BOENNING & SCATTERGOOD
ESTABLISHED 1914

Pennsylvania Insurance Department

REVIEW AND ANALYSIS REGARDING THE HARLEYSVILLE MUTUAL INSURANCE COMPANY PROPOSED MERGER WITH NATIONWIDE MUTUAL INSURANCE COMPANY

As of November 10, 2011
REPORT DATE:
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FINANCIAL ADVISOR:
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[redacted]

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[redacted]

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[redacted]

XXI. Boenning & Scattergood, Inc. Engagement Letter

[redacted]

Section I

Introduction and Overview

A. Scope of the Assignment

Boenning & Scattergood, Inc. ("***Boenning***" or "***we***" or "***our***") was engaged by the Pennsylvania Insurance Department (the "***Department***") as a financial advisor to assist the Department in its review of the proposed merger ("***Transaction***") of Harleysville Group, Inc. ("***HGIC***" or "***Harleysville Group***") and Harleysville Mutual Insurance Company ("***Harleysville Mutual***" or "***HMIC***") (collectively, HGIC and Harleysville Mutual are referred to as the ("***Company***")[1]), with Nationwide Mutual Insurance Company ("***Nationwide***" , "***Applicant***" or "***Transaction Partner***") and specifically in connection with issuing a report ("***Report***") and conclusions as to the Harleysville Mutual's Board of Directors determination that the Transaction was fair and reasonable, and conferred benefits to the Harleysville Mutual policyholders ("***Policyholders***"). The date of the Report is March 26, 2012 ("***Report Date***") and, except as otherwise noted herein, the Report is based upon the materials available to and Boenning's information gathering on or before, February 10, 2012 ("***Information Date***")[2]. Pursuant to an engagement letter between Boenning and the Department dated November 18, 2011, and amendments dated November 21, 2011, and February 15, 2012, (collectively, the "***Engagement Letter***"), Boenning was engaged to provide certain services to the Department as more fully set forth therein.

We understand the Department is reviewing the Transaction pursuant to 40 P.S. § 991.1402 (the "***Act***" or "***Section 991.1402***") and possibly other applicable laws. We further understand that the relevant portions of the Act provide, in pertinent part, as follows:

> *"(f)(1) The department shall approve any merger, consolidation or other acquisition of control referred to in subsection (a) unless it finds any of the following:*
>
> *(i) After the merger, consolidation or other acquisition of control, the domestic insurer referred to in subsection (a) would not be able to satisfy the requirements for the issuance of a license to write the line or lines of insurance for which it is presently licensed.*
>
> *(ii) The effect of the merger, consolidation or other acquisition of control would be to substantially lessen competition in insurance in this Commonwealth or tend to create a monopoly therein. In applying the competitive standard in this subparagraph:*

[1]Noted in quoted text throughout the Report the term "Company" may refer to Harleysville Mutual or the collective entity.

[2]Subsequent to the Information Date, Boenning held additional conversations with the Company and its Advisors to clarify or confirm data previously provided. In addition, Harleysville Mutual provided its response to the Department's comment letter on the PIS.

(A) the informational requirements of section 1403(c)(2) and the standards of section 1403(d)(2) shall apply;

(B) the merger, consolidation or other acquisition of control shall not be disapproved if the department finds that any of the situations meeting the criteria provided by section 1403(d)(3) exist; and

(C) the department may condition the approval of the merger, consolidation or other acquisition of control on the removal of the basis of disapproval within a specified period of time.

(iii) The financial condition of any acquiring party is such as might jeopardize the financial stability of the insurer or prejudice the interest of its policyholders.

(iv) The plans or proposals which the acquiring party has to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make any other material change in its business or corporate structure or management, are unfair and unreasonable and fail to confer benefit on policyholders of the insurer and are not in the public interest.

(v) The competence, experience and integrity of those persons who would control the operation of the insurer are such that it would not be in the interest of policyholders of the insurer and of the public to permit the merger, consolidation or other acquisition of control.

(vi) The merger, consolidation or other acquisition of control is likely to be hazardous or prejudicial to the insurance buying public.

(vii) The merger, consolidation or other acquisition of control is not in compliance with the laws of this Commonwealth, including Article VIII-A."

This Report is being provided for use by the Department in complying with its duties under applicable law, including the Act. Boenning anticipates the Department will use this Report in fulfilling those obligations, including the Department's obligations under Sections 991.1402(f)(1)(iv) and (vi).

B. Assumptions, Qualifications, Limitations and Conditions

The Report should be read in its entirety. The Report and the contents hereof are subject to all the assumptions, qualifications, limitations and conditions set forth (a) in this Section and elsewhere in this Report and (b) in the Engagement Letter.

1. Boenning has been engaged by the Department to act solely as a financial advisor to and agent of the Department. In connection with this engagement, Boenning has not been engaged to act in any other capacity or for any other reason or to provide any additional advice in connection with the Transaction or other transactions or matters contemplated thereby or related, directly or indirectly, thereto.
2. Boenning is a financial advisor and has been engaged and has acted solely as a financial advisor and based upon the perspective of a financial advisor. As a result, this Report and the conclusions and analysis contained herein are being offered by Boenning solely in its role as and within the scope of a financial advisor and from a financial advisor's point of view, and all such conclusions and analysis are so qualified. Further, any conclusions, observations or advice of Boenning offered or qualified from a "financial point of view" shall mean from a financial advisor's point of view. Boenning is not a law firm, accounting firm, actuarial firm, or employee compensation benefits consultant, is not acting as such and is not otherwise providing any legal, accounting, actuarial or compensation advice. Accordingly, neither this Report, any of the conclusions or analysis contained herein nor any other service rendered in connection with the Engagement Letter shall constitute or be deemed to constitute legal, accounting, employee compensation, or any other type of professional or other conclusion, analysis, advice or service, other than conclusions, analysis, advice and services a financial advisor would provide in the ordinary course from a financial advisor's point of view.
3. Boenning is not acting as a fiduciary of any person or entity, including, without limitation, the Department or any party to or any person or entity affected, directly or indirectly, by the Transaction or any other transactions or matters contemplated thereby or related, directly or indirectly, thereto.
4. The Report has been made only for the purpose expressly stated herein and in the Engagement Letter and shall not be deemed made or used for any other purpose.
5. The services resulting in this Report were undertaken in reliance on those terms and conditions set forth herein and in the Engagement Letter, all of which are incorporated herein by reference and made a part of this Report. By accepting delivery of this Report, the Department acknowledges that the Report fully and completely satisfies and discharges all of Boenning's duties and obligations arising under or in connection with the Engagement Letter.

6. This Report is being provided to the Department solely to assist the Department with (a) its review of the Transaction and (b) satisfaction of the Department's other duties under applicable law.
7. This Report is being provided to the Department for its sole and exclusive use, and nothing contained in this Report was prepared or intended to benefit any other person or entity, including, without limitation, any party to or any person or entity affected, directly or indirectly, by the Transaction or any other transactions or matters contemplated thereby or related, directly or indirectly, thereto. No person or entity, other than the Department, may rely on this Report or any of the conclusions or analysis set forth herein. Nevertheless, the Department, at its option, may make the Report available to the public, upon request, and may distribute copies, in its entirety subject to those redactions the Department deems necessary or appropriate to preserve confidentiality. The Department has agreed to inform Boenning in writing if such requests are made.
8. No investigation has been made of, and no responsibility is assumed for, the legal description of any property or entity being valued or any related legal matters, including title or encumbrances. Title to such property or entity is assumed to be good and marketable unless otherwise stated. All such property and any such entity is assumed to be free and clear of any liens, easements or encumbrances unless otherwise stated.
9. Information furnished by others, upon which all or any portion of the conclusions or analysis contained herein is based, is believed to be reliable, but has not been verified except as expressly set forth in the Report. No representation or warranty, express or implied, is given in this Report, including, without limitation, as to the accuracy of such information.
10. Except as expressly set forth in the Engagement Letter, neither Boenning, any of its officers, directors, employees, representatives or agents, nor any person or entity signing or associated with this Report or the preparation thereof shall be required by reason of the Report, the Engagement Letter or any matter in connection therewith, to provide further services, give further consultation, provide testimony, or appear in court or other legal proceeding.

11. It is assumed that all required licenses, certificates of occupancy, consents, or other legislative or administrative authority from any local, state, or national government or private entity or organization have been or can readily be timely obtained or renewed.
12. Full compliance with all applicable federal, state and local zoning, use, environmental and similar laws and regulations is assumed, unless otherwise stated.
13. Competent management is assumed.
14. This Report and the conclusions and analysis set forth herein have been based upon and are intended to be governed by the law of the Commonwealth of Pennsylvania without taking into account the choice or conflicts of law of that or any other jurisdiction.
15. Neither this Report nor any of the conclusions or analysis set forth herein were shared with or relied upon by any of the parties to the Transaction or other transactions or matters contemplated thereby or related, directly or indirectly, prior to the Report Date.
16. This engagement and services provided pursuant to and in connection with the Engagement Letter were undertaken after the parties entered into the Transaction and other transactions or matters contemplated thereby or related, directly or indirectly, thereto, and assumes that all such transactions and matters or another transaction would be entered into by Harleysville Mutual or HGIC.
17. Boenning was not requested to consider whether either Harleysville Mutual or HGIC should enter into this Transaction or any other transactions or matters contemplated thereby or related, directly or indirectly, thereto, or any other transaction.
18. Neither this Report nor all or any part of the contents hereof may be referred to or quoted in any way in any registration statement, prospectus, draft preliminary Harleysville Mutual Policyholder Information Statement dated December 23, 2011 and filed with the Department ("***PIS***"), Proxy Statement, including a proxy statement of HGIC ("***Proxy***") or similar document of any party to the Transaction or any other person or entity, without Boenning's prior written consent.
19. Boenning did not perform an independent evaluation of the pro forma market values of any party to the Transaction or any other person or entity. Accordingly, the Report does not express an opinion on the market value of any such party, person or entity. Additionally, the Report does not express any opinion on the prices at which shares of

any party, affiliation thereof, or any person or entity may trade at any time in the future.

20. Except as expressly set forth in this Report, this Report and conclusions and analysis set forth herein are based upon (a) the Transaction and other transactions or matters contemplated thereby or related, directly or indirectly, thereto and (b) facts and circumstances, including the financial structure of the parties to the Transaction, in each case that existed as of November 10, 2011 ("***Evaluation Date***"). Except as expressly set forth in this Report, the matters being evaluated on the Evaluation Date are based on financial information available as of June 30, 2011. Therefore, the conclusions and analyses set forth in this Report do not necessarily reflect the most recent financial information and portions of this Report may contain information for the period discussed at that point in the Report, in which case there has been no attempt to compare the information Boenning used with other information available as of the Information Date.

21. Our conclusions are based on the purchasing power of the U.S. Dollar as of the Evaluation Date.

22. Boenning has not been requested to and has not undertaken to update or revise this Report after the Information Date, including, without limitation, to reflect or account for any information, facts or circumstances occurring or that become known after the Information Date. No responsibility is taken for changes in market conditions.

23. The Report is not a recommendation and should not be construed as a recommendation to purchase or sell securities, obligations, policies or any other instrument of HGIC, Harleysville Mutual, the Transaction Partner, any affiliate of any of them, or any other person or entity. The Report is not a fairness opinion to the Policyholders or any other person, entity or constituency.

C. Summary of the Transaction and Process

A general discussion of the materials reviewed and procedures utilized by Boenning is set forth in the Appendix to this Report.

Leading up to the Transaction, the Company's Boards of Directors ("***Boards of Directors***" if referring to both entities comprising the Company or "***Harleysville Mutual Board of Directors***" or

"***HGIC Board of Directors***" if referring to one entity only) considered and rejected several transaction alternatives more fully described in Section V. As stated in the PIS and confirmed in discussions with management, the Company's Boards of Directors authorized Credit Suisse Securities (USA) LLC ("***Credit Suisse***"), its financial advisor, to solicit indications of interest from potential acquirers for a transaction in which the following objectives were sought (in no particular order):

- Maximize value to public stockholders
- Protect and enhance policyholders' position
- Provide opportunities for employees
- Preserve the culture of Harleysville
- Continue to grow the franchise

As a result of the solicitation process managed by Credit Suisse, the Company held serious discussions with three potential partners, ultimately with the Transaction Partner submitting the only formal bid by the end of the solicitation process.

On November 10, 2011, the Department received the Transaction Partner's Form A "Statement Regarding the Acquisition of Control of or Merger With a Domestic Insurer" filing dated November 10, 2011 (the "***Application***" or "***Form A***") and on or about December 23, 2011 the Department received a draft of the PIS. The Application and PIS: (i) contain significant amounts of information describing the Company, the Transaction Partner and the Transaction; (ii) are discussed more fully in Sections IV and V herein; and, (iii) should be read in connection with the Report.

A description of the process of the Transaction is explained in Item 1. "Insurer and Method of Acquisition" of the Application. A summary of the Agreement and Plan of Merger (the "***Merger Agreement***") from the Application is reproduced below:

> *"The Applicant proposes to acquire control of the Domestic Insurers pursuant to the Agreement and Plan of Merger (the "Merger Agreement") by and among Harleysville Mutual, HGIC, the Applicant and Merger Sub dated as of September 28, 2011, a copy of which is attached to this Statement as Exhibit 1. Under the terms of the Merger Agreement, (i) Harleysville Mutual will merge with and into Applicant, with Applicant continuing as the surviving entity (the "Parent Merger"), and (ii) immediately after the Parent Merger, the Merger Sub will merge with and into HGI, with HGI surviving as a wholly-owned subsidiary of Applicant (the "Subsidiary Merger," and together with the Parent Merger, the "Mergers").*
>
> *As a result of the Parent Merger, Harleysville Mutual policyholders will become policyholders of Applicant, and Harleysville Life and Harleysville Pennland will become*

wholly-owned subsidiaries of Applicant. Harleysville Life and Harleysville Pennland will remain Pennsylvania-domiciled insurance companies.

As a result of the Subsidiary Merger, HGI will become a wholly-owned subsidiary, and the HGI Domestic Insurers will become indirect subsidiaries, of Applicant. The HGI Domestic Insurers will remain Pennsylvania-domiciled insurance companies. The Subsidiary Merger will include conversion of each share of common stock of HGI not owned by Harleysville Mutual into the right to receive $60.00 payable in cash (collectively, the "Acquired Shares").”

According to the Merger Agreement, the mergers of Harleysville Mutual with and into Nationwide and Nationwide’s Merger Subsidiary (“***Merger Sub”)*** with and into HGIC will occur almost simultaneously. If either one of the mergers is not approved, neither transaction will occur.

- Harleysville Mutual will merge with and into Nationwide with Nationwide continuing as the surviving entity (the "***Parent Merger***")
- Immediately after the Parent Merger, the Merger Sub will merge with and into HGIC, with HGIC surviving as a wholly-owned subsidiary of Applicant (the "***Subsidiary Merger***")

Each transaction is mutually contingent on the other and both are encompassed in the Transaction as referred to throughout the Report. According to the Merger Agreement, Policyholders of Harleysville Mutual will become policyholders of the Transaction Partner. Stockholders of HGIC (other than Harleysville Mutual) will receive $60.00 per share in cash.

The Boards of Directors concluded separately that the Transaction Partner’s Transaction was, in totality and considering all stated objectives, in the best interests of, and fair to Harleysville Mutual and HGIC stockholders. The Boards of Directors also believed that potential benefits of the Transaction discussed by their respective advisors included improved size and financial strength, additional products for agents and Policyholders, commitment to employees, independent agents and community.

The Boards of Directors separately received opinions and advice from independent (external) advisors identified below (collectively the “***Advisors***”) experienced in matters relating to the Transaction:

Table 1) Advisor Summary

Legal Advisor	Advice / Opinion Addressing
Ballard Spahr LLP	Counsel to the Harleysville Mutual
Fox Rothschild LLP	Counsel to HGIC
Stevens & Lee, P.C.	Fiduciary duties of Harleysville Mutual directors

Financial Advisor	Advice Addressing
Credit Suisse Securities (USA) LLC	Strategic alternatives analysis and financial advisor to the Company
Griffin Financial Group LLC	Fairness to Harleysville Mutual
Keefe, Bruyette & Woods, Inc.	Fairness to HGIC public stockholders

D. Boenning's Analysis in the Context of the Act Standards

Although any part of the Report may be potentially relevant to any factor the Department may wish to consider in reviewing the Transaction under applicable law, for ease of review and at the request of the Department, Boenning offers the following summary as to potential applicability under the Act.

Act Citation	Methodologies Used	Relevant Report Sections
(iv) The plans or proposals which the acquiring party has to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make any other material change in its business or corporate structure or management, are unfair and unreasonable and fail to confer benefit on policyholders of the insurer and are not in the public interest.	Reviewed Form A and related documents regarding post-Transaction impact on Policyholders, agents and other constituents.	Section IV
	Reviewed analysis and advice rendered by the Advisors regarding strategic alternatives and potential Transaction benefits to Harleysville Mutual, HGIC, Policyholders, the community and other constituents; created alternative analysis where possible.	Section V
	Reviewed: i) comparisons of Policyholders' rights between Harleysville Mutual and Nationwide, ii) comparison of Harleysville Mutual and Nationwide from a financial point of view, and iii) benefits conferred upon Policyholders	Section VII

Act Citation	Methodologies Used	Relevant Report Sections
(vi) The merger, consolidation or other acquisition of control is likely to be hazardous or prejudicial to the insurance buying public.	Reviewed Form A and related documents regarding post-Transaction impact on Policyholders and agents.	Section IV
	Reviewed analysis and advice rendered by the Advisors regarding potential Transaction benefits to Policyholders, agents and other constituents.	Sections V.A and V.B
	Reviewed: i) comparisons of Policyholders' rights between Harleysville Mutual and Nationwide, ii) comparison of Harleysville Mutual and Nationwide from a financial point of view, and iii) benefits conferred upon Policyholders	Section VII

E. Summary of Boenning's Conclusions

As more fully described above, the Engagement Letter required Boenning to produce this written Report. This Report is for the sole use and benefit of the Department in assisting it to determine whether the Transaction complies with applicable law and meets the standards of the Act, including whether (a) the plans or proposals of Nationwide are unfair and unreasonable and fail to confer a benefit on Policyholders of Harleysville Mutual (Section 991.1402(f)(1)(iv)) and (b) the Transaction is likely to be hazardous or prejudicial to the insurance buying public (Section 991.1402(f)(1)(vi)). In preparing this Report, Boenning reviewed the factors considered by the Company, the methodologies it used, the assumptions it made, and the reasonableness from a financial point of view of the factors, methodologies and assumptions used by the Advisors and the Harleysville Mutual's Board of Directors in "determining that the proposed Merger was fair and reasonable, and conferred benefits to the Harleysville Mutual policyholders" as stated in the Applicant's response to the Department's PIS comments.

Each Section of this Report includes a description of the issues examined, analysis reviewed and conducted, and conclusions drawn from the topic to which each Section was devoted. In reaching its conclusions, Boenning examined the topics listed in its Engagement Letter. Boenning reviewed analyses prepared by the Company, its Advisors and/or the Transaction Partner, all as more fully set forth herein. Where possible and deemed appropriate by Boenning, Boenning conducted its own analysis to determine the reasonableness of one of the Company's, or its Advisors' conclusions.

Specifically, in its review of the Transaction, Boenning examined the following items:

- Harleysville Mutual Business and Background – Boenning analyzed Harleysville Mutual, its financial condition and background to the Transaction to provide context for its analysis of the Transaction *(primarily found in Sections II – IV)*
- Form A and other filings – Boenning reviewed filings provided by the Department, offered comments on the content and suggestions for changes or additional information to be included *(primarily found in Section IV)*

- Transaction Analysis – Boenning reviewed the analysis and advice rendered by the Company's Advisors. In some cases, Boenning was able to complete its own version of certain quantitative analysis to confirm or illustrate the correctness of the Company's Advisors conclusions. The Transaction analysis also included an examination of potential director conflicts and economics in the Transaction *(primarily found in Sections V – VI)*
- Policyholder's rights – Boenning reviewed analysis comparing the rights of Policyholders before and after the Transaction. This analysis also included a comparison of Nationwide and Harleysville Mutual *(primarily found in Section VII)*
- Voting agreement – Boenning examined the Voting Agreement and issues relating to its appropriateness in the Transaction *(primarily found in Section VIII)*

After examining each issue and reviewing the analysis and reasoning supporting each topic, Boenning concluded whether or not Harleysville Mutual's Board of Directors determination that the proposed Merger was fair and reasonable, and conferred benefits to the Policyholders, was correct from a financial point of view.

Additionally, Boenning specifically notes that:

- The Company's analysis (including that of its Advisors), taken as a whole, appeared thorough and complete
- Assumptions used appeared reasonable
- Independent experts were utilized and advice/recommendations appeared to be followed and/or supported or appeared to support the Boards of Directors' decisions
- Analysis completed by Advisors, taken as a whole, appeared to be complete and thorough
- The Company's Boards of Directors were advised by legal Advisors. The Boards of Directors therefore appeared to act consistently with such legal advice
- The Company analyzed the Transaction from the points of view of multiple constituencies and that analysis appeared thorough and complete
- The Company's analysis of the Transaction indicates that that the Transaction does not appear to be unfair or unreasonable, nor does it fail to confer benefit on Policyholders. Further, it does not appear to be not in the public interest
- The Company's analysis of the Transaction indicates that the Transaction does not appear to be hazardous or prejudicial to the insurance buying public

Section II

The Company Business Description

Boenning's Engagement Letter with the Department included the following:

> "(a) Assemble such financial and other information on the Company from Boenning's information request list as Boenning deems necessary or appropriate."
>
> "(c) Conduct due diligence on the Company in order to review historical financial results, financial projections, various corporate information and other information as Boenning deems necessary or appropriate."

In accordance with its customary procedures, Boenning conducted the following:

- Formal Information Request to the Company and its Advisors
- Meeting(s) with management to discuss operations and financial condition
- Analysis of non-public, confidential, and proprietary documentation in the Company's Data Room ("***Data Room***") (under obligation of confidentiality)
- Analysis of other non-public and publicly available information

The following information is provided as a general introduction to the Company. Section III of the Report focuses on Harleysville Mutual's financial information and analysis. Selected financial information analyzed in the Report was compiled by SNL Financial LC ("***SNL Financial***") a leading provider of financial and market data focused on the financial services industry.

A. Business Description

Harleysville Mutual is a property and casualty (***"P/C"***) insurer founded in 1917 and based in Harleysville, PA. Harleysville Mutual's primary lines of business include commercial multiple peril, commercial auto liability, private passenger auto, homeowners, and workers' compensation.

HGIC was formed in 1979 to to facilitate regional expansion in subsidiary operations. In 1986, HGIC sold stock in its initial public offering in an effort to raise growth capital. Harleysville Mutual's structure, a mutual insurance company owning a controlling interest in a public company (HGIC), is relatively rare among the nation's insurers. Management and its Advisors estimate that it is one of only four companies (the other three being State Auto Insurance Co., EMC Insurance Group Inc., and Donegal Group Inc.) with a similar structure.

Throughout the 1980's and 1990's, the Company made acquisitions to expand its footprint into new geographical locations in the U.S. In 2001, the Company announced the decision to consolidate all the individual companies under the "Harleysville" name in order to:

- Better convey the overall organization's size, stability, and financial strength

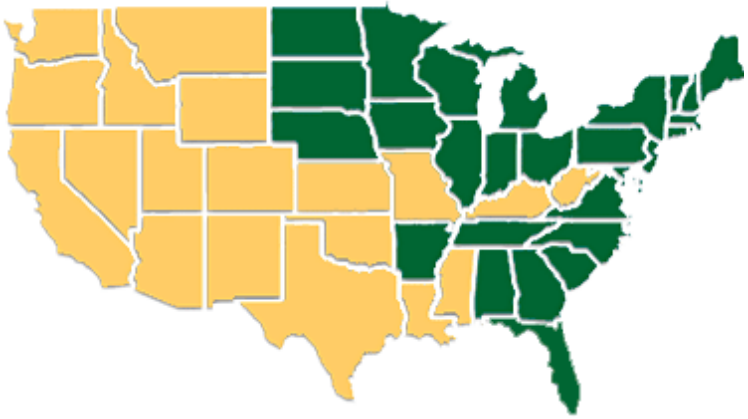
- Unify Harleysville's brand
- Position the Company more prominently in the small commercial marketplace

Harleysville Mutual and HGIC operate under an inter-company pooling agreement and share some common directors, common management and operations. The designated focus of Harleysville Mutual is commercial property insurance and the majority of premiums are written in the eastern U.S. Harleysville Mutual is licensed in 47 states with the exclusion of Arizona, New York, and Wyoming. In addition, the Company is a qualified/accredited reinsurer in the state of New York.

Table 2) Top 5 States by Premium

Harleysville Mutual Top 5 States by Premium	
NY	21.7%
PA	18.0%
NJ	13.1%
MA	5.8%
VA	4.6%

Shown in green are the states representing a principal concentration of premiums of the Company:



Currently, the Company's network is represented by approximately 1,700 employees and 1,300 agencies, and provides a variety of insurance-related products and services, including property & casualty and life insurance.

B. Business Strategy

The following is the confidential and proprietary business strategy statement from the Company:

[redacted]

[redacted]

[redacted]

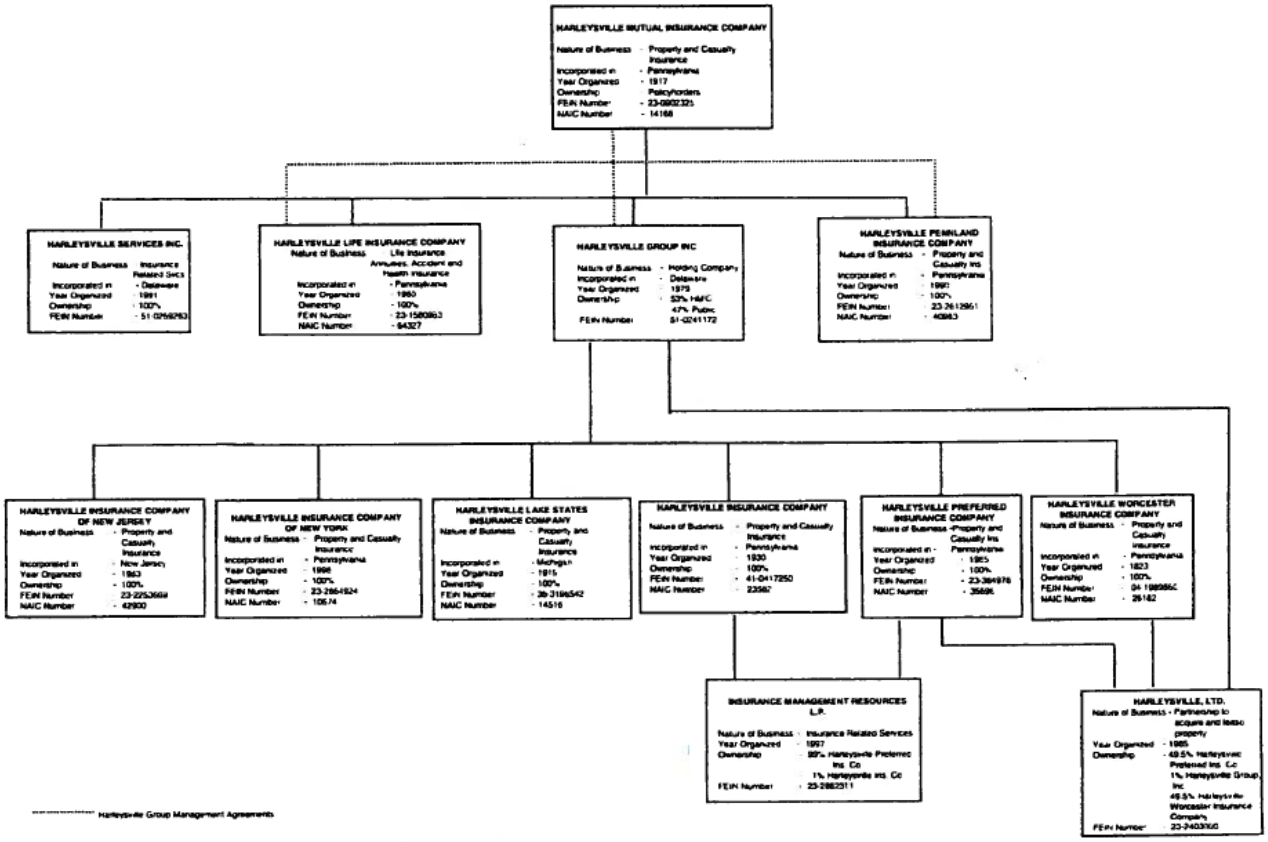
[redacted]

[redacted]

[redacted]

C. Organization

The following is the current organizational chart for the Company:



Source: Company

D. Executive Officer Biographies

The following executives are referred to by Boenning as the Company's management throughout the Report.

Michael L. Browne (*President & CEO, 64*)

Michael L. Browne was elected a director of Harleysville Group in 1986 and served as its non-executive chairman of the Board in 2003. In 2003, he was also elected as a director and appointed as the non-executive chairman of the Board of Harleysville Mutual. He held such nonexecutive chairman of the Board positions until he was appointed as chief executive officer of Harleysville Group and president and chief executive officer of Harleysville Mutual in February 2004. In January

2005, Mr. Browne was appointed president of Harleysville Group. Mr. Browne served on active duty in the U.S. Marine Corps from 1968-1971, was a Marine infantry platoon leader in Vietnam, and attained the rank of captain. From 1975 to 1977, he was special assistant to U.S. Secretary of Transportation, William T. Coleman, Jr., and from 1976 to 1977, he also served as U.S. Deputy Under Secretary of Transportation. From 1980 to 1983, Mr. Browne was the Insurance Commissioner of the Commonwealth of Pennsylvania. In 1983, he joined the law firm of Reed Smith LLP as an equity partner. Mr. Browne was the managing partner of its Delaware Valley regional office from 1993 until 2001, when he became head of Reed Smith's international insurance practice, a position he held until 2004. Mr. Browne currently is a member of the Board of Trustees of The Institutes, the Board of Directors of the Property Loss Research Bureau, the Board of Governors of the Property Casualty Insurers Association of America, the Board of Directors of the Insurance Federation of Pennsylvania, and the Board of Directors of Insurance Information Institute. He was a member of the Board of Directors of Harleysville National Corporation from 2008 to 2009.

Allan R. Becker (*SVP & Chief Actuary, 52*)

Allan R. Becker became senior vice president and chief actuary of Harleysville Group and Harleysville Mutual in October 2005. Before joining Harleysville, he was vice president and senior actuary for ACE USA. During his 18 years with ACE USA and its predecessor CIGNA Property and Casualty, Mr. Becker held a variety of actuarial management roles. He holds the FCAS and MAAA designations.

Arthur E. Chandler (*SVP & CFO, 54*)

Arthur E. Chandler was named senior vice president and chief financial officer in April 2005. Prior to that, he was senior vice president of financial controls for XL America, and he had been chief financial officer for Kemper Insurance's casualty division. Mr. Chandler also spent nearly 20 years with CIGNA in various financial positions.

Thomas E. Clark (*SVP, Field Operations, 50*)

Thomas E. Clark was named senior vice president for Harleysville Group and Harleysville Mutual in charge of branch and subsidiary operations in March 2004. Before that, he was in charge of branch operations and had been resident vice president for the New Jersey operations of

Harleysville Group and Harleysville Mutual since July 2000. From 1995 through 2000, he worked for Fireman's Fund Insurance Company as a business segment leader.

Mark R. Cummins (*EVP, CIO & Treasurer, 54*)

Mark R. Cummins is executive vice president, chief investment officer, and treasurer of Harleysville Group and Harleysville Mutual and has been in charge of the investment and treasury function since 1992.

Beth A. Friel (*SVP, Human Resources and SVP, Claims, 37*)

Beth A. Friel was appointed senior vice president, human resources for Harleysville Group and Harleysville Mutual in February 2009 and as senior vice president, claims in January 2012. She joined Harleysville in August 2006 as assistant vice president and assistant general counsel and served as vice president, human resources from April 2008 until February 2009. Before that, Ms. Friel was an attorney in the labor and employment department of the law firm of Montgomery, McCracken, Walker & Rhoads, LLP.

Arnold F. Herenstein (*SVP, Chief Information Officer, 63*)

Arnold F. Herenstein became senior vice president and chief information officer of Harleysville Group and Harleysville Mutual in July 2011. Prior to joining Harleysville, he was vice president of information technology at OneBeacon Insurance in Massachusetts.

Robert A. Kauffman (*SVP, Secretary, General Counsel & CCO, 47*)

Robert A. Kauffman has been senior vice president, secretary, and general counsel of Harleysville Group and Harleysville Mutual since November 2004. In February 2009, he was named chief compliance officer. Before joining Harleysville, he had been a stockholder in the securities litigation department of the law firm Berger & Montague. Prior to that, Mr. Kauffman was an equity partner in the law firm of Reed Smith LLP in Philadelphia. He also served as an Assistant U.S. Attorney in the criminal and asset forfeiture divisions of the U.S. Attorney's Philadelphia office.

Theodore A. Majewski (*SVP, Personal Lines; President and COO of HLIC, 59*)

Theodore A. Majewski was named senior vice president, personal lines for Harleysville Group and Harleysville Mutual in June 2003. Mr. Majewski also was appointed president and chief operating officer of Harleysville Life Insurance Company in April 2008. Prior to joining Harleysville, Mr. Majewski was, among other senior management positions, the chief underwriting director of Encompass Insurance Company (formerly CNA).

Kevin M. Toth (*SVP & Chief Underwriting Officer, 37*)

Kevin M. Toth was appointed senior vice president and chief underwriting officer of Harleysville Group and Harleysville Mutual in February 2009. He joined Harleysville in January 2005 as vice president, associate general counsel, and chief litigation counsel and served as senior vice president, claims for Harleysville Group and Harleysville Mutual from July 2005 until February 2009. Before that, Mr. Toth was an attorney in the litigation department of the law firm of Reed Smith LLP.

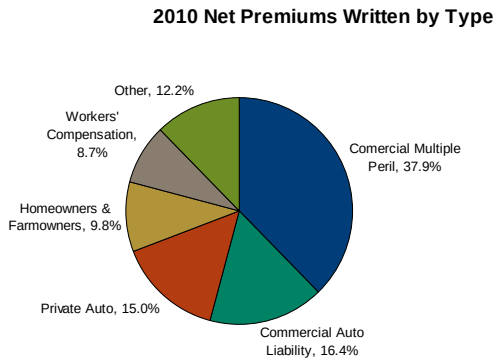
[redacted]

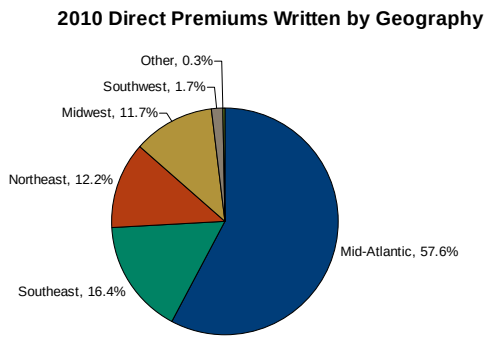
E. Business Segments

The Company underwrites a broad line of personal and commercial property and casualty coverages, including automobile, homeowners, commercial multi-peril and workers compensation. Harleysville Mutual and its insurance subsidiaries participate in an inter-company pooling arrangement under which HGIC's insurance subsidiaries and Harleysville Mutual and its property and casualty insurance subsidiary, Harleysville Pennland Insurance Company ("***Pennland***"), combine their property and casualty business.

The following chart illustrates the diversification of the Company's business lines and the volume of premiums written by geographic location. The Company offers numerous insurance products including but not limited to business, flood, human services (professional liability coverage, abuse or molestation coverage, loss of income coverage, broadened commercial auto coverage), life, non-profit, personal, and workers' compensation.

Table 3) Company 2010 Premiums Data





Source: SNL Financial

Table 4) Company 2010 Premiums by State

2010 Direct Premiums Written by State by Type ($000)										
	States									
P&C Business	**PA**	**VA**	**FL**	**MD**	**SC**	**TX**	**NC**	**GA**	**Other**	**Total**
Commercial Multiple Peril	165,234	57,462	51,266	26,528	18,841	12,934	9,245	15,079	89,108	**445,698**
Commercial Auto: State	45,552	39,380	44,223	11,843	10,681	9,467	6,938	7,672	49,857	**225,613**
Fire and Allied Lines Combined	10,392	9,543	21,860	5,040	4,546	2,007	7,168	1,693	78,055	**140,304**
Private Auto: State	4,251	50,756	1,005	5,498	7,726	8,556	3,772	2,868	43,971	**128,402**
Homeowners & Farmowners	14,491	27,010	12,313	16,308	5,020	5,585	3,720	1,628	31,199	**117,274**
Workers' Compensation	7,814	27,323	23,210	2,480	7,048	2,945	3,361	3,829	22,214	**100,224**
Other and Product Liability Lines Combined	20,383	9,855	7,810	3,723	2,994	1,542	1,804	1,501	17,480	**67,093**
Marine Lines Combined	4,865	4,766	2,548	1,751	1,027	868	717	797	12,981	**30,319**
Other Commercial	117	148	85	110	121	30	44	5	175	**834**
Fidelity & Surety	0	2	6	2	9	0	0	0	10	**29**
Total	**273,099**	**226,246**	**164,326**	**73,284**	**58,012**	**43,933**	**36,769**	**35,073**	**345,050**	**1,255,791**

Source: SNL Financial

Note: Graphs and table above represent the Company at the combined entity reporting level.
This is the combined P&C group which files a combined filing with the NAIC.

F. Reinsurance

The Company follows the customary industry practice of reinsuring a portion of its exposures and paying to reinsurers a portion of the premiums received. Insurance is ceded principally to reduce the net liability on individual risks and to protect against catastrophic losses. Ceded reinsurance contracts do not relieve the Company's primary obligation to its Policyholders. Consequently, for reinsurance arrangements that are not fully collateralized, an exposure exists with respect to reinsurance recoverable to the extent that any reinsurer is unable to meet its obligation or disputes the liability assumed under the reinsurance contract. From time to time, the Company may encounter such disputes with its reinsurers. In addition, the creditworthiness of reinsurers could deteriorate in the future due to adverse events affecting the reinsurance industry, such as a large

number of major catastrophes. The following table lists the Company's top 10 reinsurance relationships:

Table 5) Company Reinsurance Receivables Data

Harleysville Insurance Companies Reinsurance Receivables – Combined Basis* ($ in thousands)	
Reinsurer	As of December 31, 2011
Michigan Catastrophe Claims Association	$93,384
National Flood Insurance Program	$54,424
Munich Reinsurance America	$54,416
New Jersey Unsatisfied Claim & Judgment Fund	$21,812
Swiss Reinsurance America Corporation	$17,330
American States Insurance Company (Liberty Mutual)	$14,306
Lloyds of London	$12,874
General Reinsurance Corporation (Berkshire Hathaway)	$7,962
Continental Casualty Company (CNA)	$7,724
Hannover Ruchversicherungsa AG	$7,312
* Includes current recoverables and ceded reserves	

Source: Company

G. Distribution

The Company is dedicated to the independent agent channel and manages its agent relationships via its regional offices and its corporate office.

The following table lists Harleysville Mutual's top 25 agencies in terms of premiums written:

Table 6) Harleysville Mutual Top 25 Largest Agencies

[redacted]

[redacted]

The level of concentration in regard to Policyholders does not appear to be a major risk factor for Harleysville Mutual. In 2010, the distribution of premiums was not disproportionately concentrated in a small number of Policyholders. It appears the risk associated from the loss of a large Policyholder is minimal with no single Policyholder having premiums above $2 million.

The following table lists Harleysville Mutual's top 25 Policyholders by class in terms of total premiums.

Table 7) Harleysville Mutual Top 25 Policyholders by Class

SICX	Branch	Primary Stab. Multi State	Total Prem.	Premium Concentration
4213 – Trucking, Except Local	[redacted]		$1,820,519	10.32%
6513 –Operators of Apartment Buildings	[redacted]		1,123,933	6.37
6513 –Operators of Apartment Buildings	[redacted]	*	846,400	4.80
1799- Special Trade Contractors, NEC	[redacted]	*	812,633	4.60
4213-Trucking, Except Local	[redacted]		774,558	4.39
5147-Meats and Meat Products	[redacted]	*	727,826	4.12
6531-Real Estate Agents and Managers	[redacted]	*	723,167	4.10
6513-Operators of Apartment Buildings	[redacted]		719,290	4.08
5812-Eating Places	[redacted]		685,361	3.88
4212-Local Trucking Without Storage	[redacted]		670,860	3.80
5013-Motor Vehicle Supplies and New Parts	[redacted]	*	653,592	3.70
6513 –Operators of Apartment Buildings	[redacted]		653,184	3.70
6513 –Operators of Apartment Buildings	[redacted]		623,408	3.53
6513 –Operators of Apartment Buildings	[redacted]		612,487	3.47
6513 –Operators of Apartment Buildings	[redacted]	*	604,882	3.43
5148-Fresh Fruits and Vegetables	[redacted]		588,246	3.33
6513 –Operators of Apartment Buildings	[redacted]		588,052	3.33
6531-Real Estate Agents and Managers	[redacted]		578,529	3.28
2671-Packaging Paper and Plastics Film, Coated and Laminated	[redacted]	*	576,903	3.27
6513 –Operators of Apartment Buildings	[redacted]		562,852	3.19
5983-Fuel Oil Dealers	[redacted]		562,353	3.19
4213-Trucking, Except Local	[redacted]	*	552,778	3.13
3273-Ready-Mix Concrete	[redacted]		532,653	3.02
1522-General Contractors-Residential Buildings, Other than Single Family	[redacted]		532,351	3.02
5075-Warm Air Healing and Air Conditioning Equip. & Supplies	[redacted]	*	521,350	2.95
			$17,648,167	

[redacted]

H. Competition

The property and casualty insurance industry is highly competitive on the basis of both price and service. There are numerous companies competing for the categories of business underwritten by the Company in the geographic areas where the Company operates, some of which are substantially larger and have considerably greater financial resources than the Company. In addition, because the insurance products of the Company are marketed exclusively through independent insurance agencies, most of which represent more than one company, the Company faces competition within each agency.

The following is a list of competitors of the Company:

- Auto-Owners Insurance Co.
- ACUITY, A Mutual Insurance Company
- Cincinnati Insurance Co.
- Selective Insurance Group, Inc.
- State Auto Insurance Companies
- Donegal Group Inc.
- Grange Property & Casualty Insurance Co.
- Hanover Insurance Group, Inc.
- United Fire & Casualty Co.
- Westfield Insurance Company
- EMC Insurance Group Inc.

Source: Company's A.M. Best report dated 2/9/2011

I. Investment Portfolio

An important element of the financial results of the Company is the return on invested assets. An investment objective of the Company is to maintain a widely diversified fixed maturities portfolio structured to maximize after-tax investment income, while minimizing credit risk through investments in high quality instruments. The Company has adopted and follows an investment philosophy which precludes the purchase of non-investment grade fixed income securities. However, due to uncertainties in the economic environment, it is possible that the quality of investments held in the Company's portfolio may change, as a result of which the Company may hold some non-investment grade securities. Harleysville Mutual also owns approximately 54% of HGIC. This "investment" has resulted in approximately $230 million in dividends since 1986.

Management estimates that the dividends plus investment earnings on those dividends contributed significantly to Harleysville Mutual's December 31, 2010 surplus (after accounting for taxes).

Note: Except as otherwise expressly stated in this Section II, the source for all information in this Section II is publicly available information as of the Evaluation Date.

Section III

Harleysville Mutual Financial Information

Boenning's Engagement Letter with the Department included the following:

> "(a) Assemble such financial and other information on the Company from Boenning's information request list as Boenning deems necessary or appropriate."
>
> "(c) Conduct due diligence on the Company in order to review historical financial results, financial projections, various corporate information, and other information as Boenning deems necessary or appropriate."

Boenning's due diligence review of Harleysville Mutual's business and operations consisted primarily of the following:

- Formal information requests to Harleysville Mutual and its Advisors
- Meeting(s) with management to discuss operations and financial condition
- Analysis of non-public, confidential, and proprietary documentation in Harleysville Mutual's Data Room (under obligation of confidentiality)
- Analysis of other non-public and publicly available information

A. Operating Results

Provided below is an overview and analysis of Harleysville Mutual's financial results and position as of the November 10, 2011 Application date based on September 30, 2011 financials. The following 2 pages represent Harleysville Mutual's historical financial statements.

Table 8) Harleysville Mutual Financial Summary – Income Statement and Balance Sheet

Income Statement-Harleysville Mutual (SNL P&C Group)

	2002	2003	2004	2005	2006	2007	2008	2009	2010	LTM 9/30/2011
Direct Premiums Written	**$1,214,724**	**$1,247,153**	**$1,253,150**	**$1,260,858**	**$1,256,911**	**$1,273,334**	**$1,245,488**	**$1,192,969**	**$1,255,791**	**$1,351,933**
		(3%)	*(0%)*	*(1%)*	*0%*	*(1%)*	*2%*	*4%*	*(5%)*	*(8%)*
Net Premiums Written	**1,131,916**	**1,187,995**	**1,179,102**	**1,181,085**	**1,165,033**	**1,156,981**	**1,148,146**	**1,073,126**	**1,095,532**	**1,159,076**
		(5%)	*1%*	*(0%)*	*1%*	*1%*	*1%*	*7%*	*(2%)*	*(6%)*
Losses and LAE	**779,436**	**1,060,778**	**855,145**	**790,103**	**752,545**	**729,196**	**768,277**	**691,930**	**747,698**	**944,754**
		(36%)	*19%*	*8%*	*5%*	*3%*	*(5%)*	*10%*	*(8%)*	*(26%)*
Other Underwriting Expenses Incurred	**393,430**	**410,632**	**395,028**	**410,417**	**403,736**	**398,546**	**391,354**	**381,822**	**390,682**	**401,987**
		(4%)	*4%*	*(4%)*	*2%*	*1%*	*2%*	*2%*	*(2%)*	*(3%)*
Net Underwriting Gain / (Loss)	**(40,950)**	**(283,415)**	**(71,072)**	**(19,435)**	**8,753**	**29,239**	**(11,485)**	**(626)**	**(42,849)**	**(187,666)**
Investment Income										
Net Investment Income	119,483	142,397	123,749	129,740	160,824	158,243	153,993	146,550	147,899	172,899
Net Realized Capital Gain / (Loss)	(50,890)	(5,855)	56,876	3,506	53,913	35,797	(49,956)	(5,450)	(3,779)	9,715
Other Income	**(1,806)**	**824**	**1,006**	**1,988**	**3,250**	**1,973**	**1,926**	**2,627**	**2,277**	**(6,684)**
Total Revenue	**1,198,702**	**1,325,360**	**1,360,734**	**1,316,320**	**1,383,021**	**1,352,994**	**1,254,109**	**1,216,853**	**1,241,929**	**1,335,006**
		(11%)	*(3%)*	*3%*	*(5%)*	*2%*	*7%*	*3%*	*(2%)*	*(7%)*
Net Income	**$22,067**	**($125,885)**	**$98,795**	**$97,600**	**$196,017**	**$175,757**	**$58,817**	**$108,000**	**$80,248**	**$1,710**

Source: SNL Financial (P&C Group Level)

For the years ended December 31, with the exception of 9/30/2011 which is last twelve months (LTM)

Balance Sheet-Harleysville Mutual (SNL P&C Group)

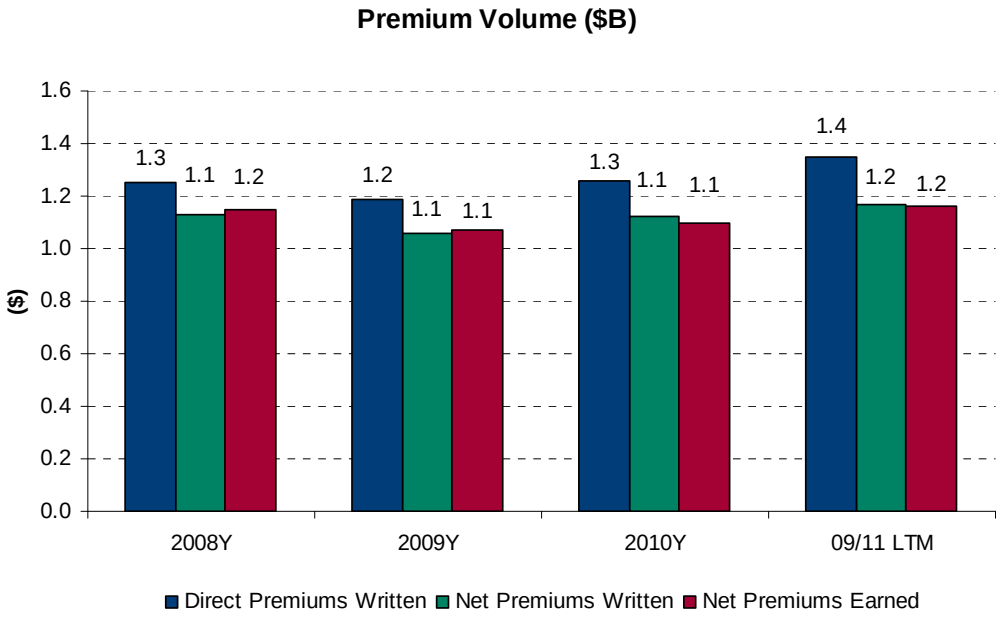
	2002	2003	2004	2005	2006	2007	2008	2009	2010	LTM 9/30/2011
Assets										
Investments:										
Bonds	$1,921,233	$2,164,297	$2,226,061	$2,451,945	$2,835,744	$2,973,699	$2,804,569	$3,033,652	$3,013,527	$2,832,967
Preferred Stocks	36	0	0	0	0	0	0	0	0	0
Common Stocks	260,425	312,648	337,469	372,792	281,058	281,805	212,777	320,871	470,366	497,094
Mortgage Loans	350	294	0	0	0	0	0	0	0	0
Real Estate	6,454	4,751	5,131	5,013	4,878	888	888	888	888	888
Contract Loans	0	0	0	0	0	0	0	0	0	0
Cash & Short Term Investments	356,823	374,154	333,907	347,395	295,437	310,816	239,566	99,426	55,615	145,843
Other Investments	38,780	37,920	38,065	50,066	37,663	37,348	43,820	65,787	37,613	37,187
Total Cash & Investments	**2,584,101**	**2,894,063**	**2,940,634**	**3,227,210**	**3,454,781**	**3,604,556**	**3,301,621**	**3,520,624**	**3,578,010**	**3,513,979**
Premiums and Considerations Due	337,856	338,672	365,159	368,395	367,053	351,677	330,667	342,179	339,209	349,584
Reinsurance Recoverable	16,603	20,802	39,394	26,460	19,289	14,606	36,105	25,511	24,750	25,265
Receivable from Parent, Subsidiary or Affiliates	24,222	45,420	9,063	15,820	14,562	14,247	4,097	7,802	8,551	8,852
All Other Admitted Assets	88,347	106,200	81,193	87,880	111,720	107,623	138,865	121,515	121,492	122,569
Total Assets	**$3,051,129**	**$3,405,157**	**$3,435,442**	**$3,725,765**	**$3,967,404**	**$4,092,710**	**$3,811,355**	**$4,017,631**	**$4,072,013**	**$4,020,249**
Liabilities										
Loss Reserves	1,043,034	1,274,081	1,330,493	1,443,604	1,528,960	1,572,541	1,592,086	1,595,230	1,589,513	1,673,413
Loss Adjustment Expense Reserves	237,770	287,877	315,552	339,611	378,433	404,009	413,419	408,590	416,093	433,021
Total Loss & LAE Reserves	**1,280,804**	**1,561,959**	**1,646,045**	**1,783,215**	**1,907,392**	**1,976,550**	**2,005,506**	**2,003,820**	**2,005,605**	**2,106,433**
Unearned Premium Reserve	557,226	568,530	568,098	564,585	564,578	571,479	553,849	545,245	567,289	586,065
Total Reinsurance Liabilities	17,706	17,451	58,330	58,651	42,713	33,451	46,266	57,322	38,058	28,141
Commissions, Other Expenses, and Taxes due	88,437	88,144	84,265	97,200	95,083	90,163	85,686	86,441	80,349	47,998
Payable to Parent, Subs or Affiliates	25,615	44,634	9,029	16,644	16,281	17,682	10,799	10,041	8,230	10,356
All Other Liabilities	309,145	392,316	275,526	324,718	308,078	332,139	53,104	137,306	112,061	60,405
Total Liabilities	**$2,278,932**	**$2,673,033**	**$2,641,293**	**$2,845,014**	**$2,934,126**	**$3,021,464**	**$2,755,210**	**$2,840,176**	**$2,811,593**	**$2,839,398**
Capital and Surplus (SE)										
Common Capital Stock	19,490	21,385	21,357	21,258	21,339	18,398	19,018	35,464	34,313	34,313
Surplus Notes	3,000	0	0	0	0	0	0	0	0	0
Unassigned Surplus	700,954	656,032	718,173	805,186	957,379	1,001,194	983,604	1,085,549	1,168,951	1,085,879
Other Including Gross Contributed	48,752	54,707	54,619	54,308	54,561	51,655	53,523	56,442	57,156	60,659
Capital & Surplus	772,196	732,124	794,149	880,752	1,033,278	1,071,246	1,056,145	1,177,454	1,260,420	1,180,851
Total Liabilities and C&S	**$3,051,129**	**$3,405,157**	**$3,435,442**	**$3,725,765**	**$3,967,404**	**$4,092,710**	**$3,811,355**	**$4,017,631**	**$4,072,013**	**$4,020,249**

Source: SNL Financial (P&C Group Level)

For the years ended December 31, with the exception of 9/30/2011 which is last twelve months (LTM)

Harleysville Mutual underwrites personal and commercial property and casualty coverages, including automobile, homeowners, commercial multi-peril and workers compensation. For the LTM period ending 9/30/2011, Harleysville Mutual reported direct premiums written of $1.35 billion which represented 8.98% growth over the LTM period one year prior. During the LTM period, the Mid-Atlantic region accounted for the greatest percentage of direct premiums written at 60.5%. Additionally, the product line of Harleysville Mutual representing the greatest share of direct premiums written in the LTM period was commercial multi-peril at 37.4%.

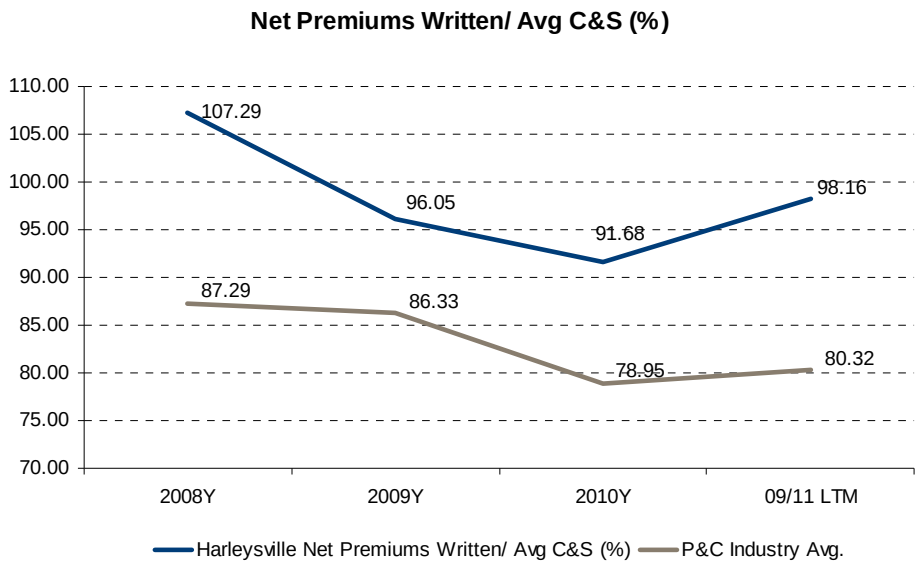
Table 9) Harleysville Mutual Premium Volume



Source: SNL Financial

Net Premiums Written/Avg. Capital and Surplus is a common operating ratio in the P/C insurance industry to measure a firm's capital efficiency. While Harleysville Mutual experienced a decline from 2008 to 2010, the ratio increased in the LTM period due to reduced capital & surplus from natural disaster losses. These historically low levels of operating leverage can be attributed to under-deployment of capital, as well as excess capital building.

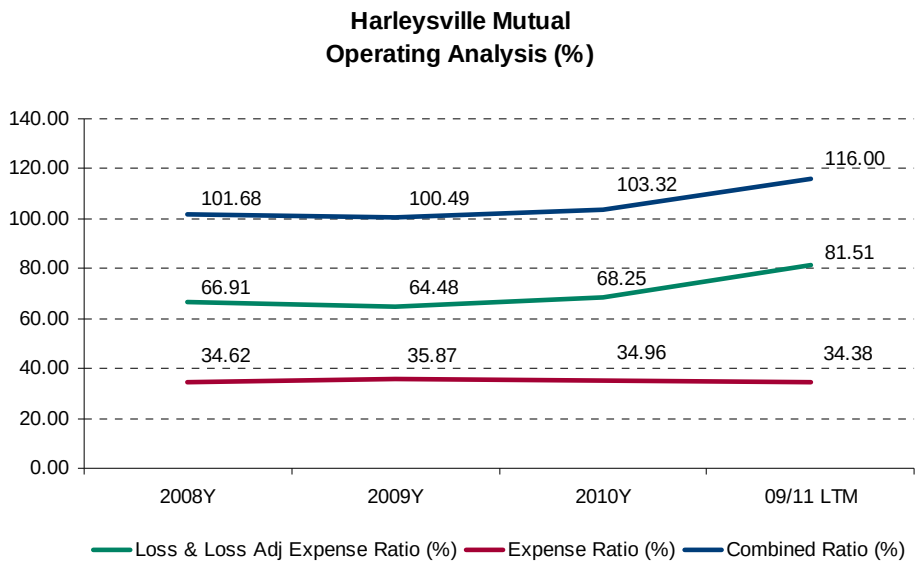
Table 10) Harleysville Mutual NPW/Avg Capital and Surplus



Source: SNL Financial

Harleysville Mutual experienced a significant rise in combined ratio from the 2010 to the LTM period. This rise was caused by an increase in loss and loss adjustment expense ratio as the expense ratio was essentially flat over the period being compared. During 2011, catastrophe losses contributed to the spike in Loss and Loss Adjusted Expense ratio experienced by Harleysville Mutual. The LTM combined ratio of 116.00% is significantly higher than the P/C industry average of 108.89%. Harleysville Mutual along with the broader P/C industry has faced a multi-year period of price competition and heightened level of catastrophes and other weather related losses leading to higher (some would say unsustainable) combined ratios. The U.S. set a record in 2011 in its declarations of federal disasters, which included both Hurricane Irene and the EF-5 tornado that struck Joplin, Missouri.

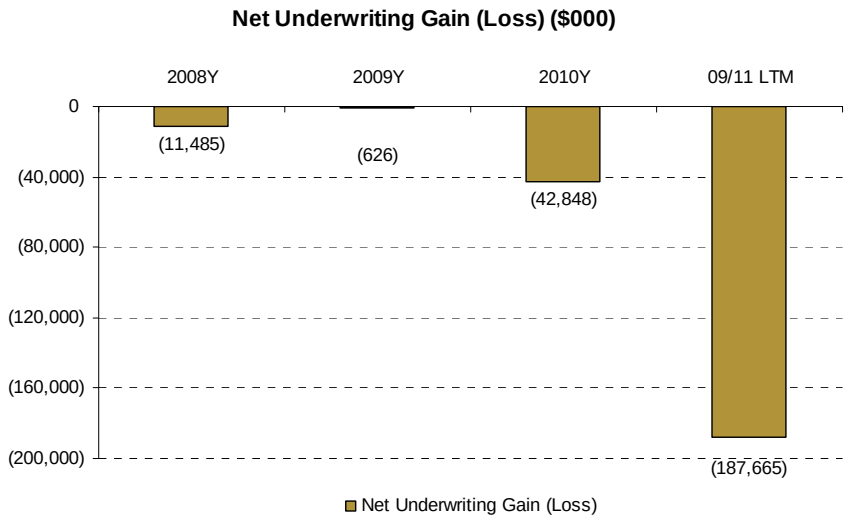
Table 11) Harleysville Mutual Operating Analysis



Source: SNL Financial

Harleysville Mutual has reported negative net underwriting profits since 2008 with the LTM period showing severe losses relative to historical levels. These LTM losses directly correlated to the major natural catastrophes which impacted the P/C industry in 2011. Analysts say catastrophes, including Hurricane Irene, which made landfall in North Carolina in August and then lashed the U.S. East Coast with rain and winds, cost the industry $9.5 billion in the third quarter of 2011. Additionally, P/C industry analysts predicted that Harleysville Mutual would have to change capital modeling that would result in greater capital requirements relative to premiums, and also that domestic geographic diversification would become increasingly important.

Table 12) Harleysville Mutual Net Underwriting Gain/Loss



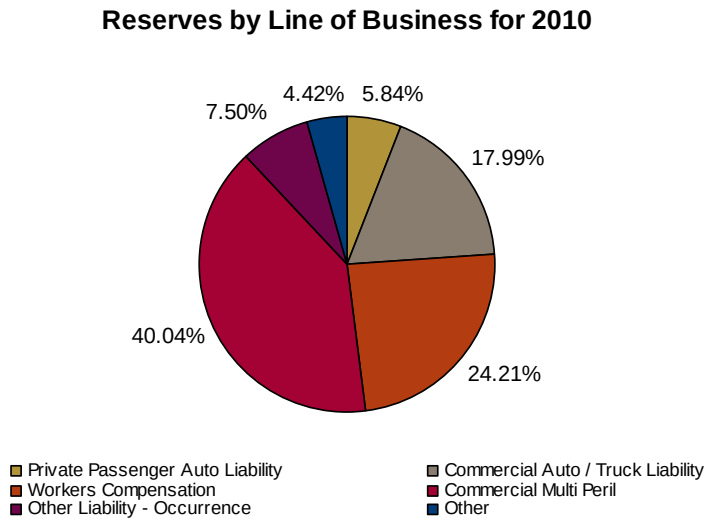
Source: SNL Financial

Table 13) Harleysville Mutual Reserve Analysis

Reserve Analysis (%)	2008 Y	2009 Y	2010 Y
1 Yr Loss Reserve Development / NPE	(3.17)	(3.81)	(4.98)
Change in Loss and LAE Reserves / Reserves	1.46	(0.08)	0.09
1 Yr Loss Reserve Dev / 1Y Prior C&S	(3.39)	(3.87)	(4.63)
IBNR / Total Reserves	45.00	45.95	46.20
Reserves / C&S	189.89	170.18	159.12

Source: SNL Financial

Table 14) Harleysville Mutual Reserves by Line of Business



Source: SNL Financial and statutory financials schedule P

B. A.M. Best Financial Strength Rating

A.M. Best is a widely recognized rating agency dedicated to the insurance industry. A.M. Best provides ratings (the "***Best's Rating***") that indicate the financial strength of insurance companies. The objective of A.M. Best's rating system is to provide an independent opinion of an insurer's financial strength and its ability to meet ongoing obligations to policyholders. The assigned rating is derived from an evaluation and analysis of a company's balance sheet strength, operating performance, and business profile. The Best's Rating's scale is comprised of 15 individual ratings grouped into 9 categories (excluding suspended ratings). The Best's Rating may be an important factor affecting the Company's ability to attract new business from customers and producers.

Best Capital Adequacy Ratio ("***BCAR***") is the ratio of adjusted surplus to net required capital, as determined by A.M. Best. BCAR provides an integrated evaluation of a company's investment, credit, and underwriting risk as it compares with a company's level of economic surplus. Harleysville Mutual's BCAR rating impacts its overall Best's Rating. A.M. Best's guidelines state

that a BCAR ratio of at least 175 implies a balance sheet strength rating of A++, the highest of such ratings. As of April 29, 2011, Harleysville Mutual's BCAR ratio was 309.6.

In its most recent report, A.M. Best cited the following in regard to its rating:

"Rating Rationale: The rating applies to the group's 10-member intercompany pool, led by Harleysville Mutual Insurance Company. The rating is based on the consolidated operating performance and financial condition of these pool participants. The rating reflects Harleysville's excellent level of risk-adjusted capitalization, sound operating performance over the long term, and strong regional market franchise. The group also benefits from the financial flexibility afforded through its publicly traded holding company, Harleysville Group Inc. (HGIC). These rating factors are partially offset by the consolidated pre-tax return on revenue measures, which slightly trail the commercial casualty composite over the long term reflective of variability in reported underwriting income given exposure to weather-related events, as well as the near-term challenges associated with the highly competitive property/casualty environment and ongoing soft market conditions.

HGIC maintains an 80% participation in the results of the pool, excluding the company's assumed catastrophe reinsurance program. Taking into consideration HGIC's capital management in recent years, which included continued significant common share repurchases, the company's financial leverage remains modest with debt-to-total capital of approximately 13% at December 31, 2010.

Harleysville's positive attributes reflect its focused underwriting discipline, commitment to conservative reserving, and prudent management of catastrophe exposures. Results also benefit from the group's strong name recognition and solid market presence. The rating also acknowledges the benefits being derived from the group's predictive modeling initiatives, which should benefit results going forward. Harleysville Insurance ranks among the top 70 property/casualty insurance organizations in the United States. The group emphasizes small to middle-market commercial accounts as well as personal lines.

Harleysville's underwriting results remain susceptible to catastrophes given the group's exposure to weather conditions directly correlated to the group's East Coast and Midwest business focus. While the group has initiated corrective actions intended to lower costs while enhancing operating efficiencies, its underwriting expense ratio remains more than six points above the commercial casualty peer composite. While the loss and loss adjustment expense (LAE) ratio has increased during the period, the measure has outperformed the peer composite during the five-year period, which partially offsets the elevated expense ratio."

A.M. Best assigned a Best's Rating of "A" (Excellent) to Harleysville Mutual effective April 29, 2011. An "A" rating is the third highest achievable rating on A.M. Best's 15 level rating scale, as stated on A.M. Best's website. The category of "Excellent" represents the second highest achievable of 9 rating categories (excluding the suspended rating). Insurance companies rated "A" are considered by A.M. Best to have "an excellent ability to meet their ongoing insurance

obligations" to policyholders. Boenning also notes the improvement in Harleysville Mutual's rating from an "A-" to "A" during a period from 2006 to 4/2011 (a period marked by numerous economic challenges and unprecedented natural disasters).

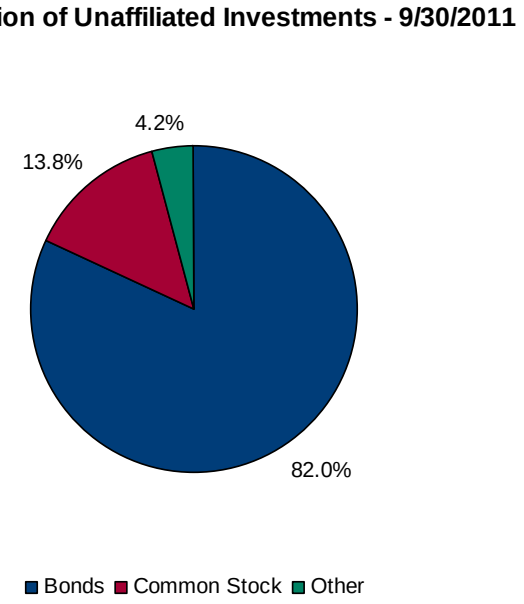
Table 15) Harleysville Mutual AM Best Ratings

A.M. Best Financial Strength Rating	
Date	Harleysville Mutual
4/29/2011	A
4/27/2010	A
2/4/2009	A-
1/17/2008	A-
12/14/2006	A-
5/9/2006	A-

C. Investment Overview

According to SNL Financial, as of September 30, 2011, the Harleysville Mutual investment portfolio had a book value of approximately $3.46 billion and was comprised mainly of bonds at 82.0% of the portfolio. The bond maturities range from less than 1 year to greater than 20 years with the majority being less than 5 years (53.9%). Long-term bonds with a maturity greater than 20 years make up only 0.4% of the bond total. The effective duration of the bond portfolio is 4.80 years as of February 9, 2011. The balance of the investment portfolio consists of common stock and other invested assets. Harleysville Mutual owns 14,526,445 shares of HGIC which had a carrying value of $339.4 million on 9/30/2011 and are carried in the common equity portfolio.

Table 16) Harleysville Mutual Investment Composition



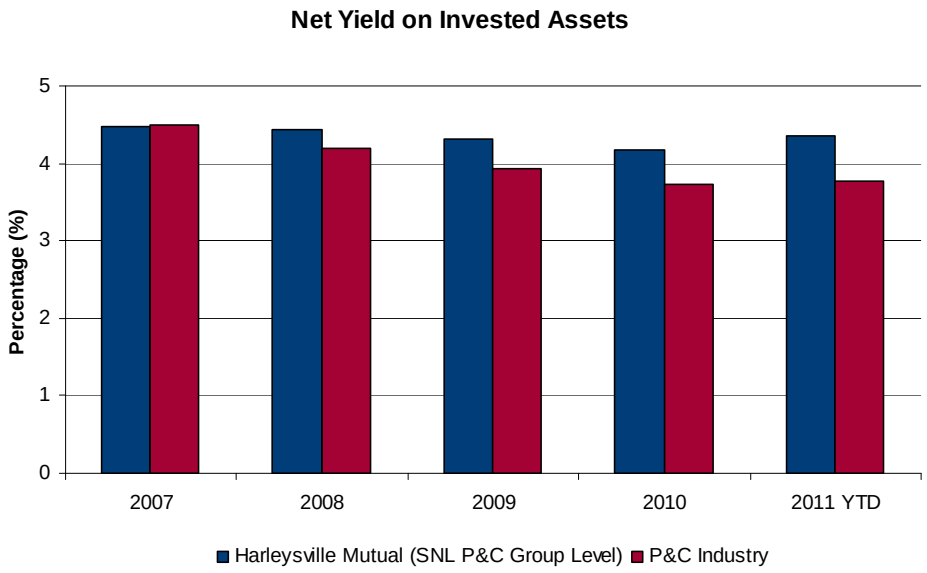
Source: SNL Financial

Harleysville Mutual Insurance Company Investment Portfolio Composition (%)					
Year Ended	12/31/2006	12/31/2007	12/31/2008	12/31/2009	12/31/2010
Total Cash & Investments	3,454,781	3,604,556	3,301,621	3,520,624	3,578,010
Affiliated Cash & Investments	23,655	21,197	56,530	56,374	56,396
Unaff. Bonds / Unaff. Investments	82.64	82.98	86.42	87.57	85.56
Unaff. Preferred Stocks / Unaff. Investments	0.00	0.00	0.00	0.00	0.00
Unaff. Common Stocks / Unaff. Investments	7.50	7.27	5.93	8.69	12.80
Unaff. Mortgage Loans / Unaff. Investments	0.00	0.00	0.00	0.00	0.00
Real Estate / Unaff. Investments	0.14	0.02	0.03	0.03	0.03
Contract Loans / Unaff. Investments	0.00	0.00	0.00	0.00	0.00
Unaff. Cash & Short Term / Unaff. Investments	8.61	8.67	7.38	2.87	1.58
Unaff. Other Investments / Unaff. Investments	1.10	1.05	0.24	0.84	0.03

Source: SNL Financial

Harleysville Mutual has outperformed the P/C industry average net yield on invested assets from 2008 to the year to date period, ended 9/30/2011 (according to SNL Financial), as can be seen on the bar graph below:

Table 17) Harleysville Mutual Net Yield on Invested Assets



Source: SNL Financial

Harleysville Mutual has a diversified bond portfolio with a blend of maturities skewed to the short-term as mentioned above. The Fitch ratings for the bonds held by Harleysville Mutual range from AAA to AA- which shows the conservative, safe, and low yield nature of these investments. Moreover, the majority of the issuers of these bonds fall under the categories:

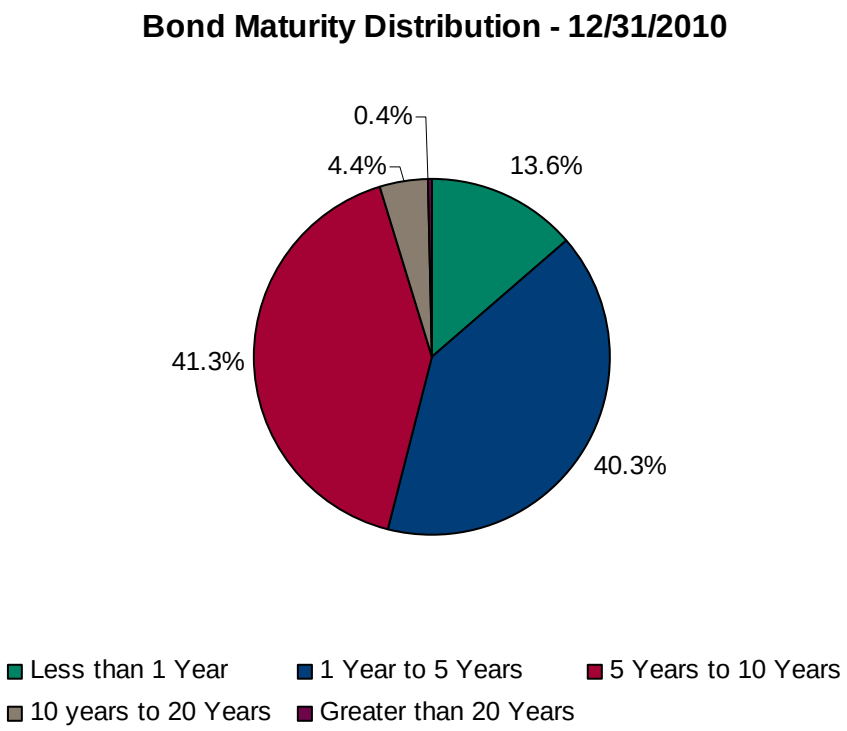
- Government Agency
- US States
- US Federal Government

Other bonds held by Harleysville Mutual include corporate issues by companies such as Colgate Palmolive Co., DuPont, and the United Parcel Service.

Table 18) Harleysville Mutual Bond Maturity

Year Ended	12/31/2006	12/31/2007	12/31/2008	12/31/2009	12/31/2010
< 1 Year / Total Bonds	13.14	18.56	20.07	14.73	13.55
1 - 5 Years / Total Bonds	41.96	40.62	40.78	41.26	40.33
5 - 10 Years / Total Bonds	39.09	37.52	36.62	37.22	41.34
10 - 20 Years / Total Bonds	5.01	2.79	2.19	6.42	4.40
> 20 Years / Total Bonds	0.79	0.51	0.35	0.37	0.38

Source: SNL Financial



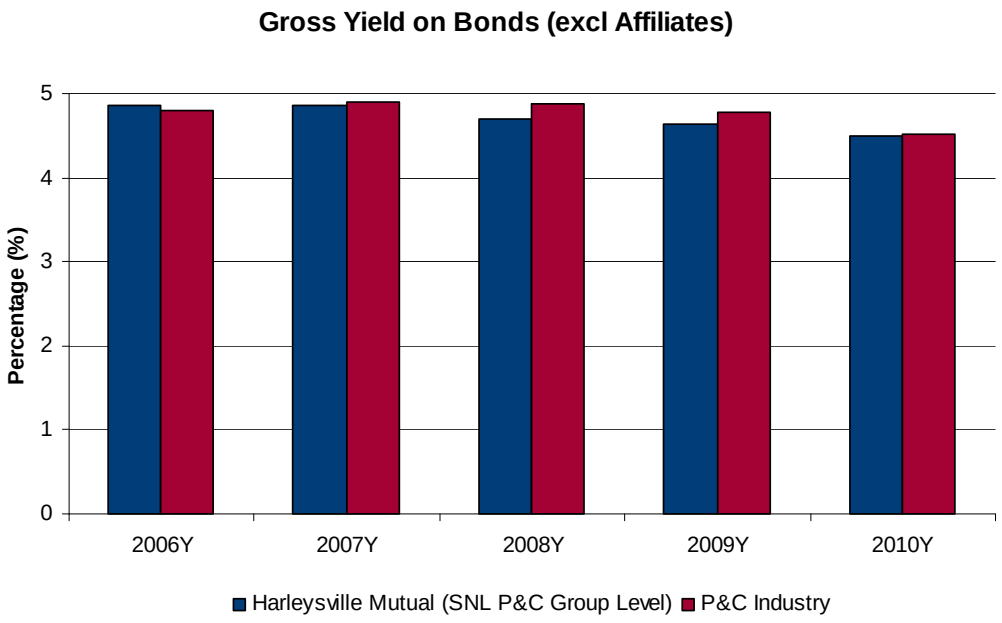
Source: SNL Financial

According to SNL Financial, from 2006 to 2010, the gross yield on bonds in Harleysville Mutual's portfolio has been consistently close to the P/C industry average, having never varied by more than 18 basis points. Given P/C insurers' attraction to defensive bond investments, Harleysville Mutual's portfolio has been representative of the broader industry. For 2010, Harleysville Mutual yielded 4.49% on its bond portfolio, while the P/C industry average was 4.51% (a 2 basis point margin). As of year-end 2010, the highest yielding bond in Harleysville Mutual's portfolio was a Federal National Mortgage Association bond with a yield of 6.1%, which is unrated.

Table 19) Harleysville Mutual Gross Yield on Bonds

	2006Y	2007Y	2008Y	2009Y	2010Y
Harleysville Mutual Insurance Company	4.85	4.85	4.70	4.64	4.49
P&C Industry	4.79	4.90	4.88	4.78	4.51

Source: SNL Financial



Source: SNL Financial

Note: Except as otherwise expressly stated in this Section III, the source for all information in this Section III is SNL Financial and the Company's Data Room as of the Evaluation Date.

Section IV

Review of Nationwide Mutual Insurance Company Form A Filing and Related Documents

Boenning's Engagement Letter with the Department included the following:

> "(b) Review any regulatory filings (including Form A merger filings) submitted by the Company or its Transaction Partner to the Department."
>
> "(d) Review the Company's registration statement filed with the Securities and Exchange Commission ("Registration Statement") and subsequent updates.
>
> > "(i) Review and comment on the Company's Mutual Policyholder Information Statement."

In accordance with its Engagement Letter, Boenning reviewed the Transaction Partner's Form A. In addition, as part of the Form A review Boenning reviewed the Business Plan for Nationwide, filed by Saul Ewing LLP on November 10, 2011 in connection with Nationwide's Form A filing ("***Business Plan***"). Our review of the Form A and related documents is intended to assist the Department in its evaluation of the Transaction pursuant to applicable provisions of the Act, including Sections 991.1402(f)(1)(iv) and (vi). To help the Department understand the Transaction from a financial point of view and to provide the Department with background and context that may be helpful to the Department in its evaluation of the Transaction, below is a brief history of the events leading up to the Transaction.

A. Transaction Background and History

Harleysville Mutual has operated as an independent P/C insurance company for over 90 years. As shown in further detail in Section III, Harleysville Mutual's financial performance was beginning to decline in late 2004 and into 2005, as reflected by Harleysville Mutual's 3% revenue decline.

In 2004, the Company's Boards of Directors undertook several changes to Harleysville's management and strategic direction. The executive team was replaced with new senior management in the areas of finance, information technology, underwriting, field operations, actuarial, and the Chief Executive Officer function. Michael Browne, who was a member of the Boards of Directors, was appointed the new CEO to bring change and a new image to the Company's brand. Arthur Chandler was added as Chief Financial Officer in 2005 and the new management team developed a strategic plan to increase profitability and grow the business.

Because of an ongoing soft market and deteriorating economic conditions, it appears that the Company's management concluded that continued recovery and growth was not attainable organically. In 2007, 2008, and 2009, the Company's revenues once again came under pressure, declining by 2%, 7%, and 3%, respectively. Without growth, the Company's relatively high expense and infrastructure costs would continue to depress profits and ultimately surplus growth. Accordingly, the Company's senior management and Boards of Directors examined the possibility of growing the Company through an acquisition.

In 2008, the Company hired a former investment banker to spearhead the M&A effort. From 2008 to 2010, the Company identified over 50 companies as potential targets of an acquisition. The Company held discussions with 30 to 40 companies regarding a possible transaction. The majority of candidates that the Company spoke to were apparently desirable and financially profitable companies, but that did not want to be acquired. The few companies that did indicate an interest in being acquired were not strong financial performers and had the chance of becoming more of a financial burden for the Company than becoming synergistic. As the Company was unable to grow either organically or by acquisition, the Company's Boards of Directors continued to examine other strategic options.

For the past several years, the Company's Boards of Directors have held offsite retreats to review strategic options and various other issues regarding the Company's growth and future. In late 2010, the Company asked Credit Suisse to analyze other strategic alternatives outside of an acquisition. Credit Suisse presented the Company with eight strategic options, which consisted of:

- various types of demutualizations
- an acquisition by Harleysville Mutual of the publicly traded shares of HGIC
- a sale of all or part of HGIC
- a restructured pooling agreement between Harleysville Mutual and HGIC
- acquisitions by HGIC
- mergers involving Harleysville Mutual in which Harleysville Mutual would be the surviving entity
- sale of some or all of Harleysville Mutual shares in HGIC
- combined merger or sale involving Harleysville Mutual and HGIC

Management described the Company's situation as "hitting the wall" with no real options available to drive continued growth. Accordingly, the Company's Boards of Directors, during their

retreat in June 2011, concluded that a sale or merger was possibly the best strategic alternative. As a result, the Boards of Directors directed Credit Suisse to pursue a merger transaction.

As noted in Harleysville Mutual's PIS:

> *"The Harleysville Mutual and Harleysville Group boards of directors (collectively referred to in this section as the "Boards"), and the senior management of both entities, regularly review and consider business alternatives to protect and enhance value for all of the constituencies of Harleysville Mutual and Harleysville Group, including stockholders, policyholders, employees, agents and the communities in which Harleysville Mutual and Harleysville Group and their respective insurance subsidiaries operate. In this Background of the Merger section, we refer to Harleysville Group, Harleysville Mutual and all such subsidiaries collectively as Harleysville. Harleysville considers its strategic options in light of the totality of the circumstances, including current and anticipated business trends, regulatory conditions, short-and long-term value for the stockholders of Harleysville Group, the impact on policyholders and the ratings environment expected to impact Harleysville and the insurance industry. In particular, for the past seven years, the Boards have undertaken an annual strategic review. At these strategic review sessions, numerous strategic options have been considered and discussed. These have included continuing as an independent company either with or without acquiring other businesses, a combination with another mutual insurance company, a demutualization of Harleysville Mutual on a standalone basis, a sponsored demutualization of Harleysville Mutual with a third party, and a conversion to a mutual holding company structure. At these meetings, the Boards have considered presentations from various financial advisors and legal counsel in which the advantages and disadvantages of some of these strategic options were outlined for discussion."*

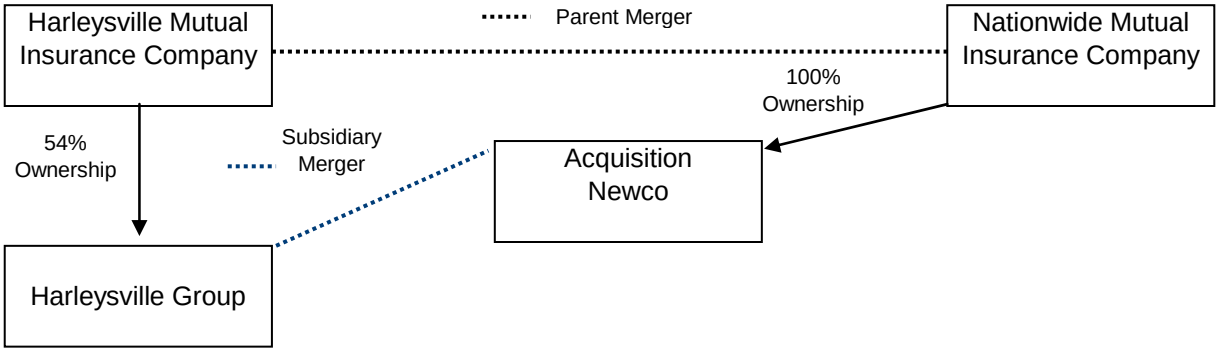
Based on (among other things) Credit Suisse's recommendations to the Boards of Directors during Credit Suisse's presentation on June 13, 2011 (the "***June Presentation***"), discussions were initiated with three parties regarding various types of potential combinations. According to the PIS, "Company A" was approached but ultimately elected not to submit a formal proposal, while "Company B" did not appear to be interested in pursuing a transaction on terms that would have been acceptable to the Company's Boards of Directors. Nationwide, the third party involved in discussions regarding a possible business combination, submitted a non-binding proposal on August 9, 2011 for a mutual-to-mutual merger and a cash payment of $60 per share to the public stockholders of HGIC. The Company's Boards of Directors authorized management to move forward to due diligence and negotiation of an acceptable transaction with Nationwide under the terms of an exclusivity agreement dated August 15, 2011.

As more fully discussed in Section V, Company B expressed an interest in pursuing a transaction with the Company after the Company had entered into an exclusivity agreement with Nationwide. According to the PIS, the Company's management and Boards of Directors appeared to

believe that a Transaction with Nationwide would provide the Company with the ability to continue to improve upon and grow its existing business model and give the Company access to Nationwide's size and scale, diverse distribution channels, geographic diversity, revenue and product line diversity, strong reputation, and stronger A.M. Best's rating.

The Transaction is compromised of two separate cross-conditioned corporate reorganizations:

- Parent Merger - Harleysville Mutual merges with and into Nationwide, with Nationwide surviving the merger
- Subsidiary Merger - A newly formed subsidiary of Nationwide merges with and into HGIC. HGIC minority stockholders will be bought out and HGIC will survive the merger as a wholly-owned subsidiary of Nationwide



[redacted]

B. Review of Nationwide Form A Filing

The Form A, which was prepared with the assistance of law firms experienced in insurance regulatory matters (namely Saul Ewing LLP and Stradley Ronon Stevens & Young LLP), contained the following items:

Item 1. Insurer and Method of Acquisition
Item 2. Identity and Background of the Applicant
Item 3. Identity and Background of Individuals Associated with the Applicant
Item 4. Nature, Source and Amount of Consideration
Item 5. Future Plans of Insurer
Item 6. Voting Securities to be Acquired
Item 7. Ownership of Voting Securities
Item 8. Contracts, Arrangements, or Understandings with Respect to Voting Securities of the Insurer
Item 9. Recent Purchases of Voting Securities
Item 10. Recent Recommendations to Purchase

Item 11. Agreements with Broker-Dealers
Item 12. Financial Statements and Exhibits

A copy of the Form A is included as Exhibit III. Other submissions to the Department in connection with the Form A filing are contained on the Department's website. The Department sought certain additional information from Nationwide and the Company in connection with the Form A filing. The Department has not indicated to Boenning that, as of the Report Date, the Form A or related submissions by Nationwide or the Company omitted any items required by applicable law, regulation or Department procedures.

The information contained in the Form A filing reviewed by Boenning appeared consistent with information conveyed to Boenning in its interviews with management and other Transaction - related documents reviewed by Boenning. Specific questions or suggestions for issues to be reviewed, or requests for additional disclosures/information, that were generated by Boenning during its review of the Form A filing, if any, were provided to the Department during the course of Boenning's engagement. Such items were addressed separately by Harleysville Mutual, HGIC and/or the Transaction Partner with the Department.

C. Review of Business Plan

[redacted]

The Business Plan's discussion of Nationwide's plans for Harleysville Mutual's employees, agents, Policyholders, management and others appeared generally consistent with information conveyed to Boenning in its interviews with the senior management of each of the Company and Nationwide. Boenning understands that certain statements in the Form A and Business Plan regarding business strategy and benefits to employees, agents, Policyholders and the community may be considered by the Department in its determination of whether the Transaction implicates the standard of Section 991.1402(f)(1)(iv) of the Act. Specifically, the Department may consider the following extrapolated from the Business Plan:

- Allied[3] will continue to conduct the Company's business at all its current locations after the consummation of the Mergers (the "Closing") in substantially the same manner as it did prior to the Closing; however, its operations will be evaluated post-Closing as Nationwide and Harleysville gain a better understanding of each other's business operations

[3] "Allied" was used in the Business Plan. The Allied companies were acquired by Nationwide in 1998.

- After the Closing Harleysville will continue to conduct business under the Harleysville brand at its headquarters
- During the two-year period after the Closing, Nationwide will substantially maintain or exceed the overall number of associates, as of September 28, 2011, at the Harleysville headquarters and will not cause a reduction in force to occur at Harleysville's Worcester, Massachusetts, location

[redacted]

- Nationwide plans to enable Allied and Harleysville to continue to provide and expand their current offerings of product to facilitate greater growth opportunities in the future
- The intent of the proposed Mergers is to focus on meeting the long-term needs of Nationwide's policyholders, increase Allied geographical diversification and provide increased ease of doing business with independent agents and Policyholders
- Because the Mergers will not have any effect on the corporate existence of any of the insurance operating companies of Harleysville, with the exception of Harleysville Mutual, those companies will continue to utilize their currently filed rules, rates, and forms
- Nationwide does not anticipate that the Mergers will affect any of Harleysville's nearly 3,200 independent agents or Allied's approximately 6,800 independent agents and their relationship with Harleysville or Allied, as applicable

Included [redacted], is the internal communication sent out to all Allied Independent Agents when Nationwide announced the Transaction. Below, Boenning highlighted several items [redacted] that the Department may determine are relevant to the standard in Section 991.1402(f)(1)(iv) of the Act.

> *"Today, we're announcing an agreement to combine with Harleysville Group, Inc. This is an investment in the independent agency channel that creates growth and strengthens our presence in the Northeast.*
>
> *This is a strategic business decision that makes sense for both organizations. Harleysville has a strong presence in the Northeast and expands our footprint as a national independent agency carrier. This change also brings us additional expertise in the commercial market, while allowing Harleysville agents to leverage our scale and expertise in personal lines, as well as our presence in the Midwest and West."*

"Why is Allied/Nationwide entering into this [T]transaction?

Harleysville Group Inc. will expand Nationwide's independent agency footprint and increase our commercial lines book of business. It would take multiple years for both organizations to achieve the same growth organically.

How does this [T]transaction benefit my agency or me as an Allied agent?

The commercial lines business has the potential for solid growth. Harleysville brings strong expertise in the commercial market, including experienced commercial lines talent, claims specialization and loss control. It also gives us access to markets in the Northeast where we don't write business today.

Will Allied agents have access to Harleysville's commercial lines products? Will Harleysville agents gain access to sell Allied products?

At this time, the organizations will continue to operate as separate companies. Should the [T] transaction close, a broader portfolio of insurance, financial and banking products would be available to agents and customers."

Similarly, Exhibit 22(b) of the Business Plan is the communication sent out to all Harleysville independent agents when the Transaction was announced. Below, Boenning highlighted several items from Exhibit 22(b) of the Business Plan the Department may determine are relevant to the standard set forth in Section 991.1402(f)(1)(iv) of the Act.

"Q1. ***Why is Harleysville entering into the contemplated transactions with Nationwide?***

Both Harleysville and Nationwide believe there is a strategic benefit in creating a national independent agency distribution network that will make the combined organization stronger over the long term. Under the Nationwide umbrella, the contemplated transactions bring together two best-in-class property & casualty carriers (Harleysville and Allied) with complementary geographic marketing territories-Harleysville's strong independent agency network, primarily east of the Mississippi, and Allied's strong independent agency network in the Midwest and West.

Q6: ***How will my Harleysville Policyholders be affected by these transactions?***

There will be no immediate impact to Policyholders. They will continue to be served by their same Harleysville agent and Harleysville customer service representatives. Our company will write new business and renew existing business based on our

current product portfolio, and will continue to have the support of our current underwriting, claims and risk control services. Additionally, upon completion of the mergers, Harleysville will have an even greater opportunity to focus on its long-term strategic goal – meeting the needs of Policyholders, agency partners and employees."

"For policyholders in particular, they will now be offered a broader portfolio of insurance, financial and banking products and services. Additionally, the policyholders will enjoy the full backing of Nationwide's financial strength. While Harleysville has approximately $1.3 billion of surplus, the combined companies will have approximately $13.5 billion of surplus after the merger is complete. Moreover, Harleysville's current A.M. Best rating is "A," and Nationwide's current rating is "A+." Finally, the combined organization will retain the mutual insurance company structure with its focus on meeting the insurance needs of its policyholders.

In light of the mutual structure and with Nationwide's deeper financial platform, the organization will have the ability to make greater investments in its products and resources. This will result in more growth, opportunities and in the long-term needs of the policyholders being better served and benefiting from even greater protection and financial security. In this regard, it is worth noting that since its merger with Nationwide in 1998, Allied has expanded from 23 states to 33 states – and had tripled its direct written premium from $900 million to nearly $3.4 billion."

D. Review of the PIS

On or about December 23, 2011, Harleysville Mutual filed the PIS with the Department. Notable sections to Boenning in the PIS included:

- Reasons for the Merger
- Background of the Merger
- Interests of the Directors and Executive Officers in the Merger
- Comparison of Member Rights

The information contained in the PIS reviewed by Boenning appeared consistent with information previously provided to Boenning by the Company's management, Boards of Directors and Advisors or included in other Transaction-related documents reviewed by Boenning. Specific questions or suggestions for issues to be reviewed, or requests for additional disclosures/information, that were generated by Boenning during its review of the Form A filing, if any, were provided to the Department during the course of Boenning's engagement. The Department appears to have incorporated a version of those suggestions in its PIS comment letter to Harleysville Mutual.

Harleysville Mutual provided a specific response to the Department's PIS comment letter. In correspondence dated February 27, 2012, Harleysville Mutual responded to each comment and provided an exhibit indicating changes to be made to the PIS to result in the final Harleysville Mutual Proxy Statement. Changes to the Harleysville Mutual PIS included an affirmation that

> *"Harleysville Mutual's Board also separately considered the requirements that would need to be met to obtain approval of the contemplated transactions by the Pennsylvania Insurance Department under the Holding Company Act, which included a determination that the proposed Merger was not unfair, unreasonable or failed to confer a benefit on policyholders of Harleysville Mutual."*

Harleysville Mutual also stated in the final Harleysville Mutual Proxy Statement that its Board of Directors determined that the Transaction was fair and reasonable, and conferred benefits to the Harleysville Mutual Policyholders.

Section V

Review of Decision Process and Alternatives

A. Financial Comparative Review of Harleysville Mutual

Boenning's Engagement Letter with the Department included the following:

> "(a) Assemble such financial and other information on the Company from Boenning's information request list as Boenning deems necessary or appropriate."
>
> "(c) Conduct due diligence on the Company in order to review historical financial results, financial projections, various corporate information and other information as Boenning deems necessary or appropriate."

Section V.A is intended to serve two primary purposes. First, Boenning, through its due diligence on Harleysville Mutual, became familiar with the ways in which Harleysville Mutual performs relative to its peers. Such due diligence provides an important factual foundation and baseline to assess, from a financial point of view, the information provided by Harleysville Mutual, its management team and the Advisors. Second, and more importantly, the analysis in this Section is intended to assist the Department in its review of the Transaction pursuant to the Act and applicable law. Specifically, it is Boenning's understanding that evaluating changes to Harleysville Mutual and its management may be relevant to the Department's determination under Section 991.1402 (f)(1)(iv), and the post-Transaction impact on the insurance buying public may be relevant to the Department's determination under Section 991.1402(f)(1)(vi). This Section provides certain comparability data and analysis that may be useful for the Department's review and determinations.

a. Financial Comparables

In addition to looking at the financial characteristics of Harleysville Mutual as indicated in Section III, Boenning also developed a peer group of mutual insurers (the "***Mutual Comparable Group***") for comparison purposes as another approach to measuring operating results. The Mutual Comparable Group includes 13 P/C mutual insurers with capital & surplus between $700 million and $1.5 billion which offer similar product lines to Harleysville Mutual. While none of the companies in the Mutual Comparable Group is identical to Harleysville Mutual, we believe that the Mutual Comparable Group on the whole provides a meaningful basis for financial comparison purposes. As noted in Section I, Harleysville Mutual has a relatively rare corporate structure. The structure does not simply affect the structure and mechanics of a potential M&A transaction, but

also requires different analysis, value assumptions and director duties than traditional stockholder-owned entities.

b. *Financial Comparison*

The following table lists financial and operating metrics typically tracked in the P/C insurance industry for the 13 mutual insurers that constitute the Mutual Comparable Group:

Table 20) Harleysville Mutual Comparable Group

Harleysville Mutual Comparable Group
As of and for the LTM period ended 6/30/2011

Company Name	Average Capital & Surplus ($000)	Net Total Assets ($000)	Total Revenue ($000)	Net Prem Writ / Avg C&S (%)	Net Investment Yield (%)	Direct Premiums Written ($000)	Loss Ratio (%)	Expense Ratio (%)	Combined Ratio (%)	(1) 3 yr Avg Combined Ratio (%)	ROAA (%)	ROAE (%)	(2) 3 yr Avg ROAA (%)	(2) 3 yr Avg ROAE (%)
Alfa Mutual Group	1,027,960	2,224,572	1,135,180	101.90	5.47	1,054,865	92.02	30.59	122.60	105.29	(5.54)	(11.71)	(0.96)	(1.73)
Andover Companies	947,070	1,768,760	465,767	45.85	2.19	399,307	67.30	36.88	104.18	92.43	0.94	1.71	4.03	7.47
Employers Mutual Casualty Co.	1,032,965	3,322,165	1,312,173	111.72	4.14	1,136,011	75.68	34.07	112.15	105.13	1.98	6.36	2.06	6.75
Grange Mutual Casualty Co.	833,087	1,938,306	1,147,948	127.18	2.36	1,119,832	73.14	32.38	105.82	102.92	0.61	1.40	1.36	3.14
KY Farm Bureau Mutual Ins Co.	876,781	1,835,521	921,820	96.18	4.49	861,986	92.11	22.45	114.56	115.95	(0.74)	(1.48)	(1.32)	(2.32)
Main Street America Group	749,879	2,093,797	977,710	120.44	3.74	871,638	70.49	32.63	103.12	97.93	2.41	6.56	2.70	7.63
NC Farm Bureau Mutual Ins Co.	895,569	1,613,770	765,985	87.34	2.68	919,567	99.17	27.31	126.48	100.63	(9.02)	(16.45)	1.76	3.08
Quincy Mutual Fire Ins Co.	736,306	1,275,451	329,928	37.75	2.40	245,954	79.81	36.10	115.91	100.73	0.62	1.01	1.30	2.13
Shelter Mutual Insurance Co.	1,246,142	2,656,148	1,406,941	102.91	4.72	1,209,855	90.22	25.37	115.59	107.71	(0.48)	(0.97)	2.00	3.81
Sthrn Farm Bureau Cas Ins Grp	1,037,609	2,211,611	1,204,230	109.14	3.54	1,066,598	87.93	21.23	109.16	105.42	(0.98)	(2.07)	0.72	1.43
Texas Mutual Insurance Co.	1,552,401	5,123,073	917,975	42.72	3.46	654,439	63.68	26.74	116.16	106.73	3.36	9.80	2.68	8.48
Utica National Insurance Group	825,937	2,669,541	823,629	84.56	3.95	734,399	74.98	37.29	112.54	111.13	1.63	5.27	0.88	2.74
Westfield Group	1,299,241	3,939,148	1,653,833	115.66	4.13	1,511,042	76.02	32.55	108.65	99.02	0.60	1.75	2.22	6.48
Group Aggregate														
Comparable Group Mean	1,004,688	2,513,220	1,004,855	91.03	3.64	906,576	80.20	30.43	112.84	103.92	(0.36)	0.09	1.49	3.78
Comparable Group Median	947,070	2,211,611	977,710	101.90	3.74	919,567	76.02	32.38	112.54	105.13	0.61	1.40	1.76	3.14
Harleysville Mutual Ins Co.	1,245,608	4,137,848	1,310,115	93.19	4.31	1,326,056	74.99	34.38	109.47	101.83	1.32	4.31	2.08	7.30

Source: SNL Financial
Data reflects the P&C group reporting level

(1) 3 year Combined Ratio reflects 2008 - 2010
(2) 3 year ROAA and ROAE reflect 2008 - 2010

It is clear that the 76.02% median loss ratio of the Mutual Comparable Group reflects a period of troubling catastrophe events for the P/C insurance industry. Catastrophes in the U.S. in 2011 were record setting, headlined by several tornados causing destruction in the Midwest and Southeast as well as Hurricane Irene's damage along the east coast. While the Mutual Comparable Group's median combined ratio was very high at the time of this analysis (the median and mean ratio approximately 112.54% and 112.84%, respectively), it can be seen at levels closer to historical norms in the 3 year average calculation of 105.13% and 103.92%, respectively. At 74.99%, Harleysville Mutual's loss ratio is in-line with its peers. However, Harleysville Mutual's expense ratio of 34.38% was elevated relative to the Mutual Comparable Group's mean and median of 30.43% and 32.38%, respectively. A high expense ratio reflects inefficiency in an insurer's efforts to generate premiums and illustrates the Company's management's conclusion that Harleysville Mutual required additional size and scale to effectively rationalize its infrastructure investment. The elevated loss ratio and expense ratio result in a historically high combined ratio median of 112.54% for the Mutual Comparable Group and 109.47% for Harleysville Mutual when compared to their respective 3 year averages. While Harleysville Mutual's return on average assets was low at 1.32% compared to its 3 year average, it outperformed relative to its peers given their median of only 0.61%, with 5 companies reporting a negative return.

As can be seen in the above comparison table, Harleysville Mutual's net investment yield for the period was 4.31%. Only 3 of the 13 insurers included in the Mutual Comparable Group boasted a superior investment yield to Harleysville Mutual. The Mutual Comparable Group yielded a mean and median yield of 3.64% and 3.74%, respectively. Additionally, Harleysville Mutual exhibited relative strength in its 3 year ROAA and ROAE ratios for the period of 2008 through 2010. The operating metric in which Harleysville Mutual shows the greatest financial difference relative to its peers is Net Premiums Written/Avg. Capital & Surplus. Harleysville Mutual reported 93.19% while the median for the Mutual Comparable Group was 101.90%. This financial difference shows Harleysville Mutual was under-leveraged during the analyzed time period and again supports the Company's conclusion that it required additional growth. Further, the Mutual Comparable Group analysis is "backward-looking" or historical. Company management has described a future outlook as one with continued challenges caused primarily by lack of growth and scale.

B. Transaction Analysis and Review of Opinions

Boenning's Engagement Letter with the Department includes the following:

> "(h) Review analysis and opinions prepared by the Company's financial and legal advisors and conduct interviews with such advisors to understand the analysis as well as the extent and limits of the analysis and opinions."

In accordance with its Engagement Letter, Boenning reviewed presentations, opinion letters, and engagement letters of the Company's Advisors. Boenning also met with the Advisors and the Company's management (as well as conducted follow-up interviews via telephone) to discuss their analysis and conclusions. In addition to reviewing each Advisor's engagement letter, opinion letter and presentation, Boenning interviewed senior management of the Company about the contents and the respective Boards of Directors' use of such materials, and interviewed each Advisor with questions, if any, developed by Boenning in its review of the Advisor materials. In addition, certain Advisors assembled on January 10, 2012 and presented to representatives of Boenning and the Department. Management indicated that they arranged the meeting to convey what the Boards of Directors heard from the Advisors during Boards of Directors' meetings in September 2011.

Management indicated to Boenning and the Department that the Boards of Directors relied on the following legal and financial advice in connection with their evaluations of the Transaction.

Table 21) Advisor Summary

Legal Advisor	Advice / Opinion Addressing
Ballard Spahr LLP	Counsel to the Harleysville Mutual
Fox Rothschild LLP	Counsel to HGIC
Stevens & Lee, P.C.	Fiduciary duties of Harleysville Mutual directors

Financial Advisor	Advice Addressing
Credit Suisse Securities (USA) LLC	Strategic alternatives analysis and financial advisor to the Company
Griffin Financial Group LLC	Fairness to Harleysville Mutual
Keefe, Bruyette & Woods, Inc.	Fairness to HGIC public stockholders

a. Credit Suisse Presentations

The Company engaged Credit Suisse as a financial advisor in connection with analyzing and evaluating the business, operations and financial position of the Company, evaluating the Company's strategic and business alternatives, evaluating and responding to any proposals received from potential acquirers of the Company and structuring and negotiating any such transaction. Credit Suisse, in a presentation made to the Boards of Directors on September 27, 2011 ("***September Presentation***") [redacted], provided strategic information to the Company's Boards of Directors regarding the results of the sale process management conducted as well as their analysis of the Transaction in light of Company's stated strategic goals and Transaction objectives. Credit Suisse was not asked to provide a fairness opinion.

Credit Suisse and management indicated that the September Presentation was provided in the context of another presentation Credit Suisse had delivered during the Harleysville Mutual and HGIC Boards of Directors' retreat in June 2011. As a result, Boenning requested, reviewed and discussed the Credit Suisse June Presentation with Credit Suisse and management.

1. The June Presentation

[redacted] The June Presentation delivered to the Boards of Directors contained the following:

[redacted]

The June Presentation was delivered to the Boards of Directors and did not refer specifically to any of its related entities. In summary, based on discussions with Credit Suisse and management, the June Presentation appeared thorough. Specifically:

- Alternatives considered were reasonable from a financial point of view and represented the range of possible alternatives from status quo, to growth via M&A, to demutualization to sale
- Thorough industry context, as described by a leading Wall Street Investment Bank, was utilized as background

- The analysis of each alternative contained details, qualitative and quantitative analysis and a review of likely outcomes commensurate with the purpose of educating the Boards of Directors on strategic alternatives

Boenning specifically noted that each alternative was analyzed within the context of the current industry environment as to each of the following: considerations, execution and financial outcome. Boenning examined the analysis and provided commentary on each alternative addressed below. (In addition, this Section V contains further analysis and commentary relative to the value of the companies under various alternatives.)

(a) Standalone

Boenning's review of the Credit Suisse June Presentation noted the following:

- Successful execution would require succeeding in an adverse market and with a company that did not successfully meet its goals in 2011
- Success financially would largely be determined by factors outside the control of Harleysville Mutual and HGIC management (e.g., insurance operating market and capital markets conditions)
- Harleysville Mutual's and HGIC's constituents would be largely unaffected by this strategy in the near term until the strategy was successful or not. Harleysville Mutual's and HGIC's community, employees, Policyholders, stockholders and/or agents would share in some ways in the success or failure of the strategy

(b) Standalone with Acquisitions

Boenning's review of the Credit Suisse June Presentation noted the following:

- Would enhance competitive position and assist with size and scale challenges
- Execution is a challenge not only from integration and transaction risk but also from the practical challenge of finding an attractive acquisition. As noted in Section IV, Harleysville expended significant effort over the past three years to consummate an acquisition and was unsuccessful
- A successful acquisition would be value enhancing if purchased at attractive pricing, via improved ROE and growth, likely benefiting the community, employees, Policyholders and stockholders alike
- An acquisition would not materially alter Harleysville Mutual's and HGIC's relative standing within the industry despite assisting with size and scale challenges

(c) Demutualization

Boenning's review of Credit Suisse's June Presentation noted the following:

- A subscription rights demutualization of Harleysville Mutual would raise significant capital and likely require a simultaneous acquisition of the minority shares of HGIC
- Execution is potentially a challenge due to the large relative size of the offering
- The financial impact of the demutualization is generally negative (depressed ROE, significant intangible asset) unless and until the capital raised is deployed
- The acquisition of HGIC for cash would be a significant benefit to HGIC stockholders. It would likely not result in significant near-term changes for the community, employees, Policyholders and agents

(d) Sale or Merger

Boenning review of Credit Suisse's June Presentation noted the following:

- Solves size and scale challenges
- Results in diminishment of control and related impacts on community, employees, etc.
- Could bring additional products, services and expertise to Harleysville Mutual, HGIC and their respective constituents
- Depending on transaction partner, execution risk can vary from moderate to significant
- Likely results in a larger and more financially stable pro forma entity

(e) Conclusions Regarding June Presentation

Boenning reviewed the June Presentation, interviewed Credit Suisse about its contents and discussed the concepts and conclusions with the Company's management.

Our review included an examination and review of Credit Suisse's financial and quantitative analysis such as:

- P/C industry returns and valuation
- Company profitability compared with a peer group
- Company projection sensitivity analysis
- Alternative acquisition candidates and financing alternatives analysis
- Demutualization analysis and scenarios
- Potential buyer analysis and pro forma transaction impact to Harleysville Mutual Policyholders
- Illustrative impact of initial Nationwide expression of interest

In some cases, the analysis was deemed by Credit Suisse "directional" or "illustrative" and not definitive. Boenning considered this information credible.

Boenning also noted Credit Suisse's conclusions on both qualitative and quantitative issues and discussed such conclusions with the Company's management. Boenning concluded that the June Presentation appeared to provide adequate detail, analysis and a review of likely outcomes commensurate with the intended purpose of educating the Boards of Directors about strategic alternatives and establishing a contextual framework for future decision-making.

2. September 27, 2011 Credit Suisse Presentation

Credit Suisse gave its September Presentation to the Boards of Directors in connection with the Boards of Directors' deliberations about the Transaction. The presentation [redacted] contained the following:

[redacted]

Credit Suisse gave a second presentation on September 28, 2011 to the Boards of Directors that was materially the same as the September Presentation in every respect with the exception of an update for market pricing in the September 28 presentation. [redacted] All the conclusions are the same.

In reviewing and analyzing the presentations, Boenning noted the presentations contained a history of the strategic alternatives reviewed over the past years by Credit Suisse with Harleysville Mutual and HGIC, as well as, the following introductory statements[4]:

- *"Credit Suisse has worked with [Harleysville] Mutual and [Harleysville] Group for several years on a variety of strategic alternatives and corporate restructurings*
- *To refresh the Boards of Directors' recollections, those alternatives have included, but were not limited to:*
    - *various types of demutualizations*
    - *an acquisition by [Harleysville] Mutual of the publicly traded shares of [Harleysville] Group*

[4] In each of the September 27 and 28, 2011 presentations, "Harleysville" is never specifically used. Accordingly, we have bracketed such term in the excerpted portions below as appropriate.

- *a sale of all or part of [Harleysville] Group*

- *a restructuring of the pooling agreement between [Harleysville] Mutual and [Harleysville] Group*
- *acquisitions by [Harleysville] Group*
- *mergers involving [Harleysville] Mutual, in which [Harleysville] Mutual would be the surviving entity*
- *sale of some or all of [Harleysville] Mutual's shares in [Harleysville] Group such that [Harleysville] Mutual would no longer have a controlling interest in [Harleysville] Group*
- *a combined merger or sale involving [Harleysville] Mutual and [Harleysville] Group*

- *Following a review of potential alternatives by the Boards of Directors in June 2011, the Company directed Credit Suisse to pursue a merger transaction. Discussions were held with three parties regarding various types of potential combinations*
- *Each of the three parties was given guidance as to the Boards' objectives for a transaction, including:*
  - *Maximize value to public stockholders*
  - *Protect and enhance policyholders' position*
  - *Provide opportunities for employees*
  - *Preserve the culture of [Harleysville]*
  - *Continue to grow the franchise"*

Ultimately, Credit Suisse indicated that the Transaction was consistent with objectives developed by the Harleysville Mutual and HGIC Boards of Directors as noted above. Credit Suisse also acknowledged that in addition to the above-listed joint or common goals, each of Harleysville Mutual and HGIC might have also had goals that were specific to their companies.

Of the analyses performed by Credit Suisse, Boenning has summarized below those deemed relevant to the Department (review of Credit Suisse's HGIC valuation and appendices were not specifically summarized).

(a) Financial Implications for Harleysville Mutual Policyholders

Credit Suisse's analysis relating to Policyholders includes the following analysis relating to benefits to Policyholders: (i) Nationwide's business description and financial size, (ii) Nationwide's financial results, (iii) the proposed combined company's pro forma geographic footprint, pro forma market share and business mix, and (iv) pro forma financial impact comparison relative to Harleysville Mutual standalone and benchmarking against other P/C

insurers. Management indicated that the Boards of Directors understood the Credit Suisse analysis as supporting that the Transaction would be favorable to HGIC stockholders, Policyholders and other constituents.

(b) Perspectives on Other Possible Transactions

Credit Suisse prepared a comparative summary of the Nationwide offer and Company B's unsolicited indication of interest (please refer to the PIS and Section IV for a description of the solicitation process timeline). Management indicated that the Boards of Directors understood the Credit Suisse comparative analysis as supporting the conclusion that the Transaction would be most favorable in the aggregate to meeting the following objectives set forth by the Boards of Directors for any potential transaction:

- Maximize value to public stockholders
- Protect and enhance Policyholders' position
- Provide opportunities for employees
- Preserve the culture of the Company
- Continue to grow the franchise

Credit Suisse acknowledged that the unsolicited indication of interest from Company B included a potential Policyholder dividend in the transaction but noted that in the aggregate, that single item did not outweigh the other aspects of the Transaction proposed by Nationwide.

In addition, management, Nationwide and the Credit Suisse presentations noted Allied Insurance's growth under Nationwide since its acquisition in 1998 as a model for how it will operate the Company post Transaction. From 1998 to 2011, Nationwide grew the Allied business from 22 to 33 states and has more than tripled its direct written premiums from approximately $900 million to approximately $3.4 billion. Nationwide has indicated that it intends to grow the "Harleysville" franchise similarly after the Transaction. Further, Boenning noted that the current CEO of Nationwide, Stephen S. Rasmussen, was originally with the acquired Allied organization.

Boenning noted that both management (in statements and in the PIS) and Credit Suisse indicated that Credit Suisse contacted third parties on behalf of the Company in order to solicit interest in a transaction even though their engagement letter did not call for such duties. Boenning

reviewed the "teaser" prepared by Company management used in connection with this function and found it customary for its intended purpose to solicit interest in a transaction. Only three parties were contacted because it was determined that these parties were the only ones that could effectuate a mutual-to-mutual transaction.

(c) Conclusion regarding Credit Suisse September Presentation

Boenning's review of the Credit Suisse presentation resulted in the following conclusions:

- The alternatives analyzed over the past several years appeared to be a comprehensive list of potential alternatives based on Boenning's experience in general and with the P/C insurance industry in particular. Most of the alternatives discussed were described in either or both of the Credit Suisse and Griffin presentations. As should be expected, the analysis of the alternatives was non-quantitative in nature. Certain of the alternatives were also able to be reviewed by certain quantitative analyses. Boenning reviewed and performed such analyses as necessary including (both included in this Section V):
    - Demutualization analysis
    - M&A transaction comparables and comparable companies analysis

- Boenning noted that the initial contact in the solicitation process was conducted by the Company's CEO and not by an external investment banker. The investment bankers participated in subsequent, more detailed meetings and discussions. Given the information that Credit Suisse indicated that it provided to management about the limited number of parties who had a corporate structure and financial capabilities sufficient to attempt a transaction with the Company, it would not have been difficult for a CEO to handle the solicitation process, regardless of the "norm" of using an investment banker to do so. Further, Credit Suisse indicated that it guided the CEO as to initial discussion content with each party so that the CEO was well prepared for an initial or high-level meeting while being ready to defer detailed, transactional and financial issues to the investment banker.
- The financial implications for Policyholders section appeared consistent with conclusions drawn by Griffin in its presentation and opinion, although was slightly less complete than the Griffin analysis. Management indicated that the purpose of the Credit Suisse presentations was not to develop each potential benefit to Policyholders and other constituents (as was Griffin's task) but to provide an overall context to the Transaction.
- The summary comparison with Company B's unsolicited indication of interest indicated that the Nationwide Transaction most completely met the stated objectives set by the Boards of Directors for a transaction.

As further support for the conclusions set forth above, the following analysis compiled by Boenning shows a comparison of the total financial consideration to Harleysville Mutual and HGIC as a group between Nationwide's proposal and Company B's unsolicited indication of interest. While an offer or expression of interest must be weighed in its entirety rather than simply from a financial point of view, this analysis is beneficial for discussion purposes.

Table 22) Illustrative Comparison of Financial Consideration

	Nationwide $60 (1)	Company B $42 (2)
Fully Diluted Share Equivalents (8/2/11) (3)	28,234,438	27,734,478
Harleysville Mutual Share Ownership (8/2/11) (3)	14,526,445	14,526,445
HGIC Shares Owned	13,707,993	13,208,033
Price Per Share to HGIC Stockholders	$60	$42
Common Stock Value to HGIC Stockholders	$822,479,601	$554,737,377
Dividend Value to Policyholders	0	$250,000,000
Total Illustrative Value Financial Consideration	$822,479,601	$804,737,377

(1) Sourced from the HGIC proxy statement.
(2) Sourced from Company B's indication of interest letter.
(3) Sourced from Company documents.
Note: Assumes Treasury Method for outstanding common share equivalents.

b. Griffin Opinion

Harleysville Mutual engaged Griffin to render its opinion as to whether the proposed Parent Merger is fair, from a financial point of view, to Harleysville Mutual. Such opinion was represented and warranted by Harleysville Mutual in the Merger Agreement Section 4.3 (c):

> *"The Board of Directors of Harleysville Mutual has received the written opinion of Harleysville Mutual's financial advisor, Griffin Financial Group LLC, to the effect that the Parent Merger is fair to Harleysville Mutual from a financial point of view, after consideration of the impact of the merger on Harleysville Mutual's constituents, including agents, creditors, employees, policyholders and the communities in which Harleysville Mutual facilities are located."*

In a written opinion dated September 28, 2011, Griffin concluded that:

> *"… the proposed Merger is fair, from a financial point of view, to Harleysville Mutual."*

In the next paragraph of its opinion letter, Griffin noted that:

> *"In providing our opinion, we considered the impact of the Merger on Harleysville Mutual's constituents, including agents, creditors, employees, policyholders and the communities in which Harleysville Mutual's facilities are located."*

The full text of Griffin's opinion is attached as Exhibit VIII. Griffin presented its analysis [redacted] in support of such opinion at a presentation to the Harleysville Mutual Board of Directors on September 27, 2011 (the "***Griffin Presentation***").

Based upon Boenning's review of Griffin's opinion letter and its experience in rendering fairness opinions, the Griffin opinion letter contains language, terms and disclaimers customary for the industry. Boenning is not able to locate examples of a fairness opinion delivered specifically in a mutual merger context, and so Boenning's commentary refers to a more general understanding of fairness opinions. Regarding any prior engagements with the Company, Griffin discloses that it:

> *"… had only[a] limited investment banking relationship with Harleysville Mutual and Group."*

Griffin's opinion also notes that it is affiliated with certain legal counsel representing Harleysville Mutual in the Transaction. Boenning has reviewed the Griffin and Stevens & Lee engagement letters and discussed their affiliation with the Company's management. As noted in this Section V, Stevens & Lee provided a legal opinion to Harleysville Mutual's Board of Directors. A potential conflict could arise from the affiliation between the law firm and the investment bank in regard to their incentives to reach conclusions that support one another. Griffin and Stevens & Lee disclosed the relationship in their respective engagement letters and opinion letters. The estimated fee to be paid to Griffin is $2,750,000 ($2,000,000 upon delivery of the fairness opinion and $750,000 upon completion of the Transaction). While Griffin's initial compensation payment of $2,000,000 is not contingent on the opinion rendered by Stevens & Lee, it could be argued the final payment of $750,000 requires a supportive conclusion by Stevens & Lee so that the Transaction can close. Further, it is Boenning's opinion that Stevens & Lee's fees could be deemed in jeopardy if Griffin did not conclude that the Transaction was fair from a financial point of view. Management indicated to Boenning that the Harleysville Mutual Board of Directors had explored the potential conflict of interest, that it was comfortable with the disclosed relationship and that it valued the advice rendered by both Griffin and Stevens & Lee.

Griffin noted in interviews that prior engagements included a fairness opinion in 2008 relating to an inter-company pooling arrangement, analyzing a potential subscription rights demutualization and buy-side analysis. Boenning does not believe this constitutes a conflict from a financial point of view in rendering the fairness opinion to Harleysville Mutual in 2011. There have been no other fees paid to Griffin (or Stevens & Lee) from Harleysville Mutual within the past two years.

The Griffin Presentation included the following

[redacted]

Boenning noted that the purposes of Griffin's presentation were to:

- *"Assist the board in meeting its fiduciary duty to Harleysville Mutual*
- *Provide an outline of the structure of the proposed transaction with Nationwide Mutual as it relates to Harleysville Mutual*
- *Deliver Griffin's opinion regarding whether the merger of Harleysville Mutual into Nationwide Mutual is fair to Harleysville Mutual from a financial point of view and analyses that support the opinion*
- *Assist the Board in meeting its duty to be informed, outline (i) other alternative structures available with respect to the Nationwide transaction and (ii) the structure proposed in the indication of interest received from Company B"*

The presentation noted that:

> *"Griffin Financial Group LLC ("Griffin") has been engaged by Harleysville Mutual to provide an opinion as to whether the merger of Harleysville Mutual into Nationwide Mutual is fair from a financial point of view to Harleysville Mutual*

- *Griffin has not been engaged to provide an opinion with respect to:*
    - *The fairness of the merger transaction of a Nationwide subsidiary with and into HGIC;*
    - *The fairness of the consideration paid to HGIC public stockholders, the cancellation of the HGIC shares owned by Harleysville Mutual*
    - *Any alternative strategy, structure, or potential transaction;*
    - *The fairness of the gains realizable by Harleysville Mutual directors and officers as stockholders of HGIC in connection with the HGIC merger and any other compensation receivable by directors and officers in connection with the transaction compared to any other party; or*
    - *The fairness of the transaction to any particular constituency of Harleysville Mutual"*

Boenning believes that the scope of the Griffin engagement as described above appears understandable from a financial point of view for the purposes of rendering its fairness opinion. Griffin cited its understanding of the rationale for the Transaction to be:

- *"Provides ability in the face of a difficult environment to continue, improve upon and grow its existing business model*
- *Gives Harleysville access to Nationwide's:*
    - *Size and scale*
    - *Diverse distribution channels*
    - *Geographic diversity*
    - *Revenue and product line diversity*
    - *Reputation, A.M. Best and rating agency ratings*

- *Strong strategic fit with Nationwide*
    - *Harleysville provides Nationwide a desired east coast independent agency platform*
    - *Cross selling opportunities through Nationwide's suite of products and financial services*
    - *Diversification of revenue streams away from core P/C insurance business*
    - *Improvement in claims paying ability, surplus, reserves, ratings, as well as access to capital*
- *Job retention and likelihood of expansion of employment as Harleysville Mutual becomes Nationwide's northeast platform*
- *Favorable impact on communities served by Harleysville Mutual from job retention, job growth, and continuity of civic focus perspective*
- *No disruption of agency network*
- *Nationwide's reputation and record as a "good" acquirer"*

The Griffin Presentation also noted:

- *"The combination with Nationwide Mutual will provide Harleysville Mutual with size and scale, geographic diversification, as well as some product line diversification*
- *Balance sheet strength and surplus levels will be markedly improved"*

The foregoing commentary is consistent with information contained in other Advisor presentations and in discussions with Company management.

(a) Analysis Context

In order to establish a context for its analysis of the fairness of the Transaction to Harleysville Mutual, Griffin analyzed the financial statements of Harleysville Mutual and Nationwide and reviewed the pro forma combined statements to draw financial conclusions about the fairness of the Transaction to Harleysville Mutual. Griffin also reviewed the potential impact on various identified constituencies. Griffin's approach includes the following assumptions:

- *"Due to Harleysville's mutual structure, HMIC can only merge with another mutual institution absent demutualization*
- *Because mutuals, like HMIC, have no shareholders or other owners, consideration is not exchanged in mutual to mutual mergers*
- *Therefore, comparable transaction analyses are not as meaningful as in mergers between stock based companies*
- *Discounted cash flow or discounted dividend analyses are also not meaningful due to (i) HMIC's mutual status without shareholders legally entitled to receive consideration, (ii) the soft market, ever-changing economic environment, and HMIC's recent CAT losses makes it difficult to estimate future performance of HMIC with any reliable degree of accuracy, and (iii) absent demutualization, it is difficult to forecast a likely terminal event or assign or estimate a terminal value of HMIC*
- *Therefore to provide this opinion, we have focused on the financial and other economic impacts of the merger on the company and each of its constituents by focusing on key metrics and other factors before the transaction and then after the transaction"*

These assumptions appear reasonable from a financial point of view and are consistent with other information examined by Boenning in preparation of the Report.

Griffin compared Harleysville Mutual's financial results and Nationwide's financial results with peer groups deemed similar by Griffin.

(b) Griffin's Selection of Comparable Companies

Factors considered by Griffin in selecting its 17 comparable companies for Harleysville Mutual were as follows:

- Commercial insurers
- Direct Written Premium between $750 million and $2 billion

Griffin utilized the following criteria for selection of the 14 peer companies for Nationwide:

- Personal lines insurers
- Direct written premium greater than $2 billion

Because insurance companies like Harleysville Mutual have somewhat unusual corporate structures and utilize inter-company pooling agreements, reasonable investors and investment bankers could utilize different sets of financial statements for comparable companies based on structure and level of financial reporting (pure mutual, combined statements, group statements etc.). Griffin utilized statements that were readily available to analysts or investors to form the basis for a comparison. Boenning adopted a similar approach to Griffin in this regard.

(c) Boenning's Selection of Comparable Companies

To assess the relevance of the Griffin comparable company group, Boenning, like Griffin, utilized the SNL database to search for public P/C insurance companies located in the U.S. and traded on the New York Stock Exchange, American Stock Exchange or the NASDAQ. Boenning focused on companies that had capital & surplus from $700 million to $1.5 billion. Please refer to the Harleysville Mutual Comparable Group table (Table 23). There is significant overlap in the Mutual Comparable Group and Griffin's group in terms of insurers selected as well as operating metrics analyzed. Griffin used a range of direct premiums written as the main filtering metric, while Boenning chose to use capital & surplus as the primary filtering metric. Griffin's methodology, while different than Boenning's, is reasonable as direct premiums written is a widely used metric for narrowing the universe of mutual insurers in such an analysis. The analysis below summarizes the 13 selected companies and their respective operating measures:

Table 23) Harleysville Mutual Comparable Group

Harleysville Mutual Comparable Group As of and for the LTM period ended 6/30/2011														
Company Name	Average Capital & Surplus ($000)	Net Total Assets ($000)	Total Revenue ($000)	Net Prem Writ / Avg C&S (%)	Net Investment Yield (%)	Direct Premiums Written ($000)	Loss Ratio (%)	Expense Ratio (%)	Combined Ratio (%)	(1) 3 yr Avg Combined Ratio (%)	ROAA (%)	ROAE (%)	(2) 3 yr Avg ROAA (%)	(2) 3 yr Avg ROAE (%)
Alfa Mutual Group	1,027,960	2,224,572	1,135,180	101.90	5.47	1,054,865	92.02	30.59	122.60	105.29	(5.54)	(11.71)	(0.96)	(1.73)
Andover Companies	947,070	1,768,760	465,767	45.85	2.19	399,307	67.30	36.88	104.18	92.43	0.94	1.71	4.03	7.47
Employers Mutual Casualty Co.	1,032,965	3,322,165	1,312,173	111.72	4.14	1,136,011	75.68	34.07	112.15	105.13	1.98	6.36	2.06	6.75
Grange Mutual Casualty Co.	833,087	1,938,306	1,147,948	127.18	2.36	1,119,832	73.14	32.38	105.82	102.92	0.61	1.40	1.36	3.14
KY Farm Bureau Mutual Ins Co.	876,781	1,835,521	921,820	96.18	4.49	861,986	92.11	22.45	114.56	115.95	(0.74)	(1.48)	(1.32)	(2.32)
Main Street America Group	749,879	2,093,797	977,710	120.44	3.74	871,638	70.49	32.63	103.12	97.93	2.41	6.56	2.70	7.63
NC Farm Bureau Mutual Ins Co.	895,569	1,613,770	765,985	87.34	2.68	919,567	99.17	27.31	126.48	100.63	(9.02)	(16.45)	1.76	3.08
Quincy Mutual Fire Ins Co.	736,306	1,275,451	329,928	37.75	2.40	245,954	79.81	36.10	115.91	100.73	0.62	1.01	1.30	2.13
Shelter Mutual Insurance Co.	1,246,142	2,656,148	1,406,941	102.91	4.72	1,209,855	90.22	25.37	115.59	107.71	(0.48)	(0.97)	2.00	3.81
Sthrn Farm Bureau Cas Ins Grp	1,037,609	2,211,611	1,204,230	109.14	3.54	1,066,598	87.93	21.23	109.16	105.42	(0.98)	(2.07)	0.72	1.43
Texas Mutual Insurance Co.	1,552,401	5,123,073	917,975	42.72	3.46	654,439	63.68	26.74	116.16	106.73	3.36	9.80	2.68	8.48
Utica National Insurance Group	825,937	2,669,541	823,629	84.56	3.95	734,399	74.98	37.29	112.54	111.13	1.63	5.27	0.88	2.74
Westfield Group	1,299,241	3,939,148	1,653,833	115.66	4.13	1,511,042	76.02	32.55	108.65	99.02	0.60	1.75	2.22	6.48
Group Aggregate														
Comparable Group Mean	1,004,688	2,513,220	1,004,855	91.03	3.64	906,576	80.20	30.43	112.84	103.92	(0.36)	0.09	1.49	3.78
Comparable Group Median	947,070	2,211,611	977,710	101.90	3.74	919,567	76.02	32.38	112.54	105.13	0.61	1.40	1.76	3.14
Harleysville Mutual Ins Co.	1,245,608	4,137,848	1,310,115	93.19	4.31	1,326,056	74.99	34.38	109.47	101.83	1.32	4.31	2.08	7.30

Source: SNL Financial
Data reflects the P&C group reporting level

(1) 3 year Combined Ratio reflects 2008 - 2010
(2) 3 year ROAA and ROAE reflect 2008 - 2010

The Boenning and Griffin mutual comparables groups vary in their constituents due mainly to the different base metric used for filtering. Boenning chose to use a range of capital & surplus while Griffin used a range of direct premiums written. Either method is an acceptable starting criteria for selecting comparables. Both the Boenning and Griffin comparables groups show an industry which has been plagued by catastrophe losses. The Mutual Comparable Group analyzed by Boenning showed that Harleysville Mutual was relatively stronger than its peers compared to the comparables group analysis of Griffin. However, such relative "improvement" between analyses does not conflict with the apparent conclusion of the Company's management or the Boards of Directors that the Company was in need of a strategic directional change to achieve size and scale. Supporting this conclusion is the Company's combined ratio of 109.47% and expense ratio of 34.38%, which both lag the peers and represent the most concerning challenges facing the Company at the time. In this regard, Boenning's conclusion based on this analysis is consistent with Griffin's.

In order to review Griffin's analysis of the financial characteristics of Nationwide, Boenning also used the comparable companies approach. An initial screen for insurance companies with capital & surplus above $4 billion produced a group of 24 companies. This was an appropriate initial filter as Nationwide had capital & surplus of $12.8 billion making its large size relatively unique in the personal lines insurance universe. Boenning professionals placed the emphasis of the comparables approach on insurers focused on personal lines. From the initial 24 insurers we removed companies which exhibited the following:

- Companies with heavy weighting of commercial lines
- Reinsurers
- Conglomerates which would not be valued as pure insurance companies

After making these adjustments, Boenning's comparable companies list included 14 companies ("***Nationwide Comparable Group***"). Additionally, of these 14 companies, three had the NAIC ownership structure of a mutual company. For comparison purposes, we created a subset of these ("***Mutual Subset Group***") to show the mean and median for these entities as a stand-alone group. A summary of the comparisons and their respective operating metrics are included in the analysis below:

Table 24) Nationwide Mutual Comparable Group

Nationwide Mutual Comparable Group As of and for the LTM period 6/30/2011														
Company Name	Average Capital & Surplus ($000)	Net Total Assets ($000)	Total Revenue ($000)	Net Prem Writ / Avg C&S (%)	Net Investment Yield (%)	Direct Premiums Written ($000)	Loss Ratio (%)	Expense Ratio (%)	Combined Ratio (%)	3 yr Avg Combined Ratio (%)	ROAA (%)	ROAE (%)	(1) 3 yr Avg ROAA (%)	(1) 3 yr Avg ROAE (%)
ACE Ltd.	5,919,934	24,542,526	5,582,755	74.50	6.09	8,120,921	75.81	21.02	96.83	89.52	4.57	18.67	3.24	13.37
Allstate Corp.	15,343,016	44,770,626	26,411,415	163.65	3.34	26,556,576	79.15	25.96	105.11	99.18	(0.12)	(0.34)	2.27	6.63
American Family Mutual*	4,346,305	11,823,876	5,857,328	117.31	3.01	5,501,967	79.36	29.83	109.24	105.78	1.06	2.88	0.53	1.19
Auto Club Exchange Group	4,079,287	7,185,868	2,838,410	61.82	3.39	2,632,702	72.41	25.06	104.14	95.84	2.42	4.05	3.99	6.75
Auto-Owners Insurance Co.*	5,818,044	13,881,127	5,029,327	79.75	3.67	4,839,040	87.14	26.53	113.71	102.87	(0.08)	(0.19)	2.07	4.61
CNA Financial Corp.	10,467,230	43,363,657	6,886,254	60.87	4.65	7,942,288	80.27	32.69	113.27	110.20	0.60	2.53	0.77	3.76
Erie Insurance Group	4,943,612	11,248,639	4,713,475	83.63	4.65	4,151,135	78.67	27.63	106.40	96.40	3.63	7.98	0.45	0.91
Fairfax Financial Holdings	5,575,480	16,567,964	3,740,759	57.42	2.44	2,275,059	85.40	35.41	121.06	110.46	0.06	0.18	3.33	9.11
Hartford Financial Services	14,769,466	41,117,973	11,133,663	66.36	4.25	10,495,467	73.21	29.31	102.71	94.79	2.34	6.45	2.35	6.58
Liberty Mutual	15,244,901	68,309,628	23,938,188	141.83	5.28	25,701,845	77.67	29.36	107.30	103.22	1.65	7.29	2.05	9.20
Progressive Corp.	5,524,206	20,097,155	15,283,424	265.85	2.75	14,507,872	70.71	22.43	93.14	93.47	6.00	21.58	4.77	17.68
State Farm Mutl Automobile Ins*	58,935,635	136,947,358	55,173,237	87.06	3.26	52,482,107	84.63	24.54	109.17	108.75	0.07	0.15	0.25	0.56
USAA Insurance Group	15,722,796	28,511,321	11,480,562	70.35	2.97	11,649,342	81.05	13.48	102.72	97.46	1.00	1.73	3.07	5.36
Zurich Financial Services Ltd	12,133,982	59,172,998	20,135,353	157.46	3.43	27,277,196	71.75	32.10	103.90	101.59	1.28	6.26	1.30	6.29
Group Aggregate														
Comparable Group Mean	12,773,135	37,681,480	14,157,439	106.28	3.80	14,580,966	78.37	26.81	106.34	100.68	1.75	5.66	2.17	6.57
Comparable Group Median	8,193,582	26,526,923	9,009,959	81.69	3.41	9,308,194	78.91	27.08	105.76	100.38	1.17	3.47	2.17	6.43
Mutual Subset Group Mean*	23,033,328	54,217,454	22,019,964	94.71	3.32	20,941,038	83.71	26.97	110.71	105.80	0.35	0.95	0.95	2.12
Mutual Subset Group Median*	5,818,044	13,881,127	5,857,328	87.06	3.26	5,501,967	84.63	26.53	109.24	105.78	0.07	0.15	0.53	1.19
Nationwide Mutual Group	12,779,760	40,001,859	15,436,498	113.09	2.63	14,875,395	74.30	34.37	108.71	104.73	(0.71)	(2.20)	1.41	4.33

Source: SNL Financial
Data reflects the P&C group reporting level
*Mutual Subset Group reflects companies within the Nationwide Mutual Comparable Group which have the NAIC ownership structure of a Mutual Company.

(1) 3 year ROAA and ROAE reflect 2008 - 2010

Nationwide's combined ratio is slightly elevated relative to the mean and median of the Nationwide Comparable Group but below the mean and median of the Mutual Subset Group. Furthermore, the Nationwide loss ratio of 74.30% is meaningfully lower than both the Nationwide Comparable Group's and Mutual Subset Group's mean and median, respectively. Nationwide's 3 year average combined ratio of 104.73%, while is slightly lower than the mutual subset peers, is higher than the overall comparable group but within the range. The 3 year combined ratios for each company illustrate the uptick in losses and expenses in the LTM period analyzed.

The Nationwide Comparable Group median for LTM ROAA and ROAE were 1.17% and 3.47%, respectively. Nationwide reported ROAA of (0.71%) and ROAE of (2.20%). Despite these negative returns for Nationwide in the recent period, Nationwide's returns are better over the 3 year period from 2008 to 2010. Nationwide reported a 3 year average ROAA of 1.41% and ROAE of 4.33% , well within the range of the Nationwide Comparable Group (median 3 year average ROAA and ROAE of 2.17% and 6.43%). Moreover, the Mutual Subset Group of comparables reported a median 3 year average ROAA and ROAE of 0.53% and 1.19%, respectively, below that of Nationwide.

The comparative analysis of Nationwide by Griffin appears to be reasonable from a financial point of view based upon the companies chosen, metrics used, and relative comparison of operating results. In this manner, Boenning's conclusion based on this analysis is consistent with Griffin's.

Griffin also analyzed the pro forma combined financial condition of the two companies after the Transaction. Griffin illustrated a pro forma return on capital & surplus of (0.42%) after making normalizing adjustments to the Nationwide statutory income statement. These adjustments and conclusions appear reasonable based upon some of the unusual circumstances surrounding the P/C industry currently. Additionally, Griffin concluded to a pro forma combined ratio of 103.70%, which is lower than both Nationwide and Harleysville Mutual individually. The pro forma analysis by Griffin also projects a BCAR rating of 222, which is lower than Nationwide at 231.4 and Harleysville Mutual at 309.6. However, the pro forma A.M. Best rating is "A+", which is Nationwide's current rating despite diluting the rating with Harleysville Mutual's "A".

Boenning believes the Griffin analysis provides a reasonable view of the pro forma effects of the Transaction.

The forgoing analysis established context for Griffin's approach to determining fairness. After establishing context, Griffin conducted its analysis.

(d) Impact Analysis

Griffin examined the potential effects of the Transaction on a series of constituencies in order to assess the fairness of the Transaction to Harleysville Mutual. This analysis supports the Harleysville Mutual Board of Directors' conclusion stated in Harleysville Mutual's response to the Department's PIS comments that "the proposed Merger was fair and reasonable, and conferred benefits to the Harleysville Mutual Policyholders." Further, Griffin's impact analysis may be relevant to the Department in its determination of whether the Transaction meets the standard of Section 991.1402 (f)(1)(iv) of the Act. The constituencies examined were:

- Policyholders (as both creditors and as members)
- Creditors
- Employees
- Community
- Agents

In summary, Griffin concluded that the Transaction benefited the constituencies as follows:

Overall:

- "*Financial Stability*
  - *By merging with Nationwide Mutual, Harleysville Mutual will benefit from higher A.M. Best Financial Strength Rating and Financial Size Category, which should enhance its claims paying ability and thus, credibility with potential policyholders. Agents, and reinsurers, notwithstanding a decline in BCAR*
- *Diversification of Business Lines*
  - *Allows for diversification of risk and provides cross selling opportunities*
  - *Nationwide has multiple specialty lines in agribusiness, financial services, etc.*
- *Diversification of Geographic Presence*
  - *Nationwide provides greater geographic diversity which allows additional protection of surplus during region-specific catastrophes*
- *Size and scale*
  - *Opportunity to leverage fixed costs over a much larger organization and expense base*
- *Large capital base and access to capital markets*

- *Opportunity for improved earnings through cost savings and revenue enhancements*
- *Substitution of a more favorable pooling agreement from a less favorable agreement*
- *Improved capital and reserve coverage"*

Specifically, Griffin reviewed each constituent as follows:

"Policyholders (as Creditors):

- *The combined entity will be a stronger competitor in most geographies in most product lines than Harleysville standalone. This should benefit Harleysville and its policyholders by increasing profitability, claims paying ability, and surplus*
- *The combined entity will offer more products to its policyholders than Harleysville standalone. This cross selling capability should benefit Harleysville and its policyholders by increasing profitability, claims paying ability, and surplus*
- *The combined entity will have a broader geographic footprint which will benefit Harleysville and its policyholders by diversity of risk for catastrophic losses and also presents the potential for increased profitability, claims paying ability, and surplus*
- *The combined entity will have the ability to spread fixed costs over a wider revenue base, resulting in the potential for increased profitability, claims paying ability, and surplus*

Creditors:

- *Improved credit ratings*
- *Improved financial strength ratings*
- *Improved liquidity*
- *The combined entity will have multiple distribution channels and more products and services, as well as a broader geographic footprint which will benefit Harleysville and its creditors by diversity of risk for catastrophic losses and also presents the potential for increased profitability, claims paying ability, and surplus"*

Griffin provided analysis to support the conclusions listed above in its presentation. The Griffin analysis appeared thorough and the conclusions rendered reasonable from a financial point of view.

"Policyholders (as members):

- *Dividend policies*
  - *Policyholders in each company have right to dividends as, if and when declared by the board*
  - *In practice, both companies pay small policyholder dividends*
- *Change in pooling arrangement*
- *Policyholder rights to or claims on surplus*
  - *Rights upon solvent liquidation*
- *Rights with respect to governance of the combined entity*
  - *Voting rights*
  - *Rights upon fundamental change or demutualization*

- *Continuation of policies and premium costs*
  - *Policyholders have an interest in continued membership and insurance coverage*
- *Surplus generation*
  - *Ability to generate surplus enhances claims paying ability and member interest in surplus"*

Although no direct comparison of Nationwide and Harleysville policies was performed, the policies will continue in the same form as Harleysville policies for a period of time post Transaction.

Griffin also noted Nationwide's "A+" A.M. Best rating versus Harleysville Mutual's "A" rating. Boenning noted that both Moody's and S&P affirmed Nationwide's rating (with a "stable" outlook) after the merger announcement and that A.M. Best commented that its ratings are unchanged. Griffin concluded that, from a financial point of view, Policyholders appeared to be at least as well off, if not better, under all but one of Griffin's comparisons.

As far as Policyholders' rights were concerned, Griffin prepared the following table illustrating that rights for Harleysville Policyholders were as good as or better than corresponding rights for Nationwide policyholders (Please refer to Section VII for a more complete explanation of Policyholders' rights.)

Table 25) Policyholders' Rights Summary

	Harleysville Mutual	Nationwide
Right to vote for Directors	Yes	Yes
Right to vote on fundamental transactions	Yes- Policyholders must vote on mergers or demutulizations	Yes- policyholders must vote on mergers or demutualizations
Rights upon demutualization	Subscription rights- Policyholders receive the first right to buy stock, based upon an appraisal value but get no free distrubition of surplus	Right to free distribution of surplus

Source: Griffin Presentation

In addition, Griffin noted that (pursuant to the Merger Agreement), "all policies in force will carry over to Nationwide", and, "renewal and premium levels will be subject to Nationwide's

policies & procedures and are not guaranteed – similar to the current arrangement at Harleysville." Griffin's analysis of Policyholders (as Members) appeared to be thorough and complete.

The one comparison where the Policyholders were not as well off was in the case of policyholder rights in the event of a liquidation of the insurance company. According to the Griffin Presentation, Griffin was advised that Pennsylvania law is ambiguous with respect to the rights of policyholders upon solvent liquidation. Griffin noted that, "Accordingly, for purposes of our analysis and in the interest of being conservative, we assume the Transaction will be dilutive to Harleysville policyholders on a pro forma basis. However, the likelihood of a solvent liquidation is so remote, this assumed dilution does not alter our conclusion." Boenning believes this approach was reasonable from a financial point of view; however, we believe the Griffin Presentation should have more clearly communicated that solvent liquidations are generally unusual occurrences. Further, should a solvent liquidation occur, the actuarial analysis required to determine the amount of capital & surplus payable to each Policyholder is extremely complex and likely does not approximate the simplified calculation of capital & surplus divided by the number of Policyholders.

Another potential issue for Policyholders is that Policyholders' current voting power is based on the relatively small size of the Harleysville Mutual voting pool, but these Policyholders will now be only a small portion of the overall Policyholder pool of Nationwide. This more than likely will not be a major determining factor for a Policyholder in its overall review of the Transaction, but we have noted it nevertheless.

(e) Policyholder "Compensation"

Based upon review of mutual-to-mutual mergers found in the Griffin Presentation, there appeared to be nothing unusual about the Policyholders not receiving compensation in the Transaction. Further, according to the Department, there is no requirement in Pennsylvania to make payments to Policyholders in connection with a mutual merger. Boenning discussed with the Company's management and their Advisors the following facts relating to the Harleysville Mutual's constituents:

- The purchase of P/C insurance policies typically does not carry with it an expectation of an investment return.
- Any constituent could buy stock in HGIC if it wanted to invest in the Company's business.

- Agents and employees could purchase stock in the open market and, in fact, could buy at a discount to market via the employee stock ownership plan and agent stock purchase plan under certain circumstances.

Boenning found the Griffin analysis of Policyholders' "Compensation" to be thorough and complete from a financial point of view.

Boenning also examined other types of transactions for information that could be helpful to the analysis of the fairness to Policyholders. Although Harleysville Mutual's "downstream stock company" structure is a rare structure in the insurance industry, an analogous structure exists more commonly in the thrift/banking industry. The structure is that of the publicly-traded mutual holding company ("***MHC***"). A MHC involves a mutually controlled organization owning a majority of the outstanding shares in a stockholder owned entity, with public stockholders owning the minority portion. Although the structure is technically different from the Harleysville Mutual form, we believe certain insights gained from transactions involving MHCs might be instructive in reviewing the Transaction from a financial point of view.

For example, Investors Bancorp Inc. (MHC) ("***Investors***") announced the acquisition of Brooklyn Federal Bancorp, Inc. (MHC) ("***Brooklyn***") on August 16, 2011, and closed the transaction January 6, 2012. In the transaction, Investors purchased the minority stockholders' interest in Brooklyn for cash while Brooklyn's depositor rights were transferred to Investors. This seems almost parallel to Nationwide's purchase of HGIC and merger with Harleysville Mutual (with transference of Policyholder's rights to Nationwide). A number of MHC mergers have occurred in the thrift industry, to our knowledge, largely without complaint and with the approval of the banking regulators.

Other items of note in the Brooklyn transaction include:

- Much like this Transaction, Brooklyn directors and Brooklyn itself agreed to vote their shares in favor of the transaction, thus ensuring with their majority position approval of the transaction. A more complete discussion of the Voting Agreement from this Transaction is found in Section VIII. The shares owned by the MHC were converted into shares in the buyer (also an MHC), a different approach than that taken in the Transaction; however, we believe the economic effect to be similar (according to the Investors' proxy, an alternate proposal to Brooklyn would have cancelled those same shares).

(f) Employees

Given the commitments made by Nationwide regarding employees noted in Section IV, Griffin noted numerous benefits to employees and management from the Transaction. Some of these benefits to Harleysville Mutual's employees include the opportunity to continue to work and retain the culture in place prior to the Transaction. In addition, growth of the pro forma entity would allow employees new opportunities only available through employment in a larger company. Such benefits were consistent with the covenants in the Merger Agreement and commentary in other documentation reviewed by Boenning. Griffin's conclusion as to the beneficial effects of the Transaction to the Company's employees appeared reasonable from a financial point of view. Boenning also noted that the Griffin Presentation was silent as to the effect of the Transaction on employees not working in "Harleysville East" locations (as defined in the Merger Agreement). It is possible that the Transaction is detrimental to some subset of employees. For the employees in the aggregate, however, we believe Griffin's conclusion is correct.

(g) Community

Given the commitments made by Nationwide regarding the community, Griffin noted numerous benefits to the community from the Transaction. Such benefits were consistent with the covenants in the Merger Agreement and commentary in other documentation reviewed by Boenning. Boenning notes that Nationwide's commitments to the Company's employees and the community are for a two-year period. However, given the Allied example, a longer period of time could be implied. This is not a guarantee, but it is a positive sign for the potential financial impact of the Transaction on the community at large. Furthermore, Boenning believes the community could see long-term economic benefits from the job creation associated with growing the pro forma business in the Harleysville, Pennsylvania location. Nationwide management confirmed such observations in its interview by Boenning.

(h) Agents

Griffin noted the following: Nationwide's A+ rating, Nationwide's more significant product set, commitment to independent agent channel, and no material overlaps with Nationwide's captive agency force. In management interviews, management acknowledged a very small percentage of its agents are currently Allied agents as well as "Harleysville" agents and therefore could experience

reductions in available markets. This was referred to as a "limited number." Although no direct comparison between commission structures of "Harleysville" and Nationwide was performed, existing "Harleysville" agents will continue to write Harleysville-branded policies and receive the same commissions unless and until changed.

Griffin summarized the impacts on Harleysville Mutual constituents as follows:

Table 26) Harleysville Mutual Constituents Summary

Policyholders (claims payout)	- 'A+' rated company - Stronger surplus - Redundant reserves - Strong liquidity - Prospect for stronger surplus generation and capital market access
Policyholders as Members	- Prospect for stronger surplus generation - Comparable governance rights other than demutualization - Better rights upon solvent liquidation
Employees & Management	- Commitment to continued employment - Honoring or buying out existing contracts - Strong employee benefits packages
Community	- Commitment to maintain business model, jobs, and charitable giving - Access to Nationwide Foundation - Commitment to maintain operations means preservation of company and continued employee civic involvement
Agents	- "A+" rated company - Stronger product suite - Little conflict with captive agents

Note - Nationwide agreed to the following covenant in Section 7.10 of the Merger Agreement:

> *"During the two-year period following the Closing Date, Nationwide Mutual agrees, to the extent permitted by applicable Law, that (i) it will not, and will cause its Subsidiaries and Affiliates not to, make major operational changes in Harleysville East to the core business functions of the property and casualty business of the Harleysville Parties set forth in Section 7.10(i) of the Nationwide Mutual Disclosure Schedule; (ii) in Harleysville East it will continue to utilize the Harleysville brand with respect to the lines of property and casualty insurance and insurance products, either independently or in conjunction with one or more brands of Nationwide Mutual or one of its Affiliates, as more particularly described in Section 7.10(ii) of the Nationwide Mutual Disclosure Schedule, (iii) it will substantially maintain or exceed the overall number of employees, as of the date hereof, at HGI's headquarters located in Harleysville, Pennsylvania and will not cause a reduction in force to occur at the Worcester, Massachusetts, location; (iv) it will substantially maintain or improve the philanthropic and charitable contributions and activities described in Section 7.10(iv) of the Harleysville Mutual Disclosure Schedule consistent with the historical practices of Harleysville Mutual and HGI since September 30, 2010; and (v) it will (a)*

migrate each employee of HGI (a "Continuing Employee") to the Benefit Plans of Nationwide Mutual or its Affiliates no later than January 1, 2013, or at such earlier time as determined by Nationwide Mutual or one of its Affiliates in its sole discretion; (b) give each Continuing Employee credit under the Benefit Plans of the Nationwide Parties or its Affiliates towards applicable deductibles, co-payments and annual out-of-pocket limits for expenses incurred under the Benefit Plans of HGI or any Subsidiary of HGI during the plan year in which the Closing Date occurs; (c) cause any preexisting conditions or limitations, evidence of insurability, exclusions and waiting periods with respect to participation and coverage requirements under any of the Benefit Plans of the Nationwide Parties or its Affiliates to be waived with respect to Continuing Employees and their eligible dependents to the same extent such limitations are waived under any comparable plan of HGI; and (d) give each Continuing Employee service credit based upon such Continuing Employee's service credit with HGI, Subsidiaries of HGI, Harleysville Mutual, and Harleysville Mutual Subsidiaries for purposes of eligibility to participate and vesting credit under each applicable Benefit Plan of the Nationwide Parties or its Affiliates (but, for avoidance of doubt, excluding benefit accrual under any defined benefit pension plan, cash-balance plan, or retiree medical) and entitlement to benefits under each severance or vacation plan of the Nationwide Parties or its Affiliates, in each case, as if such service had been performed with the Nationwide Parties or its Affiliates. Without limiting the generality of Section 11.7, this Section 7.10 shall be binding upon and inure solely to the benefit of each of the Parties to this Agreement, and nothing in it, expressed or implied, is intended to confer upon any other Person any rights or remedies of any nature whatsoever and, specifically but without limiting the generality of the foregoing, nothing in it will create any third party beneficiary rights in any current or former employee, director or individual independent contractor of the Harleysville Parties or any of their Subsidiaries in respect of continued employment (or resumed employment) or service or any other matter."

(i) Conclusion Regarding the Griffin Fairness Opinion

Griffin opined as to the fairness of the Parent Merger in terms of Harleysville Mutual. Griffin evaluated the fairness of the Transaction by factoring in each constituency considered by the Harleysville Mutual Board of Directors and then rendering an opinion based upon the entire entity. Based on Boenning's analysis and review of Griffin's fairness opinion and presentation, as well as discussions with Griffin, we believe Griffin considered the appropriate factors, analysis and approaches and that its opinion and presentation reports were thorough and complete from a financial point of view. Minor differences of opinion in the analysis were noted by Boenning in the foregoing. We believe the methodologies utilized and conclusions reached were reasonable in light of the factors considered, methods used, and assumptions made as described by Griffin. Given the lack of historical precedent for mutual-to-mutual merger fairness opinions, we do not believe an industry standard presentation/report format exists with which to compare the Griffin report, so Boenning's observations are based on its experience with fairness opinions in general.

c. *Stevens & Lee, P.C. ("**Stevens & Lee**") opinion*

Harleysville Mutual engaged Stevens & Lee to provide its:

> *"opinion with respect to the fiduciary duty of directors of a Pennsylvania mutual insurance company. Specifically, in connection with a proposed merger of HMIC with and into Nationwide Mutual Insurance Company…"*

[redacted]

The opinion also contained an acknowledgement of certain facts as Stevens & Lee understood them (these facts appear to be consistent with the Merger Agreement and other documents reviewed by Boenning). [redacted]

Stevens & Lee's opinion also noted that it is affiliated with Griffin, who (as referenced above) provided a fairness opinion to Harleysville Mutual in connection with the Transaction. Please refer to the discussion of this issue earlier in this Section V.

Stevens & Lee made a presentation to the Harleysville Mutual Board of Directors on September 27, 2011 ("***Stevens & Lee Presentation***"). The Stevens & Lee Presentation [redacted]

Boenning is not a law firm and is not qualified to evaluate a legal opinion or presentation as to its correctness from a legal perspective. Boenning reviewed the presentation from a financial

point of view to determine a) if the directions it provided appeared understandable to a reasonable business person (such as a member of the Harleysville Mutual Board of Directors) who might utilize the advice and b) if the advice provided appeared to be an opinion upon which the Harleysville Mutual Board of Directors relied in their decision regarding the potential Transaction.

Boenning, using the perspective described above, [redacted]

In its presentation, Stevens & Lee examined the pertinent provisions of Pennsylvania law in detail and compared/contrasted the laws of most states (especially Delaware) with those of Pennsylvania listing each duty and an explanation/application of Pennsylvania law. Boenning found the illustrations understandable.

Conclusion Regarding the Stevens & Lee Presentation

Boenning is not a law firm and is not providing a legal opinion or legal advice regarding any legal matters. The Stevens & Lee Presentation appeared to provide a summary we found understandable from a financial point of view. Further, and as noted above, management of the Company indicated the Harleysville Mutual Board of Directors relied on its Advisors in connection with the Transaction. Therefore, it appears the Harleysville Mutual Board of Directors relied on the advice of Steven & Lee and made its decisions about the potential Transaction consistent with such advice.

C. Understand Alternatives to the Transaction

Boenning's Engagement Letter with the Department included the following:

> "(f) Understand the alternatives to the Transaction considered by the Company in determining to proceed with the Transaction."
>
> "(k) Compare the values derived by Boenning's financial analysis relative to values potentially available from other alternatives to the Policyholders, including a subscription rights demutualization."

As Boenning's engagement evolved, it became apparent that items (f) and (k) in the Engagement Letter overlap significantly in some cases and are most effectively handled in a single, comprehensive Section of the Report. In accordance with its Engagement Letter, Boenning reviewed analysis relating to the strategic alternatives the Company reviewed prior to determining to proceed with the Transaction. Where possible, Boenning attempted to determine the accuracy of the assessment of each strategic alternative qualitatively and quantitatively by performing its own analysis.

Prior to hiring Advisors to assist in understanding strategic alternatives, the Company hired a director of M&A in 2008 in an effort to solve its size and scale challenges. As stated in Section IV, Harleysville examined over 50 companies as potential acquisition targets. Management estimated that they spoke with 30-40 companies regarding a transaction. The majority of companies, while desirable and financially profitable, had no interest in discussing a sale. The few companies that did indicate an interest in being acquired were not strong financial performers and were more likely to be a financial burden for the Company pro forma than becoming synergistic. In support of its acquisition strategy, the Company in early 2009 reviewed its corporate structure and the possibility of demutualizing to provide additional capital for its M&A effort. The Company concluded not to pursue a demutualization due to the execution risk of such a transaction, lack of quality acquisition targets, and the resulting excess capital that might not be able to be deployed profitably. The discussion and analysis of alternatives considered by the Company consists primarily of those offered in the Credit Suisse and Griffin presentations introduced earlier in this Section.

a. Credit Suisse

Credit Suisse has been a financial Advisor to the Company for several years and has helped the Company assess corporate and strategic alternatives. Below is a summary from its June Presentation of the alternatives reviewed with the Boards of Directors:

- demutualizations
- acquisition by Harleysville Mutual of the publicly traded shares of HGIC
- sale of all or part of HGIC

- restructuring of the pooling agreement between Harleysville Mutual and HGIC
- acquisitions by HGIC
- mergers involving Harleysville Mutual where Harleysville Mutual is the surviving entity; sale of some or all of Harleysville Mutual's shares in HGIC such that the Harleysville Mutual would no longer have a controlling interest in HGIC
- combined merger or sale involving Harleysville Mutual and HGIC

Credit Suisse and the Boards of Directors concluded that all of the strategic alternatives considered by Credit Suisse and the Boards of Directors were either not able to be implemented/ executed from a financial or practical standpoint, or, if actually implemented, would not solve the Company's identified challenge of addressing size and scale issues.

b. Griffin

As noted earlier in this Section V, the Harleysville Mutual Board of Directors obtained a fairness opinion from an independent financial Advisor (Griffin) regarding the fairness of the Parent Merger. As the independent advisor, one of Griffin's main objectives was to:

> *"Assist the board in meeting its duty to be informed, outline (i) other alternative structures available with respect to the Nationwide transaction…"*

Griffin analyzed seven potential strategic alternatives in respect to the Transaction. They are as follows:

- Remain Independent
- Merge with Nationwide with no change to HGIC's structure
- Merge with Nationwide with purchase of all shares of HGIC
- Merger with Nationwide; Nationwide purchases HGIC public shares and Harleysville Mutual pays special dividend to Policyholders
- Harleysville Mutual converts from mutual to stock form and purchases minority shares of HGIC, then sells to Nationwide
- Harleysville Mutual enters into a sponsored discounted merger conversion in which a stock insurance company acquires Harleysville Mutual
- Harleysville Mutual converts from mutual to stock form and HGIC uses its stock to acquire Harleysville Mutual

Following is a review of alternatives examined by Griffin on behalf of Harleysville Mutual's Board of Directors.

(a) 1. Remain Independent:

"Harleysville Mutual remains independent and continues to operate as a standalone entity. Harleysville Group continues to operate "as is"."

Some key considerations that Griffin and the Company looked at were as follows:

- *"[Harleysville] needs size and scale and geographic and product line diversification* (as noted in Section IV)
- *Historical inability to grow earnings and surplus and /or deploy excess capital*
- *Number of general economic, industry specific factors will make growth problematic for the next 3-5 years*
- *Long and rocky road to economic recovery*
- *Likely prolonged low interest rate environment and pressure on investment income*
- *Potential for additional catastrophic losses and impact on A.M. Best rating*
- *Pressure on market price for the [HGIC] common stock"*

Based on its review of Griffin's analysis, Boenning agrees that remaining independent would not likely achieve the Company's goal of attaining greater economic size and scale. The Company lacks the scale to be able to continually grow and increase profitability (please refer to Section III for a discussion of Harleysville Mutual's financial performance and outlook). Over the past several years Harleysville Mutual's top line revenues have declined (2% in 2007 and 4% in 2008). Some or all of the items noted by Griffin above would make it difficult for the Company to achieve the size and scale it believes it requires. In addition, Boenning notes the continued soft market in 2011 would make the outlook for organic growth even less promising, and prolong the time to achieve scale.

(b) 2. Merge with Nationwide with no change to HGIC's structure:
"Harleysville Mutual merges with Nationwide Mutual and Harleysville Group, the majority owned public subsidiary and remains as a majority owned subsidiary of Nationwide/Harleysville combined."

Some key considerations that Griffin and the Company looked at were as follows:

- *"Same considerations as for the Transaction with Nationwide except minority public stockholders will share in the future earnings and profits and potential losses of Harleysville Group*
- *Adverse impact on Harleysville Group shareholders (including Harleysville Mutual D&Os) if Nationwide alters outstanding pooling agreement*
- *The projected timeline for this alternative is between 60 and 120 days*
- *The execution risk associated with the alternative is "reduced compared to proposed structure because no purchase of minority interest"*

Based on its review of Griffin's analysis, Boenning agrees that merging with Nationwide with no change to HGIC's structure would not meet all of the Company's transaction objectives.

While such a transaction could assist with size and scale challenges and possibly perpetuate and grow Harleysville Mutual's culture and brand, HGIC's stockholders could be adversely affected by changes in the pooling agreement. In addition, such a transaction would require Nationwide to be comfortable with a relatively unusual corporate structure and manage duties to a minority (public stockholders). Boenning also notes that HGIC stockholders would lose a significant merger premium if a deal were to be structured in this form. Importantly, such a transaction was never presented to the Company.

(c) 3. Merge with Nationwide with purchase of all shares of the HGIC:

"Harleysville Mutual merges with and into Nationwide Mutual, and all shares of the public subsidiary, Harleysville Group, including Harleysville Mutual's ownership, are purchased at the take out price. Since 54% of the total consideration will be paid to Harleysville Mutual, Nationwide Mutual, after the merger, will in effect be repaid such consideration."

Key considerations that Griffin looked at were:

- *"May appear better optically but no net economic change*
- *The proposed timeline is the same as the proposed transactions*
- *The execution risk is the same as the proposed transaction"*

Based on its review of Griffin's analysis, Boenning agrees that merging with Nationwide with purchase of all shares of HGIC essentially offers no net economic change relative to the Transaction.

(d) 4. Merger with Nationwide; Nationwide purchases HGIC public shares and Harleysville Mutual pays special dividend to Policyholders:

"Harleysville Mutual merges with Nationwide Mutual [and] Nationwide Mutual buys interests in Harleysville Group public shareholders for cash and shares owned by Harleysville [Mutual] for cash. Harleysville [Mutual] dividends all or a portion of the cash it receives from Nationwide to its policyholders."

Some key considerations that Griffin and the Company reviewed were:

- *"Unless legally required or practically compelled to do so, why decrease pro forma combined surplus and pro forma liquidity.*
- *Note that this is similar economically to the transaction structure suggested by Company B.*
- *The proposed timeline is the same as the proposed transaction.*

- *The potential execution risk is reduced because of consideration paid to Policyholders."*

Boenning was unable to make a direct comparison of this alternative 4 because the theoretical transaction proposal does not exist. Based on its review of Griffin's analysis, Boenning agrees that merging with Nationwide, with Nationwide purchasing all of the HGIC shares and Harleysville Mutual paying a special dividend to Policyholders would be significantly more beneficial economically to Policyholders. Boenning also agrees with Griffin that considering all the constituents, in the aggregate, such a transaction is not more economically beneficial to Harleysville Mutual than the Transaction.

In addition, the Harleysville Mutual Board of Directors has stated that it considered all constituents of the Company without preference for any one constituency in accordance with advice of counsel. Boenning notes that it is theoretically possible that such a transaction could be a more attractive alternative, in the aggregate, if terms of the Nationwide Transaction were the same and differed only with the addition of a Policyholder dividend. Boenning notes that although capital would be lowered by a dividend, Boenning does not believe that there would be a material diminishment of surplus and therefore significant change in the pro forma surplus and BCAR rating from a dividend as suggested by Griffin, should the transaction partner be sufficiently large.

(Boenning also notes that Company B's indication of interest received after the solicitation process is not comparable, with all things held equal, owing to its different transaction format and different (and economically worse) impact on Harleysville Mutual's community, agents, employees and culture and operations (please refer to Section VI)).

(e) 5. Harleysville Mutual converts from mutual to stock form and purchases minority shares of HGIC then sells to Nationwide:

"Harleysville Mutual converts from mutual to stock form and raises $1.5 billion in new capital. Harleysville acquires all shares of minority public shareholders of Harleysville Group. Harleysville Mutual could offer Harleysville Group shareholders a priority right to buy shares. Harleysville then sells to Nationwide or another party in an all cash transaction with excess capital used to fund purchase."

Some key considerations that Griffin and the Company looked at were:

- *"Results in overcapitalization and reduced ROE if no sale, as does cost of transaction to Nationwide or other buyers*
- *Valuation increases*
- *Pool of potential buyers for Harleysville increases*
- *Harleysville has studied and rejected standalone conversion in the past*
- *The proposed timeline is between 12-18 months for the conversion and sale*
- *The execution risk is medium to high because of elongated time frame"*

Boenning also notes that it would be unlikely that most buyers would pay a multiple for the excess capital present at the post transaction structure. Further, with a timeline of 12-18 months, the possibility that the general economy, capital markets, and/or M&A markets will change must be introduced, further adding to the risk of execution.

(i) Demutualization Overview

A demutualization transaction would convert Harleysville Mutual into a stock company. Typically, this would occur with a public offering of shares via a subscription rights offering. The influx of capital from this offering would allow the Company to make an acquisition in a larger size range than previously possible, as well as, provide other benefits and challenges associated with that form of corporate organization.

This type of transaction carries a significant amount of risk since it takes a relatively long time period to complete and does not guarantee successful deployment of the capital raised (e.g. a successful acquisition or organic growth). Additionally, Harleysville Mutual would experience a drastic decrease in return on equity from the new proceeds as a result of the offering.

In order to analyze this transaction option it's necessary to approximate the potential proceeds which could be raised Harleysville Mutual. The method used to assess the value of Harleysville Mutual is most typically the comparable companies approach.

(ii) Comparable Companies

If Harleysville Mutual were to engage in a demutualization, it would require a third party to perform an appraisal to determine estimated pro forma fair market value. Boenning is experienced in developing appraisals in connection with subscription rights demutualizations and the following is an abbreviated version of what would transpire in this process.

Harleysville Mutual must be considered relative to a group of public peers ("***Demutualization Comparable Group***") in order to analyze operating metrics versus industry peers. This would establish base case valuation multiples and allow the appraiser to decide on the appropriate discounts to place on the multiples in the appraisal process. The companies in the following Demutualization Comparable Group were chosen based mainly upon similarity in terms of asset size and insurance product lines as is common in these financial analyses.

Table 27) Demutualization Comparable Group

Operating Performance of the Demutualization Comparable Group As of and for the LTM period ended 9/30/2011 unless otherwise noted									
Company Name	Ticker	Net Premiums Written/ Avg Equity (x)	GAAP Expense Ratio (%)	GAAP Combined Ratio (%)	Investment Yield (%)	ROAA (%)	ROAE (%)	3 Year ROAA (%) 2008 - 2010	3 Year ROAE (%) 2008 - 2010
Selective Insurance Group, Inc.	SIGI	1.32	32.30	101.60	4.08	0.51	2.53	0.95	4.82
State Auto Financial Corporation	STFC	1.87	33.80	104.60	4.79	(7.47)	(26.93)	0.02	0.16
Tower Group, Inc.	TWGP	1.53	35.70	96.40	5.24	1.82	7.08	3.54	13.27
United Fire & Casualty Company	UFCS	0.78	31.00	99.90	4.09	(0.23)	(1.10)	0.23	1.06
Cincinnati Financial Corporation	CINF	0.68	32.80	101.70	5.18	1.03	3.14	2.86	8.82
Hanover Insurance Group, Inc.	THG	1.35	34.80	100.10	5.14	0.50	1.87	1.51	5.50
Donegal Group Inc.	DGICA	1.15	32.10	104.70	3.92	0.50	1.54	2.06	5.04
EMC Insurance Group Inc.	EMCI	1.14	36.90	102.30	5.12	(0.06)	(0.19)	2.16	7.58
W.R. Berkley Corporation	WRB	1.10	34.30	94.50	4.69	2.25	10.57	2.04	10.01
OneBeacon Insurance Group, Ltd.	OB	0.89	38.20	100.70	1.89	0.81	3.99	0.62	3.58
Navigators Group, Inc.	NAVG	0.84	36.90	100.70	4.25	0.91	3.99	1.80	8.18
Safety Insurance Group, Inc.	SAFT	0.94	31.30	96.70	3.81	1.51	3.38	4.17	9.86
Group Aggregate									
Comparable Group Mean		1.13	34.18	100.33	4.35	0.17	0.82	1.83	6.49
Comparable Group Median		1.12	34.05	100.70	4.47	0.66	2.84	1.92	6.54
Harleysville Mutual Insurance Company*		0.99	34.38	116.00	4.86	0.04	0.14	2.08	7.30

Source: SNL Financial
* figures reflect statutory financials

To gain further insight into the pro forma fair market value of Harleysville Mutual, the appraiser would need to look at the trading performance of the Demutualization Comparable Group. This is significant because it would give the appraiser multiples for similar insurance companies to Harleysville Mutual. Price to book is the most widely accepted metric for assessing value in a demutualization transaction and consistent with Boenning's experience. This would be the starting point for the appraiser before considering discounts to account for the risk factors specific to Harleysville Mutual. Some of the discounts common to demutualization transactions include risks associated with size, earnings prospects, management, liquidity of issue, subscription interest, stock market conditions, dividend outlook, and being a new issue. The following chart shows the trading characteristics of the Demutualization Comparable Group before any discounts.

Table 28) Demutualization Comparable Set Trading Metrics

Trading Performance of the Demutualization Comparable Group As of and for the LTM period end 9/30/2011										
Company Name	Ticker	Closing Price	Total Shares Outstand.	Total Market Value ($Ms)	Price / Book (%)	Price / Tang. Book (%)	Price / LTM EPS (x)	Current Div. Yield (%)	(1) Price / LTM Rev. (x)	(2) Price / Assets (%)
		12/27/2011								
Selective Insurance Group, Inc.	SIGI	18.11	54,220,632	981.9	90.37	91.03	36.96	3.98	0.62	17.08
State Auto Financial Corporation	STFC	13.98	40,274,009	563.0	93.57	93.84	NM	4.56	0.37	20.02
Tower Group, Inc.	TWGP	20.82	39,877,466	830.2	81.90	128.43	12.47	3.28	0.48	19.10
United Fire & Casualty Company	UFCS	20.50	25,502,667	522.8	76.27	79.95	NM	3.39	0.79	14.50
Cincinnati Financial Corporation	CINF	30.58	162,078,694	4,956.4	103.51	103.51	31.53	6.11	1.31	32.16
Hanover Insurance Group, Inc.	THG	35.27	44,870,688	1,582.6	64.08	69.78	35.27	3.10	0.44	12.48
Donegal Group Inc.	DGICA	14.33	25,552,384	377.1	94.32	95.95	62.30	3.99	0.83	29.35
EMC Insurance Group Inc.	EMCI	20.68	12,870,541	266.2	74.67	74.87	NM	4.13	0.57	21.25
W.R. Berkley Corporation	WRB	34.63	137,102,059	4,747.8	122.91	125.86	12.68	1.08	0.95	25.90
OneBeacon Insurance Group, Ltd.	OB	15.91	94,438,457	1,502.5	136.57	NA	32.47	6.16	1.33	25.36
Navigators Group, Inc.	NAVG	48.26	14,291,310	689.7	86.42	87.18	23.09	0.00	0.91	19.03
Safety Insurance Group, Inc.	SAFT	41.48	15,186,787	629.9	96.13	96.13	28.61	5.29	0.97	42.30
Group Aggregate										
Comparable Group Mean		26.21	55,522,141	1,470.85	93.39	95.14	30.60	3.76	0.80	23.21
Comparable Group Median		20.75	40,075,738	759.97	91.97	93.84	31.53	3.99	0.81	20.64

(1) Price / LTM Revenue is calculated by dividing market cap by LTM revenue
(2) Price / Assets is calculated by dividing market cap by total assets

(iii) Comparable Demutualization Transactions

While mutual-to-stock conversions are commonplace in the savings institution industry, such conversions and demutualizations are far less common in the insurance industry. Previous insurance subscriptions rights demutualizations, which include Old Guard Group Inc, Mercer Insurance Group, Eastern Insurance Holdings (Educators Mutual), and Penn Millers were oversubscribed, although purchasers with subscription rights for Eastern and Penn Millers common stock did not purchase enough stock to reach the pro forma valuation range, and a community offering was required to complete the sale of stock.

Further, the P/C industry is currently experiencing a challenging market, characterized by intense price competition, significant catastrophe losses, weak underwriting integrity, low relative interest rate environment for fixed income investments and an uneven and slow growth macro-economic environment. Each of these factors would likely serve to moderate subscription interest.

Conversely, demutualized insurance companies have historically had an immediate "step up" in value based on pro forma share price after an initial public offering ("***IPO***"). This is because investors in a conversion always buy at a discount to book value. Demutualizing insurance companies, in general, have historically had a positive return after an IPO, as shown in the following table. It should be noted, however, that the most recent demutualized insurance company did not experience such initial appreciation in stock value, reflecting potential investors' view of stock market conditions and risk of investing in IPO stock at that time.

Table 29) Demutualization Precedent Transactions

					Stock Price		
Company Name	Ticker	Offer Date	Price / Share Offering	Midpoint Discount	1 Day	1 Month	1 Year
Old Guard Group, Inc	OGGI	2/18/1997	$10	45%	$14.63	$14.63	$17.57
Mercer Insurance Group	MIGP	12/16/2003	10	46	12.15	13.66	13.36
Eastern Insurance Holdings (Educators Mutual)	EIHI	6/19/2006	10	42	11.41	12.90	14.99
Penn Millers	PMIS	10/9/2009	10	25	10.75	10.16	14.35

(iv) Valuation

Historically, median discount to median price to book multiples have ranged from 25% - 46%. Boenning estimates that the likely discount in a Harleysville Mutual demutualization transaction could be 35% - 45%. Using a mid-point discount of 40% results in an implied offering

amount of $1 billion. As illustrated in Table 30, the demutualization yields an approximately 57% pro forma price/book value.

Many offerings for savings institution conversions have not fulfilled the minimum number of shares offered in the subscription offering phase, and community and syndicated community offerings were necessary to complete the aggregate stock sale. There were 5 completed savings bank conversion offerings in 2011 at a mean and median price/book of 60.4% and 64.0%, respectively.

Table 30) Demutualization Valuation Range

	Minimum	Midpoint	Maximum
Total implied shares offered	85,000,000	100,000,000	115,000,000
Offering price	$10.00	$10.00	$10.00
Implied Gross Proceeds:	$850,000	$1,000,000	$1,150,000
Less: estimated expenses	(42,500)	(50,000)	(57,500)
Implied net offering proceeds	807,500	950,000	1,092,500
Less: ESOP	(80,750)	(95,000)	(109,250)
Net investable proceeds	$726,750	$855,000	$983,250
Total Revenue:			
LTM ended 12/31/2010	253,098	253,098	253,098
Pro forma revenue on net proceeds, pre-tax	8,456	9,948	11,440
Pro forma total revenue	261,554	263,046	264,538
Pro forma total revenue per share	3.08	2.63	2.30
Total Equity:			
As of 12/31/2010	904,393	904,393	904,393
Net offering proceeds	807,500	950,000	1,092,500
Less: ESOP	(80,750)	(95,000)	(109,250)
Pro forma total equity	1,631,143	1,759,393	1,887,643
Pro forma book value per share	19.19	17.59	16.41
Total Assets:			
Total assets at 12/31/2010	1,505,482	1,505,482	1,505,482
Net offering proceeds	807,500	950,000	1,092,500
Less: ESOP	(80,750)	(95,000)	(109,250)
Pro forma total assets	2,232,232	2,360,482	2,488,732
Pro forma total assets per share	26.26	23.60	21.64
Pro Forma Ratios:			
Price / LTM Revenue	3.25	3.80	4.35
Price / Book Value	0.52	0.57	0.61
Price / Total Assets	0.38	0.42	0.46
Total Equity / Assets	73.07%	74.54%	75.85%

Note: Harleysville Mutual financials presented in the table above reflect the stand-alone company level.
(1) The initial offering price is $10.00 per share and the number of shares offered is calculated by dividing the estimated pro forma market value by the offering price.
(2) Expenses estimated at 5%
(3) Proceeds invested at 10 yr US Treasury rate

The following analysis by Boenning shows the effects of a demutualization conversion and acquisition of HGIC by Harleysville Mutual. The acquisition of HGIC assumes a price of $55.00 a share and the resulting pro forma GAAP transaction adjustments have been applied. Boenning professionals have concluded that the surviving pro forma entity would be over-capitalized but to a

lesser degree than concluded by Credit Suisse's analysis due to the smaller amount of capital raised. Additionally, we estimate a pro forma ROAE of 3.35%, approximately 98 basis points lower than the 3 year average ROAE of Harleysville Mutual of 4.33%, which illustrates the negative effect of engaging in such a transaction until and unless an accretive acquisition can be completed.

Table 31) Demutualization Conversion and Acquisition by HGIC

	Pro Forma Conversion			→	HGIC Acquisition		
($ in millions except shares)	(1) 12/31/2010 Harleysville Mutual Insurance Company	(2) Demutualization Conversion Proceeds	Harleysville Mutual Insurance Company Pro Forma		3/31/2011 Harleysville Group	Transaction Adjustments	Surviving Entity Pro Forma
Cash and Equivalents	(6.4)	1,000.0	993.6		0.0	(748.1)	245.5
Investments	1,264.9	-	1,264.9		2,633.8	(365.8)	3,532.9
Intangible assets	-	-	-		23.4	772.3	795.7
Other assets	247.0	-	247.0		571.7	-	818.6
Assets	1,505.5	1,000.0	2,505.5		3,228.9	-	5,392.8
Total liabilities	601.1	-	601.1		2,454.1		3,055.2
Non-controlling interests	-	-	-		-		-
Common Equity	904.4	1,000.0	1,904.4		774.8	(341.6)	2,337.5
Liabilities & Equity	1,505.5	1,000.0	2,505.5		3,228.9		5,392.8

Note: Boenning professionals used an alternate accounting method to analyze transaction and achieved the same tangible equity.
(1) Harleysville Mutual Insurance Company balance sheet represents the statutory figures for the stand alone mutual company.
(2) Proceeds generated represent the midpoint of the conversion valuation range in Boenning & Scattergood analysis.
Note: 6/30/11 10Q shares outstanding as of 8/2/2011, basic shares outstanding of 27,165,247 fully diluted using the treasury stock method.
Note: Diluted shares outstanding of 28,128,386 shares at $55 a share

ROE Calculation	($000)
Pro Forma Net income	78,282
PF equity	2,337,547
ROE	3.35%

Boenning thought there was merit to exploring a variation in the preceding transaction alternative. The following analysis illustrates the effects of an acquisition of HGIC by Harleysville Mutual in the absence of a demutualization. In conducting this variation, Boenning assumed the same acquisition price for HGIC of $55 per share. Due to the lack of cash on Harleysville Mutual's balance sheet, this acquisition would have required the liquidation of investments totaling $754.5 million. This alternative transaction produces a pro forma return on equity of 5.85% and return on assets of 1.78%, which are both higher than in the demutualization alternative due to the lower surplus in this example. This transaction, however, does not provide Harleysville Mutual any new capital. Moreover, this transaction would not solve the issue Harleysville Mutual looked to rectify, which is a lack of size and scale. The pro forma entity in this example would more than likely continue to face the growth challenges described in detail by management. Further complicating this transaction alternative is the effect the greater leverage would have on the pro forma A.M. Best's Rating and BCAR rating. Whether or not this transaction is feasible, it does not address the main strategic concerns of the Company's management.

Table 32) Acquisition of HGIC by Harleysville Mutual Without Demutualization

($ in millions except shares)	(1) 12/31/2010 Harleysville Mutual	Harleysville Mutual Post Liquidation	3/31/2011 HGIC	Transaction Adjustments	Surviving Entity Pro Forma
	Investment Liquidation		HGIC Acquisition		
Cash and Equivalents	(6.4)	748.1	0.0	(748.1)	0.0
Investments	1,264.9	510.4	2,633.8	(365.8)	2,778.4
Intangible assets	-	-	23.4	772.3	795.7
Other assets	247.0	247.0	571.7	-	818.6
Assets	1,505.5	1,505.5	3,228.9	-	4,392.8
Total liabilities	601.1	601.1	2,454.1		3,055.2
Non-controlling interests	-	-	-		-
Common Equity	904.4	904.4	774.8	(341.6)	1,337.5
Liabilities & Equity	1,505.5	1,505.5	3,228.9		4,392.8

Note: Boenning professionals used an alternate accounting method to analyze transaction and achieved the same tangible equity.
(1) Harleysville Mutual Insurance Company balance sheet represents the statutory figures for the stand alone mutual company.
Note: 6/30/11 10Q shares outstanding as of 8/2/2011, basic shares outstanding of 27,165,247 fully diluted using the treasury stock method.
Note: Diluted shares outstanding of 28,128,386 shares at $55 a share

(v) Conclusion

If Harleysville Mutual elected a demutualization transaction, we believe it would have potentially raised approximately $1 billion in additional capital proceeds. This would have caused significant overcapitalization and in turn a significant reduction in return on equity. Boenning's conclusion is largely consistent with the opinions given by Credit Suisse and Griffin. Importantly, as an independent financial advisor, Boenning's analysis is financial in nature and the Boenning analysis does not address important non-financial issues regarding a decision to demutualize Harleysville Mutual.

Based on its review of Griffin's analysis, Boenning agrees that converting from mutual to stock form and purchasing minority shares of HGIC, then selling to Nationwide or another party is a potentially more difficult, risky, and time consuming alternative than a simultaneous Parent Merger and Subsidiary Merger. Although it would provide Policyholders an additional opportunity to invest in the Company, the potential execution risk regarding the transaction alternative may outweigh the potential transaction benefits as compared to the Transaction. In addition, Harleysville Mutual's Board of Directors appear to have analyzed this alternative and rejected it in the past.

(f) 6. Harleysville Mutual enters into a sponsored discounted merger conversion in which a stock insurance company acquires Harleysville Mutual:

Harleysville Mutual enters into an agreement with a stock company ("***Sponsor***") where the Sponsor would offer its stock in the subscription "waterfall" to Policyholders. Stock could be offered at a discount to market value to provide "acquisition premium" and confers benefit on members who purchase stock. HGIC stockholders would then be "taken out" for cash. Some key considerations that Griffin and the Harleysville Mutual Board of Directors looked at were:

- Transaction structure is used to facilitate the conversion of a mutual insurance company with significantly less execution risk
- Mutual buyers can not participate in process
- Transaction is usually significantly accretive to acquirer from both a capital and an earnings perspective
- The proposed timeline is between 12-18 months
- The execution risk is medium to high because of elongated time frame but acquirer bears most of the cost

Based on its review of Griffin's analysis, Boenning agrees that entering into a sponsored discounted merger conversion in which a stock insurance company acquires Harleysville Mutual would be challenging given the high execution risk as compared to the Transaction because of an elongated time frame and the fact that the acquirer bears most of the cost of the merger conversion. Although this would be accretive from both a capital and earnings perspective to the acquirer, mutual buyers would be excluded because they could not participate in the merger conversion process potentially excluding parties who have demonstrated an interest in the acquiring company (including the Transaction Partner, the party expressing the most serious interest in merging with the Company in a transaction that meets the Company's strategic objectives).

(g) 7. Harleysville Mutual converts from Mutual to stock form and HGIC uses its stock to acquire Harleysville Mutual:

HGIC sponsors the conversion of Harleysville Mutual from mutual to stock form and HGIC offers its stock in the subscription "waterfall". The subsidiary would buy the parent and the stock could be offered at a discount to market value to provide "acquisition premium." A subsequent sale of HGIC could occur. Some key considerations that Griffin and Harleysville Mutual looked at were:

- Does not address many of the Company's reasons for the transaction
- Generates excess capital which will be difficult to deploy

- The proposed timeline is between 9-12 months with no subsequent sale; 12-18 months with sale
- The execution risk is low

Based on its review of Griffin's analysis, Boenning agrees that converting from mutual to stock form and HGIC using its stock to acquire Harleysville Mutual would not be more financially beneficial to Harleysville Mutual than the Transaction. The proposed transaction alternative does not add size, or scale to the Company's operation which has been their primary stated reason for a strategic transaction. It also generates excess capital, thus reducing Harleysville Mutual's return on equity. (Refer to Alternative 5 above for more detailed information)

c. Other Alternatives Reviewed by Boenning

Aside from reviewing transaction alternatives developed by Griffin, Boenning also noted two additional potential alternatives discussed in conversations with Credit Suisse. They are as follows:

- Buy-in of Shares: This alternative focuses on financial capacity and capital ratios. The potential alternative does not solve the company's primary strategic concern of size and scale. In addition, this alternative leaves the Company with reduced capacity for future acquisitions
- Restructuring Pooling Agreement: Like many of the previously stated transaction alternatives, restructuring the pooling agreement does not address the Company's primary strategic concern of size and scale. Restructuring the agreement changes the allocation of net premiums earned, which, depending on the timing and current economic conditions, could potentially be better or worse for Harleysville Mutual

d. Alternatives to Transaction Conclusion

The information reviewed by Boenning appeared consistent with information noted in interviews with management and Advisors and in other Transaction-related documents reviewed by Boenning. Credit Suisse and Griffin's analysis appears to be thorough and complete and we are unable to disagree with the strategic alterative considerations produced. Minor differences of opinion as well as additional thoughts and conclusions generated by Boenning are included in the discussion of each alternative above.

The Boards of Directors considered numerous alternatives to the Transaction under the guidance of their Advisors. Boenning believes that their financial advisors' analysis appears to be thorough, reasonable and complete from a financial point of view. The rationale for dismissing each

of the seven transaction alternatives relative to the Transaction appears reasonable. In addition, Boenning agrees with both the quantitative and qualitative reasoning and conclusions the financial Advisors and Boards of Directors developed.

D. Alternative Proposals

Boenning's Engagement Letter with the Department included the following:

> "(f) Understand the alternatives to the Transaction considered by the Company in determining to proceed with the Transaction."
>
> "(k) Compare the values derived by Boenning's financial analysis relative to values potentially available from other alternatives to the Policyholders, including a subscription rights demutualization."

In accordance with the Engagement Letter, Boenning researched the transaction proposal solicitation process to understand what alternative proposals the Company received and considered. In addition, Boenning reviewed and attempted to compare the Transaction with an alternative expression of interest that was received after the solicitation process ended.

As stated prior in Section IV, Harleysville Mutual believed it lacked the size and scale to organically grow its business. They instead turned to becoming the target of a strategic transaction for what ultimately turned out to be three companies. Company A has asked that its identity not be disclosed; Company B and Nationwide are the other two parties that expressed interest.

Beginning in the Spring of 2011, the Company, via CEO Michael Browne, began discussing the possibilities of strategic transactions with Company A, Company B, and Nationwide. In late June, Company A had initial discussions with Credit Suisse. Throughout the summer, Company A maintained communication with the Company and had several meetings to review operational synergies and the structure of a potential transaction. The Company requested that Credit Suisse inform potential transaction partners to address Harleysville Mutual's constituencies, including Policyholders, members, agents, the community and brand. The week following July 29th, the CEO of Company A indicated that any proposed Transaction by Company A would not provide all of the constituency benefits as described by Harleysville Mutual.

In early July, Company CEO Browne met with the Chairman of the Board of Directors and the CEO of Company B to discuss potential synergies between the two companies and other factors relating to a transaction. Company B also expressed their views as to how Harleysville Mutual

would fit into their corporate structure. Following this meeting, the CEOs again met to discuss the various structural alternatives via telephone. The Company believed that the proposed transaction structures would involve significant structural change to Harleysville Mutual and could take up to two years to complete. According to the PIS:

> *"Harleysville believed that each of Company B's proposed transaction structures was complex, would involve significant structural changes to Harleysville, and would take anywhere from nine months to 24 months to consummate."*

Management specifically noted that Company B indicated that the Company's commercial business would be carved up among Company B companies and restricted to Pennsylvania and two other states while personal lines would be merged into a Company B subsidiary. Company B was reported also to be uninterested in the Company's headquarters and personnel. Beyond these undesirable effects of a merger, management further noted concerns that Company B, given its suggested structure and consideration, could potentially be worse off from a financial perspective, on a pro forma basis.

In early August of 2011, Credit Suisse spoke with representatives of Company B. Credit Suisse discussed HGIC's expectation for the per share consideration payable to its public stockholders. In light of other offers and alternative proposals that Credit Suisse expected to receive on behalf of the Company, a per share price that would "start with a six" was communicated. Company B acknowledged that they understood that pricing guidance they were being given and later informed Credit Suisse that they would not be prepared to pay a per share price as discussed. According to the PIS:

> *"…on this call, the representatives of Company B said that Company B would not be prepared to pay anything close to a per share price of $60 to the Company's public stockholders, and, instead, contemplated a per share price that would reflect a premium of approximately 50% over the then-current trading price of the Company's shares (which would imply a per share price of approximately $45). The representatives of Company B also said that Company B would be prepared to pay some amount to Harleysville Mutual's policyholders. Harleysville believes such offer of a payment to policyholders was based upon Company B's structure and its proposal to effect a demutualization or a conversion of Harleysville Mutual."*

During this time, the Company and/or Credit Suisse were gaining additional insight into the possibility of a transaction with Nationwide. Several meetings were held to review potential

synergies, pricing, and overall strategy for the potential combined company and how Harleysville Mutual would fit in the combined corporate structure.

On August 5th (a regular Boards of Directors' meeting), the Boards of Directors discussed the status of negotiations with Company A, Company B, and Nationwide. After discussions, the Boards of Directors concluded that based on prior conversations, Company B did not appear interested in pursuing a transaction that would be considered acceptable for both the Harleysville Mutual Board of Directors and HGIC Board of Directors. In addition the Boards of Directors accepted that Company A had made it known that they too would not be able to achieve a transaction structure deemed to be acceptable for both Boards of Directors. The Boards of Directors, however, concluded to move forward with Nationwide in an attempt to negotiate a transaction. The Company and Nationwide then executed an exclusivity agreement on or about August 15, 2011.

After this decision was made, Company B presented an unsolicited indication of interest for a transaction. In a letter dated August 26, 2011, to CEO Browne, Company B's CEO is quoted as stating:

[redacted]

The letter continues on to generally describe the structure of the transaction to the public stockholders, Policyholders, employees and senior management.

In a letter dated September 1, 2011, Company B's CEO sent an unsolicited indication of interest to the Company. This time however, the information was more specific. The potential deal structure is outlined below:

- *"Company B would affiliate with Harleysville Mutual and buy out the public shareholders of HGIC for a price of $42 per share*

- *Harleysville Mutual would convert to a stock insurance company and Company B would provide your members with a special dividend of $250 million coupled with member rights in Company B's holding company.*
- *Company B would be flexible as to the timing and sequencing of the affiliation, buy out and conversion*
- *Company B would offer you and your senior managers a transaction and retention compensation program of approximately $25 million.*
- *Harleysville operations would retain its identity as a strong brand within our regional companies group*
- *Company B would maintain a real presence within PA and in other significant Harleysville locations while also establishing "The Harleysville Mutual Foundation" with initial funding of $5 million to support and enhance the surrounding communities."*

In a letter dated August 30, 2011, the Company indicated that it was "not in position to have any further discussions with you or your advisors." As previously stated, the Company had signed an exclusivity agreement with Nationwide, which the Company believed prevented such interaction while the agreement was in place.

In reviewing the Nationwide proposal, the Boards of Directors concluded that Company B's unsolicited indication of interest was not as attractive as Nationwide's because of the lower share price, higher execution risk, potential changes to the "Harleysville brand", its employees, and the Harleysville community and complex corporate structure. According to the PIS:

> *"Mr. Browne pointed out that, based on the various discussions that had occurred with Company B, it appeared that a transaction with Company B would involve reductions in employment at Harleysville, reduction in the number of states in which Harleysville would write business, overlapping geographic regions and disruptions in the independent agency force."*

In totality, the Boards of Directors determined that Nationwide's Transaction was the better proposal after considering all factors.

a. Advisors' View of Alternative Proposals

In late September, Credit Suisse made its September Presentation to the Boards of Directors that outlined the strategic alternatives previously considered by the Boards of Directors, the Transaction by Nationwide, considerations for the Nationwide Transaction, considerations for Company B's unsolicited indication of interest and an array of financial analysis including Wall Street analyst outlooks on HGIC, comparable companies analysis, and management projections.

Credit Suisse reviewed the potential transaction partners that had been contacted, reviewed the terms, and discussed the pros and cons of each.

As discussed earlier, at the end of the solicitation period (August 2011), Company B declined to submit an initial proposal when they were invited to do so. In late August, Company B again approached the Company about a possible strategic transaction. By that time, the Company had already entered into an exclusivity agreement with Nationwide, which the Company believed did not permit the Company to engage in discussions with Company B. Such exclusivity agreements are very common in transactions based on Boenning's experience. Notwithstanding the exclusivity agreement, in the September 27 and 28 meetings, the Boards of Directors reviewed analysis of the Company B expression of interest comparatively with the Nationwide transaction.

Because of Company B's structure, it was unable to effect a true mutual-to-mutual merger. The Advisors also indicated that a potential transaction with Company B could take significantly longer to complete than the Transaction with Nationwide and it did not offer the same type of protections to the Company's employees, agents and the "Harleysville" Brand.

After Credit Suisse's September Presentation, Harleysville Mutual's Board of Directors met with Griffin. Griffin discussed their view of the Parent Merger and its consequences for the various constituencies of Harleysville Mutual. Griffin summarized the Transaction with Nationwide and the unsolicited indication of interest from Company B during this meeting. Their analysis was consistent with Credit Suisse's analysis and concluded that Nationwide's Transaction was superior to Company B's unsolicited indication of interest. Harleysville Mutual's Board of Director's decision to proceed with the Transaction Partner appears to be based on a comparison of the Nationwide proposal with an alternative based on the information examined including total consideration, benefits to stockholders, benefits to Policyholders, benefits to the Company's employees, benefits to agents, and benefits to the community.

Further, it appears that all of the potential transaction partners were guided by Credit Suisse to the type of transaction structure that would meet the Company's goals and objectives. In the case of Company B, it appears from correspondence that Company B unilaterally determined to propose an alternative transaction structure - a structure that was deemed less attractive by the Boards of

Directors. In Boenning's experience, a potential buyer ignoring the advice of a seller's advisor often leads to an unsuccessful proposal.

As an investment bank that has represented sellers and reviewed potential transaction offers and alternatives with boards of directors, Boenning believes the Company's analysis indicates that the Company reviewed Company B's unsolicited indication of interest as if it were as fully negotiated as Nationwide's fully negotiated offer. This approach appears to be reasonable from a financial point of view. Further, the analysis provided by the Advisors indicates that Company B's unsolicited indication of interest was reviewed and deemed to be less attractive than the Transaction.

In addition, according to the PIS, Stevens & Lee noted that the Harleysville Mutual Board of Directors did not need to conduct an extensive process solely to "maximize value" and that the Harleysville Mutual Board of Directors could accept or reject proposals so long as the Board of Directors acts in good faith on an informed basis and in the best interests of Harleysville Mutual.

The information reviewed by Boenning appeared consistent with information noted in interviews with management and Advisors and in other Transaction related documents reviewed by Boenning. The advisors representing the Harleysville Mutual Board of Directors concluded that they thoroughly reviewed the alternatives to the Transaction and specifically an alternative expression of interest (not a fully negotiated offer) and concluded that the Transaction was fair to Harleysville Mutual. Similarly the advisors representing the HGIC Board of Directors came to the same conclusion on behalf of HGIC.

Section VI

Management and Director Issues

A. Examination of Potential Director Conflicts

Boenning's Engagement Letter with the Department included the following:

> "(m) Examine and provide commentary on the measures taken by the Company to preserve independence and manage potential conflicts of interest among Company directors.
>
> "(n) Examine and provide commentary on the differences, similarities and potential differences, between the responsibilities and potential conflicts of interest of Harleysville Mutual directors and those of the stock holding company."

In accordance with its Engagement Letter, Boenning reviewed advice provided to, and the measures taken by, the Company to preserve independence and manage potential conflicts of interest. As indicated by (n) above, there are potential differences in the fiduciary duties of the directors of Harleysville Mutual as opposed to those of HGIC. Such potential differences are discussed later in this Section of the Report. In addition to reviewing analysis relating to this issue, Boenning also reviewed the PIS, Proxy, Boards of Directors' minutes, comments and responses posted on the Department's website, and interviewed Harleysville Mutual's legal advisors and the senior management team of the Company for history, background and additional information relating to this issue.

After reviewing the Proxy, Boenning noted that there was clear overlap between and among the HGIC Board of Directors and Harleysville Mutual's Board of Directors. Six members of the Boards of Directors had direct overlap and sat on both HGIC's Board of Directors and Harleysville Mutual's Board of Directors. There were three members who sat only on Harleysville Mutual's Board of Directors and two members who only sat on the HGIC Board of Directors.

a. Potential Differences in Goals and Duties

According to the Advisors, many of the goals and duties of Harleysville Mutual and HGIC directors (such as operating the business soundly, growing the financial strength of the companies and otherwise assuring its ability to effectively carry out/execute its business purpose etc.) are common to both entities. According to the legal advisors, the potential differences could arise in connection with the evaluation of a potential transaction or in the event that the Harleysville Mutual

Board of Directors and HGIC Board of Directors are required to negotiate against one another. Also according to Stevens & Lee, there are differences in the duties as summarized below.

Harleysville Mutual is a Pennsylvania domiciled insurer and a Pennsylvania corporation. Its special legal counsel, Stevens & Lee, noted that under PA BCL Section 1712 (a) each:

> *"director of a [Pennsylvania] business corporation shall stand in a fiduciary relation to the corporation and shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation ..."*

Harleysville Mutual's Board of Directors were advised by Stevens & Lee that it owes its fiduciary duty to Harleysville Mutual alone.

Further, Stevens & Lee noted that Sections 1715 (a) and (b) of the PA BCL essentially provides that:

> *"[i]n discharging the duties of their respective positions, the board of directors, committees of the board and individual directors of a business corporation may, in considering the best interests of the corporation, consider to the extent they deem appropriate:" (1) the interests of policyholders, employees, suppliers, customers, independent agents and the communities in which they have offices; (2) the long-term as well as short-term interests of the corporation; (3) the resources, intent and conduct of any person seeking to acquire control of the corporation; and (4) any other pertinent factors. None of "the interests of any particular group affected by [any] action" shall be "a dominant or controlling interest or factor" in the decisions of the individual directors, special committees or board of directors."*

It appears, based on the advice of Stevens & Lee, that the Harleysville Mutual Board of Directors believed that it owed fiduciary duties to Harleysville Mutual itself, and in fulfilling such duties the Harleysville Mutual Board of Directors could, but was not required to, give consideration to any single constituency over another, and it could consider factors only to the extent that they impact the best interests of HMIC. Further, they were advised that the extent of their duty was to find a transaction that was good for Harleysville Mutual, not necessarily the highest or best economic transaction for any single constituency. HGIC Board of Directors, as directors of a Delaware corporation, as advised of these duties by Fox Rothschild focused their attention, once they decided to pursue a merger, on the best price for the stockholders of HGIC.

However, according to Stevens & Lee, the differences in these duties do not necessarily equate to a conflict between the Harleysville Mutual Board of Directors and HGIC Board of Directors and their respective fiduciary duties. The Harleysville Mutual Board of Directors and

HGIC Board of Directors each stated that they did not negotiate with one another, which is one case by which a conflict could arise. Stevens & Lee concluded that the Harleysville Mutual Board of Directors and HGIC Boards of Directors approved separate transactions by separate sets of criteria.

According to the PIS and interviews with management and Ballard Spahr LLP, legal counsel to both Harleysville Mutual and HGIC during the period from January 2011 to August 2011, the Harleysville Mutual Board of Directors and HGIC Board of Directors each understood the differences in their respective fiduciary duties. Further, management and the minutes of both boards indicate that the Boards of Directors were experienced in managing the differences in practice, switching roles as required and serving appropriately as the Harleysville Mutual Board of Directors when required and in other cases as HGIC Board of Directors. According to the PIS, the Boards of Directors took measures as noted within the following subsection of the Report to assure independence.

b. Measures Taken

In interviews with management and legal counsel (Ballard Spahr, Fox Rothschild and Stevens & Lee) as well as reviews of Boards of Directors minutes, Proxy and PIS, management and the Advisors advised Boenning that directors of both the Harleysville Mutual Board of Directors and the HGIC Board of Directors were accustomed to switching roles and managing their respective fiduciary duties to the respective entities. The directors were reported to have a working knowledge of and experience with the issues and fiduciary duties in their separate roles as Harleysville Mutual Board of Directors and HGIC Board of Directors. It was also reported to Boenning that, when voting as directors of Harleysville Mutual, the directors complied with these duties.

In terms of the measures taken for the Transaction, in addition to relying on prior director experience, legal advice and knowledge of the differences in fiduciary duties, the PIS notes that on August 5, 2011:

> *"The Boards also discussed whether, depending on the ultimate structure of the proposed transaction with Nationwide Mutual, it would be advisable for each of the Boards to have its own separate advisors and for each to form a special committee composed of non-employee directors who served only on the Board of Harleysville Mutual or on the Board of*

Harleysville Group but not both. Based on such discussion, each Board authorized the formation of a special committee."

Table 33) Harleysville Mutual and HGIC Special Committee Members

Special Committee HGIC	Special Committee HMIC
Ms. Austell	Mr. DeBenedictis
Ms. Graddick-Weir	Mr. Lapeyrouse

A review of Boards of Directors minutes confirms the formation of the special committees and that the committees adopted charters. Boenning interviewed Mr. DeBenedictis and Mr. Lapeyrouse in their capacity as the directors serving on the Harleysville Mutual Special Committee ("***Special Committee***"). These directors appeared to understand their roles and special focus necessary to avoid any actual or potential conflict of interest.

The PIS also notes that the Harleysville Mutual Board of Directors of and HGIC Board of Directors engaged separate legal and financial advisors and held meetings separately from the full Boards of Directors. Measures were also taken and documented in the PIS that the Harleysville Mutual Board of Directors and its respective legal and financial advisors met separately from the HGIC Board of Directors and advisors of HGIC. The minutes of the Boards of Directors confirms these measures occurred.

c. Additional Background

In interviews with management, review of Boards of Directors minutes, and in the PIS, Harleysville Mutual indicated that directors of both Harleysville Mutual and HGIC were knowledgeable of their respective fiduciary duties to each entity and accustomed to switching roles when needed. Boards of Directors minutes and presentations to the Boards of Directors by independent Advisors confirm an awareness of potential issues and the measures taken to assure independence and appropriate decision making processes.

The use of separate counsel and financial advisors, differences in representations and covenants in the Merger Agreement and in presentations to aid in the decision process reflect that the Boards of Directors were aware of the differences in the fiduciary duties of each board.

Management reported to Boenning in interviews that the Harleysville Mutual Board of Directors and HGIC Board of Directors negotiated two separate and distinct (but mutually conditioned) transactions with Nationwide and in no instance did the Harleysville Mutual Board of Directors or HGIC Board of Directors negotiate with one another. Management further reported such procedures enabled the directors to avoid any potential conflict that could arise if separate boards with overlapping directors were required to negotiate against one another. Management noted in one interview that "No board received something at the other's expense."

Further, the Boards of Directors' minutes and presentations/opinions by independent Advisors reviewed by Boenning appeared consistent with information noted in interviews with management and other transaction related documents reviewed by Boenning.

d. Director Financial Interest in the Potential Transaction

As described more fully later in this Section VI, directors of the HGIC Board of Directors, who also constituted a majority of the Harleysville Mutual Board of Directors, stood to gain financially from the HGIC transaction with Nationwide. Such gains are common in the case of a stockholder-owned company being acquired for a profit. To the extent the HGIC directors are also stockholders of HGIC, their interests in the potential Transaction are aligned with stockholders.

According to the Advisors, as discussed in Section V, the Harleysville Mutual Board of Directors' duty to Harleysville Mutual in the Transaction appears to have been met in that the Transaction is, in its advisors' opinions, noted as being beneficial to Harleysville Mutual and its constituents.

A potential concern reviewed by Boenning is that all members of the Boards of Directors as of the Evaluation Date, will receive compensation as stockholders of HGIC in the Subsidiary Merger. Boenning's concern was whether the directors were "interested parties" and unable to

fulfill their duties under the business judgment rule in the PA BCL. [redacted]

As reported in interviews with Boenning, Harleysville Mutual Board of Director members followed the advice of legal counsel, specifically Ballard Spahr and Stevens & Lee, in terms of the fiduciary duties and obligations of directors as well as suggestions for measures to be taken to eliminate or and/or manage potential conflicts of interest among directors.

Boenning, as part of its interview process, attempted to verify that there were no conflicts among the Company or its independent Advisors and so inquired of each Advisor as to:

- Prior engagement experience with the Company
- Any conflicts of interest
- Any familial or professional relationships between the Advisor and the Boards of Directors or management of the Company

B. Executive Officers and Boards of Directors Economic Benefits in the Transaction

Boenning's Engagement Letter with the Department included the following:

(r) "Review the Company's rationale for executive level and director compensation, including the analysis and opinions of expert compensation consultants utilized by the Company.

(s) Review the Transaction Partner's rationale and explanation for retention, severance and other executive level and director compensation for Company employees.

(t) Include a summary of the Company's and Transaction Partner's analysis in the Report, including Boenning's conclusions as to the reasonableness of the supporting analysis

and if the Company followed the recommendations of its consultants in determining compensation. The Department acknowledges that Boenning is not a compensation consultant and its opinion will be limited to the reasonableness of the analysis and not the specific conclusions drawn by the consultants or Company as the case may be."

In accordance with its Engagement Letter, Boenning reviewed various documents and analyses prepared by the Company, Advisors, and its compensation consultants. These included, but were not limited to, the PIS, the 2011 HGIC proxy statement filed for the 2011 Annual Meeting of Stockholders ("***2011 Proxy***"), the Griffin opinion dated September 27, 2011, and the Harleysville Insurance – Executive Compensation Memorandum dated January 23, 2012 prepared at Boenning's request ("***Compensation Memo***"). In addition, Boenning interviewed the senior management team of the Company, Nationwide, and the members of the Special Committee of Harleysville Mutual's Board of Directors for history, background and additional information relating to compensation. As noted above, Boenning is acting solely as a financial advisor, is providing advice to the Department solely from a financial point of view, and is not offering or deemed to offer advice as an executive compensation consultant or otherwise. Thus, the scope of our review was limited to reviewing the compensation policies, procedure, and process as a financial advisor from a financial point of view to determine the level of total compensation (cash and long-term incentive) received by both the executive officers and the Boards of Directors.

Also, due to the inherent link between the compensation packages (described in detail below) and the economics derived from such compensation packages as a result of the Transaction, Boenning completed a thorough review of the economics received by the executive officers and Boards of Directors. The intent of this review was to delineate which economic benefits received by the executive officers and Boards of Directors was driven by historically received compensation versus economics "created" solely by the Transaction. Further, Boenning was focused on determining, based on its review, whether its finding appeared to be consistent with "market" based on Boenning's experience as a financial advisor in other transactions.

a. Summary of the Members of the Boards of Directors

The Company has 10 non-employee members of the Boards of Directors, as listed in Table 34 below. Five of these members serve on the HGIC Board of Directors and the Harleysville Mutual

Board of Directors. As noted elsewhere in the Report the three directors that are members of only the Harleysville Mutual Board of Directors were candidates for the Special Committee for the Transaction. As Ms. Dunn recused herself because of a perceived conflict, Mr. DeBenedictis and Mr. Lapeyrouse were the only two independent directors to serve on the Special Committee of Harleysville Mutual.

Table 34) Non Employee Boards of Directors Members as of September 28, 2011

Non-employee Boards of Directors Members

Name	Director Since	Board Membership
Barbara A. Austell	2007	Group
W. Thacher Brown	1994	Mutual/Group
G. Lawrence Buhl	2004	Mutual/Group
Nicholas DeBenedictis	2005	Mutual
Ellen M. Dunn	2007	Mutual
Mirian M. Graddick-Weir	2000	Group
Michael L. Lapeyrouse	2002	Mutual
Jerry S. Rosenbloom	1995	Mutual/Group
William W. Scranton III	2004	Mutual/Group
William E. Storts	2001	Mutual/Group

Source: PIS and 2011 Proxy

As detailed in the 2011 Proxy, the Company pays each non-employee director cash-based fees, including an annual retainer ($35,000; additional $75,000 for chairman and $8,000 - $12,000 for committee chair), per meeting-and committee-based fees ($1,500 - $2,000). It issues Deferred Stock Units with a value of $50,000 to each non-employee director continuing in office at each annual meeting. Each of the members of the Boards of Directors serves on at least two committees.

With the number of years of service logged, non-employee directors have accumulated a certain amount of owned shares (some of which are required by the Company's stock ownership guidelines of 4x annual cash retainer), stock options, restricted stock, and deferred stock units that are completely independent from the Transaction. Table 35 below, sourced from the PIS and Compensation Memo, sets out the number of projected owned shares, options, restricted stock, and deferred stock units for each Boards of Directors member as if the Transaction were to close on March 31, 2012.

Table 35) Boards of Directors Shares and Share Equivalents

Boards of Directors Shares and Share Equivalents

Name	Projected Owned Shares (3/31/12)	Projected Shares Underlying Stock Awards (3/31/12)	Projected Shares Underlying Stock Options (3/31/12)	Total Shares
Barbara A. Austell	0.000	7,436	0	**7,436.00**
W. Thacher Brown	39,889.000	15,792	7,500	**63,181.00**
G. Lawrence Buhl	3,000.377	10,146	0	**13,146.38**
Nicholas DeBenedictis	20,061.000	8,646	0	**28,707.00**
Ellen M. Dunn	0.000	7,641	0	**7,641.00**
Mirian M. Graddick-Weir	16,631.082	10,146	7,500	**34,277.08**
Michael L. Lapeyrouse	95.427	10,146	5,000	**15,241.43**
Jerry S. Rosenbloom	27,797.420	15,792	7,500	**51,089.42**
William W. Scranton III	7,082.890	10,146	7,500	**24,728.89**
William E. Storts	19,982.767	10,146	0	**30,128.77**
TOTAL	**134,539.963**	**106,037**	**35,000**	**275,576.96**

[redacted]

An additional component of the Boards of Directors' compensation packages is the ability to defer receipt of some or all of their director or committee fees under the Directors' Standard Deferred Compensation Plan, or in prior years, the directors' Corporate Owned Life Insurance ("***COLI***") Plan. Receipt of the deferred compensation is triggered by retirement from the Boards of Directors or a change in control event. Further detail and a history of the plans are available in the 2011 Proxy. A summary of the estimated balances as presented in the Compensation Memo are included in Table 36 below.

Table 36) Non Employee Boards of Directors Deferred Compensation

Non-Employee Boards of Directors Deferred Compensation

Name	Deferred Comp Balance (12/31/11)	Projected COLI Balance (3/31/12)
Barbara A. Austell	$0	$0
W. Thacher Brown	67,740	652,437
G. Lawrence Buhl	0	0
Nicholas DeBenedictis	110,016	0
Ellen M. Dunn	34,155	0
Mirian M. Graddick-Weir	418,654	0
Michael L. Lapeyrouse	307,456	0
Jerry S. Rosenbloom	69,788	0
William W. Scranton III	0	0
William E. Storts	0	162,463
Sub-Total	**$1,007,809**	**$814,900**

[redacted]

b. *Summary of the Executive Officers*

There are 10 executive officers of the Company[5]. Table 37 below identifies the current executive officers of the Company.

Table 37) Executive Officers

Executive Officers

Name	Age	Title	Position Since
Michael L. Browne	64	President & Chief Executive Officer	2004
Arthur E. Chandler	54	Senior Vice President & Chief Financial Officer	2005
Allan R. Becker	52	Senior Vice President & Chief Actuary	2005
Thomas E. Clark	50	Senior Vice President, Field Operations	2004
Mark R. Cummins	54	Executive Vice President, Chief Investment Officer & Treasurer	1992
Beth A. Friel	37	Senior Vice President, Human Resources and Senior Vice President, Claims	2009 / 2012
Robert A. Kauffman	47	Senior Vice President, Secretary, General Counsel & Chief Compliance Officer	2004
Theodore A. Majewski	59	SVP, Personal Lines; President and COO of Harleysville Life Insurance Company	2003
Kevin M. Toth	37	Senior Vice President & Chief Underwriting Officer	2009
Arnold F. Herenstein	63	Senior Vice President & Chief Inormation Officer	2011

Five of these executives are named executive officers ("***NEOs***"). The NEO designation is given to the five most highly compensated executive officers for disclosure purposes as part of HGIC's annual proxy statement filing requirement with the Securities and Exchange Commission ("***SEC***"). Described in detail in the 2011 Proxy, compensation for the NEOs consists of three components:

- Fixed compensation through an annual base salary
- Variable compensation through annual cash-based incentive awards
- Long-term compensation through annual time and performance-based equity awards

The non-cash compensation is awarded or granted through a combination of the following:

- stock options
- restricted stock awards
- restricted stock units awards
- performance stock awards

The Company embraces a "pay for performance" philosophy that is designed to reward executives for driving organizational performance and creating stockholder value. Boenning noted that some combination of these three compensation methods also extends deep into the employee base. This is intended as both a retention strategy and a motivation/reward tool.

To further support this philosophy, the Company has, according to the 2011 Proxy, established stock ownership guidelines for its NEOs to encourage continued stock ownership and

[5] For the remainder of this Section VI, references to the "Company" refer to HGIC.

further align the interest of the executives with the interests of stockholders. Table 38 below from the 2011 Proxy summarizes the required guidelines of equity ownership as of 12/31/2010. All the NEOs exceed the ownership guidelines.

Table 38) Share Ownership Guidelines

Share Ownership Guidelines of NEOs

Name	Multiple of base Salary	Share Ownership Target	Shares Owned at 12/31/10
Michael L. Browne	6.0x	107,784	214,226
Arthur E. Chandler	2.5x	22,795	27,872
Allan R. Becker	2.5x	18,713	30,765
Thomas E. Clark	2.5x	22,403	27,933
Mark R. Cummins	2.5x	18,713	22,963

By the nature of the Company's compensation program, the executive officers and certain employees have accumulated a number of shares of HGIC during their respective employment periods with the Company. The ownership of these shares and share equivalents were obtained as a result of the compensation program of the Company and not as a result of the Transaction. Table 39, sourced from [redacted], sets out the number of projected owned shares, options and stock awards for each executive officer as if the Transaction were to close on March 31, 2012.

Table 39) Executive Officers Shares and Share Equivalents

Executive Officers - Shares and Share Equivalents Owned from Historical Compensation

Name	Projected Owned Shares (3/31/12)	Projected Shares Underlying Stock Awards (3/31/12)	Projected Shares Underlying Stock Options (3/31/12)	Total Shares
Michael L. Browne	199,247.997	44,030	448,415	**691,693.00**
Arthur E. Chandler	23,024.074	4,110	80,760	**107,894.07**
[redacted]				
Kevin M. Toth	17,460.311	8,600	65,182	**91,242.31**
Allan R. Becker	19,501.922	2,085	26,319	**47,905.92**
Beth A. Friel	9,465.131	1,925	20,159	**31,549.13**
[redacted]				
TOTAL	**371,531.254**	**86,690**	**926,897**	**1,385,118.25**
[redacted]				

In addition to the cash and incentive based components of the compensation package, the Company offers its executive officers certain post-retirement benefits. These include a non-qualified

deferred compensation plan, supplemental retirement plan (SERP), defined contribution plan, and a non-qualified excess contribution and match program. Table 40 summarizes the SERP, deferred compensation, and COLI balances as these plans are paid out at close of the Transaction or "accelerated". Details on the other post-retirement accounts can be found in the 2011 Proxy.

Table 40) Deferred Compensation Plans

Deferred Compensation Plans Accelerated by Mergers

Name	SERP Balance (12/31/11)	Deferred Comp Balance (12/31/11)	Projected COLI Balance (3/31/12)
Michael L. Browne	$193,100	$1,373,876	$1,511,476
Arthur E. Chandler	15,000	54,442	0
[redacted]			
Kevin M. Toth	0	15,716	0
Allan R. Becker	0	4,881	0
Beth A. Friel	0	1,190	0
[redacted]			
TOTAL	**$460,600**	**$1,715,872**	**$1,511,476**

[redacted]

Lastly, the Company has entered into a change-in-control agreement (each a "***CIC Agreement***") with its executive officers. Boenning was told by senior management that these agreements are necessary to attract and retain its executive officers. Details of the CIC Agreements can be found in the 2011 Proxy.

c. Review of the Compensation Policies and Procedures

As a publicly traded company, HGIC is subject to the stringent disclosure requirements of the SEC regarding the compensation of its NEOs and board of directors. To meet its disclosure requirements, the Compensation Memorandum states that:

> *"HGI, through its Compensation Committee, has established and adheres to robust executive compensation oversight and approval practices. These include a detailed annual review of compensation policies and practices."*

Further the Compensation Memorandum states that:

> *"The Compensation Committee has engaged the services of an independent compensation consultant to provide the Compensation Committee with information and advice regarding Harleysville's compensation practices and best practices generally. From September 2009 to the present, that independent compensation consultant has been Compensation Advisory Partners LLC. Prior thereto, Mercer provided such consulting services to the Compensation Committee."*

Boenning reviewed the "Compensation Discussion and Analysis" section of the 2011 Proxy which thoroughly details the Compensation Committee's compensation process, philosophy, methodology and program for 2010.

The 2011 Proxy also notes that in addition to the use of its compensation consultant:

> *"The Compensation Committee, which consists entirely of independent directors as defined in Section 162(m) of the Internal Revenue Code and as defined by NASDAQ, oversees the Company's management compensation program. The Compensation Committee is the principal decision-maker with respect to the Company's compensation philosophy and executive compensation components, but it seeks input and recommendations from the CEO and other members of senior leadership. Human Resources and General Counsel management representatives have assisted the Compensation Committee in evaluating executive compensation programs."*

To understand the Company's compensation practices further, Boenning held a meeting on January 24, 2012 with representatives of the Company's management and Ballard Spahr ("***Compensation Meeting***"). Boenning was informed about the HGIC Compensation Committee and its retention of its compensation consultant, Compensation Advisory Partners LLC ("***CAP***"). The Company's representatives explained how the consultant's services are used and relied upon by the Compensation Committee. The representatives of the Company also described the Compensation Committee's independence requirements. Also, Boenning noted that the Compensation Committee is chaired by HGIC Board of Directors member Mirian Graddick-Weir who currently serves as head of Human Resources at Merck, a $118 billion publicly traded pharmaceuticals company.

At the core of the services provided by CAP and the process of the Compensation Committee is a benchmarking analysis. Regarding benchmarking, the Compensation Memorandum states:

> *"At least five years ago, the Compensation Committee determined that it would use benchmarking against a peer group of companies as the principal method of establishing total annual compensation targets for Harleysville's executive officers. "Benchmarking" is the process of comparing total annual compensation, and the mix of such compensation, against a selected industry group of companies and/or best practices in the industry. The specific peer group used by the Compensation Committee, in the fall of 2010 to guide 2011 compensation decisions is set forth below. This peer group has remained constant since 2008, subject to individual change in control transactions impacting the peer group of companies."*

While the above statement from the Compensation Memo references the executive officers, the Compensation Committee also engages CAP to perform the same analysis for the compensation paid to members of the Boards of Directors. The peer group in the table below is used for both the executive officer and Boards of Directors compensation studies compiled by CAP.

Table 41) Peer Group Used by Compensation Committee

Peer Group used by Compensation Committee

Alleghany Corporation	One Beacon Insurance Group
W.R. Berkley Corporation	RLI Corporation
Cincinnati Financial Corporation	Safety Insurance Group
Donegal Group Inc.	Selective Insurance Group Inc.
EMC Insurance Group Inc.	State Auto Financial Corporation
Erie Indemnity Company	Tower Group Inc.
Hanover Insurance Group Inc.	United Fire and Casualty Company
HCC Insurance Holding Company	

[redacted]

[redacted] The 2011 Proxy, apparently based on this report, states:

> *"The Compensation Committee reviews, on a retrospective basis, the relationship between Company performance and actual compensation of the Named Executive Officers as compared to the benchmark companies (when information regarding the benchmark companies becomes available). To evaluate Company performance, the Compensation Committee evaluates a number of performance metrics, including net written premium growth; operating income growth; return on equity (ROE); combined ratio; and relative TSR [Total Shareholder Return]. Over the past few years, this analysis has confirmed that the Company's relative performance on key metrics is aligned with relative earned compensation as compared to the peer group companies."*

The median revenue, asset size, net income, market cap and number of employees of the peer group approximate the corresponding metrics of HGIC. Based on Boenning's experience compiling peer groups for financial analysis purposes, Boenning believes that the peer group utilized by the Compensation Committee for the executive compensation program framework appears to consist of companies comparable to HGIC. Boenning noted the program framework [redacted]

> *"Harleysville's [the Company] overall executive compensation program continues to reflect competitive and best practices in overall design. The majority of executives have target pay opportunities that align with the company's median pay philosophy and performance based incentive programs support business objectives of underwriting profitability and shareholder value creation"*

The corresponding analysis done for the Boards of Directors [redacted]

- *"Harleysville's total outside directors compensation program positions total pay just slightly below the peer group median. Program changes made in 2009 help better position directors' pay against the peer group, yet even with minimal increases in peer group pay, Harleysville falls just short of the peer median*
- *The overall structure of Harleysville's program is well aligned with peers; i.e., the use of meeting fees, premium committee chair retainers, full value equity awards, value based equity grant, cash/equity mix*
- *Equity holding/award settlement at Board termination, and stock ownership guidelines, are reflective of broader market based practices*
- *The non-executive chair premium reflects the peer group median for the nine companies with such a role"*

In connection with the summary of the Boards of Directors and executive officer historical compensation outlined earlier, it was conveyed to Boenning during the Compensation Meeting that

the compensation received, both in terms of cash and stock incentives, seemed reasonable to the Compensation Committee and largely in keeping with the recommendations of CAP. In fact, Boenning notes that in many cases the executive officers and the Boards of Directors appear to receive lower pay on a cash basis with a heavier weighting toward incentive compensation to approach the peer medians. Based on information provided to Boenning, even though the historically received stock incentives account for a large portion of the cash to be received as part of the Transaction, the sources of this compensation appear both to not have been put in place in anticipation of a Transaction and unrelated to the Transaction event itself.

d. Summary of the Total Economic Benefits to be Received by Executive Officers and Boards of Directors

Based on discussions during the Compensation Meeting, Boenning understood that the majority of economic benefits to be received in the Transaction by executive officers and Boards of Directors are a function of three main components as generally laid out in the PIS:

- Owned Shares and Share Equivalents - Receiving the indicated value per share of $60.00 being offered in the Transaction in exchange for all the owned shares and share equivalents of HGIC as summarized in Table 35
- Deferred Payments - Acceleration of certain post-retirement compensation program benefits triggered by the change-in-control nature of the Transaction
- Transaction Specific - compensation received specifically as a result of the Transaction

e. Owned Shares and Share Equivalents

In this Section VI it is documented how the executive officers and Boards of Directors received the securities that are subject to receipt of $60 per share and share equivalent in the Transaction. The mechanics of this are materially similar to how other similar change-in-control transactions would exchange shares and share equivalents into their cash value.

f. Deferred Payments

From the PIS:

> *"Harleysville sponsors and maintains (1) the Standard Deferred Compensation Plan for Directors of Harleysville Mutual Insurance Company and Harleysville Group Inc. (Amended and Restated as of January 1, 2008) (the "Directors' Plan"), (2) the Harleysville Group Inc. Non-Qualified Deferred Compensation Plan (amended and restated as of January 1, 2008) (the "Deferred Compensation Plan"), and (3) the Harleysville Group Inc. Supplemental Retirement Plan (amended and restated as of January 1, 2008) (the "SERP"). These plans provide directors and/or executive officers with deferral opportunities, including company contributions, to defer compensation earned in any given fiscal year to a later date."*

Prior to the current Standard Deferred Compensation Plan for Directors, the Company offered a COLI plan, established in 1988. Two current directors, W. Thacher Brown and William E. Storts were directors at the time the plan was in place and participated as indicated in Table 40. Additionally, before Michael L. Browne was CEO of the Company he served as a director of HGIC and also participated in the COLI plan (included in Table 40).

As noted in the PIS:

> *"…each named executive officer is entitled to this amount regardless of the Group Merger, but that, as a result of the Group Merger, the SERP and the Excess Plan will be terminated and the payments will be accelerated so that the named executive officer receives the distribution within 12 months of the Group Merger."*

As is similar to the share-based economics, Boenning noted specifically that the effect of the Transaction on deferred payments to the Boards of Directors and executive officers appears to be only as a trigger to their payments and not as contributing to their accumulated value.

g. Transaction Specific

The last components of the economics to be received by the Boards of Directors and executive officers are items that are a specific direct result of the nature of a company entering into a change-in-control transaction. In the Transaction, as detailed in the PIS, there are three Transaction specific sources of economics for the Boards of Directors and executive officers. These are:

- Advisory Group Compensation - Boards of Directors
- 2011 Target Bonuses - Executive Officers
- Change-in-Control Payments - Executive Officers

In addition, as disclosed in the PIS, executive officers have been offered retention bonuses by Nationwide.

Boenning principally relied on its discussion with the senior members of the Nationwide management team to understand the appropriateness and motivation behind the levels of the compensation extended through the 2011 target bonuses, CIC payout and retention bonus in the Transaction.

The nature of the Advisory Group Compensation is summarized in the PIS as:

> *"All directors of Harleysville Mutual (except those members of the Special Litigation Committee described below under the heading "Litigation Related to the Merger") and Harleysville Group immediately prior to the effective time of the Mergers will be invited to become members of an Advisory Group to Nationwide Mutual to be established after the effective time of the Mergers. In addition, three directors of Nationwide Mutual's board of directors, who will be selected by the Chairman of Nationwide Mutual's board of directors, will become members of such Advisory Group. Mr. Scranton will serve as Chairman of the Advisory Group, which will meet three times per year at Harleysville Group's headquarters. Each member of the Advisory Group will serve for a term of at least two years. The members of the Advisory Group will be reimbursed for their out-of-pocket expenses, and each member will receive annual compensation of $40,000 for service as a member of the Advisory Group, except for Mr. Scranton who will receive annual compensation of $80,000 for serving as Chairman of the Advisory Group. The members of the Advisory Group will receive information with respect to the integration of Harleysville Group and Harleysville Mutual into Nationwide Mutual."*

In Boenning's experience as a financial advisor, the establishment of an advisory group of directors after a change-in-control transaction is not uncommon. Nationwide's management indicated in an interview that the compensation to be paid to the Company's advisory group members was based on the current levels being paid to the Boards of Directors. As noted earlier, the compensation process for the Boards of Directors resulted in compensation similar to the compensation of the consultant's comparison peer group.

According to management, all the executive officers have CIC Agreements in keeping with long-term historical practices of the Company. In fact, it appears that any compensation due under the CIC Agreements was set long ago and is routinely market tested and reported in HGIC's annual proxy filing with the SEC. Boenning learned from its review of the 2011 Proxy and discussion at the Compensation Meeting, that the Company believes CIC Agreements are necessary to attract and retain senior executives who may face potential job loss as a result of a consolidation or merger.

The details of the CIC Agreements are spelled out in the 2011 Proxy. Boenning concluded that they are customary "double trigger" agreements. Double Trigger is defined in the PIS as:

> *"…both a "change in control" of Harleysville Group or Harleysville Mutual occurs and the executive officer's employment is subsequently terminated (either by Harleysville Group without "cause" or by the executive officer for "good reason"). The agreements define "cause" as a failure by the executive officer to perform his or her duties or willful conduct that injures Harleysville Group, and define "good reason" as a substantial change in the status of the executive officer's role with Harleysville Group, including a diminution of responsibilities, reduction in pay, failure to continue comparable incentive plans or other compensation or benefit plans, the failure of Harleysville Group to cause the assumption of the agreements by any successor to Harleysville Group, any involuntary termination of employment which is not effected by a properly crafted notice of termination, or a change of place of employment."*

As noted elsewhere in the Report, the Transaction provides the opportunities for all the employees of the Company to keep their jobs for a minimum period of time. However, at the Compensation Meeting Boenning was told that the executive officers viewed their CIC Agreements as being triggered based on a substantial change in their status for "good reason" as defined above. Nationwide believed that in order to induce the officers to remain and not accept a "guaranteed payment" from their change in control agreement, Nationwide would offer to restructure payments due under the change in control agreements. Nationwide believed that, without some additional compensation to entice the executive officers to remain with the Company that it was likely that the group of executive officers would terminate their positions and were likely to try to collect CIC Payments.

The strong desire of Nationwide to ensure that the executive officers and all employees remained with the Company appeared to give rise to both the Retention Bonus Agreements and 2011 Target Bonuses. The Retention Bonus Agreements appear to have been specifically designed to entice the executive officers of the Company not to simply take their CIC Payments and leave, but instead to remain with the Company. Further, the Company advised that its existing change in control agreements did not contain non-compete or non-solicitation agreements. Nationwide reported that the restructured agreements allowed Nationwide to have the employees enter into customer and employee non-solicitation agreements. The principles of the Retention Bonus Agreements are summarized in the PIS as follows:

> *"As consideration for entering into a retention bonus agreement, each of the executive officers will be asked to agree to the termination of his or her change-in-control agreement. As consideration for such termination of the change-in-control agreement, each executive officer will receive a payment in an amount equal to the payment the executive officer would have received if the executive officer had been terminated by Harleysville Group without cause or the executive officer would have terminated their employment for good reason, in each case, following the change in control ("CIC Payment")."*

Because the above language stipulated a payment in an amount that was already committed to each executive officer, the Retention Bonus Agreement further offers an additional bonus as highlighted in the PIS:

> *"The retention bonus agreements will provide for retention bonuses of either one times or two times the sum of base salary plus the short-term incentive award(s), if any, actually paid to the executive officer attributable to the portion of the performance period(s) that occur(s) during the applicable retention period plus any outstanding short-term incentive award(s) eligible to be paid to the executive officer attributable to the portion of the performance period(s) that occur(s) during the retention period but that have not been paid as of the end of the retention period. The retention period will be 12 months from the closing date in the case of executive officers who will receive one times the payment, and 24 months in the case of executive officers who will receive two times the payment…"*

It has been well-documented through this Section VI how the executive officers will benefit from their CIC Payments and Retention Bonus payments. However, what was made much more understandable at the Compensation Meeting, was how far beyond the rank of executive officer Nationwide intended the retention bonuses to extend. This aspect of the package offered by Nationwide appears to demonstrate the extent to which it was concerned with retention of employees overall. It was described to Boenning during the Compensation Meeting that Nationwide intended to pay out retention bonuses in the following manner:

Table 42) Breakdown of Retention Bonuses

	Targeted Employees	Number of Employees	Structure	[redacted]
"Wave 1"	Executive Officers	10	1x or 2x Base; Incentive Bonus	
	Officers	60	1x or 2x Base	
"Wave 2"	Salesmen	60	60% - 69% of Base	
"Wave 3"	Critical Role People	NA	NA	

Source: Company HR director and discussions with Nationwide

Nationwide executives confirmed that the retention program has a budget of $35 million. This amount was determined by Nationwide to be within its corporate retention agreement

guidelines and human resources determination of best practices. Nationwide reported that the retention agreements are not "gifted" in that they must be earned by continued employment and attainment of employee goals. In addition, Nationwide and the Company reported the retention agreements provide for non-compete and non-solicitation covenants that were otherwise not part of the CIC Agreements.

To further build goodwill with the Company's employees and to ensure a smooth transition in the Transaction, Nationwide and the Company reported that it agreed to pay the 2011 performance bonuses to all eligible employees. Beth Friel described to Boenning at our Compensation Meeting how critical this was in terms of employee morale. [redacted] Again, Boenning was unaware prior to the meeting (and the PIS did not set forth in detail) the number of employees that the 2011 Target Bonus payments reach.

Table 43) 2011 Target Bonuses

	Type	[redacted]
Executive Officers	Total Bonus	
Other Officers	Total Bonus	
Non-officers	Total Bonus	
Total Bonus		

Source: Company information

Boenning questioned the need for such 2011 Bonus payments to be made to the executive officers given their other sources of retention compensation, but was told that the 2011 Target Bonuses were always discussed for all employees as a group.

There was one additional item relating to the acceleration of certain compensation triggered by the Transaction that Boenning believed was worth noting. As stated in the PIS:

> *"In order to preserve economic benefits to Harleysville Group and to Harleysville Mutual, and their respective stockholders and policyholders, of approximately $14.0 million that would otherwise have been expended or lost in connection with excise taxes, lost tax deductions and tax "gross-up" payments associated with change in control payments made pursuant to the Mergers, on December 20, 2011, the Compensation and Personal*

Development Committee of Harleysville Group (the "Committee") approved, for five executive officers: (1) payment, on an accelerated basis, of 2011 cash bonuses, at a target level of performance (the "2011 Target Bonuses"), which 2011 Target Bonuses are committed to be paid by Nationwide Mutual to executive officers and other employees of Harleysville Group within 60 days after the closing of the Mergers; and (2) the vesting of time-based restricted stock/restricted stock unit awards held by certain executive officers (subject to transfer restrictions described below); and committed to accelerate, at the end of the performance period, certain performance-based restricted stock/restricted stock unit awards held by certain executive officers of Harleysville Group. The executive officers receiving such accelerated compensation include Michael L. Browne and Arthur E. Chandler. In addition, 2011 Target Bonuses and equity-based compensation that would otherwise be due to be paid to three additional executive officers of Harleysville Group were accelerated. Such accelerated compensation will be paid on December 30, 2011."

The 2011 Target Bonuses and the outstanding equity awards represent compensation that, but for the acceleration, would have been paid to the executive officers either on vesting dates arising at various times in 2012 or, if not paid earlier, at the time of or following the closing of the HGIC merger. As conveyed by Company management, they believed that the acceleration in payment of such compensation is in the best interests of HGIC and its stockholders.

In connection with the acceleration of the 2011 Target Bonuses and the accelerated vesting of selected equity awards, HGIC and each impacted executive officer entered into an agreement that imposes significant transfer restrictions on the accelerated compensation. Under the Agreement, each impacted executive officer agreed to return the 2011 Target Bonus, less the Federal, state and local income and employment taxes paid by the executive officer with respect to the 2011 Target Bonus, if: (1) the Subsidiary Merger is not consummated and a change in control of the Company does not otherwise occur before the effective date of the termination of the Merger Agreement, or (2) if the executive officer's employment by HGIC is terminated prior to the 60th day following the closing of the Subsidiary Merger for any reason other than termination by HGIC without cause. In addition, in the event of a return of the 2011 Target Bonus compensation, the executive officer agreed to assign to HGIC any and all rights to a refund for taxes paid, and to assist HGIC in its pursuit of such refunds. With respect to accelerated equity-based compensation, under the Agreement each executive officer cannot transfer, assign, gift, pledge, hypothecate or otherwise transfer, for value or otherwise, any of the shares of common stock received until the earlier of the original vesting date of such shares or the closing date of the Subsidiary Merger.

On the following page are two charts that summarize the total economic benefits to be received by the Boards of Directors and executive officers. As laid out in the preceding pages, the charts are grouped into:

- Compensation from owned shares and shares equivalents
- Deferred compensation
- Transaction specific compensation

Of the $100 million in potential economic benefits identified in Table 44, Boenning noted that 95% of the Boards of Directors' share and 72% of the executive officers' share, or approximately $74 million altogether, appears to be driven by factors relating to market-based compensation and benefit programs that originated in some cases more than 15 years ago. Further, the CIC Agreements were entered into prior to the Transaction and do not appear to be specifically linked to Nationwide or to the Transaction.

Table 44) Executive Officers Total Economics

Executive Officers - Total Economics Driven by Transaction

	Owned Shares and Share Equivalents			Accelerated Payments			Transaction Specific			
Name	Value of Owned Shares	Value of Shares Underlying Stock Awards	Value of Stock Options	SERP Balance (12/31/11)	Deferred Comp Balance (12/31/11)	Projected COLI Balance (3/31/12)	2011 Target Bonus	CIC Payment	Retention Bonus Offered	Total Economics
Michael L. Browne	$11,954,880	$2,641,800	$12,026,117	$193,100	$1,373,876	$1,511,476	$528,000	$3,620,635	$2,376,000	**$36,225,883**
Arthur E. Chandler	1,381,444	246,600	2,102,543	15,000	54,442	0	234,000	1,176,933	594,000	**5,804,963**
[redacted]										
Kevin M. Toth	1,047,619	516,000	1,698,947	0	15,716	0	177,000	958,180	944,000	**5,357,462**
Allan R. Becker	1,170,115	125,100	682,233	0	4,881	0	119,250	802,498	768,500	**3,672,577**
Beth A. Friel	567,908	115,500	518,314	0	1,190	0	119,250	806,508	768,500	**2,897,170**
[redacted]										
TOTAL	**$22,291,875**	**$5,201,400**	**$25,384,208**	**$460,600**	**$1,715,872**	**$1,511,476**	**$1,792,154**	**$11,810,839**	**$8,363,634**	**$78,532,058**

Table 45) Non-Employee Directors Total Economics

Non-Employee Directors - Total Economics Driven by Transaction

	Owned Shares and Share Equivalents			Accelerated Payments		Transaction Specific	
Name	Value of Owned Shares	Value of Shares Underlying Stock Awards	Value of Stock Options	Deferred Comp Balance (12/31/11)	Projected COLI Balance (3/31/12)	Advisory Committee Fees	Total Economics
Barbara A. Austell	$0	$446,160	$0	$0.00	$0.00	$80,000	**$526,160**
W. Thacher Brown	2,393,340	947,520	273,978	67,740	652,437	80,000	**4,415,015**
G. Lawrence Buhl	180,023	608,760	0	0	0	80,000	**868,783**
Nicholas DeBenedictis	1,203,660	518,760	0	110,016	0	80,000	**1,912,436**
Ellen M. Dunn	0	458,460	0	34,155	0	80,000	**572,615**
Mirian M. Graddick-Weir	997,865	608,760	273,978	418,654	0	80,000	**2,379,256**
Michael L. Lapeyrouse	5,726	608,760	191,978	307,456	0	80,000	**1,193,919**
Jerry S. Rosenbloom	1,667,845	947,520	273,978	69,788	0	80,000	**3,039,131**
William W. Scranton III	424,973	608,760	273,978	0	0	160,000	**1,467,711**
William E. Storts	1,198,966	608,760	0	0	162,463	80,000	**2,050,189**
TOTAL	**$8,072,398**	**$6,362,220**	**$1,287,888**	**$1,007,809**	**$814,900**	**$880,000**	**$18,425,214**

h. Conclusion

Based on many different factors pointed out in this Section, the compensation process at the Company appears to utilize sophisticated, consistent, and well thought-out median market-based metrics. A review of the public disclosures revealed that in conjunction with a comprehensive market-based compensation and benefit program and long tenure among certain employees, a substantial base of shares, share equivalents and compensation deferrals was accumulated. An accumulated base of equity fueled by an acquisition premium could lead to a large economic value to the Boards of Directors and executive officers in any change of control scenario. The value in the Transaction from CIC payments, retention bonuses and 2011 target bonuses was, according to Nationwide, driven by Nationwide's strategic goals for retention and growth of the "Harleysville" franchise. The fact that the overall retention program covers so much of the employee base appears to suggest that the decision to pay this compensation was not motivated by any interest in the executive officers alone.

Furthermore, from the Policyholders' perspective, the retention of the Boards of Directors through the advisory group, executive officers and employee base suggests that there will be continuity for the Policyholders. Though not highlighted in the PIS, this appears to be another Policyholder benefit in support of the overall Transaction.

Note: Except as otherwise expressly stated in this Section VI, the source for all information in this Section VI is Compensation Memo, PIS, 2011 Proxy, SNL Financial and Capital IQ as of the Evaluation Date

Section VII

Comparisons of both Policyholder's Rights and Harleysville Mutual to Nationwide and benefits conferred upon Policyholders

Boenning's Engagement Letter with the Department included the following:

> "(l) Examine the rights of Policyholders under the Transaction and how such rights are proposed to be modified by the Transaction."

In accordance with its Engagement Letter, Boenning reviewed the PIS and Proxy provided by the Company, the Griffin opinion and the opinion provided by Stevens & Lee with respect to the rights of the Policyholders as well as a comparison of those rights with those at Nationwide. Beyond a comparison of the Policyholders' rights (Policyholders as members), Boenning also noted in its review, as summarized below, that several benefits will be conferred upon the Policyholders as creditors as a result of the Transaction. Taken together, Policyholders' rights and benefits would appear to be relevant to the Department's analysis of the standard set forth in Section 991.1402(f)(1)(vi) of the Act. Boenning has reviewed and assembled in this Section the body of work provided by the Company and its Advisors that may be relevant to the Department's analysis.

A. Policyholder's Rights at Harleysville Mutual

According to the PA BCL [redacted], Policyholders have several rights:

> *"The rights of a policyholder of a PA mutual insurance company are determined by the PA Business Corporation Law of 1988, as amended (the PA BCL) ,[1] the articles of incorporation and bylaws of the insurance company, and the terms of the policy issued to the policyholder. Membership is conferred solely by the purchase of an insurance policy and carries with it the right to vote on company matters, the contractual right to enforce the policy by its terms, the right to dividends as, if, and when declared, a priority right to purchase stock in the event of demutualization, and the potential for distribution of surplus on dissolution of the company. Membership creates no other rights."*

> [1] *"Section 2101 (a)(3) of Chapter 21 of the PA Associations Code provides that Chapter 21 shall be applicable to certain nonstock corporations, including a domestic insurance corporation that is a mutual insurance company. 15 PA.C.S.A § 2102(a)(3). Section 2101(c) of Chapter 21 provides that the BCL shall be generally applicable to all nonstock corporations and that references to "shares" and "shareholder" shall mean "memberships" and "member", respectively, with respect to a mutual insurance company. 15 PA.C.S.A § 2101(c). Accordingly, the provisions of the BCL that are applicable to stock corporations are applicable to HMIC, and any reference in the BCL to "shares" or "shareholder" will be a reference to membership interests in HMIC and the members of HMIC, respectively. "*

[redacted] Section 2124 of the PA BCL grants every member of a mutual insurance company the right to one vote on each matter presented to the members of the company:

> *"Except as otherwise provided in a bylaw adopted by the members or in a written document evidencing membership, every member of record of a nonstock corporation shall have the right, at every meeting of members, to one vote. 15 PaC.S.A. § 2124."*

[redacted] the potential right to a distribution of surplus on dissolution derives from Section 2126 of the PA BCL which states:

> *"If at the time of dissolution of a nonstock corporation the articles, bylaws and documents evidencing membership fail to define the respective rights and preferences of the members upon dissolution, the surplus of cash or property remaining after discharging all liabilities of the corporation shall be paid to or distributed among the members according to such a plan of distribution as the members may adopt. 15 PA.C.S.A § 2126."*

In contrast, [redacted], Section 21205(f) of the Pennsylvania Associations Code, which specifically addresses dissolution of mutual companies, states:

> *"…the assets of mutual companies, other than mutual life companies, which may not be properly credited to policyholders and members, shall be escheated to the Commonwealth upon the dissolution of such companies. 15 PA.C.S.A § 21205 (f). "*

[redacted]

[redacted]

Boenning notes that [redacted] the Associations Code and the BCL, in the event of a solvent dissolution, "there remains the possibility that … a member of [Harleysville Mutual] would receive no distribution of any excess. At the same time, it appears that members of Ohio mutual insurance companies do not face the possibility of escheat of surplus." Nationwide is an Ohio domiciled insurance company. Given the Transaction and new corporate

structure, Harleysville Mutual would be merged into Nationwide with Nationwide surviving, and thus become subject to Ohio mutual insurance company law. [redacted] Policyholders may have rights to excess surplus upon dissolution – which may constitute a potential improvement.

B. Griffin Presentation – Analysis of Policyholder Rights

In addition to reviewing [redacted] the PA BCL, the Associations Code, and the differences in mutual Policyholder's rights during dissolution, Boenning reviewed a number of other considerations that Griffin had analyzed with respect to Policyholders.

As stated in the Griffin presentation, they are:

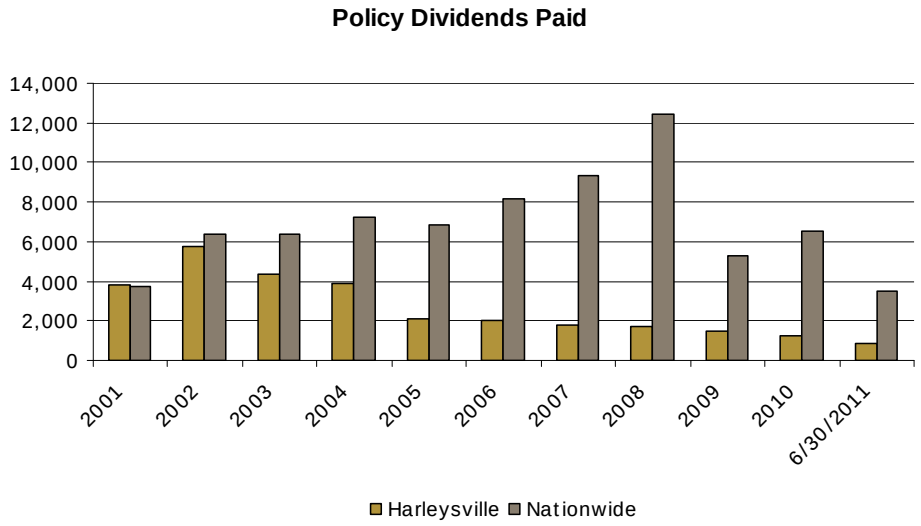
- *"Dividend Policies-*
  - *Policyholders in each company have right to dividends as, if and when declared by the board.*
  - *In practice, both companies pay small policyholder dividends.*
- *Change in pooling arrangement*
- *Policyholder rights to or claims on surplus-*
  - *Rights upon solvent liquidation*
- *Rights with respect to governance of the combined entity-*
  - *Voting rights*
  - *Rights upon fundamental change or demutualization*
- *Continuation of Policies and premium costs-*
  - *Policyholders have an interest in continued membership and insurance coverage*
- *Surplus Generation-*
  - *Ability to generate surplus enhances claims paying ability and member interest in surplus"*

a. *Dividend Policies*

According to Griffin, Harleysville Mutual routinely pays a dividend on workers compensation participating policies, and declaration and payment of such dividend is at the sole discretion of Harleysville Mutual's Board of Directors. According to Nationwide executives, Nationwide does not have a formal dividend policy, but has paid quarterly dividends on workers compensation policies. Nationwide typically does not pay dividends on personal or other commercial lines policies. Harleysville Mutual also has a non-guaranteed dividend program with respect to its Pennsylvania School Bus Transportation Program, but such policy dividends have not been paid in years due to the failure to achieve certain performance thresholds. The Griffin analysis regarding Policyholder dividends appears to be reasonable.

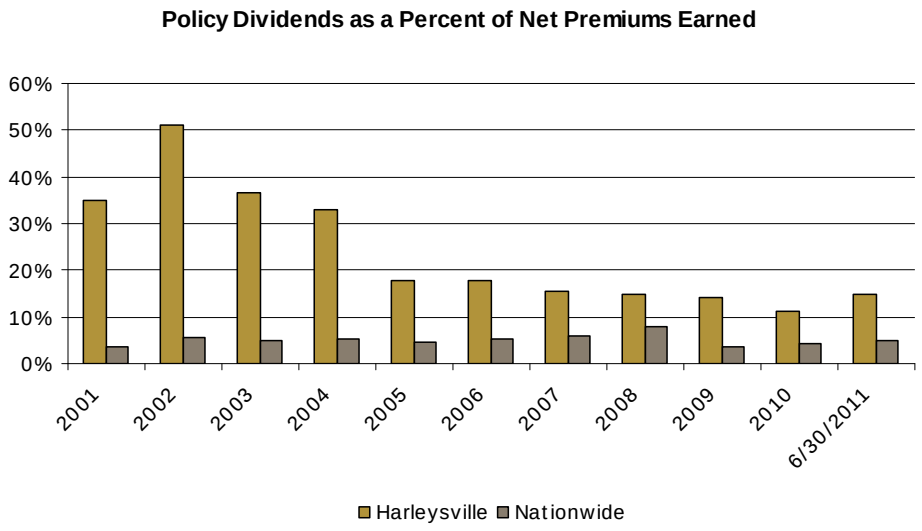
On a gross basis, Nationwide tends to pay higher policy dividends but less as a percent of net premiums written.

Table 46) Policy Dividends Paid



Source: SNL Financial

Table 47) Policy Dividends as a Percent of Net Premiums Earned



Source: SNL Financial

b. *Change in Pooling Agreement*

"Griffin assumed that Harleysville Mutual would join the Nationwide Group 28 company pool. Currently, 84% of premiums, losses, and LAE are allocated to Nationwide Mutual and Harleysville Mutual members will become members of the dominant pool. The transaction will eliminate the sharing of net premiums with Harleysville Group minority shareholders. Historically, the pooling agreement resulted in a benefit to Harleysville Group and the non-controlling interests, as they received 80% of premiums, losses and LAE."

Table 48) Pooling Agreement

	For the year Ended December 31,		
	2008	2009	2010
Premiums Earned from Affiliates	$918,515	$858,500	$866,350
Losses and Loss Settlement Expenses	610,768	552,491	589,105
Net	307,747	306,009	277,245
Premiums Ceded to Affiliates	761,751	730,699	783,340
Losess and Expenses Ceded to Affiliates	524,735	476,641	540,619
Net	237,016	254,058	242,721
Net Premiums Recorded By Public Company In Excess of Net Premiums Ceded	$70,731	$51,951	$34,524

Source: 2010 Harleysville 10-k

Boenning agrees with Griffin's analysis regarding the financial impact on the Company pooling agreement under the Transaction.

c. Policyholder's Rights: Claim on Surplus

According to Griffin:

> *"except in the case of a voluntary liquidation, policyholders of a PA mutual have no claim on surplus, so that surplus is relevant only from a claims paying and loss absorption perspective. PA law is ambiguous as to policyholder rights upon solvent liquidation. One statute states that residual goes to policyholders, while another provides that residual goes to the Commonwealth. Ohio law appears to prove that residual goes to policyholders. Voluntary liquidations are rare; this proposed merger is not a voluntary liquidation. Merging with Nationwide Mutual preserves or potentially enhances the rights of policyholders to residual surplus in a voluntary liquidation of Nationwide. Griffin was unable to obtain data to evaluate a policyholder's pro rata share of surplus either at Harleysville or on a pro forma basis assuming a solvent liquidation. For purposes of Griffins analysis and in the interest of being conservative, Griffin assumed the transaction would be dilutive to Harleysville policyholders on a pro forma basis. However, the likelihood of a solvent liquidation is so remote, this assumed dilution does not alter Griffins conclusion."*

Assuming that Griffin's analysis and explanation of Pennsylvania and Ohio law are correct, Griffin's conclusions regarding Policyholders' rights and claims on surplus appear to be reasonable from a financial point of view.

d. Policyholder's Rights and Policy Continuation

According to Griffin:

> *"mutual members have limited corporate governance rights but policyholders rights are enhanced by margins with Nationwide Mutual because of different demutualization statutes. In addition, pursuant to the agreement, policies in force will carry over to Nationwide. Renewal and premium levels will be subject to Nationwide policies and procedures and are not guaranteed- similar to the current arrangement at Harleysville."*

Table 49) Policyholder's Rights

	Harleysville Mutual	Nationwide
Right to vote for Directors	Yes	Yes
Right to vote on fundamental transactions	Yes- Policyholders must vote on mergers or demutulizations	Yes- policyholders must vote on mergers or demutualizations
Rights upon demutualization	Subscription rights- Policyholders receive the first right to buy stock, based upon an appraisal value but get no free distrubition of surplus	Right to free distribution of surplus

Source: Griffin Presentation

Assuming Griffin's analysis of Pennsylvania and Ohio law is accurate, its analysis appears to be reasonable from a financial point of view.

e. Surplus Generation

As stated in the PIS:

"With respect to policyholders as members, Griffin noted that Nationwide Mutual had the prospect for stronger surplus generation than Harleysville would have as a standalone entity, that its members have governance rights with respect to Nationwide Mutual that are comparable to the rights that Harleysville Mutual's members hold with respect to Harleysville Mutual, that its members enjoy a right to a distribution of surplus under Ohio law in the event of demutualization, compared to a stock subscription right as provided under Pennsylvania law, and that its members have more favorable rights upon a solvent liquidation of Nationwide Mutual than would the members of Harleysville Mutual upon a solvent liquidation of Harleysville Mutual."

Boenning agrees with Griffin in stating that Harleysville Mutual had the prospect for stronger capital surplus generation as a pro forma entity with Nationwide than that of a stand-alone company.

f. Benefits Conferred Upon Policyholders as Creditors

Beyond the comparison of the Policyholder's rights, which are essentially the benefits conferred on Policyholders as Members, Boenning noted from various sources during its review that the Transaction also confers benefits on Policyholders as creditors. The Department may consider these benefits important to its analysis of the standard set forth under Section 991.1402(f)(1)(iv). Griffin's Opinion specifically focused on the Policyholders as both creditors and members as one

constituent impacted by the Transaction. This portion of the Griffin analysis is included in Section V. For the purpose of this Section, Boenning has summarized the items noted in Griffin's Opinion that highlight the benefits conferred on the Policyholders.

According to Griffin, the benefits conferred on Policyholders as creditors include:

- Combined entity creates a stronger competitor in the marketplace giving Policyholders access to increasing profitability, claims paying ability and a stronger surplus
- Policyholders will benefit from the cross selling capabilities arising out of the greater product offering of the combined entity
- The broader geographic footprint of the combined entity diversifies the Policyholders' risk for catastrophic losses
- Combined entity will spread fixed costs over a wider revenue base benefiting Policyholders through increased profitability, claims paying ability and a stronger surplus

While not identified in any of the information reviewed by Boenning, Boenning noted one additional benefit to Policyholders as both members and creditors. In Section VI.B., Boenning highlighted the fact that the nature of the compensation plan utilized by the Company and the retention compensation paid by Nationwide in the Transaction were both apparently designed to retain the management and employees. Successful retention of the management and employee base may be a significant benefit to the Policyholders, because they will apparently continue to have the same management team. This may be relevant to the Department's analysis of the standards set forth under Section 991.1402(f)(1)(iv) and (vi), both because it should serve to mitigate changes to the corporate structure and management and that may in turn impact the Department's assessment as to whether the Transaction is hazardous or injurious to the insurance buying public.

In totality, the information reviewed by Boenning appeared consistent with information noted in interviews with management and Advisors and in other transaction related documents reviewed by Boenning. Griffin's and Stevens & Lee's comparisons of Policyholder's rights indicate no diminution in Policyholder's rights. Rather, under their analysis, the Transaction would confer several meaningful benefits upon Policyholders, especially as creditors.

Section VIII

Review of Stockholder Voting Agreement between Harleysville Mutual Insurance Company and Nationwide Mutual Insurance Company, dated September 28, 2011

Boenning's Engagement Letter with the Department included the following:

> "(b) Review any regulatory filings (including Form A merger filings) submitted by the Company or its Transaction Partner to the Department.", and
>
> "(n) Examine and provide commentary on the differences, similarities and potential differences, between the responsibilities and potential conflicts of interest of Harleysville Mutual directors and those of the stock holding company."

In accordance with its Engagement Letter, Boenning reviewed the Transaction Partner's Form A filing. The Form A filing included as an exhibit the Voting Agreement. As discussed below, the Voting Agreement obligates Harleysville Mutual, as a stockholder in HGIC, to vote its shares in favor of the Transaction. A public comment objecting to the Transaction cites the Voting Agreement as one item that might be of concern. Company management indicated that the determination of the appropriateness of the Voting Agreement involves both the nature of the role of Harleysville Mutual Board of Directors in the approval of the Voting Agreement as well as differences between the duties of the Harleysville Mutual Board of Directors and those of the HGIC Board of Directors. The latter issue is examined in more detail in Section VI ("Examination of Potential Director Conflicts"). The analysis and commentary in this Section reviews the appropriateness of the Voting Agreement.

A copy of the Voting Agreement is included as Exhibit XV. The Voting Agreement, in summary, appears to compel Harleysville Mutual, the owner of a majority of the shares in HGIC, to vote such shares in favor of the Transaction as noted below:

SECTION 3. Covenants of the Stockholder. The Stockholder covenants and agrees as follows:

> *"(a) (1) At any meeting of the stockholders of the Company, or at any postponement or adjournment thereof, called to seek the affirmative vote of the holders of a majority of the outstanding Shares to adopt the Merger Agreement (the "Requisite Stockholder Vote") or in any other circumstances upon which a vote, consent or other approval (including by written consent) with respect to the Merger Agreement, the Subsidiary Merger or other Transactions is sought, the Stockholder shall vote (or cause to be voted or provide written consent with respect to) the Subject Shares in favor of granting the Requisite Stockholder Vote.*
>
> *(2) The Stockholder hereby irrevocably grants to, and appoints, Nationwide and any individual designated in writing by Nationwide, and each of them individually, as the Stockholder's proxy and attorney-in-fact (with full power of substitution), for and in the*

name, place and stead of the Stockholder, to vote the Subject Shares, or grant a consent or approval in respect of the Subject Shares in a manner consistent with this Section 3. The Stockholder understands and acknowledges that Nationwide is entering into the Merger Agreement in reliance upon the Stockholder's execution and delivery of this Agreement. The Stockholder hereby affirms that the irrevocable proxy set forth in this Section 3(a)(2) is given in connection with the execution of the Merger Agreement and is therefore coupled with an interest. The Stockholder hereby further affirms that the irrevocable proxy may under no circumstances be revoked, as long as this Agreement remains in effect. Such irrevocable proxy is executed and intended to be irrevocable, as long as this Agreement remains in effect. The irrevocable proxy granted hereunder shall automatically terminate upon the termination of this Agreement in accordance with its terms. '

(b) At any meeting of stockholders of the Company or at any postponement or adjournment thereof or in any other circumstances upon which the Stockholder's vote, consent or other approval (including by written consent) is sought, the Stockholder shall vote (or cause to be voted) the Subject Shares against and withhold consent with respect to (i) any merger agreement or merger (other than the Merger Agreement and the Mergers), consolidation, combination, sale of substantial assets, reorganization, recapitalization, dissolution, liquidation or winding up of or by the Company, (ii) any Alternative Transaction or Alternative Transaction Proposal, and (iii) any other action, agreement or transaction that would reasonably be expected to result in a breach of any covenant, representation or warranty or any other obligation or agreement of the Company contained in the Merger Agreement or of the Stockholder contained in this Agreement or that would impede, interfere or be inconsistent with, delay, postpone, discourage or adversely affect the timely consummation of the Subsidiary Merger or any other Transaction. The Stockholder shall not commit or agree to take any action inconsistent with the foregoing.

(c) Except as otherwise provided in this Agreement, the Stockholder shall not (i) sell, transfer, exchange, pledge, assign, hypothecate, encumber, or tender or otherwise create a Lien on or dispose of(including by gift) (collectively, "Transfer"), or enter into any Contract, option or other arrangement (including any profit sharing arrangement) with respect to the Transfer of, any Subject Shares, any economic interest therein, or any rights to acquire any securities or equity interests of the Company to any Person other than pursuant to the Merger Agreement or (ii) grant any proxies or enter into any voting trust or other agreement or arrangement, whether by proxy, voting agreement or otherwise, with respect to any Subject Shares or any rights to acquire any securities or equity interests of the Company and shall not commit or agree to take any of the foregoing actions. As used in this Agreement, the term "Transfer," shall also include any pledge, hypothecation, encumbrance, assignment or other disposition of such security or the record or beneficial ownership thereof, the offer to make a sale, transfer or other disposition, and each agreement, arrangement or understanding whether or not in writing, to effect any of the foregoing.

(d) The Stockholder hereby consents to and approves the actions taken by the Company Board in approving the Subsidiary Merger. The Stockholder hereby waives, and agrees not to exercise or assert, any appraisal or dissenter's rights in connection with the Subsidiary Merger.

(e) The Stockholder hereby agrees that, in the event (i) of any stock dividend, stock split, recapitalization, reclassification, combination or exchange of shares of capital stock of the Company of, or affecting, the Subject Shares, (ii) that the Stockholder purchases or otherwise acquires beneficial ownership of or an interest in any shares of capital stock of the Company after the execution of this Agreement or (iii) that the Stockholder voluntarily acquires the right to vote or share in the voting of any shares of capital stock of the Company other than the Subject Shares (collectively, the "New Shares"), the Stockholder shall deliver promptly to Nationwide written notice of its acquisition of New Shares which notice shall state the number of New Shares so acquired. The Stockholder agrees that any New Shares acquired or purchased by the Stockholder shall be subject to the terms of this Agreement, including the representations and warranties set forth in Section 1, and shall constitute Subject Shares to the same extent as if those New Shares were owned by the Stockholder on the date of this Agreement."

As owner of 14,526,445 of the 27,128,314 shares outstanding as of June 30, 2011 (or approximately 54%) of HGIC, it is understandable that a buyer of HGIC would wish to secure the vote of Harleysville Mutual in favor of a transaction. Securing the vote of Harleysville Mutual would effectively render approval of the Transaction a certainty given Harleysville Mutual's majority ownership position. Nationwide appeared to agree with this premise by noting in the recitals to the Voting Agreement:

"WHEREAS, as a condition to their willingness to enter into the Merger Agreement, Nationwide … [has] requested that the Stockholder [i.e. Harleysville Mutual] enter into this Agreement."

In its review of the Voting Agreement, Boenning noted potential issues for examination with the Company:

- Nature of the role of the directors in approving the Voting Agreement
- Duty to all constituents when agreeing to the Voting Agreement
- Difference between "superior proposal" to Harleysville Mutual and HGIC

A. Role of Harleysville Mutual Board of Directors in approving Voting Agreement

The following section is based on the PIS and interviews with management and legal advisors of the Company. The nature of the role of the Harleysville Mutual Board of Directors in evaluating the Voting Agreement is described as one that is separate from the Board of Director's role in considering the potential Transaction. The Harleysville Mutual Board of Director's role in evaluating the potential Transaction is more closely examined in Section V ("***Review of Decision***

Process and Alternatives") and is reported as a duty to the corporation. The Harleysville Mutual Board of Directors' role in approving the Voting Agreement is described as a duty to Harleysville Mutual in its role as stockholder of HGIC.

Through Boenning's interview with the members of the Special Committee of the Harleysville Mutual Board of Directors, it was conveyed to Boenning that an additional constituency, the HGIC public minority stockholders (because of Harleysville Mutual's role as majority stockholder of HGIC), was also considered (as part of the Board of Director's fair and reasonable determination). As a result, Boenning believed it was appropriate to review the Keefe, Bruyette & Woods ("***KBW***") fairness opinion received by HGIC as this was the material available to the Boards of Directors to assist them in assessing the impact of the Transaction on the minority stockholder constituency. Boenning's review of the KBW Fairness Opinion, including analysis of the Subsidiary Merger, from a financial point of view is detailed in the Appendix.

In that context, and according to the Advisors of both Harleysville Mutual and HGIC, the Harleysville Mutual Board of Directors, as directors of the majority stockholder of HGIC, examined whether the potential Transaction was in the best interests of the minority stockholders of HGIC. According to the KBW analysis in the Appendix, the potential Transaction appears to be fair and in the best interest of the HGIC minority stockholders.

B. "Duty to all constituents when agreeing to the Voting Agreement"

According to the Company and its Advisors, HGIC directors had different duties than directors of Harleysville Mutual. According to the Company and its Advisors, a fiduciary out provides for an opportunity for a Delaware Board of Directors to honor its fiduciary duty to its stockholder constituents if presented with a more attractive financial offer. Also, according to the Company and its Advisors, as directors of a Delaware corporation, the HGIC directors were advised that a fiduciary duty out was required and, therefore, the Merger Agreement provides the "out" noted in Section 7.2 (d) cited above.

Boenning noted that Harleysville Mutual is a Pennsylvania domiciled insurer and a Pennsylvania corporation. Harleysville Mutual's legal counsel, Stevens & Lee and Ballard Spahr, cite PA BCL Section 1712 (a):

> *"each director of a [Pennsylvania] business corporation shall stand in a fiduciary relation to the corporation and shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation ..."*

According to the Company and its legal advisors, Harleysville Mutual's Board of Directors owe their fiduciary duties to Harleysville Mutual. Further, Stevens & Lee summarized Section 1715 (a) and (b) of the PA BCL:

> *"[i]n discharging the duties of their respective positions, the board of directors, committees of the board and individual directors of a business corporation may, in considering the best interests of the corporation, consider to the extent they deem appropriate": (1) the interests of Policyholders, employees, suppliers, customers, independent agents and the communities in which they have offices; (2) the long-term as well as short-term interests of the corporation; (3) the resources, intent and conduct of any person seeking to acquire control of the corporation; and (4) any other pertinent factors."*

> *"[None of] the interests of any particular group affected by [any] action" shall be "a dominant or controlling interest or factor" in the decisions of the individual directors, special committees or board of directors."*

According to the Company and its legal advisors, the Harleysville Mutual Board of Directors was advised that its fiduciary duties are to Harleysville Mutual itself. The Company's legal advisors also advised the directors that directors of a Pennsylvania corporation can simply reject any potential transaction. Accordingly, the Harleysville Mutual Board of Directors was advised that the authorization to execute the Voting Agreement was consistent with its fiduciary duties.

C. <u>Difference between "superior proposal" to Harleysville Mutual and HGIC</u>

Based on the analysis of the legal advisors and the Boards of Directors, there appears to be a possibility that a proposal for a transaction could be made that could meet a third party's definition of a superior proposal for Harleysville Mutual while not meeting the definition for a superior proposal to HGIC and thus not triggering HGIC's fiduciary out contained within the Voting

Agreement. Such a proposal could include, among other possibilities, a promise of potential proceeds, dividends or Policyholder credits to the Policyholders, the prospect of merging with a more secure or highly rated company than Nationwide, or the prospect of better alternatives for agents, employees or the community. However, given the Advisors' opinions of the influence the Company's unique structure places on potential transaction structures, the pool of potential parties who could make such an offer appears to be limited.

Additional examination of the potential for different responsibilities of the Harleysville Mutual Board of Directors and HGIC Board of Directors are contained in Section VI.

D. Conclusions

Harleysville Mutual received and appeared to rely on advice of counsel in assessing the Voting Agreement. The documentation reviewed by Boenning indicates that the Harleysville Mutual Board of Directors thoroughly considered the potential Transaction and Voting Agreement. Further, based on the analysis of the Advisors described in this Report, the likelihood of a superior proposal to Harleysville Mutual appears to be remote.

Appendix

A. Background and Independence of Boenning

Boenning is an investment banking and investment advisory firm focusing generally on financial advisory, mergers & acquisitions and raising capital for companies engaged in a variety of industries. Boenning specializes in the financial services industry and its senior professionals have significant experience working with companies in the insurance industry. Boenning is regularly engaged in the valuation of securities and companies for a variety of purposes and in connection with various types of transactions. Exhibit II presents the background and experience of Boenning's professional staff contributing to the Report. We believe that Boenning and its principals, officers, directors, employees, and related interests are independent of the Transaction Partner, the Company, and the Department.

B. Materials Reviewed and Procedures Undertaken

In preparing the Report for the Department, Boenning visited with the Company's management on several occasions and interviewed their President & CEO, Chief Financial Officer, and General Counsel, among others. Boenning also met with Harleysville Mutual's and HGIC's respective Advisors on one or more occasions and conducted telephone interviews with management and Advisors to address various questions that developed during the course of Boenning's analysis. Boenning provided an information request list and follow-up requests (collectively "***Information Request***") to the Company to further understand specific items. The scope of Boenning's analysis included, but was not limited to the following:

- Discussions with management concerning current and historical operations including:
  - Management discussion and analysis for the period ended December 31, 2010
  - KPMG LLP audited GAAP and statutory consolidated financial statements for the years ended December 31, 2009 and December 31, 2010
  - Unaudited GAAP financials statements (draft) for interim periods
- The assumptions underlying the business plan and risk factors that could affect the financial performance of Harleysville Mutual and HGIC
- The strategic alternatives and factors considered in determining that the Transaction was the best alternative available to Harleysville Mutual and HGIC. The alternatives and their challenges are in Section V of the Report

- Review of the minutes of the Harleysville Mutual and HGIC Boards of Directors Meetings during the past two years
- Review of the Application and amendments thereto, and the PIS
- Reviewing the responses of Harleysville Mutual and HGIC to Boenning's Information Request during January and February 2012
- Obtaining and reviewing certain financial and other information regarding the business of Harleysville Mutual and HGIC
- Review and discussion of the Transaction with management
- Review and discussion of the Advisors' analyses and opinions
- Analyzing the business, economic and competitive environment, including the industry in which Harleysville Mutual and HGIC operate, to assess current and anticipated trends
- Reviewing the financial performance and market valuation of insurance companies that are publicly-traded
- Considering other similar transactions in the merger & acquisition market
- Considering such other information regarding Harleysville Mutual and HGIC, the insurance industry, and the market for insurance company equities that Boenning believes appropriate

Boenning reviewed various documents, both public and private, with respect to Harleysville Mutual and HGIC. Boenning was granted access to the Data Room in order to view and analyze various forms of information relating to Harleysville Mutual and HGIC. In our review and analysis, we have assumed and relied upon the accuracy and completeness of all of the financial and other information provided to us (including information furnished to us verbally, or otherwise discussed with us, by the Company's and the Transaction Partner's management and their respective Advisors, as well as information provided by recognized independent sources), or publicly available, and have neither attempted to verify, nor assumed responsibility for verifying, any of such information. We have relied upon the assurances of the Company's and the Transaction Partner's management that they are not aware of any facts, or the omission of any facts, that would make such information inaccurate or misleading. Furthermore, we did not obtain, make, or assume any responsibility for obtaining or making, any independent evaluation or appraisal of any individual asset or liability (contingent or otherwise) of Nationwide, Harleysville Mutual or HGIC. We did not make any independent evaluation of the adequacy of the reserves and assume they reflect the best available estimates and judgments of the Company and the Transaction Partner.

C. KBW Opinion

HGIC engaged KBW to render its opinion as to the fairness, from a financial point of view, to the holders of HGIC common shares (excluding Harleysville Mutual or its successors) of the Merger Consideration (as defined in their letter) provided for in the Subsidiary Merger (as defined). In a written opinion dated September 28, 2011, KBW concluded that:

> *"the Merger Consideration payable to holders of the Common Shares (other than Mutual Parent or its successors) is fair, from a financial point of view."*

The full text of KBW's opinion is attached as Exhibit VI. [redacted]

Based upon Boenning's review of the opinion letter and its experience in rendering fairness opinions, the KBW opinion letter contains language, terms and disclaimers customary for such opinions.

KBW disclosed that it received $50,000 for services (described in interviews as buy -side advice) to Harleysville Mutual in 2009. Boenning does not believe this prior engagement constitutes a conflict in rendering the fairness opinion to HGIC in 2011.

The KBW presentation includes the following:

- Executive Summary
- Transaction Overview
- Valuation Information
- Appendix

In the KBW presentation the $60 per share offer exceeded all valuation ranges established by the quantitative methods utilized by KBW in determining fairness. Their presentation also commented on Nationwide's post-closing commitments to employees and philanthropic activities.

a. Financial Analysis Methodologies

In determining the fairness of the transaction pricing to HGIC, an investment banker would typically consider two commonly utilized methodologies referred to as: (i) the market approach; and (ii) the income approach. A third methodology, the asset-based approach, is generally not utilized in this context for reasons discussed below. A brief discussion of each approach follows.

There are two variations of the Market Approach. One variation of the Market Approach is the Guideline Company Approach, which measures value through an analysis of publicly-traded companies operating in the same or similar lines of business. Equity securities of these corporations are traded in a free and open market, either on an exchange or over-the-counter. When applied to the valuation of businesses, consideration is given to the financial condition and operating performance of the company being reviewed relative to those of the publicly-traded companies. Sometimes, adjustments to account for significant differences between the subject company and the guideline companies are made to the valuation multiples of the guideline companies.

The other variation of the Market Approach is the Merger & Acquisition Transaction Approach. The Transaction Approach measures the value of a company through an analysis of transactions involving similar companies in the mergers and acquisitions market.

The Income Approach measures the value of an asset by the present value of its future earnings or cash flows. When applied to equity interests in businesses, value indications are developed by discounting expected cash flows to their present value at a rate of return that incorporates the risk-free rate for the use of funds and the expected risks associated with the particular investment. The discount rate selected is generally based on rates of return available from alternative investments of similar type and quality as of the valuation date.

The Asset Based or Cost Approach measures the value of an asset by the cost to reconstruct or replace it with another of like utility. When applied to the valuation of equity interests in businesses, value is based on the net aggregate fair market value of the entity's underlying assets. The technique entails a restatement of the balance sheet of the enterprise substituting the fair market value of its assets and liabilities for their book values. The resulting equity is reflective of a 100% ownership interest in the business.

KBW utilized both the Income Approach and the Market Approach to assist in determining the fairness of the Transaction to HGIC stockholders. The cost approach is typically utilized in determining the liquidation value of a company and generally not for situations where the subject business is valued as a going concern. We agree with KBW that in the context of valuing a publicly-

traded stock company for sale in a transaction such as the Transaction, the income and market approaches provide the best indicator of value because of the readily available market and financial data for comparable companies and transactions.

b. Guideline Company Approach

The Guideline Company Approach entails the following process: (i) identification of guideline companies; (ii) a comparison of the performance of the subject company to the guideline companies; (iii) the calculation of relevant valuation multiples or ratios for each of the guideline companies; (iv) choosing the appropriate valuation multiple for the subject company; and (v) application of the chosen multiple to the subject company's financial data.

Although it is clear that no two companies will ever be entirely alike, the only restrictive requirement imposed by this approach is that the publicly-traded companies selected as guideline companies be engaged in the same or similar lines of business. Other relevant factors such as size, profitability and leverage, are also considered.

c. KBW's Selection of Comparable Companies

Factors considered by KBW in selecting its comparable companies were as follows:

- Publicly-traded companies
- Regional P/C companies that underwrite standard market commercial and personal lines risks
- Market value between $200 million and $5 billion

Utilizing the constraints and criteria described above, KBW determined that eight companies were comparable to HGIC. The range of Price/ Book in this analysis was .64% to 87% with an implied median of .71%.

d. Boenning Selection of Comparable Companies

To determine the reasonableness of the KBW comparable company analysis, Boenning performed its own analysis and selected a comparative group of companies. To identify insurance

companies that displayed similar characteristics to HGIC we identified companies by using peers with total assets between $2 billion and $10 billion and with similar business lines and geographic footprint as HGIC. We believe that the criteria utilized by KBW were reasonable; however Boenning felt that to achieve a peer group even closer to that of HGIC, it was important to include companies that write business in a similar geographic region to HGIC. Boenning's peer group consisted of 10 companies of which 6 companies overlapped with KBW's analysis. Boenning decided to increase the broadness of peers based on proximity of business and similar product offerings to HGIC.

Boenning, like KBW, utilized the SNL database to search for public property and casualty insurance companies located in the U.S. and traded on the New York Stock Exchange, American Stock Exchange or the NASDAQ. Our initial search yielded a total universe of 112 companies. We identified 10 companies deemed most comparable to HGIC are as follows:

- Hanover Insurance, Inc.
- Kemper Corporation
- Alleghany Corporation
- Selective Insurance Group, Inc.
- AnTrust Financial Services, Inc.
- Tower Group, Inc.
- United Fire & Casualty Company
- State Auto Financial Corporation
- RLI Corp.
- Donegal Group Inc.

A summary of the comparable companies key trading metrics are included in Table 50 on the following page:

Table 50) HGIC Trading Performance

Trading Performance of HGIC
As of and for the LTM period ended 6/30/2011

Company Name	Ticker	9/27/2011 Closing Price	Total Market Value ($Ms)	Price / Book (%)	Price / Tang. Book (%)	Price / LTM EPS (x)	6/30/2011 FWD EPS 2011F (x)	6/30/2011 FWD EPS 2012F (x)	Current Div. Yield (%)	(1) Price / LTM Rev. (x)	(2) Price / Assets (%)
Alleghany Corporation	Y	286.99	2,543	84.17	88.27	16.03	13.67	9.48	0.00	2.73	39.66
Kemper Corporation	KMPR	24.77	1,498	70.11	82.09	9.95	12.84	11.41	3.88	0.60	18.52
Hanover Insurance Group, Inc.	THG	35.56	1,617	64.68	69.70	15.07	21.84	23.79	3.09	0.41	12.81
AmTrust Financial Services, Inc.	AFSI	22.36	1,340	162.31	224.30	8.13	13.85	10.21	1.61	1.02	24.73
RLI Corp.	RLI	62.61	1,319	152.63	163.30	9.36	8.82	8.21	1.92	2.11	48.95
Tower Group, Inc.	TWGP	22.73	937	87.38	133.29	8.33	9.06	7.59	3.30	0.54	21.56
Selective Insurance Group, Inc.	SIGI	13.41	726	65.97	66.44	11.36	NM	NM	3.88	0.45	12.66
State Auto Financial Corporation	STFC	12.79	526	76.28	76.47	NM	NM	14.71	4.69	0.35	18.70
United Fire & Casualty Company	UFCS	17.61	456	64.67	67.71	NM	14.79	14.96	3.41	0.69	12.64
Donegal Group Inc.	DGICA	12.52	334	83.66	85.12	NM	NM	NM	3.83	0.74	25.96
Min			334	64.67	66.44	8.13	8.82	7.59	0.00	0.35	12.64
Median			1,128	79.97	83.60	9.95	13.67	10.81	3.35	0.64	20.13
Average			1,130	91.18	105.67	11.18	13.55	12.55	2.96	0.96	23.62
Max			2,543	162.31	224.30	16.03	21.84	23.79	4.69	2.73	48.95
Harleysville Group Inc.	HGIC	32.18	874	111.68	115.13	18.39	0.00	NM	4.72	0.91	26.64

(1) Price / LTM Revenue is calculated by dividing market cap by LTM revenue.
(2) Price / Assets is calculated by dividing market cap by total assets.

"NM" = Not Meaningful

Note: Includes peers with total assets between $2 billion and $10 billion with similar business lines and geographic footprint as HGIC.
Pricing data is as of 9/27/11 close.
FWD multiples are based on what was reported as of 6/30/2011.

Based on Boenning's analysis, the median Price/Book value of HGIC's peers is 79.97% with a range of 64.67% to 162.31%. Based on this information, Boenning agrees with KBW's conclusion that the Transaction Price/Book multiple of 208% exceeds both the median and the maximum of the indicated range of the guideline companies.

Potentially, another adjustment to the guideline companies would be the application of a control premium because the Comparable Companies represent the value of a minority position. Based on Boenning's comparable transactions the expected control premium is approximately 35%. Applying these premiums to the values in the table above results in the following:

Table 51) HGIC Control Premium Analysis

Control Premium Analysis of HGIC				
	Control Premium[1]	Price / Book (%)	Price / Tang. Book (%)	Price / LTM EPS (x)
Min	35%	87.30	89.70	10.98
Median	35%	107.96	112.87	13.43
Max	35%	219.12	302.80	21.64
Harleysville Group Inc.[2]		208.3	222.5	34.3

(1) Based on median one day premium from M&A transaction comps
(2) Implied multiples based on the transaction value

The result is the transaction multiple remains above or within the range established by the median Guideline Company method.

KBW noted that the shares subject to its fairness opinion represented a minority and not control value. The fact that the use of a control premium does not change the conclusion of the analysis renders the debate meaningless in this context.

e. Transaction Approach

KBW selected nine transactions it deemed comparable to the subject transaction. Factors chosen in the selection included:

- Transactions announced since January 1, 2005
- Target company underwrites standard commercial and personal P/C risks
- Independent agency channel of distribution
- Transaction values $25 million to $5 billion
- Cash consideration

The results of KWB's analysis yielded a minimum Price/Book of 89% and a minimum P/LTM EPS of 8.9x. In addition, their analysis yielded a maximum Price/Book of 175% and maximum Price/LTM EPS of 14.4x. Unlike the comparable company approach, the Transaction Approach yields control value so application of a control premium is not required. KBW concluded that the Transaction book multiple of 208% was within or exceeded the range developed by the Transaction Approach.

f. Boenning Selection of Transactions

In order to test the reasonableness of KBW's Transaction Comps Analysis, Boenning selected potentially comparable transactions using the following criteria:

- Transactions announced since January 1, 2001
- Target company underwrites standard commercial and personal P/C risks
- Transaction values greater than $25 million
- Cash or stock consideration
- All of the transactions listed in KBW's analysis were included in Boenning's.

A summary of the 13 selected transactions and their key metrics are included in Table 52.

Table 52) HGIC Precedent Transaction Analysis

Precedent Transaction Analysis

Announce Date	Buyer	Target	Deal Value ($)	Price / Book Value (%)	Price / Tang. Book Value (%)	Price/ LTM EPS (x)	One Day Premium (%)
9/7/2011	ACE Limited	Penn Millers Holding Corporation	105	101.13	101.13	NM	25.77
4/15/2011	Auto Club Insurance Association	Fremont Michigan InsuraCorp, Inc.	68	131.36	131.36	26.78	35.14
11/30/2010	United Fire & Casualty Company	Mercer Insurance Group, Inc.	191	109.03	112.42	12.28	50.91
11/4/2010	Erie Insurance Exchange	Erie Indemnity Co. P&C subsidiaries	293	100.00	NA	NA	NA
7/15/2010	Donegal Group Inc.	Michigan Insurance Company	39	121.80	NA	15.63	NA
4/26/2010	National Interstate Corporation	Vanliner Group, Inc.	138	102.72	NA	11.04	NA
6/21/2009	Tower Group, Inc.	Specialty Underwriters' Alliance, Inc.	109	76.98	83.48	22.40	69.70
4/23/2008	Liberty Mutual Holding Company Inc.	Safeco Corporation	6,225	180.51	NA	9.79	50.90
5/6/2007	Liberty Mutual Holding Company Inc.	Ohio Casualty Corporation	2,744	165.10	175.30	11.92	32.05
10/31/2006	American European Group	Merchants Group, Inc.	71	91.79	91.79	11.38	8.55
8/4/2006	Delek Group Ltd.	Republic Companies Group, Inc.	289	175.11	175.11	14.68	34.03
4/29/2005	Mercer Insurance Group, Inc.	Financial Pacific Insurance Group, Inc.	41	115.42	NA	6.92	NA
3/28/2003	Nationwide Mutual Insurance Company	THI Holdings, Inc.	138	89.79	NA	NA	NA
Min			39.00	76.98	83.48	6.92	8.55
Median			137.95	109.03	112.42	12.10	34.59
Max			6,225.00	180.51	175.30	26.78	69.70
Average			803.94	120.06	124.37	14.28	38.38
		Harleysville Group Inc.[3]		208.26	222.52	34.29	

Note: (1) Includes transactions announced after 1/1/2001 involving target companies that underwrote similar business to HGIC. Only includes transactions where the the announced deal value was greater than $25 million, the Buyer was acquiring 100% of the business and GAAP P/Book Value multiples were publically disclosed
(2) All deal multiples are based off of GAAP financials
(3) Implied multiples based on the transaction value

Based on Boenning's Transaction Approach, Boenning agrees with KBW's conclusion that the transaction price meets/exceeds the range established by the Transaction Approach.

g. Income Approach

KBW performed a discounted dividend analysis ("***DDA***") to generate implied values for HGIC shares. KBW generated an implied range of $26.32 to $41.85 per share. Using management projections, Boenning constructed its own DDA. Boenning developed a cost of equity discount rate for its DDA analysis utilizing CAPM. The result of the analysis yielded a discount rate of 10%. The terminal multiple for the DDA was based on a 10.9x forward multiple with a 35% control premium (as stated earlier). Lastly, the annual cash dividend was based on a $1.48 total dividend in 2011, growing 5% each year. Boenning developed a DDA range by varying the discount rate and terminal multiple on earnings. The analysis summary in Table 53 highlights the range of $32.51 to $48.41 per share. Such a range would support a conclusion that the Transaction at $60.00 a share was fair to HGIC stockholders.

Table 53) HGIC DDA Analysis

Harleysville Group Discounted Dividend Analysis

	2010	2011	2012	2013	2014	2015
		Fiscal Year				
Fully Diluted Earnings Per Share[1]	$2.42	($0.01)	$2.29	$2.92	$3.59	$3.75
Earnings Per Share Year Over Year Growth		*NM %*	*NM %*	*27.5 %*	*22.9 %*	*4.5 %*
Assumed P/E Multiple Applied to Earnings[2]						13.5 x
Market Value Per Share						$50.67
Cash Dividends Per Share[3]		$1.48	$1.55	$1.63	$1.71	$1.80
Cash Dividends Paid		$1.48	$1.55	$1.63	$1.71	$1.80
Year Five Terminal Value						$50.67
Total Cash Flow to Shareholders'		$1.48	$1.55	$1.63	$1.71	$52.47
			Net Present Value of Cash Flows			**$38.72**

Net Present Value Sensitivity to Discount Rate and Terminal P/E Multiple:

Discount Rate%	*Multiple on Annual Earnings* 12.0 x	13.0 x	14.0 x	15.0 x	16.0 x
8.0%	$38.01	$40.61	$43.21	$45.81	**$48.41**
9.0%	36.53	39.01	41.50	43.99	46.48
10.0%	35.12	37.50	39.88	42.27	44.65
11.0%	33.78	36.06	38.35	40.63	42.91
12.0%	**$32.51**	34.70	36.88	39.07	41.26

Notes: (1) Based on Management Estimates (Diluted EPS) provided in Credit Suisse Presentation in Exhibit XIII
(2) Multiple on annual earnings uses a 25% control premium based Business Valution Discounts and Premiums by Shannon P. Pratt
(3) Cash dividends per share are based off of 2011actuals with a growth rate of 5% each year after

h. Conclusion Regarding the KBW Fairness Opinion

Based on our analysis and review of KBW's fairness opinion and presentation, as well as discussions with KBW, we believe KBW considered the appropriate factors, analysis and approaches and that its opinion and presentation reports were thorough and complete from a financial point of view. We believe the methodologies utilized and conclusion reached was reasonable from a financial point of view in light of the purposes for which they were intended (determining fairness to public stockholders of HGIC).