

SHEBOYGAN FALLS MUTUAL INSURANCE COMPANY  
RESOLUTIONS OF THE BOARD OF DIRECTORS

WHEREAS, Donegal Mutual Insurance Company, a mutual fire insurance company organized under the laws of the Commonwealth of Pennsylvania ("Donegal Mutual"), filed a Form A Statement with the Office of the Commissioner of Insurance of the State of Wisconsin ("OCI") on December 28, 2006 requesting OCI permission to acquire control of Sheboygan Falls Mutual Insurance Company, a mutual insurance company organized pursuant to Chapter 611 of the Wisconsin Statutes ("Sheboygan Falls Mutual"), and, on May 29, 2007, OCI approved Donegal Mutual's acquisition of control of Sheboygan Falls Mutual; and

WHEREAS, as part of Donegal Mutual's acquisition of control of Sheboygan Falls Mutual, Donegal Mutual entered into a Contribution Note Purchase Agreement pursuant to which Donegal Mutual purchased on June 7, 2007 the contribution note (the "Contribution Note") of Sheboygan Falls Mutual in the principal amount of \$3,500,000; and

WHEREAS, designees of Donegal Mutual, all of whom are directors of Donegal Mutual, were appointed as six of the ten members of the board of directors (the "Board") of Sheboygan Falls Mutual; and

WHEREAS, Donegal Mutual entered into a Services Agreement with Sheboygan Falls Mutual, a Technology Agreement with Sheboygan Falls Mutual and a Retrocessional Reinsurance Agreement with Sheboygan Falls Mutual; and

WHEREAS, the services provided by Donegal Mutual to Sheboygan Falls Mutual pursuant to the Services Agreement will enable Sheboygan Falls Mutual to reduce its expense ratio over time and will provide Sheboygan Falls Mutual with the economies of scale of a much larger property and casualty insurance company; and

WHEREAS, the Technology Agreement makes available to Sheboygan Falls Mutual certain information systems and applications licensed to or developed by Donegal Mutual, including systems that provide automated underwriting and policy issuance and enhanced policyholder services that are essential today for a property and casualty insurance company to be competitive and that a smaller insurer, such as Sheboygan Falls Mutual, simply cannot afford; and

WHEREAS, although the Retrocessional Reinsurance Agreement with Sheboygan Falls Mutual does not transfer risk for statutory accounting purposes, it does have the important benefit of allowing Sheboygan Falls Mutual to be a part of Donegal Mutual's group A.M. Best rating of A (Excellent) and the importance of an A.M. Best rating of A

(Excellent) to a small insurance company such as Sheboygan Falls Mutual cannot be overestimated; and

WHEREAS, Sheboygan Falls Mutual entered into its affiliation with Donegal Mutual because the Board had the foresight to recognize Sheboygan Falls Mutual's need to develop additional sources of surplus in order to remain competitive, obtain the advantages of technology in order to reduce its expense ratio, have the capacity to expand its business and to assure its long-term viability; and

WHEREAS, when Donegal Mutual addressed similar concerns in the mid-1980s, Donegal Mutual, like a number of other mutual property and casualty insurance companies at that time, determined to implement a downstream holding company structure which resulted in the formation of Donegal Group Inc., an insurance holding company organized under the laws of the State of Delaware, 66% of whose voting power is held by Donegal Mutual ("DGI"); and

WHEREAS, since 1986, DGI has raised \$95.0 million dollars of public capital and had total assets of \$834.1 million and stockholders' equity of \$352.7 million as of December 31, 2007, and Donegal Mutual has thereby assured its future viability; and

WHEREAS, the Form A Statement Donegal Mutual filed with OCI on December 28, 2006 seeking OCI approval to acquire control of Sheboygan Falls Mutual explicitly stated that Donegal Mutual had the intention of seeking to convert Sheboygan Falls Mutual to a stock insurance corporation at an unspecified future time, and that it was Donegal Mutual's expectation that Sheboygan Falls Mutual would become more profitable, expand its operations in Wisconsin and serve as a major component of the presence of Donegal Mutual and DGI (collectively, "Donegal Insurance Group") in Wisconsin; and

WHEREAS, if Donegal Mutual were unable to proceed with the conversion of Sheboygan Falls Mutual first disclosed in 2006, it is likely that Donegal Mutual would not provide Sheboygan Falls Mutual with additional capital through the purchase of additional contribution notes because of the inherent economic disadvantages of holding contribution notes, which in turn would make it more likely than not that Donegal Mutual would have to consider the exercise of its rights to terminate the Services Agreement, the Technology Agreement and the Retrocessional Reinsurance Agreement in accordance with the terms of those agreements; and

WHEREAS, Sheboygan Falls Mutual's loss of its affiliation with Donegal Mutual could reasonably be expected to have significant adverse consequences for the financial health of, and future prospects for, Sheboygan Falls Mutual; and

WHEREAS, in order to avoid the adverse consequences of a loss of Sheboygan Falls Mutual's affiliation with Donegal Mutual and to preserve the benefits of such an affiliation,

as described above, the Board has considered a proposed demutualization (the "Demutualization") of Sheboygan Falls Mutual, whereby Sheboygan Falls Mutual would convert from a mutual insurance company owned by its policyholders to a stock insurance corporation all of whose capital stock would be acquired by DGI (the "Acquisition"); and

WHEREAS, the policyholders of Sheboygan Falls Mutual would directly benefit from the Demutualization and the Acquisition as well as the continuing affiliation with Donegal Insurance Group through access to additional surplus, greater access to public capital markets, higher levels of technology and economies of scale while local management, underwriting and claims adjustment processes remain in Sheboygan Falls, Wisconsin; and

WHEREAS, the Board, to avoid any appearance of a conflict of interest, appointed a Demutualization Committee, all of whose members are independent of Donegal Mutual and DGI; and

WHEREAS, Sheboygan Falls Mutual has retained Foley & Lardner LLP as its independent legal counsel in connection with the transactions contemplated by the Demutualization and the Acquisition; and

WHEREAS, the Demutualization Committee has retained Parrett & O'Connell, LLP as its independent legal counsel in connection with the transactions contemplated by the Demutualization and the Acquisition; and

WHEREAS, the Board believes the Demutualization is in the best interests of Sheboygan Falls Mutual and its policyholders; now, therefore, the Board hereby adopts the following resolutions:

RESOLVED, that the Board deems it advisable that the management of Sheboygan Falls Mutual develop and prepare a plan of conversion (the "Plan of Conversion") for submission to and consideration by the Board, the voting policyholders of Sheboygan Falls Mutual and OCI, whereby, in accordance with Section 4m of Chapter 611.76 of the Wisconsin Statutes, each policyholder of Sheboygan Falls Mutual during the five years preceding the date of adoption of these resolutions shall receive a cash payment equal to such policyholder's proportionate share of the value of Sheboygan Falls Mutual after payment of all of the expenses of the Demutualization, which value shall be exclusively determined by an appraisal committee to be appointed by OCI in accordance with Section 3(c) of Chapter 611.76 of the Wisconsin Statutes and whereby DGI shall, pursuant to a Note Purchase and Investment Agreement, make a capital contribution to the converted company, so that the converted company shall have surplus as of the effective date of the conversion of no less than \$10,500,000 which may include the Contribution Note, unless the conversion of the Contribution Note into equity is approved by OCI no later than simultaneously with DGI's approval of the Demutualization;

FURTHER RESOLVED, that the Board has unanimously determined, after receiving the unanimous recommendation of its Demutualization Committee, that the Demutualization is in the best interests of the policyholders of Sheboygan Falls Mutual, in light of the fact that such policyholders will receive cash consideration in an amount determined by an independent expert appraisal committee appointed by OCI to be equal to the value of their equitable shares in Sheboygan Falls Mutual, which are otherwise illiquid, while at the same time, as policyholders of Sheboygan Falls Mutual, they will be insured by a much stronger company that maintains higher levels of technology, has access to public sources of capital and can achieve a significantly lower expense ratio, all of which will give Sheboygan Falls Mutual a more assured future; and

FURTHER RESOLVED, that the Board has reviewed the financial advisor proposals of Keefe Bruyette & Woods, Inc., Fox-Pitt Cochran Caronia Waller (USA) LLC and Stoneridge Advisors, LLC, as well as the recommendation of the Demutualization Committee that the financial advisor with the most competitively priced proposal that meets the approval of OCI be selected, the Board hereby recommends to OCI that OCI retain Stoneridge Advisors, LLC on substantially the same terms set forth in Stoneridge Advisors, LLC's March 31, 2008 proposal and that Sheboygan Falls Mutual be responsible directly for the payment of the fees and expenses of Stoneridge Advisors, LLC as well as the fees and expenses of the members of the Appraisal Committee; and

FURTHER RESOLVED, that the Board hereby authorizes the indemnification and holding harmless of the members of the Appraisal Committee against any threatened or actual claim, action, suit, proceeding or investigation, whether civil, criminal or investigative in which such member is or is threatened to be made a party based in whole or in part out of, or pertaining to the conversion to (i) the fact that member is or was a member of the Appraisal Committee or (ii) the Plan of Conversion or any transaction contemplated thereby; and

FURTHER RESOLVED, that the Board deems it advisable that the management of Sheboygan Falls Mutual prepare all documentation required in connection with the Plan of Conversion including: (i) proposed Articles of Incorporation and Bylaws of Sheboygan Falls Mutual as a Wisconsin-domiciled stock insurance corporation, (ii) an Information Statement to be mailed to the voting policyholders of Sheboygan Falls Mutual describing the Demutualization proposal and notifying the voting policyholders of the calling of a special meeting of such policyholders to consider and vote upon the Plan of Conversion and transactions that are a part of the Demutualization and (iii) all other documents deemed necessary in furtherance of the Demutualization.