service as a Non-Employee Subsidiary Director or a Consultant) with Corporation.

17.6 Other Corporation Benefit and Compensation Programs. Payments and other benefits received by a Participant under an Award made



pursuant to the Plan shall not be deemed a part of a Participant's regular, recurring compensation for purposes of the termination indemnity or severance pay law of any state or country and shall not be included in, nor have any effect on, the determination of benefits under any other employee benefit plan or similar arrangement provided by Corporation or a Subsidiary unless expressly so provided by such other plan or arrangements, or except where the Committee expressly determines that an Award or portion of an Award should be included to accurately reflect competitive compensation practices or to recognize that an Award has been made in lieu of a portion of cash compensation. Awards under the Plan may be made in combination with or in tandem with, or as alternatives to, grants, awards, or payments under any other Corporation or Subsidiary plans, arrangements, or programs. The Plan notwithstanding, Corporation or any Subsidiary may adopt such other compensation programs and additional compensation arrangements as it deems necessary to attract, retain, and reward employees and directors for their service with Corporation and its Subsidiaries.

17.7 Securities Law Restrictions. No Shares shall be issued under the Plan unless counsel for Corporation shall be satisfied that such issuance will be in compliance with applicable federal and state securities laws. Certificates for Shares delivered under the Plan may be subject to such stop-transfer orders and other restrictions as the Committee may deem

- 22 -

advisable under the rules, regulations, and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Common Stock is then listed, and any applicable federal or state securities law. The Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions.

17.8 Governing Law. Except with respect to references to the Code or federal securities laws, the Plan and all actions taken thereunder shall be governed by and construed in accordance with the laws of the state of Maryland.

ARTICLE 18  
SHAREHOLDER APPROVAL

The adoption of the Plan and the grant of Awards under the Plan are expressly subject to the approval of the Plan by Corporation's shareholders holding a majority of Corporation's outstanding Shares.

- 23 -

BARRETT BUSINESS SERVICES, INC.  
STATEMENT OF CALCULATION OF AVERAGE  
COMMON SHARES OUTSTANDING

<TABLE>  
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Year	Three Months	
Ended	Ended	
31, 1996	Dec. 31, 1996	Dec.
	-----	----
-----		
Primary Earnings Per Share:	<C>	
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Weighted average number of shares	6,783,811	
6,713,943		
Stock option plan shares to be issued at prices ranging from \$3.50 to \$18.6875 per share	488,855	
501,310		
Warrant issues at a price of \$4.20 per share	90,000	
90,000		
Less: Assumed purchase at average market price during the period using proceeds received upon exercise of options and purchase of stock, and using tax benefits of compensation due to premature dispositions	(406,013)	
(370,365)		
-----		
Total Primary Shares	6,956,653	
6,934,888		
=====		
Fully Diluted Earnings Per Share:		
Weighted average number of shares	6,783,811	
6,713,943		
Stock option plan shares to be issued at prices ranging from \$3.50 to \$18.6875 per share	488,855	
501,310		
Warrant issues at a price of \$4.20 per share	90,000	
90,000		
Less: Assumed purchase at the higher of ending or average market price during the period using proceeds received upon exercise of options and purchase of stock, and using tax benefits of compensation due to premature dispositions	(406,013)	
(361,698)		
-----		
Total Diluted Shares	6,956,653	
6,943,555		
=====		

</TABLE>

CONSENT OF INDEPENDENT ACCOUNTANTS

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (Nos. 33-71792, 33-55117 and 33-52871) and on Form S-3 (Nos. 33-62979 and 333-07751) of Barrett Business Services, Inc. of our report dated February 4, 1997 appearing on page 29 of this Annual Report on Form 10-K.

/s/ Price Waterhouse LLP

PRICE WATERHOUSE LLP

Portland, Oregon  
March 27, 1997

## POWER OF ATTORNEY

Each person whose signature appears below designates and appoints WILLIAM W. SHERERTZ and MICHAEL D. MULHOLLAND, and either of them, true and lawful attorney-in-fact and agents to sign the Annual Report on Form 10-K of Barrett Business Services, Inc., a Maryland corporation, for the year ended December 31, 1996, and to file said report, with all exhibits thereto, with the Securities and Exchange Commission under the Securities Exchange Act of 1934. Each person whose signature appears below also grants full power and authority to these attorneys-in-fact and agents to perform every act and execute any instruments that they deem necessary or desirable in connection with said report, as fully as he could do in person, hereby ratifying and confirming all that the attorneys-in-fact and agents or their substitutes may lawfully do or cause to be done.

IN WITNESS WHEREOF, this power of attorney has been executed by each of the undersigned as of the 12th day of March, 1997.

SIGNATURE	TITLE
/s/ WILLIAM W. SHERERTZ William W. Sherertz	President and Chief Executive Officer and Director (Principal Executive Officer)
/s/ MICHAEL D. MULHOLLAND Michael D. Mulholland	Vice President-Finance (Principal Financial Officer)
/s/ JAMES D. MILLER James D. Miller	Controller (Principal Accounting Officer)
/s/ ROBERT R. AMES Robert R. Ames	Director
/s/ JEFFREY L. BEAUDOIN Jeffrey L. Beaudoin	Director
/s/ STEPHEN A. GREGG Stephen A. Gregg	Director
/s/ ANTHONY MEEKER Anthony Meeker	Director
/s/ STANLEY G. RENECKER Stanley G. Renecker	Director

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This schedule contains summary financial information extracted from the Company's balance sheets and related statements of operations for the period ended December 31, 1996 and is qualified in its entirety by reference to such financial statements.

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