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STATE AUTO FINANCIAL CORP
Form DEF 14A
April 19, 2004

SCHEDULE 14A
(RULE 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT
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-11c or Section 240.14a-12

STATE AUTO FINANCIAL CORPORATION

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement)

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(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

[State Auto Financial Corporation Logo]

STATE AUTO FINANCIAL CORPORATION

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

To the Shareholders of
STATE AUTO FINANCIAL CORPORATION:

Notice is hereby given that the Annual Meeting of Shareholders of State Auto Financial Corporation (the "Company") will be held at the Company's principal executive offices located at 518 East Broad Street, Columbus, Ohio, on Friday, May 28, 2004, at 10:00 A.M., local time, for the following purposes:

1. To elect three Class I directors, each to hold office for a three-year term and until a successor is elected and qualified;
2. To ratify the selection of Ernst and Young LLP as the Company's independent public accountants for 2004; and
3. To transact such other business as may properly come before the meeting or any adjournment thereof.

The close of business on April 5, 2004, has been fixed as the record date for the determination of shareholders entitled to notice of and to vote at the meeting and any adjournment thereof.

In order that your shares may be represented at this meeting and to assure a quorum, please sign and return the enclosed proxy promptly. A return addressed envelope, which requires no postage, is enclosed. In the event you are able to attend and wish to vote in person, at your request we will cancel your proxy.

By Order of the Board of Directors

JOHN R. LOWTHER
Secretary

Dated: April 19, 2004

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STATE AUTO FINANCIAL CORPORATION

PROXY STATEMENT

GENERAL

This Proxy Statement is furnished in connection with the solicitation of proxies by the Board of Directors of State Auto Financial Corporation (the "Company") to be used at its Annual Meeting of Shareholders to be held May 28, 2004 (the "Annual Meeting"). Shares represented by properly executed proxies will be voted at the Annual Meeting in accordance with the choices indicated on the proxy. A proxy may be revoked at any time, insofar as it has not been exercised, by delivery to the Company of a subsequently dated proxy or by giving notice of revocation to the Company in writing or in open meeting. A shareholder's presence at the Annual Meeting does not by itself revoke the proxy.

The mailing address of the principal executive offices of the Company is 518 East Broad Street, Columbus, Ohio 43215. The approximate date on which this Proxy Statement and the form of proxy are first being sent or given to shareholders is April 19, 2004.

PROXIES AND VOTING

The close of business on April 5, 2004, has been fixed as the record date for the determination of shareholders entitled to notice of and to vote at the Annual Meeting and any adjournment thereof. On the record date there were outstanding and entitled to vote 39,719,413 of the Company's common shares, without par value (the "Common Shares"). Each Common Share is entitled to one vote.

Shareholders do not have the right to cumulate their votes in the election of directors, and the nominees receiving the highest number of votes will be elected as the Class I directors. The vote required for the ratification of the selection of Ernst & Young LLP as the Company's independent public accountants for 2004 is the favorable vote of a majority of the outstanding Common Shares present in person or by proxy at the Annual Meeting.

All Common Shares represented by properly executed proxies will be voted at the Annual Meeting in accordance with the choices indicated on the proxy. If no choices are indicated on a proxy, the Common Shares represented by that proxy will be voted in favor of the nominees listed in this Proxy Statement for election as Class I directors and in favor of the ratification of the selection of Ernst & Young LLP. Any proxy may be revoked at any time prior to its exercise by delivering to the Company a subsequently dated proxy or by giving notice of revocation to the Company in writing or in open meeting. A shareholder's presence at the Annual Meeting does not by itself revoke the proxy.

Abstentions will be considered as Common Shares present and entitled to vote at the Annual Meeting and will be counted for purposes of determining whether a quorum is present. Abstentions will not be counted in determining the votes cast for the election of directors and will not have a positive or negative effect on the outcome of the election. Because the ratification of the selection of Ernst & Young LLP requires the favorable vote of a majority of the outstanding Common Shares present in person or by proxy at the Annual Meeting, abstentions will have the same effect as a vote against this ratification.

If your Common Shares are held in street name, you will need to instruct your broker regarding how to vote your Common Shares. If you do not provide voting instructions to your broker, and if your broker does not have discretion

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to vote your Common Shares without your instructions, a "broker non-vote" will occur. Broker non-votes will not be counted in determining the votes cast for the election of directors or with respect to the ratification of the selection of Ernst & Young LLP and will not have a positive or negative effect on the outcome of these matters.

PROPOSAL ONE: ELECTION OF DIRECTORS

The number of directors currently is fixed at nine. The Board of Directors is divided into three classes, Class I, Class II and Class III, with three directors in each Class. The term of office of directors in one Class expires annually at each annual meeting of shareholders at such time as their successors are elected and qualified. Directors in each Class are elected for three-year terms. The term of office of the Class I directors expires concurrently with the holding of the Annual Meeting. Messrs. Paul W. Huesman, John R. Lowther and Robert H. Moone, the three persons recommended by the Nominating and Governance Committee of the Company's Board of Directors, and each of whom is an incumbent Class I director, have been nominated for re-election.

At the Annual Meeting, it is the intention of the persons named in the accompanying form of proxy, unless a contrary position is indicated on such proxy, to vote the proxy for the election of the three nominees named in the following table as Class I directors, each to hold office until the 2007 annual meeting of shareholders and until a successor is elected and qualified. Each of the nominees has consented to being named in this Proxy Statement and to serve if elected. In the event that any nominee named in the table as a Class I director is unable to serve (which is not anticipated), the persons named in the proxy may vote it for another nominee of their choice.

Proxies cannot be voted at the Annual Meeting for a greater number of persons than the three nominees named in this Proxy Statement.

2

Set forth below is information about each of the Class I director nominees:

CLASS I DIRECTOR NOMINEES (TERMS EXPIRING IN 2007)

NAME OF DIRECTOR NOMINEE AND POSITION(S) WITH COMPANY -----	AGE(1) -----	PRINCIPAL OCCUPATION(S) DURING THE PAST FIVE YEARS -----	A DIRECTOR OF THE COMPANY SINCE -----	COMMON SHARES OWNED BENEFICIALLY A OF APRIL 5, 2004(2) (3) -----
Paul W. Huesman(4) Director	68	Consultant to Huesman-Schmid Insurance Agency, Inc., an insurance agency, 6/03 to present; Agent with Huesman-Schmid Insurance Agency, Inc., 01/03 to 6/03; Formerly President of Huesman-Schmid Insurance Agency, Inc., for more than five years prior to 01/03.	1991	77,564
John R. Lowther(5)..... Senior Vice President, Secretary and General Counsel	53	Senior Vice President of the Company, State Auto Property and Casualty Insurance Company ("State Auto P&C"), Milbank Insurance Company ("Milbank"), State Auto	1991	117,127

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<p>Robert H. Moone(6)..... Chairman, President and CEO</p>	<p>60</p>	<p>National Insurance Company ("National"), and Farmers Casualty Insurance Company ("Farmers Casualty"), each a wholly owned subsidiary of the Company, and of State Automobile Mutual Insurance Company ("State Auto Mutual"), 3/01 to present; Secretary and General Counsel of the Company, State Auto P&C, Milbank, National, and State Auto Mutual for more than five years; Vice President of the Company, State Auto P&C, Milbank, National and State Auto Mutual for more than five years prior to 3/01. Chairman of the Board of the Company, State Auto P&C, Milbank, National, Farmers Casualty and State Auto Mutual, 1/01 to present; President and CEO of the Company, State Auto P&C, Milbank, National, Farmers Casualty and State Auto Mutual, 5/99 to present; President and COO of the Company, State Auto P&C, Milbank, National and State Auto Mutual, 5/96 to 5/99.</p>	<p>1998</p>	<p>298,880</p>
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3

Set forth below is information about the directors whose terms of office continue after the Annual Meeting.

CLASS II DIRECTORS
(TERMS EXPIRING IN 2005)

NAME OF DIRECTOR AND POSITION(S) WITH COMPANY -----	AGE(1) -----	PRINCIPAL OCCUPATION(S) DURING THE PAST FIVE YEARS -----	A DIRECTOR OF THE COMPANY SINCE -----	COMMON SHARES OWNED BENEFICIALLY A OF APRIL 5, 2004(2) (3) -----
<p>David J. D'Antoni(7)... Director</p>	<p>59</p>	<p>Senior Vice President and Group Operating Officer, Ashland, Inc., 3/99 to present; President of APAC, Inc., a subsidiary of Ashland, Inc., 7/03 to 1/04; Senior Vice President of Ashland, Inc. and President, Ashland Chemical, a division of Ashland, Inc., 7/88 to 3/99. Ashland, Inc. is involved in oil refining and marketing, highway construction, automotive after market products, specialty chemicals and chemical and plastics distribution. Mr. D'Antoni is also a director of Omnova Solutions Inc., a producer of decorative and</p>	<p>1995</p>	<p>53,200</p>

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William J. Lhota..... Director	64	functional surfaces, coatings, and specialty chemicals. Principal, LHOTA SERVICES, a firm providing business and engineering ethics consulting and arbitration/mediation services, 1/02 to present; Retired President - Energy Delivery, American Electric Power, 6/00 to 12/01; Retired Executive Vice President, American Electric Power Service Corporation, a management, technical, and professional subsidiary of American Electric Power, 11/89 to 6/00. Mr. Lhota is also a director of Huntington Bancshares, Inc., a bank holding company.	1994	40,200
S. Elaine Roberts..... Director	51	President and CEO of the Columbus Regional Airport Authority, 01/03 to present; Executive Director of Columbus Airport Authority, 12/00 to 01/03; Executive Director of Rhode Island Airport Corporation, 12/94 to 12/00.	2002	4,200

4

CLASS III DIRECTORS
(TERMS EXPIRING IN 2006)

NAME OF DIRECTOR AND POSITION(S) WITH COMPANY -----	AGE(1) -----	PRINCIPAL OCCUPATION(S) DURING THE PAST FIVE YEARS -----	A DIRECTOR OF THE COMPANY SINCE -----	COMMON SHARES OWNED BENEFICIALLY A OF APRIL 5, 2004 (2) (3) -----
Urlin G. Harris, Jr.... Director	67	Secretary and Treasurer of Aspen Ski & Board Co., a ski equipment retailer, 7/99 to present; retired 4/97 as an officer of the Company, State Auto P&C, Milbank, National, and State Auto Mutual; prior to his retirement, Mr. Harris was an executive officer of the Company since its formation in 1991 and an officer of State Auto Mutual since before 1991.	1991	52,807
Richard K. Smith(8).... Director	59	Retired 6/97 as Partner of KPMG, LLP, a public accounting firm; Partner of KPMG, LLP, for more than five years prior to 6/97.	1999	17,200
Paul S. Williams..... Director	44	Executive Vice President, Chief Legal Officer and Secretary of Cardinal Health, Inc. ("Cardinal"), a provider of products and services to healthcare providers and manufacturers, 4/01 to present;	2003	0

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Senior Vice President of Cardinal, 1/01 to 4/01; Vice President of Cardinal, 6/98 to 1/01; Deputy General Counsel of Cardinal, 7/99 to 1/01; Assistant Secretary of Cardinal, 6/98 to 4/01; Assistant General Counsel of Cardinal, 6/98 to 7/99.

* Less than one (1%) percent.

- (1) Ages shown are as of the date of the Annual Meeting.
- (2) Except as indicated in the notes to this table, the persons named in the table have sole voting and investment power with respect to all Common Shares shown as beneficially owned by the named person. With respect to stock options, this table includes only stock options for Common Shares which are currently exercisable or exercisable within 60 days of April 5, 2004.
- (3) The amount reported includes Common Shares attributable to options granted under the Company's 1991 Stock Option Plan and the 2000 Stock Option Plan for Messrs. Moone (186,013) and Lowther (60,333) and Common Shares attributable to options granted under both the Company's 1991 Directors Stock Option Plan and 2000 Directors Stock Option Plan for Messrs. Lhota (19,200), D'Antoni (19,200), Huesman (22,200), Smith (9,200), Harris (13,200) and Ms. Roberts (3,200).
- (4) Includes 2,873 Common Shares owned by Mrs. Huesman, as to which Mr. Huesman disclaims beneficial ownership, and 17,006 Common Shares owned by the Huesman-Schmid Insurance Agency, Inc. Defined Benefit Pension Plan. Mr. Huesman shares voting and investment power with the other trustee of this plan with respect to these Common Shares.

5

- (5) Includes 6,500 Common Shares attributable to options granted to Mr. Lowther under the Company's 1991 Stock Option Plan, which he assigned to his spouse pursuant to the terms of the 1991 Stock Option Plan, and 2,000 Common Shares attributable to options granted under the 1991 Stock Option Plan, which he assigned pursuant to the 1991 Stock Option Plan to trusts maintained for the benefit of his children and 14,244 Common Shares owned by Mrs. Lowther. Mr. Lowther disclaims beneficial ownership of these Common Shares.
- (6) Includes 38,190 Common Shares attributable to options granted to Mr. Moone under the 1991 Stock Option Plan, which he assigned to the Anna Moone Living Trust (Anna Moone and Robert H. Moone, co-trustees) pursuant to the terms of the 1991 Stock Option Plan, and 11,400 Common Shares owned by Mrs. Moone. Mr. Moone disclaims beneficial ownership of these Common Shares.
- (7) Includes 12,000 Common Shares owned by Mrs. D'Antoni, as to which Mr. D'Antoni disclaims beneficial ownership.
- (8) Includes 5,000 Common Shares owned by Mrs. Smith, as to which Mr. Smith disclaims beneficial ownership.

In addition to the Common Shares owned beneficially by Messrs. Lowther and Moone, as set forth above, Mark A. Blackburn, Steven J. Johnston and Steven R.

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Hazelbaker, the other named executive officers in the Summary Compensation Table set forth below, owned beneficially 39,048, 106,728, and 7,707 Common Shares, respectively, of the Company as of April 5, 2004, each of which represents less than 1% of the Company's outstanding Common Shares. These amounts include Common Shares attributable to options which are currently exercisable or exercisable within 60 days of April 5, 2004, granted under the Company's 1991 Stock Option Plan and the Company's 2000 Stock Option Plan in the amounts of 34,064, 73,464, and 4,832 for Messrs. Blackburn, Johnston and Hazelbaker, respectively. These persons and/or their spouses have sole voting and investment power with respect to all Common Shares beneficially owned by them. As of April 5, 2004, all directors and executive officers of the Company as a group (23 persons) owned beneficially 1,375,729 (3.5%) Common Shares of the Company, which included options for 785,812 Common Shares.

BOARD OF DIRECTORS AND BOARD COMMITTEES

The Company's Board of Directors (the "Board") has affirmatively determined that six of the Company's nine directors, namely David J. D'Antoni, Urlin G. Harris, Jr., William J. Lhota, S. Elaine Roberts, Richard K. Smith and Paul S. Williams, are "independent" as defined by the NASDAQ Marketplace Rules ("NASDAQ"). During the fiscal year ended December 31, 2003, the Board held nine meetings. No incumbent director attended fewer than 75% of the aggregate of the meetings of the Board and the meetings of all committees on which he or she served.

The Board has established an Audit Committee, a Compensation Committee, a Nominating and Governance Committee (the "Nominating Committee"), an Investment Committee, and a standing Independent Committee. All of the members of the Audit, Compensation, Nominating and Independent Committees are "independent" as defined by NASDAQ. In addition, all of the members of the Audit Committee are independent as defined by the applicable rules of the Securities and Exchange Commission (the "SEC"). The Board has adopted charters for each of the foregoing Committees. Copies of the current charters for each of these Committees, along with copies of the Company's current Corporate Governance Guidelines, Code of Business Conduct, and Code of Ethics for Senior

6

Financial Officers, are available on the Company's website at www.stfc.com under "Corporate Governance."

The Audit Committee is charged with several responsibilities, including: 1) appointment, compensation, retention and oversight of the work performed by the Company's independent auditors; 2) reviewing the Company's accounting functions, operations, and management; 3) considering the adequacy and effectiveness of the internal controls and internal auditing methods and procedures of the Company; 4) meeting and consulting with the Company's independent auditors and with the Company's financial and accounting personnel concerning the foregoing matters; 5) reviewing with the Company's independent auditors the scope of their audit of the Company and the results of their examination of its financial statements; 6) participating in the process of administering the Company's Code of Business Conduct; 7) establishing procedures for receipt, retention and treatment of compliance regarding accounting, internal accounting controls or auditing matters, including procedures for the confidential, anonymous submission by employees of concerns regarding accounting or auditing matters; and 8) approving in advance any other work performed by the Company's independent auditors that they are permitted by law to perform for the Company. Present members are Chairman Richard K. Smith, David J. D'Antoni and William J. Lhota. Based on a recommendation of the Audit Committee, the Board has designated Richard K. Smith as the "Audit Committee Financial Expert." The Audit Committee held eight meetings during 2003. See also "Report of the Audit Committee" contained

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elsewhere in this Proxy Statement.

The Compensation Committee is charged with several responsibilities, including: 1) administering the Company's 2000 Stock Option Plan and 1991 Stock Option Plan; 2) evaluating and approving the compensation, fringe benefits and perquisites provided to the Company's executive officers and adopting compensation policies applicable to the Company's officers; and 3) evaluating the compensation provided to the members of the Board and its committees. Present members of such committee are Chairman William J. Lhota, David J. D'Antoni, and Richard K. Smith. See also "Compensation Committee Report" contained elsewhere in this Proxy Statement. The Compensation Committee held four meetings during 2003.

The Nominating Committee is charged with several responsibilities, including: 1) selecting nominees for election as directors; 2) reviewing the performance of the Board; and 3) annually reviewing and recommending to the Board changes to the Company's Corporate Governance Guidelines. The members of the Nominating Committee are Chairperson S. Elaine Roberts, William J. Lhota, and Paul S. Williams. This Committee met seven times in 2003.

The Nominating Committee will set the minimum qualifications for persons whom it would recommend for nomination for election or re-election (election and re-election are hereafter collectively referred to as "election") as a director of the Company, which minimum qualifications are described in the Nominating Committee's charter. The following matters will be considered in the Nominating Committee's selection of a person to recommend for nomination as a director of the Company: such person's status as independent (based on the then current NASDAQ rules); business or professional skills and experience; temperament; integrity; educational background; and judgment. The objective of the Nominating Committee in this regard is to nominate for election as directors persons who share the values of the Company and possess the following minimum qualifications: high personal and professional integrity; the ability to exercise sound business judgment; an inquiring mind; professional demeanor, and the time available to devote to Board activities and the willingness to do so. The Nominating Committee will consider these criteria in the context of an assessment of

7

the perceived needs of the Board as a whole and will seek to achieve diversity of occupational and personal backgrounds. Ultimately, the Nominating Committee's intention is to select nominees for election to the Board whom the Nominating Committee believes will be effective, in conjunction with the other members of the Board, in collectively serving the long-term interests of the shareholders. In the context of recommending an incumbent director to be nominated for election to the Board, the Nominating Committee will focus its assessment on the contributions of such person during his or her Board tenure and such person's independence at that time.

Based on the criteria described above, the Nominating Committee will recommend to the Board nominees for election to the Board at each annual shareholders meeting and at any other shareholders meeting held for the election of one or more directors.

In addition to incumbent directors who will be evaluated for re-nomination as described above, the Nominating Committee may maintain a list of other potential candidates whom the Nominating Committee may evaluate pursuant to the criteria set forth above for consideration as Board members. By following the procedures set forth below, shareholders may recommend potential candidates to be included on this list. As a matter of policy, the Nominating Committee will consider and evaluate such candidates recommended by shareholders in the same manner as all other candidates for nomination to the Board who are not incumbent

directors.

In the absence of extraordinary circumstances, when a director vacancy arises for any reason, the Nominating Committee will use the following process to identify the person(s) whom the Nominating Committee will recommend to the Board for election as a director to fill such vacancy(ies). The Nominating Committee will first look to the list of names of potential nominees, as described above, and make a preliminary evaluation of such person(s) based on the criteria set forth above. If there are no names on the list or if all of the names on this list are eliminated following such evaluation process, the Nominating Committee may solicit other potential nominees' names from other directors of the Company, directors of the Company's parent, the Chairman or other persons whom the Nominating Committee reasonably believes would have the opportunity to possess first hand knowledge of a suitable candidate based on the criteria described above. The Nominating Committee may also hire a director search firm, as contemplated below.

Once the Nominating Committee has preliminarily concluded that a person(s) may meet the criteria described above, the Nominating Committee will, at a minimum, obtain from such person(s) a completed Prospective Director Questionnaire which shall solicit information regarding the person's business experience, educational background, personal information, and information relating to the person's business, personal or family relationships with the Company and other directors, among other matters. Following a review of such completed Prospective Director Questionnaire by the Nominating Committee, the Chairman and counsel for the Company, the Nominating Committee will conduct at least one interview with a person(s) whose candidacy it desires to pursue. Based on all information secured from the prospective nominee, which will include a background check and a criminal record check, the Nominating Committee will meet and decide whether or not to recommend such person(s) for nomination for election as a director of the Company. Any decision by the Committee in this regard will reflect its considered judgment of the person(s) being able to fulfill the objectives outlined above.

The Company has adopted procedures by which shareholders may recommend individuals for membership to the Board. As described in its charter, it is the policy of the Nominating Committee to

consider and evaluate candidates recommended by shareholders for membership on the Board in the same manner as all other candidates for nomination to the Board who are not incumbent directors. If a shareholder desires to recommend an individual for Board membership, then that shareholder must provide a written notice to the Secretary of the Company at 518 East Broad Street, Columbus, Ohio 43215 (the "Recommendation Notice"). For a recommendation to be considered by the Nominating Committee, the Recommendation Notice must contain, at a minimum, the following: the name and address, as they appear on the Company's books, and telephone number of the shareholder making the recommendation, including information on the number of shares owned; and if such person is not a shareholder of record or if such shares are owned by an entity, reasonable evidence of such person's ownership of such shares or such person's authority to act on behalf of such entity; the full legal name, address and telephone number of the individual being recommended, together with a reasonably detailed description of the background, experience and qualifications of that individual; a written acknowledgement by the individual being recommended that he or she has consented to that recommendation and consents to the Company's undertaking of an investigation into that individual's background, experience and qualifications in the event that the Nominating Committee desires to do so; the disclosure of any relationship of the individual being recommended with the Company or any of its subsidiaries or affiliates, whether direct or indirect; and, if known to the

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shareholder, any material interest of such shareholder or individual being recommended in any proposals or other business to be presented at the Company's next annual meeting of shareholders (or a statement to the effect that no material interest is known to such shareholder).

As of April 12, 2004, the Company had not received any such recommendations from shareholders for nominees for the Board.

The Investment Committee oversees the investment functions of the Company and its insurance subsidiaries. The members of the Investment Committee are Chairman Urlin G. Harris, Jr., Paul W. Huesman, S. Elaine Roberts, and Richard K. Smith. This Committee met four times in 2003.

The standing Independent Committee principally serves to review inter-company transactions between or among the Company and its subsidiaries and State Auto Mutual and its subsidiaries. This Committee also helps determine which entity, the Company or State Auto Mutual, is best suited to take advantage of transactional opportunities presented by a third party. The members of the standing Independent Committee are Chairman David J. D'Antoni, Paul S. Williams, and S. Elaine Roberts. This Committee only meets as needed, which was one time in 2003.

As further described in the Company's Corporate Governance Guidelines, the Company provides a process by which security holders may send communications to the Board. Any security holder who desires to communicate with a director of the Company may send such communication to any or all directors through the Secretary of the Company, John Lowther, by e-mail to Mr. Lowther at John.Lowther@stateauto.com or in writing to Mr. Lowther at the home office, 518 East Broad Street, Columbus, Ohio 43215. Security holders should designate whether such communication should be sent to a specific director or to all directors. Mr. Lowther is responsible for forwarding such communication to the director or directors so designated by the security holder.

The Company's Corporate Governance Guidelines also provide that directors are expected to attend the Company's annual meetings of shareholders. All of the directors of the Company who were directors last year attended last year's annual meeting of shareholders.

9

Since 2002, the Board has met in executive session, without management present, prior to each regular quarterly Board meeting. During 2003, there were four such executive sessions. The Board's policy in regard to the role of chair for each of these sessions is that it would rotate among the various committee chairs. The persons who led these meetings during 2003 were Mr. Lhota, Mr. D'Antoni, Ms. Roberts and Mr. Harris. In 2004, the Company's Corporate Governance Guidelines and the NASDAQ Marketplace Rules changed, requiring at least two executive sessions of the Board annually, at which only independent directors are present. The Board intends to comply with these new rules in 2004.

COMPENSATION OF DIRECTORS

Directors of the Company who are not also officers of the Company receive from the Company an annual fee of \$20,000, plus travel expenses incurred in attending directors meetings, and a fee of \$500, plus travel expenses, for each committee meeting attended. In addition to the foregoing, each committee chair receives an additional \$5,000 annual retainer (up to a maximum of \$5,000 even if a director chairs more than one committee). The Company pays \$500, plus travel expenses, for attending a special board meeting. In addition, there has been a Special Independent Committee in place to address issues created by the attempted takeover of the Company by Gregory M. Shepard. The chair of the

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Special Independent Committee receives \$1,000 per meeting. Directors may defer all or a portion of these fees under the Company's deferred compensation plan for directors. In addition, directors of the Company who are not full-time employees of the Company or its parent or subsidiary corporations receive stock options pursuant to the 2000 Directors Stock Option Plan. Under this plan, promptly following each annual meeting of shareholders of the Company, each eligible director is granted a non-qualified option to purchase 4,200 Common Shares of the Company at the fair market value of such shares on the last trading day prior to the annual meeting. Options are immediately exercisable in whole or in part and must be exercised within ten years of the date of grant. A director's compliance with the Stock Ownership Guidelines is a condition to his or her eligibility for receipt of options under this plan.

COMPENSATION OF EXECUTIVE OFFICERS

Pursuant to the 2000 Management Agreement (see "Certain Transactions" on page 26), the executive officers of the Company, State Auto P&C, Milbank, and National, as well as every other person providing services to these companies, are employees of State Auto P&C rather than State Auto Mutual, while State Auto Mutual acts as the common paymaster and common agent. The costs and expenses associated with these employees of State Auto P&C are reimbursed to State Auto Mutual, as paymaster, in accordance with the terms of the 2000 Management Agreement. See "Certain Transactions" below.

10

SUMMARY OF CASH AND CERTAIN OTHER COMPENSATION

Set forth below is information concerning the compensation paid or accrued by, or reimbursed to, State Auto Mutual for the Company's fiscal years ended December 31, 2003, 2002, and 2001, to the Company's chief executive officer and its four most highly compensated executive officers, other than the chief executive officer:

SUMMARY COMPENSATION TABLE

NAME AND PRINCIPAL POSITION	YEAR	ANNUAL COMPENSATION		LONG TERM	ALL OTHER
		SALARY (1)	BONUS (2)	COMPENSATION AWARDS	
				SECURITIES UNDERLYING OPTIONS GRANTED (3)	COMPENSATION (4)
Robert H. Moone.....	2003	\$484,000	\$ 29,111	48,000	\$17,770
Chairman, President and	2002	\$440,000	\$287,445	27,500	\$16,230
Chief Executive Officer	2001	\$400,000	\$256,298	24,100	\$14,830
Mark A. Blackburn.....	2003	\$231,231	\$ 14,070	14,500	\$ 906
Senior Vice President	2002	\$220,220	\$ 85,012	10,400	\$ 906
	2001	\$197,892	\$ 50,314	9,100	\$ 906
Steven J. Johnston.....	2003	\$264,507	\$ 16,018	14,500	\$ 9,069
Senior Vice President,	2002	\$235,155	\$ 94,806	11,600	\$ 6,803
Treasurer and	2001	\$189,860	\$ 44,345	9,200	\$ 6,063
Chief Financial Officer					
John R. Lowther.....	2003	\$226,893	\$ 13,773	14,500	\$ 7,960
Senior Vice President,	2002	\$214,049	\$ 82,282	10,200	\$ 7,236
Secretary and General	2001	\$174,036	\$ 69,721	7,900	\$ 6,639

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Counsel					
Steven R. Hazelbaker.....	2003	\$225,000	\$ 13,863	4,500	\$ 7,858
Vice President	2002	\$225,000	\$ 2,388	5,000	\$ 6,663
	2001	\$ 131,250	--	--	\$ 4,933

(1) Includes amounts deferred pursuant to the State Auto Insurance Companies Capital Accumulation Plan (the "CAP") and the Non-Qualified Incentive Deferred Compensation Plan (the "Deferred Compensation Plan"). The CAP is a defined contribution plan (within the meaning of the Employee Retirement Income Security Act of 1974) ("ERISA") and is intended to be a qualified plan under Sections 401(a) and 401(k) of the Internal Revenue Code of 1986, as amended (the "Code"). Under the CAP, each participant is eligible to enter into a written salary reduction agreement with the participant's employer whereby the participant's salary will be reduced by a whole percentage from 1% to 50%, as elected by the participant, in accordance with the rules governing cash or deferred arrangements under Section 401(k) of the Code. The amount deferred by a participant is contributed by his or her employer to the trust fund for the CAP and invested in accordance with the election of the participant from among investment funds established under the trust agreement, including the Common Shares. The Deferred Compensation Plan is a non-qualified, unfunded deferred compensation plan for eligible key employees who are legally precluded from contributing a full 6% of compensation to the CAP or who

11

choose to defer a portion of their salary beyond the amount matched by the CAP. Under the Deferred Compensation Plan, such employees are eligible to enter into a salary reduction agreement to defer payment of an additional portion of the employee's salary as the employee prescribes on an election form executed annually in advance of the year in which such compensation would be earned. The total amount of salary deferred under the CAP and the Deferred Compensation Plan cannot exceed in the aggregate 50% of salary. Deferred amounts, along with the Company matching amounts on that portion deferred that is eligible for the match (see footnote (4), below), are invested by State Auto P&C in a variety of investment options made available to participants in the Deferred Compensation Plan pursuant to the terms of such plan.

(2) The amounts appearing in this column represent bonuses paid pursuant to the State Auto Quality Performance Bonus Plan (the "QPB"). Under the QPB for 2003, quarterly bonuses were paid to employees who had completed two full calendar quarters of service if the direct statutory combined ratio for such quarter was 100% or less for all combined affiliated insurers.

Also included in this column are special incentive bonuses earned in 2002 and 2001 under special incentive bonus plans recommended by the Chief Executive Officer and approved by the Compensation Committee for Mr. Johnston, Mr. Blackburn, and Mr. Lowther. While similar plans were in place for 2003, the amounts of those bonuses were not determined as of the date this Proxy Statement was printed. The Compensation Committee also had in place special incentive bonus plans for Mr. Moone in 2003, 2002 and 2001. The bonus shown for Mr. Moone for 2002 and 2001 includes the special bonus

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earned in each such year. The 2003 incentive bonus for Mr. Moone has not been determined as of the date this Proxy Statement was printed (see "Compensation Committee Report").

- (3) In each year noted, the persons listed in the Summary Compensation Table were granted options to purchase the number of Common Shares of the Company set forth in this column pursuant to the Company's 2000 Stock Option Plan.
- (4) The amounts appearing in this column represent the Company's contributions and credits on behalf of each named person under the CAP or the Deferred Compensation Plan. Each participant in the CAP is credited annually with his or her allocable share of employer matching contributions made to the CAP from the consolidated net accumulated or current earnings of State Auto P&C and its affiliates. A participant's share of the matching contribution equals 75% of his or her salary reduction contributions up to 2% of compensation, plus 50% of his or her salary reduction contributions from 3% to 6% of compensation. While a participant is always vested in his or her own salary reduction contributions, the rights of a participant to amounts credited to his or her account as matching contributions vest as follows: (a) one-third of matching contributions allocated for the plan year preceding the plan year in which termination of employment occurs, two-thirds of matching contributions allocated for the second plan year before the plan year in which termination of employment occurs, and 100% of the matching contributions allocated for the third and earlier plan years before the plan year in which termination of employment occurs; and (b) notwithstanding the foregoing, after the participant has completed three or more years of service with State Auto P&C and its affiliates, all matching contributions become vested. The following are the amounts of the Company matching contributions under the CAP for 2003 for the officer indicated: Mr. Moone -- \$7,000; Mr. Johnston -- \$7,000; Mr. Lowther -- \$7,000; and Mr. Hazelbaker -- \$7,000. Each employee who is eligible to participate in the Deferred Compensation Plan is credited annually with his or her allocable share of Company matching contributions on the same basis that contributions are

12

matched under the CAP, provided that no more than 6% of any employee's salary is subject to being matched under either the CAP or the Deferred Compensation Plan. The following amounts reflect the Company's contribution to the Deferred Compensation Plan for 2003: Mr. Moone -- \$9,940; Mr. Johnston -- \$1,416; and Mr. Lowther -- \$288. The amounts appearing in this column also represent the premiums for policies of whole life insurance purchased on behalf of the officers of the Company, including the executive officers named above. The following amounts represent the premiums paid for whole life insurance for 2003: Mr. Moone -- \$830; Mr. Johnston -- \$653; Mr. Blackburn -- \$906; Mr. Lowther -- \$672; and Mr. Hazelbaker -- \$858.

OPTION GRANTS IN LAST FISCAL YEAR

The following table shows the number of options granted in 2003 to the individuals named in the Summary Compensation Table and estimates the potential realizable value of these option grants.

INDIVIDUAL GRANTS	POTENTIAL	P
-----	REALIZABLE VALUE	REAL
NUMBER OF	AT ASSUMED	A
SECURITIES	ANNUAL RATES OF	ANNU
UNDERLYING	STOCK PRICE	ST
% OF TOTAL	APPRECIATION FOR	APPR
OPTIONS		
GRANTED TO		
EMPLOYEES		
EXERCISE		
OR BASE		

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NAME	OPTIONS GRANTED (1)	IN FISCAL YEAR	PRICE (\$/SH) (2)	EXPIRATION DATE	OPTION TERM 5% (\$) (3)	OP 1
Robert H. Moone.....	48,000	11.79%	\$18.74	05/21/2013	\$565,703	\$
Mark A. Blackburn....	14,500	3.56%	\$18.74	05/21/2013	\$170,890	\$
Steven J. Johnston...	14,500	3.56%	\$18.74	05/21/2013	\$170,890	\$
John R. Lowther.....	14,500	3.56%	\$18.74	05/21/2013	\$170,890	\$
Steven R. Hazelbaker.....	4,500	1.11%	\$18.74	05/21/2013	\$ 53,035	\$

(1) Options were granted on May 22, 2003. The options are fully exercisable in 1/3 increments over a three-year vesting period, so long as employment with the Company or its subsidiaries or its parent continues. There are no stock appreciation rights, performance units, or other instruments granted in tandem with these options, nor are there any reload provisions, tax reimbursement features or performance-based conditions to exercisability.

(2) The option exercise price is the closing price of the Company's shares on the NASDAQ National Market System on the day of the grant.

(3) The dollar amounts under these columns are the result of calculations at the 5% and 10% rates dictated by the Securities and Exchange Commission when the "Potential Realizable Value" alternative is used and are not intended to be a forecast of the Company's stock price.

AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND FISCAL YEAR END OPTION VALUES

The following table sets forth stock option exercises during 2003 by the executive officers named in the Summary Compensation Table and shows the number of Common Shares represented by both exercisable and non-exercisable stock options and the value of in-the-money stock options

13

(exercisable and non-exercisable) held by each of the named executive officers as of December 31, 2003.

NAME	SHARES ACQUIRED ON EXERCISE (#)	VALUE REALIZED (\$) (1)	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS AT FY-END (#) EXERCISABLE/ UNEXERCISABLE	VALUE OF UNEXERCISED IN-THE-MONEY OPTIONS AT FY-END (\$) EXERCISABLE/ UNEXERCISABLE
Robert H. Moone(3).....	-0-	-0-	152,812/74,368	\$1,916,909/41
Mark A. Blackburn.....	-0-	-0-	22,732/24,468	\$ 228,127/13
Steven J. Johnston.....	2,800	\$ 32,116	61,698/25,302	\$ 779,419/14
John R. Lowther(4).....	13,500	\$161,258	57,966/23,934	\$ 757,183/13
Steven R. Hazelbaker...	-0-	-0-	1,666/7,834	\$ 12,228/4

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- (1) Aggregate market value of the Common Shares covered by the option less the aggregate price paid by the executive officer.
- (2) The value of in-the-money options was determined by subtracting the exercise price from the market value of the Company's Common Shares as of December 31, 2003 (\$23.34), based on the closing price of the Company's Common Shares on the NASDAQ National Market System on that date, the last trading day of 2003.
- (3) 38,190 of the options indicated as exercisable at fiscal year end have been assigned to the living trust of Mr. Moone's spouse of which he is the co-trustee.
- (4) 6,500 of the options indicated as exercisable at fiscal year end have been assigned to Mr. Lowther's spouse and 2,000 of such options have been assigned to trusts maintained for the benefit of Mr. Lowther's children.

EMPLOYEES' RETIREMENT PLAN

During 2003, the executive officers named in the Summary Compensation Table, as well as substantially all employees of State Auto P&C, were eligible to participate in the State Auto Insurance Companies' Employee Retirement Plan (the "Retirement Plan"). The Retirement Plan is a defined benefit plan (within the meaning of ERISA) which is intended to be a qualified plan under Section 401(a) of the Code, and is subject to the minimum funding standards of Section 412 of the Code. Benefits payable under the Retirement Plan are funded through employer contributions to a trust fund.

In addition, the executive officers named in the Summary Compensation Table benefited in 2003 from a non-qualified Amended and Restated Supplemental Executive Retirement Plan (the "Supplemental Plan"). The Supplemental Plan is intended to offset the impact of the Code's and ERISA's limitations on retirement benefits available under the Retirement Plan by providing for a lump sum or deferred cash payments in an actuarially determined amount upon retirement of officers whose participation in the Supplemental Plan is approved by the Board of Directors of State Auto Mutual.

14

The table below shows estimated annual benefits payable under the Retirement Plan and the Supplemental Plan to a participant upon retirement at age 65 with indicated average annual compensation and period of service:

ESTIMATED ANNUAL RETIREMENT BENEFIT

ANNUAL AVERAGE COMPENSATION	ANNUAL RETIREMENT BENEFIT BASED ON YEARS OF SERVICE				
	15 YEARS	20 YEARS	25 YEARS	30 YEARS	35 YEARS
\$125,000	\$42,197	\$53,629	\$ 65,062	\$ 76,494	\$ 87,876
\$150,000	\$50,431	\$64,399	\$ 78,368	\$ 92,336	\$106,242
\$175,000	\$53,965	\$70,470	\$ 86,974	\$103,479	\$119,917
\$200,000	\$56,544	\$75,584	\$ 94,625	\$113,665	\$136,639
\$225,000	\$59,122	\$80,699	\$102,275	\$123,852	\$145,360
\$250,000	\$61,700	\$85,813	\$109,925	\$134,038	\$158,082
\$300,000	\$64,690	\$91,742	\$118,795	\$145,848	\$172,831
\$400,000	\$64,690	\$91,742	\$118,795	\$145,848	\$172,831
\$450,000	\$64,690	\$91,742	\$118,795	\$145,848	\$172,831

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\$500,000 \$64,690 \$91,742 \$118,795 \$145,848 \$172,831

Note: The annual average compensation applies to post-1988 salaries. Post-1988 salaries have been capped according to the Internal Revenue Code. Benefit amounts are based on the straight life annuity and are not subject to offset by Social Security.

Benefits shown above are computed as a straight single life annuity beginning at age 65. Such amounts are not subject to offset for Social Security benefits or other amounts payable to participants in the Retirement Plan. As of December 31, 2003, the years of credited service to the nearest whole year and annual average compensation for each of the named executive officers in the Summary Compensation Table actively participating in the Retirement Plan on such date were as follows:

NAME OF INDIVIDUAL -----	YEARS OF CREDITED SERVICE -----	CURRENT ANNUAL AVERAGE COMPENSATION FOR PURPOSES OF RETIREMENT PLAN -----
Robert H. Moone.....	33	\$200,000
Mark A. Blackburn.....	4	\$200,000
Steven J. Johnston.....	18	\$200,000
John R. Lowther.....	17	\$200,000
Steven R. Hazelbaker.....	9	\$200,000

EMPLOYMENT CONTRACTS AND CHANGE-IN-CONTROL ARRANGEMENTS

EMPLOYMENT AGREEMENT WITH MR. MOONE

Robert H. Moone, the Company's Chairman, President, and Chief Executive Officer, has entered into an Employment Agreement with the Company, with the current term continuing through December 31, 2005, or until his earlier death or disability, or upon earlier termination by either Mr. Moone or the Company as permitted by the agreement. The Employment Agreement may be renewed at the end of the current term for one additional two-year term with the mutual consent of

the parties. If Mr. Moone does not desire to renew the agreement in December 2005, while State Auto does, then that shall be a voluntary termination of Mr. Moone's employment. On the other hand, if Mr. Moone desires to renew the agreement in December 2005, but State Auto does not, then that shall be an involuntary termination of Mr. Moone's employment. Mr. Moone's Employment Agreement provides that his annual rate of compensation will not be less than