

National Interstate CORP
Form SC 14D9/A
March 11, 2014

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Schedule 14D-9

**SOLICITATION/RECOMMENDATION STATEMENT UNDER SECTION 14(d)(4) OF THE SECURITIES
EXCHANGE ACT OF 1934**

(Amendment No. 3)

NATIONAL INTERSTATE CORPORATION

(Name of Subject Company)

NATIONAL INTERSTATE CORPORATION

(Name of Person(s) Filing Statement)

Common Shares, par value \$0.01 per share

(Title of Class of Securities)

63654U100

(CUSIP Number of Class of Securities)

Arthur J. Gonzales

Vice President, General Counsel and Secretary

3250 Interstate Drive

Richfield, Ohio 44286-9000

(303) 659-8900

**(Name, address and telephone number of person authorized to receive notice and communications
on behalf of the person(s) filing statement)**

With a copy to:

Anthony E. Kuhel, Jr.

Thomas A. Aldrich

Thompson Hine LLP

3900 Key Center

127 Public Square

Cleveland, Ohio 44114-1291

(216) 566-5500

“ Check the box if the filing relates solely to preliminary communications made before the commencement of a tender offer.

This Amendment No. 3 (this Amendment No. 3) amends and supplements the Solicitation/Recommendation Statement on Schedule 14D-9 filed with the Securities and Exchange Commission (the SEC) on March 3, 2014 by National Interstate Corporation, an Ohio corporation (as amended or supplemented from time to time, including as amended by this Amendment No. 3, the Statement).

Except as otherwise set forth below, the information set forth in the Statement remains unchanged and is incorporated herein by reference to the extent relevant to the items in this Amendment No. 3. Capitalized terms used but not otherwise defined herein have the meanings ascribed to such terms in the Statement.

Item 4. *The Solicitation or Recommendation*

(a) The following is added immediately before the discussion of the board meeting held on February 17, 2014 in the section entitled *Item 4 The Solicitation or Recommendation Background of the Offer* :

On February 17, 2014, the board of directors received the management five year financial projections for the Company, consisting of projected financial statements for 2014-2018, including projected profit and loss statements, projected balance sheets and projected required capital. The projections had also been provided to Duff & Phelps in connection with its analysis of the Initial Offer Price. The projections assumed organic growth in Gross Premiums Written of 9.5% in 2014 and 10.0% in each of 2015-2018, retention ratio (Net Premiums Written/Gross Premiums Written) of 83.6% in 2014 and 85.0% in each of 2015-2018, and Loss Ratio of 72.8% in 2014 and 72.0% in each of 2015-2018. The projections, including for 2014, do not consider favorable or unfavorable development from prior years loss reserves. The projections are attached as Annex A to this Statement and are incorporated herein by reference.

In addition, in connection with the consideration of a potential acquisition by the Company in January 2014 unrelated to the offer, management of the Company prepared certain initial five year (2014-2018) financial projections that were shared, in the ordinary course, with senior executives of the Purchaser and AFG solely in connection with the consideration of such potential acquisition by the Company. The Company did not ultimately pursue the potential acquisition. The projections assumed organic growth in Gross Premiums Written of 10.2% in 2014, 12.9% in 2015, 13.0% in 2016, and 12.0% in each of 2017 and 2018, retention ratio (Net Premiums Written/Gross Premiums Written) of 83.6% in 2014 and 85.0% in each of 2015-2018, and Loss Ratio of 73.0% in 2014 and 72.0% in each of 2015-2018. The projections, including for 2014, do not consider favorable or unfavorable development from prior years loss reserves. The projections are attached as Annex B to this Statement and are incorporated herein by reference.

Starting with 2015, projections for every year have higher potential variability than projections for a preceding year because projections for succeeding years reflect the assumption that projections for preceding years have been realized. The projections were not prepared for the purpose of evaluating the offer; rather they were prepared and utilized for purposes of internal management analysis. The projections contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Please see *Certain Forward-Looking Statements* for more information and the first page of Annex A for additional disclosures specifically related to the projections.

Certain Forward-Looking Statements

This Statement contains and incorporates by reference certain forward-looking statements. All statements other than statements of historical fact included or incorporated by reference in this Statement are forward-looking statements. There is no assurance that the Company's expectations reflected in such forward-looking statements will prove to have been correct. A number of risks and uncertainties could cause actual events or results to differ materially from these statements, including without limitation, the risk factors described from time to time in the Company's documents and reports filed with the SEC. Accordingly, actual future events may differ materially from those expressed or implied in any such forward-looking statements.

SIGNATURE

After reasonable inquiry and to the best of its knowledge and belief, the undersigned certifies that the information set forth in this statement is true, complete and correct.

NATIONAL INTERSTATE CORPORATION

By: /s/ ARTHUR J. GONZALES

Name: **Arthur J. Gonzales**

Title: **Vice President, General Counsel and Secretary**

Dated: March 11, 2014

Annex A

National Interstate Corporation

Financial 4.0 Projected Financial Statements

These projections are only utilized in management analysis for M&A valuation models and excess capital forecasts and as such have not been presented to or approved by our Board of Directors.

Disclaimers:

The 2014 projections are based upon a detailed product, investment and cost center expense budget process and have been vetted by management and approved by the Board of Directors.

The 2015-2018 projections are estimates only and have not been prepared at a detailed product, investment or cost center ground up level. Such projections do not anticipate any material economic, insurance industry or National Interstate Corporation specific changes including, but not limited to, the following:

Insurance regulatory or market changes

Loss of any material customers or sale of any existing businesses

Acquisition growth or costs

Volatility in investment markets

Change in business mix or niche focus

NATL Projections
Projected Profit and Loss Statements
GAAP Basis Income Statements (000 s)

Income Statement

| | 2012 | 2013 | Estimated 2014 | NATL Estimated 2015 | Estimated 2016 | Estimated 2017 | Estimated 2018 |
|--|------------|------------|-------------------|---------------------------|-------------------|-------------------|-------------------|
| Gross Premiums Written - organic | \$ 573,470 | \$ 631,993 | \$ 691,855 | \$ 761,040 | \$ 837,144 | \$ 920,858 | \$ 1,012,944 |
| Gross Premiums Written - M&A | | | | | | | |
| Total gross premiums written | 573,470 | 631,993 | 691,855 | 761,040 | 837,144 | 920,858 | 1,012,944 |
| Net Premiums Written | \$ 492,215 | \$ 537,604 | \$ 578,724 | \$ 646,884 | \$ 711,572 | \$ 782,730 | \$ 861,003 |
| Net Premiums Earned | \$ 458,049 | \$ 525,710 | \$ 551,239 | \$ 612,804 | \$ 679,228 | \$ 747,151 | \$ 821,866 |
| Net Investment Income | 34,927 | 33,377 | 36,145 | 44,887 | 52,391 | 61,583 | 72,022 |
| Realized G/L | 6,219 | 6,536 | 5,738 | 6,180 | 6,744 | 7,441 | 8,293 |
| Other Income | 3,278 | 3,275 | 2,549 | 3,805 | 4,186 | 4,604 | 5,065 |
| Total Revenues | 502,474 | 568,899 | 595,671 | 667,677 | 742,548 | 820,779 | 907,246 |
| Losses and loss adjustment expenses | 341,008 | 429,556 | 401,391 | 441,219 | 489,044 | 537,949 | 591,744 |
| Commissions | 38,419 | 36,805 | 39,348 | 45,282 | 49,810 | 54,791 | 60,270 |
| Premium taxes | 12,677 | 13,155 | 15,079 | 16,587 | 18,246 | 20,070 | 22,077 |
| Assessments | 4,279 | 5,019 | 5,378 | 5,916 | 6,507 | 7,158 | 7,874 |
| Other operating and general expenses | 54,336 | 54,687 | 62,042 | 66,635 | 74,887 | 82,375 | 90,613 |
| Change in DPAC | (644) | 2,221 | (3,073) | (1,926) | (2,626) | (2,889) | (3,178) |
| Total Expenses | 450,076 | 541,444 | 520,166 | 573,713 | 635,868 | 699,455 | 769,400 |
| Interest expense - debt | 616 | 706 | 560 | 590 | 620 | 650 | 680 |
| Interest on funds held | 3,953 | 5,057 | 4,886 | 6,068 | 7,082 | 8,325 | 9,567 |
| Total interest expense | 4,569 | 5,763 | 5,446 | 6,658 | 7,702 | 8,975 | 10,247 |
| Income before income taxes | 47,829 | 21,692 | 70,060 | 87,306 | 98,978 | 112,349 | 127,598 |
| | 13,535 | 4,119 | 21,018 | 27,501 | 31,178 | 35,390 | 40,193 |

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| Provision for income taxes | | | | | | | |
|-------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| Net income | \$ 34,294 | \$ 17,573 | \$ 49,042 | \$ 59,804 | \$ 67,800 | \$ 76,959 | \$ 87,405 |
| Loss and LAE Ratio (% of NEP) | 74.4% | 81.7% | 72.8% | 72.0% | 72.0% | 72.0% | 72.0% |
| Expense Ratio (% of NEP) | 23.1% | 20.7% | 21.1% | 21.0% | 21.0% | 21.0% | 21.0% |
| Combined Ratio | 97.5% | 102.4% | 93.9% | 93.0% | 93.0% | 93.0% | 93.0% |

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NATL Projections
Projected Balance Sheets
Balance Sheet
GAAP Basis Balance Sheets (000 s)

| | 2012 | 2013 | Estimated 2014 | Estimated 2015 | Estimated 2016 | Estimated 2017 | Estimated 2018 |
|---|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Assets | | | | | | | |
| Investments | \$ 1,054,792 | \$ 1,074,528 | \$ 1,194,177 | \$ 1,286,204 | \$ 1,403,503 | \$ 1,548,517 | \$ 1,725,995 |
| Accrued Investment | 8,937 | 8,644 | 9,398 | 11,671 | 13,622 | 16,012 | 18,726 |
| Premium Receivable | 215,690 | 246,756 | 242,149 | 266,364 | 293,000 | 322,300 | 344,401 |
| Reinsurance Recoverable | 174,345 | 169,210 | 209,826 | 219,414 | 234,776 | 255,897 | 280,636 |
| Prepaid reinsurance premiums | 32,570 | 37,867 | 46,660 | 51,772 | 56,624 | 61,960 | 67,831 |
| DPAC | 25,246 | 23,025 | 26,098 | 28,024 | 30,650 | 33,539 | 36,716 |
| Deferred taxes | 19,883 | 25,826 | 30,508 | 32,399 | 34,871 | 38,049 | 41,707 |
| Fixed Assets | 24,539 | 24,753 | 34,593 | 38,052 | 41,857 | 46,043 | 50,647 |
| Intangible assets | 8,355 | 8,073 | 7,791 | 7,509 | 7,227 | 6,945 | 6,663 |
| Other Assets | 5,866 | 6,067 | 8,681 | 9,703 | 10,674 | 11,741 | 12,915 |
| Total Assets | \$ 1,570,224 | \$ 1,624,749 | \$ 1,809,880 | \$ 1,951,112 | \$ 2,126,804 | \$ 2,341,003 | \$ 2,586,237 |
| Liabilities | | | | | | | |
| Unearned Premiums | \$ 266,126 | 283,582 | \$ 311,067 | \$ 345,147 | \$ 377,491 | \$ 413,069 | \$ 452,206 |
| Gross Reserves | 775,305 | 803,782 | 909,246 | 950,794 | 1,017,362 | 1,108,885 | 1,216,089 |
| Long-term debt | 12,000 | 12,000 | 12,000 | 12,000 | 12,000 | 12,000 | 12,000 |
| Amounts withheld | 67,002 | 82,821 | 90,666 | 99,733 | 109,706 | 120,677 | 132,744 |
| Reinsurance balances payable | 19,473 | 26,317 | 26,586 | 26,827 | 29,509 | 32,460 | 35,706 |
| Accounts payable and other liabilities | 59,058 | 43,616 | 47,748 | 52,522 | 57,775 | 63,552 | 69,907 |
| Commission payable and assessments | 17,316 | 20,346 | 20,756 | 22,831 | 25,114 | 27,626 | 30,388 |
| Total Liabilities | \$ 1,216,279 | \$ 1,272,464 | \$ 1,418,068 | \$ 1,509,854 | \$ 1,628,957 | \$ 1,778,269 | \$ 1,949,041 |

| | | | | | | | |
|-------------------------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Equity | | | | | | | |
| Total Capital | \$ 81,328 | \$ 70,767 | \$ 70,767 | \$ 70,767 | \$ 70,767 | \$ 70,767 | \$ 70,767 |
| Retained Earnings | 272,618 | 281,518 | 321,046 | 370,491 | 427,080 | 491,967 | 566,430 |
| Total Equity | \$ 353,946 | \$ 352,285 | \$ 391,812 | \$ 441,258 | \$ 497,847 | \$ 562,733 | \$ 637,197 |
| Total Liabilities and Equity | | | | | | | |
| Total Liabilities and Equity | \$ 1,570,224 | \$ 1,624,749 | \$ 1,809,880 | \$ 1,951,112 | \$ 2,126,804 | \$ 2,341,003 | \$ 2,586,237 |
| GAAP Net Income | | | | | | | |
| Average | 34,294 | 17,573 | 49,042 | 59,804 | 67,800 | 76,959 | 87,405 |
| Equity | 351,422 | 353,115 | 372,049 | 416,535 | 469,552 | 530,290 | 599,965 |
| GAAP ROE | 9.76% | 4.98% | 13.18% | 14.36% | 14.44% | 14.51% | 14.57% |

NATL Projections
Projected Required Capital
BCAR Model

BCAR - Excess Capital Calculation

| | NATL | | | | | | |
|---------------------------------|--------------|--------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| | 2012 | 2013 | Estimated 2014 | Estimated 2015 | Estimated 2016 | Estimated 2017 | Estimated 2018 |
| <u>Net Premiums</u> | | | | | | | |
| <u>Written</u> | | | | | | | |
| NPW | \$ 492,215 | \$ 537,604 | \$ 578,724 | \$ 646,884 | \$ 711,572 | \$ 782,730 | \$ 861,003 |
| Capital Factor | 0.2780 | 0.2760 | 0.2760 | 0.2760 | 0.2760 | 0.2760 | 0.2760 |
| Growth Factor | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 |
| Diversification Factor | 0.8100 | 0.8100 | 0.8100 | 0.8100 | 0.8100 | 0.8100 | 0.8100 |
| BCAR Requirement | 110,837 | 120,187 | 129,380 | 144,617 | 159,079 | 174,987 | 192,486 |
| <u>Reserve Risk</u> | | | | | | | |
| Reserves | \$ 600,960 | \$ 647,511 | \$ 700,080 | \$ 731,380 | \$ 782,586 | \$ 852,989 | \$ 935,453 |
| Deficiency Factor | 1.0050 | 1.0040 | 1.0040 | 1.0040 | 1.0040 | 1.0040 | 1.0040 |
| Discount Factor | 0.9280 | 0.9290 | 0.9290 | 0.9290 | 0.9290 | 0.9290 | 0.9290 |
| Capital Factor | 0.2900 | 0.2870 | 0.2870 | 0.2870 | 0.2870 | 0.2870 | 0.2870 |
| Growth Factor | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 |
| Diversification Factor | 0.8400 | 0.8300 | 0.8300 | 0.8300 | 0.8300 | 0.8300 | 0.8300 |
| BCAR Requirement | 136,533 | 143,865 | 155,545 | 162,500 | 173,877 | 189,519 | 207,841 |
| <u>Investment Risk</u> | | | | | | | |
| Investments | | | | | | | |
| Subject to Charge | \$ 1,054,792 | \$ 1,074,528 | \$ 1,194,177 | \$ 1,286,204 | \$ 1,403,503 | \$ 1,548,517 | \$ 1,725,995 |
| Investment Asset Risk Factor | 0.0405 | 0.0405 | 0.0360 | 0.0360 | 0.0360 | 0.0360 | 0.0360 |
| | 0.0030 | 0.0030 | 0.0030 | 0.0030 | 0.0030 | 0.0030 | 0.0030 |
| Spread of Risk Factor | 1.1850 | 1.1850 | 1.1850 | 1.1850 | 1.1850 | 1.1850 | 1.1850 |
| BCAR Requirement | 50,622 | 51,569 | 50,944 | 54,869 | 59,873 | 66,060 | 73,631 |
| | 12,816 | 13,056 | 12,897 | 13,891 | 15,158 | 16,724 | 18,641 |
| | 29,903 | 30,463 | 30,093 | 32,412 | 35,368 | 39,023 | 43,495 |
| | 7,903 | 8,051 | 7,953 | 8,566 | 9,347 | 10,313 | 11,495 |
| <u>Business Risk</u> | | | | | | | |
| Risk | \$ 927 | \$ 953 | \$ 953 | \$ 953 | \$ 953 | \$ 953 | \$ 953 |
| <u>Credit Risk</u> | | | | | | | |
| Premiums | | | | | | | |
| Receivable | \$ 215,690 | \$ 246,756 | \$ 242,149 | \$ 266,364 | \$ 293,000 | \$ 322,300 | \$ 344,401 |

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| | | | | | | | |
|---|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| Accrued Investment Income | 8,937 | 8,644 | 9,398 | 11,671 | 13,622 | 16,012 | 18,726 |
| Other Assets | 5,866 | 6,067 | 8,681 | 9,703 | 10,674 | 11,741 | 12,915 |
| Reinsurance Recoverable | 174,345 | 169,210 | 209,826 | 219,414 | 234,776 | 255,897 | 280,636 |
| Asset Risk Factor | 0.0540 | 0.0780 | 0.0740 | 0.0740 | 0.0740 | 0.0740 | 0.0740 |
| BCAR Requirement | 21,861 | 33,593 | 34,784 | 37,529 | 40,853 | 44,840 | 48,594 |
| Gross Required Capital (NRC) | 320,780 | 350,167 | 371,606 | 400,469 | 434,636 | 476,359 | 523,505 |
| Less: Covariance Adjustment | 132,048 | 145,002 | 151,372 | 164,059 | 178,643 | 196,211 | 216,120 |
| Net Required Capital (NRC) | 188,732 | 205,165 | 220,234 | 236,410 | 255,993 | 280,149 | 307,385 |
| Adjusted Policyholder Surplus (APHS) | 330,281 | 359,038 | 385,409 | 413,717 | 447,987 | 490,260 | 537,924 |
| BCAR Ratio | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 |
| GAAP Net Income | 34,294 | 17,573 | 49,042 | 59,804 | 67,800 | 76,959 | 87,405 |
| DAC Net of Tax | (418) | 1,444 | (1,997) | (1,252) | (1,707) | (1,878) | (2,065) |
| Other (incl Equity changes) | 2,206 | 4,706 | (2,163) | 0 | 0 | 0 | 0 |
| Amortization of STAT goodwill Net of Tax | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| STAT Net Income | 36,082 | 23,723 | 44,882 | 58,552 | 66,093 | 75,082 | 85,339 |
| BOY STAT Retained Earnings | 293,614 | 339,728 | 354,166 | 396,197 | 446,865 | 504,137 | 571,868 |
| UPR Equity (net of tax) | 22,528 | 1,005 | 3,532 | 2,944 | 2,243 | 3,194 | 4,503 |
| Loss Reserve Equity | 29,713 | 3,442 | 2,598 | 171 | 935 | 2,455 | 3,801 |
| Assets Equity (net of tax) | 19,788 | (3,731) | 1,020 | 0 | 0 | 0 | 0 |
| Potential CAT Loss | (1,997) | 0 | 0 | 0 | 0 | 0 | 0 |
| STAT Net Income (Equity changes) | 36,082 | 23,723 | 44,882 | 58,552 | 66,093 | 75,082 | 85,339 |
| Dividends | (60,000) | (10,000) | (10,000) | (11,000) | (12,000) | (13,000) | (14,000) |
| EOY STAT Retained Earnings | 339,728 | 354,166 | 396,197 | 446,865 | 504,137 | 571,868 | 651,511 |

| | | | | | | | |
|--------------------------------|---------------|----------------|---------------|---------------|---------------|----------------|----------------|
| Excess Capital (A+) | 9,447 | (4,872) | 10,788 | 33,147 | 56,149 | 81,608 | 113,587 |
| Excess Capital (A) | 37,757 | 25,903 | 43,823 | 68,609 | 94,548 | 123,630 | 159,695 |

NATL Projections

Annex B

Projected Profit and Loss Statements

National Interstate Corporation

GAAP Basis Income Statements (000 s)

| | 2012 | Estimated 2013 | Estimated 2014 | Estimated 2015 | Estimated 2016 | Estimated 2017 | Estimated 2018 | 5 Yr Combined |
|--|------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|------------------|
| Gross Premiums Written organic | \$ 573,470 | \$ 636,968 | \$ 702,193 | \$ 792,425 | \$ 895,678 | \$ 1,003,159 | \$ 1,123,538 | \$ 5,153,960 |
| Gross Premiums Written M&A | | | | | | | | |
| Total gross premiums written | 573,470 | 636,968 | 702,193 | 792,425 | 895,678 | 1,003,159 | 1,123,538 | 5,153,960 |
| Net Premiums Written | \$ 492,215 | \$ 539,435 | \$ 587,181 | \$ 673,561 | \$ 761,326 | \$ 852,685 | \$ 955,007 | \$ 4,369,196 |
| Net Premiums Earned | \$ 458,049 | \$ 523,615 | \$ 563,308 | \$ 630,371 | \$ 717,444 | \$ 807,006 | \$ 903,846 | \$ 4,145,590 |
| Net Investment Income | 34,927 | 32,787 | 36,145 | 52,905 | 63,314 | 74,598 | 86,205 | 345,954 |
| Realized G/L | 6,219 | 6,808 | 5,738 | 6,190 | 6,737 | 7,481 | 8,402 | 41,357 |
| Other Income | 3,278 | 3,262 | 2,547 | 3,962 | 4,478 | 5,016 | 5,618 | 24,883 |
| Total Revenues | 502,473 | 566,472 | 607,738 | 693,428 | 791,973 | 894,100 | 1,004,072 | 4,557,783 |
| Losses and loss adjustment expenses | 341,008 | 424,927 | 411,215 | 453,867 | 516,559 | 581,044 | 650,769 | 3,038,382 |
| Commissions | 38,419 | 37,673 | 39,869 | 47,149 | 53,293 | 59,688 | 66,851 | 304,523 |
| Premium taxes | 12,677 | 13,632 | 15,312 | 17,280 | 19,531 | 21,875 | 24,500 | 112,130 |
| Assessments | 4,279 | 5,176 | 5,465 | 6,167 | 6,971 | 7,807 | 8,744 | 40,329 |
| Other operating and general expenses | 54,336 | 55,523 | 62,660 | 68,583 | 79,077 | 89,000 | 99,680 | 454,523 |
| Change in DPAC | (644) | 1,222 | (2,802) | (2,839) | (3,730) | (3,883) | (4,349) | (16,381) |
| Total Expenses | 450,075 | 538,153 | 531,718 | 590,207 | 671,701 | 755,531 | 846,195 | 3,933,505 |
| Interest expense debt | 616 | 538 | 560 | 324 | 354 | 384 | 414 | 2,574 |
| Interest on funds held | 3,953 | 4,880 | 4,886 | 7,151 | 8,559 | 10,084 | 11,653 | 47,213 |

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| | | | | | | | | |
|-------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|------------|
| Total interest expense | 4,569 | 5,418 | 5,446 | 7,475 | 8,913 | 10,468 | 12,067 | 49,787 |
| Income before income taxes | 47,829 | 22,902 | 70,574 | 95,745 | 111,360 | 128,101 | 145,810 | 574,492 |
| Provision for income taxes | 13,535 | 4,924 | 21,172 | 30,160 | 35,078 | 40,352 | 45,930 | 177,616 |
| Net income | \$ 34,294 | \$ 17,978 | \$ 49,401 | \$ 65,585 | \$ 76,281 | \$ 87,749 | \$ 99,880 | \$ 396,875 |
| Loss and LAE Ratio (% of NEP) | 74.4% | 81.2% | 73.0% | 72.0% | 72.0% | 72.0% | 72.0% | 73.3% |
| Expense Ratio (% of NEP) | 23.1% | 21.0% | 20.9% | 21.0% | 21.0% | 21.0% | 21.0% | 21.0% |
| Combined Ratio | 97.5% | 102.2% | 93.9% | 93.0% | 93.0% | 93.0% | 93.0% | 94.3% |

NATL Projections**Projected Balance Sheets****GAAP Basis Balance Sheets (000 s)**

| | 2012 | Estimated 2013 | Estimated 2014 | Estimated 2015 | Estimated 2016 | Estimated 2017 | Estimated 2018 |
|--|---------------------|---------------------------|---------------------------|---------------------------|---------------------------|---------------------------|---------------------------|
| Assets | | | | | | | |
| Investments | \$ 1,054,792 | \$ 1,118,194 | \$ 1,206,288 | \$ 1,312,929 | \$ 1,457,876 | \$ 1,637,412 | \$ 1,845,588 |
| Accrued Investment Premium Receivable | 8,937 | 10,164 | 11,205 | 16,400 | 19,627 | 23,125 | 26,724 |
| Reinsurance Recoverable | 215,690 | 222,939 | 245,768 | 277,349 | 313,487 | 351,106 | 393,238 |
| Prepaid reinsurance premiums | 174,345 | 199,284 | 211,215 | 222,836 | 242,536 | 269,511 | 301,160 |
| DPAC | 32,570 | 42,292 | 45,873 | 52,351 | 58,934 | 65,786 | 73,460 |
| Deferred taxes | 25,246 | 24,024 | 26,826 | 29,666 | 33,396 | 37,279 | 41,627 |
| Fixed Assets | 19,883 | 28,638 | 30,527 | 32,866 | 36,097 | 40,161 | 44,869 |
| Intangible assets | 24,539 | 31,848 | 35,110 | 39,621 | 44,784 | 50,158 | 56,177 |
| Other Assets | 8,355 | 8,073 | 7,791 | 7,509 | 7,227 | 6,945 | 6,663 |
| | 5,866 | 8,092 | 8,808 | 10,103 | 11,420 | 12,790 | 14,325 |
| Total Assets | \$ 1,570,224 | \$ 1,693,549 | \$ 1,829,411 | \$ 2,001,631 | \$ 2,225,385 | \$ 2,494,273 | \$ 2,803,831 |
| Liabilities | | | | | | | |
| Unearned Premiums | \$ 266,126 | \$ 281,946 | \$ 305,819 | \$ 349,009 | \$ 392,892 | \$ 438,571 | \$ 489,732 |
| Gross Reserves | 775,305 | 863,566 | 915,266 | 965,622 | 1,050,990 | 1,167,883 | 1,305,025 |
| Long-term debt Amounts withheld | 12,000 | 12,000 | 12,000 | 12,000 | 12,000 | 12,000 | 12,000 |
| Reinsurance balances payable | 67,002 | 74,420 | 82,041 | 92,583 | 104,647 | 117,204 | 131,269 |
| Accounts payable and other liabilities | 19,473 | 22,920 | 27,028 | 27,933 | 31,573 | 35,361 | 39,605 |
| Commission payable and assessments | 59,058 | 65,597 | 72,314 | 81,606 | 92,239 | 103,308 | 115,705 |
| | 17,316 | 19,109 | 21,066 | 23,773 | 26,870 | 30,095 | 33,706 |
| Total Liabilities | \$ 1,216,279 | \$ 1,339,558 | \$ 1,435,533 | \$ 1,552,527 | \$ 1,711,211 | \$ 1,904,423 | \$ 2,127,043 |
| Equity | | | | | | | |
| Total Capital | \$ 81,328 | \$ 74,237 | \$ 74,237 | \$ 74,237 | \$ 74,237 | \$ 74,237 | \$ 74,237 |
| | 272,618 | 279,754 | 319,641 | 374,868 | 439,937 | 515,614 | 602,552 |

Retained
Earnings

| | | | | | | | |
|---------------------|------------|------------|------------|------------|------------|------------|------------|
| Total Equity | \$ 353,946 | \$ 353,990 | \$ 393,878 | \$ 449,104 | \$ 514,174 | \$ 589,850 | \$ 676,789 |
|---------------------|------------|------------|------------|------------|------------|------------|------------|

| | | | | | | | |
|---|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Total Liabilities and Equity | \$ 1,570,224 | \$ 1,693,549 | \$ 1,829,411 | \$ 2,001,631 | \$ 2,225,385 | \$ 2,494,273 | \$ 2,803,831 |
|---|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|---------------------|

NATL Projections**Projected Required Capital****BCAR Model**

| | 2012 | 2013 | Estimated 2014 | Estimated 2015 | Estimated 2016 | Estimated 2017 | Estimated 2018 |
|---------------------------------|--------------|--------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Net Premiums | | | | | | | |
| Written | | | | | | | |
| NPW | \$ 492,215 | \$ 539,435 | \$ 587,181 | \$ 673,561 | \$ 761,326 | \$ 852,685 | \$ 955,007 |
| Capital Factor | 0.2780 | 0.2780 | 0.2780 | 0.2780 | 0.2780 | 0.2780 | 0.2780 |
| Growth Factor | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 |
| Diversification Factor | 0.8100 | 0.8100 | 0.8100 | 0.8100 | 0.8100 | 0.8100 | 0.8100 |
| BCAR Requirement | 110,837 | 121,470 | 132,221 | 151,672 | 171,435 | 192,008 | 215,049 |
| Reserve Risk | | | | | | | |
| Reserves | \$ 600,960 | \$ 664,282 | \$ 704,051 | \$ 742,786 | \$ 808,454 | \$ 898,371 | \$ 1,003,866 |
| Deficiency Factor | 1.0050 | 1.0050 | 1.0050 | 1.0050 | 1.0050 | 1.0050 | 1.0050 |
| Discount Factor | 0.9280 | 0.9280 | 0.9280 | 0.9280 | 0.9280 | 0.9280 | 0.9280 |
| Capital Factor | 0.2900 | 0.2880 | 0.2880 | 0.2880 | 0.2880 | 0.2880 | 0.2880 |
| Growth Factor | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 | 1.0000 |
| Diversification Factor | 0.8400 | 0.8300 | 0.8300 | 0.8300 | 0.8300 | 0.8300 | 0.8300 |
| BCAR Requirement | 136,533 | 148,094 | 156,960 | 165,596 | 180,235 | 200,281 | 223,800 |
| Investment Risk | | | | | | | |
| Investments | | | | | | | |
| Subject to Charge | \$ 1,054,792 | \$ 1,118,194 | \$ 1,206,288 | \$ 1,312,929 | \$ 1,457,876 | \$ 1,637,412 | \$ 1,845,588 |
| Investment Asset Risk Factor | 0.0405 | 0.0400 | 0.0405 | 0.0405 | 0.0405 | 0.0405 | 0.0405 |
| Spread of Risk Factor | 1.1850 | 1.1850 | 1.1850 | 1.1850 | 1.1850 | 1.1850 | 1.1850 |
| BCAR Requirement | 50,622 | 53,002 | 57,893 | 63,011 | 69,967 | 78,583 | 88,574 |
| | 12,816 | 13,418 | 14,656 | 15,952 | 17,713 | 19,895 | 22,424 |
| | 29,903 | 31,309 | 34,198 | 37,222 | 41,331 | 46,421 | 52,322 |
| | 7,903 | 8,275 | 9,038 | 9,837 | 10,923 | 12,268 | 13,828 |
| Credit Risk | | | | | | | |
| Premiums | | | | | | | |
| Receivable | \$ 215,690 | \$ 222,939 | \$ 245,768 | \$ 277,349 | \$ 313,487 | \$ 351,106 | \$ 393,238 |
| Accrued Investment | 8,937 | 10,164 | 11,205 | 16,400 | 19,627 | 23,125 | 26,724 |

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| | | | | | | | |
|---|----------------|----------------|----------------|----------------|----------------|----------------|----------------|
| Income | | | | | | | |
| Other Assets | 5,866 | 8,092 | 8,808 | 10,103 | 11,420 | 12,790 | 14,325 |
| Reinsurance | | | | | | | |
| Recoverable | 174,345 | 199,284 | 211,215 | 222,836 | 242,536 | 269,511 | 301,160 |
| Asset Risk Factor | 0.0540 | 0.0540 | 0.0540 | 0.0540 | 0.0540 | 0.0540 | 0.0540 |
| BCAR | | | | | | | |
| Requirement | 21,861 | 23,786 | 25,758 | 28,441 | 31,702 | 35,453 | 39,714 |
| Business Risk | 927 | 927 | 927 | 927 | 927 | 927 | 927 |
| Gross Required Capital (NRC) | | | | | | | |
| | 320,780 | 347,279 | 373,759 | 409,647 | 454,267 | 507,252 | 568,064 |
| Less: Covariance Adjustment | | | | | | | |
| | 132,048 | 142,095 | 153,835 | 169,393 | 188,326 | 210,674 | 236,319 |
| Net Required Capital (NRC) | 188,732 | 205,184 | 219,924 | 240,254 | 265,941 | 296,578 | 331,745 |
| Adjusted Policyholder Surplus (APHS) | | | | | | | |
| | 330,281 | 359,072 | 384,867 | 420,444 | 465,397 | 519,012 | 580,554 |
| BCAR Ratio | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 | 1.75 |
| GAAP Net | | | | | | | |
| Income | 34,294 | 17,978 | 49,401 | 65,585 | 76,281 | 87,749 | 99,880 |
| DAC Net of Tax | (418) | 794 | (1,821) | (1,846) | (2,425) | (2,524) | (2,827) |
| Other (incl Equity changes) | 2,206 | 848 | (3,800) | 0 | 0 | 0 | 0 |
| Amortization of STAT goodwill Net of Tax | | | | | | | |
| | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| STAT Net Income | 36,082 | 19,620 | 43,780 | 63,740 | 73,857 | 85,225 | 97,053 |
| BOY STAT | | | | | | | |
| Retained Earnings | 293,614 | 339,728 | 352,697 | 386,052 | 442,931 | 511,638 | 592,029 |
| UPR Equity (net of tax) | 22,528 | 1,053 | 803 | 4,064 | 4,820 | 5,017 | 5,619 |
| Loss Reserve | | | | | | | |
| Equity | 29,713 | 3,712 | (228) | 1,076 | 3,030 | 4,149 | 4,868 |
| Assets Equity (net of tax) | 19,788 | (1,416) | 0 | 0 | 0 | 0 | 0 |
| Potential CAT | | | | | | | |
| Losses | (1,997) | 0 | 0 | 0 | 0 | 0 | 0 |
| STAT Net Income (Equity changes) | 36,082 | 19,620 | 43,780 | 63,740 | 73,857 | 85,225 | 97,053 |
| Dividends | (60,000) | (10,000) | (11,000) | (12,000) | (13,000) | (14,000) | (15,000) |
| EOY STAT | | | | | | | |
| Retained Earnings | 339,728 | 352,697 | 386,052 | 442,931 | 511,638 | 592,029 | 684,569 |

| | | | | | | | |
|-------------------------------|---------------|----------------|---------------|---------------|---------------|----------------|----------------|
| Excess (Deficient) | | | | | | | |
| Capital A+ Level | 9,447 | (6,375) | 1,185 | 22,487 | 46,241 | 73,017 | 104,015 |
| Excess (Deficient) | | | | | | | |
| Capital A Level | 37,757 | 24,402 | 34,174 | 58,525 | 86,132 | 117,504 | 153,777 |
| LTIP | | 9,013 | 17,679 | 40,506 | 66,186 | 95,260 | 128,896 |