

Keystone Large Deductible Alternative – Detailed Product Overview

I. Features of the Segregated Cell Large Deductible Alternative:

- ✚ Fully Insured Plan
- ✚ Contractual Return of Underwriting Profit & Investment Income
- ✚ Ability to Unbundle Claims and Risk Management Services
- ✚ Reduce Reliance on Customer Provided Letters of Credit & Eliminate “Stacking”
- ✚ Stable Long Term Cash Flow
- ✚ Tailored, Multi Year Solutions
- ✚ Innovative Financing of Wealth Accumulation & Estate Planning
- ✚ Comprehensive Quarterly Financial Reporting Package
- ✚ Potential Tax Deductibility for Qualifying Structures
- ✚ Individual “Protected Cells” Established for Each Participant
- ✚ Legal Segregation of Customer Assets & Liabilities
- ✚ Access to Proprietary Claims & Risk Mitigation Platform.

II. Technical overview of the product:

Keystone Risk Partners (Keystone) has developed a fully insured product designed to lower the ultimate cost of insurance and provide unique benefits to privately held businesses.

This product will involve two (2) policies both issued by the same insurance carrier and will combine the inherent flexibility of a large deductible policy with a uniquely crafted second policy called a Deductible Reimbursement Policy or DRP. This DRP is highly customized to satisfy the traditional large deductible obligations including collateral requirements, claims escrow and paid loss reimbursement. At its core, the product presents the insured with a “first dollar” insurance program, an opportunity to receive both underwriting profit & investment income and the exclusive ability to tailor the long term funding of their future insurance obligations.

In this coordinated approach, Keystone will provide its agents and their larger insureds with the following comprehensive, dual policy structure:

Policy # 1, the large deductible contract, will be provided by Am Best Rated “A Excellent - XV” insurance carrier (the Carrier). The flexibility of this contract enables the premium of the policy to be tailored to the client’s desired retention and contain the majority of the program’s expenses. The primary objective of Policy #1 is to provide evidence of highly rated insurance in all states of exposure as well as provide catastrophic loss protection excess of the client’s per occurrence retention.

In order for the Carrier to issue a large deductible policy and in return for the substantial premium credit offered under this contract, the insurer must make arrangements to secure the credit risk for ultimate loss obligations under their policy. Traditional large deductible plans require a letter of credit from the customer to meet this prerequisite which tends to grow or “stack” with successive renewals of a typical program.

Under the Keystone approach, this requirement is addressed through a premium remitted to a second policy as follows:

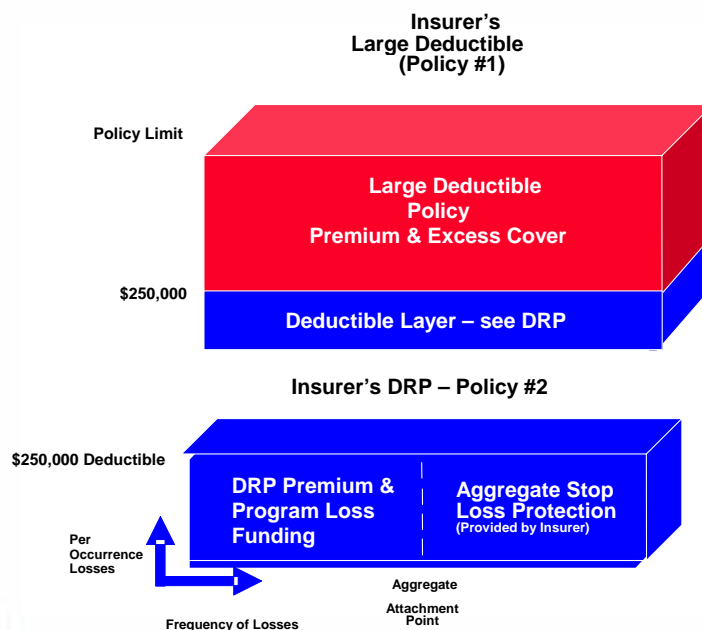
Policy #2 – The DRP, also issued by the Carrier, will satisfy the large deductible obligations, eliminate the cash flow variability of reimbursing the TPA for monthly paid claims as well as provide for an aggregate stop loss to limit the insured’s obligations in the deductible layer. This policy will be issued with an occurrence limit equal to the client’s selected large deductible retention and provide unlimited coverage for losses incurred under Policy #1.

The DRP policy will allow the insured to participate in a portion of their own risk by reinsuring the customer’s aggregate retention to a protected cell captive insurance company (Captive). This will result in the movement of a substantial portion of the DRP premium (referred to as *loss fund*) to the Captive. As part of this transaction, the Captive will in turn establish a separate account with individual banking and financial reporting to legally partition the program. The assets of this separate account will only be used to satisfy the insured’s current and future aggregate liabilities assumed under this dual policy approach.

The premium for DRP will be individually negotiated and centered on the expected losses, DRP policy expenses and liquidity needs for current liabilities (funding TPA escrows and the first 12 months of paid loss obligations). DRP premiums can be audited on a composite rate basis or issued flat, not subject to audit. Finally, DRP premiums can be remitted on an installment basis subject to the credit rating of the insured.

Under the DRP, all program loss fund, not used to pay losses or DRP expenses, will earn investment income. The amount of investment income will depend on the flow of funds and interest rates. In addition, one of the major features of the program is that loss fund held in the insured’s separate account, not used to pay losses or collateralize the Carrier, may be used to satisfy future program years or be returned as a dividend distribution to the program beneficiary.

III. Policy Retention Schematic:

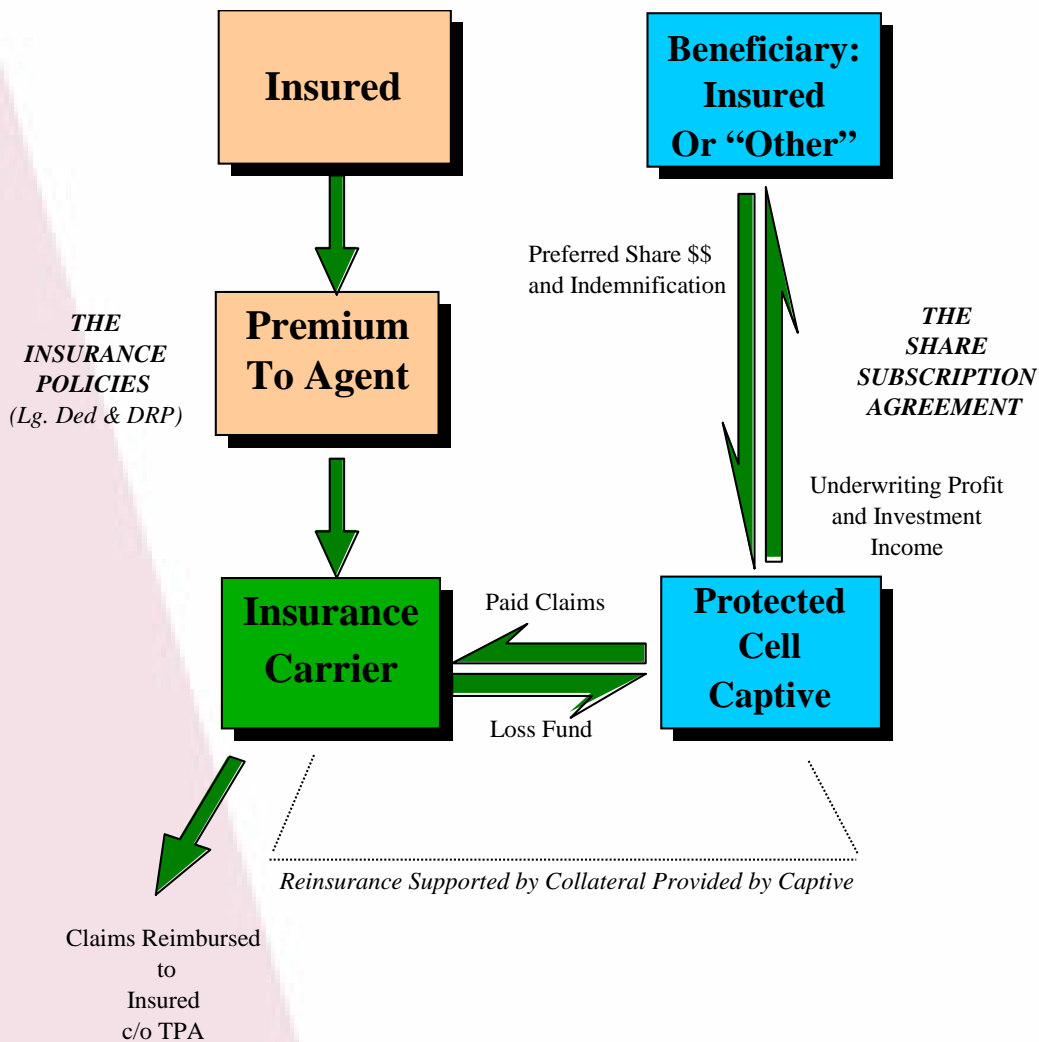


IV. Contractual Return of Profits – Share Subscription Agreement:

In order to participate in a portion of the risk and to gain access to the underwriting profit and investment income (dividends) generated by the program, the insured or the designated beneficiary will enter into a share subscription agreement with the protected cell captive. This agreement defines the relationship between the insured and captive by identifying the program beneficiary (preferred shareholder), the timing of distributions, security and indemnification provisions. As consideration for executing this agreement, the preferred shareholder will be required to purchase a non-voting series of preferred shares to discretely identify their separate account.

An important aspect of the series of preferred shares is the flexibility they present in receiving program distributions. Under the terms of the share subscription agreement, a distribution can be paid as a dividend from the preferred shares or the cell captive can repurchase the shares for the value of the net assets held in the program. This may provide some future strategic or tax benefit to the program beneficiary.

V. Relationship of the Parties Schematic:



VI. Program Summary:

The Keystone Large Deductible Alternative is designed to offer benefits not commonly found in traditional large deductible offers:

Underwriting Profit - Underwriting profit defined as DRP premium, less plan expenses, less ultimate losses, will be returned to the participant. It is important to note that there is no sharing of risk among programs; underwriting profit is determined solely by each program's own loss experience.

Investment Income - Investment income is earned on all cash funds held in the Preferred Shareholders' separate account, including case reserves, and is likewise returned to participants.

Premium Deductibility - As a general rule, premiums paid to an insurer are deductible as an ordinary and necessary business expense. However, since various factors could affect the tax treatment of the program, no assurance can be given as to the tax consequences of participating in a protected cell captive program. Insured's should consult with tax professionals in this area.

Financial Safeguards – the program is designed to provide the maximum in financial security with all relationships among the parties being contractual in nature. Additionally, a protected cell captive (segregated cell structure) differs from traditional rent-a-captive structures in that the participants are legally partitioned into separate accounts which are not combinable by charter. Finally, the obligations of the separate account to the large deductible policy-issuing carrier are internally secured by a clean, irrevocable letter of credit, issued by a member bank of the U.S. Federal Reserve System.

Documentation – Participants receive comprehensive documentation and financial reporting services. Every participant receives quarterly financial statements, including a balance sheet, income statement and policy year summaries, of their individual program. Additionally, the protected cell captive will publish an annual, independently-audited financial statement which will be made available to all participants.

Access to Keystone's risk mitigation platform - designed to *significantly reduce* workers compensation claims this platform implements an innovative coordination of claims and strategic medical management vendors. The results include a dramatic impact on Direct Costs (medical and indemnity payments) while managing Indirect Costs such as Benefit Delivery Services (medical management and legal) and Claim Closure rates. This product also provides proprietary Benchmarking & Assessment Tools to measure the effectiveness of claim interventions (e.g. return to work, medical case management etc.) against related metrics and to monitor ongoing performance.

Wealth Accumulation & Estate Planning – Another unique benefit of this program for privately held or family businesses is the ability to develop an independent profit center designed to fund wealth accumulation strategies or fund estate planning objectives of the owners. The key to this feature is the structure and selection of the preferred shareholder under the share subscription agreement.

Appendix I - Sample Comparison to Traditional Large Deductible:

A) Year One Cash Flows:

	Traditional Large Deductible Offer		The Keystone Large Deductible Alternative		Variance Rate/\$100
I. PROGRAM EXPOSURE					
Insured Payroll	\$ 75,000,000	Rate/\$100	\$ 75,000,000	Rate/\$100	0%
Insured Standard Premium Equivalent	\$ 2,000,000	2.67	\$ 2,000,000	2.67	0%
II. PROGRAM RISK RETENTION					
Per Occurrence	\$ 350,000		\$ 350,000		
Aggregate Stop Loss	\$ 3,000,000	4.00	\$ 2,000,000	2.67	-33%
Estimated Expected Losses	\$ 1,000,000	1.33	\$ 1,000,000	1.33	0%
III. PROGRAM CASH FLOW & SECURITY - Year 1 Commitments					
Expense & Security Commitments					
Program Expenses	\$ 500,000	0.67	\$ 550,000	0.73	
Deductible Reimbursement Loss Fund	\$ -	0.00	\$ 1,450,000	1.93	
Total Gross Premium	\$ 500,000	0.67	\$ 2,000,000	2.67	
Less Tax Deduction (@ 40%)*	\$ (200,000)	-0.27	\$ (800,000)	-1.07	
Net Premium Cash Flow	\$ 300,000	0.40	\$ 1,200,000	1.60	300%
Plus Program Collateral Requirements:	\$ 1,000,000	1.33	\$ -	0.00	
Estimated Paid Loss Reimbursements (year 1)	\$ 200,000	0.27	<i>Included</i>	0.00	
Less Tax Deduction (@ 40% of Paid losses)	\$ (80,000)	-0.11	\$ -	0.00	
Total Commitments - program year 1	\$ 1,420,000	1.89	\$ 1,200,000	1.60	-15%

B) Ultimate Cost Comparison:

	Traditional Large Deductible Offer		The Keystone Large Deductible Alternative		Variance Rate/\$100
Net Present Value of Plan Expenses & Losses:					
Total Gross Expenses	\$ 500,000	0.67	\$ 550,000	0.73	
Less NPV of Investment Income**	\$ (94,027)	-0.13	\$ (197,587)	-0.26	
Net Expenses	\$ 405,973	0.54	\$ 352,413	0.47	-13%
Plus Ultimate Losses	\$ 1,000,000	1.33	\$ 1,000,000	1.33	
Less NPV of Tax Deduction**	\$ (522,954)	-0.70	\$ (698,349)	-0.93	
Net Ultimate Cost of Risk	\$ 883,019	1.18	\$ 654,064	0.87	-26%

*Tax deduction assumes qualifying structure

**NPV for simplicity is based on a 5% rate of return, 12% discount rate and an equal payout of losses over a 60 month horizon

C) Multi Year Program View:

	Year 1	Year 2	Year 3	Year 4	Year 5	TOTAL
Annual Premium	2,000,000	2,000,000	2,000,000	2,000,000	2,000,000	10,000,000
<i>Less Annual Program Expenses</i>	(550,000)	(550,000)	(550,000)	(550,000)	(550,000)	(2,750,000)
<i>Less Paid Losses - Policy Year 1</i>	(200,000)	(200,000)	(200,000)	(200,000)	(200,000)	(1,000,000)
<i>Less Paid Losses - Policy Year 2</i>	-	(200,000)	(200,000)	(200,000)	(200,000)	(800,000)
<i>Less Paid Losses - Policy Year 3</i>	-	-	(200,000)	(200,000)	(200,000)	(600,000)
<i>Less Paid Losses - Policy Year 4</i>	-	-	-	(200,000)	(200,000)	(400,000)
<i>Less Paid Losses - Policy Year 5</i>	-	-	-	-	(200,000)	(200,000)
Available Loss Fund	1,250,000	1,050,000	850,000	650,000	450,000	4,250,000
Plus Investment Income	43,665	104,351	157,909	203,975	242,166	752,066
					Total Cash Position @ 60 months	5,002,066
					<i>Less Remaining Case Reserves/IBNR</i>	(2,000,000)
					Net Equity @ 60 months	3,002,066

Assumptions:

Annual premium and program expenses are the same for all years.

Loss pay out pattern (% of ultimate losses): 20% per year for simplicity of illustration

Investment income illustrated at 5% average return

Appendix II – Protected Cell Captives

Alternative risk financing solutions involving protected cell captives often referred to as rent-a-captive companies are designed to provide insureds with the benefits associated with a wholly-owned captive insurance company, without the capitalization and administrative requirements. Protected cell programs can be structured for individual corporations, associations or agency-designed groups all with a single underlying idea: to capture the return of underwriting profit and investment income normally retained by the traditional insurer as well as provide for a long term stable insurance solution. These programs are most effective for lines of insurance with frequent and predictable losses that are suitable for self funding including workers compensation, auto liability and general liability.