

DONEGAL GROUP INC
Form 11-K
June 18, 2015
Table of Contents

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

FORM 11-K

x **ANNUAL REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2014

.. **TRANSITION REPORT PURSUANT TO SECTION 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission file no.: 333-93785

A. Full title of the plan and the address of the plan, if different from that of the issuer named below:
Donegal Mutual Insurance Company 401(k) Plan

1195 River Road

Marietta, Pennsylvania 17547

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

Donegal Group Inc.

1195 River Road

Marietta, Pennsylvania 17547

Table of Contents

**DONEGAL MUTUAL INSURANCE
COMPANY 401(k) PLAN
FINANCIAL STATEMENTS WITH
SUPPLEMENTAL SCHEDULE
YEARS ENDED DECEMBER 31, 2014 AND 2013
AND
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

TABLE OF CONTENTS

	Page
<u>Report of Independent Registered Public Accounting Firm</u>	1
Financial Statements	
<u>Statements of Net Assets Available for Benefits</u>	2
<u>Statements of Changes in Net Assets Available for Benefits</u>	3
<u>Notes to Financial Statements</u>	4
Supplemental Schedule	
<u>Schedule H - Part IV Line 4i Schedule of Assets (Held at End of Year)</u>	15
<u>Signatures</u>	16
Exhibit 23.1	18

Table of Contents

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Plan Administrator

Donegal Mutual Insurance Company 401(k) Plan

We have audited the accompanying statements of net assets available for benefits of the Donegal Mutual Insurance Company 401(k) Plan (the Plan) as of December 31, 2014 and 2013, and the related statements of changes in net assets available for benefits for the years then ended. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Plan is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Plan's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the net assets available for benefits of the Plan as of December 31, 2014 and 2013, and the changes in net assets available for benefits for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The accompanying supplemental schedule of Schedule H, Part IV, Line 4i Schedule of Assets (Held at End of Year) as of December 31, 2014 has been subjected to audit procedures performed in conjunction with the audit of the Plan's financial statements. The supplemental schedule is the responsibility of the Plan's management. Our audit procedures included determining whether the supplemental schedule reconciles to the financial statements or the underlying accounting and other records, as applicable, and performing procedures to test the completeness and accuracy of the information presented in the supplemental schedule. In forming our opinion on the supplemental schedule, we evaluated whether the supplemental schedule, including its form and content, is presented in conformity with the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. In our opinion, the supplemental schedule is fairly stated, in all material respects, in relation to the financial statements as a whole.

/s/ BDO USA, LLP

Philadelphia, Pennsylvania

June 18, 2015

Table of Contents**DONEGAL MUTUAL INSURANCE COMPANY****401(k) PLAN**

STATEMENTS OF NET ASSETS AVAILABLE FOR BENEFITS

DECEMBER 31, 2014 AND 2013

	2014	2013
Assets		
Investments, at fair value:		
Interest-bearing cash	\$ 5,814,533	\$ 5,753,107
Common/collective trust funds	7,693,231	6,575,486
Registered investment companies	61,342,067	56,634,319
Employer securities	7,930,286	7,123,896
Net Assets Available for Benefits	82,780,117	76,086,808

The accompanying notes are an integral part of these financial statements.

Table of Contents**DONEGAL MUTUAL INSURANCE COMPANY****401(k) PLAN**

STATEMENTS OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

YEARS ENDED DECEMBER 31, 2014 AND 2013

	2014	2013
Investment Income:		
Interest	\$ 7,602	\$ 7,479
Dividends	5,129,753	3,244,838
Net (depreciation) appreciation in fair value of investments	(901,097)	10,293,967
	4,236,258	13,546,284
Contributions:		
Employer	2,203,142	2,008,105
Participants	3,695,637	3,353,140
Rollover	324,134	1,445,514
	6,222,913	6,806,759
Total Additions	10,459,171	20,353,043
Benefits Paid to Participants	(3,765,862)	(5,347,199)
Net Increase	6,693,309	15,005,844
Net Assets Available for Benefits - Beginning of Year	76,086,808	61,080,964
End of Year	\$ 82,780,117	\$ 76,086,808

The accompanying notes are an integral part of these financial statements.

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

1. DESCRIPTION OF PLAN

The following description of the Donegal Mutual Insurance Company 401(k) Plan (the Plan) provides only general information. Participants should refer to the Plan Document for a more complete description of the Plan s provisions.

General

The Plan is a defined contribution 401(k) plan, which became effective January 1, 1998. All employees of Donegal Mutual Insurance Company (the Company) are eligible to participate as of the first day of the month after the month in which their employment with the Company commences. The Plan is subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA).

Contributions

Participants may contribute between 1% and 100% of their annual compensation up to the maximum limit established by the Internal Revenue Code (IRC). Contributions made to each participant s account will be invested, based on the individual s direction, in various investment options. The Company will contribute, on behalf of each participant, a sum equal to 100% of the first 3% of participant deferrals and 50% of the next 6%. Participants may also contribute qualified rollover balances from their prior plans.

Newly hired employees are automatically enrolled into the Plan at 3% of eligible compensation. Employee deferrals will automatically be increased by 1% at the beginning of each successive year until the deferred percentage reaches 6%. Employees not selecting an investment option for their deferrals have their contributions invested in the Putnam Dynamic Asset Allocation Conservative Fund. Employees have the option to opt out of participation or change their elective deferral at any time following their eligibility date.

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

1. DESCRIPTION OF PLAN (Cont d)

Participant Accounts

Each participant's account is credited with the participant's contribution and an allocation of the following in accordance with Plan provisions: (a) the Company's contribution and (b) Plan earnings. Allocations are based on participant earnings, deferrals or account balances, as defined. The benefit to which a participant is entitled is the benefit that can be provided from the participant's vested account.

Participant Loans

The Plan does not currently allow participant loans.

Vesting

Participants are immediately vested in their salary deferral, rollover contributions, and all amounts that transferred into the Plan from certain predecessor company-sponsored defined contribution plans and earnings thereon. Vesting of Company contributions and earnings thereon is based on years of service. A participant is 100% vested after 2 years of credited service.

Payment of Benefits

The normal retirement date is the first of the month following attainment of age 65. Early retirement is possible at age 55. Benefits are paid in the form of a lump-sum distribution. Upon termination of service for other reasons, participants will receive a lump-sum distribution if the total of their vested balance does not exceed \$1,000. If the vested balance exceeds \$1,000, but is less than \$5,000, the participant may elect to receive a lump-sum distribution, however, if no election is made, the Plan Committee will pay the distribution in a direct rollover to an individual retirement account designated by the Plan Committee. If the vested balance exceeds \$5,000, the assets will generally be held in the Plan until the participant's normal or early retirement date. However, participants are entitled to receive the entire balance in their employee account and employer account (if vested) as a lump-sum distribution, as soon as administratively possible. There is a provision available to allow hardship withdrawals of benefits prior to termination of employment as defined in the Plan and in compliance with the IRC.

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

1. DESCRIPTION OF PLAN (Cont d)

Forfeitures

Forfeitures arising from distributions to participants who are less than 100% vested will be used to restore any accounts of participants reemployed during the Plan year or to reduce Company contributions per guidelines established by the Plan. Forfeitures used to reduce Company contributions totaled \$41,607 in 2014 and \$31,684 in 2013. As of December 31, 2014 and 2013, there were \$29,899 and \$41,607 of unallocated forfeitures, respectively.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The financial statements are prepared under the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of changes in net assets available for benefits during the reporting period. The most significant estimate is the determination of the fair values of the Plan s investments. Actual results could differ from those estimates.

Investment Valuation and Income Recognition

Investments are valued at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. See Note 3 for a discussion of fair value measurements.

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont d)

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date. Net (depreciation) appreciation includes the Plan's realized gains and losses on investments bought and sold as well as net unrealized gains and losses on those held during the year.

Net investment returns reflect certain fees paid by the investment funds to their affiliated investment advisors, transfer agents, and others as further described in each fund prospectus or other published documents. These fees are deducted by the investment funds prior to allocation of the Plan's investment earnings activity and thus are not separately identifiable as an expense.

Payment of Benefits

Benefits are recorded when paid.

Subsequent Events

The Company and Plan have evaluated subsequent events for potential recognition and/or disclosure through the date these financial statements were issued.

3. FAIR VALUE MEASUREMENTS

The Plan accounts for financial assets and liabilities using a framework that establishes a hierarchy that ranks the quality of inputs, or assumptions, used in the determination of fair value, and the Plan classifies financial assets and liabilities carried at fair value in one of the following three categories of inputs:

Level 1 quoted prices in active markets for identical assets and liabilities;

Level 2 directly or indirectly observable inputs other than Level 1 quoted prices; and

Level 3 unobservable inputs not corroborated by market data.

The fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

Following is a description of the valuation methodologies used for investments measured at fair value. There have been no significant changes in the methodologies used or transfers between levels during the years ended December 31, 2014 or 2013.

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

3. FAIR VALUE MEASUREMENTS (Cont d)

The Plan values employer securities and registered investment companies based on the closing price reported on the active market on which the individual securities/funds are traded and classified as level 1. Interest bearing cash carrying value is deemed to be fair value and classified as level 1. The Plan values its common/collective trust funds based on the underlying market values provided by the Plan trustee. Further information concerning the common/collective trust funds may be obtained from their separate audited financial statements. The Plan classifies common/collective trust funds as Level 2. The Plan had no investments classified as Level 3 during the years ended December 31, 2014 and 2013.

The Plan invests in three common/collective trust funds, the Putnam Bond Index Fund, the Wells Fargo Stable Value Fund M Shares and the Putnam S&P 500 Index Fund. The common/collective trust funds are valued based upon significant observable inputs, not based upon quoted market prices in an active market. The value is based upon the units of the collective trust fund held by the Plan at year end multiplied by the respective unit value. The unit value is based on the fair value of the underlying investments. The Putnam Bond Index Fund's investment objective is to achieve a return, before the assessment of fees, that closely approximates the return of the Barclay's Aggregate Bond index, a common measure of U. S. investment-grade bond market performance. To achieve its investment objective, the Putnam Bond Index Fund invests a significant portion of its assets in securitized debt instruments, including mortgage-backed and asset backed investments. The Wells Fargo Stable Value Fund M Shares' investment objective is to seek safety of principal and consistency of returns while attempting to maintain minimal volatility. To achieve its investment objective, the Wells Fargo Stable Value Fund M Shares is primarily comprised of investment contracts including Guaranteed Investment Contracts (GICs), Separate Account GICs, and Security Backed Investment Contracts. GICs are issued by insurance companies which guarantee the return of principal and a stated rate of interest. The unit value is reported at contract value given the adjustment to fair value is not material. The Putnam S&P 500 Index Fund's investment objective is to achieve a return, before the assessment of fees, that closely approximates the return of the Standard & Poor's 500 Composite Stock Price Index, a common measure of U.S. market performance. To achieve its investment objective, the Putnam S&P 500 Index Fund invests primarily in the securities that constitute the Standard & Poor's 500 Composite Stock Price Index either directly or through the purchase of shared or collective investment trusts having investment objectives similar to that of the Putnam S&P 500 Index Fund. For liquidity and hedging purposes, the Putnam S&P 500 Index Fund may invest in high-quality, money market instruments and in money market funds that invest exclusively in high-quality money market instruments. The Putnam S&P 500 Index Fund also uses stock index futures contracts in order to

Table of Contents**DONEGAL MUTUAL INSURANCE COMPANY****401(k) PLAN**

NOTES TO FINANCIAL STATEMENTS

4. INVESTMENTS

The following table presents the fair values of investments that represent 5% or more of the Plan's net assets available for benefits as of December 31:

	2014	2013
Interest-bearing cash:		
Putnam Money Market Fund	\$ 5,814,533	\$ 5,753,107
Common/collective trust:		
Putnam S&P 500 Index Fund	6,167,303	5,291,354
Registered investment companies:		
PIMCO Total Return Fund	4,029,228*	4,088,716
Putnam Dynamic Asset Allocation Growth Fund	5,893,250	4,953,176
Putnam Dynamic Asset Allocation Balanced Fund	8,790,252	7,491,687
Putnam Dynamic Asset Allocation Conservative Fund	5,175,345	3,836,020
Putnam International Equity Fund	3,744,287*	4,286,295
Putnam Equity Income Fund	5,731,261	5,053,897
Artisan Mid Cap Value Fund Investor Class	4,212,363	3,961,419
Neuberger & Berman Genesis Trust	3,702,153*	4,240,710
Employer securities:		
Donegal Group Inc. Class A Common Stock	6,769,918	5,849,055

* Investment did not represent 5% or more of the Plan's net assets available for benefits, rather this investment is shown for comparative purposes.

During 2014 and 2013, the Plan's investments (including gains and losses on investments bought, sold and held during the year) (depreciated) appreciated in value as follows:

	2014	2013
At fair value as determined by quoted market prices:		
Registered investment companies	\$ (1,612,700)	\$ 8,074,161
Employer securities	(56,215)	997,965
Otherwise determined:		
Common/collective trust funds	767,818	1,221,841
	\$ (901,097)	10,293,967

5. TAX STATUS

The Internal Revenue Service has determined and informed the Company by letters dated September 28, 2009 and May 11, 2015 that the Plan is designed in accordance with applicable sections of the IRC. U.S. GAAP requires Plan management to evaluate tax

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

5. TAX STATUS (Cont d)

positions taken by the Plan and recognize a tax liability if the organization has taken an uncertain position that more likely than not would not be sustained upon examination by the Internal Revenue Service. The Plan administrator has analyzed the tax positions taken by the Plan and has concluded that as of December 31, 2014, there are no uncertain positions taken, or expected to be taken, that would require recognition of a liability or disclosure in the financial statements. The Plan is subject to routine audits by taxing jurisdictions. The Plan administrator believes it is no longer subject to income tax examinations for years prior to 2011.

6. RELATED PARTY AND PARTY-IN-INTEREST TRANSACTIONS

Donegal Group Inc. is a regional insurance holding company that was formed by the Company in 1986. The Plan held 423,649 shares of Class A and 53,971 shares of Class B Donegal Group Inc. common stock with fair values of \$6,769,918 and \$1,160,368, respectively, as of December 31, 2014. The Plan held 367,865 shares of Class A and 53,905 shares of Class B Donegal Group Inc. common stock with fair values of \$5,849,055 and \$1,274,841, respectively, as of December 31, 2013. The net realized/unrealized (depreciation) appreciation in fair value of Donegal Group Inc. common stock (including Class A and Class B) during 2014 and 2013 was (\$56,215) and \$997,965, respectively. Dividends received from Donegal Group Inc. in 2014 and 2013 were \$227,348 and \$194,474, respectively. During 2014, the Plan purchased (excluding reinvested dividends) 45,456 shares of Donegal Group Inc. Class A common stock at an aggregate cost of \$704,862 and sold 5,101 shares of Donegal Group Inc. Class A common stock for total proceeds of \$78,099. During 2013, the Plan purchased (excluding reinvested dividends) 56,875 shares of Donegal Group Inc. Class A common stock at an aggregate cost of \$807,124 and sold 16,170 shares of Donegal Group Inc. Class A common stock for total proceeds of \$255,493. As of December 31, 2014 and 2013, the Class A shares of Donegal Group Inc. common stock represent more than 5% of net assets available for benefits.

7. ADMINISTRATION OF PLAN ASSETS

The Plan's assets are administered under a contract with Mercer Trust Company (Mercer), the custodian and trustee of the Plan since June 1, 2011. Mercer invests funds received from contributions, investment sales, interest, and dividend income and makes distribution payments to participants. Certain administrative functions are performed by officers or employees of the Plan's sponsor. No such officer or employee receives

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

NOTES TO FINANCIAL STATEMENTS

7. ADMINISTRATION OF PLAN ASSETS (Cont d)

compensation from the Plan. Certain administrative expenses of maintaining the Plan were paid by the Company in 2014 and 2013 and are excluded from these financial statements. Investment related expenses are included in net (depreciation) appreciation of fair value of investments.

8. PLAN TERMINATION

Although it has not expressed an intention to do so, the Company has the right under the Plan to discontinue its contributions at any time and to terminate the Plan subject to the provisions of ERISA. In the event of Plan termination, participants will become 100% vested in their accounts.

9. RISKS AND UNCERTAINTIES

The Plan invests in various investment securities. Investment securities are exposed to various risks, such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statements of net assets available for benefits.

Table of Contents

SUPPLEMENTAL SCHEDULE

Table of Contents

Schedule H - Financial Information (Form 5500)

Part IV - Line 4i - Schedule of Assets (Held at End of Year)

Name of Plan Sponsor: Donegal Mutual Insurance Company

Name of Plan: Donegal Mutual Insurance Company 401(k) Plan

Employer Identification Number: 23-1336198

Three-digit Plan Number: 003

December 31, 2014

(a)	(b)	(c)	(d)	(e)
	Identity of issue, borrower, lessor, or similar party	Description of investment including maturity date, rate of interest, collateral, par, or maturity value	Cost	Current Value
	Putnam Money Market Fund	5,814,533 Shares of Money Market Fund	**	\$ 5,814,533
	Total interest-bearing cash			5,814,533
	Putnam Bond Index Fund	53,870 Common/Collective Trust Units	**	1,155,739
	Wells Fargo Stable Value Fund M Shares	7,682 Common/Collective Trust Units	**	370,189
	Putnam S&P 500 Index Fund	97,430 Common/Collective Trust Units	**	6,167,303
	Total common/collective trust funds			7,693,231
	Oakmark Equity & Income Fund	85,165 Registered Investment Companies	**	2,717,623
	MSIF Small Company Growth Fund	177,672 Registered Investment Companies	**	2,647,306
	PIMCO Total Return Fund	377,976 Registered Investment Companies	**	4,029,228
	Columbia Contrarian Core Fund Class R4	138,977 Registered Investment Companies	**	3,053,324
	American Funds New Perspective Fund R4 Class	32,781 Registered Investment Companies	**	1,175,511
	T. Rowe Price Small Cap Stock ADV	41,940 Registered Investment Companies	**	1,842,415
	American Funds Growth Fund of America	64,834 Registered Investment Companies	**	2,747,032
	Putnam Dynamic Asset Allocation Growth Fund	373,700 Registered Investment Companies	**	5,893,250

Putnam Dynamic Asset Allocation Balanced Fund	607,901	Registered Investment Companies	**	8,790,252
Putnam Dynamic Asset Allocation Conservative Fund	482,775	Registered Investment Companies	**	5,175,345
Putnam International Equity Fund	165,970	Registered Investment Companies	**	3,744,287
Putnam Equity Income Fund	272,398	Registered Investment Companies	**	5,731,261
Alger Capital Appreciation Fund Class A	167,060	Registered Investment Companies	**	3,429,747
Putnam Diversified Income Trust	74,879	Registered Investment Companies	**	569,827
Baron Asset Fund	29,508	Registered Investment Companies	**	1,881,143
Artisan Mid Cap Value Fund Investor Class	170,956	Registered Investment Companies	**	4,212,363
Neuberger & Berman Genesis Trust	62,494	Registered Investment Companies	**	3,702,153
Total registered investment companies				61,342,067
* Donegal Group Inc.	423,649	Shares of Class A Common Stock	**	6,769,918
* Donegal Group Inc.	53,971	Shares of Class B Common Stock	**	1,160,368
Total employer securities				7,930,286
Total assets				\$ 82,780,117

* Party-in-interest

** Historical cost information is not required to be disclosed for participant-directed investments.

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

SIGNATURES

The Plan. Pursuant to the requirements of the Securities Exchange Act of 1934, the trustees (or other persons who administer the employee benefit plan) have duly caused this annual report to be signed on its behalf by the undersigned hereunto duly authorized.

DONEGAL MUTUAL INSURANCE COMPANY
401(k) PLAN

Date: June 18, 2015

By: /s/ Donald H. Nikolaus
Donald H. Nikolaus, Trustee

By: /s/ Jeffrey D. Miller
Jeffrey D. Miller, Trustee

By: /s/ Daniel J. Wagner
Daniel J. Wagner, Trustee

Table of Contents

DONEGAL MUTUAL INSURANCE COMPANY

401(k) PLAN

EXHIBIT INDEX

Exhibit Number	Description
23.1	Consent of BDO USA, LLP (filed herewith)