UNITED FIRE & CASUALTY CO
Form 10-Q
August 05, 2011
Table of Contents

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

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FORM 10-Q

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Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

for the quarterly period ended June 30, 2011

Commission File Number 001-34257

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UNITED FIRE & CASUALTY COMPANY
(Exact name of registrant as specified in its charter)

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| Iowa | 42-0644327 |
|---|---|
| (State of Incorporation) | (IRS Employer Identification No.) |

118 Second Avenue, S.E., Cedar Rapids, Iowa 52407
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (319) 399-5700

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 R NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).
YES R NO o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer R Non-accelerated filer o Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES o NO R

As of August 1, 2011, 25,880,210 shares of common stock were outstanding.

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United Fire & Casualty Company and Subsidiaries
Index to Quarterly Report on Form 10-Q
June 30, 2011


| | Page |
|---|---|
| Forward-Looking Information | 1 |
| Part I. Financial Information | |
| Item 1. Financial Statements | |
| Consolidated Balance Sheets as of June 30, 2011 (unaudited) and December 31, 2010 | 2 |
| Consolidated Statements of Income (unaudited) for the three and six month periods ended June 30, 2011 and 2010 | 3 |
| Consolidated Statement of Stockholders' Equity (unaudited) for the six month period ended June 30, 2011 | 4 |
| Consolidated Statements of Cash Flows (unaudited) for the six month periods ended June 30, 2011 and 2010 | 5 |
| Notes to Unaudited Consolidated Financial Statements | 6 |
| Report of Independent Registered Public Accounting Firm | 39 |
| Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations | 40 |
| Item 3. Quantitative and Qualitative Disclosures about Market Risk | 56 |
| Item 4. Controls and Procedures | 57 |
| Part II. Other Information | |
| Item 1. Legal Proceedings | 57 |
| Item 1A. Risk Factors | 57 |
| Item 2. Unregistered Sales of Equity Securities and Use of Proceeds | 58 |
| Item 3. Defaults Upon Senior Securities | 58 |
| Item 4. (Removed and Reserved) | 58 |
| Item 5. Other Information | 58 |
| Item 6. Exhibits | 59 |
| Signatures and Certifications | 60 |

Exhibit 31.1
Exhibit 31.2
Exhibit 32.1
Exhibit 32.2

Table of Contents

FORWARD-LOOKING INFORMATION

It is important to note that our actual results could differ materially from those projected in our forward-looking statements. Information concerning factors that could cause actual results to differ materially from those in the forward-looking statements is contained in Part I, Item 2 “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Part II, Item 1A “Risk Factors.”

Table of Contents

PART I — FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

United Fire & Casualty Company and Subsidiaries
Consolidated Balance Sheets

| (In Thousands, Except Per Share Data and Number of Shares) | June 30, 2011 (unaudited) | December 31, 2010 |
|---|---|---|
| ASSETS | | |
| Investments | | |
| Fixed maturities | | |
| Held-to-maturity, at amortized cost (fair value $5,699 in 2011 and $6,422 in 2010) | $5,664 | $6,364 |
| Available-for-sale, at fair value (amortized cost $2,526,183 in 2011 and $2,178,666 in 2010) | 2,644,475 | 2,278,429 |
| Equity securities, at fair value (cost $69,858 in 2011 and $54,139 in 2010) | 166,315 | 149,706 |
| Trading securities, at fair value (amortized cost $14,763 in 2011 and $12,322 in 2010) | 15,058 | 12,886 |
| Mortgage loans | 6,423 | 6,497 |
| Policy loans | 7,328 | 7,875 |
| Other long-term investments | 20,647 | 20,041 |
| Short-term investments | 1,500 | 1,100 |
| | $2,867,410 | $2,482,898 |
| Cash and cash equivalents | $177,414 | $180,057 |
| Accrued investment income | 32,211 | 28,977 |
| Premiums receivable (net of allowance for doubtful accounts of $715 in 2011 and $1,001 in 2010) | 189,582 | 124,459 |
| Deferred policy acquisition costs | 111,290 | 87,524 |
| Property and equipment (primarily land and buildings, at cost, less accumulated depreciation of $34,962 in 2011 and $33,397 in 2010) | 36,929 | 21,554 |
| Reinsurance receivables and recoverables | 124,840 | 46,731 |
| Prepaid reinsurance premiums | 8,477 | 1,586 |
| Income taxes receivable | 24,432 | 17,772 |
| Goodwill and intangible assets | 31,681 | — |
| Other assets | 17,668 | 15,881 |
| TOTAL ASSETS | $3,621,934 | $3,007,439 |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Liabilities | | |
| Future policy benefits and losses, claims and loss settlement expenses | | |
| Property and casualty insurance | $949,668 | $603,090 |
| Life insurance | 1,419,797 | 1,389,331 |
| Unearned premiums | 302,133 | 200,341 |
| Accrued expenses and other liabilities | 133,217 | 78,439 |
| Deferred income taxes | 13,828 | 19,814 |
| Debt | 82,900 | — |
| Trust preferred securities | 15,618 | — |
| TOTAL LIABILITIES | $2,917,161 | $2,291,015 |
| Stockholders' Equity | | |

| | | |
|---|---|---|
| Common stock, $3.33 1/3 par value; authorized 75,000,000 shares; 25,880,210 and 26,195,552 shares issued and outstanding in 2011 and 2010, respectively | $86,267 | $87,318 |
| Additional paid-in capital | 132,200 | 136,147 |
| Retained earnings | 396,037 | 415,981 |
| Accumulated other comprehensive income, net of tax | 90,269 | 76,978 |
| TOTAL STOCKHOLDERS’ EQUITY | $704,773 | $716,424 |
| TOTAL LIABILITIES AND STOCKHOLDERS’ EQUITY | $3,621,934 | $3,007,439 |

The Notes to Unaudited Consolidated Financial Statements are an integral part of these statements.

Table of Contents

United Fire & Casualty Company and Subsidiaries
Consolidated Statements of Income (Unaudited)

| (In Thousands, Except Per Share Data and Number of Shares) | Three Months Ended June 30, 2011 | Three Months Ended June 30, 2010 | Six Months Ended June 30, 2011 | Six Months Ended June 30, 2010 |
|---|---|---|---|---|
| Revenues | | | | |
| Net premiums earned | $152,210 | $117,082 | $266,414 | $231,390 |
| Investment income, net of investment expenses | 27,741 | 28,291 | 54,804 | 56,259 |
| Net realized investment gains | | | | |
| Other-than-temporary impairment charges | — | (117) | — | (459) |
| All other net realized gains | 1,124 | 2,463 | 3,777 | 5,531 |
| Total net realized investment gains | 1,124 | 2,346 | 3,777 | 5,072 |
| Other income | 729 | 295 | 885 | 418 |
| | $181,804 | $148,014 | $325,880 | $293,139 |
| Benefits, Losses and Expenses | | | | |
| Losses and loss settlement expenses | $135,811 | $72,757 | $211,993 | $141,120 |
| Future policy benefits | 7,880 | 7,375 | 16,062 | 13,765 |
| Amortization of deferred policy acquisition costs | 43,732 | 27,922 | 69,778 | 54,438 |
| Other underwriting expenses | 14,720 | 10,973 | 30,777 | 20,186 |
| Interest on policyholders' accounts | 10,657 | 10,647 | 21,327 | 21,448 |
| | $212,800 | $129,674 | $349,937 | $250,957 |
| Income (loss) before income taxes | $(30,996) | $18,340 | $(24,057) | $42,182 |
| Federal income tax expense (benefit) | (13,082) | 4,409 | (11,953) | 9,138 |
| Net Income (Loss) | $(17,914) | $13,931 | $(12,104) | $33,044 |
| Weighted average common shares outstanding | 26,101,842 | 26,356,353 | 26,148,438 | 26,395,593 |
| Basic earnings (loss) per common share | (0.69) | 0.53 | (0.46) | 1.25 |
| Diluted earnings (loss) per common share | (0.69) | 0.53 | (0.46) | 1.25 |
| Cash dividends declared per common share | 0.15 | 0.15 | 0.30 | 0.30 |

The Notes to Unaudited Consolidated Financial Statements are an integral part of these statements.

Table of Contents

United Fire & Casualty Company and Subsidiaries
Consolidated Statement of Stockholders' Equity (Unaudited)

| (In Thousands, Except Per Share Data) | Six Months Ended June 30, 2011 |
|---|---|
| **Common stock** | |
| Balance, beginning of year | $87,318 |
| Shares repurchased (323,597 shares) | (1,078) |
| Shares issued for stock-based awards (8,255 shares) | 27 |
| Balance, end of period | $86,267 |
| **Additional paid-in capital** | |
| Balance, beginning of year | $136,147 |
| Compensation expense and related tax benefit for stock-based award grants | 945 |
| Shares repurchased | (5,004) |
| Shares issued for stock-based awards | 112 |
| Balance, end of period | $132,200 |
| **Retained earnings** | |
| Balance, beginning of year | $415,981 |
| Net income (loss) | (12,104) |
| Dividends on common stock ($0.30 per share) | (7,840) |
| Balance, end of period | $396,037 |
| **Accumulated other comprehensive income, net of tax** | |
| Balance, beginning of year | $76,978 |
| Change in net unrealized appreciation [1] | 12,455 |
| Change in underfunded status of employee benefit plans | 836 |
| Balance, end of period | $90,269 |
| **Summary of changes** | |
| Balance, beginning of year | $716,424 |
| Net income (loss) | (12,104) |
| All other changes in stockholders' equity accounts | 453 |
| Balance, end of period | $704,773 |

(1) The change in net unrealized appreciation is net of reclassification adjustments.

The Notes to Unaudited Consolidated Financial Statements are an integral part of these statements.

Table of Contents

United Fire & Casualty Company and Subsidiaries
Consolidated Statements of Cash Flows (Unaudited)

| (In Thousands) | Six Months Ended June 30, 2011 | 2010 |
|---|---|---|
| Cash Flows From Operating Activities | | |
| Net income (loss) | $(12,104) | $33,044 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities | | |
| Net accretion of bond premium | 3,768 | 1,891 |
| Depreciation and amortization | 1,708 | 1,455 |
| Stock-based compensation expense | 939 | 878 |
| Net realized investment gains | (3,777) | (5,072) |
| Net cash flows from trading investments | (2,104) | 2,379 |
| Deferred income tax expense (benefit) | (7,571) | 2,976 |
| Changes in: | | |
| Accrued investment income | 507 | (761) |
| Premiums receivable | (29,226) | (16,915) |
| Deferred policy acquisition costs | (6,373) | (4,614) |
| Reinsurance receivables | (5,883) | (7,374) |
| Prepaid reinsurance premiums | (602) | (86) |
| Income taxes receivable | (4,029) | 11,464 |
| Other assets | (806) | 1,859 |
| Future policy benefits and losses, claims and loss settlement expenses | 52,813 | 12,659 |
| Unearned premiums | 29,542 | 16,881 |
| Accrued expenses and other liabilities | 25,493 | (4,377) |
| Deferred income taxes | (1,019) | (2,325) |
| Other, net | (486) | (494) |
| Total adjustments | $52,894 | $10,424 |
| Net cash provided by operating activities | $40,790 | $43,468 |
| Cash Flows From Investing Activities | | |
| Proceeds from sale of available-for-sale investments | $21,367 | $3,402 |
| Proceeds from call and maturity of held-to-maturity investments | 709 | 1,603 |
| Proceeds from call and maturity of available-for-sale investments | 316,235 | 192,888 |
| Proceeds from short-term and other investments | 1,554 | 3,200 |
| Purchase of available-for-sale investments | (292,808) | (277,962) |
| Purchase of short-term and other investments | (1,706) | (3,308) |
| Change in securities lending collateral | — | (75,013) |
| Net purchases and sales of property and equipment | 3,486 | (960) |
| Acquisition of property and casualty company, net of cash acquired | (172,619) | — |
| Net cash used in investing activities | $(123,782) | $(156,150) |
| Cash Flows From Financing Activities | | |
| Policyholders' account balances | | |
| Deposits to investment and universal life contracts | $71,489 | $70,669 |
| Withdrawals from investment and universal life contracts | (57,263) | (55,437) |
| Borrowings of short-term debt | 79,900 | — |
| Change in securities lending payable | — | 75,013 |
| Payment of cash dividends | (7,840) | (7,910) |
| Repurchase of common stock | (6,082) | (3,689) |
| Issuance of common stock | 139 | 23 |

| | | |
|---|---|---|
| Tax benefit from issuance of common stock | 6 | 1 |
| Net cash provided by financing activities | $80,349 | $78,670 |
| Net Change in Cash and Cash Equivalents | $(2,643) | $(34,012) |
| Cash and Cash Equivalents at Beginning of Period | 180,057 | 190,852 |
| Cash and Cash Equivalents at End of Period | $177,414 | $156,840 |

The Notes to Unaudited Consolidated Financial Statements are an integral part of these statements.

Table of Contents

United Fire & Casualty Company and Subsidiaries
Notes to Unaudited Consolidated Financial Statements

## NOTE 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

### Nature of Business

The terms "United Fire," "we," "us," or "our" refer to United Fire & Casualty Company or United Fire & Casualty Company and its consolidated subsidiaries and its affiliate, as the context requires. We are engaged in the business of writing property and casualty insurance and life insurance and selling annuities through a network of independent agencies. We report our operations in two business segments: property and casualty insurance and life insurance. We are licensed as a property and casualty insurer in 43 states plus the District of Columbia and as a life insurer in 29 states.

### Basis of Presentation

We maintain our records in conformity with the accounting practices prescribed or permitted by the insurance departments of the states in which we are domiciled. To the extent that certain of these practices differ from U.S. generally accepted accounting principles ("GAAP"), we have made adjustments to present the accompanying unaudited Consolidated Financial Statements in conformity with GAAP. Certain financial information that is included in our Annual Report on Form 10-K, including certain financial statement footnote disclosures, are not required by the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial reporting and have been condensed or omitted.

The preparation of financial statements in conformity with 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 reporting period. Actual results could differ from those estimates. The financial statement categories that are most dependent on management estimates and assumptions include: investments; deferred policy acquisition costs; goodwill and intangible assets; and future policy benefits and losses, claims and loss settlement expenses.

In the preparation of the accompanying unaudited Consolidated Financial Statements, we have evaluated all material subsequent events or transactions that occurred after the balance sheet date through the date on which the financial statements were issued for potential recognition or disclosure therein.

Certain prior year amounts have been reclassified to conform to the current year presentation.

In the opinion of the management of United Fire, the accompanying unaudited Consolidated Financial Statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows for the periods presented. All significant intercompany transactions have been eliminated in consolidation. The results reported for the interim periods are not necessarily indicative of the results of operations that may be expected for the year. The unaudited Consolidated Financial Statements should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2010. The review report of Ernst & Young LLP as of and for the three- and six-month periods ended June 30, 2011, accompanies the unaudited Consolidated Financial Statements included in Part I, Item 1 "Financial Statements."

### Acquisition of Mercer Insurance Group

On March 28, 2011, we acquired 100 percent of the outstanding common stock of Mercer Insurance Group for cash consideration of $191.5 million. Accordingly, the results of operations for Mercer Insurance Group have been included in the accompanying unaudited Consolidated Financial Statements from that date forward. After the acquisition, we market through over 1,200 independent property and casualty agencies. In addition, the acquisition allows us to diversify our exposure to weather and other catastrophe risks across our geographic markets.

Table of Contents

This transaction was accounted for under the purchase method of accounting using Mercer Insurance Group historical financial information and applying fair value estimates to the acquired assets, liabilities and commitments as of the acquisition date. For additional information related to this acquisition, see Note 10, "Business Combinations."
In connection with this acquisition, we incurred $5.5 million of expense in the first quarter of 2011 related to change in control payments made to the former executive officers of Mercer Insurance Group.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash, money market accounts, and non-negotiable certificates of deposit with original maturities of three months or less.
For the six-month periods ended June 30, 2011 and 2010, we made payments for income taxes of $0.6 million and $10.5 million, respectively. For the six-month period ended June 30, 2011, we received no tax refunds compared to tax refunds of $13.5 million for the same period of 2010, that were received due to the overpayment of prior year tax and operating loss carrybacks.
We made no significant payments of interest for the six-month periods ended June 30, 2011 and 2010, other than for interest credited to policyholders' accounts.

Income Taxes

Deferred tax assets and liabilities are established based on differences between the financial statement bases of assets and liabilities and the tax bases of those same assets and liabilities, using the currently enacted statutory tax rates. Deferred income tax expense is measured by the year-to-year change in the net deferred tax asset or liability, except for certain changes in deferred tax amounts that affect stockholders' equity and do not impact federal income tax expense.
We reported a federal income tax benefit of $12.0 million and a federal income tax expense of $9.1 million for the six-month periods ended June 30, 2011 and 2010, respectively. Our effective tax rate is different than the federal statutory rate of 35.0 percent due principally to the effect of tax-exempt municipal bond interest income and non-taxable dividend income.
We have recognized no liability for unrecognized tax benefits at June 30, 2011 or December 31, 2010, or at any time during the six-month period ended June 30, 2011. In addition, we have not accrued for interest and penalties related to unrecognized tax benefits. However, if interest and penalties would need to be accrued related to unrecognized tax benefits, such amounts would be recognized as a component of federal income tax expense.
We file a consolidated federal income tax return. We also file income tax returns in various state jurisdictions. We are no longer subject to federal or state income tax examination for years before 2006. There are ongoing examinations of income tax returns by the Internal Revenue Service of the 2008 tax year, by the State of Illinois of the 2007 and 2008 tax years and by the State of Florida of the 2008 through 2010 tax years.

Recently Issued Accounting Standards

Adopted Accounting Standards

Fair Value Measurements

In January 2010, the Financial Accounting Standards Board ("FASB") issued revised accounting guidance that clarifies and provides additional disclosure requirements related to recurring and non-recurring fair value measurements. The guidance requires separate disclosures for the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements, along with an explanation for the transfers. Additionally, a separate disclosure is required for purchases, sales, issuances and settlements on a gross basis for Level 3 fair value measurements. The guidance also provides additional clarification for both the level of disaggregation reported for

Table of Contents

each class of assets or liabilities and disclosures of inputs and valuation techniques used to measure fair value for both recurring and non-recurring fair value measurements for assets and liabilities categorized as Level 2 or Level 3.
The new disclosures and clarifications of existing disclosures were effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements, which are effective for fiscal years beginning after December 15, 2010. Refer to Note 3 "Fair Value of Financial Instruments" for the information required to be disclosed upon our adoption of the guidance, effective January 1, 2011.

Pending Adoption of Accounting Standards

Policy Acquisition Costs

In October 2010, the FASB issued updated accounting guidance to address the diversity in practice for the accounting for costs associated with acquiring or renewing insurance contracts. This guidance modifies the definition of acquisition costs to specify that a cost must be incremental and directly related to the successful acquisition of a new or renewal insurance contract in order to be deferred. Acquisition costs that are not eligible for deferral are to be charged to expense in the period incurred. If application of this guidance would result in the capitalization of acquisition costs that had not previously been capitalized by a reporting entity, the entity may elect not to capitalize those costs. The updated guidance is effective for interim and annual reporting periods beginning after December 15, 2011. We are currently evaluating the impact that our adoption of the guidance, effective January 1, 2012, will have on our Consolidated Financial Statements.

Fair Value Measurements

In May 2011, the FASB issued updated accounting guidance that changes the wording used to describe many of the requirements in GAAP for measuring fair value and for disclosing information about fair value measurements to ensure consistency between GAAP and International Financial Reporting Standards. The guidance also expands the disclosures for fair value measurements that are estimated using significant unobservable (Level 3) inputs. This new guidance is to be applied prospectively. We are currently evaluating the impact that our adoption of the guidance, effective January 1, 2013, will have on the information disclosed in our Consolidated Financial Statements.

Comprehensive Income

In June 2011, the FASB issued revised accounting guidance that eliminates the option to present the components of other comprehensive income as part of the statement of stockholders' equity. Instead, comprehensive income must be reported in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. The guidance will be effective for public companies during the interim and annual periods beginning after December 15, 2011 with early adoption permitted. This new guidance is to be applied retrospectively. We have not adopted this guidance and currently we are evaluating the impact that our adoption of this guidance will have on the presentation of our Consolidated Financial Statements.

NOTE 2. SUMMARY OF INVESTMENTS

Fair Value of Investments

A reconciliation of the amortized cost (cost for equity securities) to fair value of investments in held-to-maturity and available-for-sale fixed maturity and equity securities as of June 30, 2011 and December 31, 2010, is as follows:

Table of Contents

| June 30, 2011 | (Dollars in Thousands) | | | |
|---|---|---|---|---|
| Type of Investment | Cost or Amortized Cost | Gross Unrealized Appreciation | Gross Unrealized Depreciation | Fair Value |
| HELD-TO-MATURITY | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| States, municipalities and political subdivisions | | | | |
| General obligations | $733 | $8 | $— | $741 |
| Special revenue | | | | |
| Midwest | | | | |
| North central - East | 353 | 20 | — | 373 |
| North central - West | 268 | 19 | — | 287 |
| Northeast | 230 | 6 | — | 236 |
| South | 793 | 2 | 94 | 701 |
| West | 2,838 | 30 | — | 2,868 |
| Collaterialized mortgage obligations | 64 | 3 | — | 67 |
| Mortgage-backed securities | 385 | 41 | — | 426 |
| Total Held-to-Maturity Fixed Maturities | $5,664 | $129 | $94 | $5,699 |
| AVAILABLE-FOR-SALE | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| U.S. government and government- sponsored enterprises | | | | |
| U.S. Treasury | $40,100 | $1,163 | $— | $41,263 |
| Agency | 107,197 | 195 | 433 | 106,959 |
| States, municipalities and political subdivisions | | | | |
| General obligations | | | | |
| Midwest | | | | |
| North central - East | 123,304 | 8,439 | 84 | 131,659 |
| North central - West | 74,823 | 5,612 | — | 80,435 |
| Northeast | 38,952 | 2,343 | — | 41,295 |
| South | 104,747 | 8,136 | 12 | 112,871 |
| West | 67,618 | 4,241 | 20 | 71,839 |
| Special revenue | | | | |
| Midwest | | | | |
| North central - East | 69,969 | 3,526 | 44 | 73,451 |
| North central - West | 51,540 | 2,620 | 96 | 54,064 |
| Northeast | 13,907 | 470 | 2 | 14,375 |
| South | 95,604 | 4,622 | 40 | 100,186 |
| West | 55,804 | 3,090 | 3 | 58,891 |
| Foreign bonds | | | | |
| Canadian | 63,569 | 3,596 | 159 | 67,006 |
| Other foreign | 98,242 | 4,940 | 217 | 102,965 |
| Public utilities | | | | |
| Electric | 218,289 | 12,012 | 327 | 229,974 |
| Oil and gas | 27,430 | 1,584 | 106 | 28,908 |
| Other | 9,044 | 343 | — | 9,387 |
| Corporate bonds | | | | |

| | | | | |
|---|---|---|---|---|
| Oil and gas | 179,621 | 6,665 | 306 | 185,980 |
| Chemicals | 66,191 | 3,159 | 160 | 69,190 |
| Basic resources | 18,609 | 564 | 182 | 18,991 |
| Construction and materials | 20,409 | 737 | — | 21,146 |
| Industrial goods and services | 162,890 | 7,318 | 370 | 169,838 |

Table of Contents

| | | | | |
|---|---|---|---|---|
| Auto and parts | 12,680 | 611 | 41 | 13,250 |
| Food and beverage | 73,454 | 2,708 | 39 | 76,123 |
| Personal and household goods | 64,197 | 3,053 | 127 | 67,123 |
| Health care | 109,703 | 6,050 | 45 | 115,708 |
| Retail | 49,796 | 2,290 | 31 | 52,055 |
| Media | 40,239 | 1,980 | 99 | 42,120 |
| Travel and leisure | 5,867 | 12 | 50 | 5,829 |
| Telecommunications | 42,250 | 1,851 | 7 | 44,094 |
| Utilities | 10,500 | 619 | — | 11,119 |
| Banks | 142,485 | 6,814 | 929 | 148,370 |
| Insurance | 28,926 | 1,031 | — | 29,957 |
| Real estate | 21,732 | 2,811 | 202 | 24,341 |
| Financial services | 109,912 | 3,766 | 756 | 112,922 |
| Technology | 29,857 | 1,174 | 196 | 30,835 |
| Collaterialized mortgage obligations | | | | |
| Government | 30,339 | 2,360 | 8 | 32,691 |
| Other | 302 | 2 | — | 304 |
| Mortgage-backed securities | 39,108 | 570 | 2 | 39,676 |
| Asset-backed securities | 6,572 | 524 | 220 | 6,876 |
| Redeemable preferred stocks | 405 | 4 | — | 409 |
| Total Available-For-Sale Fixed Maturities | $2,526,183 | $123,605 | $5,313 | $2,644,475 |
| Equity securities | | | | |
| Common stocks | | | | |
| Public utilities | | | | |
| Electric | $5,921 | $4,945 | $1 | $10,865 |
| Oil and gas | 928 | 2,004 | — | 2,932 |
| Other | 76 | 4 | — | 80 |
| Corporate | | | | |
| Oil and gas | 5,094 | 7,126 | — | 12,220 |
| Chemicals | 2,734 | 3,649 | — | 6,383 |
| Industrial good and services | 9,427 | 15,158 | 55 | 24,530 |
| Auto and parts | 257 | 621 | — | 878 |
| Food and beverage | 2,124 | 3,861 | — | 5,985 |
| Personal and household goods | 6,857 | 3,729 | — | 10,586 |
| Health care | 7,612 | 7,365 | 134 | 14,843 |
| Retail | 2,609 | 491 | 63 | 3,037 |
| Media | 147 | — | 3 | 144 |
| Telecommunications | 2,399 | 3,741 | 3 | 6,137 |
| Utilities | 1,502 | 138 | — | 1,640 |
| Banks | 12,971 | 31,708 | 178 | 44,501 |
| Insurance | 3,209 | 10,025 | 8 | 13,226 |
| Real estate | 393 | 782 | 43 | 1,132 |
| Financial services | 300 | 241 | — | 541 |
| Technology | 1,664 | 1,436 | 17 | 3,083 |
| Nonredeemable preferred stocks | 3,634 | 19 | 81 | 3,572 |
| Total Available-for-Sale Equity Securities | $69,858 | $97,043 | $586 | $166,315 |
| Total Available-for-Sale Securities | $2,596,041 | $220,648 | $5,899 | $2,810,790 |

| December 31, 2010 | (Dollars in Thousands) | | | |
|---|---|---|---|---|
| Type of Investment | Cost or Amortized Cost | Gross Unrealized Appreciation | Gross Unrealized Depreciation | Fair Value |
| HELD-TO-MATURITY | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| States, municipalities and political subdivisions | | | | |
| General obligations | 731 | 10 | — | 741 |
| Special revenue | | | | |
| Midwest | | | | |
| North central - East | 364 | 27 | — | 391 |
| North central - West | 488 | 23 | — | 511 |
| Northeast | 230 | 12 | — | 242 |
| South | 1,067 | 4 | 108 | 963 |
| West | 2,957 | 36 | — | 2,993 |
| Collateralized mortgage obligations | 83 | 4 | — | 87 |
| Mortgage-backed securities | 444 | 50 | — | 494 |
| Total Held-to-Maturity Fixed Maturities | $6,364 | $ 166 | $ 108 | $6,422 |
| AVAILABLE-FOR-SALE | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| U.S. government and government- sponsored enterprises | | | | |
| U.S. Treasury | 38,133 | 943 | — | 39,076 |
| Agency | 104,049 | 96 | 1,014 | 103,131 |
| States, municipalities and political subdivisions | | | | |
| General obligations | | | | |
| Midwest | | | | |
| North central - East | 121,273 | 6,634 | 137 | 127,770 |
| North central - West | 76,699 | 4,491 | 58 | 81,132 |
| Northeast | 27,861 | 1,664 | — | 29,525 |
| South | 92,795 | 6,555 | 53 | 99,297 |
| West | 53,160 | 2,983 | 90 | 56,053 |
| Special revenue | | | | |
| Midwest | | | | |
| North central - East | 59,063 | 2,205 | 175 | 61,093 |
| North central - West | 38,827 | 1,744 | 266 | 40,305 |
| Northeast | 4,505 | 247 | 9 | 4,743 |
| South | 71,486 | 3,405 | 144 | 74,747 |
| West | 42,363 | 2,182 | — | 44,545 |
| Foreign bonds | | | | |
| Canadian | 69,209 | 3,908 | 194 | 72,923 |
| Other foreign | 85,434 | 4,588 | 268 | 89,754 |
| Public utilities | | | | |
| Electric | 207,047 | 12,179 | 519 | 218,707 |
| Oil and gas | 53,919 | 1,724 | 359 | 55,284 |
| Corporate bonds | | | | |
| Oil and gas | 150,692 | 6,957 | 138 | 157,511 |

| | | | | |
|---|---|---|---|---|
| Chemicals | 58,570 | 2,808 | 35 | 61,343 |
| Basic resources | 8,043 | 582 | — | 8,625 |
| Construction and materials | 19,385 | 873 | — | 20,258 |
| Industrial goods and services | 141,509 | 7,102 | 481 | 148,130 |
| Auto and parts | 13,453 | 1,003 | — | 14,456 |

Table of Contents

| | | | | |
|---|---|---|---|---|
| Food and beverage | 70,613 | 3,531 | 111 | 74,033 |
| Personal and household goods | 65,525 | 2,953 | 289 | 68,189 |
| Health care | 78,595 | 4,933 | 186 | 83,342 |
| Retail | 42,150 | 2,139 | 329 | 43,960 |
| Media | 33,276 | 1,786 | — | 35,062 |
| Travel and leisure | 5,882 | 61 | 77 | 5,866 |
| Telecommunications | 33,131 | 2,094 | 51 | 35,174 |
| Utilities | 13,620 | 521 | — | 14,141 |
| Banks | 117,506 | 5,817 | 1,689 | 121,634 |
| Insurance | 25,682 | 799 | 14 | 26,467 |
| Real estate | 20,903 | 1,101 | 267 | 21,737 |
| Financial services | 94,036 | 3,770 | 983 | 96,823 |
| Technology | 15,952 | 1,070 | 334 | 16,688 |
| Collateralized mortgage obligations | 17,564 | 2,013 | — | 19,577 |
| Mortgage-backed securities | 2 | — | — | 2 |
| Asset-backed securities | 6,754 | 572 | — | 7,326 |
| Total Available-For-Sale Fixed Maturities | $2,178,666 | $108,033 | $8,270 | $2,278,429 |
| Equity securities | | | | |
| Common stocks | | | | |
| Public utilities | | | | |
| Electric | $5,921 | $4,164 | $1 | $10,084 |
| Oil and gas | 928 | 1,746 | — | 2,674 |
| Corporate | | | | |
| Oil and gas | 4,903 | 6,235 | — | 11,138 |
| Chemicals | 2,734 | 3,345 | — | 6,079 |
| Industrical goods and services | 8,112 | 15,185 | — | 23,297 |
| Auto and parts | 704 | 922 | — | 1,626 |
| Food and beverage | 682 | 3,792 | — | 4,474 |
| Personal and household goods | 4,785 | 2,985 | — | 7,770 |
| Health care | 6,366 | 6,368 | 187 | 12,547 |
| Retail | 380 | 348 | — | 728 |
| Travel and leisure | 1 | — | — | 1 |
| Telecommunications | 2,150 | 3,138 | — | 5,288 |
| Utilities | 1,102 | 47 | 2 | 1,147 |
| Banks | 9,517 | 34,636 | 100 | 44,053 |
| Insurance | 3,129 | 11,320 | 41 | 14,408 |
| Real estate | 619 | 967 | 40 | 1,546 |
| Financial services | 282 | — | 15 | 267 |
| Technology | 363 | 826 | — | 1,189 |
| Nonredeemable preferred stocks | 1,461 | 3 | 74 | 1,390 |
| Total Available-for-Sale Equity Securities | $54,139 | $96,027 | $460 | $149,706 |
| Total Available-for-Sale Securities | $2,232,805 | $204,060 | $8,730 | $2,428,135 |

12

Table of Contents

Maturities

The amortized cost and fair value of held-to-maturity, available-for-sale and trading securities at June 30, 2011, by contractual maturity, are shown in the following table. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Asset-backed securities, mortgage-backed securities and collateralized mortgage obligations may be subject to prepayment risk and are therefore not categorized by contractual maturity.

| (In Thousands) | Held-To-Maturity | | Available-For-Sale | | Trading | |
|---|---|---|---|---|---|---|
| June 30, 2011 | Amortized Cost | Fair Value | Amortized Cost | Fair Value | Amortized Cost | Fair Value |
| Due in one year or less | $245 | $251 | $261,784 | $268,500 | $2,712 | $2,798 |
| Due after one year through five years | 4,967 | 4,952 | 1,173,647 | 1,240,235 | 4,645 | 4,681 |
| Due after five years through 10 years | 3 | 3 | 950,562 | 990,505 | 496 | 495 |
| Due after 10 years | — | — | 63,869 | 65,688 | 6,910 | 7,084 |
| Asset-backed securities | — | — | 6,572 | 6,876 | — | — |
| Mortgage-backed securities | 385 | 426 | 39,108 | 39,676 | — | — |
| Collateralized mortgage obligations | 64 | 67 | 30,641 | 32,995 | — | — |
| | $5,664 | $5,699 | $2,526,183 | $2,644,475 | $14,763 | $15,058 |

Net Realized Investment Gains and Losses

Net realized gains (losses) on disposition of investments are computed using the specific identification method and are included in the computation of net income. A summary of net realized investment gains resulting from investment sales, calls and other-than-temporary impairment (“OTTI”) charges is as follows:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| Net realized investment gains (losses) | | | | |
| Fixed maturities | $1,048 | $373 | $2,434 | $862 |
| Equity securities | 218 | 2,565 | 1,334 | 4,909 |
| Trading securities | (38) | (592) | 278 | (684) |
| Other long-term investments | (104) | — | (269) | (15) |
| Total net realized investment gains | $1,124 | $2,346 | $3,777 | $5,072 |

The proceeds and gross realized gains and losses on the sale of available-for-sale securities are as follows:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| Proceeds from sales | $16,520 | $2,800 | $21,367 | $3,402 |
| Gross realized gains | 261 | 1,513 | 351 | 1,915 |
| Gross realized losses | 172 | — | 688 | — |

There were no sales of held-to-maturity securities during the six-month periods ended June 30, 2011 and 2010.

Our investment portfolio includes trading securities with embedded derivatives. These securities, which are primarily convertible redeemable preferred debt securities, are recorded at fair value. Income or loss, including the change in the fair value of these trading securities, is recognized currently in earnings as a component of net realized investment gains and losses. Our portfolio of trading securities had a fair value of $15.1 million and $12.9 million at June 30, 2011 and December 31, 2010, respectively.

Table of Contents

The realized gains and losses attributable to the change in fair value during the reporting period of trading securities held at June 30, 2011 and 2010 are as follows:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| Trading | | | | |
| Realized gains | $(164) | $— | $31 | $— |
| Realized losses | 273 | 609 | 300 | 896 |

Off-Balance Sheet Arrangements

Pursuant to an agreement with one of our limited liability partnership holdings, we are contractually committed to make capital contributions up to $15.0 million, upon request by the partnership, through December 31, 2017. Our remaining potential contractual obligation was $10.1 million at June 30, 2011.

Unrealized Appreciation and Depreciation

A summary of changes in net unrealized investment appreciation during the reporting period is as follows:

| | Six Months Ended June 30, | |
|---|---|---|
| (In Thousands) | 2011 | 2010 |
| Change in net unrealized investment appreciation | | |
| Available-for-sale fixed maturities and equity securities | $19,419 | $24,526 |
| Deferred policy acquisition costs | (257) | (11,576) |
| Income tax effect | (6,707) | (4,533) |
| Total change in net unrealized appreciation, net of tax | $12,455 | $8,417 |

In the above table, changes in deferred policy acquisition costs for our life insurance segment are affected by fluctuations that may occur in the interest rate environment from time to time.

We continually monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires OTTI charges to be recorded when we determine that it is more likely than not that we will be unable to collect all amounts due according to the contractual terms of the fixed maturity security or that the anticipated recovery in fair value of the equity security will not occur in a reasonable amount of time. Impairment charges on investments are recorded based on the fair value of the investments at the measurement date. Factors considered in evaluating whether a decline in value is other-than-temporary include: the length of time and the extent to which fair value has been less than cost; the financial condition and near-term prospects of the issuer; our intention to hold the investment; and the likelihood that we will be required to sell the investment.

The tables on the following pages summarize our fixed maturity and equity securities that were in an unrealized loss position at June 30, 2011 and December 31, 2010. The securities are presented by the length of time they have been continuously in an unrealized loss position. It is possible that we could recognize OTTI charges in future periods on securities held at June 30, 2011, if future events or information cause us to determine that a decline in fair value is other-than-temporary.

We believe the unrealized depreciation in value of securities in our fixed maturity portfolio is primarily attributable to changes in market interest rates and not the credit quality of the issuer. We have no intent to sell and it is more likely than not that we will not be required to sell these securities until such time as the fair value recovers to at least equal our cost basis or the securities mature.

We have evaluated the unrealized losses reported for all of our equity securities at June 30, 2011, and have concluded that the duration and severity of these losses do not warrant the recognition of an OTTI charge at June 30, 2011. Our largest unrealized loss greater than 12 months on an individual equity security at June 30, 2011 was $0.1 million. We have no intention to sell any of these securities prior to a recovery in value, but will continue to monitor the fair value reported for these securities as part of our overall process to evaluate investments for OTTI recognition.

Table of Contents

| (In Thousands) | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| June 30, 2011 | Less than 12 months | | | 12 months or longer | | | Total | |
| Type of Investment | Number of Issues | Fair Value | Gross Unrealized Depreciation | Number of Issues | Fair Value | Gross Unrealized Depreciation | Fair Value | Gross Unrealized Depreciation |
| HELD-TO-MATURITY | | | | | | | | |
| Fixed maturities | | | | | | | | |
| Bonds | | | | | | | | |
| States, municipalities and political subdivisions | | | | | | | | |
| Special revenue | | | | | | | | |
| South | — | $— | $ — | 1 | $601 | $ 94 | $601 | $ 94 |
| Total Held-to-Maturity Fixed Maturities | — | $— | $ — | 1 | $601 | $ 94 | $601 | $ 94 |
| AVAILABLE-FOR-SALE | | | | | | | | |
| Fixed maturities | | | | | | | | |
| Bonds | | | | | | | | |
| U.S. government and government-sponsored enterprises | | | | | | | | |
| Agency | 13 | 52,606 | 433 | — | — | — | 52,606 | 433 |
| States, municipalities and political subdivisions | | | | | | | | |
| General obligations | | | | | | | | |
| Midwest | 5 | 2,688 | 84 | — | — | — | 2,688 | 84 |
| South | 3 | 1,992 | 12 | — | — | — | 1,992 | 12 |
| West | 1 | 771 | 20 | — | — | — | 771 | 20 |
| Special revenue | | | | | | | | |
| Midwest | | | | | | | | |
| North central - East | — | — | — | 1 | 866 | 44 | 866 | 44 |
| North central - West | 3 | 1,637 | 29 | 2 | 2,647 | 67 | 4,284 | 96 |
| Northeast | — | — | — | 1 | 618 | 2 | 618 | 2 |
| South | 6 | 4,461 | 40 | — | — | — | 4,461 | 40 |
| West | 1 | 245 | 3 | — | — | — | 245 | 3 |
| Foreign bonds | | | | | | | | |
| Canadian | 2 | 7,403 | 159 | — | — | — | 7,403 | 159 |
| Other foreign | 5 | 14,658 | 190 | 1 | 1,115 | 27 | 15,773 | 217 |
| Public utilities | | | | | | | | |
| Electric | 5 | 18,982 | 216 | 1 | 1,171 | 111 | 20,153 | 327 |
| Oil and gas | 2 | 4,558 | 106 | — | — | — | 4,558 | 106 |
| Corporate bonds | | | | | | | | |
| Oil and gas | 6 | 22,175 | 306 | — | — | — | 22,175 | 306 |
| Chemicals | 2 | 8,374 | 160 | — | — | — | 8,374 | 160 |
| Basic resources | 2 | 7,992 | 182 | — | — | — | 7,992 | 182 |
| Industrial goods and services | 10 | 22,094 | 268 | 1 | 2,897 | 102 | 24,991 | 370 |
| Auto and parts | 2 | 3,117 | 41 | — | — | — | 3,117 | 41 |
| Food and beverage | 1 | 3,060 | 19 | 1 | 1,449 | 20 | 4,509 | 39 |
| Personal and household goods | 2 | 6,201 | 127 | — | — | — | 6,201 | 127 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Health care | 1 | 3,005 | 45 | — | — | — | 3,005 | 45 |
| Retail | 1 | 3,431 | 31 | — | — | — | 3,431 | 31 |
| Media | 3 | 7,008 | 99 | — | — | — | 7,008 | 99 |
| Travel and leisure | 4 | 5,016 | 50 | — | — | — | 5,016 | 50 |
| Telecommunications | 1 | 1,975 | 7 | — | — | — | 1,975 | 7 |
| Banks | 4 | 2,845 | 1 | 8 | 17,488 | 928 | 20,333 | 929 |
| Real estate | 1 | 2,297 | 28 | 1 | 4,469 | 174 | 6,766 | 202 |
| Financial services | 2 | 8,378 | 109 | 15 | 5,297 | 647 | 13,675 | 756 |

Table of Contents

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Technology | 4 | 9,390 | 196 | — | — | — | 9,390 | 196 |
| Collateralized mortgage obligations | 8 | 1,476 | 8 | — | — | — | 1,476 | 8 |
| Mortgage backed securities | — | — | — | 3 | 745 | 2 | 745 | 2 |
| Asset backed securities | 2 | 466 | 220 | — | — | — | 466 | 220 |
| Total Available-For-Sale Fixed Maturities | 102 | $228,301 | $3,189 | 35 | $38,762 | $2,124 | $267,063 | $5,313 |
| Equity securities | | | | | | | | |
| Common stocks | | | | | | | | |
| Public utilities | — | $— | $— | 4 | $— | $1 | $— | $1 |
| Corporate | | | | | | | | |
| Industrial goods and services | 12 | 1,564 | 55 | — | — | — | 1,564 | 55 |
| Health care | 4 | 439 | 25 | 1 | 385 | 109 | 824 | 134 |
| Retail | 6 | 689 | 63 | — | — | — | 689 | 63 |
| Media | 1 | 144 | 3 | — | — | — | 144 | 3 |
| Telecommunications | 1 | 16 | 3 | — | — | — | 16 | 3 |
| Banks | 2 | 360 | 65 | 1 | 441 | 113 | 801 | 178 |
| Insurance | 1 | 79 | 2 | 1 | 50 | 6 | 129 | 8 |
| Real estate | 1 | 78 | 11 | 2 | 156 | 32 | 234 | 43 |
| Technology | 3 | 575 | 17 | — | — | — | 575 | 17 |
| Nonredeemable preferred stocks | — | — | — | 2 | 1,151 | 81 | 1,151 | 81 |
| Total Available-for-Sale Equity Securities | 31 | $3,944 | $244 | 11 | $2,183 | $342 | $6,127 | $586 |
| Total Available-for-Sale Securities | 133 | $232,245 | $3,433 | 46 | $40,945 | $2,466 | $273,190 | $5,899 |
| Total | 133 | $232,245 | $3,433 | 47 | $41,546 | $2,560 | $273,791 | $5,993 |

Table of Contents

| (In Thousands)<br>December 31, 2010 | Less than 12 months | | | 12 months or longer | | | Total | |
|---|---|---|---|---|---|---|---|---|
| Type of Investment | Number of Issues | Fair Value | Gross Unrealized Depreciation | Number of Issues | Fair Value | Gross Unrealized Depreciation | Fair Value | Gross Unrealized Depreciation |
| HELD-TO-MATURITY | | | | | | | | |
| Fixed maturities | | | | | | | | |
| Bonds | | | | | | | | |
| States, municipalities and political subdivisions | | | | | | | | |
| Special revenue | — | $— | $ — | 2 | $590 | $ 108 | $590 | $ 108 |
| Total Held-to-Maturity Fixed Maturities | — | $— | $ — | 2 | $590 | $ 108 | $590 | $ 108 |
| AVAILABLE-FOR-SALE | | | | | | | | |
| Fixed maturities | | | | | | | | |
| Bonds | | | | | | | | |
| U.S. government and government-sponsored enterprises | | | | | | | | |
| Agency | 12 | $41,374 | $ 626 | 7 | $30,661 | $ 388 | $72,035 | $ 1,014 |
| States, municipalities and political subdivisions | | | | | | | | |
| General obligations | | | | | | | | |
| Midwest | | | | | | | | |
| North central - East | 3 | 2,346 | 105 | 1 | 497 | 32 | 2,843 | 137 |
| North central - West | 1 | 860 | 58 | — | — | — | 860 | 58 |
| South | 2 | 947 | 53 | — | — | — | 947 | 53 |
| West | 3 | 2,723 | 90 | — | — | — | 2,723 | 90 |
| Special revenue | | | | | | | | |
| Midwest | | | | | | | | |
| North central - East | 7 | 8,275 | 96 | 2 | 2,554 | 79 | 10,829 | 175 |
| North central - West | 2 | 3,092 | 102 | 2 | 2,555 | 164 | 5,647 | 266 |
| Northeast | — | — | — | 1 | 771 | 9 | 771 | 9 |
| South | 3 | 3,964 | 144 | — | — | — | 3,964 | 144 |
| Foreign bonds | | | | | | | | |
| Canadian | 1 | 5,687 | 194 | — | — | — | 5,687 | 194 |
| Other foreign | 2 | 6,634 | 235 | 2 | 2,873 | 33 | 9,507 | 268 |
| Public utilities | | | | | | | | |
| Electric | 3 | 4,490 | 100 | 3 | 10,003 | 419 | 14,493 | 519 |
| Oil and gas | — | — | — | 3 | 5,840 | 359 | 5,840 | 359 |
| Corporate bonds | | | | | | | | |
| Oil and gas | — | — | — | 2 | 5,748 | 138 | 5,748 | 138 |
| Chemicals | 3 | 3,366 | 19 | 1 | 4,939 | 16 | 8,305 | 35 |
| Industrial goods and services | 5 | 13,642 | 170 | 3 | 9,748 | 311 | 23,390 | 481 |
| Food and beverage | 1 | 2,006 | 12 | 2 | 4,491 | 99 | 6,497 | 111 |
| Personal and household goods | 3 | 9,233 | 241 | 2 | 3,039 | 48 | 12,272 | 289 |
| Health care | 4 | 14,416 | 186 | — | — | — | 14,416 | 186 |
| Retail | 4 | 9,370 | 322 | 1 | 2,308 | 7 | 11,678 | 329 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Travel and leisure | 1 | 2,013 | 69 | 2 | 792 | 8 | 2,805 | 77 |
| Telecommunications | 2 | 2,696 | 51 | — | — | — | 2,696 | 51 |
| Banks | 1 | 2,920 | 18 | 15 | 28,887 | 1,671 | 31,807 | 1,689 |
| Insurance | 1 | 2,169 | 14 | — | — | — | 2,169 | 14 |
| Real estate | 1 | 4,539 | 177 | 1 | 2,256 | 90 | 6,795 | 267 |
| Financial services | 3 | 11,660 | 236 | 15 | 5,270 | 747 | 16,930 | 983 |
| Other | — | — | — | 3 | 8,628 | 334 | 8,628 | 334 |

Table of Contents

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Total Available-For-Sale Fixed Maturities | 68 | $158,422 | $3,318 | 68 | $131,860 | $4,952 | $290,282 | $8,270 |
| Equity securities | | | | | | | | |
| Common stocks | | | | | | | | |
| Public utilities | — | $— | $— | 4 | $— | $1 | $— | $1 |
| Corporate | | | | | | | | |
| Health care | 2 | 1,437 | 63 | 1 | 371 | 124 | 1,808 | 187 |
| Utilities | 3 | 306 | 2 | — | — | — | 306 | 2 |
| Banks | 2 | 594 | 32 | 1 | 488 | 68 | 1,082 | 100 |
| Insurance | 1 | 260 | 28 | 1 | 43 | 13 | 303 | 41 |
| Real estate | 1 | 79 | 10 | 2 | 158 | 30 | 237 | 40 |
| Financial services | 1 | 267 | 15 | — | — | — | 267 | 15 |
| Nonredeemable preferred stocks | — | — | — | 2 | 1,158 | 74 | 1,158 | 74 |
| Total Available-for-Sale Equity Securities | 11 | $2,963 | $150 | 11 | $2,218 | $310 | $5,181 | $460 |
| Total Available-for-Sale Securities | 79 | $161,385 | $3,468 | 79 | $134,078 | $5,262 | $295,463 | $8,730 |
| Total | 79 | $161,385 | $3,468 | 81 | $134,668 | $5,370 | $296,053 | $8,838 |

Table of Contents

NOTE 3. FAIR VALUE OF FINANCIAL INSTRUMENTS

We estimate the fair value of our financial instruments based on relevant market information or by discounting estimated future cash flows at estimated current market discount rates appropriate to the specific asset or liability.

In most cases, we use quoted market prices to determine the fair value of fixed maturities, equity securities, trading securities and short-term investments. When quoted market prices do not exist, we base fair values on pricing or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement of the financial instrument. Such inputs may reflect management's own assumptions about the assumptions a market participant would use in pricing the financial instrument.

We base the estimated fair value of mortgage loans on discounted cash flows, utilizing the market rate of interest for similar loans in effect at the valuation date.

The estimated fair value of policy loans is equivalent to carrying value. We do not make policy loans for amounts in excess of the cash surrender value of the related policy. In all instances, the policy loans are fully collateralized by the related liability for future policy benefits for traditional insurance policies or by the policyholders' account balance for non-traditional policies.

Our other long-term investments consist primarily of holdings in limited liability partnership funds that are valued by the various fund managers and are recorded on the equity method of accounting. In management's opinion, these values represent fair value.

For cash and cash equivalents and accrued investment income, carrying value is a reasonable estimate of fair value due to the short-term nature of these financial instruments.

We calculate the fair value of the liabilities for all of our annuity products based upon the estimated value of the business, using current market rates and forecast assumptions and risk-adjusted discount rates, when relevant observable market data does not exist.

A summary of the carrying value and estimated fair value of our financial instruments at June 30, 2011 and December 31, 2010 is as follows:

| | June 30, 2011 | | December 31, 2010 | |
|---|---|---|---|---|
| (In Thousands) | Fair Value | Carrying Value | Fair Value | Carrying Value |
| Assets | | | | |
| Investments | | | | |
| Held-to-maturity fixed maturities | $5,699 | $5,664 | $6,422 | $6,364 |
| Available-for-sale fixed maturities | 2,644,475 | 2,644,475 | 2,278,429 | 2,278,429 |
| Equity securities | 166,315 | 166,315 | 149,706 | 149,706 |
| Trading securities | 15,058 | 15,058 | 12,886 | 12,886 |
| Mortgage loans | 7,273 | 6,423 | 7,658 | 6,497 |
| Policy loans | 7,328 | 7,328 | 7,875 | 7,875 |
| Other long-term investments | 20,647 | 20,647 | 20,041 | 20,041 |
| Short-term investments | 1,500 | 1,500 | 1,100 | 1,100 |
| Cash and cash equivalents | 177,414 | 177,414 | 180,057 | 180,057 |
| Accrued investment income | 32,211 | 32,211 | 28,977 | 28,977 |
| Liabilities | | | | |
| Policy reserves | | | | |
| Annuity (accumulations) (1) | $1,003,859 | $962,819 | $965,932 | $948,920 |
| Annuity (benefit payments) | 110,213 | 90,359 | 102,511 | 86,874 |

(1) Annuity accumulations represent deferred annuity contracts which are currently earning interest.

Table of Contents

Current accounting guidance on fair value measurements includes the application of a fair value hierarchy that requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Our financial instruments that are recorded at fair value are categorized into a three-level hierarchy, which is based upon the priority of the inputs to the valuation technique. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets (i.e., Level 1) and the lowest priority to unobservable inputs (i.e., Level 3). If the inputs used to measure fair value fall within different levels of the hierarchy, the category level is based on the lowest priority level input that is significant to the fair value measurement of the financial instrument.
Financial instruments recorded at fair value are categorized in the fair value hierarchy as follows:

- Level 1: Valuations are based on unadjusted quoted prices in active markets for identical financial instruments that we have the ability to access.
- Level 2: Valuations are based on quoted prices for similar financial instruments, other than quoted prices included in Level 1, in markets that are not active or on inputs that are observable either directly or indirectly for the full term of the financial instrument.
- Level 3: Valuations are based on pricing or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement of the financial instrument. Such inputs may reflect management’s own assumptions about the assumptions a market participant would use in pricing the financial instrument.

Transfers between levels, if any, are recorded as of the beginning of the reporting period.
To determine the fair value of the majority of our investments, we utilize prices obtained from independent, nationally recognized pricing services. We obtain one price for each security. When the pricing services cannot provide a determination of fair value for a specific security, we obtain non-binding price quotes from broker-dealers with whom we have had several years experience and who have demonstrated knowledge of the subject security. We request and utilize one broker quote per security.
We validate the prices obtained from pricing services and brokers prior to their use for reporting purposes by evaluating their reasonableness on a monthly basis. Our validation process includes a review for unusual fluctuations. In our opinion, the pricing obtained at June 30, 2011 was reasonable.
In order to determine the proper classification in the fair value hierarchy for each security where the price is obtained from an independent pricing service, we obtain and evaluate the vendors’ pricing procedures and inputs used to price the security, which include unadjusted quoted market prices for identical securities, such as a New York Stock Exchange closing price and quoted prices for identical securities in markets that are not active. For fixed maturity securities, an evaluation of interest rates and yield curves observable at commonly quoted intervals, volatility, prepayment speeds, credit risks and default rates may also be performed. We have determined that these processes and inputs result in fair values and classifications consistent with the applicable current accounting guidance on fair value measurements.
We review our fair value hierarchy categorizations on a quarterly basis at which time the classification of certain financial instruments may change if the input observations have changed.

The following tables present the categorization for our financial instruments measured at fair value on a recurring basis at June 30, 2011 and December 31, 2010:

Table of Contents

| (In Thousands) | | Fair Value Measurements | | |
|---|---|---|---|---|
| Description | June 30, 2011 | Level 1 | Level 2 | Level 3 |
| AVAILABLE-FOR-SALE | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| U.S. government and government-sponsored enterprises | | | | |
| U.S. Treasury | $41,263 | $— | $41,263 | $— |
| Agency | 106,959 | — | 106,959 | — |
| States, municipalities and political subdivisions | | | | |
| General obligations | | | | |
| North central - East | 131,659 | — | 131,659 | — |
| North central - West | 80,435 | — | 80,435 | — |
| Northeast | 41,295 | — | 41,295 | — |
| South | 112,871 | — | 112,871 | — |
| West | 71,839 | — | 71,839 | — |
| Special revenue | | | | |
| North central - East | 73,451 | — | 72,511 | 940 |
| North central - West | 54,064 | — | 54,064 | — |
| Northeast | 14,375 | — | 14,375 | — |
| South | 100,186 | — | 100,186 | — |
| West | 58,891 | — | 58,891 | — |
| Foreign bonds | | | | |
| Canadian | 67,006 | — | 67,006 | — |
| Other foreign | 102,965 | — | 101,850 | 1,115 |
| Public utilities | | | | |
| Electric | 229,974 | — | 229,974 | — |
| Oil and gas | 28,908 | — | 28,908 | — |
| Other | 9,387 | — | 9,387 | — |
| Corporate bonds | | | | |
| Oil and gas | 185,980 | — | 185,980 | — |
| Chemicals | 69,190 | — | 69,190 | — |
| Basic resources | 18,991 | — | 18,991 | — |
| Construction and materials | 21,146 | — | 21,146 | — |
| Industrial goods and services | 169,838 | — | 169,838 | — |
| Auto and parts | 13,250 | — | 13,250 | — |
| Food and beverage | 76,123 | — | 76,123 | — |
| Personal and household goods | 67,123 | — | 64,674 | 2,449 |
| Health care | 115,708 | — | 115,708 | — |
| Retail | 52,055 | — | 52,055 | — |
| Media | 42,120 | — | 42,120 | — |
| Travel and leisure | 5,829 | — | 5,829 | — |
| Telecommunications | 44,094 | — | 44,094 | — |
| Utilities | 11,119 | | 11,119 | — |
| Banks | 148,370 | — | 148,370 | — |
| Insurance | 29,957 | — | 29,957 | — |
| Real estate | 24,341 | — | 20,934 | 3,407 |
| Financial services | 112,922 | — | 112,922 | — |

| | | | | |
|---|---|---|---|---|
| Technology | 30,835 | — | 30,835 | — |
| Collateralized mortgage obligations | | | | |
| Government | 32,691 | — | 32,691 | — |
| Other | 304 | — | 304 | — |

Table of Contents

| | | | | |
|---|---|---|---|---|
| Mortgage-backed securities | 39,676 | — | 39,676 | — |
| Asset-backed securities | 6,876 | — | 6,561 | 315 |
| Redeemable preferred stocks | 409 | — | 409 | — |
| Total Available-For-Sale Fixed Maturities | $2,644,475 | $— | $2,636,249 | $8,226 |
| Equity securities | | | | |
| Common stocks | | | | |
| Public utilities | | | | |
| Electric | $10,865 | $10,865 | $— | $— |
| Oil and gas | 2,932 | 2,932 | — | — |
| Other | 80 | 80 | — | — |
| Corporate | | | | |
| Oil and gas | 12,220 | 12,220 | — | — |
| Chemicals | 6,383 | 6,383 | — | — |
| Industrial goods and services | 24,530 | 24,530 | — | — |
| Autos and parts | 878 | 878 | — | — |
| Food and beverage | 5,985 | 5,985 | — | — |
| Personal and household goods | 10,586 | 10,586 | — | — |
| Health care | 14,843 | 14,843 | — | — |
| Retail | 3,037 | 3,037 | — | — |
| Media | 144 | 144 | — | — |
| Telecommunications | 6,137 | 6,137 | — | — |
| Utilities | 1,640 | 1,640 | — | — |
| Banks | 44,501 | 39,694 | — | 4,807 |
| Insurance | 13,226 | 13,226 | — | — |
| Real estate | 1,132 | 1,132 | — | — |
| Financial services | 541 | 541 | — | — |
| Technology | 3,083 | 3,083 | — | — |
| Nonredeemable preferred stocks | 3,572 | 1,853 | 1,719 | — |
| Total Available-for-Sale Equity Securities | $166,315 | $159,789 | $1,719 | $4,807 |
| Total Available-for-Sale Securities | $2,810,790 | $159,789 | $2,637,968 | $13,033 |
| TRADING | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| Foreign bonds | | | | |
| Canadian | 1,566 | — | 1,566 | — |
| Other foreign | 1,372 | — | 1,372 | — |
| Corporate | | | | |
| Basic resources | 1,347 | — | 1,347 | — |
| Food and beverage | 1,098 | — | 1,098 | — |
| Health care | 1,952 | — | 1,952 | — |
| Utilities | 1,447 | — | 1,447 | — |
| Banks | 2,383 | — | 2,383 | — |
| Insurance | 495 | — | 495 | — |
| Real estate | 431 | — | 431 | — |
| Redeemable preferred stocks | 2,967 | — | 2,967 | — |
| Total Trading Securities | $15,058 | $— | $15,058 | $— |
| Short-Term Investments | $1,500 | $1,500 | $— | $— |
| Money Market Accounts | $83,099 | $83,099 | $— | $— |
| Total | $2,910,447 | $244,388 | $2,653,026 | $13,033 |

Table of Contents

| (In Thousands) | | Fair Value Measurements | | |
|---|---|---|---|---|
| Description | December 31, 2010 | Level 1 | Level 2 | Level 3 |
| AVAILABLE-FOR-SALE | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| U.S. government and government-sponsored enterprises | | | | |
| U.S. Treasury | $39,076 | $— | $39,076 | $— |
| Agency | 103,131 | — | 103,131 | — |
| States, municipalities and political subdivisions | | | | |
| General obligations | | | | |
| North central - East | 127,770 | — | 127,770 | — |
| North central - West | 81,132 | — | 81,132 | — |
| Northeast | 29,525 | — | 29,525 | — |
| South | 99,297 | — | 99,297 | — |
| West | 56,053 | — | 56,053 | — |
| Special revenue | | | | |
| North central - East | 61,093 | — | 60,092 | 1,001 |
| North central - West | 40,305 | — | 40,305 | — |
| Northeast | 4,743 | — | 4,743 | — |
| South | 74,747 | — | 74,747 | — |
| West | 44,545 | — | 44,545 | — |
| Foreign bonds | | | | |
| Canadian | 72,923 | — | 72,923 | — |
| Other foreign | 89,754 | — | 88,639 | 1,115 |
| Public utilities | | | | |
| Electric | 218,707 | — | 218,672 | 35 |
| Oil and gas | 55,284 | — | 55,284 | — |
| Corporate bonds | | | | |
| Oil and gas | 157,511 | — | 157,511 | — |
| Chemicals | 61,343 | — | 61,343 | — |
| Basic resources | 8,625 | — | 8,625 | — |
| Construction and materials | 20,258 | — | 20,258 | — |
| Industrial goods and services | 148,130 | — | 145,233 | 2,897 |
| Auto and parts | 14,456 | — | 14,456 | — |
| Food and beverage | 74,033 | — | 72,551 | 1,482 |
| Personal and household goods | 68,189 | — | 65,686 | 2,503 |
| Health care | 83,342 | — | 83,342 | — |
| Retail | 43,960 | — | 43,960 | — |
| Media | 35,062 | — | 35,062 | — |
| Travel and leisure | 5,866 | — | 5,866 | — |
| Telecommunications | 35,174 | — | 35,174 | — |
| Utilities | 14,141 | — | 14,141 | — |
| Banks | 121,634 | — | 114,111 | 7,523 |
| Insurance | 26,467 | — | 26,467 | — |
| Real estate | 21,737 | — | 13,764 | 7,973 |
| Financial services | 96,823 | — | 95,722 | 1,101 |
| Technology | 16,688 | — | 16,688 | — |

| | | | | |
|---|---|---|---|---|
| Collateralized mortgage obligations | 19,577 | — | 19,577 | — |
| Mortgage-backed securities | 2 | — | 2 | — |
| Asset-backed securities | 7,326 | — | 7,326 | — |
| Total Available-For-Sale Fixed Maturities | $2,278,429 | $— | $2,252,799 | $25,630 |

Table of Contents

| | | | | |
|---|---|---|---|---|
| Equity securities | | | | |
| Common stocks | | | | |
| Public utilities | | | | |
| Electric | $10,084 | $10,084 | $— | $— |
| Oil and gas | 2,674 | 2,674 | — | — |
| Corporate | | | | |
| Oil and gas | 11,138 | 11,138 | — | — |
| Chemicals | 6,079 | 6,079 | — | — |
| Industrial goods and services | 23,297 | 23,297 | — | — |
| Auto and parts | 1,626 | 1,626 | — | — |
| Food and beverage | 4,474 | 4,474 | — | — |
| Personal and household goods | 7,770 | 7,770 | — | — |
| Health care | 12,547 | 12,547 | — | — |
| Retail | 728 | 728 | — | — |
| Travel and leisure | 1 | 1 | — | — |
| Telecommunications | 5,288 | 5,257 | 31 | — |
| Utilities | 1,147 | 1,147 | — | — |
| Banks | 44,053 | 42,518 | — | 1,535 |
| Insurance | 14,408 | 14,408 | — | — |
| Real estate | 1,546 | 1,546 | — | — |
| Financial services | 267 | 267 | — | — |
| Technology | 1,189 | 1,189 | — | — |
| Nonredeemable preferred stocks | 1,390 | 1,158 | 232 | — |
| Total Available-for-Sale Equity Securities | $149,706 | $147,908 | $263 | $1,535 |
| Total Available-for-Sale Securities | $2,428,135 | $147,908 | $2,253,062 | $27,165 |
| TRADING | | | | |
| Fixed maturities | | | | |
| Bonds | | | | |
| Foreign bonds | $2,283 | $— | $2,283 | $— |
| Corporate bonds | | | | |
| Oil and gas | 2,843 | — | 2,843 | — |
| Health care | 1,917 | — | 1,917 | — |
| Utilities | 1,394 | — | 1,394 | — |
| Banks | 1,198 | — | 1,198 | — |
| Financial services | 384 | — | 384 | — |
| Redeemable preferred stocks | 2,867 | 1,476 | 1,391 | — |
| Total Trading Securities | $12,886 | $1,476 | $11,410 | $— |
| Short-Term Investments | $1,100 | $1,100 | $— | $— |
| Money Market Accounts | $34,384 | $34,384 | $— | $— |
| Total | $2,476,505 | $184,868 | $2,264,472 | $27,165 |

Table of Contents

The fair value of securities that are categorized as Level 1 is based on quoted market prices that are readily and regularly available.
The fair value of securities that are categorized as Level 2 is determined by management after reviewing market prices obtained from independent pricing services and brokers. Such estimated fair values do not necessarily represent the values for which these securities could have been sold at the reporting date. Our independent pricing services and brokers obtain prices from reputable pricing vendors in the marketplace. They continually monitor and review the external pricing sources, while actively participating to resolve any pricing issues that may arise.
For the six-month period ended June 30, 2011, the change in our available-for-sale securities categorized as Level 1 and Level 2 is the result of investment purchases (and disposals) made during the period, which were made from funds held in our money market accounts, and the change in unrealized gains on both fixed maturities and equity securities. There were no significant transfers of securities in or out of Level 1 or Level 2 during the period.
Securities that may be categorized as Level 3 include holdings in certain private placement fixed maturity and equity securities and certain other securities that were determined to be other-than-temporarily impaired in a prior period and for which an active market does not currently exist.
The fair value of our Level 3 private placement securities is determined by management relying on pricing received from our independent pricing services and brokers consistent with the process to estimate fair value for Level 2 securities.
The fair value of our Level 3 impaired securities was determined primarily based upon management's assumptions regarding the timing and amount of future cash inflows. If a security has been written down or the issuer is in bankruptcy, management relies in part on outside opinions from rating agencies, our lien position on the security, general economic conditions and management's expertise to determine fair value. We have the ability and the positive intent to hold securities until such time that we are able to recover all or a portion of our original investment. If a security does not have a market at the balance sheet date, management will estimate the security's fair value based on other securities in the market. Management will continue to monitor securities after the balance sheet date to confirm that their estimated fair value is reasonable.

The following table provides a summary of the changes in fair value of our Level 3 securities for the three-month period ended June 30, 2011:

| (In Thousands) | States, municipalities and political subdivisions | Foreign bonds | Corporate bonds | Asset-backed securities | Equities | Total |
|---|---|---|---|---|---|---|
| Balance at April 1, 2011 | $1,000 | $1,115 | $22,742 | $1,423 | $4,803 | $31,083 |
| Realized gains [(1)] | — | — | — | 12 | — | 12 |
| Unrealized gains [(1)] | — | — | 415 | 1 | — | 416 |
| Amortization | — | — | — | (15) | — | (15) |
| Purchases | — | — | — | 13 | 4 | 17 |
| Disposals | (60) | — | (145) | (1,119) | — | (1,324) |
| Transfers in | — | — | — | — | — | — |
| Transfers out | — | — | (17,156) | — | — | (17,156) |
| Balance at June 30, 2011 | $940 | $1,115 | $5,856 | $315 | $4,807 | $13,033 |

(1) Realized gains are recorded as a component of current operations whereas unrealized gains are recorded as a component of comprehensive income.
The securities reported as "transfers out" relate to securities where an updated market value was available and the securities were transferred from Level 3 to either Level 1 or 2. The reported "disposals" relate to the receipt of principal on calls or sinking fund bonds, in accordance with the indentures.

Table of Contents

The following table provides a summary of the changes in fair value of our Level 3 securities for the six-month period ended June 30, 2011:

| (In Thousands) | States, municipalities and political subdivisions | Foreign bonds | Public utilities | Corporate bonds | Asset-backed securities | Equities | Total |
|---|---|---|---|---|---|---|---|
| Balance at January 1, 2011 | $1,001 | $1,115 | $35 | $23,479 | $— | $1,535 | $27,165 |
| Realized gains [1] | — | — | — | — | 12 | — | 12 |
| Unrealized gains (losses) [1] | — | — | (2) | (50) | 1 | — | (51) |
| Amortization | — | — | — | — | (15) | — | (15) |
| Purchases | — | — | — | — | 1,436 | 3,272 | 4,708 |
| Disposals | (61) | — | (33) | (417) | (1,119) | — | (1,630) |
| Transfers in | — | — | — | — | — | — | — |
| Transfers out | — | — | — | (17,156) | — | — | (17,156) |
| Balance at June 30, 2011 | $940 | $1,115 | $— | $5,856 | $315 | $4,807 | $13,033 |

(1) Realized gains are recorded as a component of current operations whereas unrealized gains (losses) are recorded as a component of comprehensive income.

The equity securities reported as “purchases” relate to our acquisition of Mercer Insurance Group. As a part of the acquisition financing, we purchased securities in the Federal Home Loan Bank of Des Moines, as a requirement to obtain membership and secure the loan. These securities were classified as Level 3 as we had no observable market price at June 30, 2011.

The securities reported as “transfers out” relate to securities where an updated market value was available and the securities were transferred from Level 3 to either Level 1 or 2. The reported “disposals” relate to the receipt of principal on calls or sinking fund bonds, in accordance with the indentures.

Table of Contents

NOTE 4. EMPLOYEE BENEFITS

Pension and Postretirement Periodic Benefit Cost

The components of the net periodic benefit cost for our plans are as follows:

| (In Thousands) | Pension Plan | | Postretirement Benefit Plan | |
|---|---|---|---|---|
| Three Months Ended June 30, | 2011 | 2010 | 2011 | 2010 |
| Net periodic benefit cost | | | | |
| Service cost | $870 | $739 | $614 | $337 |
| Interest cost | 1,237 | 1,231 | 439 | 306 |
| Expected return on plan assets | (1,512) | (1,262) | — | — |
| Amortization of prior service cost | 3 | (14) | (2) | (15) |
| Amortization of net loss | 639 | 488 | 92 | — |
| Net periodic benefit cost | $1,236 | $1,182 | $1,143 | $628 |

| (In Thousands) | Pension Plan | | Postretirement Benefit Plan | |
|---|---|---|---|---|
| Six Months Ended June 30, | 2011 | 2010 | 2011 | 2010 |
| Net periodic benefit cost | | | | |
| Service cost | $1,583 | $1,426 | $993 | $674 |
| Interest cost | 2,380 | 2,285 | 795 | 611 |
| Expected return on plan assets | (2,644) | (2,263) | — | — |
| Amortization of prior service cost | 6 | 5 | (16) | (28) |
| Amortization of net loss | 1,184 | 1,091 | 112 | — |
| Net periodic benefit cost | $2,509 | $2,544 | $1,884 | $1,257 |

Employer Contributions

We previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2010 that we expected to contribute $6.0 million to the pension plan for the 2011 plan year. For the six-month period ended June 30, 2011, we contributed $2.3 million to the pension plan. We anticipate that the total contribution for the 2011 plan year will not vary significantly from our expected contribution.

NOTE 5. STOCK-BASED COMPENSATION

Non-qualified Employee Stock Award Plan

The United Fire & Casualty Company 2008 Stock Plan (the “2008 Stock Plan”) authorizes the issuance of restricted and unrestricted stock awards, stock appreciation rights, incentive stock options, and non-qualified stock options for up to 1,900,000 shares of United Fire common stock to employees, with 671,808 authorized shares available for future issuance at June 30, 2011. The 2008 Stock Plan is administered by the Board of Directors, which determines those employees who will receive awards, when awards will be granted, and the terms and conditions of the awards. The Board of Directors may also take any action it deems necessary and appropriate for the administration of the 2008 Stock Plan. Pursuant to the 2008 Stock Plan, the Board of Directors may, at its sole discretion, grant awards to employees of United Fire or any of its affiliated companies who are in positions of substantial responsibility with United Fire.

Option awards granted pursuant to the 2008 Stock Plan are granted to buy shares of United Fire's common stock at the market value of the stock on the date of grant. All outstanding option awards vest and are exercisable in installments of 20.0 percent of the number of shares covered by the option award each year from the grant date, unless the Board of

Directors authorizes the acceleration of vesting. To the extent not exercised, vested option awards accumulate and are exercisable by the awardee, in whole or in part, in any subsequent year included in the



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Table of Contents

option period, but not later than 10.0 years from the grant date. Restricted and unrestricted stock awards granted pursuant to the 2008 Stock Plan are granted at the market value of our stock on the date of the grant. Restricted stock awards fully vest after 5.0 years from the date of issuance, unless accelerated upon the approval of the Board of Directors, at which time United Fire common stock will be issued to the awardee. All awards are generally granted free of charge to the eligible employees of United Fire as designated by the Board of Directors.
The activity in the 2008 Stock Plan is displayed in the following table:

| Authorized Shares Available for Future Award Grants | Six Months Ended June 30, 2011 | Inception to Date |
|---|---|---|
| Beginning balance | 833,495 | 1,900,000 |
| Number of awards granted | (174,987) | (1,314,217) |
| Number of awards forfeited or expired | 13,300 | 86,025 |
| Ending balance | 671,808 | 671,808 |
| Number of option awards exercised | 6,325 | 173,617 |
| Number of unrestricted stock awards vested | 730 | 2,485 |
| Number of restricted stock awards vested | — | — |

Non-qualified Non-employee Director Stock Option and Restricted Stock Plan
We have a non-employee director stock option and restricted stock plan that authorizes United Fire to grant restricted and unrestricted stock and non-qualified stock options to purchase shares of United Fire’s common stock. At our annual stockholders’ meeting on May 18, 2011, United Fire stockholders approved an amendment to the United Fire & Casualty Company 2005 Non-Qualified Non-Employee Director Stock Option and Restricted Stock Plan to increase from 150,000 to 300,000 the number of shares that may be issued under the Director Plan and to extend the life of the Director Plan from December 31, 2014 to December 31, 2020. At June 30, 2011, we had 160,009 authorized shares available for future issuance.
The Board of Directors has the authority to determine which non-employee directors receive awards, when options and restricted and unrestricted stock shall be granted, the option price, the option expiration date, the date of grant, the vesting schedule of options or whether the options shall be immediately vested, the terms and conditions of options and restricted stock (other than those terms and conditions set forth in the plan) and the number of shares of common stock to be issued pursuant to an option agreement or restricted stock agreement. The Board of Directors may also take any action it deems necessary and appropriate for the administration of the plan.

The activity in our non-employee director stock option and restricted and unrestricted stock plan is displayed in the following table:

| Authorized Shares Available for Future Award Grants | Six Months Ended June 30, 2011 | Inception to Date |
|---|---|---|
| Beginning balance | 37,003 | 150,000 |
| Additional authorization | 150,000 | 150,000 |
| Number of awards granted | (33,000) | (152,000) |
| Number of awards forfeited or expired | 6,006 | 12,009 |
| Ending balance | 160,009 | 160,009 |
| Number of awards exercised | — | — |

Table of Contents

Stock-Based Compensation Expense

For the three-month periods ended June 30, 2011 and 2010, we recognized stock-based compensation expense of $0.5 million and $0.4 million, respectively. For both of the six-month periods ended June 30, 2011 and 2010, we recognized stock-based compensation expense of $0.9 million.

As of June 30, 2011, we had $4.7 million in stock-based compensation expense that has yet to be recognized through our results of operations. We expect this compensation to be recognized over the remainder of 2011 and subsequent years according to the following table, except with respect to awards that are accelerated by the Board of Directors, in which case we will recognize any remaining compensation expense in the period in which the awards are accelerated.

| (In Thousands) | |
|---|---|
| 2011 | $890 |
| 2012 | 1,432 |
| 2013 | 996 |
| 2014 | 765 |
| 2015 | 533 |
| 2016 | 58 |
| Total | $4,674 |

Table of Contents

NOTE 6. SEGMENT INFORMATION

We have two reportable business segments in our operations: property and casualty insurance and life insurance. Mercer Insurance Group is included in the property and casualty insurance segment subsequent to their acquisition on March 28, 2011. The property and casualty insurance segment has six domestic locations from which it conducts its business. All offices target a similar customer base, market the same products and use the same marketing strategies and are therefore aggregated. The life insurance segment operates from our home office. Because all of our insurance is sold domestically, we have no revenues allocable to foreign operations.

We evaluate the two segments on the basis of both statutory accounting practices prescribed by our states of domicile and GAAP. We analyze results based on profitability (i.e., loss ratios), expenses, and return on equity. The basis we use to determine and analyze segments and to measure segment profit or loss have not changed from that reported in our Annual Report on Form 10-K for the year ended December 31, 2010.

The following tables for the three-month periods ended June 30, 2011 and 2010 have been reconciled to the amounts reported in our unaudited Consolidated Financial Statements to adjust for intersegment eliminations.

| (In Thousands) | Property and Casualty Insurance | Life Insurance | Total |
|---|---|---|---|
| Three Months Ended June 30, 2011 | | | |
| Net premiums earned | $139,009 | $13,293 | $152,302 |
| Investment income, net of investment expenses | 9,495 | 18,350 | 27,845 |
| Net realized investment gains | 393 | 731 | 1,124 |
| Other income | 530 | 199 | 729 |
| Total reportable segment | $149,427 | $32,573 | $182,000 |
| Intersegment eliminations | (44) | (152) | (196) |
| Total revenues | $149,383 | $32,421 | $181,804 |
| Net income (loss) | $(19,574) | $1,660 | $(17,914) |
| Assets at June 30, 2011 | $1,902,215 | $1,719,719 | $3,621,934 |
| Invested assets at June 30, 2011 | $1,284,623 | $1,582,787 | $2,867,410 |
| | | | |
| Three Months Ended June 30, 2010 | | | |
| Net premiums earned | $105,396 | $11,766 | $117,162 |
| Investment income, net of investment expenses | 9,049 | 19,288 | 28,337 |
| Net realized investment gains (losses) | (721) | 3,067 | 2,346 |
| Other income | 75 | 220 | 295 |
| Total reportable segment | $113,799 | $34,341 | $148,140 |
| Intersegment eliminations | (46) | (80) | (126) |
| Total revenues | $113,753 | $34,261 | $148,014 |
| Net income | $9,961 | $3,970 | $13,931 |
| Assets at June 30, 2010 | $1,344,024 | $1,712,555 | $3,056,579 |
| Invested assets at June 30, 2010 | $956,108 | $1,501,701 | $2,457,809 |

Table of Contents

The following tables for the six-month periods ended June 30, 2011 and 2010, have been reconciled to the amounts reported in our unaudited Consolidated Financial Statements to adjust for intersegment eliminations.

| (In Thousands) | Property and Casualty Insurance | Life Insurance | Total |
|---|---|---|---|
| Six Months Ended June 30, 2011 | | | |
| Net premiums earned | $240,773 | $25,825 | $266,598 |
| Investment income, net of investment expenses | 18,276 | 36,679 | 54,955 |
| Net realized investment gains | 1,601 | 2,176 | 3,777 |
| Other income | 538 | 347 | 885 |
| Total reportable segment | $261,188 | $65,027 | $326,215 |
| Intersegment eliminations | (88) | (247) | (335) |
| Total revenues | $261,100 | $64,780 | $325,880 |
| Net income (loss) | $(16,224) | $4,120 | $(12,104) |
| Assets at June 30, 2011 | $1,902,215 | $1,719,719 | $3,621,934 |
| Invested assets at June 30, 2011 | $1,284,623 | $1,582,787 | $2,867,410 |
| Six Months Ended June 30, 2010 | | | |
| Net premiums earned | $207,375 | $24,174 | $231,549 |
| Investment income, net of investment expenses | 17,731 | 38,619 | 56,350 |
| Net realized investment gains | 1,455 | 3,617 | 5,072 |
| Other income | 17 | 401 | 418 |
| Total reportable segment | $226,578 | $66,811 | $293,389 |
| Intersegment eliminations | (91) | (159) | (250) |
| Total revenues | $226,487 | $66,652 | $293,139 |
| Net income | $25,758 | $7,286 | $33,044 |
| Assets at June 30, 2010 | $1,344,024 | $1,712,555 | $3,056,579 |
| Invested assets at June 30, 2010 | $956,108 | $1,501,701 | $2,457,809 |

Table of Contents

NOTE 7. EARNINGS PER COMMON SHARE

Basic earnings (loss) per share is computed by dividing net income (loss) by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings (loss) per share gives effect to all dilutive common shares outstanding during the reporting period. The dilutive shares we consider in our diluted earnings (loss) per share calculation relate to our outstanding stock options and restricted stock awards.

We determine the dilutive effect of our outstanding stock options using the “treasury stock” method. Under this method, we assume the exercise of all of the outstanding stock options whose exercise price is less than the weighted-average fair market value of our common stock during the reporting period. This method also assumes that the proceeds from the hypothetical stock option exercises are used to repurchase shares of our common stock at the weighted-average fair market value of the stock during the reporting period. The net of the assumed stock options exercised and assumed common shares repurchased represents the number of dilutive common shares, which we add to the denominator of the earnings per share calculation.

The components of basic and diluted earnings (loss) per share were as follows for the three-month periods ended June 30, 2011 and 2010:

| | Three Months Ended June 30, | | | |
|---|---|---|---|---|
| (In Thousands Except Per Share Data) | 2011 | | 2010 | |
| | Basic | Diluted | Basic | Diluted |
| Net income (loss) | $(17,914) | $(17,914) | $13,931 | $13,931 |
| Weighted-average common shares outstanding | 26,102 | 26,102 | 26,356 | 26,356 |
| Add dilutive effect of restricted stock awards | — | — | — | 19 |
| Add dilutive effect of stock options | — | — | — | 25 |
| Weighted-average common shares for EPS calculation | 26,102 | 26,102 | 26,356 | 26,400 |
| Earnings (loss) per common share | $(0.69) | $(0.69) | $0.53 | $0.53 |
| Awards excluded from diluted EPS calculation[1] | — | 1,206 | — | 814 |

(1) Outstanding awards were excluded from the diluted earnings (loss) per share calculation because the effect of including them would have been anti-dilutive.

The components of basic and diluted earnings (loss) per share were as follows for the six-month periods ended June 30, 2011 and 2010:

| | Six Months Ended June 30, | | | |
|---|---|---|---|---|
| (In Thousands Except Per Share Data) | 2011 | | 2010 | |
| | Basic | Diluted | Basic | Diluted |
| Net income (loss) | $(12,104) | $(12,104) | $33,044 | $33,044 |
| Weighted-average common shares outstanding | 26,148 | 26,148 | 26,396 | 26,396 |
| Add dilutive effect of restricted stock awards | — | — | — | 19 |
| Add dilutive effect of stock options | — | — | — | — |
| Weighted-average common shares for EPS calculation | 26,148 | 26,148 | 26,396 | 26,415 |
| Earnings (loss) per common share | $(0.46) | $(0.46) | $1.25 | $1.25 |
| Awards excluded from diluted EPS calculation[1] | — | 1,206 | — | 814 |

(1) Outstanding awards were excluded from the diluted earnings (loss) per share calculation because the effect of including them would have been anti-dilutive.

Table of Contents

NOTE 8. COMPREHENSIVE INCOME

Comprehensive income includes all changes in stockholders’ equity during the reporting period except those resulting from investments by stockholders and dividends to stockholders.

The following table sets forth the components of our comprehensive income (loss) and the related tax effects for the three-month periods ended June 30, 2011 and 2010:

| | Three Months Ended June 30, | |
|---|---|---|
| (In Thousands) | 2011 | 2010 |
| Net income (loss) | $(17,914) | $13,931 |
| Other comprehensive income (loss) | | |
| Change in net unrealized appreciation on investments | 21,439 | (3,455) |
| Adjustment for net realized gains included in income | (1,124) | (2,346) |
| Adjustment for costs included in employee benefit expense | 732 | 453 |
| Other comprehensive income (loss), before tax | 21,047 | (5,348) |
| Income tax effect | (7,366) | 1,858 |
| Other comprehensive income (loss), after tax | 13,681 | (3,490) |
| Comprehensive income (loss) | $(4,233) | $10,441 |

The following table sets forth the components of our comprehensive income (loss) and the related tax effects for the six-month periods ended June 30, 2011 and 2010:

| | Six Months Ended June 30, | |
|---|---|---|
| (In Thousands) | 2011 | 2010 |
| Net income (loss) | $(12,104) | $33,044 |
| Other comprehensive income | | |
| Change in net unrealized appreciation on investments | 22,939 | 18,022 |
| Adjustment for net realized gains included in income | (3,777) | (5,072) |
| Adjustment for costs included in employee benefit expense | 1,286 | 1,068 |
| Other comprehensive income, before tax | 20,448 | 14,018 |
| Income tax effect | (7,157) | (4,907) |
| Other comprehensive income, after tax | 13,291 | 9,111 |
| Comprehensive income | $1,187 | $42,155 |

Table of Contents

NOTE 9. CONTINGENT LIABILITIES

Legal Proceedings

We are named as a defendant in various lawsuits relating to disputes arising from damages that occurred as a result of Hurricane Katrina in 2005. These lawsuits include actions seeking certification from the court to proceed as a class action suit and actions filed by individual policyholders. These cases involve, among other claims: disputes as to the amount of reimbursable claims in particular cases; the scope of insurance coverage under homeowners and commercial property policies due to flooding, civil authority actions, loss of use and business interruption; breach of the duty of good faith or violations of Louisiana insurance claims-handling laws or regulations (which cases involve claims for statutory damages and, in some cases, punitive or exemplary damages); the applicability of Louisiana's so-called "Valued Policy Law," pursuant to which insurers must pay the total insured value of a structure that is totally destroyed if any portion of such damage was caused by a covered peril, even if the principal cause of the loss was an excluded peril; and the scope or enforceability of the water damage exclusion in the policies. We have established our loss and loss settlement expense reserves on the assumption that the application of the Valued Policy Law will not result in our having to pay damages for perils not otherwise covered. We believe that, in the aggregate, these reserves are adequate.

We intend to continue to defend the cases related to losses incurred as a consequence of Hurricane Katrina. There are approximately 69 individual policyholder cases pending and three class action cases pending as of June 30, 2011. Our evaluation of these claims and the adequacy of recorded reserves may change if we encounter adverse developments in the further defense of these claims. In the six-month periods ended June 30, 2011 and 2010, we incurred $5.8 million and $5.4 million of loss and loss settlement expenses from Hurricane Katrina claims and related litigation.

We are a defendant in two lawsuits filed in the Superior Court of Mercer County, New Jersey, Chancery Division, relating to our merger with Mercer Insurance Group. We have negotiated a settlement of both suits that is subject to court approval. The obligation of United Fire and Mercer Insurance Group pursuant to settlement is not material. If the court does not approve the settlement, we believe that the exposure faced by United Fire and Mercer Insurance Group is not material.

We consider all of our other litigation pending as of June 30, 2011, to be ordinary, routine, and incidental to our business.

NOTE 10. BUSINESS COMBINATIONS

On March 28, 2011, we purchased 100.0 percent of the outstanding voting stock of Mercer Insurance Group, which was funded through a combination of cash and short-term debt. The excess of the purchase price over the estimated fair value of the tangible assets acquired and liabilities assumed at the acquisition date has been allocated to goodwill and intangible assets of the property and casualty insurance segment.

We are in the process of completing valuation procedures of the separately identifiable intangible assets acquired and assessing the related useful lives of those assets. The purchase price allocations below have been established on a preliminary basis and may be subject to adjustment within one year from the acquisition date. We expect to continue to obtain further information during the measurement period to assist us in determining the fair value of certain of the assets acquired and liabilities assumed. Any adjustment to the fair values that have been preliminarily established will be recognized in the period that the adjustment is identified.

Table of Contents

The following is a summary of the estimated fair value of the assets acquired and liabilities assumed of Mercer Insurance Group at the date of acquisition based on preliminary purchase price allocations:

| (In Thousands) | March 28, 2011 |
|---|---|
| Assets | |
| Available-for-sale fixed maturity securities | $401,548 |
| Equity securities | 10,666 |
| Cash and cash equivalents | 18,855 |
| Accrued investment income | 3,741 |
| Premiums receivable | 35,822 |
| Value of business acquired | 27,436 |
| Property and equipment | 15,228 |
| Reinsurance receivables and recoverables | 58,193 |
| Prepaid reinsurance premiums | 6,289 |
| Income taxes receivable | 2,732 |
| Deferred income taxes | 3,543 |
| Goodwill and intangible assets | 31,500 |
| Other assets | 11,333 |
| Total assets | $626,886 |
| Liabilities | |
| Reserves for losses, claims and loss settlement expenses | $310,647 |
| Unearned premiums | 72,249 |
| Accrued expenses and other liabilities | 33,902 |
| Debt | 3,000 |
| Trust preferred securities | 15,614 |
| Total liabilities | $435,412 |
| Total net assets acquired | $191,474 |

The fair value of available-for-sale fixed maturity securities is primarily based on quoted prices for similar financial instruments in markets that are not active or on inputs that are observable either directly or indirectly for the full term of the financial instrument. The fair value of equity securities is primarily based on unadjusted quoted prices in active markets for identical financial instruments that we have the ability to access.

The fair value of reserves for losses, claims and loss settlement expenses related to incurred claims and reinsurance receivables and recoverables is determined using a valuation model that is based on actuarial estimates of future cash flows for the underwriting liabilities. These future cash flows are adjusted for the time value of money using duration-matched risk-free interest rates, which approximate current U.S. Treasury bill rates, and a risk margin to compensate the acquirer for the risk associated with these liabilities.

The value of business acquired (“VOBA”) at the acquisition date is an intangible asset relating to the difference between the unearned premium reserves acquired in the transaction and the estimated fair value of the unexpired insurance policies, which consists of two components: (1) a provision for loss and loss settlement expenses that will be incurred as the premium is earned and (2) a provision for policy maintenance costs related to servicing those policies until they expire. Loss and loss settlement expenses are valued in a manner identical to that used for loss reserve valuation. Policy maintenance costs are valued based on estimates of future cash flows that are discounted to present value using duration-matched risk-free interest rates. VOBA is reported as a component of deferred policy acquisition costs in the accompanying unaudited Consolidated Balance Sheets and will be substantially amortized over a twelve-month period from the acquisition date in proportion to the timing of the estimated underwriting profit associated with the in-force business. The amortization pattern for the VOBA asset will be greater in the initial months subsequent to the acquisition date in correlation to the large number of six-month policies that were underwritten by Mercer Insurance Group.

Table of Contents

The fair value of property and equipment related to land and buildings approximates the appraised value of the respective assets at the acquisition date.
The fair value of all other tangible assets and liabilities approximate their carrying values at the acquisition date due to their short-term duration.
The following is a summary of our unaudited pro forma historical results, as if Mercer Insurance Group had been acquired on January 1, 2010:

| (In Thousands) | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2011 | 2010 | 2011 | 2010 |
| Revenue | $181,804 | $186,030 | $362,705 | $370,324 |
| Net income (loss) [(1)] | (17,914) | 17,711 | (23,001) | 40,296 |
| Basic earnings (loss) per share | (0.69) | 0.67 | (0.88) | 1.53 |
| Diluted earnings (loss) per share | (0.69) | 0.67 | (0.88) | 1.53 |

(1) The three- and six-month periods ended June 30, 2011, include transaction related expenses incurred that reduced net income by $0.1 million and $11.5 million, respectively.
The unaudited pro forma results above have been prepared for comparative purposes only and do not purport to be indicative of the results of operations that actually would have resulted had the acquisition occurred at January 1, 2010, and they are not necessarily indicative of future operating results. Annualized revenues of Mercer Insurance Group approximates $146.0 million for 2011. For both the three- and six-month periods ended June 30, 2011, total revenues and net loss recorded in our unaudited Consolidated Financial Statements related to Mercer Insurance Group was $36.2 million and $7.0 million, respectively.

NOTE 11. DEBT

We have the following debt outstanding at June 30, 2011:
(In Thousands)

| | Repayment of Funds are Due on or Before | Amount Due |
|---|---|---|
| Federal Home Loan Bank of Des Moines | September 26, 2011 | $29,900 |
| Bankers Trust Company | March 23, 2012 [(1)] | 50,000 |
| Union Bank of California | November 16, 2011 | 3,000 |
| Total | | $82,900 |

(1) The borrowing under the line of credit is due on March 23, 2012; however, we have agreed to prepay to the lender the outstanding amount of any loan or loans, plus interest, on or before the nine-month anniversary of the loan issuance date, which was March 24, 2011.
The proceeds of our loans with Federal Home Loan Bank of Des Moines and Bankers Trust Company were used to finance our acquisition of Mercer Insurance Group.
In the first quarter of 2011, United Life Insurance Company borrowed $29.9 million from the Federal Home Loan Bank of Des Moines. Under the terms of the loan, the effective interest rate is 0.37 percent and is calculated on a ratio of a 360 day year and the actual days of the month the principal is outstanding. The loan agreement contains customary terms and conditions. Interest payments are due at maturity on this line. We deposited $35.2 million in collateral with the Federal Home Loan Bank of Des Moines to secure that loan.
In the first quarter of 2011, we entered into a $50.0 million line of credit with Bankers Trust Company. For the six-month period ended June 30, 2011, we utilized our entire line of credit to assist in the funding of our acquisition of Mercer Insurance Group. Under the terms of our credit agreement, interest on outstanding balances is adjusted monthly to the monthly London Interbank Offered Rate ("LIBOR"), as published in the Wall Street Journal, plus 180 basis points, calculated using a 360 day year and the actual days of the month the principal is outstanding. In addition, the line of credit incurs an annual facility charge of $25,000. Interest payments are due monthly on this line. The line of credit contains certain financial covenants including covenants that require us to maintain our A.M. Best rating, a debt to capitalization ratio and minimum stockholders equity.

Table of Contents

In addition, Mercer Insurance Group has the ability to borrow up to $7.5 million on a bank line of credit with Union Bank of California. Under the terms of that credit agreement, the line of credit bears interest at the bank's base rate or an optional rate based on LIBOR. The effective annual interest rate as of June 30, 2011, was 3.25 percent. In addition, the line of credit incurs an annual facility charge of $10,000. Interest payments are due monthly on this line. The line of credit contains certain financial covenants, including covenants that require Mercer Insurance Group to maintain a minimum statutory surplus and to distribute from subsidiaries no more than 50.0 percent of allowable dividends.
We were in compliance with all covenants for all credit agreements as of June 30, 2011.

NOTE 12. TRUST PREFERRED SECURITIES

In connection with our acquisition of Mercer Insurance Group, we acquired the following Trust Preferred Securities, which were outstanding as of June 30, 2011:

| (In Thousands) | Issue Date | Amount | Interest Rate | Maturity Date |
|---|---|---|---|---|
| Financial Pacific Statutory Trust I | 12/4/2002 | $5,029 | LIBOR + 4.00% | 12/4/2032 |
| Financial Pacific Statutory Trust II | 5/15/2003 | 3,016 | LIBOR + 4.10% | 5/15/2033 |
| Financial Pacific Statutory Trust III | 9/30/2003 | 7,573 | LIBOR + 4.05% | 9/30/2033 |
| Total Trust Preferred Securities | | $15,618 | | |

The Trust Preferred Securities were issued by three statutory business trusts formed by Mercer Insurance Group to issue Floating Rate Capital Securities ("Trust Preferred Securities") and to invest the proceeds in Junior Subordinated Debentures of Mercer Insurance Group. Mercer Insurance Group holds $.5 million of equity securities to capitalize the Trusts. The three trusts issued a total of $15.5 million Trust Preferred Securities to the public.
Financial Pacific Statutory Trust I ("Trust I") is a Connecticut statutory business trust. The Trust issued 5.0 million shares of the Trust Preferred Securities at a price of $1 per share for $5.0 million. The Trust purchased $5.2 million in Junior Subordinated Debentures from Mercer Insurance Group that mature on December 4, 2032. The annual effective rate of interest at June 30, 2011 is 8.74 percent.
Financial Pacific Statutory Trust II ("Trust II") is a Connecticut statutory business trust. The Trust issued 3.0 million shares of the Trust Preferred Securities at a price of $1 per share for $3.0 million. The Trust purchased $3.1 million in Junior Subordinated Debentures from Mercer Insurance Group that mature on May 15, 2033. The annual effective rate of interest at June 30, 2011 is 8.9 percent.
Financial Pacific Statutory Trust III ("Trust III") is a Delaware statutory business trust. The Trust issued 7.5 million shares of the Trust Preferred Securities at a price of $1 per share for $7.5 million. The Trust purchased $7.7 million in Junior Subordinated Debentures from Mercer Insurance Group that mature on September 30, 2033. The annual effective rate of interest at June 30, 2011 is 8.89 percent.
Mercer Insurance Group has the right, at any time, so long as there are no continuing events of default, to defer payments of interest on the Junior Subordinated Debentures for a period not exceeding 20.0 consecutive quarters; but not beyond the stated maturity of the Junior Subordinated Debentures. To date no interest has been deferred. Mercer Insurance Group entered into three interest rate swap agreements to economically hedge the floating interest rate on the Junior Subordinated Debentures (see Note 13, "Derivative Instruments and Hedging Activities").
The Trust Preferred Securities are subject to mandatory redemption, in whole or in part, upon repayment of the Junior Subordinated Debentures at maturity or their earlier redemption. Mercer Insurance Group has the right to redeem the Junior Subordinated Debentures after December 4, 2007 for Trust I, after May 15, 2008 for Trust II and after September 30, 2008 for Trust III. Mercer Insurance Group has not exercised these rights as of June 30, 2011.

Table of Contents

NOTE 13. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

In connection with our acquisition of Mercer Insurance Group, we acquired three interest-rate swap agreements that hedge against interest rate risk on the Trust Preferred Securities. The interest rate swaps are contracts to convert, for a period of time, the floating rate of the trust preferred securities described in Note 12, "Trust Preferred Securities" into a fixed rate without exchanging the instruments themselves. As of June 30, 2011, the interest-rate swap agreements had an aggregate notional principal amount of $15.5 million.

The interest rate swaps are designated as non-hedge instruments. Accordingly, the fair value of the interest rate swaps is recognized as an asset or liability, with changes in fair value recognized in earnings. The estimated fair value of the interest rate swaps is based on the valuation received from the financial institution counterparty (“counterparty”).

By using financial instruments to manage exposure to changes in interest rates, we are exposed to market and credit risk. In this instance, market risk is the potential for loss due to a decrease in the fair value of securities resulting from uncontrollable fluctuations in interest rates. Credit risk is the potential failure of the counterparty to perform under the terms of the contract. If the fair value of a contract is positive, the counterparty would owe, therefore exposing us to credit risk. The inherent credit risk has been minimized by entering into transactions with high-quality counterparties, whose credit rating is higher than Aa, as rated by Moody's.

A summary of the fair value of interest rate swaps outstanding as of June 30, 2011, is as follows:

| (In Thousands) | Balance Sheet Location | Fair Value Liability |
|---|---|---|
| Interest rate swaps | | |
| Union Bank of California (Trust I) | Accrued expenses and other liabilities | $323 |
| Union Bank of California (Trust II) | Accrued expenses and other liabilities | 254 |
| Union Bank of California (Trust III) | Accrued expenses and other liabilities | 691 |
| Total derivatives | | $1,268 |

Table of Contents

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders of
United Fire & Casualty Company

We have reviewed the consolidated balance sheet of United Fire & Casualty Company as of June 30, 2011, and the related consolidated statements of income for the three-month and six-month periods ended June 30, 2011 and 2010, the consolidated statements of cash flows for the six-month periods ended June 30, 2011 and 2010, and the consolidated statement of stockholders' equity for the six-month period ended June 30, 2011. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of United Fire & Casualty Company as of December 31, 2010, and the related consolidated statements of income, stockholders' equity, and cash flows for the year then ended, not presented herein, and in our report dated February 28, 2011, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2010, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Ernst & Young LLP
Ernst & Young LLP

Chicago, Illinois
August 5, 2011

Table of Contents

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

FORWARD-LOOKING STATEMENTS

This report may contain forward-looking statements about our operations, anticipated performance and other similar matters. The Private Securities Litigation Reform Act of 1995 provides a safe harbor under the Securities Act of 1933 and the Securities Exchange Act of 1934 for forward-looking statements. The forward-looking statements are not historical facts and involve risks and uncertainties that could cause actual results to differ materially from those expected and/or projected. Such forward-looking statements are based on current expectations, estimates, forecasts and projections about our company, the industry in which we operate, and beliefs and assumptions made by management. Words such as "expect(s)," "anticipate(s)," "intend(s)," "plan(s)," "believe(s)," "continue(s)," "seek(s)," "estimate(s)," "goal(s)," "target(s)," "forecast(s)," "project(s)," "predict(s)," "should," "could," "may," "will continu "hope," "can" and other words and terms of similar meaning or expression in connection with a discussion of future operations, financial performance or financial condition, are intended to identify forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed in such forward-looking statements. Information concerning factors that could cause actual results to differ materially from those in the forward-looking statements is contained in Part II Item 1A, "Risk Factors" of this document. Among the factors that could cause our actual outcomes and results to differ are:

- The adequacy of our loss and loss settlement expense reserves established for Hurricane Katrina, which are based on management's estimates.
- The frequency and severity of claims, including those related to catastrophe losses, and the impact those claims have on our loss reserve adequacy.
- Developments in the domestic and global financial markets that could affect our investment portfolio and financing plans.
- The calculation and recovery of deferred policy acquisition costs ("DAC").
- The valuation of pension and other postretirement benefit obligations.
- Our relationship with our agents.
- Our relationship with our reinsurers.
- The financial strength rating of our reinsurers.
- Changes in industry trends and significant industry developments.
- The resolution of regulatory issues and litigation pertaining to and arising out of Hurricane Katrina.
- Governmental actions, policies and regulations, including, but not limited to, domestic health care reform, financial services regulatory reform, corporate governance, new laws or regulations or court decisions interpreting existing laws and regulations or policy provisions.
- NASDAQ policies or regulations relating to corporate governance and the cost to comply.

These are representative of the risks, uncertainties, and assumptions that could cause actual outcomes and results to differ materially from what is expressed in forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date of this report or as of the date they are made. Except as required under the federal securities laws and the rules and regulations of the Securities and

Table of Contents

Exchange Commission, we do not have any intention or obligation to update publicly any forward-looking statements, whether as a result of new information, future events, or otherwise.

## CRITICAL ACCOUNTING ESTIMATES

Critical accounting estimates are defined as those that are representative of significant judgments and uncertainties and that potentially may result in materially different results under different assumptions and conditions. We base our discussion and analysis of our results of operations and financial condition on the amounts reported in our Consolidated Financial Statements, which we have prepared in accordance with GAAP. As we prepare these Consolidated Financial Statements, we must make estimates and assumptions that affect the reported amounts of assets and liabilities; the disclosure of contingent assets and liabilities at the date of the financial statements; and the reported amounts of revenues and expenses for the reporting period. We evaluate our estimates on an ongoing basis. We base our estimates on historical experience and on other assumptions that we believe to be reasonable under the circumstances. Actual results could differ from those estimates. Our critical accounting estimates are: the valuation of investments; the valuation of reserves for losses, claims, and loss settlement expenses; the valuation of reserves for future policy benefits; and the calculation of the deferred policy acquisition costs asset. These critical accounting estimates are more fully described in our Management's Discussion and Analysis of Results of Operations and Financial Condition presented in our Annual Report on Form 10-K for the year ended December 31, 2010.

## INTRODUCTION

The purpose of the Management's Discussion and Analysis is to provide an understanding of our results of operations and consolidated financial position. Our Management's Discussion and Analysis should be read in conjunction with the consolidated financial statements and related notes, including those in our Annual Report on Form 10-K for the year ended December 31, 2010. When we provide information on a statutory basis, we label it as such, otherwise, all other data is presented in accordance with GAAP.

This discussion and analysis is presented in these sections:

- Our Business
- Consolidated Financial Highlights
- Results of Operations for Property and Casualty Insurance, Life Insurance and Investment Portfolio
- Liquidity and Capital Resources
- Statutory Financial Measures

## OUR BUSINESS

Founded in 1946, United Fire & Casualty Company provides insurance protection for individuals and businesses through several regional companies. We are licensed as a property and casualty insurer in 43 states plus the District of Columbia and are represented by more than 1,200 independent agencies. Our life insurance subsidiary is licensed in 29 states and is represented by more than 900 independent agencies.

We operate two business segments, each with a wide range of products:

- property and casualty insurance, which includes commercial insurance, personal insurance, surety bonds and assumed insurance; and

- life insurance, which includes deferred and immediate annuities, universal life products and traditional life (primarily single premium whole life insurance) products.

Table of Contents

We manage these business segments separately, as they generally do not share the same customer base, and each has different products, pricing, and expense structures.

For the six months ended June 30, 2011, property and casualty business accounted for 90.4 percent of our net premiums earned, of which 89.6 percent was generated from commercial lines. Life insurance business made up 9.6 percent of our net premiums earned, of which 61.3 percent was generated from traditional life insurance products.

For the six months ended June 30, 2011, more than half of our property and casualty direct premiums were written in Iowa, Texas, Missouri, California, Louisiana, and Illinois, and over three-fourths of our life insurance premiums, excluding annuities, were written in Iowa, Wisconsin, Illinois, Nebraska and Minnesota.

We evaluate segment profit or loss based upon operating and investment results. Segment profit or loss described in the following sections of the Management's Discussion and Analysis is reported on a pre-tax basis. Additional segment information is presented in Part I, Item 1, Note 6 “Segment Information” to the unaudited Consolidated Financial Statements.

Our primary sources of revenue are premiums and investment income. Major categories of expenses include losses and loss settlement expenses, changes in reserves for future policy benefits, operating expenses and interest on policyholders’ accounts.

The profitability of our company is influenced by many factors, including price, competition, economic conditions, interest rates, catastrophic events and other natural disasters, man-made disasters, state regulations, court decisions, and changes in the law. Management believes that climate change considerations will not have a material impact on our profitability, unless a connection between future increased extreme weather events and climate change is ultimately proven true.

To manage these risks and uncertainties, we seek to achieve consistent profitability through strong agency relationships, exceptional customer service, fair and prompt claims handling, disciplined underwriting, superior loss control services, and effective and efficient use of technology.

Table of Contents

CONSOLIDATED FINANCIAL HIGHLIGHTS

| | Three Months Ended June 30, | | | Six Months Ended June 30, | | |
|---|---|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | % | 2011 | 2010 | % |
| Revenues | | | | | | |
| Net premiums earned | $152,210 | $117,082 | 30.0 % | $266,414 | $231,390 | 15.1 % |
| Investment income, net of investment expenses | 27,741 | 28,291 | (1.9 ) | 54,804 | 56,259 | (2.6 ) |
| Net realized investment gains | | | | | | |
| Other-than-temporary impairment charges | — | (117 ) | — | — | (459 ) | — |
| All other net realized gains | 1,124 | 2,463 | (54.4 ) | 3,777 | 5,531 | (31.7 ) |
| Total net realized investment gains | 1,124 | 2,346 | (52.1 ) | 3,777 | 5,072 | (25.5 ) |
| Other income | 729 | 295 | 147.1 | 885 | 418 | 111.7 |
| | $181,804 | $148,014 | 22.8 % | $325,880 | $293,139 | 11.2 % |
| Benefits, Losses and Expenses | | | | | | |
| Losses and loss settlement expenses | $135,811 | $72,757 | 86.7 | $211,993 | $141,120 | 50.2 |
| Future policy benefits | 7,880 | 7,375 | 6.8 | 16,062 | 13,765 | 16.7 |
| Amortization of deferred policy acquisition costs | 43,732 | 27,922 | 56.6 | 69,778 | 54,438 | 28.2 |
| Other underwriting expenses | 14,720 | 10,973 | 34.1 | 30,777 | 20,186 | 52.5 |
| Interest on policyholders' accounts | 10,657 | 10,647 | 0.1 | 21,327 | 21,448 | (0.6 ) |
| | $212,800 | $129,674 | 64.1 % | $349,937 | $250,957 | 39.4 % |
| Income (loss) before income taxes | $(30,996 ) | $18,340 | NM | $(24,057 ) | $42,182 | (157.0 )% |
| Federal income tax expense (benefit) | (13,082 ) | 4,409 | NM | (11,953 ) | 9,138 | NM |
| Net Income (Loss) | $(17,914 ) | $13,931 | NM | $(12,104 ) | $33,044 | (136.6 )% |

NM = not meaningful

The following is a summary of our financial performance for the three- and six-month periods ended June 30, 2011:

Consolidated Results of Operations

- For the three-month period ended June 30, 2011, we incurred a net loss of $17.9 million, compared to net income of $13.9 million for the same period of 2010. The deterioration is primarily due to the following:

Loss and loss settlement expenses increased due to our direct catastrophe loss experience, primarily from the storms that occurred in April in the southern states and in May in Joplin, Missouri. Also contributing were a few large losses that impacted our workers' compensation, other liability and fire and allied lines of business.

Policy acquisition costs, transaction costs and the value of business acquired ("VOBA") asset related to our acquisition of Mercer Insurance Group led to a significant increase in both amortization of deferred policy acquisition costs and other underwriting expenses. We expect deferred policy acquisition costs related to Mercer Insurance Group to be higher than normal the remainder of 2011 and into the first quarter of 2012, as we amortize these costs in the first year from the date of acquisition.

For the six-month period ended June 30, 2011, we incurred a net loss of $12.1 million, compared to net income of $33.0 million for the same period of 2010. The deterioration is primarily due to the following:

- Loss and loss settlement expenses increased due to our direct catastrophe loss experience and our assumed reinsurance losses related to the New Zealand earthquake and the earthquake and tsunami

Table of Contents

in Japan in the first quarter of 2011. Also contributing were large losses in our workers' compensation, commercial auto, other liability and fire and allied lines of business.

Policy acquisition costs, transaction costs and the VOBA asset related to our acquisition of Mercer Insurance Group led to a significant increase in both amortization of deferred policy acquisition costs and other underwriting expenses.

- Net premiums written for the property and casualty insurance segment increased 35.8 percent and 20.3 percent in the three- and six-month periods ended June 30, 2011, compared to the same periods of 2010, reflecting our acquisition of Mercer Insurance Group, a combination of small rate increases, primarily in personal lines, and our internal initiatives to improve growth in several market segments and to increase penetration with existing agencies.

- Deferred annuity deposits (sales) increased 24.3 percent and 4.5 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010. This increase is directly attributable to the activity of a new agency. However, we do not project increased deferred annuity sales as a trend. In fact, deferred annuity sales have continued to decline overall, as interest rates remain at historic lows and as some consumers with a greater tolerance for risk are choosing to surrender their annuities and place the funds in products with greater risk and potentially greater return. Deferred annuity deposits are not recorded as a component of net premiums written or net premiums earned. However, they do generate investment income.

- Pre-tax catastrophe losses totaled $34.9 million and $47.3 million for the three- and six-month periods ended June 30, 2011, respectively, compared to $7.6 million and $10.7 million in the same periods of 2010, due primarily to the storms that occurred in April and May. Also contributing to our year-to-date losses were assumed reinsurance losses related to the New Zealand earthquake and the earthquake and tsunami in Japan that occurred in the first quarter of 2011.

- Our combined ratio was affected by our direct catastrophe losses, assumed reinsurance losses, amortization of deferred policy acquisition costs and expenses related to our acquisition of Mercer Insurance Group. The ratio increased 35.4 percentage points and 26.7 percentage points in the three- and six-month periods ended June 30, 2011, compared to the same periods of 2010.

Consolidated Financial Condition

- Net cash inflow related to our annuity business was $3.6 million in the three-month period ended June 30, 2011, compared to $0.5 million net cash outflow in the same period of 2010, as a result of one-time activity of a new agency as described previously. For the six-month periods ended June 30, 2011 and 2010, net cash outflow was $2.6 million and $1.6 million, respectively.

- As of June 30, 2011, the book value per share of our common stock was $27.23. In the three- and six-month periods ended June 30, 2011, United Fire repurchased 323,597 shares of our common stock for $6.1 million, at an average cost of $18.80 per share. Under our Share Repurchase Program, which expires in August 2013, we are authorized to purchase an additional 849,229 shares of common stock.

- Net unrealized investment gains totaled $115.1 million as of June 30, 2011, an increase of $12.5 million or 12.1 percent since December 31, 2010. The increase in unrealized gains was driven by an increase in the value of both our fixed maturity and equity portfolios.

- Our stockholders' equity decreased to $704.8 million at June 30, 2011, from $716.4 million at December 31, 2010, primarily as a result of our year-to-date net loss.

Table of Contents

RESULTS OF OPERATIONS

Property and Casualty Insurance Segment Results

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| Net premiums written [1] | $159,027 | $117,099 | $269,753 | $224,223 |
| Net premiums earned | $139,009 | $105,396 | $240,773 | $207,375 |
| Losses and loss settlement expenses | (130,124) | (68,253) | (201,789) | (131,881) |
| Amortization of deferred policy acquisition costs | (41,086) | (25,347) | (65,116) | (49,390) |
| Other underwriting expenses | (11,800) | (7,960) | (24,526) | (14,320) |
| Underwriting gain (loss) [1] | $(44,001) | $3,836 | $(50,658) | $11,784 |
| | | | | |
| Investment income, net of investment expenses | 9,451 | 9,003 | 18,188 | 17,640 |
| Net realized investment gains (losses) | | | | |
| Other-than-temporary impairment charges | — | (117) | — | (153) |
| All other net realized gains (losses) | 393 | (604) | 1,601 | 1,608 |
| Total net realized investment gains (losses) | 393 | (721) | 1,601 | 1,455 |
| Other income | 530 | 75 | 538 | 17 |
| Income (loss) before income taxes | $(33,627) | $12,193 | $(30,331) | $30,896 |
| | | | | |
| GAAP Ratios: | | | | |
| Net loss ratio | 68.5 % | 57.6 % | 64.1 % | 58.4 % |
| Catastrophes - effect on net loss ratio | 25.1 | 7.2 | 19.7 | 5.2 |
| Net loss ratio | 93.6 % | 64.8 % | 83.8 % | 63.6 % |
| Expense ratio [2] | 38.1 | 31.5 | 37.2 | 30.7 |
| Combined ratio | 131.7 % | 96.3 % | 121.0 % | 94.3 % |

(1) The Statutory Financial Measures section of this report defines data prepared in accordance with statutory accounting practices which, is a comprehensive basis of accounting other than U.S. GAAP.
(2) Includes policyholder dividends.

- Net premiums written increased 35.8 percent in the three-month period ended June 30, 2011, which is attributable to:

Acquisition of Mercer Insurance Group - Total net premiums written increased by 31.6 percent for the quarter as a result of our acquisition of Mercer Insurance Group, which was effective March 28, 2011. The acquisition of Mercer Insurance Group resulted in increases of $32.1 million and $4.9 million, respectively, in our commercial and personal lines net premiums written for the quarter.

Organic growth - The additional increase in our net premiums written is the result of a combination of small rate increases, primarily in personal lines, and our internal initiatives to improve growth in several market segments, and to increase penetration with existing agencies.

- Commercial lines - Competitive market conditions persisted during the quarter, with large accounts still very difficult to write and retain. However, we have seen improvement in our commercial lines renewal pricing on small accounts.

Our pricing on new business remains unchanged, and new business premium written has increased compared to the second quarter of 2010. While the sluggish economy is still creating financial concerns for many of our policyholders, reductions in premium audit returns and out-of-business policy cancellations have moderated in some regions of the country.

Table of Contents

- Personal lines - We continue to see positive growth in our personal lines written premium, along with a second consecutive year of rate increases.

- Policy retention rates remained strong for both commercial and personal lines, with approximately 81.0 percent of our policies renewing.

- GAAP combined ratio increased by 35.4 and 26.7 percentage points in the three- and six-month periods ended June 30, 2011, respectively, compared with the same periods of 2010, attributable to the following factors:

Losses and loss settlement expenses increased 90.7 percent and 53.0 percent in the three- and six-month periods ended June 30, 2011, respectively, compared with the same periods in 2010. The deterioration for the quarter is primarily due to our direct catastrophe loss experience, predominantly from the storms that occurred in April and May in the southern states and Joplin, Missouri. Also contributing to our year-to-date deterioration were assumed reinsurance losses related to the New Zealand earthquake and the earthquake and tsunami in Japan that occurred in the first quarter of 2011.

- Non-catastrophe claims experience - overall claims frequency and severity were both relatively flat in the three-month period ended June 30, 2011.

- Acquisition of Mercer Insurance Group accounted for $28.0 million, or an increase of 41.0 percent and 21.2 percent, in loss and loss settlement expenses in the three- and six-month periods ended June 30, 2011, respectively.

Expense ratio is a component of the combined ratio, increased 6.6 percentage points and 6.5 percentage points in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010. This ratio is the highest we have experienced in recent years, which is attributable to:

- Other underwriting expenses and amortization of deferred policy acquisition costs together increased 58.8 percent and 40.7 percent in the three- and six-month periods ended June 30, 2011, respectively, primarily due to an increase in both amortization of deferred acquisition costs and transaction costs related to our acquisition of Mercer Insurance Group. Mercer Insurance Group related costs totaled $19.5 million and $27.5 million in the three- and six-month periods ended June 30, 2011, respectively. Amortization of deferred policy acquisition costs related to Mercer Insurance Group will be higher than normal over the remainder of 2011 and into the first quarter of 2012, as we amortize the VOBA asset that was recognized in connection with the acquisition in the first year from the date of acquisition.

For a detailed discussion of our consolidated investment results, refer to the “Investment Portfolio” section of this item.

Table of Contents

The following table displays our premiums earned, losses and loss settlement expenses and loss ratio by line of business for the three-month periods ended June 30, 2011 and 2010:

Three Months Ended June 30,

| | 2011 | | | | 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| (In Thousands) Unaudited | Premiums Earned | Losses and Loss Settlement Expenses Incurred | Loss Ratio | | Premiums Earned | Losses and Loss Settlement Expenses Incurred | Loss Ratio | |
| Commercial lines | | | | | | | | |
| Other liability (1) | $29,021 | $10,629 | 36.6 | % | $28,507 | $13,104 | 46.0 | % |
| Fire and allied lines (2) | 44,270 | 67,009 | 151.4 | | 24,460 | 19,482 | 79.6 | |
| Automobile | 29,891 | 17,697 | 59.2 | | 23,216 | 16,653 | 71.7 | |
| Workers' compensation | 13,457 | 11,668 | 86.7 | | 11,628 | 7,505 | 64.5 | |
| Fidelity and surety | 3,844 | 28 | 0.7 | | 4,297 | 2,273 | 52.9 | |
| Miscellaneous | 208 | 168 | 80.8 | | 197 | 9 | 4.6 | |
| Total commercial lines | $120,691 | $107,199 | 88.8 | % | $92,305 | $59,026 | 63.9 | % |
| | | | | | | | | |
| Personal lines | | | | | | | | |
| Fire and allied lines (3) | $9,789 | $17,310 | 176.8 | % | $6,108 | $5,758 | 94.3 | % |
| Automobile | 4,918 | 4,107 | 83.5 | | 3,616 | 3,076 | 85.1 | |
| Miscellaneous | 222 | 101 | 45.5 | | 116 | (49 ) | (42.2 ) | |
| Total personal lines | $14,929 | $21,518 | 144.1 | % | $9,840 | $8,785 | 89.3 | % |
| Reinsurance assumed | $3,389 | $1,407 | 41.5 | % | $3,251 | $442 | 13.6 | % |
| Total | $139,009 | $130,124 | 93.6 | % | $105,396 | $68,253 | 64.8 | % |

(1) “Other liability” is business insurance covering bodily injury and property damage arising from general business operations, accidents on the insured's premises, and products manufactured or sold.
(2) “Fire and allied lines” includes fire, allied lines, commercial multiple peril, and inland marine.
(3) “Fire and allied lines” includes fire, allied lines, homeowners, and inland marine.

Table of Contents

The following table displays our premiums earned, losses and loss settlement expenses and loss ratio by line of business for the six-month periods ended June 30, 2011 and 2010:

Six Months Ended June 30,

| | 2011 | | | | 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| (In Thousands) Unaudited | Premiums Earned | Losses and Loss Settlement Expenses Incurred | Loss Ratio | | Premiums Earned | Losses and Loss Settlement Expenses Incurred | Loss Ratio | |
| Commercial lines | | | | | | | | |
| Other liability | $56,950 | $21,810 | 38.3 | % | $56,721 | $31,945 | 56.3 | % |
| Fire and allied lines | 68,168 | 86,677 | 127.2 | | 48,844 | 39,281 | 80.4 | |
| Automobile | 52,585 | 31,355 | 59.6 | | 46,226 | 30,483 | 65.9 | |
| Workers' compensation | 25,095 | 21,559 | 85.9 | | 22,846 | 11,783 | 51.6 | |
| Fidelity and surety | 7,905 | 19 | 0.2 | | 8,976 | 2,482 | 27.7 | |
| Miscellaneous | 411 | 385 | 93.7 | | 399 | 45 | 11.3 | |
| Total commercial lines | $211,114 | $161,805 | 76.6 | % | $184,012 | $116,019 | 63.0 | % |
| Personal lines | | | | | | | | |
| Fire and allied lines | $16,036 | $19,509 | 121.7 | % | $12,087 | $7,825 | 64.7 | % |
| Automobile | 8,662 | 5,970 | 68.9 | | 7,083 | 5,957 | 84.1 | |
| Miscellaneous | 345 | 103 | 29.9 | | 203 | (76 ) | (37.4 ) | |
| Total personal lines | $25,043 | $25,582 | 102.2 | % | $19,373 | $13,706 | 70.7 | % |
| Reinsurance assumed | $4,616 | $14,402 | NM | | $3,990 | $2,156 | 54.0 | % |
| Total | $240,773 | $201,789 | 83.9 | % | $207,375 | $131,881 | 63.6 | % |

- Other liability - The loss ratio improved by 9.4 percentage points and 18.0 percentage points to 36.6 percent and 38.3 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010. The improvement in this line was due to a slight decrease in severity and frequency, as well as favorable development on prior year claims.

- Commercial fire and allied lines - The loss ratio deteriorated by 71.8 percentage points and 46.8 percentage points to 151.4 percent and 127.2 percent in the three- and six-month periods ended June 30, 2011, respectively, as compared to the same periods of 2010, due primarily to our significant catastrophe loss experience in 2011.

- Workers' compensation - The loss ratio deteriorated by 22.2 percentage points and 34.3 percentage points to 86.7 percent and 85.9 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010. The deterioration in this line was due to an increase in severity and frequency, as a result of several large losses that occurred in the first six months of 2011, as well as development incurred in 2011 on claims that occurred in 2010.

- Fidelity and surety - The loss ratio improved by 52.2 percentage points and 27.5 percentage points to 0.7 percent and 0.2 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010. The improvement in this line is due to minimal losses in the first six months of 2011, along with recoveries from salvage and subrogation on prior year claims.

- Personal fire and allied lines - The loss ratio deteriorated by 82.5 percentage points and 57.0 percentage points to 176.8 percent and 121.7 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to

the same periods of 2010, due primarily to our significant catastrophe loss experience in 2011.



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Table of Contents

Life Insurance Segment Results

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| Revenues | | | | |
| Net premiums earned | $13,201 | $11,686 | $25,641 | $24,015 |
| Investment income, net | 18,290 | 19,288 | 36,616 | 38,619 |
| Net realized investment gains | | | | |
| Other-than-temporary impairment charges | — | — | — | (306) |
| All other net realized gains | 731 | 3,067 | 2,176 | 3,923 |
| Total net realized investment gains | 731 | 3,067 | 2,176 | 3,617 |
| Other income | 199 | 220 | 347 | 401 |
| Total revenues | $32,421 | $34,261 | $64,780 | $66,652 |
| | | | | |
| Benefits, Losses and Expenses | | | | |
| Losses and loss settlement expenses | $5,687 | $4,504 | $10,204 | $9,239 |
| Future policy benefits | 7,880 | 7,375 | 16,062 | 13,765 |
| Amortization of deferred policy acquisition costs | 2,646 | 2,575 | 4,662 | 5,048 |
| Other underwriting expenses | 2,920 | 3,013 | 6,251 | 5,866 |
| Interest on policyholders' accounts | 10,657 | 10,647 | 21,327 | 21,448 |
| Total benefits, losses and expenses | $29,790 | $28,114 | $58,506 | $55,366 |
| | | | | |
| Income before income taxes | $2,631 | $6,147 | $6,274 | $11,286 |

- Net income decreased 58.2 percent and 43.5 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010, which is attributable to:

Net premiums earned increased 13.0 percent and 6.8 percent in the three- and six-month periods ended June 30, 2011, respectively, compared to the same periods of 2010, due to an increase in sales of single premium immediate annuities.

Investment income decreased 5.2 percent in both the three- and six-month periods ended June 30, 2011, compared to the same periods of 2010, as we were unable to obtain the same level of return on the reinvestment of our fixed maturity securities that were called or matured.

Loss and loss settlement expenses increased 26.3 percent and 10.4 percent in the three- and six-month periods ended June 30, 2011, compared to the same periods of 2010, reflecting a rise in both annuity benefits and traditional life insurance death benefits.

Increase in liability for future policy benefits increased 16.7 percent in the six-month period ended June 30, 2011, compared to the same period of 2010, as a result of the growth of our single premium whole life and single premium immediate annuity products.

- Deferred annuity deposits (sales) increased 24.3 percent and 4.5 percent in the three- and six-month periods ended June 30, 2011, respectively, compared with the same periods of 2010. This increase is directly attributable to the activity of a new agency. However, we do not project increased deferred annuity sales as a trend. In fact, deferred annuity sales have continued to decline overall, as interest rates remain at historic lows and as some consumers with a greater tolerance for risk are choosing to surrender their annuities and place the funds in products with greater risk and potentially greater return. Deferred annuity deposits are not recorded as a component of net premiums written or net

premiums earned. However, they do generate investment income.



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- Net cash inflow related to our annuity business was $3.6 million in the three-month period ended June 30, 2011, compared to $0.5 million net cash outflow in the same period of 2010, as a result of one-time activity of a new agency as described above. In the six-month periods ended June 30, 2011 and 2010, net cash outflow was $2.6 million and $1.6 million, respectively.

Investment Portfolio

Our invested assets totaled $2,867.4 million at June 30, 2011, compared to $2,482.9 million at December 31, 2010, an increase of $384.5 million, which is due primarily to our acquisition of Mercer Insurance Group. As of June 30, 2011, the portfolio acquired from Mercer Insurance Group accounted for $398.9 million of our invested assets.

At June 30, 2011, fixed maturity securities comprised 92.4 percent of our investment portfolio, while equity securities accounted for 5.8 percent of the value of our portfolio. Because the primary purpose of our investment portfolio is to fund future claims payments, we follow a conservative investment philosophy, investing in a diversified portfolio of high quality, intermediate-term taxable corporate bonds, taxable U.S. government bonds and tax-exempt U.S. municipal bonds.

Composition

We develop our investment strategies based on a number of factors, including estimated duration of reserve liabilities, short- and long-term liquidity needs, projected tax status, general economic conditions, expected rates of inflation and regulatory requirements. We administer our investment portfolio based on investment guidelines approved by management and the investment committee of our Board of Directors that comply with applicable statutory regulations.

The composition of our investment portfolio at June 30, 2011, is presented at carrying value in the following table:

| | Property & Casualty Insurance Segment | | | Life Insurance Segment | | | Total | | |
|---|---|---|---|---|---|---|---|---|---|
| (Dollars in Thousands) | | Percent of Total | | | Percent of Total | | | Percent of Total | |
| Fixed maturities [1] | $1,105,438 | 86.1 | % | $1,544,701 | 97.6 | % | $2,650,139 | 92.4 | % |
| Equity securities | 145,752 | 11.3 | | 20,563 | 1.3 | | 166,315 | 5.8 | |
| Trading securities | 15,058 | 1.2 | | — | — | | 15,058 | 0.5 | |
| Mortgage loans | — | — | | 6,423 | 0.4 | | 6,423 | 0.2 | |
| Policy loans | — | — | | 7,328 | 0.5 | | 7,328 | 0.3 | |
| Other long-term investments | 16,875 | 1.3 | | 3,772 | 0.2 | | 20,647 | 0.7 | |
| Short-term investments | 1,500 | 0.1 | | — | — | | 1,500 | 0.1 | |
| Total | $1,284,623 | 100.0 | % | $1,582,787 | 100.0 | % | $2,867,410 | 100.0 | % |

(1) Available-for-sale fixed maturities are carried at fair value. Held-to-maturity fixed maturities are carried at amortized cost.

At June 30, 2011, we classified $2,644.5 million, or 99.8 percent, of our fixed maturities portfolio as available-for-sale, compared to $2,278.4 million, or 99.7 percent, at December 31, 2010. We classify our remaining fixed maturities as held-to-maturity or trading. We record held-to-maturity securities at amortized cost. We record trading securities, primarily convertible redeemable preferred debt securities, at fair value, with any changes in fair value recognized in earnings.

As of June 30, 2011 and December 31, 2010, we did not have direct exposure to investments in subprime mortgages or other credit enhancement vehicles. Our exposure to derivative instruments and hedging is described in detail in Part I, Item 1, Note 13, “Derivative Instruments and Hedging Activities.”

50

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Table of Contents

Credit Quality

The following table shows the composition of fixed maturity securities held in our available-for-sale, held-to-maturity and trading security portfolios, by credit rating at June 30, 2011 and December 31, 2010. Information contained in the table is generally based upon the issue credit ratings provided by Moody's, unless the rating is unavailable, in which case we obtain it from Standard & Poor's.

| (In Thousands) | June 30, 2011 | | | December 31, 2010 | | |
|---|---|---|---|---|---|---|
| Rating | Carrying Value | % of Total | | Carrying Value | % of Total | |
| AAA | $375,053 | 14.1 | % | $279,009 | 12.1 | % |
| AA | 618,009 | 23.2 | | 480,478 | 20.9 | |
| A | 584,720 | 21.9 | | 476,044 | 20.7 | |
| Baa/BBB | 960,359 | 36.0 | | 938,781 | 40.9 | |
| Other/Not Rated | 127,056 | 4.8 | | 123,367 | 5.4 | |
| | $2,665,197 | 100.0 | % | $2,297,679 | 100.0 | % |

Changes in the credit ratings of our fixed maturity securities portfolio at June 30, 2011, from December 31, 2010, is primarily due to the inclusion of Mercer Insurance Group's invested assets in our portfolio at June 30, 2011.

Duration

Our investment portfolio is comprised primarily of fixed maturity securities whose fair value is susceptible to market risk, specifically interest rate changes. Duration is a measurement used to quantify our inherent interest rate risk and analyze our ability to match our invested assets to our claims liabilities. If our invested assets and claims liabilities have similar durations, then any change in interest rates will have an equal and opposite effect on these accounts. Mismatches in the duration of assets and liabilities can cause significant fluctuations in our results of operations. The primary purpose for matching invested assets and claims liabilities is liquidity. With appropriate matching, our investments will mature when cash is needed, preventing the need to liquidate other assets prematurely.

Group

The weighted average duration of our portfolio of fixed maturity securities, at June 30, 2011, is 6.3 years compared to 5.2 years at December 31, 2010.

Property and Casualty Insurance Segment

The weighted average duration of our portfolio of fixed maturity securities, at June 30, 2011, is 7.4 years compared to 6.5 years at December 31, 2010.

Life Insurance Segment

The weighted average duration of our portfolio of fixed maturity securities, at June 30, 2011 is 3.8 years compared to 3.6 years at December 31, 2010.

Investment Results

We invest the premiums received from our policyholders and annuitants in order to generate investment income, which is an important component of our revenues and profitability. The amount of investment income that we are able to generate is affected by many factors, some of which are beyond our control. Some of these factors are: volatility in the financial markets, economic growth, inflation, interest rates, world political conditions, terrorist attacks or threats of terrorism, adverse events affecting other companies in our industry or the industries in which we invest and other unpredictable national or world events.

Table of Contents

In our life insurance segment, net investment income decreased 5.2 percent in both the three- and six-month periods ended June 30, 2011, compared with the same periods of 2010, due to historically low yields, which we have been mitigating by increasing the duration of our investments in order to achieve better yields.
In our property and casualty insurance segment, our acquisition of Mercer Insurance Group contributed to the 5.0 percent and 3.1 percent increase in net investment income in the three- and six-month periods ended June 30, 2011, compared to with the same periods of 2010. The increase was somewhat offset by the impact of low interest rates and a decrease in the value of our investments in limited liability partnership holdings. Our property and casualty insurance segment holds certain investments in limited liability partnership that are accounted for under the equity method of accounting, with changes in the value of these investments recorded in investment income.
Net realized investment gains were $1.1 million and $3.8 million in the three- and six-month periods ended June 30, 2011, compared to $2.3 million and $5.1 million in the same periods of 2010. There were no other-than-temporary impairment charges in the three- and six-month periods ended June 30, 2011, compared to $0.1 million and $0.5 million in the same periods of 2010.
We continually monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires OTTI charges to be recorded when we determine that it is more likely than not that we will be unable to collect all amounts due according to the contractual terms of the fixed maturity security or that the anticipated recovery in fair value of the equity security will not occur in a reasonable amount of time. Impairment charges on investments are recorded based on the fair value of the investments at the measurement date. Factors considered in evaluating whether a decline in value is other-than-temporary include: the length of time and the extent to which fair value has been less than cost; the financial condition and near-term prospects of the issuer; our intention to hold the investment; and the likelihood that we will be required to sell the investment.
Changes in unrealized gains on available-for-sale securities do not affect net income and earnings per share but do impact comprehensive income, stockholders' equity and book value per share. We believe that any unrealized losses on our available-for-sale securities at June 30, 2011, are temporary based upon our current analysis of the issuers of the securities that we hold and current market events. It is possible that we could recognize impairment losses in future periods on securities that we own at June 30, 2011, if future events and information cause us to determine that a decline in value is other-than-temporary. However, we endeavor to invest in high quality assets to provide protection from future credit quality issues and corresponding impairment write-downs.

## LIQUIDITY AND CAPITAL RESOURCES

Liquidity measures our ability to generate sufficient cash flows to meet our short- and long-term cash obligations. Our cash inflows are primarily a result of premiums, annuity deposits, reinsurance recoveries, sales or maturities of investments, and investment income. Cash provided from these sources is used primarily for loss and loss settlement expenses, payment of policyholder benefits under life insurance contracts; annuity withdrawals, operating expenses, dividends, pension plan contributions, and in recent years, common stock repurchases.
Cash outflows may be variable because of the uncertainty regarding settlement dates for losses. In addition, the timing and amount of individual catastrophe losses are inherently unpredictable and could increase our liquidity requirements. The timing and amount of reinsurance recoveries may be affected by reinsurer solvency and reinsurance coverage disputes.
Historically, we have generated substantial cash inflows from operations. It is our policy to invest the cash generated from operations in securities with maturities that correlate to the anticipated timing of payments for losses and loss settlement expenses of the underlying insurance policies. The majority of our assets are invested in available-for-sale fixed maturity securities.

Table of Contents

The following table displays a summary of cash sources and uses in 2011 and 2010.

| Cash Flow Summary | Six Months Ended June 30, | |
|---|---|---|
| (In Thousands) | 2011 | 2010 |
| Cash used in | | |
| Operating activities | $40,790 | $43,468 |
| Investing activities | (123,782) | (156,150) |
| Financing activities | 80,349 | 78,670 |
| Net decrease in cash and cash equivalents | $(2,643) | $(34,012) |

Operating Activities

Net cash flows provided by operating activities totaled $40.8 million and $43.5 million for the six-month periods ended June 30, 2011 and 2010, respectively. Cash flows for the six-month period ended June 30, 2011, reflected a higher level of property and casualty insurance premiums collected, which was somewhat offset by a higher level of loss and loss settlement expense payments and operating expenses paid, compared to the same period of 2010. Additionally, we experienced a lower level of investment income received.

Our cash flows from operations were sufficient to meet our liquidity needs for the six-month periods ended June 30, 2011 and 2010.

Investing Activities

Cash in excess of operating requirements is generally invested in fixed maturity securities and equity securities. Fixed maturities provide regular interest payments and allow us to match the duration of our liabilities. Equity securities provide dividend income, potential dividend income growth and potential appreciation. For further discussion of our investments, including our philosophy and portfolio, see the “Investment Portfolio” section contained in this item.

In addition to investment income, possible sales of investments and proceeds from calls or maturities of fixed maturity securities also can provide liquidity. During the next five years, $1.5 billion, or 57.1 percent of our fixed maturity portfolio will mature.

We invest funds required for short-term cash needs primarily in money market accounts, which are classified as cash equivalents. At June 30, 2011, our cash and cash equivalents included $83.1 million related to these money market accounts, compared to $34.4 million at December 31, 2010.

Net cash flows used in investing activities totaled $123.8 million and 156.2 million for the six-month periods ended June 30, 2011 and 2010, respectively. In the six-month period ended June 30, 2011, we had cash inflows from scheduled and unscheduled investment maturities, redemptions, prepayments, and sales of investments that totaled $339.9 million compared to $201.1 million for the same period in 2010.

Our cash outflows for investment purchases totaled $294.5 million for the six-month period ended June 30, 2011, compared to $281.3 million for the same period in 2010. In 2011, as in 2010, we purchased a higher level of fixed maturity securities rather than other investment vehicles, such as short-term investments, which continue to be less profitable due to the lower market interest rates. In the six-month period ended June 30, 2011, we had net cash outflows totaling $172.6 million related to our acquisition of Mercer Insurance Group.

Financing Activities

Net cash flows provided by financing activities totaled $80.3 million and $78.7 million for the six-month periods ended June 30, 2011 and 2010, respectively. Included in our 2010 cash flows was $75.0 million related to the change in our securities lending collateral for a program that we terminated in December 2010. In addition, impacting our 2011 cash flows were borrowed funds totaling $79.9 million related to our acquisition of Mercer Insurance Group. For further discussion of our outstanding debt, please see Part I, Item 1, Note 11, “Debt.”

Table of Contents

In the six-month period ended June 30, 2011, net cash inflows from our life insurance segment's annuity and universal life deposits totaled $14.2 million, compared to $15.2 million for the same period of 2010, as interest rates continue to remain at historic lows, some consumers continue to seek products with greater risk. In the six-month period ended June 30, 2011, we repurchased $6.1 million of our common stock, compared to $3.7 million in the same period in 2010.

Line of Credit

In the first quarter of 2011, we entered into a $50.0 million line of credit with Bankers Trust Company. This line of credit is available if our operating and investing cash flows are not sufficient to support our operations. For the six-month period ended June 30, 2011, we utilized our entire line of credit to assist in the funding of our acquisition of Mercer Insurance Group. For further discussion of the utilization of our line of credit, please see Part I, Item 1, Note 11, “Debt.”

Under the terms of our credit agreement with Bankers Trust Company, interest on outstanding notes is adjusted monthly to the monthly London Interbank Offered Rate (“LIBOR”), as published in the Wall Street Journal, plus 180 basis points, calculated using a 360 day year and the actual days of the month the principal is outstanding. In addition, the line of credit incurs an annual facility charge of $25,000. Interest payments are due monthly on this line. The line of credit contains certain financial covenants including covenants that require us to maintain our A.M. Best rating, a debt to capitalization ratio and minimum stockholders equity.

In addition, Mercer Insurance Group has the ability to borrow up to $7.5 million on a bank line of credit with Union Bank of California. Under the terms of that credit agreement with Union Bank of California, the line of credit bears interest at the bank’s base rate or an optional rate based on LIBOR. The effective annual interest rate as of June 30, 2011 was 3.25 percent. In addition, the line of credit incurs an annual facility charge of $10,000. Interest payments are due monthly on this line. The line of credit contains certain financial covenants, including covenants that require Mercer Insurance Group to maintain a minimum statutory surplus and to distribute from subsidiaries no more than 50.0 percent of allowable dividends.

As of June 30, 2011, Mercer Insurance Group has utilized $3.0 million of the outstanding line of credit.

We were in compliance with all covenants for all credit agreements as of June 30, 2011.

Stockholders' Equity

Stockholders' equity decreased 1.6 percent to $704.8 million at June 30, 2011, from $716.4 million at December 31, 2010. The decrease in our stockholders' equity was primarily attributable to a net loss of $12.1 million, along with stockholder dividends of $7.8 million and stock repurchases of $6.1 million. The decrease was somewhat offset by net unrealized investment appreciation of $12.5 million, net of tax. At June 30, 2011, book value per share was $27.23 compared to $27.35 at December 31, 2010.

Off-Balance Sheet Arrangements

Pursuant to an agreement with one of our limited liability partnership holdings, we are contractually committed to make capital contributions up to $15.0 million, upon request by the partnership, through December 31, 2017. As of June 30, 2011, our remaining potential contractual obligation was $10.1 million.

STATUTORY FINANCIAL MEASURES

United Fire and its subsidiaries are required to file financial statements based on statutory accounting principles in each of the states where our insurance companies are domiciled and licensed to conduct business. Management analyzes financial data and statements that are prepared in accordance with statutory accounting principles and GAAP.

Table of Contents

Regulation G promulgated by the Securities and Exchange Commission does not require reconciliation to GAAP of data prepared under a system of regulation of a government or governmental authority or self-regulatory organization that is applicable to the registrant.

The following definitions of key statutory financial measures are provided for our readers' convenience.

Premiums written is a measure of our overall business volume. Net premiums written comprise direct and assumed premiums written, less ceded premiums written. Direct premiums written is the amount of premiums charged for policies issued during the period. For the property and casualty insurance segment there are no differences between direct statutory premiums written and direct premiums written under GAAP. However, for the life insurance segment, deferred annuity deposits (i.e., sales) are included in direct statutory premiums written, whereas they are excluded for GAAP.

Assumed premiums written is consideration or payment we receive in exchange for insurance we provide to other insurance companies. We report these premiums as revenue as they are earned over the underlying policy period.

Ceded premiums written is the portion of direct premiums written that we cede to our reinsurers under our reinsurance contracts. Premiums written is an important measure of business production for the period under review.

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| Net premiums written | $172,196 | $128,749 | $295,355 | $248,185 |
| Net change in unearned premium | (20,453) | (11,695) | (29,543) | (16,881) |
| Net change in prepaid reinsurance premium | 467 | 28 | 602 | 86 |
| Net premiums earned | $152,210 | $117,082 | $266,414 | $231,390 |

Combined ratio is a commonly used statutory financial measure of underwriting performance. A combined ratio below 100.0 percent generally indicates a profitable book of business. The combined ratio is the sum of two separately calculated ratios, the loss and loss settlement expense ratio (the "net loss ratio") and the underwriting expense ratio (the "expense ratio").

When prepared in accordance with GAAP, the net loss ratio is calculated by dividing the sum of losses and loss settlement expenses by net premiums earned. The expense ratio is calculated by dividing nondeferred underwriting expenses and amortization of deferred policy acquisition costs by net premiums earned.

When prepared in accordance with statutory accounting principles, the net loss ratio is calculated by dividing the sum of losses and loss settlement expenses by net premium earned; the expense ratio is calculated by dividing underwriting expenses by net premiums written.

Underwriting gain (loss) is the gain or loss by an insurance company from the business of insurance. Underwriting income is equal to net premiums earned less incurred losses and loss settlement expenses, amortization of deferred policy acquisition costs, and other underwriting expenses. We use this financial measure in evaluating the results of our operations and to analyze the profitability of our property and casualty insurance segment underwriting operations.

Statutory surplus is the excess of admitted assets, those recognized and accepted by the state insurance laws to determine solvency, over liabilities.

NON-GAAP FINANCIAL MEASURES

We believe that disclosure of certain Non-GAAP financial measures enhances investor understanding of our financial performance. The following Non-GAAP financial measure is utilized in this filing:

Catastrophe losses utilize the designations of the Insurance Services Office (ISO) and are reported with loss and loss settlement expense amounts net of reinsurance recoverables, unless specified otherwise. According to the ISO,

55

Table of Contents

a catastrophe loss is defined as a single unpredictable incident or series of closely related incidents that result in $25.0 million or more in U.S. industry-wide direct insured losses to property and that affect a significant number of insureds and insurers (“ISO catastrophe”). In addition to ISO catastrophes, we also include as catastrophes those events (“non-ISO catastrophes”), which may include U.S. or international losses, that we believe are, or will be, material to our operations, either in amount or in number of claims made. Management, at times, may determine for comparison purposes that it is more meaningful to exclude extraordinary catastrophe losses and resulting litigation, such as Hurricane Katrina. The frequency and severity of catastrophic losses we experience in any year affect our results of operations and financial position. In analyzing the underwriting performance of our property and casualty insurance segment, we evaluate performance both including and excluding catastrophe losses. Portions of our catastrophe losses may be recoverable under our catastrophe reinsurance agreements. We include a discussion of the impact of catastrophes because we believe it is meaningful for investors to understand the variability in periodic earnings.

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| (In Thousands) | 2011 | 2010 | 2011 | 2010 |
| ISO catastrophes [1] | $32,535 | $7,545 | $32,892 | $10,573 |
| Non-ISO catastrophes [2] | 2,371 | 25 | 14,436 | 153 |
| Total catastrophes | $34,906 | $7,570 | $47,328 | $10,726 |

(1) This number does not include loss and loss settlement expenses incurred for Hurricane Katrina claims and related litigation totaling $1.9 million for the three-month period ended June 30, 2011. There were no loss and loss settlement expenses incurred in the same period of 2010. For the six-month periods ended June 30, 2011 and 2010, loss and loss settlement expenses incurred totaled $5.8 million and $5.4 million, respectively.
(2) This number includes international assumed losses.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We have exposure to market risk arising from potential losses in our investment portfolio due to adverse changes in interest rates and market prices. However, we have the ability to hold fixed maturity investments to maturity. Our investment guidelines define the overall framework for managing our market and other investment risks including accountability and controls. In addition, each of our subsidiaries has specific investment policies that delineate the investment limits and strategies that are appropriate given each entity's liquidity, surplus, product, and regulatory requirements. We respond to market risk by managing the character of investment purchases.

It is our philosophy that we do not utilize financial instrument hedges or derivative financial instruments to manage risks, nor do we enter into any swap, forward or option contracts, but attempt to mitigate our exposure through active portfolio management. However, as a result of our acquisition of Mercer Insurance Group in 2011, our investment portfolio does utilize derivative instruments and hedges. Our exposure to derivative instruments and hedging is described in detail in Part I, Item 1, Note 13, “Derivative Instruments and Hedging Activities.”

In addition, we place the majority of our investments in high-quality, liquid securities and limit the amount of credit exposure to any one issuer. At June 30, 2011, we did not hold investments in sub-prime mortgages, credit default swaps, or other credit-enhancement exposures.

While our primary market risk exposure is change in interest rates, we do have exposure to changes in equity prices and limited exposure to foreign currency exchange rates.

There have been no material changes in our market risk or market risk factors from that reported in our Annual Report on Form 10-K for the year ended December 31, 2010.

Table of Contents

## ITEM 4. CONTROLS AND PROCEDURES

### Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, have evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based on that evaluation, the chief executive officer and chief financial officer concluded that our disclosure controls and procedures, as of the end of the period covered by this report, were designed and functioning effectively to provide reasonable assurance that the information required to be disclosed by us in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. We believe that a control system, no matter how well designed and operated, cannot provide absolute assurance that the objectives of the control system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

### Changes in Internal Control Over Financial Reporting

Our management, including our chief executive officer and chief financial officer, has evaluated our internal control over financial reporting to determine whether any changes occurred during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on this evaluation, no such change in our internal control over financial reporting occurred during the fiscal quarter to which this report relates.

# PART II - OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

For a detailed discussion of our legal proceedings, refer to Note 9, "Contingent Liabilities" in the Notes to Unaudited Consolidated Financial Statements of this Form 10-Q.

## ITEM 1A. RISK FACTORS

Our business is subject to a number of risks, including those identified in Part I, Item 1A of our 2010 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 1, 2011, that could have a material effect on our business, results of operations, financial condition, and/or liquidity and that could cause our operating results to vary significantly from period to period. The risks described in the above mentioned document are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial could also have a material effect on our business, results of operations, financial condition and/or liquidity.

Table of Contents

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Under our Share Repurchase Program, first announced in August 2007, we may purchase United Fire common stock from time to time on the open market or through privately negotiated transactions. The amount and timing of any purchases will be at our discretion and will depend upon a number of factors, including the share price, economic and general market conditions, and corporate and regulatory requirements. We will generally consider repurchasing our common stock on the open market if (i) the trading price on NASDAQ drops below 130 percent of its book value, (ii) sufficient excess capital is available to purchase the stock, and (iii) we are optimistic about future market trends and the performance of our company. Our Share Repurchase Program may be modified or discontinued at any time.

Our Board of Directors has authorized us to purchase up to an additional 1,000,000 shares of common stock through August 2013 with remaining authorization at June 30, 2011 of 849,229 shares.

The following table provides information with respect to purchases of shares of common stock made by or on our behalf or by any "affiliated purchaser," as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, during the three-month period ended June 30, 2011.

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as a Part of Publicly Announced Plans or Programs | Maximum Number of Shares that may be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| 4/1/2011 - 4/30/2011 | — | $— | — | 172,826 |
| 5/1/2011 - 5/31/2011 | 147,977 | 19.19 | 147,977 | 1,024,849 |
| 6/1/2011 - 6/30/2011 | 175,620 | 18.46 | 175,620 | 849,229 |

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. (REMOVED AND RESERVED)

None.

ITEM 5. OTHER INFORMATION

None.

Table of Contents

ITEM 6. EXHIBITS

| Exhibit number | Exhibit description | Filed herewith |
|---|---|---|
| 11 | Statement Re Computation of Per Share Earnings. All information required by Exhibit 11 is presented within Note 7 of the Notes to Unaudited Consolidated Financial Statements, in accordance with the FASB guidance on Earnings per Share | X |
| 31.1 | Certification of Randy A. Ramlo pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | X |
| 31.2 | Certification of Dianne M. Lyons pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | X |
| 32.1 | Certification of Randy A. Ramlo pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | X |
| 32.2 | Certification of Dianne M. Lyons pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | X |
| 101.1 | The following financial information from United Fire & Casualty Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2011 formatted in XBRL: (i) Consolidated Balance Sheets at June 30, 2011 (unaudited) and December 31, 2010; (ii) Consolidated Statements of Income (unaudited) for the three months and six months ended June 30, 2011 and 2010; (iii) Consolidated Statement of Stockholders' Equity (unaudited) for the six months ended June 30, 2011; (iv) Consolidated Statements of Cash Flows (unaudited) for the six months ended June 30, 2011 and 2010; and (v) Notes to Unaudited Consolidated Financial Statements, tagged as a block of text. | X |

Table of Contents

SIGNATURES

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

UNITED FIRE & CASUALTY COMPANY
(Registrant)

/s/ Randy A. Ramlo
Randy A. Ramlo
President, Chief Executive Officer,
Director and Principal Executive Officer

August 5, 2011
(Date)

/s/ Dianne M. Lyons
Dianne M. Lyons
Vice President, Chief Financial Officer and
Principal Accounting Officer

August 5, 2011
(Date)