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CONTRIBUTION NOTE

\$3,500,000

Sheboygan Falls, Wisconsin  
\_\_\_\_\_, 2007

FOR VALUE RECEIVED, SHEBOYGAN FALLS MUTUAL INSURANCE COMPANY, a Wisconsin mutual fire and casualty insurance company with its principal office at 511 Water Street, Sheboygan Falls, Wisconsin 53085 ("Sheboygan Falls"), in consideration of a Three Million Five Hundred Thousand Dollar (\$3,500,000) contribution loan received by Sheboygan Falls on the date hereof from DONEGAL MUTUAL INSURANCE COMPANY, a Pennsylvania mutual fire insurance company with its principal office at 1195 River Road, Marietta, Pennsylvania 17547 ("Donegal Mutual"), hereby promises and agrees to pay to the order of Donegal Mutual the principal amount of Three Million Five Hundred Thousand Dollars (\$3,500,000) in accordance with the terms and conditions of this Contribution Note, plus interest thereon at the rate specified in Section 2 hereof from the date hereof until paid.

This Contribution Note is issued under and pursuant to the terms and provisions of a Contribution Note Purchase Agreement dated as of December 27, 2006, entered into by Sheboygan Falls and Donegal Mutual (the "Note Purchase Agreement") and this Contribution Note and the holder hereof is entitled to all the benefits provided for thereby or referred to therein. Unless otherwise defined in this Contribution Note, terms used herein shall have the meanings attributed to them in the Note Purchase Agreement, subject to prior compliance with the provisions of Section 3 of this Contribution Note.

In the event of a conflict between the terms of this Contribution Note and the terms of the Note Purchase Agreement, the terms of the Note Purchase Agreement shall be subordinate to and controlled by the terms of this Contribution Note.

This Contribution Note is subject to mandatory and voluntary prepayment and may be declared due prior to its expressed maturity dates, all in the events, on the terms and in the manner and amounts as provided in the Note Purchase Agreement.

1. Payment of Principal Amount.

(a) Subject to prior compliance with the provisions of Section 3, the principal amount outstanding hereunder shall be payable by Sheboygan Falls to Donegal Mutual in one payment that shall be due on the earlier of (i) December 31, 2010, or (ii) the date on which

the designees of Donegal Mutual cease to constitute a majority of the members of the Board of Directors of Sheboygan Falls (the "Board").

(b) Subject to prior compliance with the provisions of Section 3, Sheboygan Falls shall have the right to prepay all or any part of this Contribution Note from time to time without premium or penalty by paying to Donegal Mutual the principal amount being prepaid together with all accrued but unpaid interest thereon to the date of prepayment.

(c) Any payment made shall first apply to accrued interest, and the balance of such payment shall apply to reduce the principal of this Contribution Note.

2. Interest. Interest shall accrue on the outstanding principal amount hereunder at an annual rate equal to the lesser of: (i) the Prime Rate minus .5% (fifty basis points) but not less than 5.5% nor greater than 8.0% or (ii) the maximum rate permitted pursuant to Wisconsin law. For purposes of this Contribution Note, "Prime Rate" shall equal the prime rate as reported in The Wall Street Journal (i.e., the base rate on corporate loans posted by at least 75% of the U.S.'s 30 largest banks, which was \_\_\_\_% as of \_\_\_\_\_, 2007). Interest payable hereunder shall be payable in arrears on the last day of each calendar quarter during which any portion of the principal amount hereof is outstanding commencing on \_\_\_\_\_, 2007. The inability or failure of Sheboygan Falls to pay interest as specified herein on this Contribution Note shall not relieve Sheboygan Falls of the obligation to pay such interest; but such unpaid interest, if any, shall cumulate and bear interest at the rate specified herein and be payable in accordance with the terms and conditions of this Contribution Note.

3. Conditions of Payment. Notwithstanding the foregoing:

(a) Sheboygan Falls shall not repay, discharge or retire this Contribution Note nor pay any principal or accrued interest arising under this Contribution Note or the Note Purchase Agreement (together, "Payment Obligations") unless it shall have given the Office of the Wisconsin Commissioner of Insurance ("OCI") at least 60 days' prior written notification of the proposed payment, repayment, discharge or retirement and said Commissioner has indicated his or her prior written approval of said payment. The Commissioner has complete discretion to approve or refuse to approve a payment, repayment, discharge or retirement. The Commissioner may consider any factors in making his or her determination including, but not limited to, the compliance of Sheboygan Falls with compulsory and security surplus requirements.

(b) Payment Obligations, if any, which are not paid when due because of the provisions of paragraph (a) above, shall become general obligations of Sheboygan Falls but subject to the subordination provided by paragraph (c) below, except that any payment of such unpaid Payment Obligations thereafter shall be made only in accordance with all the terms and conditions of this Contribution Note.

(c) The rights of the holder hereof to payment of any Payment Obligations are and shall remain subject and subordinate to the claims of all policyholders and of all contract creditors and all other obligations of Sheboygan Falls, and, in the event of any insolvency proceedings, dissolution or liquidation of Sheboygan Falls, no Payment Obligations shall be due or payable upon this Contribution Note until the just claims of all claimants under policies of insurance issued by Sheboygan Falls and all contract creditors of Sheboygan Falls have been paid in full. Sheboygan Falls may establish an appropriate reserve account, out of its surplus, to provide for the orderly payment of this Contribution Note, but any such reserve account shall be subject to this provision for subordination. In the event of any such proceeding, liquidation or winding-up, after payment in full of all sums owing with respect to the Payment Obligations, Donegal Mutual shall be entitled to be paid from the remaining assets of Sheboygan Falls the unpaid principal amount of this Contribution Note and interest accrued and unpaid hereon. The foregoing subordination provisions of this Contribution Note are solely for the purpose of defining the relative rights of the holders of the Payment Obligations and Donegal Mutual, and none of such provisions shall impair, as between Sheboygan Falls and Donegal Mutual, the obligation of Sheboygan Falls to pay Donegal Mutual the principal hereof and the interest hereon and any other sums payable hereunder in accordance with the terms hereof, nor shall such subordination provisions prevent Donegal Mutual from exercising all remedies otherwise permitted under the terms hereof upon an Event of Default hereunder, subject to the rights, if any, of the holders of the Payment Obligations to be paid in full before any payment shall be made on account of this Contribution Note.

(d) No modification of this Contribution Note is effective and no other agreement may modify or supersede the terms of this Contribution Note, whether existing on the date of this Contribution Note or subsequently entered into, unless the modification or agreement is approved in writing by the Commissioner.

(e) Nothing in the foregoing shall be deemed to have the effect of subordinating the claims of the holder of this Contribution Note to the claims of the holders of any other surplus note issued by Sheboygan Falls or to the proprietary claims of the equity owners of Sheboygan Falls.

(f) No recourse under or upon any obligation, covenant or agreement contained in this Contribution Note or the Note Purchase Agreement, or for any claim based thereon or otherwise in respect thereof, shall be had against any shareholder, officer or director, as such, past, present or future, of Sheboygan Falls or of any successor corporation, either directly or through any trustee, receiver or any other person; it being expressly understood that this Contribution Note is solely a corporate obligation of Sheboygan Falls, and that any and all personal liability, and any and all rights and claims against every such shareholder, officer or director, as such, are hereby expressly waived and released by every

holder hereof by the acceptance of this Contribution Note and as a part of the consideration for the issuance hereof.

(g) The obligations of Sheboygan Falls under this Contribution Note or the Note Purchase Agreement may not be offset or be subject to recoupment with respect to any liability or obligation owed to Sheboygan Falls. No security agreement or interest, whether existing on the date of this Contribution Note or subsequently entered into, applies to the obligation under this Contribution Note or the Note Purchase Agreement.

4. Place of Payment. All amounts payable by Sheboygan Falls to Donegal Mutual hereunder shall be paid in lawful money of the United States of America directly to Donegal Mutual at Donegal Mutual's address set forth above or at such other address of which Donegal Mutual shall give written notice to Sheboygan Falls.

5. Event of Default. An event of default hereunder (an "Event of Default") shall exist if:

(a) Sheboygan Falls fails to pay any amount of principal of, or accrued interest on, this Contribution Note in full when due hereunder if Sheboygan Falls has obtained the approval of the Commissioner for such payment;

(b) Sheboygan Falls shall be adjudicated as bankrupt or insolvent, or admit in writing its inability to pay its debts as they mature, or Sheboygan Falls shall apply for or consent to the appointment of any receiver, trustee, liquidator or similar officer for it or for all or any substantial part of its property, or such receiver, trustee, liquidator or similar officer shall be appointed without the application or consent of Sheboygan Falls and such appointment shall continue undischarged for a period of 60 days; or

(c) The amount of Sheboygan Falls' surplus shall be less than the minimum amount of statutory surplus required of Sheboygan Falls by the laws of the State of Wisconsin for the issuance of a certificate of authority to transact the class or classes of insurance that Sheboygan Falls is then authorized to transact.

6. Remedies. Upon the occurrence of an Event of Default and subject to the limitations set forth in Section 3, Donegal Mutual may (a) by notice to Sheboygan Falls, declare the entire unpaid principal amount of this Contribution Note, all interest accrued and unpaid hereon and all other amounts payable hereunder to be forthwith due and payable, whereupon this Contribution Note, all such accrued interest and all such amounts shall become and be forthwith due and payable, without presentment, demand, protest or further notice of any kind, all of which are hereby expressly waived by Sheboygan Falls and (b) proceed to enforce its rights under this Contribution Note by exercising such remedies as are available to Donegal Mutual in respect thereof under applicable law, either by suit in equity or by action of law, or both, whether for specific performance of any agreement contained in

this Contribution Note or in aid of exercise of any power granted in this Contribution Note. No remedies are intended to be exclusive and each such remedy shall be cumulative.

7. Conversion. In the event Sheboygan Falls converts to a stock property and casualty insurance company, Donegal Mutual shall have the option, in its sole discretion, subject to any stock purchase rights of any former policyholders of Sheboygan Falls arising under Wisconsin law, of cancelling this Contribution Note in exchange for such number of shares of stock in the corporation resulting from such conversion as the amount of unpaid principal and interest will purchase at the price specified in Sheboygan Falls' plan of demutualization or taking any such other action permitted under the Laws of the State of Wisconsin. If such unpaid principal and interest would entitle Donegal Mutual to a fractional share of stock in exchange for the cancellation of this Contribution Note, Donegal Mutual shall have the option, in its sole discretion, of being paid the value of such fractional share in cash or of purchasing such additional fractional interest as will entitle Donegal Mutual to purchase a full share.

IN WITNESS WHEREOF, and intending to be legally bound hereby, Sheboygan Falls has executed this Contribution Note on the date and year first above written.

SHEBOYGAN FALLS MUTUAL INSURANCE COMPANY

Attest:

By: \_\_\_\_\_  
Lee F. Wilcox, President

\_\_\_\_\_  
Kenneth F. Maurer, Secretary