

UNITED FIRE GROUP INC  
Form 10-Q  
May 08, 2013  
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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 March 31, 2013

Commission File Number 001-34257

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UNITED FIRE GROUP, INC.  
(Exact name of registrant as specified in its charter)

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Iowa  
(State of Incorporation)

45-2302834  
(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):

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Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐ Smaller reporting company ☐

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

As of May 6, 2013, 25,281,042 shares of common stock were outstanding.

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Exhibit 31.1

Exhibit 31.2

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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.”

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## PART I — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

United Fire Group, Inc.

Consolidated Balance Sheets

(In Thousands, Except Share Data)

|  | March 31,<br>2013<br>(unaudited) | December 31,<br>2012 |
|--|----------------------------------|----------------------|
| <b>ASSETS</b>  |                                  |                      |
| Investments  |                                  |                      |
| Fixed maturities   |                                  |                      |
| Held-to-maturity, at amortized cost (fair value \$1,668 in 2013 and \$1,681 in 2012)   | \$1,638                          | \$1,655              |
| Available-for-sale, at fair value (amortized cost \$2,666,902 in 2013 and \$2,657,800 in 2012)   | 2,807,582                        | 2,808,078            |
| Trading securities, at fair value (amortized cost \$12,470 in 2013 and \$12,645 in 2012)   | 13,738                           | 13,353               |
| Equity securities  |                                  |                      |
| Available-for-sale, at fair value (cost \$67,464 in 2013 and \$66,892 in 2012)   | 195,677                          | 177,127              |
| Trading securities, at fair value (cost \$1,772 in 2013 and \$1,772 in 2012)   | 2,131                            | 2,018                |
| Mortgage loans   | 4,581                            | 4,633                |
| Policy loans   | 6,566                            | 6,671                |
| Other long-term investments  | 30,646                           | 30,028               |
| Short-term investments   | 800                              | 800                  |
|  | 3,063,359                        | 3,044,363            |
| Cash and cash equivalents  | 101,948                          | 107,466              |
| Accrued investment income  | 30,079                           | 30,375               |
| Premiums receivable (net of allowance for doubtful accounts of \$888 in 2013 and \$866 in 2012)  | 207,920                          | 188,289              |
| Deferred policy acquisition costs  | 113,088                          | 105,300              |
| Property and equipment (primarily land and buildings, at cost, less accumulated depreciation of \$34,060 in 2013 and \$34,093 in 2012) | 42,328                           | 43,090               |
| Reinsurance receivables and recoverables   | 120,140                          | 114,399              |
| Prepaid reinsurance premiums   | 3,218                            | 2,963                |
| Income taxes receivable  | 2,386                            | 16,536               |
| Goodwill and intangible assets   | 27,624                           | 28,259               |
| Other assets   | 12,600                           | 13,613               |
| <b>TOTAL ASSETS</b>  | <b>\$3,724,690</b>               | <b>\$3,694,653</b>   |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                                  |                      |
| Liabilities  |                                  |                      |
| Future policy benefits and losses, claims and loss settlement expenses   |                                  |                      |
| Property and casualty insurance  | \$971,239                        | \$971,911            |
| Life insurance   | 1,484,362                        | 1,498,176            |
| Unearned premiums  | 326,320                          | 311,650              |
| Accrued expenses and other liabilities   | 157,801                          | 164,111              |
| Deferred income taxes  | 26,826                           | 19,628               |
| <b>TOTAL LIABILITIES</b>   | <b>\$2,966,548</b>               | <b>\$2,965,476</b>   |
| Stockholders' Equity   |                                  |                      |
|  | \$25                             | \$25                 |

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Common stock, \$0.001 par value; authorized 75,000,000 shares; 25,266,295 and 25,227,463 shares issued and outstanding in 2013 and 2012, respectively

|  |             |             |
|--|-------------|-------------|
| Additional paid-in capital                         | 209,472     | 208,536     |
| Retained earnings                                  | 444,035     | 425,428     |
| Accumulated other comprehensive income, net of tax | 104,610     | 95,188      |
| TOTAL STOCKHOLDERS' EQUITY                         | \$758,142   | \$729,177   |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY         | \$3,724,690 | \$3,694,653 |

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

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United Fire Group, Inc.

Consolidated Statements of Income and Comprehensive Income (Unaudited)

| (In Thousands, Except Share Data)  | Three Months Ended March 31, |            |
|--|------------------------------|------------|
|  | 2013                         | 2012       |
| Revenues   |                              |            |
| Net premiums earned  | \$176,817                    | \$161,503  |
| Investment income, net of investment expenses  | 26,464                       | 29,146     |
| Net realized investment gains  |                              |            |
| Other-than-temporary impairment charges  | —                            | —          |
| All other net realized gains (includes reclassifications for net unrealized gains on available-for-sale securities of \$1,909 in 2013; and \$2,794 in 2012; previously included in accumulated other comprehensive income) | 1,909                        | 2,794      |
| Total net realized investment gains  | 1,909                        | 2,794      |
| Other income   | 115                          | 256        |
| Total revenues   | \$205,305                    | \$193,699  |
| Benefits, Losses and Expenses  |                              |            |
| Losses and loss settlement expenses  | \$97,470                     | \$91,484   |
| Future policy benefits   | 8,236                        | 10,138     |
| Amortization of deferred policy acquisition costs  | 38,081                       | 34,551     |
| Other underwriting expenses (includes reclassifications for employee benefit costs of \$1,242 in 2013; and \$643 in 2012; previously included in accumulated other comprehensive income)                                   | 22,348                       | 21,994     |
| Interest on policyholders' accounts  | 9,320                        | 10,656     |
| Total benefits, losses and expenses  | \$175,455                    | \$168,823  |
| Income before income taxes   | \$29,850                     | \$24,876   |
| Federal income tax expense (includes reclassifications of \$234 in 2013; and \$752 in 2012; previously included in accumulated other comprehensive income)   | 7,457                        | 5,692      |
| Net income   | \$22,393                     | \$19,184   |
| Other comprehensive income   |                              |            |
| Change in net unrealized appreciation on investments   | \$15,161                     | \$13,603   |
| Change in liability for underfunded employee benefit plans   | —                            | —          |
| Other comprehensive income, before tax and reclassification adjustments  | \$15,161                     | \$13,603   |
| Income tax effect  | (5,306)                      | (4,761)    |
| Other comprehensive income, after tax, before reclassification adjustments   | \$9,855                      | \$8,842    |
| Reclassification adjustment for net realized gains included in income  | \$(1,909)                    | \$(2,794)  |
| Reclassification adjustment for employee benefit costs included in expense   | 1,242                        | 643        |
| Total reclassification adjustments, before tax   | \$(667)                      | \$(2,151)  |
| Income tax effect  | 234                          | 752        |
| Total reclassification adjustments, after tax  | \$(433)                      | \$(1,399)  |
| Comprehensive income   | \$31,815                     | \$26,627   |
| Weighted average common shares outstanding   | 25,245,497                   | 25,505,962 |
| Basic earnings per common share  | \$0.89                       | \$0.75     |
| Diluted earnings per common share  | 0.88                         | 0.75       |
| Cash dividends declared per common share   | 0.15                         | 0.15       |
| The Notes to Unaudited Consolidated Financial Statements are an integral part of these statements.   |                              |            |



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Consolidated Statement of Stockholders' Equity (Unaudited)

| (In Thousands, Except Per Share Data)  | Three Months Ended<br>March 31, 2013 |
|--|--------------------------------------|
| Common stock   |                                      |
| Balance, beginning of year   | \$25                                 |
| Shares issued for stock-based awards (38,832 shares)   | —                                    |
| Balance, end of period   | \$25                                 |
| Additional paid-in capital   |                                      |
| Balance, beginning of year   | \$208,536                            |
| Compensation expense and related tax benefit for stock-based award grants                              | 333                                  |
| Shares issued for stock-based awards   | 603                                  |
| Balance, end of period   | \$209,472                            |
| Retained earnings  |                                      |
| Balance, beginning of year   | \$425,428                            |
| Net income   | 22,393                               |
| Dividends on common stock (\$0.15 per share)   | (3,786)                              |
| Balance, end of period   | \$444,035                            |
| Accumulated other comprehensive income, net of tax   |                                      |
| Balance, beginning of year   | \$95,188                             |
| Change in net unrealized investment appreciation <sup>(1)</sup>  | 8,614                                |
| Change in liability for underfunded employee benefit plans <sup>(2)</sup>                              | 808                                  |
| Balance, end of period   | \$104,610                            |
| Summary of changes   |                                      |
| Balance, beginning of year   | \$729,177                            |
| Net income   | 22,393                               |
| All other changes in stockholders' equity accounts   | 6,572                                |
| Balance, end of period   | \$758,142                            |
| (1) The change in net unrealized appreciation is net of reclassification adjustments and income taxes. |                                      |
| (2) The change in liability for underfunded employee benefit plans is net of income taxes.             |                                      |

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

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## United Fire Group, Inc.

## Consolidated Statements of Cash Flows (Unaudited)

| (In Thousands)   |  | Three Months Ended March 31, |             |
|--|--|------------------------------|-------------|
|  |  | 2013                         | 2012        |
| Cash Flows From Operating Activities   |  |                              |             |
| Net income   |  | \$22,393                     | \$19,184    |
| Adjustments to reconcile net income to net cash provided by operating activities |  |                              |             |
| Net accretion of bond premium  |  | 3,981                        | 3,520       |
| Depreciation and amortization  |  | 1,785                        | 2,285       |
| Stock-based compensation expense   |  | 411                          | 396         |
| Net realized investment gains  |  | (1,909)                      | (2,794)     |
| Net cash flows from trading investments  |  | 46                           | (1,343)     |
| Deferred income tax expense  |  | 460                          | 5,011       |
| Changes in:  |  |                              |             |
| Accrued investment income  |  | 296                          | (344)       |
| Premiums receivable  |  | (19,631)                     | (14,560)    |
| Deferred policy acquisition costs  |  | (2,917)                      | 1,526       |
| Reinsurance receivables  |  | (5,741)                      | (23,199)    |
| Prepaid reinsurance premiums   |  | (255)                        | 2,650       |
| Income taxes receivable  |  | 14,150                       | 3,926       |
| Other assets   |  | 1,013                        | 2,691       |
| Future policy benefits and losses, claims and loss settlement expenses           |  | 6,364                        | 20,596      |
| Unearned premiums  |  | 14,670                       | 15,228      |
| Accrued expenses and other liabilities   |  | (5,068)                      | 5,721       |
| Deferred income taxes  |  | 1,665                        | (3,409)     |
| Other, net   |  | 31                           | (1,200)     |
| Total adjustments  |  | \$9,351                      | \$16,701    |
| Net cash provided by operating activities  |  | \$31,744                     | \$35,885    |
| Cash Flows From Investing Activities   |  |                              |             |
| Proceeds from sale of available-for-sale investments                             |  | \$2,810                      | \$3,000     |
| Proceeds from call and maturity of held-to-maturity investments                  |  | 19                           | 75          |
| Proceeds from call and maturity of available-for-sale investments                |  | 127,514                      | 149,285     |
| Proceeds from short-term and other investments                                   |  | 407                          | 2,590       |
| Purchase of available-for-sale investments                                       |  | (142,615)                    | (252,345)   |
| Purchase of short-term and other investments                                     |  | (900)                        | (2,950)     |
| Net purchases and sales of property and equipment                                |  | (386)                        | (893)       |
| Net cash used in investing activities  |  | \$(13,151)                   | \$(101,238) |
| Cash Flows From Financing Activities   |  |                              |             |
| Policyholders' account balances  |  |                              |             |
| Deposits to investment and universal life contracts                              |  | \$25,369                     | \$40,390    |
| Withdrawals from investment and universal life contracts                         |  | (46,219)                     | (33,743)    |
| Repayment of trust preferred securities  |  | —                            | (8,047)     |
| Payment of cash dividends  |  | (3,786)                      | (3,826)     |
| Issuance of common stock   |  | 603                          | 43          |
| Tax impact from issuance of common stock   |  | (78)                         | 9           |
| Net cash used in financing activities  |  | \$(24,111)                   | \$(5,174)   |
| Net Change in Cash and Cash Equivalents  |  | \$(5,518)                    | \$(70,527)  |
| Cash and Cash Equivalents at Beginning of Period                                 |  | 107,466                      | 144,527     |

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|  |            |           |
|--|------------|-----------|
| Cash and Cash Equivalents at End of Period | \$ 101,948 | \$ 74,000 |
|--|------------|-----------|

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

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UNITED FIRE GROUP, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Amounts in thousands, unless otherwise noted)

NOTE 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of Business

United Fire Group, Inc. ("United Fire", "Registrant", the "Company", "we", "us", or "our") and its consolidated subsidiaries and affiliates 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 36 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; reinsurance receivables and recoverables (for net realizable value); future policy benefits and losses, claims and loss settlement expenses; and pension and postretirement benefit obligations.

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.

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, 2012. The review report of Ernst & Young LLP as of and for the three-month period ended March 31, 2013, accompanies the unaudited Consolidated Financial Statements included in Part I, Item 1 "Financial Statements."

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.

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For the three-month periods ended March 31, 2013 and 2012, we made payments for income taxes totaling \$5 and \$151, respectively. We received a tax refund of \$8,744 during the three months ended March 31, 2013. We received no tax refunds during the three months ended March 31, 2012.

For the three-month period ended March 31, 2013, we made no interest payments. For the three-month period ended March 31, 2012, we made interest payments totaling \$492. These payments exclude interest credited to policyholders' accounts.

**Deferred Policy Acquisition Costs ("DAC")**

Certain costs associated with underwriting new business (primarily commissions, premium taxes and variable underwriting and policy issue expenses associated with successful acquisition efforts) are deferred. The following table is a summary of the components of DAC, including the related amortization recognized for the three-month period ended March 31, 2013.

|  | Property & Casualty | Life Insurance | Total     |
|--|---------------------|----------------|-----------|
| Recorded asset at beginning of period                | \$64,947            | \$40,353       | \$105,300 |
| Underwriting costs deferred                          | 39,835              | 1,163          | 40,998    |
| Amortization of deferred policy acquisition costs    | (36,355 )           | (1,726 )       | (38,081 ) |
| Ending unamortized deferred policy acquisition costs | \$68,427            | \$39,790       | \$108,217 |
| Change in "shadow" deferred policy acquisition costs | —                   | 4,871          | 4,871     |
| Recorded asset at end of period                      | \$68,427            | \$44,661       | \$113,088 |

Property and casualty policy acquisition costs are deferred and amortized as premium revenue is recognized. The accounting method we follow in computing DAC limits the amount of such deferred costs to their estimated realizable value. This takes into account the premium to be earned, losses and loss settlement expenses to be incurred and certain other costs expected to be incurred as the premium is earned.

For traditional life insurance policies, DAC is amortized to income over the premium-paying period in proportion to the ratio of the expected annual premium revenue to the expected total premium revenue. For non-traditional policies, DAC is amortized over the anticipated terms in proportion to the ratio of the expected annual gross profits to the total expected gross profits. Expected premium revenue and gross profits are based on the same mortality and withdrawal assumptions used in determining future policy benefits. For non-traditional policies, changes in the amount or timing of expected gross profits result in adjustments to the cumulative amortization of these costs. The effect on amortization of DAC for revisions to estimated gross profits is reported in earnings in the period the estimated gross profits are revised.

The effect on DAC that results from the assumed realization of unrealized gains (losses) on investments allocated to non-traditional life insurance business is recognized with an offset, or "shadow" DAC, to net unrealized investment appreciation as of the balance sheet date. The "shadow" DAC adjustment decreased the DAC asset by \$33,824 and \$38,695 at March 31, 2013 and December 31, 2012, respectively.

**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.



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We reported a federal income tax expense of \$7,457 and \$5,692 for the three-month periods ended March 31, 2013 and 2012, 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 did not recognize any liability for unrecognized tax benefits at March 31, 2013 or December 31, 2012. 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 2009. The Internal Revenue Service is conducting an examination of our income tax return for the 2011 tax year.

Recently Issued Accounting Standards

Adopted Accounting Standards

### Comprehensive Income

In February 2013, the Financial Accounting Standards Board ("FASB") issued guidance (Accounting Standards Update ("ASU") 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income). The new guidance requires significant items that are reclassified out of accumulated other comprehensive income ("AOCI") to net income in their entirety in the same reporting period, to be reported to show the effect of the reclassifications on the respective line items of the statement where net income is presented. These reclassifications can be presented either on the face of the statement where net income is presented or in the notes to the financial statements. For items that are not reclassified to net income in their entirety in the same reporting period a cross reference to other disclosures currently required under GAAP is required in the notes to the financial statements. The new guidance also requires companies to report changes in the accumulated balances of each component of AOCI. This new guidance is effective for annual and interim periods beginning after December 15, 2012. The Company adopted the new guidance effective January 1, 2013. The adoption of the new guidance affects presentation only and therefore had no impact on the Company's results of operations or financial position.

Adopted Accounting Standards in 2012

### Comprehensive Income

In June and December 2011, the FASB issued guidance (ASU 2011-05, Presentation of Comprehensive Income and ASU 2011-12, Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05) amending the presentation of comprehensive income and its components. Under the new guidance, a reporting entity has the option to present comprehensive income in a single continuous statement or in two separate but consecutive statements. This new guidance is to be applied retrospectively. The Company adopted the new guidance in the first quarter of 2012 by electing to report comprehensive income in a single continuous statement as shown in the accompanying Consolidated Statements of Income and Comprehensive Income. The adoption of the new guidance affects presentation only and therefore had no impact on the Company's results of operations or financial position.

### Fair Value Measurements

In May 2011, the FASB issued updated accounting guidance (ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards ("IFRS")) that changed 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 IFRS. The guidance also requires additional disclosures for fair value measurements that are estimated using significant unobservable (i.e., Level 3) inputs. The Company adopted the updated guidance on a prospective basis effective



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January 1, 2012, and has provided the additional disclosures required in "Note 3 Fair Value of Financial Instruments". The adoption of the new guidance did not have any impact on the Company's financial position or results of operations.

**Indefinite-Lived Intangible Assets**

In July 2012, the FASB issued guidance (ASU 2012-02, Intangibles - Goodwill and Other) for the testing of indefinite-lived intangible assets for impairment. The new guidance provides an option to perform a qualitative approach to test indefinite-lived intangible assets for impairment. If an entity concludes that it is more likely than not that the indefinite-lived intangible asset is impaired, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test by comparing the fair value with the carrying amount. However, if an entity concludes otherwise, then the entity is not required to take further action. This new guidance is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012, and early adoption is permitted. The Company early adopted the updated guidance for purposes of the impairment test performed for 2012. The adoption of the new guidance did not have any impact on the Company's financial position or results of operations.

**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 March 31, 2013 and December 31, 2012, is as follows:

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March 31, 2013

| Type of Investment                                | Cost or<br>Amortized<br>Cost | Gross<br>Unrealized<br>Appreciation | Gross<br>Unrealized<br>Depreciation | Fair Value   |
|---|------------------------------|-------------------------------------|-------------------------------------|--------------|
| <b>HELD-TO-MATURITY</b>                           |                              |                                     |                                     |              |
| Fixed maturities                                  |                              |                                     |                                     |              |
| Bonds   |                              |                                     |                                     |              |
| States, municipalities and political subdivisions | \$ 1,187                     | \$ 18                               | \$ —                                | \$ 1,205     |
| Corporate bonds - financial services              | 200                          | —                                   | —                                   | 200          |
| Mortgage-backed securities                        | 242                          | 12                                  | —                                   | 254          |
| Collateralized mortgage obligations               | 9                            | —                                   | —                                   | 9            |
| Total Held-to-Maturity Fixed Maturities           | \$ 1,638                     | \$ 30                               | \$ —                                | \$ 1,668     |
| <b>AVAILABLE-FOR-SALE</b>                         |                              |                                     |                                     |              |
| Fixed maturities                                  |                              |                                     |                                     |              |
| Bonds   |                              |                                     |                                     |              |
| U.S. Treasury                                     | \$ 36,845                    | \$ 845                              | \$ 4                                | \$ 37,686    |
| U.S. government agency                            | 84,527                       | 440                                 | 243                                 | 84,724       |
| States, municipalities and political subdivisions | 731,004                      | 52,291                              | 1,662                               | 781,633      |
| Foreign bonds                                     | 200,286                      | 11,035                              | 31                                  | 211,290      |
| Public utilities                                  | 231,379                      | 14,804                              | 7                                   | 246,176      |
| Corporate bonds                                   |                              |                                     |                                     |              |
| Energy  | 167,556                      | 8,717                               | —                                   | 176,273      |
| Industrials                                       | 260,157                      | 13,345                              | 101                                 | 273,401      |
| Consumer goods and services                       | 190,279                      | 9,015                               | 99                                  | 199,195      |
| Health care                                       | 106,528                      | 6,151                               | 133                                 | 112,546      |
| Technology, media and telecommunications          | 122,922                      | 5,792                               | 701                                 | 128,013      |
| Financial services                                | 252,334                      | 14,759                              | 377                                 | 266,716      |
| Mortgage-backed securities                        | 24,808                       | 756                                 | 26                                  | 25,538       |
| Collateralized mortgage obligations               | 253,855                      | 7,130                               | 1,450                               | 259,535      |
| Asset-backed securities                           | 4,044                        | 430                                 | —                                   | 4,474        |
| Redeemable preferred stocks                       | 378                          | 4                                   | —                                   | 382          |
| Total Available-for-Sale Fixed Maturities         | \$ 2,666,902                 | \$ 145,514                          | \$ 4,834                            | \$ 2,807,582 |
| Equity securities                                 |                              |                                     |                                     |              |
| Common stocks                                     |                              |                                     |                                     |              |
| Public utilities                                  | \$ 7,231                     | \$ 9,119                            | \$ 49                               | \$ 16,301    |
| Energy  | 5,094                        | 7,552                               | —                                   | 12,646       |
| Industrials                                       | 13,015                       | 22,253                              | 124                                 | 35,144       |
| Consumer goods and services                       | 10,394                       | 11,509                              | 42                                  | 21,861       |
| Health care                                       | 7,920                        | 13,045                              | 25                                  | 20,940       |
| Technology, media and telecommunications          | 6,204                        | 6,255                               | 80                                  | 12,379       |
| Financial services                                | 15,681                       | 58,902                              | 103                                 | 74,480       |
| Nonredeemable preferred stocks                    | 1,925                        | 21                                  | 20                                  | 1,926        |
| Total Available-for-Sale Equity Securities        | \$ 67,464                    | \$ 128,656                          | \$ 443                              | \$ 195,677   |
| Total Available-for-Sale Securities               | \$ 2,734,366                 | \$ 274,170                          | \$ 5,277                            | \$ 3,003,259 |



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December 31, 2012

| Type of Investment                                | Cost or<br>Amortized<br>Cost | Gross<br>Unrealized<br>Appreciation | Gross<br>Unrealized<br>Depreciation | Fair Value  |
|---|------------------------------|-------------------------------------|-------------------------------------|-------------|
| <b>HELD-TO-MATURITY</b>                           |                              |                                     |                                     |             |
| Fixed maturities                                  |                              |                                     |                                     |             |
| Bonds   |                              |                                     |                                     |             |
| States, municipalities and political subdivisions | \$1,185                      | \$11                                | \$—                                 | \$1,196     |
| Corporate bonds - financial services              | 200                          | —                                   | —                                   | 200         |
| Mortgage-backed securities                        | 256                          | 15                                  | —                                   | 271         |
| Collateralized mortgage obligations               | 14                           | —                                   | —                                   | 14          |
| Total Held-to-Maturity Fixed Maturities           | \$1,655                      | \$26                                | \$—                                 | \$1,681     |
| <b>AVAILABLE-FOR-SALE</b>                         |                              |                                     |                                     |             |
| Fixed maturities                                  |                              |                                     |                                     |             |
| Bonds   |                              |                                     |                                     |             |
| U.S. Treasury                                     | \$37,887                     | \$939                               | \$5                                 | \$38,821    |
| U.S. government agency                            | 45,566                       | 429                                 | 67                                  | 45,928      |
| States, municipalities and political subdivisions | 739,752                      | 55,572                              | 819                                 | 794,505     |
| Foreign bonds                                     | 207,359                      | 11,863                              | 62                                  | 219,160     |
| Public utilities                                  | 232,550                      | 15,208                              | 32                                  | 247,726     |
| Corporate bonds                                   |                              |                                     |                                     |             |
| Energy  | 169,973                      | 9,758                               | —                                   | 179,731     |
| Industrials                                       | 280,185                      | 13,690                              | 212                                 | 293,663     |
| Consumer goods and services                       | 193,313                      | 9,813                               | 151                                 | 202,975     |
| Health care                                       | 115,654                      | 7,111                               | 80                                  | 122,685     |
| Technology, media and telecommunications          | 123,660                      | 6,909                               | 198                                 | 130,371     |
| Financial services                                | 271,061                      | 13,858                              | 1,059                               | 283,860     |
| Mortgage-backed securities                        | 27,940                       | 888                                 | 21                                  | 28,807      |
| Collateralized mortgage obligations               | 208,042                      | 7,702                               | 1,160                               | 214,584     |
| Asset-backed securities                           | 4,480                        | 406                                 | —                                   | 4,886       |
| Redeemable preferred stocks                       | 378                          | —                                   | 2                                   | 376         |
| Total Available-for-Sale Fixed Maturities         | \$2,657,800                  | \$154,146                           | \$3,868                             | \$2,808,078 |
| Equity securities                                 |                              |                                     |                                     |             |
| Common stocks                                     |                              |                                     |                                     |             |
| Public utilities                                  | \$7,231                      | \$7,268                             | \$83                                | \$14,416    |
| Energy  | 5,094                        | 6,903                               | —                                   | 11,997      |
| Industrials                                       | 13,031                       | 19,827                              | 174                                 | 32,684      |
| Consumer goods and services                       | 10,394                       | 8,535                               | 50                                  | 18,879      |
| Health care                                       | 7,920                        | 10,286                              | 125                                 | 18,081      |
| Technology, media and telecommunications          | 5,367                        | 5,155                               | 95                                  | 10,427      |
| Financial services                                | 15,701                       | 52,936                              | 145                                 | 68,492      |
| Nonredeemable preferred stocks                    | 2,154                        | 25                                  | 28                                  | 2,151       |
| Total Available-for-Sale Equity Securities        | \$66,892                     | \$110,935                           | \$700                               | \$177,127   |
| Total Available-for-Sale Securities               | \$2,724,692                  | \$265,081                           | \$4,568                             | \$2,985,205 |



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## Maturities

The amortized cost and fair value of held-to-maturity, available-for-sale and trading securities at March 31, 2013, 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.

| March 31, 2013                        | Held-To-Maturity |            | Available-For-Sale |             | Trading        |            |
|---------------------------------------|------------------|------------|--------------------|-------------|----------------|------------|
|                                       | Amortized Cost   | Fair Value | Amortized Cost     | Fair Value  | Amortized Cost | Fair Value |
| Due in one year or less               | \$594            | \$597      | \$275,551          | \$281,662   | \$2,838        | \$2,803    |
| Due after one year through five years | 793              | 808        | 1,005,859          | 1,067,382   | 6,439          | 7,374      |
| Due after five years through 10 years | —                | —          | 860,281            | 921,673     | 508            | 533        |
| Due after 10 years                    | —                | —          | 242,504            | 247,318     | 2,685          | 3,028      |
| Asset-backed securities               | —                | —          | 4,044              | 4,474       | —              | —          |
| Mortgage-backed securities            | 242              | 254        | 24,808             | 25,538      | —              | —          |
| Collateralized mortgage obligations   | 9                | 9          | 253,855            | 259,535     | —              | —          |
|                                       | \$1,638          | \$1,668    | \$2,666,902        | \$2,807,582 | \$12,470       | \$13,738   |

## 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. The following table is a summary of net realized investment gains (losses).

|   | Three Months Ended March 31, |         |
|---|------------------------------|---------|
|   | 2013                         | 2012    |
| Net realized investment gains (losses)  |                              |         |
| Fixed maturities:   |                              |         |
| Available-for-sale  | \$720                        | \$1,531 |
| Trading securities  |                              |         |
| Change in fair value  | 560                          | 191     |
| Sales   | —                            | 371     |
| Equity securities   |                              |         |
| Available-for-sale  | 516                          | 701     |
| Trading securities  |                              |         |
| Change in fair value  | 113                          | —       |
| Total net realized investment gains   | \$1,909                      | \$2,794 |
| The proceeds and gross realized gains (losses) on the sale of available-for-sale securities are as follows: |                              |         |
|   | Three Months Ended March 31, |         |
|   | 2013                         | 2012    |
| Proceeds from sales   | \$2,810                      | \$3,000 |
| Gross realized gains  | 142                          | 470     |
| Gross realized losses   | —                            | (25 )   |

There were no sales of held-to-maturity securities during the three-month periods ended March 31, 2013 and 2012.

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



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investment gains and losses. Our portfolio of trading securities had a fair value of \$15,869 and \$15,371 at March 31, 2013 and December 31, 2012, respectively.

Off-Balance Sheet Arrangements

Pursuant to an agreement with one of our limited liability partnership investments, we are contractually committed through December 31, 2017 to make capital contributions upon request of the partnership. Our obligation was \$4,200 at March 31, 2013.

Unrealized Appreciation

The following table is a summary of changes in net unrealized investment appreciation during the reporting period.

|  | Three Months Ended March 31, |             |
|--|------------------------------|-------------|
|  | 2013                         | 2012        |
| Change in net unrealized investment appreciation                   |                              |             |
| Available-for-sale fixed maturities                                | \$ (9,598 )                  | \$ (4,401 ) |
| Equity securities  | 17,978                       | 15,106      |
| Deferred policy acquisition costs                                  | 4,871                        | 104         |
| Income tax effect  | (4,637 )                     | (3,784 )    |
| Total change in net unrealized investment appreciation, net of tax | \$8,614                      | \$7,025     |

We continually monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires other-than-temporary impairment ("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 March 31, 2013 and December 31, 2012. 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 March 31, 2013, 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 the fair value recovers to at least equal our cost basis or the securities mature.

We have evaluated the near-term prospects of the issuers of our equity securities in relation to the severity and duration of the unrealized loss, and unless otherwise noted, these losses do not warrant the recognition of an OTTI charge at March 31, 2013. Our largest unrealized loss greater than 12 months on an individual security at March 31, 2013 was \$212. 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.

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| March 31, 2013                                       | Less than 12 months    |               |                                     | 12 months or longer    |               |                                     | Total         |                                     |
|--|------------------------|---------------|-------------------------------------|------------------------|---------------|-------------------------------------|---------------|-------------------------------------|
| Type of Investment                                   | Number<br>of<br>Issues | Fair<br>Value | Gross<br>Unrealized<br>Depreciation | Number<br>of<br>Issues | Fair<br>Value | Gross<br>Unrealized<br>Depreciation | Fair<br>Value | Gross<br>Unrealized<br>Depreciation |
| <b>AVAILABLE-FOR-SALE</b>                            |                        |               |                                     |                        |               |                                     |               |                                     |
| Fixed maturities                                     |                        |               |                                     |                        |               |                                     |               |                                     |
| Bonds  |                        |               |                                     |                        |               |                                     |               |                                     |
| U.S. Treasury  | 2                      | \$1,717       | \$ 4                                | —                      | \$—           | \$ —                                | \$1,717       | \$ 4                                |
| U.S. government agency                               | 14                     | 45,452        | 243                                 | —                      | —             | —                                   | 45,452        | 243                                 |
| States, municipalities and<br>political subdivisions | 82                     | 83,557        | 1,662                               | —                      | —             | —                                   | 83,557        | 1,662                               |
| Foreign bonds  | 1                      | 3,327         | 31                                  | —                      | —             | —                                   | 3,327         | 31                                  |
| Public utilities                                     | 2                      | 3,277         | 7                                   | —                      | —             | —                                   | 3,277         | 7                                   |
| Corporate bonds                                      |                        |               |                                     |                        |               |                                     |               |                                     |
| Industrials  | 2                      | 6,069         | 101                                 | —                      | —             | —                                   | 6,069         | 101                                 |
| Consumer goods and services                          | 1                      | 2,344         | 11                                  | 6                      | 3,301         | 88                                  | 5,645         | 99                                  |
| Health care  | 3                      | 7,336         | 133                                 | —                      | —             | —                                   | 7,336         | 133                                 |
| Technology, media and<br>telecommunications          | 5                      | 18,271        | 701                                 | —                      | —             | —                                   | 18,271        | 701                                 |
| Financial services                                   | 2                      | 3,883         | 4                                   | 3                      | 11,139        | 373                                 | 15,022        | 377                                 |
| Mortgage-backed securities                           | 7                      | 4,244         | 25                                  | 2                      | 22            | 1                                   | 4,266         | 26                                  |
| Collateralized mortgage<br>obligations               | 46                     | 109,284       | 1,318                               | 1                      | 21            | 132                                 | 109,305       | 1,450                               |
| Total Available-for-Sale Fixed<br>Maturities         | 167                    | \$288,761     | \$ 4,240                            | 12                     | \$14,483      | \$ 594                              | \$303,244     | \$ 4,834                            |
| Equity securities                                    |                        |               |                                     |                        |               |                                     |               |                                     |
| Common stocks  |                        |               |                                     |                        |               |                                     |               |                                     |
| Public utilities                                     | 3                      | \$259         | \$ 49                               | —                      | \$—           | \$ —                                | \$259         | \$ 49                               |
| Industrials  | 1                      | 278           | 36                                  | 7                      | 529           | 88                                  | 807           | 124                                 |
| Consumer goods and services                          | 4                      | 243           | 25                                  | 3                      | 62            | 17                                  | 305           | 42                                  |
| Health care  | 1                      | 33            | 1                                   | 1                      | 470           | 24                                  | 503           | 25                                  |
| Technology, media and<br>telecommunications          | 5                      | 299           | 16                                  | 5                      | 197           | 64                                  | 496           | 80                                  |
| Financial services                                   | 1                      | 47            | 19                                  | 5                      | 538           | 84                                  | 585           | 103                                 |
| Nonredeemable preferred<br>stocks                    | —                      | —             | —                                   | 2                      | 1,211         | 20                                  | 1,211         | 20                                  |
| Total Available-for-Sale<br>Equity Securities        | 15                     | \$1,159       | \$ 146                              | 23                     | \$3,007       | \$ 297                              | \$4,166       | \$ 443                              |
| Total Available-for-Sale<br>Securities               | 182                    | \$289,920     | \$ 4,386                            | 35                     | \$17,490      | \$ 891                              | \$307,410     | \$ 5,277                            |

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| December 31, 2012                                    | Less than 12 months    |               |                                     | 12 months or longer    |               |                                     | Total         |                                     |
|--|------------------------|---------------|-------------------------------------|------------------------|---------------|-------------------------------------|---------------|-------------------------------------|
| Type of Investment                                   | Number<br>of<br>Issues | Fair<br>Value | Gross<br>Unrealized<br>Depreciation | Number<br>of<br>Issues | Fair<br>Value | Gross<br>Unrealized<br>Depreciation | Fair<br>Value | Gross<br>Unrealized<br>Depreciation |
| <b>AVAILABLE-FOR-SALE</b>                            |                        |               |                                     |                        |               |                                     |               |                                     |
| Fixed maturities                                     |                        |               |                                     |                        |               |                                     |               |                                     |
| Bonds  |                        |               |                                     |                        |               |                                     |               |                                     |
| U.S. Treasury  | 2                      | \$1,724       | \$ 5                                | —                      | \$—           | \$ —                                | \$1,724       | \$ 5                                |
| U.S. government agency                               | 5                      | 17,654        | 67                                  | —                      | —             | —                                   | 17,654        | 67                                  |
| States, municipalities and<br>political subdivisions | 31                     | 41,775        | 819                                 | —                      | —             | —                                   | 41,775        | 819                                 |
| Foreign bonds  | 1                      | 3,323         | 48                                  | 1                      | 558           | 14                                  | 3,881         | 62                                  |
| Public utilities                                     | 2                      | 3,155         | 32                                  | —                      | —             | —                                   | 3,155         | 32                                  |
| Corporate bonds                                      |                        |               |                                     |                        |               |                                     |               |                                     |
| Industrials  | 4                      | 12,194        | 109                                 | 1                      | 2,897         | 103                                 | 15,091        | 212                                 |
| Consumer goods and services                          | —                      | —             | —                                   | 7                      | 4,606         | 151                                 | 4,606         | 151                                 |
| Health care  | 3                      | 7,416         | 80                                  | —                      | —             | —                                   | 7,416         | 80                                  |
| Technology, media and<br>telecommunications          | 5                      | 13,402        | 198                                 | —                      | —             | —                                   | 13,402        | 198                                 |
| Financial services                                   | 2                      | 1,005         | 1                                   | 24                     | 24,693        | 1,058                               | 25,698        | 1,059                               |
| Mortgage-backed securities                           | 7                      | 4,472         | 21                                  | —                      | —             | —                                   | 4,472         | 21                                  |
| Collateralized mortgage<br>obligations               | 27                     | 74,702        | 1,004                               | 1                      | 29            | 156                                 | 74,731        | 1,160                               |
| Redeemable preferred stocks                          | 2                      | 376           | 2                                   | —                      | —             | —                                   | 376           | 2                                   |
| Total Available-for-Sale Fixed<br>Maturities         | 91                     | \$181,198     | \$ 2,386                            | 34                     | \$32,783      | \$ 1,482                            | \$213,981     | \$ 3,868                            |
| Equity securities                                    |                        |               |                                     |                        |               |                                     |               |                                     |
| Common stocks  |                        |               |                                     |                        |               |                                     |               |                                     |
| Public utilities                                     | 3                      | \$225         | \$ 83                               | —                      | \$—           | \$ —                                | \$225         | \$ 83                               |
| Industrials  | 4                      | 482           | 52                                  | 9                      | 621           | 122                                 | 1,103         | 174                                 |
| Consumer goods and services                          | 2                      | 280           | 19                                  | 4                      | 372           | 31                                  | 652           | 50                                  |
| Health care  | 1                      | 31            | 2                                   | 3                      | 896           | 123                                 | 927           | 125                                 |
| Technology, media and<br>telecommunications          | 5                      | 241           | 7                                   | 7                      | 581           | 88                                  | 822           | 95                                  |
| Financial services                                   | 1                      | 47            | 19                                  | 7                      | 1,109         | 126                                 | 1,156         | 145                                 |
| Nonredeemable preferred<br>stocks                    | —                      | —             | —                                   | 2                      | 1,203         | 28                                  | 1,203         | 28                                  |
| Total Available-for-Sale<br>Equity Securities        | 16                     | \$1,306       | \$ 182                              | 32                     | \$4,782       | \$ 518                              | \$6,088       | \$ 700                              |
| Total Available-for-Sale<br>Securities               | 107                    | \$182,504     | \$ 2,568                            | 66                     | \$37,565      | \$ 2,000                            | \$220,069     | \$ 4,568                            |

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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 estimates of 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.

The fair value of our mortgage loans is determined by modeling performed by us based on the stated principal and coupon payments provided for in the loan agreement. These cash flows are then discounted using an appropriate risk-adjusted discount rate to determine the security's fair value, which is a Level 3 fair value measurement.

The fair value of our policy loans is equivalent to carrying value, which is a reasonable estimate of fair 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 our interests in limited liability partnerships that are valued by 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.

Policy reserves are developed and recorded for deferred annuities, which is an interest-sensitive product, and income annuities. The fair value of the reserve liability for these annuity products is based upon an estimate of the discounted pretax cash flows that are forecast for the underlying business, which is a Level 3 fair value measurement. We base the discount rate on the current U.S. Treasury spot yield curve, which is then risk-adjusted for nonperformance risk and, for interest-sensitive business, market risk factors. The risk-adjusted discount rate is developed using interest rates that are available in the market and representative of the risks applicable to the underlying business.

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A summary of the carrying value and estimated fair value of our financial instruments at March 31, 2013 and December 31, 2012 is as follows:

|  | March 31, 2013 |                | December 31, 2012 |                |
|--|----------------|----------------|-------------------|----------------|
|  | Fair Value     | Carrying Value | Fair Value        | Carrying Value |
| Assets                                 |                |                |                   |                |
| Investments                            |                |                |                   |                |
| Fixed maturities:                      |                |                |                   |                |
| Held-to-maturity securities            | \$1,668        | \$1,638        | \$1,681           | \$1,655        |
| Available-for-sale securities          | 2,807,582      | 2,807,582      | 2,808,078         | 2,808,078      |
| Trading securities                     | 13,738         | 13,738         | 13,353            | 13,353         |
| Equity securities:                     |                |                |                   |                |
| Available-for-sale securities          | 195,677        | 195,677        | 177,127           | 177,127        |
| Trading securities                     | 2,131          | 2,131          | 2,018             | 2,018          |
| Mortgage loans                         | 4,800          | 4,581          | 5,037             | 4,633          |
| Policy loans                           | 6,566          | 6,566          | 6,671             | 6,671          |
| Other long-term investments            | 30,646         | 30,646         | 30,028            | 30,028         |
| Short-term investments                 | 800            | 800            | 800               | 800            |
| Cash and cash equivalents              | 101,948        | 101,948        | 107,466           | 107,466        |
| Accrued investment income              | 30,079         | 30,079         | 30,375            | 30,375         |
| Liabilities                            |                |                |                   |                |
| Policy reserves                        |                |                |                   |                |
| Annuity (accumulations) <sup>(1)</sup> | \$1,022,644    | \$963,017      | \$1,043,866       | \$983,579      |
| Annuity (benefit payments)             | 139,757        | 93,170         | 139,213           | 93,701         |

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

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

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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 independent 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 March 31, 2013 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 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 in our Consolidated Balance Sheets at March 31, 2013 and December 31, 2012:

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| Description                                       | March 31, 2013 | Fair Value Measurements |             |          |
|---|----------------|-------------------------|-------------|----------|
|   |                | Level 1                 | Level 2     | Level 3  |
| AVAILABLE-FOR-SALE                                |                |                         |             |          |
| Fixed maturities                                  |                |                         |             |          |
| Bonds   |                |                         |             |          |
| U.S. Treasury                                     | \$37,686       | \$—                     | \$37,686    | \$—      |
| U.S. government agency                            | 84,724         | —                       | 84,724      | —        |
| States, municipalities and political subdivisions | 781,633        | —                       | 780,758     | 875      |
| Foreign bonds                                     | 211,290        | —                       | 210,669     | 621      |
| Public utilities                                  | 246,176        | —                       | 246,176     | —        |
| Corporate bonds                                   |                |                         |             |          |
| Energy  | 176,273        | —                       | 176,273     | —        |
| Industrials                                       | 273,401        | —                       | 270,210     | 3,191    |
| Consumer goods and services                       | 199,195        | —                       | 197,632     | 1,563    |
| Health care                                       | 112,546        | —                       | 112,546     | —        |
| Technology, media and telecommunications          | 128,013        | —                       | 128,013     | —        |
| Financial services                                | 266,716        | —                       | 253,385     | 13,331   |
| Mortgage-backed securities                        | 25,538         | —                       | 25,538      | —        |
| Collateralized mortgage obligations               | 259,535        | —                       | 259,535     | —        |
| Asset-backed securities                           | 4,474          | —                       | 2,033       | 2,441    |
| Redeemable preferred stocks                       | 382            | 382                     | —           | —        |
| Total Available-for-Sale Fixed Maturities         | \$2,807,582    | \$382                   | \$2,785,178 | \$22,022 |
| Equity securities                                 |                |                         |             |          |
| Common stocks                                     |                |                         |             |          |
| Public utilities                                  | \$16,301       | \$16,301                | \$—         | \$—      |
| Energy  | 12,646         | 12,646                  | —           | —        |
| Industrials                                       | 35,144         | 35,120                  | 24          | —        |
| Consumer goods and services                       | 21,861         | 21,861                  | —           | —        |
| Health care                                       | 20,940         | 20,940                  | —           | —        |
| Technology, media and telecommunications          | 12,379         | 12,379                  | —           | —        |
| Financial services                                | 74,480         | 70,785                  | 59          | 3,636    |
| Nonredeemable preferred stocks                    | 1,926          | 1,926                   | —           | —        |
| Total Available-for-Sale Equity Securities        | \$195,677      | \$191,958               | \$83        | \$3,636  |
| Total Available-for-Sale Securities               | \$3,003,259    | \$192,340               | \$2,785,261 | \$25,658 |
| TRADING   |                |                         |             |          |
| Bonds   |                |                         |             |          |
| Foreign bonds                                     | \$1,304        | \$—                     | \$1,304     | \$—      |
| Corporate bonds                                   |                |                         |             |          |
| Industrials                                       | 1,227          | —                       | 1,227       | —        |
| Consumer goods and services                       | 1,572          | —                       | 1,572       | —        |

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|  |             |           |             |          |
|--|-------------|-----------|-------------|----------|
| Health care                              | 1,628       | —         | 1,628       | —        |
| Technology, media and telecommunications | 2,765       | —         | 2,765       | —        |
| Financial services                       | 1,542       | —         | 1,542       | —        |
| Redeemable preferred stocks              | 3,700       | 3,700     | —           | —        |
| Equity securities - health care          | 327         | 327       | —           | —        |
| Nonredeemable preferred stocks           | 1,804       | 1,804     | —           | —        |
| Total Trading Securities                 | \$15,869    | \$5,831   | \$10,038    | \$—      |
| Short-Term Investments                   | \$800       | \$800     | \$—         | \$—      |
| Money Market Accounts                    | \$52,271    | \$52,271  | \$—         | \$—      |
| Total Assets Measured at Fair Value      | \$3,072,199 | \$251,242 | \$2,795,299 | \$25,658 |

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| Description                                       | December 31, 2012 | Fair Value Measurements |             |          |
|---|-------------------|-------------------------|-------------|----------|
|   |                   | Level 1                 | Level 2     | Level 3  |
| AVAILABLE-FOR-SALE                                |                   |                         |             |          |
| Fixed maturities                                  |                   |                         |             |          |
| Bonds   |                   |                         |             |          |
| U.S. Treasury                                     | \$38,821          | \$—                     | \$38,821    | \$—      |
| U.S. government agency                            | 45,928            | —                       | 45,928      | —        |
| States, municipalities and political subdivisions | 794,505           | —                       | 793,755     | 750      |
| Foreign bonds                                     | 219,160           | —                       | 218,602     | 558      |
| Public utilities                                  | 247,726           | —                       | 247,726     | —        |
| Corporate bonds                                   |                   |                         |             |          |
| Energy  | 179,731           | —                       | 179,731     | —        |
| Industrials                                       | 293,663           | —                       | 290,766     | 2,897    |
| Consumer goods and services                       | 202,975           | —                       | 201,633     | 1,342    |
| Health care                                       | 122,685           | —                       | 122,685     | —        |
| Technology, media and telecommunications          | 130,371           | —                       | 130,371     | —        |
| Financial services                                | 283,860           | —                       | 271,991     | 11,869   |
| Mortgage-backed securities                        | 28,807            | —                       | 28,807      | —        |
| Collateralized mortgage obligations               | 214,584           | —                       | 214,584     | —        |
| Asset-backed securities                           | 4,886             | —                       | 2,398       | 2,488    |
| Redeemable preferred stocks                       | 376               | 376                     | —           | —        |
| Total Available-for-Sale Fixed Maturities         | \$2,808,078       | \$376                   | \$2,787,798 | \$19,904 |
| Equity securities                                 |                   |                         |             |          |
| Common stocks                                     |                   |                         |             |          |
| Public utilities                                  | \$14,416          | \$14,416                | \$—         | \$—      |
| Energy  | 11,997            | 11,997                  | —           | —        |
| Industrials                                       | 32,684            | 32,658                  | 26          | —        |
| Consumer goods and services                       | 18,879            | 18,879                  | —           | —        |
| Health care                                       | 18,081            | 18,081                  | —           | —        |
| Technology, media and telecommunications          | 10,427            | 10,427                  | —           | —        |
| Financial services                                | 68,492            | 64,800                  | 56          | 3,636    |
| Nonredeemable preferred stocks                    | 2,151             | 1,906                   | 245         | —        |
| Total Available-for-Sale Equity Securities        | \$177,127         | \$173,164               | \$327       | \$3,636  |
| Total Available-for-Sale Securities               | \$2,985,205       | \$173,540               | \$2,788,125 | \$23,540 |
| TRADING   |                   |                         |             |          |
| Bonds   |                   |                         |             |          |
| Foreign bonds                                     | \$1,379           | \$—                     | \$1,379     | \$—      |
| Corporate bonds                                   |                   |                         |             |          |
| Industrials                                       | 1,299             | —                       | 1,299       | —        |
| Consumer goods and services                       | 1,532             | —                       | 1,532       | —        |
| Health care                                       | 1,824             | —                       | 1,824       | —        |
| Technology, media and telecommunications          | 2,250             | —                       | 2,250       | —        |



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|                                     |             |           |             |          |
|-------------------------------------|-------------|-----------|-------------|----------|
| Financial services                  | 1,486       | —         | 1,486       | —        |
| Redeemable preferred stocks         | 3,583       | 3,583     | —           | —        |
| Equity securities - health care     | 303         | 303       | —           | —        |
| Nonredeemable preferred stocks      | 1,715       | 1,715     | —           | —        |
| Total Trading Securities            | \$15,371    | \$5,601   | \$9,770     | \$—      |
| Short-Term Investments              | \$800       | \$800     | \$—         | \$—      |
| Money Market Accounts               | \$45,613    | \$45,613  | \$—         | \$—      |
| Total Assets Measured at Fair Value | \$3,046,989 | \$225,554 | \$2,797,895 | \$23,540 |

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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 three-month period ended March 31, 2013, the change in our available-for-sale securities categorized as Level 1 and Level 2 is the result of investment purchases, which were made using funds held in our money market accounts, disposals and the change in unrealized gains on both fixed maturities and equity securities. There were no significant transfers of securities between Level 1 and Level 2 during the period.

Securities 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. If we cannot obtain pricing from these sources, which occurs on a limited basis, management will perform an analysis of the contractual cash flows of the underlying security to estimate fair value.

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 there is no market for the impaired security 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 March 31, 2013:

|                                 | States,<br>municipalities<br>and political<br>subdivisions | Foreign<br>bonds | Corporate<br>bonds | Asset-backed<br>securities | Equities | Total    |
|---------------------------------|--|------------------|--------------------|----------------------------|----------|----------|
| Balance at December 31, 2012    | \$ 750   | \$558            | \$16,108           | \$2,488                    | \$3,636  | \$23,540 |
| Unrealized gains <sup>(1)</sup> | 125  | 63               | 2,249              | 46                         | —        | 2,483    |
| Disposals                       | —  | —                | (272 )             | (93 )                      | —        | (365 )   |
| Balance at March 31, 2013       | \$ 875   | \$621            | \$18,085           | \$2,441                    | \$3,636  | \$25,658 |

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

The fixed maturities reported as disposals relate to the receipt of principal on calls or sinking fund bonds, in accordance with the indentures.



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## NOTE 4. EMPLOYEE BENEFITS

## Net Periodic Benefit Cost

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

| Three Months Ended March 31,       | Pension Plan |          | Postretirement Benefit Plan |       |
|------------------------------------|--------------|----------|-----------------------------|-------|
|                                    | 2013         | 2012     | 2013                        | 2012  |
| Net periodic benefit cost          |              |          |                             |       |
| Service cost                       | \$1,282      | \$791    | \$753                       | \$496 |
| Interest cost                      | 1,262        | 1,190    | 424                         | 398   |
| Expected return on plan assets     | (1,336 )     | (1,322 ) | —                           | —     |
| Amortization of prior service cost | —            | 3        | —                           | (8 )  |
| Amortization of net loss           | 1,106        | 592      | 136                         | 56    |
| Net periodic benefit cost          | \$2,314      | \$1,254  | \$1,313                     | \$942 |

## Employer Contributions

We previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012 that we expected to contribute \$7,000 to the pension plan for the 2013 plan year. For the three-month period ended March 31, 2013, we contributed \$1,750 to the pension plan. We anticipate that the total contribution for the 2013 plan year will not vary significantly from our expected contribution.

## NOTE 5. STOCK-BASED COMPENSATION

## Non-qualified Employee Stock Award Plan

The United Fire Group, Inc. 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 337,509 authorized shares available for future issuance at March 31, 2013. 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 our employees who are in positions of substantial responsibility with United Fire.

Options 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 option period, but not later than 10 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 five 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.



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The activity in the 2008 Stock Plan is displayed in the following table:

| Authorized Shares Available for Future Award Grants | Three Months Ended<br>March 31, 2013 | Inception to Date |
|---|--------------------------------------|-------------------|
| Beginning balance                                   | 568,746                              | 1,900,000         |
| Number of awards granted                            | (237,737 )                           | (1,681,561 )      |
| Number of awards forfeited or expired               | 6,500                                | 119,070           |
| Ending balance                                      | 337,509                              | 337,509           |
| Number of option awards exercised                   | 27,050                               | 253,892           |
| Number of unrestricted stock awards granted         | —                                    | 3,620             |
| Number of restricted stock awards vested            | —                                    | —                 |

#### Non-qualified Non-employee Director Stock Option and Restricted Stock Plan

The United Fire Group, Inc. 2005 Non-qualified Non-Employee Director Stock Option and Restricted Stock Plan (the "Director Plan") authorizes the issuance of restricted and unrestricted stock awards and non-qualified stock options to purchase shares of United Fire's common stock to non-employee directors. At March 31, 2013, we had 130,012 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 Director Plan.

The activity in the Director Plan is displayed in the following table:

| Authorized Shares Available for Future Award Grants | Three Months Ended<br>March 31, 2013 | Inception to Date |
|---|--------------------------------------|-------------------|
| Beginning balance                                   | 130,012                              | 300,000           |
| Number of awards granted                            | —                                    | (175,991 )        |
| Number of awards forfeited or expired               | —                                    | 6,003             |
| Ending balance                                      | 130,012                              | 130,012           |
| Number of option awards exercised                   | 2,182                                | 2,182             |

#### Stock-Based Compensation Expense

For the three-month periods ended March 31, 2013 and 2012, we recognized stock-based compensation expense of \$411 and \$396, respectively.

As of March 31, 2013, we had \$4,349 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 2013 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.

|       |         |
|-------|---------|
| 2013  | \$1,049 |
| 2014  | 1,237   |
| 2015  | 1,025   |
| 2016  | 578     |
| 2017  | 411     |
| 2018  | 49      |
| Total | \$4,349 |



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## NOTE 6. SEGMENT INFORMATION

We have two reportable business segments in our operations: property and casualty insurance and life insurance. The property and casualty insurance segment has six domestic locations from which it conducts its business. 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 or permitted 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, 2012.

The following tables for the three-month periods ended March 31, 2013 and 2012 have been reconciled to the amounts reported in our unaudited Consolidated Financial Statements to adjust for intersegment eliminations.

|   | Property and<br>Casualty Insurance | Life Insurance | Total        |
|---|------------------------------------|----------------|--------------|
| Three Months Ended March 31, 2013             |                                    |                |              |
| Net premiums earned                           | \$ 162,701                         | \$ 14,239      | \$ 176,940   |
| Investment income, net of investment expenses | 10,421                             | 15,979         | 26,400       |
| Net realized investment gains                 | 1,029                              | 880            | 1,909        |
| Other income                                  | 12                                 | 103            | 115          |
| Total reportable segment                      | \$ 174,163                         | \$ 31,201      | \$ 205,364   |
| Intersegment eliminations                     | 64                                 | (123)          | (59)         |
| Total revenues                                | \$ 174,227                         | \$ 31,078      | \$ 205,305   |
| Net income                                    | \$ 20,730                          | \$ 1,663       | \$ 22,393    |
| Assets  | \$ 1,941,227                       | \$ 1,783,463   | \$ 3,724,690 |
| Invested assets                               | \$ 1,378,188                       | \$ 1,685,171   | \$ 3,063,359 |
| Three Months Ended March 31, 2012             |                                    |                |              |
| Net premiums earned                           | \$ 146,756                         | \$ 14,858      | \$ 161,614   |
| Investment income, net of investment expenses | 10,678                             | 18,508         | 29,186       |
| Net realized investment gains                 | 1,133                              | 1,614          | 2,747        |
| Other income                                  | 100                                | 156            | 256          |
| Total reportable segment                      | \$ 158,667                         | \$ 35,136      | \$ 193,803   |
| Intersegment eliminations                     | 7                                  | (111)          | (104)        |
| Total revenues                                | \$ 158,674                         | \$ 35,025      | \$ 193,699   |
| Net income                                    | \$ 16,636                          | \$ 2,548       | \$ 19,184    |
| Assets  | \$ 1,901,748                       | \$ 1,785,427   | \$ 3,687,175 |
| Invested assets                               | \$ 1,325,793                       | \$ 1,696,391   | \$ 3,022,184 |

## NOTE 7. EARNINGS PER COMMON SHARE

Basic earnings per share is computed by dividing net income by the weighted-average number of common shares outstanding during the reporting period. Diluted earnings per share gives effect to all dilutive common shares outstanding during the reporting period. The dilutive shares we consider in our diluted earnings 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 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 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.

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The components of basic and diluted earnings per share were as follows for the three-month periods ended March 31, 2013 and 2012:

| (In Thousands Except Per Share Data)                        | Three Months Ended March 31, |            |            |            |
|---|------------------------------|------------|------------|------------|
|   | 2013                         |            | 2012       |            |
|   | Basic                        | Diluted    | Basic      | Diluted    |
| Net income  | \$22,393                     | \$22,393   | \$19,184   | \$19,184   |
| Weighted-average common shares outstanding                  | 25,245,497                   | 25,245,497 | 25,505,962 | 25,505,962 |
| Add dilutive effect of restricted stock awards              | —                            | 79,787     | —          | 50,206     |
| Add dilutive effect of stock options                        | —                            | 15,385     | —          | 16,373     |
| Weighted-average common shares for EPS calculation          | 25,245,497                   | 25,340,669 | 25,505,962 | 25,572,541 |
| Earnings per common share                                   | \$0.89                       | \$0.88     | \$0.75     | \$0.75     |
| Awards excluded from diluted EPS calculation <sup>(1)</sup> | —                            | 643,066    | —          | 1,085,547  |

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

**NOTE 8. DEBT**

In December 2011, United Fire entered into a credit agreement with a syndicate of financial institutions as lenders, KeyBank National Association as administrative agent, lead arranger, sole book runner, swingline lender, and letter of credit issuer, and Bankers Trust Company as syndication agent. The four-year credit agreement provides for a \$100,000 unsecured revolving credit facility that includes a \$20,000 letter of credit subfacility and a swing line subfacility of up to \$5,000.

During the term of this credit agreement, we have the right to increase the total credit facility from \$100,000 up to \$125,000 if no event of default has occurred and is continuing and certain other conditions are satisfied. The credit facility is available for general corporate purposes, including working capital, acquisitions and liquidity purposes. Principal of the credit facility is due in full at maturity, on December 22, 2015. The interest rate is based on our monthly choice of either a base rate or the London Interbank Offered Rate ("LIBOR") plus, in each case, a calculated margin amount. A commitment fee on each lender's unused commitment under the credit facility is also payable quarterly.

The credit agreement contains customary representations, covenants and events of default, including certain covenants that limit or restrict our ability to engage in certain activities. Subject to certain exceptions, these activities include restricting our ability to sell or transfer assets or enter into a merger or consolidate with another company, grant certain types of security interests, incur certain types of liens, impose restrictions on subsidiary dividends, enter into leaseback transactions, or incur certain indebtedness. The credit agreement contains certain financial covenants including covenants that require us to maintain a minimum consolidated net worth, a debt to capitalization ratio and minimum stockholders' equity.

There was no outstanding balance on the credit facility at March 31, 2013. The outstanding balance on the line of credit was \$45,000 at March 31, 2012 at an interest rate of 2.0 percent. For the three-month period ended March 31, 2013, we did not incur any interest expense related to this credit facility. For the three-month period ended March 31, 2012, we incurred \$341 in interest expense related to this credit facility. We were in compliance with all covenants for the credit agreement at March 31, 2013.

In connection with our acquisition of Mercer Insurance Group, we acquired three statutory trusts with outstanding issuances of trust preferred securities with a balance as of the acquisition date of \$15,614. We redeemed two of the issuances totaling \$8,035 during the three-month period ended March 31, 2012 and the remaining issuance in full in April 2012. We incurred \$151 of interest expense related to these trust preferred securities for the three-month period ended March 31, 2012.



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## NOTE 9. ACCUMULATED OTHER COMPREHENSIVE INCOME

The after-tax components of our accumulated other comprehensive income (loss) are as follows:

|   | Net unrealized<br>appreciation<br>on investments | Liability for<br>underfunded<br>employee<br>benefit costs | Total     |
|---|--|---|-----------|
| Balance as of January 1, 2013   | \$144,096  | \$(48,908 )   | \$95,188  |
| Change in accumulated other comprehensive income before reclassifications | 9,855  | —   | 9,855     |
| Reclassification adjustments from accumulated other comprehensive income  | (1,241 )   | 808   | (433 )    |
| Balance as of March 31, 2013  | \$152,710  | \$(48,100 )   | \$104,610 |

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Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders  
United Fire Group, Inc.

We have reviewed the consolidated balance sheet of United Fire Group, Inc. as of March 31, 2013, and the related consolidated statements of income and comprehensive income for the three-month periods ended March 31, 2013 and 2012, the consolidated statements of cash flows for the three-month periods ended March 31, 2013 and 2012, and the consolidated statement of stockholders' equity for the three-month period ended March 31, 2013. 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 Group, Inc. as of December 31, 2012, and the related consolidated statements of income and comprehensive income, stockholders' equity, and cash flows for the year then ended, not presented herein, and in our report dated March 4, 2013, 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, 2012, 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  
May 8, 2013

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with Part 1, Item 1 "Financial Statements."

#### 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 the 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 continue," "might," "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. See Part I Item 1A "Risk Factors" in the 2012 Annual Report on Form 10-K and Part II Item 1A, "Risk Factors" of this document, for more information concerning factors that could cause actual results to differ materially from those in the forward-looking statements. Accordingly, 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 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 POLICIES

Critical accounting policies 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 policies 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, 2012.

#### 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 our consolidated financial statements and related notes, including those in our Annual Report on Form 10-K for the year ended December 31, 2012. When we provide information on a statutory basis, we label it as such, otherwise, all other data is presented in accordance with GAAP.

#### OUR BUSINESS

Founded in 1946 as United Fire & Casualty Company, United Fire Group, Inc. ("United Fire", "Registrant", the "Company", "we", "us", "our") and its consolidated insurance subsidiaries provide insurance protection for

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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 approximately 1,200 independent agencies. Our life insurance subsidiary is licensed in 36 states and is represented by more than 900 independent agencies.

## Segments

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.

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 three-month period ended March 31, 2013, property and casualty insurance business accounted for approximately 90.0 percent of our net premiums earned, of which 90.3 percent was generated from commercial lines. Life insurance business accounted for approximately 10.0 percent of our net premiums earned, of which 73.3 percent was generated from traditional life insurance products.

## Pooling Arrangement

All of our property and casualty insurance subsidiaries, with the exception of Texas General Indemnity Company, which is in runoff, are members of an intercompany reinsurance pooling arrangement. Pooling arrangements permit the participating companies to rely on the capacity of the entire pool's capital and surplus, rather than being limited to policy exposures of a size commensurate with each participant's own surplus level.

## Geographic Concentration

For the three-month period ended March 31, 2013, approximately 50.0 percent of our property and casualty premiums were written in Iowa, Texas, California, New Jersey, and Missouri; approximately 78.0 percent of our life insurance premiums were written in Iowa, Minnesota, Wisconsin, Illinois, and Nebraska.

## Segment Revenue and Expense

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, future policy benefits, underwriting and other operating expenses and interest on policyholders' accounts.

## Profit Factors

Our profitability 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. 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.

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## CONSOLIDATED FINANCIAL HIGHLIGHTS

| (In Thousands)                                    | Three Months Ended March 31, |           |       |   |
|---|------------------------------|-----------|-------|---|
|   | 2013                         | 2012      | %     |   |
| Revenues  |                              |           |       |   |
| Net premiums earned                               | \$176,817                    | \$161,503 | 9.5   | % |
| Investment income, net of investment expenses     | 26,464                       | 29,146    | (9.2  | ) |
| Net realized investment gains                     | 1,909                        | 2,794     | (31.7 | ) |
| Other income                                      | 115                          | 256       | (55.1 | ) |
| Total revenues                                    | \$205,305                    | \$193,699 | 6.0   | % |
| Benefits, Losses and Expenses                     |                              |           |       |   |
| Losses and loss settlement expenses               | \$97,470                     | \$91,484  | 6.5   | % |
| Future policy benefits                            | 8,236                        | 10,138    | (18.8 | ) |
| Amortization of deferred policy acquisition costs | 38,081                       | 34,551    | 10.2  |   |
| Other underwriting expenses                       | 22,348                       | 21,994    | 1.6   |   |
| Interest on policyholders' accounts               | 9,320                        | 10,656    | (12.5 | ) |
| Total benefits, losses and expenses               | \$175,455                    | \$168,823 | 3.9   | % |
| Income before income taxes                        | \$29,850                     | \$24,876  | 20.0  | % |
| Federal income tax expense                        | 7,457                        | 5,692     | 31.0  |   |
| Net income  | \$22,393                     | \$19,184  | 16.7  | % |

The following is a summary of our financial performance for the three-month periods ended March 31, 2013 and 2012:

## Consolidated Results of Operations

For the three-month period ended March 31, 2013, net income was \$22.4 million compared to \$19.2 million for the same period of 2012, driven primarily by growth in property and casualty premium revenue. Consolidated net premiums earned increased to \$176.8 million, compared to \$161.5 million for the same period of 2012. This increase represents organic growth and is the result of a combination of rate increases across most commercial and personal lines, growth in premium audit collections, and new business writings.

Losses and loss settlement expenses increased by \$6.0 million during the first quarter of 2013 compared to the first quarter of 2012, primarily due to the overall growth in our business, partially offset by a decrease in catastrophe loss experience. Pre-tax catastrophe losses totaled \$4.5 million compared to \$14.1 million in the first quarter of 2012, which was impacted by losses from severe storms in the Midwest.

## Consolidated Financial Condition

At March 31, 2013, the book value per share of our common stock was \$30.01. We did not repurchase any shares of our common stock in the three-month period ended March 31, 2013. Under our share repurchase program, which expires in August 2014, we are authorized to repurchase an additional 1,129,720 shares of our common stock.

Net unrealized investment gains totaled \$152.7 million as of March 31, 2013, an increase of \$8.6 million, net of tax, or 6.0 percent, since December 31, 2012. The increase in net unrealized gains resulted from an increase in the fair value of our equity portfolios, offset slightly by a decrease in our fixed maturity portfolios.

Our stockholders' equity increased to \$758.1 million at March 31, 2013, from \$729.2 million at December 31, 2012. The increase was primarily attributable to net income of \$22.4 million and net unrealized investment gains of \$8.6 million, net of tax, which was partially offset by stockholder dividends of \$3.8 million.

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## RESULTS OF OPERATIONS

## Property and Casualty Insurance Segment Results

| (In Thousands)                                    | Three Months Ended March 31, |   |           |   |
|---|------------------------------|---|-----------|---|
|   | 2013                         |   | 2012      |   |
| Net premiums written <sup>(1)</sup>               | \$177,119                    |   | \$164,633 |   |
| Net premiums earned                               | \$162,701                    |   | \$146,756 |   |
| Losses and loss settlement expenses               | (92,093                      | ) | (87,310   | ) |
| Amortization of deferred policy acquisition costs | (36,355                      | ) | (32,413   | ) |
| Other underwriting expenses                       | (18,415                      | ) | (17,868   | ) |
| Underwriting gain <sup>(1)</sup>                  | \$15,838                     |   | \$9,165   |   |
| Investment income, net of investment expenses     | 10,485                       |   | 10,638    |   |
| Net realized investment gains                     | 1,029                        |   | 1,180     |   |
| Other income                                      | 12                           |   | 100       |   |
| Income before income taxes                        | \$27,364                     |   | \$21,083  |   |
| GAAP Ratios:                                      |                              |   |           |   |
| Net loss ratio                                    | 53.8                         | % | 49.9      | % |
| Catastrophes - effect on net loss ratio           | 2.8                          |   | 9.6       |   |
| Net loss ratio                                    | 56.6                         | % | 59.5      | % |
| Expense ratio <sup>(2)</sup>                      | 33.7                         |   | 34.3      |   |
| Combined ratio                                    | 90.3                         | % | 93.8      | % |

(1) The Measurement of Results 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.

For the three months ended March 31, 2013, our property and casualty segment reported income before taxes of \$27.4 million or an increase of \$6.3 million compared to the same period in 2012, primarily due to an increase in the underwriting gain.

The property and casualty insurance segment experienced \$23.7 million of favorable development in our net reserves for prior accident years during the three months ended March 31, 2013. These results are consistent with results from first quarter 2012. Development amounts can vary significantly from quarter-to-quarter and year-to-year depending on a number of factors, including the number of claims settled and the settlement terms, and are subject to reallocation between accident years and lines of business. In the first quarter 2013, our total reserves remained relatively flat and within our actuarial estimates.

The net loss ratio, a component of the combined ratio, decreased by 2.9 percentage points to 53.8 percentage points in the three-month period ended March 31, 2013, as compared to the same period in 2012. The decrease is due primarily to reduced catastrophe loss experience. Pre-tax catastrophe losses totaled \$4.5 million for the three-month period ended March 31, 2013, as compared to \$14.1 million for the same period of 2012.

The expense ratio, a component of the combined ratio, of 33.7 percentage points for the quarter ended March 31, 2013 decreased 0.6 percentage points compared with the same period in 2012.

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



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The following tables display our premiums earned, losses and loss settlement expenses and loss ratio by line of business:

| Three Months Ended March 31, 2013 |           |                   |         | 2012            |                   |        |   |
|-----------------------------------|-----------|-------------------|---------|-----------------|-------------------|--------|---|
| (In Thousands)                    | Net       | Losses and Loss   |         |                 | Losses and Loss   |        |   |
| Unaudited                         | Premiums  | Settlement        | Loss    | Net             | Settlement        | Loss   |   |
| Commercial lines                  | Earned    | Expenses Incurred | Ratio   | Premiums Earned | Expenses Incurred | Ratio  |   |
| Other liability                   | \$45,329  | \$20,697          | 45.7    | % \$46,120      | \$22,348          | 48.5   | % |
| Fire and allied lines             | 40,974    | 18,601            | 45.4    | 31,546          | 25,842            | 81.9   |   |
| Automobile                        | 34,958    | 26,173            | 74.9    | 31,609          | 23,269            | 73.6   |   |
| Workers' compensation             | 19,108    | 16,363            | 85.6    | 15,609          | 5,492             | 35.2   |   |
| Fidelity and surety               | 4,759     | 294               | 6.2     | 4,297           | (44               | ) (1.0 | ) |
| Miscellaneous                     | 45        | 614               | NM      | 232             | 1                 | 0.4    |   |
| Total commercial lines            | \$145,173 | \$82,742          | 57.0    | % \$129,413     | \$76,908          | 59.4   | % |
| Personal lines                    |           |                   |         |                 |                   |        |   |
| Fire and allied lines             | \$10,436  | \$6,201           | 59.4    | % \$10,153      | \$3,618           | 35.6   | % |
| Automobile                        | 5,346     | 3,195             | 59.8    | 5,129           | 3,136             | 61.1   |   |
| Miscellaneous                     | 53        | 234               | NM      | 222             | 185               | 83.3   |   |
| Total personal lines              | \$15,835  | \$9,630           | 60.8    | % \$15,504      | \$6,939           | 44.8   | % |
| Reinsurance assumed               | \$1,693   | \$(279            | ) (16.5 | )% \$1,839      | \$3,463           | 188.3  | % |
| Total                             | \$162,701 | \$92,093          | 56.6    | % \$146,756     | \$87,310          | 59.5   | % |

NM=Not meaningful

Commercial fire and allied lines - The loss ratio improved 37.7 percentage points in the three-month period ended March 31, 2013, compared to the same period of 2012. The improvement was due to incurred losses from severe storms in the Midwest in the three-month period ended March 31, 2012.

Workers' compensation - The loss ratio deteriorated by 50.4 percentage points in the three-month period ended March 31, 2013 compared to the same period of 2012 when we experienced particularly low losses and loss settlement expenses.

Personal fire and allied lines - The loss ratio deteriorated 31.2 percentage points in the three-month period ended March 31, 2013, compared to the same period of 2012 primarily due to unfavorable development in the three-month period ending March 31, 2013 on prior year claims.



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## Life Insurance Segment Results

| (In Thousands)                                    | Three Months Ended March 31, |          |
|---|------------------------------|----------|
|   | 2013                         | 2012     |
| Revenues  |                              |          |
| Net premiums earned                               | \$14,116                     | \$14,747 |
| Investment income, net                            | 15,979                       | 18,508   |
| Net realized investment gains                     | 880                          | 1,614    |
| Other income                                      | 103                          | 156      |
| Total revenues                                    | \$31,078                     | \$35,025 |
| Benefits, Losses and Expenses                     |                              |          |
| Losses and loss settlement expenses               | \$5,377                      | \$4,174  |
| Future policy benefits                            | 8,236                        | 10,138   |
| Amortization of deferred policy acquisition costs | 1,726                        | 2,138    |
| Other underwriting expenses                       | 3,933                        | 4,126    |
| Interest on policyholders' accounts               | 9,320                        | 10,656   |
| Total benefits, losses and expenses               | \$28,592                     | \$31,232 |
| Income before income taxes                        | \$2,486                      | \$3,793  |

Income before income taxes decreased by \$1.3 million in the three-month period ended March 31, 2013, as compared to the same period of 2012. Net premiums earned decreased 4.3 percent in the three-month period ended March 31, 2013, as compared to the same period of 2012, primarily due to decreased sales of immediate annuities.

Loss and loss settlement expenses increased 28.8 percent in the three-month period ended March 31, 2013, as compared to the same period of 2012, due to an increase in policy claims. Future policy benefits decreased 18.8 percent in the three-month period ended March 31, 2013, as compared to the same period of 2012, primarily due to an increase in net withdrawals of deferred annuity products in the three-month period ended March 31, 2013.

Deferred annuity deposits decreased 51.7 percent for the three-month period ended March 31, 2013, as compared with the same periods in 2012. It has been prudent to lower the credited rate we have offered during the low investment return environment, thus affecting current deposits. Sales of single premium deferred annuities have also decreased in regard to overall portfolio production, due to strong sales of traditional life products. While deferred annuity deposits are not recorded as a component of net premiums written or net premiums earned, they do generate investment income.

Net cash outflow related to our annuity business was \$25.9 million in the three-month period ended March 31, 2013, compared to a net cash outflow of \$0.3 million in the same periods of 2012. We attribute this to the activity described in the prior paragraph.

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

## Investment Portfolio

Our invested assets totaled \$3.1 billion at March 31, 2013, compared to \$3.0 billion at December 31, 2012, an increase of \$19.0 million. At March 31, 2013, fixed maturity securities and equity securities made up 92.2 percent and 6.5 percent of the value of our investment portfolio, respectively. Because the primary purpose of our investment portfolio is to fund future claims payments, we use 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. Our overall investment strategy is to keep our cash on hand low in the current interest rate environment. If extra cash is needed, we can borrow funds available under our revolving credit facility.

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## 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 March 31, 2013, is presented at carrying value in the following table:

|                                 | Property & Casualty<br>Insurance Segment |                     | Life Insurance Segment |                     | Total         |                     |
|---------------------------------|--|---------------------|------------------------|---------------------|---------------|---------------------|
| (In Thousands)                  |  | Percent<br>of Total |                        | Percent<br>of Total |               | Percent<br>of Total |
| Fixed maturities <sup>(1)</sup> |  |                     |                        |                     |               |                     |
| Held-to-maturity                | \$1,128                                  | 0.1                 | % \$510                | —                   | % \$1,638     | 0.1                 |
| Available-for-sale              | 1,160,023                                | 84.2                | 1,647,559              | 97.8                | 2,807,582     | 91.7                |
| Trading securities              | 13,738                                   | 1.0                 | —                      | —                   | 13,738        | 0.4                 |
| Equity securities               |  |                     |                        |                     |               |                     |
| Available-for-sale              | 175,158                                  | 12.6                | 20,519                 | 1.2                 | 195,677       | 6.4                 |
| Trading securities              | 2,131                                    | 0.2                 | —                      | —                   | 2,131         | 0.1                 |
| Mortgage loans                  | —  | —                   | 4,581                  | 0.3                 | 4,581         | 0.1                 |
| Policy loans                    | —  | —                   | 6,566                  | 0.4                 | 6,566         | 0.2                 |
| Other long-term investments     | 25,210                                   | 1.8                 | 5,436                  | 0.3                 | 30,646        | 1.0                 |
| Short-term investments          | 800                                      | 0.1                 | —                      | —                   | 800           | —                   |
| Total                           | \$1,378,188                              | 100.0               | % \$1,685,171          | 100.0               | % \$3,063,359 | 100.0               |

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

At March 31, 2013, we classified \$2.8 billion, or 99.5 percent, of our fixed maturities portfolio as available-for-sale, compared to \$2.8 billion, or 99.5 percent, at December 31, 2012. 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 March 31, 2013 and December 31, 2012, we did not have direct exposure to investments in subprime mortgages or other credit enhancement vehicles.

## 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 March 31, 2013 and December 31, 2012. 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)  | March 31, 2013 |            | December 31, 2012 |            |
|-----------------|----------------|------------|-------------------|------------|
| Rating          | Carrying Value | % of Total | Carrying Value    | % of Total |
| AAA             | \$571,755      | 20.3       | \$481,754         | 17.1       |
| AA              | 598,325        | 21.2       | 646,516           | 22.9       |
| A               | 647,283        | 22.9       | 632,962           | 22.4       |
| Baa/BBB         | 946,695        | 33.5       | 998,818           | 35.4       |
| Other/Not Rated | 58,900         | 2.1        | 63,036            | 2.2        |

|             |       |   |             |       |   |
|-------------|-------|---|-------------|-------|---|
| \$2,822,958 | 100.0 | % | \$2,823,086 | 100.0 | % |
|-------------|-------|---|-------------|-------|---|

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### Duration

Our investment portfolio is invested primarily in 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 reserve liabilities. If our invested assets and reserve liabilities have similar durations, then any change in interest rates will have an equal effect on these accounts. The primary purpose for matching invested assets and reserve liabilities is liquidity. With appropriate matching, our investments will mature when cash is needed, preventing the need to liquidate other assets prematurely. Mismatches in the duration of assets and liabilities can cause significant fluctuations in our results of operations.

### Group

The weighted average effective duration of our portfolio of fixed maturity securities, at March 31, 2013, is 4.3 years compared to 4.0 years at December 31, 2012.

### Property and Casualty Insurance Segment

The weighted average effective duration of our portfolio of fixed maturity securities, at March 31, 2013, is 4.4 years compared to 4.0 years at December 31, 2012.

### Life Insurance Segment

The weighted average effective duration of our portfolio of fixed maturity securities, at March 31, 2013 is 4.2 years compared to 4.0 years at December 31, 2012.

### 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. Our net investment income decreased 9.2 percent in the three-month period ended March 31, 2013, compared with the same period of 2012, due to historically low yields that reduce our investment income and margin on earnings. We are maintaining our investment philosophy of purchasing investments rated investment grade or better, and we are more closely matching the duration of our investment portfolio to our liabilities.

We continually monitor the difference between our cost basis and the estimated fair value of our investments. Our accounting policy for impairment recognition requires other-than-temporary impairment 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 and losses 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 March 31, 2013, 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 charges in future periods on securities that we own at March 31, 2013, 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

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assets to provide protection from future credit quality issues and corresponding other-than-temporary 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 the receipt of premiums, annuity deposits, reinsurance recoveries, sales or maturities of investments, and investment income. Cash provided from these sources is used to fund the payment of losses and loss settlement expenses, policyholder benefits under life insurance contracts, annuity withdrawals, the purchase of investments, 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.

The following table displays a summary of cash sources and uses in 2013 and 2012.

| Cash Flow Summary<br>(In Thousands)       | Three Months Ended March 31, |            |
|---|------------------------------|------------|
|   | 2013                         | 2012       |
| Cash provided by (used in)                |                              |            |
| Operating activities                      | \$31,744                     | \$35,885   |
| Investing activities                      | (13,151)                     | (101,238)  |
| Financing activities                      | (24,111)                     | (5,174)    |
| Net decrease in cash and cash equivalents | \$(5,518)                    | \$(70,527) |

**Operating Activities**

Net cash flows provided by operating activities totaled \$31.7 million and \$35.9 million for the three-month periods ended March 31, 2013 and 2012, respectively. The decrease reflects a higher level of property and casualty loss payments, which were partially offset by a higher level of property and casualty premiums collected.

Our cash flows from operations were sufficient to meet our liquidity needs for the three-month periods ended March 31, 2013 and 2012.

**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, \$1.2 billion, or 43.8 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 March 31, 2013, our cash and cash equivalents included \$52.3 million related to these money market accounts, compared to \$45.6 million at December 31, 2012.

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Net cash flows used in investing activities totaled \$13.2 million and \$101.2 million for the three-month periods ended March 31, 2013 and 2012, respectively. For the three-month period ended March 31, 2013, we had cash inflows from scheduled and unscheduled investment maturities, redemptions, prepayments, and sales of investments that totaled \$130.8 million compared to \$155.0 million for the same period in 2012.

Our cash outflows for investment purchases totaled \$143.5 million for three-month period ended March 31, 2013, compared to \$255.3 million for the same period in 2012. In 2013, we continued to purchase a higher level of fixed maturity securities, which are more profitable than other categories of investments when market interest rates are low.

### Financing Activities

Net cash flows used in financing activities totaled \$24.1 million for the three-month period ended March 31, 2013 compared to net cash flows used in financing activities of \$5.2 million for the three-month period ended March 31, 2012. The increase was primarily due to higher net annuity withdrawals in the three-month period ended March 31, 2013 compared to the same period of 2012.

### Credit Facilities

In December 2011, United Fire entered into a credit agreement with a syndicate of financial institutions as lenders, KeyBank National Association as administrative agent, lead arranger, sole book runner, swingline lender, and letter of credit issuer, and Bankers Trust Company as syndication agent. As of March 31, 2013, there were no balances outstanding under this credit agreement. For further discussion of our credit agreements, refer to Part 1, Item 1, Note 8 "Debt."

### Stockholders' Equity

Stockholders' equity increased 4.0 percent to \$758.1 million at March 31, 2013, from \$729.2 million at December 31, 2012. The increase was primarily attributable to net income of \$22.4 million and an increase in net unrealized investment gains of \$8.6 million during the first quarter ended March 31, 2013, net of tax, which was partially offset by stockholder dividends of \$3.8 million. At March 31, 2013, the book value per share of our common stock was \$30.01, compared to \$28.90 at December 31, 2012.

### Off-Balance Sheet Arrangements

Pursuant to an agreement with one of our limited liability partnership investments, we are contractually committed through December 31, 2017, to make capital contributions upon request of the partnership. Our obligation was \$4.2 million at March 31, 2013.

## MEASUREMENT OF RESULTS

Our consolidated financial statements are prepared on the basis of GAAP. We also prepare financial statements for each of our insurance subsidiaries based on statutory accounting principles and file them with insurance regulatory authorities in the states where they do business.

Management evaluates our operations by monitoring key measures of growth and profitability. We believe that disclosure of certain non-GAAP financial measures enhances investor understanding of our financial performance. The following sections provide further explanation of the key measures management uses to evaluate our results.

Premiums written is a statutory measure of our overall business volume. Premiums written is an important measure of business production for the period under review. 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,

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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.

| (In Thousands)                            | Three Months Ended March 31, |           |
|---|------------------------------|-----------|
|   | 2013                         | 2012      |
| Net premiums written                      | \$191,232                    | \$179,380 |
| Net change in unearned premium            | (14,670 )                    | (14,806 ) |
| Net change in prepaid reinsurance premium | 255                          | (3,071 )  |
| Net premiums earned                       | \$176,817                    | \$161,503 |

Combined ratio is a commonly used statutory financial measure of property and casualty 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. We use the net loss ratio as a measure of the overall underwriting profitability of the insurance business we write and to assess the adequacy of our pricing. Our net loss ratio is meaningful in evaluating our financial results as reported in our Consolidated Financial Statements

When prepared in accordance with GAAP, the underwriting expense ratio is calculated by dividing nondeferred underwriting expenses and amortization of deferred policy acquisition costs by net premiums earned. The underwriting expense ratio measures a company's operational efficiency in producing, underwriting and administering its insurance business.

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



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Catastrophe losses is a commonly used non-GAAP financial measure that uses 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, 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. 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.

| (In Thousands)                      | Three Months Ended March 31, |          |
|-------------------------------------|------------------------------|----------|
|                                     | 2013                         | 2012     |
| ISO catastrophes                    | \$4,511                      | \$13,988 |
| Non-ISO catastrophes <sup>(1)</sup> | —                            | 110      |
| Total catastrophes                  | \$4,511                      | \$14,098 |

(1) This number includes international assumed losses.

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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 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. 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 March 31, 2013, we did not hold investments in sub-prime mortgages, credit default swaps, or other credit-enhancement exposures.

While our primary market risk exposure is to changes 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 what we reported in our Annual Report on Form 10-K for the year ended December 31, 2012.

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, has 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.

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## PART II - OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

We consider all our litigation pending as of March 31, 2013, to be ordinary, routine, and incidental to our business.

## ITEM 1A. RISK FACTORS

Our business is subject to a number of risks, including those identified in Part I, Item 1A of our 2012 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 4, 2013, 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.

## 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, general economic and market conditions, and corporate and regulatory requirements.

We are authorized to purchase 1,129,720 shares of common stock at March 31, 2013. Our share repurchase program is scheduled to end in August 2014.

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 March 31, 2013.

| Period               | Total<br>Number of<br>Shares Purchased | Average Price<br>Paid per Share | Total Number of Shares<br>Purchased as a Part of<br>Publicly Announced<br>Plans or Programs | Maximum Number of<br>Shares that may be<br>Purchased Under the<br>Plans or Programs |
|----------------------|--|---------------------------------|---|---|
| 1/1/2013 - 1/31/2013 | —                                      | \$—                             | —   | 1,129,720   |
| 2/1/2013 - 2/28/2013 | —                                      | —                               | —   | 1,129,720   |
| 3/1/2013 - 3/31/2013 | —                                      | —                               | —   | 1,129,720   |

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. MINE SAFETY DISCLOSURES

None.

## ITEM 5. OTHER INFORMATION

None.

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## 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 Group, Inc.'s Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 formatted in XBRL: (i) Consolidated Balance Sheets at March 31, 2013 (unaudited) and December 31, 2012; (ii) Consolidated Statements of Income and Comprehensive Income (unaudited) for the three months ended March 31, 2013 and 2012; (iii) Consolidated Statement of Stockholders' Equity (unaudited) for the three months ended March 31, 2013; (iv) Consolidated Statements of Cash Flows (unaudited) for the three months ended March 31, 2013 and 2012; and (v) Notes to Unaudited Consolidated Financial Statements, tagged as a block of text | X              |

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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 GROUP, INC.  
(Registrant)

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

May 8, 2013  
(Date)

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

May 8, 2013  
(Date)