

National Interstate CORP
Form DEF 14A
March 24, 2009
Table of Contents

SCHEDULE 14A
SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a)
of the Securities Exchange Act of 1934

Filed by the Registrant Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to Section 240.14a-12

NATIONAL INTERSTATE CORPORATION

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

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(4) Date Filed:

Table of Contents

3250 Interstate Drive

Richfield, Ohio 44286

**Notice of Annual Meeting of Shareholders
and Proxy Statement**

To Be Held On April 29, 2009

Dear Shareholder:

We invite you to attend our Annual Meeting of Shareholders on Wednesday, April 29, 2009 at 9:00 AM, Eastern Daylight Saving Time, at 3250 Interstate Drive, Richfield, Ohio. At the meeting, we will report on our operations and you will have an opportunity to meet our directors and executives.

This booklet includes the formal notice of the meeting and the Proxy Statement. The Proxy Statement tells you more about the agenda and procedures for the meeting. It also describes how our Board of Directors operates, provides information about the director candidates and discusses our executive compensation information.

All shareholders are important to us. We want your shares to be represented at the meeting and urge you to vote by promptly returning a properly completed proxy form.

Sincerely,

David W. Michelson

President and Chief Executive Officer

Richfield, Ohio

March 30, 2009

Table of Contents

**NOTICE OF ANNUAL MEETING OF SHAREHOLDERS
OF NATIONAL INTERSTATE CORPORATION**

Date: Wednesday, April 29, 2009

Time: 9:00 AM Eastern Daylight Saving Time

Place: 3250 Interstate Drive
Richfield, Ohio 44286

Purpose:

1. Elect as directors four Class I nominees named in the proxy statement and recommended by the Board of Directors
2. Approval of the National Interstate Corporation Long Term Incentive Plan
3. Ratify appointment of Ernst & Young LLP as our independent registered public accounting firm
4. Conduct other business if properly raised

Record Date: March 3, 2009 Shareholders registered in our records or our agents' records on that date are entitled to receive notice of and to vote at the meeting.

Mailing Date: The approximate mailing date of this Proxy Statement and accompanying proxy form is March 30, 2009.

**Important Notice Regarding the Availability of Proxy Materials
for the Annual Meeting of Shareholders to be held on April 29, 2009:**

The proxy statement, proxy card and Annual Report on Form 10-K for the year ended December 31, 2008 are available at our Investor Relations internet website at <http://invest.natl.com>

Your vote is important

Whether or not you attend the meeting, you may vote by mailing a signed proxy form, which is the bottom portion of the enclosed perforated form. If you do attend the meeting, you may either vote by proxy or revoke your proxy and vote in person. You may also revoke your proxy in writing at any time before the vote is taken at the meeting by submitting a later-dated proxy form.

Table of Contents

Table Of Contents

<u>GENERAL INFORMATION</u>	1
<u>MATTERS TO BE CONSIDERED</u>	2
<u>PRINCIPAL SHAREHOLDERS</u>	13
<u>MANAGEMENT</u>	14
<u>COMPENSATION DISCUSSION AND ANALYSIS</u>	17
<u>SUMMARY COMPENSATION TABLE</u>	25
<u>GRANTS OF PLAN-BASED AWARDS</u>	26
<u>OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END</u>	28
<u>OPTION EXERCISES AND STOCK VESTED</u>	28
<u>POTENTIAL PAYMENTS UPON TERMINATION OR CHANGE IN CONTROL</u>	29
<u>2008 DIRECTOR COMPENSATION</u>	32
<u>COMMITTEE DESCRIPTIONS, REPORTS AND MEETINGS</u>	34
<u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS</u>	37
<u>NOMINATIONS AND SHAREHOLDER PROPOSALS</u>	40
<u>COMMUNICATIONS WITH DIRECTORS</u>	40
<u>CODE OF ETHICS AND CONDUCT</u>	40

We make available, free of charge on our website, all of our filings that are made electronically with the Securities and Exchange Commission, including Forms 10-K, 10-Q and 8-K. To access these filings, go to our investor relations website (<http://invest.natl.com>) and click on the Financial Information tab at the right. Copies of our Annual Report on Form 10-K for the year ended December 31, 2008, including financial statements and schedules thereto, filed with the Securities and Exchange Commission, are also available without charge to shareholders upon written request addressed to:

Gary N. Monda

Vice President

National Interstate Corporation

3250 Interstate Drive

Richfield, Ohio 44286

Table of Contents

GENERAL INFORMATION

This statement is furnished in connection with the solicitation of proxies for use at our Annual Meeting of Shareholders to be held at 9:00 AM, Eastern Daylight Saving Time, on Wednesday, April 29, 2009, at 3250 Interstate Drive, Richfield, Ohio 44286, and at any adjournment thereof. This statement, our Annual Report to Shareholders for the fiscal year ended December 31, 2008, and the accompanying proxy will be sent to shareholders on or about March 30, 2009.

Record Date; Shares Outstanding

As of March 3, 2009, the record date for determining shareholders entitled to notice of and to vote at the meeting, we had approximately 19,391,896 shares of common stock deemed outstanding and eligible to vote, which excludes 2,510,000 shares owned by one of our subsidiaries. Under Ohio law, shares held by subsidiaries are not entitled to vote and are therefore not considered to be outstanding for purposes of the meeting. Each share of outstanding common stock is entitled to one vote on each matter to be presented at the meeting. Abstentions (including instructions to withhold authority to vote for one or more nominees) and broker non-votes are counted for purposes of determining a quorum, but will have no effect on the outcome of any matter voted on at the meeting.

Cumulative Voting

Shareholders have cumulative voting rights in the election of directors and one vote per share on all other matters. Cumulative voting allows a shareholder to multiply the number of shares owned on the record date by the number of directors to be elected and to cast the total for one nominee or distribute the votes among the nominees, as the shareholder desires. Nominees who receive the greatest number of votes will be elected. In order to invoke cumulative voting, notice of cumulative voting must be given in writing to our Secretary not less than 48 hours before the Annual Meeting.

Proxies and Voting Procedures

Solicitation of proxies through the mail, in person and otherwise, is conducted by management at the direction of our Board of Directors, without additional compensation. We will pay all costs of soliciting proxies. In addition, we will request brokers and other custodians, nominees and fiduciaries to forward proxy-soliciting material to the beneficial owners of shares held of record by such persons at our expense.

Registered shareholders may vote by completing a proxy form and mailing it to our proxy tabulator, National City Bank, now a part of PNC. To vote, shareholders should complete and sign the bottom portion of the proxy form and return only that portion to the proxy tabulator. Shareholders whose shares are held in the name of a broker, bank or other nominee should refer to the proxy card or the information forwarded by such broker, bank or other nominee to see what voting options are available to them.

If a choice is specified on a properly executed proxy form, the shares will be voted accordingly. If a proxy form is signed without a preference indicated, those shares will be voted FOR the election of the four nominees recommended by our Board of Directors, FOR the approval of the National Interstate Corporation Long Term Incentive Plan and FOR the ratification of Ernst & Young LLP as our independent registered public accounting firm. The authority solicited by this Proxy Statement includes discretionary authority to cumulate votes in the election of directors. If any other matters properly come before the meeting or any adjournment thereof, each properly executed proxy form will be voted in the discretion of the proxies named therein.

A shareholder may revoke a prior proxy by writing to our Secretary at our principal offices or by properly executing and delivering a proxy bearing a later date. In addition, persons attending the meeting in person may withdraw their proxies at the meeting and then vote in person.

Table of Contents

With respect to Proposal No. 1, the four nominees who receive the greatest number of votes will be elected. Proposals No. 2 and 3 will be adopted only if they receive approval of a majority vote of those shares cast at the meeting.

Adjournment and Other Matters

Approval of a motion for adjournment or other matters brought before the meeting requires the affirmative vote of a majority of the shares voting at the meeting. We know of no other matters to be presented at the meeting other than those stated in this document.

MATTERS TO BE CONSIDERED

Proposal No. 1 Elect Four Directors

The Board of Directors oversees our management on your behalf. The Board reviews our long-term strategic plans and exercises direct decision-making authority in key areas such as choosing the president and chief executive officer, setting the scope of their respective authority to manage our business day-to-day and evaluating management's performance.

Our Board of Directors is currently comprised of eight directors divided into two classes. Each director serves for a two-year term, with Class I directors elected in odd numbered years and Class II directors elected in even numbered years. The term for our Class I directors expires at this year's Annual Meeting of Shareholders. Joseph E. (Jeff) Consolino, Theodore H. Elliott, Jr., Gary J. Gruber and Donald D. Larson are our current Class I directors. Keith A. Jensen, James C. Kennedy, Joel Schiavone and Alan R. Spachman are our current Class II directors. During 2008, the entire Board of Directors met eleven times. We expect our directors to attend the Annual Meeting of Shareholders. Seven of our eight directors attended the Annual Meeting of Shareholders held on April 30, 2008. No director attended fewer than 75 percent of the aggregate number of meetings of the Board and Board committees on which he served.

After considering all relevant facts and circumstances, including those described under *Certain Relationships and Related Transactions* beginning on page 37 of this Proxy Statement, our Board of Directors has determined that three of our current eight directors, Mr. Consolino, Mr. Elliott and Mr. Schiavone are independent in accordance with Nasdaq Global Select Market listing standards and Securities and Exchange Commission regulations. We are not required to have a majority of independent directors on our Board as would otherwise be required by the rules of the Nasdaq Global Select Market because of the controlled company exemption from these rules that applies to companies where more than 50% of the shareholder voting power is held by an individual, a group or another company. As described elsewhere in this Proxy Statement, Great American Insurance Company holds approximately 53% of our voting power.

Our Board of Directors, acting on the advice of its Nominating/Governance Committee, has nominated four individuals to hold office until the 2011 Annual Meeting of Shareholders or until their successors are elected and qualified. If any of the nominees should become unable to serve as a director, the proxies will be voted for any substitute nominee designated by our Board of Directors but, in any event, no proxy may be voted for more than four nominees. The four nominees who receive the greatest number of votes will be elected.

Table of Contents

The nominees for election as Class I members of the Board of Directors are:

Joseph E. (Jeff) Consolino

Director since May 2006

Mr. Consolino is executive vice president and chief financial officer for Validus Holdings, Ltd., a Bermuda-based reinsurance company. Prior to joining Validus in March 2006, Mr. Consolino was a managing director in Merrill Lynch's Financial Institutions Group specializing in insurance company advisory and financing transactions. Mr. Consolino also serves as a director for AmWINS Group, Inc., a wholesale insurance brokerage based in Charlotte, North Carolina. Mr. Consolino is the Chair of the Audit Committee and a member of the Compensation Committee.

Theodore H. Elliott, Jr.

Director since 1989

Since 1981, Mr. Elliott has been in the venture capital business as the chairman of Prime Capital Management Company, Inc. and as a private investor. Prime Capital was one of our founding investors in 1989. Prior to Prime Capital Management, Mr. Elliott was vice president of General Electric's venture capital subsidiary. Mr. Elliott is a director of ION Geophysical Corporation (NYSE). Mr. Elliott is a member of the Audit and Compensation Committees.

Gary J. Gruber

Director since April 1991

Mr. Gruber serves as senior vice president of Great American Insurance Company, our largest shareholder. Mr. Gruber joined Great American Insurance Company in 1977 and has held a variety of financial, management and officer positions since 1990. Mr. Gruber has served as a director of Great American Insurance Company since 1993. Mr. Gruber is a member of the Nominating/Governance Committee.

Donald D. Larson

Director since April 1991

Mr. Larson served as our Chairman from 1993 until 2004. Mr. Larson has served as executive vice president and president, specialty group, for the Great American Property and Casualty Insurance Group since 1999. Mr. Larson began his career with American Financial Group, Inc., parent of our largest shareholder, in 1973 and joined Great American Insurance Company, our largest shareholder, in 1981. Mr. Larson has served as a director of Great American Insurance Company since 1988. Mr. Larson is the Chair of the Compensation Committee and a member of the Nominating/Governance Committee.

Table of Contents

Below is information about our Class II directors:

Keith A. Jensen

Director since April 2000

Mr. Jensen has served as senior vice president of American Financial Group, Inc., parent of our largest shareholder, since 1999 and was named its chief financial officer in January 2005. Mr. Jensen joined the Great American Property and Casualty Insurance Group in 1999 as senior vice president and chief financial officer and was promoted to executive vice president in 2004. Mr. Jensen has served on the Board of Directors of Great American Insurance Company, our largest shareholder, since 1999. From February 2003 to December 2003, Mr. Jensen served on the Board of Directors of Infinity Property & Casualty Corporation. Before working with American Financial Group, Inc., Mr. Jensen was a partner with Deloitte & Touche LLP. Mr. Jensen is a member of the Compensation Committee.

James C. Kennedy

Director since January 2005

Mr. Kennedy has been the vice president, deputy general counsel and secretary of American Financial Group, Inc., parent of our largest shareholder, since 1998. Mr. Kennedy joined American Financial Group, Inc. in 1976, was named secretary in 1984, deputy general counsel in 1988 and vice president in 1998. Mr. Kennedy is the Chair of the Nominating/Governance Committee.

Joel Schiavone

Director from January 1989 until December 1989 and then re-elected in 2001

Since 1999, Mr. Schiavone has been the managing partner of several privately-held New Haven, Connecticut based real estate companies. Prior to that, Mr. Schiavone was the owner and chief executive officer of Schiavone Corporation, a holding company for a variety of investments. Mr. Schiavone is a member of the Audit and Nominating/Governance Committees.

Alan R. Spachman

Director since 1989

Alan R. Spachman is our founder, and has served as Chairman since 2004. Mr. Spachman served as the chief executive since our inception in 1989 through 2007, and continues to transition his management responsibilities and develop new growth opportunities for us. From 1984 to 1988, Mr. Spachman was a senior vice president at Progressive Corporation, where he initiated its passenger transportation insurance business. In addition to his insurance experience, Mr. Spachman previously held various labor relations and human resource management positions with Collins and Aikman, Inc. and Frito-Lay, Inc.

Our Board of Directors recommends that shareholders vote FOR the election of these four Class I nominees as directors.

Table of Contents

Proposal No. 2 Approval of the National Interstate Corporation Long Term Incentive Plan

We are requesting your approval of the National Interstate Corporation Long Term Incentive Plan (the "LTIP"). The LTIP was adopted by our Board of Directors and approved by shareholders on October 18, 2004, prior to our initial public offering. Even though the LTIP continues to be in full force and effect after the initial public offering, shareholder approval is required to ensure that certain awards granted under the LTIP continue to comply with the performance-based compensation exception to Section 162(m) of the Internal Revenue Code of 1986, as amended (the "Internal Revenue Code").

Section 162(m) of the Internal Revenue Code provides that a public company cannot take a federal income tax deduction for compensation paid to any "covered employee" to the extent the compensation exceeds \$1 million in any tax year. A "covered employee" is any employee who on the last day of the tax year is either (1) the Chief Executive Officer or (2) among the other three highest compensated executive officers (other than the Chief Financial Officer). This deduction limitation does not, however, apply to certain performance-based compensation, including stock options and other performance-based awards granted under a plan approved by shareholders. In addition, the deduction limitation does not apply to any compensation paid pursuant to a plan that existed during the period in which a corporation was not publicly held, to the extent the prospectus accompanying the initial public offering disclosed information concerning such plan that satisfied all applicable securities laws. However, the foregoing exception may be relied upon only for awards made before the earliest of (1) the expiration of the plan; (2) the material modification of the plan; (3) the issuance of all shares allocated under the plan; or (4) the first meeting of shareholders at which Directors are elected occurring after the close of the third calendar year following the calendar year in which the initial public offering occurs.

For this reason, awards granted under the LTIP prior to the 2009 annual meeting are eligible to qualify for the performance-based compensation exception. In order for certain awards granted after that meeting to qualify for the performance-based compensation exception, our shareholders must approve the material terms of the LTIP. If our shareholders do not approve the LTIP, then we will not grant any awards under the plan that are intended to qualify for the performance-based compensation exception to Section 162(m) of the Internal Revenue Code. This means that stock options, appreciation rights and other performance-based awards granted under the plan to our covered employees after the 2009 annual meeting may not be deductible by us for federal income tax purposes, depending on the facts and circumstances.

The complete text of the LTIP is attached as *Appendix A* to this proxy statement. The following summary of the LTIP does not purport to be complete and is qualified in its entirety by reference to *Appendix A*.

General

The LTIP provides for the grant of incentive awards, including incentive stock options, stock appreciation rights, performance units, performance shares, restricted shares, deferred shares, other awards relating to our common shares and dividend equivalents to key employees, consultants and non-employee Directors.

Administration and Amendments

The Compensation Committee administers and interprets the LTIP, except with respect to awards granted to non-employee Directors, which are administered by our entire Board. The LTIP may be amended by our Board as long as any amendment that must be approved by our shareholders in order to comply with applicable law or the rules of any securities exchange on which our common shares are traded or quoted is not effective until shareholder approval has been obtained.

Table of Contents

Shares Available; Adjustment

We have reserved a total of 1,338,800 common shares for issuance or transfer for awards under the LTIP, subject to adjustment in the event of forfeitures, transfers of common shares to us in payment of the exercise price or tax withholding amounts. The closing price of our common shares on March 3, 2009 as reported on the Nasdaq Global Select Market was \$14.08 per share.

Of the total number of common shares that are available under the LTIP, the number of shares that may be issued upon exercise of incentive stock options may not exceed 921,200 shares. During any calendar year, no participant may be granted option rights and appreciation rights, in the aggregate, for more than 115,200 shares, nor shall any participant be granted performance shares, restricted shares specifying management objectives or other share-based awards specifying management objectives, in the aggregate, for more than 69,000 shares, nor shall any participant be granted performance units having an aggregate maximum value in excess of \$375,000. During any calendar year, no non-employee Director may be granted awards for more than 69,000 shares. The number of shares covered by outstanding awards, the number of shares reserved for issuance under the LTIP and other share limits contained in the LTIP are subject to adjustment in the event of stock splits, stock dividends, recapitalizations and other similar events.

Eligibility

Any officer, key employee or consultant of the company or its subsidiaries (or any individual who has agreed to commence serving in any such capacities within 90 days of the date of grant), and our non-employee Directors may be selected by the Compensation Committee to receive benefits under the LTIP. Accordingly, approximately 15 officers and three non-employee Directors may be eligible for awards under the LTIP.

Officers, key employees and consultants may be granted each type of award available under the LTIP. Non-employee Directors may be granted nonqualified stock options, appreciation rights, restricted shares, deferred shares and other share-based awards, but are not eligible for grants of incentive stock options, performance shares or performance units. At this time, however, the Compensation Committee anticipates that only our officers and non-employee Directors will receive awards under the LTIP.

The Compensation Committee may provide for special terms for awards to participants who are foreign nationals or who are employed by us outside the United States as the Compensation Committee may deem necessary or appropriate to accommodate differences in local law, tax policy or custom.

Stock Options

The Compensation Committee may, in its discretion, award option rights to participants that provide the right to purchase common shares at a specified price, which may not be less than their fair market value on the date of grant. Option rights may include incentive stock options or nonqualified stock options. No option rights may be exercised more than ten years from the date of grant. Each grant must specify the period of continuous employment that is necessary before the option rights become exercisable, and may provide for the earlier exercise of such option rights in the event of a change in control of the company, retirement, death or disability of the optionee, or other similar transaction or event approved by the Compensation Committee. Any grant of option rights may specify management objectives (as described below) that must be achieved as a condition to exercise such rights.

Appreciation Rights

The Compensation Committee may, in its discretion, award appreciation rights to participants. Appreciation rights represent the right to receive an amount, determined by the Compensation Committee and expressed as a percentage, not exceeding 100 percent, of the difference between the base price established for such appreciation

Table of Contents

rights (not less than the fair market value of a share on the date of grant) and the market value of our common shares on the date the appreciation rights are exercised. Appreciation rights may be granted in tandem (granted with option rights to provide an alternative to exercise of the option rights) or freestanding and payable in cash, in common shares or in any combination thereof.

Each grant must specify the period of continuous employment that is necessary before the appreciation rights become exercisable, and may provide for the earlier exercise of the appreciation rights in the event of a change in control of the company, retirement, death or disability of the employee or other similar transaction or event approved by the Compensation Committee. Any grant of stock appreciation rights may specify management objectives (as described below) that must be achieved as a condition to exercise such rights.

Performance Shares and Performance Units

The Compensation Committee may, in its discretion, award performance shares and/or performance units to participants. A performance share is the equivalent of one common share and a performance unit is the equivalent of \$1.00. The participant will be given one or more management objectives (as described below) to meet within a specified period (the performance period). The Compensation Committee will also establish a minimum level of acceptable achievement. If by the end of the performance period, the participant has achieved the specified management objectives, the participant will be deemed to have fully earned the performance shares or performance units. If the participant has not achieved the management objectives, but has attained or exceeded a predetermined minimum level of acceptable achievement, the participant will be deemed to have partly earned the performance shares or performance units in accordance with a predetermined formula. To the extent earned, the performance shares or performance units will be paid to the participant at the time and in the manner determined by the Compensation Committee in cash, common shares or any combination thereof. The grant may provide for the payment of dividend equivalents in cash or in common shares on a current, deferred or contingent basis. The grant may also provide for the earlier termination of the performance period in the event of a change in control of the company, retirement, death or disability of the participant or other similar transaction or event approved by the Compensation Committee.

Restricted Shares

The Compensation Committee may, in its discretion, award restricted shares to participants, which constitute an immediate transfer of ownership to the recipient in consideration of the performance of services. The participant has dividend and voting rights on such shares. Restricted shares must be subject to a substantial risk of forfeiture for a period determined by the Compensation Committee on the date of the grant, and may provide for the earlier termination of the forfeiture provisions in the event of a change in control of the company, retirement, death or disability of the participant or other similar transaction or event approved by the Compensation Committee. In order to enforce these forfeiture provisions, the transferability of restricted shares will be prohibited or restricted in the manner prescribed by the Compensation Committee on the date of grant for the period during which such forfeiture provisions are to continue.

Any grant of restricted shares may specify management objectives which, if achieved, will result in termination or early termination of the restrictions applicable to such shares. Any such grant may also specify in respect of such specified management objectives, a minimum acceptable level of achievement and must set forth a formula for determining the number of restricted shares on which restrictions will terminate if performance is at or above the minimum level, but below full achievement of the specified management objectives.

Deferred Shares

The Compensation Committee may, in its discretion, award deferred shares to participants, which constitute an agreement to deliver common shares in the future subject to the terms and conditions established by the Compensation Committee. Prior to the delivery of such shares, the participant has no right to vote or receive

Table of Contents

dividends on the deferred shares, but the Compensation Committee may authorize the payment of dividend equivalents with respect to the deferred shares in cash or common shares on a current, deferred or contingent basis. The Compensation Committee must fix a restriction period at the time of grant, and may provide for the earlier termination of the restriction period in the event of a change in control of the company, retirement, death or disability of the employee or other similar transaction or event approved by the Compensation Committee.

Other Awards

The Compensation Committee may, subject to limitations under applicable law, grant to any participant such other awards that may be denominated or payable in, valued in whole or in part by reference to, or otherwise based on, or related to, common shares or factors that may influence the value of common shares. The Compensation Committee may also grant cash awards as an element of or supplement to any other award granted under the LTIP. The Compensation Committee will determine the terms and conditions of these awards.

Non-employee Directors

The Board may, from time to time and upon such terms and conditions as it may determine, authorize the grant to non-employee Directors of option rights (that are not intended to qualify as incentive stock options), appreciation rights, restricted shares, deferred shares, or any combination of the foregoing. Each such grant shall be upon terms and conditions consistent with the above description of such awards.

Management Objectives

The LTIP requires that the Compensation Committee establish management objectives for purposes of performance shares and performance units. When so determined by the Compensation Committee, option rights, appreciation rights and restricted shares may also specify management objectives.

Management objectives may be described in terms of either company-wide objectives or objectives that are related to the performance of the individual participant or subsidiary, division, department, region or function within the company or a subsidiary in which the participant is employed. Management objectives applicable to any award to a participant who is, or is determined by the Compensation Committee likely to become, a covered employee within the meaning of Section 162(m)(3) of the Internal Revenue Code (and that is intended to qualify for the performance-based compensation exception to Section 162(m) of the Internal Revenue Code) will be limited to specified levels of or growth in one or more of the following criteria: revenues, earnings from operations, earnings from underwriting activities, earnings from investment activities, earnings before or after interest and taxes, net income, cash flow, earnings per share, debt to capital ratio, economic value added, return on total capital, return on invested capital, return on equity, return on assets, total return to stockholders earnings before or after interest, depreciation, amortization or extraordinary or special items, return on investment, free cash flow, cash flow return on investment (discounted or otherwise), net cash provided by operations, cash flow in excess of cost of capital, operating margin, profit margin, stock price and/or strategic business criteria consisting of one or more objectives based on meeting specified product development, strategic partnering, research and development, market penetration, geographic business expansion goals, cost targets, customer satisfaction, employee satisfaction, management of employment practices and employee benefits, supervision of litigation and information technology and goals relating to acquisitions or divestitures of subsidiaries, affiliates and joint ventures. Except in the case of a covered employee where such modification would result in the loss of an otherwise available exemption under Section 162(m) of the Internal Revenue Code, if the Compensation Committee determines that a change in our business, operations, corporate structure or capital structure of the company, or the manner in which we conduct our business, or other events or circumstances render the management objectives unsuitable, the Compensation Committee may modify such management objectives, in whole or in part, as the Compensation Committee deems appropriate and equitable.

Table of Contents

Transferability

Except as otherwise determined by the Compensation Committee, option rights, appreciation rights and any other derivative security granted under the LTIP will not be transferable by a participant other than by will or the laws of descent and distribution. Except as otherwise determined by the Compensation Committee, option rights and appreciation rights are exercisable during a participant's lifetime only by him or her or by his or her guardian or legal representative. Any award made under the LTIP may provide that any common shares issued or transferred as a result of the award will be subject to further restrictions upon transfer.

Adjustments

The Compensation Committee shall make or provide for such adjustments in the numbers of common shares covered by outstanding option rights, appreciation rights, performance shares, deferred shares and other share-based awards, in the option price and base price provided in outstanding options and appreciation rights, and in the kind of shares covered thereby, as the Compensation Committee in its sole discretion may in good faith determine to be equitably required in order to prevent dilution or enlargement of the rights of participants that would otherwise result from (1) any stock dividend, stock split, combination of shares, recapitalization or other change in the capital structure of the company, (2) any merger, consolidation, spinoff, spin-out, split-off, split-up, reorganization, partial or complete liquidation or other distribution of assets, issuance of rights or warrants to purchase securities, or (3) any other corporate transaction or event having an effect similar to any of the foregoing. In the event of any such transaction or event, the Compensation Committee may provide in substitution for any or all of the outstanding awards under the LTIP such alternative consideration (or no consideration) as it may in good faith determine to be equitable in the circumstances and may require in connection therewith the surrender of all awards so replaced.

Miscellaneous

The Compensation Committee may permit participants to elect to defer the issuance of common shares or the settlement of awards in cash under the LTIP pursuant to such rules, procedures or programs as it may establish. The Compensation Committee is not permitted to grant stock options or appreciation rights at an exercise price that is less than the fair market value of the underlying shares on the date of grant (*i.e.*, in-the-money options) and may not re-price outstanding option rights or appreciation rights granted under the LTIP without the approval of our shareholders.

Acceleration of Awards

Where the Compensation Committee has established conditions to the exercisability or retention of certain awards, the LTIP allows the Compensation Committee to take action in its sole discretion at or after the date of grant to adjust such conditions in certain circumstances, including in the case of a change in control of the company or the death, disability, retirement or hardship of a participant. With respect to all stock option and restricted share awards granted under the LTIP since our initial public offering, the Compensation Committee has exercised this discretion by including a provision in each award agreement requiring the acceleration of awards in the event of a change in control in the company. Generally, a change in control will be deemed to have occurred if (1) any person or group becomes the beneficial owner of 30% or more of the combined voting power of our outstanding securities (subject to certain exceptions), (2) there is a change in the majority of our Board of Directors, (3) certain corporate reorganizations take place where the existing shareholders do not retain more than 51% of the combined voting power of the outstanding securities or (4) our shareholders approve a complete liquidation or dissolution.

Awards Under the LTIP

Because it is within the discretion of our Compensation Committee or the Board, as applicable, to determine which officers, key employees, consultants and non-employee Directors will receive awards, and the amount and type of awards received, it is not presently possible to determine the number of individuals to whom awards will be made in the future under the LTIP or the amount of the awards.

Table of Contents

Federal Income Tax Consequences

The following is a brief summary of the federal income tax consequences of certain transactions under the LTIP. The discussion is general in nature and does not take into account a number of considerations which may apply in light of the circumstances of a particular participant under the LTIP. The income tax consequences under applicable state and local tax laws may not be the same as under federal income tax laws.

Non-Qualified Stock Options. A participant will not recognize taxable income at the time of grant of a non-qualified stock option, and we will not be entitled to a tax deduction at such time. A participant will recognize compensation taxable as ordinary income (and subject to income tax withholding in respect of an employee) upon exercise of a non-qualified stock option equal to the excess of the fair market value of the shares purchased over their exercise price, and we generally will be entitled to a corresponding deduction. At the time of sale of common shares acquired upon exercise of a non-qualified stock option, appreciation (or depreciation) in value of the common shares after the date of exercise will be treated as either short-term or long-term capital gain (or loss) to the participant, depending on how long the shares have been held.

Incentive Stock Options. A participant will not recognize taxable income at the time of grant of an incentive stock option. A participant will not recognize taxable income (except for purposes of the alternative minimum tax) upon exercise of an incentive stock option. If the shares acquired by exercise of an incentive stock option are held for the longer of two years from the date the option was granted and one year from the date the shares were transferred, any gain or loss arising from a subsequent disposition of such shares will be taxed as long-term capital gain or loss, and we will not be entitled to any deduction. If, however, such shares are disposed of within such two or one year periods, then in the year of such disposition the participant will recognize compensation taxable as ordinary income equal to the excess of the lesser of the amount realized upon such disposition and the fair market value of such shares on the date of exercise over the exercise price, and we generally will be entitled to a corresponding deduction.

Appreciation Rights. A participant will not recognize taxable income at the time of grant of an appreciation right, and we will not be entitled to a tax deduction at such time. Upon exercise, a participant will recognize compensation taxable as ordinary income (and subject to income tax withholding in respect of an employee) equal to the fair market value of any shares delivered and the amount of cash paid by us, and we generally will be entitled to a corresponding deduction.

Performance Shares. A participant will not recognize taxable income at the time of grant of performance shares, and we will not be entitled to a tax deduction at such time. A participant will recognize compensation taxable as ordinary income (and subject to income tax withholding in respect of an employee) at the time of settlement of the award equal to the fair market value of any shares or property delivered and the amount of cash paid by us, and we will be entitled to a corresponding deduction, except to the extent the deduction limits of Section 162(m) of the Internal Revenue Code apply.

Restricted Shares. A participant will not recognize taxable income at the time of grant of shares of restricted stock, and we will not be entitled to a tax deduction at such time, unless the participant makes an election under Section 83(b) of the Internal Revenue Code to be taxed at such time. If such election is made, the participant will recognize compensation taxable as ordinary income (and subject to income tax withholding in respect of an employee) at the time of the grant equal to the excess of the fair market value of the shares at such time over the amount, if any, paid for such shares. If such election is not made, the participant will recognize compensation taxable as ordinary income (and subject to income tax withholding in respect of an employee) at the time the restrictions lapse in an amount equal to the excess of the fair market value of the shares at such time over the amount, if any, paid for such shares. We are entitled to a corresponding deduction at the time the ordinary income is recognized by the participant, except to the extent the deduction limits of Section 162(m) of the Internal Revenue Code apply. In addition, a participant receiving dividends with respect to restricted stock for which the above-described election has not been made and prior to the time the restrictions lapse will recognize

Table of Contents

compensation taxable as ordinary income (and subject to income tax withholding in respect of an employee), rather than dividend income. We will be entitled to a corresponding deduction, except to the extent the deduction limits of Section 162(m) of the Internal Revenue Code apply.

Deferred Shares. Generally, a participant will not recognize taxable income at the time of grant of deferred shares, and we will not be entitled to a tax deduction at such time. The participant will be subject to tax at ordinary income rates on the fair market value of unrestricted common shares on the date that such shares are transferred to the participant under the award (reduced by any amount paid by the participant for such deferred shares), and the capital gain/loss holding period for such shares will also commence on that date.

Other Share-Based Awards. The recipient of a share-based award other than an award described above generally will be subject to tax at ordinary income rates on the fair market value of common shares on the date of grant of the share-based award, and the capital gain/loss holding period for such shares also will commence on such date.

Dividend Equivalents. Any dividend equivalents awarded with respect to awards granted under the LTIP and paid in cash or unrestricted common shares will be taxed to the participant at ordinary income rates when received by the participant.

Section 409A. Awards granted under the LTIP will be designed and administered in such a manner that they are either exempt from the application of, or comply with, the requirements of Section 409A of the Internal Revenue Code.

Because the tax consequences to a participant may vary depending on his or her individual circumstances, each participant should consult his or her personal tax advisor regarding the federal and any state, local, foreign or other consequences to him or her.

Tax Consequences to the Company. To the extent that a participant recognizes ordinary income in the circumstances described above, the company or the subsidiary for which the participant performs services will be entitled to a corresponding deduction provided that, among other things, (1) the income meets the test of reasonableness, (2) is an ordinary and necessary business expense, (3) is not an excess parachute payment within the meaning of Section 280G of the Internal Revenue Code and (4) is not disallowed by the \$1 million limitation on certain executive compensation.

Term

The LTIP will terminate in 2014, but awards effective at the time of the termination of the LTIP will continue in accordance with their terms.

Vote Required

Approval of the LTIP will require the affirmative vote of the holders of a majority of our outstanding common shares represented in person or by proxy at the annual meeting.

Our Board of Directors recommends that shareholders vote FOR the approval of the National Interstate Corporation Long Term Incentive Plan.

Table of Contents***Proposal No. 3 Ratification of Our Independent Registered Public Accounting Firm***

Our Audit Committee Charter provides that the Audit Committee shall recommend annually to the Board of Directors the appointment of an independent registered public accounting firm to serve as auditors. In April 2009, the Audit Committee expects to recommend the appointment of Ernst & Young LLP to serve as auditors for the year ending December 31, 2009. Ernst & Young LLP (or its predecessor) has served as our independent registered public accounting firm since our formation in 1989.

Both our Board of Directors and Audit Committee would like to know the opinion of shareholders regarding the appointment of Ernst & Young LLP as auditors for the year ending December 31, 2009. For this reason, shareholders are being asked to ratify this appointment. If the shareholders do not ratify the appointment, our Audit Committee and Board of Directors will take that fact into consideration, but may, nevertheless, continue to retain Ernst & Young LLP. We may also engage a different independent registered public accounting firm at any time during the year if our Audit Committee and Board of Directors determine that such a change would be in our best interests.

Audit Fees and Non-Audit Fees

The following table presents fees for professional audit services by Ernst & Young LLP for the audit of our annual financial statements for the years ended December 31, 2008 and December 31, 2007, and fees billed for other services rendered by them during these periods.

	2008	2007
Audit fees (1)	\$ 751,600	\$ 790,495
Tax fees (2)	15,000	15,225
All other fees (3)	2,656	2,656
Total	\$ 769,256	\$ 808,376

- (1) Ernst & Young LLP's aggregate fees for services related to the audits of the U.S. generally accepted accounting principles financial statements, statutory insurance company audits, reviews of Securities and Exchange Commission filings and for quarterly reviews.
 - (2) Ernst & Young LLP's tax fees included charges related to the review of federal and state tax returns.
 - (3) All other fees are related to an EYOnline subscription, which we use to conduct financial research.
- Representatives of Ernst & Young LLP are expected to be at the meeting and will be given the opportunity to make a statement if they desire to do so. They will also be available to respond to appropriate questions from shareholders.

Our Board of Directors recommends that shareholders vote FOR the ratification of the appointment of Ernst & Young LLP as our independent registered public accounting firm for the year ending December 31, 2009.

Table of Contents**PRINCIPAL SHAREHOLDERS**

The following shareholders are the only persons known by us to beneficially own 5% or more of our outstanding common shares as of March 3, 2009:

Name and Address of Beneficial Owner	Common Shares Held (1)	Percent of Class	Percent of Voting Power (2)
Great American Insurance Company 530 Walnut Street Cincinnati, Ohio 45202	10,200,000	46.6%	52.6%
Alan R. Spachman c/o National Interstate Corporation 3250 Interstate Drive Richfield, Ohio 44286	2,394,000	10.9%	12.3%
T. Rowe Price Associates, Inc. (3) 100 E. Pratt Street Baltimore, Maryland 21202	1,939,300	8.9%	10.0%

- (1) Beneficial ownership is determined in accordance with Rule 13d-3 of the Securities Exchange Act of 1934 and generally includes voting and investment power with respect to securities, subject to community property laws, where applicable. The table also includes the number of common shares that may be acquired pursuant to options that are currently exercisable or will be exercisable within 60 days of March 3, 2009.
- (2) Does not include 2,510,000 common shares held by our subsidiary, National Interstate Insurance Company. Under Ohio law, shares held by an issuer's wholly-owned subsidiary do not have voting rights and are not counted for quorum purposes.
- (3) Based on information contained in a Schedule 13G/A filed with the Securities and Exchange Commission on March 10, 2009. T. Rowe Price Associates, Inc. has sole voting power with respect to 719,900 of these shares and has sole dispositive power with respect to all of these shares. These securities are owned by various individuals and institutional investors including T. Rowe Price Small-Cap Value Fund, Inc., which owns 1,168,300 shares, representing 6.0% of the shares outstanding. T. Rowe Price Associates, Inc. serves as investment adviser with the power to direct investments and/or sole power to vote the securities, but however, Price Associates expressly disclaims beneficial ownership of such securities.

Table of Contents**MANAGEMENT**

The table below provides information regarding our directors and executive officers as of March 3, 2009. There are no family relationships among any of our directors or executive officers.

Name	Age	Position	Director or Executive Officer Since
David W. Michelson(1)	51	President and Chief Executive Officer	1992
Julie A. McGraw	45	Vice President, Treasurer and Chief Financial Officer	2006
Terry E. Phillips	59	Senior Vice President	1999
Gary N. Monda	52	Vice President and Chief Investment Officer	1999
Alan R. Spachman	61	Chairman of the Board	1989
Joseph E. (Jeff) Consolino(3)(5)	42	Director	2006
Theodore H. Elliott, Jr.(2)(3)	73	Director	1991
Gary J. Gruber(4)	53	Director	1991
Keith A. Jensen(3)	58	Director	2000
James C. Kennedy(7)	58	Director	2005
Donald D. Larson(4)(6)	57	Director	1991
Joel Schiavone(2)(4)	72	Director	2001

- (1) David W. Michelson was initially employed by us in 1992 through 1998 and rejoined us in 1999.
- (2) Member of the Audit Committee.
- (3) Member of the Compensation Committee.
- (4) Member of the Nominating/Governance Committee.
- (5) Chair of the Audit Committee.
- (6) Chair of Compensation Committee.
- (7) Chair of Nominating/Governance Committee.

For biographical information concerning the directors and nominees for director, please see pages 3-4.

David W. Michelson became our President and Chief Executive Officer effective January 1, 2008. Prior to being named Chief Executive Officer, Mr. Michelson served as our President and Chief Operating Officer during 2007. He has held several other positions during his initial employment with us from 1992-1998 and since rejoining us in 1999. Mr. Michelson has also held various positions in the insurance industry at Reliance Insurance Company, Liberty National Fire and Progressive Corporation.

Julie A. McGraw has served as our Vice President, Treasurer and Chief Financial Officer since January 2006. Prior to joining us, Ms. McGraw held various positions at HMI Industries Inc. from 1996 to 2006, including vice president and chief financial officer/treasurer. Additionally, Ms. McGraw held various financial management positions at Moen Inc. and Isolab Inc. and worked for five years at the public accounting firm of Price Waterhouse.

Terry E. Phillips has served as our Senior Vice President since May 2006. Mr. Phillips has held other executive positions with our subsidiary, National Interstate Insurance Company, including Vice President, Claims, since 1999. Prior to joining us, Mr. Phillips was senior vice president for Continental National Indemnity from 1989 to 1999. Mr. Phillips previously served in both management and claims capacities for Midwestern Group, USF&G and TransAmerica Group Insurance Companies.

Gary N. Monda has served as our Vice President and Chief Investment Officer since January 2006 and was previously our Vice President and Chief Financial Officer since 1999. Prior to joining us, Mr. Monda served the insurance industry as vice president, strategic planning, for Victoria Financial Corporation and held various financial and general management positions with Progressive Corporation over a period of fifteen years. Mr. Monda also worked for four years at the public accounting firm of Ernst & Young LLP.

Table of Contents**Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our directors, executive officers and the holders of more than 10% of our common shares to file reports with the Securities and Exchange Commission. Such reports include initial reports of ownership of our common shares and other equity securities on a Form 3 and reports of changes in such ownership on a Form 4 or Form 5. Executive officers, directors and 10% stockholders are required by Securities and Exchange Commission regulations to furnish us with copies of all Section 16(a) forms that they file.

Based on our review of the copies of such forms we have received, we believe that all of our executive officers, directors and 10% shareholders complied with all filing requirements applicable to them with respect to transactions during fiscal year 2008.

Securities Ownership

The following table sets forth information, as of March 3, 2009, concerning the beneficial ownership of our equity securities by our current directors, the Named Executive Officers in the Summary Compensation Table and by all of our directors and executive officers as a group. Such information is based on data furnished by the persons named. Except as set forth in the following table, no director or executive officer beneficially owned 1% or more of any class of our equity securities outstanding at March 3, 2009. Unless otherwise indicated, beneficial ownership of the equity securities held by each individual consists of sole voting power and sole investment power or of voting power and investment power that is shared with the individual's spouse or family member.

Name of Beneficial Owner	Number of Shares (1)	Percent	Voting Power (2)
David W. Michelson(3)	233,308	1.1%	1.2%
Julie A. McGraw	24,000	*	*
Terry E. Phillips	106,000	*	*
Gary N. Monda	85,600	*	*
Donald B. Davis Jr.(4)	600	*	*
Alan R. Spachman	2,394,000	10.9%	12.3%
Joseph E. (Jeff) Consolino	2,469	*	*
Theodore H. Elliott, Jr.	145,200	*	*