PUBLIC VERSION

UNITED STATES OF AMERICA
BEFORE FEDERAL TRADE COMMISSION

| | | |
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| In the Matter of | ) | |
| | ) | |
| **Service Corporation International,** | ) | |
| a corporation, and | ) | Docket No. C-4174 |
| | ) | File No. 061-0156 |
| **Alderwoods Group, Inc.,** | ) | |
| a corporation | ) | |
| | ) | |

**PETITION FOR APPROVAL OF PROPOSED DIVESTITURES TO KEYSTONE NORTH AMERICA, INC.**

Pursuant to Section 2.41(f) of the Federal Trade Commission ("Commission") Rules of Practice and Procedure, 16 C.F.R. § 2.41(f) (2006), and Paragraph II.A. of the Decision and Order contained in the Agreement Containing Consent Orders accepted for public comment in this matter ("Decision and Order"), Respondent Service Corporation International ("SCI") hereby petitions the Commission to approve the divestiture to Keystone America, Inc. ("Keystone America"), a wholly-owned subsidiary of Keystone North America, Inc. ("Keystone"), of the Divestiture Businesses that include the following facilities:

- Hankins & Whittington-Dilworth Chapel, 1111 East Blvd., Charlotte, NC
- Bush River Memorial Gardens, 5400 Bush River Road, Columbia, SC
- Elmwood Cemetery, 501 Elmwood Avenue, Columbia, SC
- Southland Memorial Gardens, 700 W Dunbar Road, West Columbia, SC
- Caughman-Harman Funeral Home, 5400 Bush River Road, Columbia, SC

- Caughman-Harman Funeral Home, 820 West Dunbar Road, West Columbia, SC
- Diuguid Funeral Service, 811 Wiggington Road, Lynchburg, VA
- Diuguid Waterlick Chapel, 21914 Timberlake Road, Lynchburg, VA
- T.J. McGowan Sons Funeral Home, 71 North Central Highway, Garnersville, NY
- T.J. McGowan Sons Funeral Home, 133 Broadway, Haverstraw, NY
- Shaw & Sons Funeral Directors, Inc., 201 N. 2nd Street, Yakima, WA
- Glen Haven Memorial Gardens, 7070 Houston Road, Macon, GA
- Lambeth Troxler Funeral Home, 300 W. Wendover Avenue, Greensboro, NC

The Divestiture Businesses associated with these facilities (as defined in the Decision and Order, and hereinafter collectively referred to as the "Keystone Divestiture Assets") will be sold to Keystone pursuant to the Contingent Asset Sale Agreement dated October 30, 2006 (the "Sale Agreement"), by and among Keystone America and SCI Funeral Services, Inc. ("FSI"), a wholly-owned affiliate of SCI.[1] The executed Sale Agreement is attached hereto as Confidential Exhibit A.

<u>Background</u>

On October 13, 2006, SCI and Respondent Alderwoods Group, Inc. ("Alderwoods") (collectively, the "Respondents") executed an Agreement Containing Consent Orders that included the Decision and Order and an Order to Hold Separate and

[1] The Sale Agreement was initially "contingent" because, on the date that it was signed, SCI's acquisition of Alderwoods had not yet been consummated, and certain subsidiaries of Alderwoods owned and operated several of the Keystone Divestiture Assets. As a result, the Sale Agreement was subject to consummation of the SCI-Alderwoods Acquisition, and FSI was required to cause the subsidiaries that own the Keystone Divestiture Assets to join in the execution of the Sale Agreement within ten days following the consummation date. Now that SCI has completed its acquisition of Alderwoods, those subsidiaries have joined the agreement, as reflected in Confidential Exhibit A. The Sale Agreement also includes the Caughman-Harman Funeral Home locations at 503 North Lake Drive, Lexington, South Carolina, and 123 Columbia Road, Chapin, South Carolina. Keystone America and Keystone do not own any funeral homes in the relevant geographic market for these facilities, as defined by the Commission in the Complaint in this matter.

Maintain Assets (collectively, the "Consent Agreement") to settle the Commission's charges that the proposed acquisition by SCI of Alderwoods would violate Section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. § 45, and Section 7 of the Clayton Act, as amended, 15 U.S.C. § 18. On November 22, 2006, the Commission accepted the Consent Agreement for public comment, and on November 28, 2006, SCI consummated its acquisition of Alderwoods. Alderwoods is now a wholly-owned subsidiary of SCI. The Consent Agreement is presently before the Commission for final approval and issuance of the Decision and Order.

Because Confidential Exhibit A to this petition contains confidential and competitively sensitive business information relating to the divestiture of the Keystone Divestiture Assets — the disclosure of which may prejudice the Respondents and Keystone, cause harm to the ongoing competitiveness of the Keystone Divestiture Assets, and impair the Respondents' ability to comply with their obligations under the Consent Agreement — the Respondents have redacted Confidential Exhibit A from the public version of this petition. Pursuant to Sections 2.41(f)(4) and 4.9(c) of the Commission's Rules of Practice and Procedure, 16 C.F.R. §§ 2.41(f)(4) & 4.9(c) (2006), the Respondents request that the confidential version of this petition and the information contained herein be accorded confidential treatment under 5 U.S.C. § 552 and Section 4.10(a)(2) of the Commission's Rules of Practice and Procedure, 16 C.F.R. § 4.10(a)(2) (2006). The confidential version of this petition is also exempt from disclosure under Exemptions 4, 7(A), 7(B), and 7(C) of the Freedom of Information Act, 5 U.S.C. §§ 552(b)(4), 552(b)(7)(A), 552(b)(7)(B), & 552(b)(7)(C), and the Hart-Scott-Rodino Antitrust Improvements Act of 1976, as amended, 15 U.S.C. § 18a(h).

SCI desires to complete the proposed divestiture of the Keystone Divestiture Assets as soon as possible, following Commission approval thereof. All conditions other than Commission approval and any required state regulatory approval have already been satisfied, so that SCI through FSI and Keystone America are in a position to close the divestiture within a few days of such approval.[2]

Prompt consummation will further the purposes of the Decision and Order and is in the interests of the public, Keystone, and the Respondents, because it will allow Keystone to move forward with its business plans for the competitive operation of the Keystone Divestiture Assets. SCI accordingly requests that the Commission promptly commence the period of public comment pursuant to Section 2.41(f)(2) of the Commission's Rules of Practice and Procedure, 16 C.F.R. § 2.41(f)(2) (2006), limit the public comment period to the customary 30-day period, and grant this petition by approving the divestiture of the Keystone Divestiture Assets to Keystone pursuant to the above-referenced Sale Agreement as soon as practicable after the close of the public comment period.

## I. The Sale Agreement Is Final and Consistent with the Decision and Order's Terms

Paragraph II.A of the Decision and Order requires the Respondents to divest the Divestiture Businesses (as defined in the Decision and Order) within 180 days of November 28, 2006, the date on which SCI consummated its acquisition of Alderwoods. Pursuant to this

[2] Keystone is responsible for obtaining applicable state licensing as required to operate the Divestiture Assets. In Washington, New York, North Carolina, South Carolina and Virginia, there is no requirement for state approval of funeral home transfers prior to closing. In each of these states, the primary purpose of the approval is to allow Keystone to operate these funeral homes, rather than to allow SCI to transfer them to Keystone, and Keystone will be permitted to operate the funeral homes while the applications are pending. As a result, and consistent with industry practice, Keystone will submit these applications on or about the closing date. Keystone has submitted applications in Georgia and for cemeteries in South Carolina, where prior approval is required, and Keystone expects to receive approval of these applications prior to the expiration of the FTC's 30-day public comment period for this divestiture application.

requirement, SCI has diligently sought a buyer that would be acceptable to the Commission over several months preceding Commission action on the Consent Agreement, through an extensive auction process that produced great interest in the properties. On October 30, 2006, SCI caused FSI to enter into a Sale Agreement that requires SCI to sell the Keystone Divestiture Assets to Keystone America, the highest bidder.

The Sale Agreement with Keystone America complies with the requirements of Paragraph II of the Decision and Order:

A. Paragraph II.A. requires that Respondents divest the Keystone Divestiture Assets, absolutely and in good faith. Keystone America will acquire the Keystone Divestiture Assets pursuant to Section 1.1 of the Sale Agreement.

B. Paragraph II.B. requires that Respondents divest the divestiture assets in three geographic areas in South Carolina, Virginia and New York to no fewer than one buyer per group. The groups in question are as follows:

> *The South Carolina group* consists of two funeral homes and three cemeteries in Lexington/West Columbia/Columbia, South Carolina: (i) Caughman-Harman Funeral Home, 5400 Bush River Road, Columbia, South Carolina, (ii) Caughman-Harman Funeral Home, 820 West Dunbar Road, West Columbia, South Carolina, (iii) Bush River Memorial Gardens Cemetery, 5400 Bush River Road, Columbia, South Carolina, (iv) Elmwood Cemetery, 501 Elmwood Avenue, Columbia, South Carolina, and (v) Southland Memorial Gardens, 700 West Dunbar Road, West Columbia, South Carolina;
>
> *The Virginia group* consists of two funeral homes in Lynchburg, Virginia, those being: (i) Diuguid Funeral Service, 811 Wiggington Road, Lynchburg, Virginia,

and (ii) Diuguid Waterlick Chapel, 21914 Timberlake Road, Lynchburg, Virginia; and

*The New York group* consists of two funeral homes located in Northern Rockland County New York: (i) T.J. McGowan Sons Funeral Home, 71 North Central Highway, Garnerville, New York, and (ii) T.J. McGowan Sons Funeral Home, 133 Broadway, Haverstraw, New York.

The Sale Agreement contemplates that Keystone America will acquire all three of these groups, satisfying this requirement. In addition, Keystone America will acquire individual facilities in four other areas, constituting the sole divestiture assets in those areas, including: Hankins & Whittington-Dilworth Chapel, 1111 East Blvd., Charlotte, North Carolina; Shaw & Sons Funeral Directors, Inc., 201 N. 2nd Street, Yakima, Washington; Glen Haven Memorial Gardens, 7070 Houston Road, Macon, Georgia; and Lambeth Troxler Funeral Home, 300 W. Wendover Avenue, Greensboro, North Carolina.

* * *

As demonstrated above and in the accompanying Sale Agreement, SCI has caused FSI to enter into an agreement relating to the sale of the Keystone Divestiture Assets that fully complies with the Commission's Decision and Order. Accordingly, the Respondents hereby seek Commission approval of the proposed divestitures pursuant to Paragraph II.A. of the Decision and Order.

## II. The Proposed Acquirer Will Be a Strong and Effective Competitor

Keystone has extensive experience in acquiring and operating funeral homes and cemeteries, and Keystone possesses the financial wherewithal to make this acquisition. The acquisition will assure that the Keystone Divestiture Assets remain strong and effective competitors in Charlotte and Greensboro, North Carolina; Macon, Georgia; Columbia, West

Columbia and Lexington, South Carolina; Lynchburg, Virginia; Northern Rockland County, New York; and Yakima, Washington.

Background

Keystone is a leading owner and operator of funeral homes across the United States, with 174 funeral homes and 8 cemeteries; Keystone management estimates that the company is the fourth largest provider of funeral services in the United States. Publicly traded on the Toronto stock exchange since February 8, 2005, detailed financial information on Keystone is available at keystonenorthamerica.ca, along with copies of Keystone's annual reports and other structural and financial information pertaining to Keystone and Keystone America. Attached hereto are copies of Keystone's 2005 prospectus (Exhibit B), its Audited Financial Statements for 2005 (Exhibit C), and its Third Quarter Report, September 30, 2006 financial statements (Exhibit D).

Formed in 1996, Keystone has built a solid reputation for providing a full range of funeral services on both an at-need (at time of death) and a pre-need (prior to death) basis. These services include removal of human remains, planning and coordinating personalized funerals and cremations, professional embalming, use of our funeral home facilities, merchandise sales, conducting memorial services, performing cremations, and cemetery interment services.

Over the last ten years, Keystone has completed approximately 90 transactions, the majority of which were acquisitions of funeral homes and/or cemeteries from private owners. Keystone has successfully completed transactions of all sizes, including large ones. In one 2005 transaction, for example, Keystone acquired and successfully integrated 87 funeral homes from The Hamilton Group. Keystone has also bought funeral homes and cemeteries from SCI, in two transactions: In March 2006, Keystone purchased the assets of a large cemetery (Roselawn

Cemetery), and two small funeral homes (Thomas Funeral Home and McClanahan-Lee Funeral Home) in Terre Haute, Indiana. In September 2006, Keystone purchased the assets of three cemeteries and two funeral homes in Springfield, Missouri. Keystone successfully operates these facilities and all of the other funeral homes and cemeteries that it has acquired since its formation in 1996. In these transactions, and indeed in all of its acquisitions, Keystone's operations team makes every effort to ensure the quick, seamless integration of the business, with continued operation under Keystone's ownership. Based on its substantial track record of acquisitions, there can be not doubt that Keystone is able to successfully acquire and quickly integrate the businesses it purchases, whether from SCI or others.

Keystone has enjoyed relatively quick closings, and trouble-free operations, in part because of Keystone's good standing with state licensing agencies. In prior acquisitions, Keystone focused on small to middle markets, making it a good match for the present divestiture targets. Keystone has garnered a strong reputation in the funeral industry for managing small to medium sized businesses, that is, businesses of the size and scope of the Keystone Divestiture Assets at issue here.

Keystone America and Keystone do not presently have any competitive assets in the markets, as defined by the Commission in its Complaint, served by the Keystone Divestiture Assets.

<u>Financial Capability</u>

Keystone is in a strong financial position, as shown in Keystone's Third Quarter Report, September 30, 2006 financial statements (Exhibit D). Revenues are in excess of $62 Million for 2006 through September 30, 2006, with gross profit for this nine month period in excess of $22 Million. Keystone has sufficient funds available under its existing credit facilities to pay the purchase price, and Keystone's financials demonstrate that it is a strong company. Thus, Keystone has the ability both to purchase the Keystone Divestiture Assets and to ensure the continued use of these assets as part of a viable, competitive business. Keystone's ability to complete this transaction is also demonstrated by its successful completion of many prior acquisitions, including the much larger acquisition of 87 funeral homes from The Hamilton Group in 2005.

Operations Experience

Keystone has significant experience owning and operating funeral homes and cemeteries, with 174 funeral homes and 8 cemeteries. Headquartered in Tampa, Florida, Keystone has over 1,000 employees across the United States, and in Ontario, Canada. Keystone has a seasoned management team with extensive experience in owning, operating and acquiring funeral homes. The executive management team is comprised of four seasoned funeral professionals who collectively have spent over 125 years successfully acquiring, integrating and managing funeral businesses. The four senior members of Keystone's management are as follows:

**Robert G. Horn,** Keystone's co-founder, serves as Chief Executive Officer / Chairman. Mr. Horn has 46 years of funeral industry experience. Mr. Horn was an organizer, Partner and Chief Operating Officer of Prime Succession, Inc. from its inception until the sale of the company in 1996.[3] Prior to Prime Succession, Mr. Horn was Executive Vice President of Pierce Brothers Holding Company, a Los Angeles based funeral home consolidator.[4] He was an

[3] Prime Succession was a consolidator of funeral homes and cemeteries formed by Mr. Horn and others in 1992. By the time Mr. Horn and his colleagues sold the company in 1996, Prime Succession had grown into a very successful company with over 120 funeral home and cemetery locations around the United States.

[4] Although Pierce Brothers had been in existence for decades when Mr. Horn was hired, the company had only operated a handful of funeral homes in Southern California. Following Mr. Horn's involvement, Pierce Brothers grew to over 30 locations in California, with more than 30 additional locations in Florida. Mr. Horn was primarily responsible for acquiring and integrating these new facilities.

organizer and served as Vice President for 16 years at International Funeral Services, Industries ("IFS"), the first publicly held, multi-state consolidator of funeral homes and cemeteries. He had brief experience with SCI following its merger with IFS in 1981. He began his career with a small family-owned funeral home, which was subsequently sold to IFS. Mr. Horn currently serves as a Trustee and is the Chair Elect of The National Funeral Service Foundation, is a member of the Death Care Management Council, an instructor at the International Cemetery and Funeral Association's Summer Executive program at Memphis University and is a Clavigerii Society Member of Loyola Marymount University, Los Angeles.

**Steven A. Tidwell**, a co-founder, serves as President of Keystone. Mr. Tidwell has 27 years of funeral industry experience including a focus on mergers and acquisitions and experience as a funeral director. He attended John A. Gupton College where he obtained an Associate of Arts in Mortuary Science. Mr. Tidwell is a licensed funeral director and embalmer and has his national certification. He was a Partner at Prime Succession, Inc. where he was Vice President of Corporate Development. Prior to Prime Succession, Mr. Tidwell was Regional Vice President covering 6 states with Thomas-Pierce & Company, a succession planning company. Mr. Tidwell was previously employed with Arlington Corporation, a funeral home consolidator and Woodlawn Funeral Home and Memorial Park. He is also a member of the National Funeral Directors Association and an active alumnus of Sigma Chi Fraternity.

**Stephen M. Shaffer**, a co-founder, serves as Keystone's Chief Financial Officer. Mr. Shaffer has served as Chief Financial Officer of Keystone since its inception and was previously Corporate Controller of Prime Succession prior to its sale. Mr. Shaffer was employed as an auditor with Ernst & Young in Indianapolis from 1987 to 1994. While working as a CPA at Ernst & Young, Mr. Shaffer's audit clients included two cemetery and funeral consolidation companies, Gibraltar Mausoleum Corporation and Prime Succession. Mr. Shaffer graduated in 1987 from Indiana University School of Business, Bloomington, Indiana with a Bachelor of Science in Accounting.

**James D. Price**, a co-founder, serves as Keystone's Chief Operating Officer. Mr. Price has 40 years of funeral industry experience. Mr. Price previously served (in reverse chronological order) as President and CEO of Bonny-Watson, a large Seattle based funeral home and Cemetery Company; Southern Regional Vice President at Prime Succession, Inc.; Regional Vice President for SCI; and Operations Vice President at Pierce Brothers Holding Company. He also worked as an area manager at IFS and a local funeral home. Mr. Price is a graduate of the California College of Mortuary Science, Mira Costa College. He is a licensed Funeral Director and Embalmer in California (he is the third generation in his family to serve as a funeral director) and holds a National Board Certificate. Mr. Price is a member of the National Funeral Directors Association, the Cremation Association of North America and the International Funeral and Cemetery Association.

These four individuals constitute a very strong and highly experienced senior management team. They have been together since Keystone's inception in 1996, and also worked together before that at Prime Succession. They assure that Keystone is an eminently qualified buyer for the Keystone Divestiture Assets.

Keystone believes that keeping good personnel helps ensure the continuity of the business, allowing Keystone to compete effectively in each market from the date of acquisition forward. Keystone takes pride in its ability to be financially competitive while maintaining the local staff, which contributes to the long-term success of each business. As a result, Keystone intends to offer positions to key individuals currently employed at the Keystone Divestiture

Assets, and consistent with prior acquisitions and its business model, Keystone anticipates offering employment to most, if not all, of the employees currently employed at the Keystone Divestiture Assets, on terms and at compensation roughly equivalent to existing particulars. FSI has agreed in the Sale Agreement not to solicit the employment of any such employee hired by Keystone for a period of two years following closing, as required by Paragraph II.H.4. of the Decision and Order.

The foregoing demonstrates that Keystone has the resources, operating expertise and commitment to its business to not only ensure the continued competitiveness of the Keystone Divestiture Assets, but to provide the acquired businesses with a competitive advantage in order to enhance their competitiveness and grow market share.

## III. The Proposed Divestiture Will Achieve the Purposes of the Decision and Order and Result in No Harm to Competition

The proposed divestiture of the Keystone Divestiture Assets, as embodied in the Sale Agreement, will achieve the purposes of the Decision and Order. Keystone is an experienced operator of funeral homes and cemeteries, with a proven track record of successfully operating and enhancing the funeral homes and cemeteries that it has acquired in the past. Keystone enjoys a strong financial position that will enable it to complete this acquisition, continue the operation of the Keystone Divestiture Assets and enhance their competitiveness in the market for funeral and cemetery services. Combining the Keystone Divestiture Assets with Keystone's experience and financial wherewithal will ensure that the objectives of the Decision and Order will be realized.

The proposed divestiture will result in no harm to competition. Keystone America and Keystone do not currently compete in any market, as defined in the Commission's Complaint, in which the Keystone Divestiture Assets operate. Consequently, there is no overlap between the operations of Keystone America or Keystone and the Keystone Divestiture Assets, and the proposed divestiture does not raise any competitive issue.

In sum, the proposed divestiture will remedy any anticompetitive effects that could result from the Acquisition. The Sale Agreement will achieve the Commission's stated purposes of ensuring the continued use of the Keystone Divestiture Assets in the same business in which they were engaged at the time of the announcement of the proposed Acquisition and remedying the lessening of competition alleged in the Commission's Complaint.

## Conclusion

For the foregoing reasons, the Respondents respectfully request that the Commission approve the proposed divestiture of the Keystone Divestiture Assets to Keystone, as embodied in the Sale Agreement with Keystone America, as soon as practicable after expiration of the public comment period.

Respectfully submitted,

David A. Schwartz

David A. Schwartz
Wachtell, Lipton, Rosen & Katz
51 West 52nd Street
New York, New York 10019
(212) 403-1000
Counsel for Respondents
Dated: December 21, 2006

## CERTIFICATION OF SERVICE CORPORATION INTERNATIONAL

The facts and information related in the foregoing Petition, insofar as they pertain to Service Corporation International, its subsidiaries, and its assets, are, to the best of my knowledge, true, correct, and complete.

Pursuant to 28 U.S.C. § 1746, I certify under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Christopher H. Cruger
Vice President, Business Development
Service Corporation International

CERTIFICATION OF KEYSTONE NORTH AMERICA, INC.

The facts and information related in the foregoing Petition, insofar as they pertain to Keystone North America, Inc., its subsidiaries, and its assets, are, to the best of my knowledge, true, correct, and complete.

Pursuant to 28 U.S.C. § 1746, I certify under penalty of perjury under the laws of the United States of America that the foregoing is true and correct.

Stephen M. Shaffer
Chief Financial Officer
Keystone North America, Inc.

# EXHIBIT A

# [REDACTED FROM THE PUBLIC RECORD VERSION]

# EXHIBIT B

*No securities regulatory authority has expressed an opinion about these securities and it is an offence to claim otherwise. This prospectus constitutes a public offering of these securities only in those jurisdictions where they may be lawfully offered for sale and only by persons permitted to sell these securities in those jurisdictions. These securities have not been and will not be registered under the United States Securities Act of 1933, as amended, or any state securities laws and may not be offered or sold in the United States or to U.S. persons except in compliance with the registration requirements of the United States Securities Act of 1933, as amended, and applicable state securities laws or under exemptions from those laws. See "Plan of Distribution".*

**PROSPECTUS**

*Initial Public Offering* January 31, 2005

KEYSTONE

# Keystone North America Inc.
# and
# Keystone Newport ULC
# C$171,000,000
# 17,100,000 Income Participating Securities™

This offering is an initial public offering of Income Participating Securities™, or IPS™s. Each IPS represents one common share, a "Common Share", of Keystone North America Inc., or "Keystone North America", and C$4.286 principal amount of 14.5% subordinated notes, the "Subordinated Notes", of Keystone Newport ULC, or "Keystone ULC". Keystone North America and Keystone ULC are collectively referred to in this prospectus as the "Issuer". In connection with the closing of this offering, the Issuer will acquire and hold all of the issued and outstanding Class A common shares and preferred shares of Keystone Group Holdings, Inc., or "Keystone", representing a 85.3% voting interest in Keystone. Keystone is a leading owner and operator of funeral homes across the United States. Following the closing of this offering, Keystone will own and operate 177 funeral homes and nine cemeteries in 26 states in the United States, making it, in management's estimate, the fifth largest funeral home operator in the United States. See "Investment Agreement" and "Use of Proceeds".

Holders of IPSs will have the right to separate the IPSs into Common Shares and Subordinated Notes at any time after 45 days following the closing of this offering or upon the occurrence of a change of control of Keystone North America or Keystone ULC. Separation of the IPSs will occur automatically upon a repurchase, redemption or maturity of the Subordinated Notes and in certain other circumstances described herein. Similarly, any holder of Common Shares and Subordinated Notes may, at any time prior to an automatic separation of the Subordinated Notes, combine the applicable number of Common Shares and principal amount of Subordinated Notes to form IPSs. See "Description of IPSs".

The Subordinated Notes will have a term of 12 years. On or after the fifth anniversary of the closing of this offering, Keystone ULC will have the option to redeem the Subordinated Notes in whole or in part at any time, for cash, at a redemption price equal to a premium over the principal amount of the Subordinated Notes, which premium decreases over time. See "Description of Subordinated Notes". In connection with this offering, Keystone ULC is also selling, on a private placement basis, approximately C$10 million principal amount of Subordinated Notes that are not in the form of IPSs, which we refer to as "Separate Subordinated Notes". The completion of the offering of Separate Subordinated Notes is a condition to the Issuer's sale of IPSs.

The pricing of the IPSs has been determined, in part, based on an estimate of distributable cash for the 12 months ended September 30, 2004. See "Summary of Distributable Cash of the Issuer".

A return on your investment in the Issuer is not comparable to the return on an investment in a fixed-income security. The recovery of your initial investment is at risk, and the anticipated return on your investment is based on many performance assumptions. Although the Issuer intends to make distributions of its available cash to you, these cash distributions may be reduced or suspended. The actual amount distributed will depend on numerous factors including: the financial performance of Keystone and its direct and indirect subsidiaries (including the indirect subsidiaries acquired from HFSC Holdings, Inc. on the closing of this offering), which we refer to collectively as the "Company", the Company's debt covenants and other contractual obligations, working capital requirements, future capital requirements, and the deductibility for U.S. federal income tax purposes of interest payments on the Subordinated Notes, all of which are susceptible to a number of risks. In addition, the market value of the IPSs may decline if the Issuer is unable to meet its cash distribution targets in the future, and that decline may be significant.

It is important for you to consider the particular risk factors that may affect the industry in which you are investing, and therefore the stability of the distributions that you receive. See, for example, the risks associated with predicting deaths from market to market over the short term; price competition; increasing cremation rates and all of the other risks described in the section "Risk Factors". This section also describes the Issuer's assessment of those risk factors, as well as the potential consequences to you if a risk should occur.

**Investing in the IPSs involves a number of risks that should be considered by a prospective investor.** See "Risk Factors".

## Price: C$10.00 per IPS

| | Price to the Public(1) | Underwriters' Fee | Net Proceeds to the Issuer(2) |
|---|---|---|---|
| Per IPS | C$10.00 | C$0.575 | C$9.425 |
| Total(3) | C$171,000,000 | C$9,832,500 | C$161,167,500 |

(1) The offering price of the IPSs was determined by negotiation between the Issuer and the Underwriters and no third-party valuation was obtained.

(2) Before deducting expenses of the offering, estimated at approximately C$5.7 million, which, together with the Underwriters' Fee, will be paid out of the proceeds of the offering.

(3) The Issuer has granted the Underwriters an over-allotment option, exercisable for a period of 30 days from the date of closing of this offering, to purchase up to a total of 1,668,017 additional IPSs on the same terms as set out above to cover over-allotments, if any, and for market stabilization purposes. If the over-allotment option is exercised in full, the total "Price to the Public", "Underwriters' Fee" and "Net Proceeds" will be C$187,680,170, C$10,791,610 and C$176,888,560, respectively. This prospectus qualifies the distribution of the over-allotment option and the distribution of the IPSs issuable upon exercise of that option. See "Plan of Distribution".

**"Income Participating Securities" and "IPS" are trademarks of BMO Nesbitt Burns Corporation Limited**

*(continued on next page)*

KEYSTONE

*(continued from cover)*

The Issuer will allocate the price paid for each IPS on the basis of C$5.714 to the Common Share and C$4.286 to the Subordinated Notes and by purchasing such IPS, the holder is deemed to agree to such allocation and agrees to not take a contrary position for any purpose. The Canadian and U.S. tax consequences of acquiring, holding and disposing of the Common Shares and Subordinated Notes represented by IPSs may, in part, depend on the Canada Customs and Revenue Agency and United States Internal Revenue Service agreeing with this allocation. See "Certain Canadian Federal Income Tax Considerations" and "Certain U.S. Federal Income Tax Considerations". Distributions on the IPSs will consist of interest payments on the Subordinated Notes and dividend payments on the Common Shares represented thereby. See "Description of IPSs" and "Certain Canadian Federal Income Tax Considerations". The first monthly distribution, in an amount of C$0.0625 per IPS, is expected to be made to holders of IPSs on March 15, 2005 for the period from the closing of this offering to February 28, 2005 (assuming closing occurs on February 8, 2005). See "Distribution Policy".

In connection with this offering, BMO Nesbitt Burns Inc., Scotia Capital Inc., CIBC World Markets Inc. RBC Dominion Securities Inc., National Bank Financial Inc. and TD Securities Inc. who in this prospectus are referred to collectively as the "Underwriters", are permitted to engage in transactions that stabilize or maintain the market price of the IPSs at levels other than those that might otherwise prevail on the open market. The Underwriters may offer the IPSs at a lower price than stated below. **There is currently no market through which the IPSs, and the Common Shares and Subordinated Notes represented thereby, may be sold and purchasers may not be able to resell securities purchased under this prospectus.** The Toronto Stock Exchange has conditionally approved the listing of the IPSs and the Common Shares. Listing is subject to the Issuer fulfilling all of the requirements of the Toronto Stock Exchange on or before April 22, 2005. See "Plan of Distribution".

An affiliate of BMO Nesbitt Burns Inc. has arranged to make credit facilities available to a subsidiary of the Issuer. As a result, the Issuer may be considered a "connected issuer" of BMO Nesbitt Burns Inc. See "Plan of Distribution".

**Unless a non-U.S. holder provides appropriate documentation establishing entitlement to a reduction or elimination of United States withholding tax, a 30% United States withholding tax will be assessed on interest payments paid on the Subordinated Notes to that non-U.S. holder. See "Certain U.S. Federal Income Tax Considerations".**

The Underwriters, as principals, conditionally offer the IPSs, subject to prior sale, if, as and when issued by the Issuer and accepted by the Underwriters in accordance with the conditions contained in the underwriting agreement referred to under "Plan of Distribution" and subject to the approval of certain legal matters on behalf of the Issuer and Keystone by Goodmans LLP and Kirkland & Ellis LLP and on behalf of the Underwriters by Torys LLP. Subscriptions for the IPSs will be received subject to rejection or allotment, in whole or in part, and the right is reserved to close the subscription books at any time without notice. A book entry only certificate representing the IPSs will be issued in registered form to The Canadian Depository for Securities Limited ("CDS") or its nominee and will be deposited with CDS on the closing of the offering. Closing is expected to occur on or about February 8, 2005 or such later date as the Issuer and the Underwriters may agree, but in any event not later than February 22, 2005. A purchaser of IPSs will receive only a customer confirmation from the registered dealer that is a CDS participant and from or through which the IPSs are purchased.

Keystone is the promoter of this offering and is organized under the laws of a foreign jurisdiction and resides outside Canada. Although Keystone has appointed Keystone North America, Suite 2400, 250 Yonge Street, Toronto, Ontario, Canada, M5B 2M6 as its agent for service of process in Ontario, it may not be possible for investors to collect from the promoter judgments obtained in courts in Canada predicated on the civil liability provisions of securities legislation of certain of the provinces and territories of Canada. See "Risk Factors".

## TABLE OF CONTENTS



**In this prospectus, references to "C$" and "Canadian dollars" are to the lawful currency of Canada and references to "$", "US$" and "U.S. dollars" are to the lawful currency of the United States. All dollar amounts herein are in U.S. dollars, unless otherwise stated.**

## MEANING OF CERTAIN REFERENCES

Keystone North America Inc. ("Keystone North America"), an Ontario corporation, is the issuer of the Common Shares and Keystone Newport ULC ("Keystone ULC"), a Nova Scotia unlimited liability company, is the issuer of the Subordinated Notes that, together with the Common Shares, form the IPSs. Keystone North America and Keystone ULC are referred to in this prospectus, collectively, as the "Issuer". Unless otherwise stated or the context otherwise requires, references in this prospectus to "we", "us" or the "Company" refer to Keystone Group Holdings, Inc. ("Keystone") and all of its direct and indirect subsidiaries (including the indirect subsidiaries acquired from HFSC Holdings, Inc., or "Hamilton"), immediately following consummation of the transactions described under the captions "Investment Agreement" and "Post-Closing Structure"; and "management" refers to management of the Company and the Issuer.

Throughout this prospectus, unless otherwise indicated, all references to "GAAP" are to accounting principles generally accepted in Canada. The financial statements of Keystone North America, Keystone and Hamilton contained in this prospectus have been prepared in accordance with GAAP.

Unless otherwise stated or the context otherwise requires, references to the outstanding number of IPSs, the number of Common Shares and the principal amount of Subordinated Notes underlying the IPSs assume that the Underwriters' over-allotment option is not exercised.

## DEFINITION OF EBITDA, NORMALIZED EBITDA, NORMALIZED REVENUE AND DISTRIBUTABLE CASH

References in this prospectus to "EBITDA" are to earnings before interest, taxes, depreciation, amortization and certain other adjustments listed in the reconciliation tables provided herein (*e.g.*, in the case of Hamilton, non-compete and consulting expense). References in this prospectus to "Normalized EBITDA" are to EBITDA adjusted for dispositions of funeral homes no longer in the portfolio of funeral homes that will be acquired by the Issuer, indirectly, on closing of the offering. References in this prospectus to "Normalized Revenue" are to revenue adjusted for dispositions of funeral homes no longer in the portfolio of funeral homes that will be acquired by the Issuer, indirectly, on closing of the offering. Management believes such adjustments facilitate the comparison of historical periods. See "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash".

The Issuer believes that EBITDA, Normalized EBITDA and Distributable Cash are useful supplemental measures of cash available for distribution on the IPSs prior to debt service, capital expenditures and income taxes and the appropriate measure from which to make adjustments to determine Distributable Cash (being Normalized EBITDA, as adjusted for: cost savings from the Hamilton acquisition; maintenance capital expenditures; additional administrative expenses; interest on the new credit facility; interest on the Separate Subordinated Notes; and income taxes paid in cash). However, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized earnings measures under GAAP and do not have standardized meanings prescribed by GAAP. Investors are cautioned that neither EBITDA nor Normalized EBITDA should be construed as an alternative to net income or loss determined in accordance with GAAP as an indicator of the Issuer's performance or to cash flows from operating, investing and financing activities as a measure of liquidity and cash flows. The Issuer's method of calculating EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may differ materially from the methods used by other public companies and accordingly, may not be comparable to similarly titled measures used by other public companies. Distributable Cash is not assured, and the actual amount received by holders of IPSs will depend on, among other things, the operations and assets of the Company, obligations under the New Credit Facility (as defined herein), fluctuations in working capital, the sustainability of margins, and the Company's capital expenditure requirements. See "Summary of Distributable Cash of the Issuer".

## FORWARD-LOOKING STATEMENTS

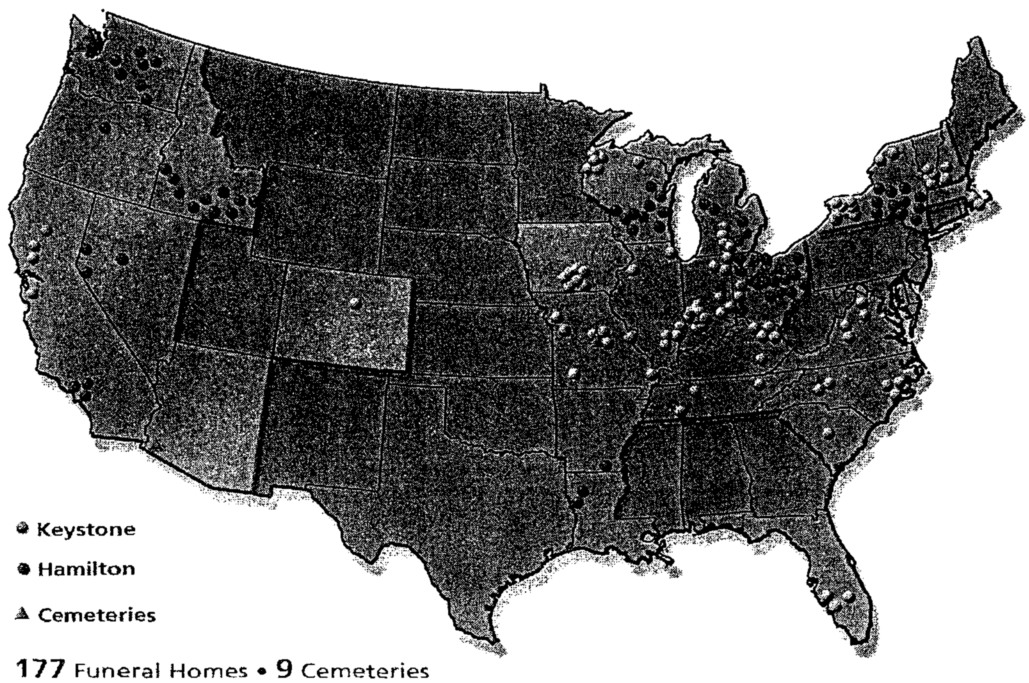
Certain statements in this prospectus are "forward-looking statements" that reflect the expectations of management regarding the Issuer and the Company's future growth, results of operations, performance and business prospects and opportunities. These forward-looking statements reflect management's current expectations regarding future events and operating performance and speak only as of the date of this prospectus. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not or the times at or by which such performance or results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under "Risk Factors". Although the forward-looking statements contained in this prospectus are based upon what management believes to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. These forward-looking statements are made as of the date of this prospectus and none of the Issuer, Keystone or their respective management or the Underwriters assumes any obligation to update or revise them to reflect new events or circumstances.

## PROSPECTUS SUMMARY

*The following is a summary of the principal features of this offering of IPSs and should be read together with the more detailed information and financial data and statements contained elsewhere in this prospectus. Unless otherwise indicated, the disclosure contained in this prospectus assumes that the steps under the heading "Investment Agreement" and "Post-Closing Structure" have been completed and that the Underwriters' over-allotment option has not been exercised.*

## KEYSTONE

We are a leading owner and operator of funeral homes across the United States. Upon completion of this offering and our acquisition of Hamilton, we will be the owner of a funeral service business with 177 funeral homes and nine cemeteries and, in management's estimate, will be the fifth largest provider of funeral services in the United States. Generally, our funeral homes are located in the Midwest, Northeast, Southeast and Northwest regions of the continental United States with individual service markets primarily made up of non-urban areas. The following map illustrates the states in which we operate:

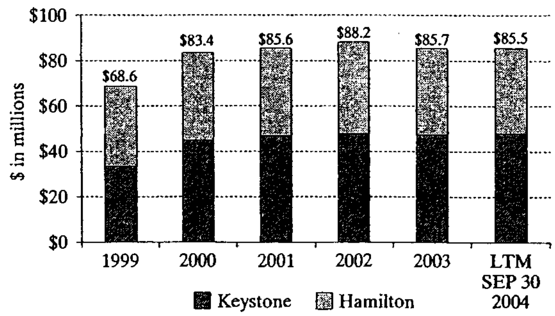



Our funeral homes represent well-established businesses with an average age of the original business in excess of 50 years. In our respective markets, our funeral homes have historically provided a full range of funeral services on both an at-need (at time of death) and pre-need (prior to death) basis. These services include removal of human remains, planning and coordinating personalized funerals and cremations, professional embalming, use of our funeral home facilities, merchandise sales, conducting memorial services, performing cremation and cemetery interment services.

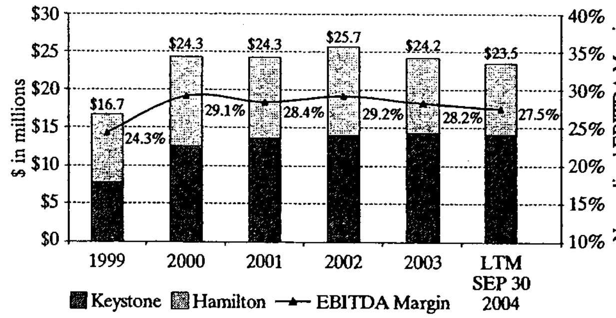
Our executive management team is comprised of four seasoned funeral professionals who collectively have spent 125 years successfully acquiring, integrating and managing funeral businesses. Local management consists substantially of former owners, their former managers and their other key employees. We have very strong relationships with the former owners of these funeral businesses, with over 80% still actively supporting our funeral homes in some significant way.

By successfully executing a business strategy that emphasizes operating efficiency and margin improvement, we have experienced stable and consistent Normalized Revenue and Normalized EBITDA, as illustrated in the following charts:

**Combined Keystone Normalized Revenue(1)**




**Combined Keystone Normalized EBITDA(1)**

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(1) EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may not be comparable to similar measures presented by other companies. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash" and "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". As the Issuer intends to distribute substantially all of the Issuer's cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA and Distributable Cash are important measures in evaluating the Issuer's performance and in determining whether to invest in IPSs.

## OUR BUSINESS

### Business Strengths

Our funeral home businesses have a number of attributes that promote stable revenue and EBITDA, including:

- *Strong Franchise Value:* Heritage and tradition are two of the most important factors driving client selection of a funeral home. More than 89% of our funeral homes were established before 1960. Our funeral homes are typically the largest and premier operations in their respective geographical markets. We typically require former owners of the acquired funeral homes to remain active in the daily operations for up to five years to facilitate the transition to corporate ownership while leveraging local heritage.

- *Focus on Stable Funeral Services:* Unlike the four U.S. publicly-traded funeral services companies that have cemetery operations providing approximately 25% to 50% of their revenue, over 95% of our revenue and 95% of our EBITDA is derived from our funeral home operations. Revenue in the funeral home business is far more stable than in the cemetery businesses, as services are provided at the time of death and therefore involve non-discretionary spending.

- *Expansion of Product Offering:* Since 2001, we have been implementing a number of value added services to increase revenue and secure market share, including the implementation of the 'Key Memories' program in our funeral homes that increases family participation in the planning process. In addition, we have focused on adding more services to our burial and cremation options and increasing our advance planning sales.

- *Strong Supplier Relationships:* As one of the largest funeral home operators in the U.S., we enjoy preferred rates and volume discounts over smaller competitors from many of our suppliers.

- *High Quality Portfolio of Diverse Long-Term Sustainable Assets:* Our business includes a total of 177 funeral homes in 26 states with no one state representing more than 15% of aggregate revenue. We own a portfolio of established funeral home businesses, with our average funeral home business having been in operation for over 50 years. Our properties also have significant value as real estate assets.

- *Focus on Suburban and Rural Markets:* Suburban and rural markets, relative to large urban markets, offer lower migration rates, stronger community ties, less price sensitivity among consumers and a limited number of alternative service providers. In addition, our competition in such areas tends to be smaller operators that do not benefit from certain advantages that we enjoy as a national operator.

- *Experienced Management Team:* Our executive management team has 125 years of combined experience in funeral home and cemetery operations and our senior management team has been in place since 1996. Our management team has developed expertise in identifying, executing and integrating strategic acquisitions, completing 65 acquisitions since 1996 and assembling, integrating and successfully managing the businesses over a period of four to seven years.

### Growth Strategies

Our growth strategies are designed to increase market share and enhance profitability. Our organic and external growth strategies are outlined below.

#### *Organic Growth*

Our organic growth strategy focuses on three key areas:

- *Increase revenue per case:* We have enhanced service and merchandise packages, and developed a full line of marketing materials used in presenting burial and cremation package selections to customers. Package presentations generally generate higher revenue than customer selection of individual items. We carefully select additional merchandise and service items for inclusion in packages that provide for greater value while increasing the overall package price and margin. In addition, we offer a range of personalized memorial programs and paper goods, again designed to increase case average while further enhancing personalization and thus value for the customer. We have historically been successful in increasing average revenue per case, even as case count has varied and cremation levels have increased from year to year.

- *Increase the volume of full service cremations:* In recognition of the growing proportion of cremations, arrangement presentations have been designed to ensure that families are well informed as to all available options and considerations when contemplating this type of service. The objective of these efforts is to increase the number of customers selecting additional service and merchandise options, thereby enhancing perceived value and increasing revenue generated by cremations as well as overall profit margin percentages. Supporting marketing and advertising materials, together with best practices sales training programs, have been developed and are being utilized by our higher volume cremation facilities to increase the average revenue per case and number of cremations with memorial service.
- *Increase market share:* Given the importance of tradition and heritage in selecting a funeral home, gains in market share are won through long-term marketing and pre-need sales. To that end, management has focused on programs to build awareness of the Keystone tradition and to build goodwill in the communities that we serve. In addition, we have remained focused on increasing pre-need sales in our funeral business. The growth of our advance planning program at a rate faster than our competition in any given market eventually results in direct market share gains from that competition.

*External Growth*

Our external growth strategy focuses primarily on selective strategic acquisitions of existing funeral homes that complement our existing portfolio. We believe that growing our organization through acquisitions will continue to be a good business strategy, as we enjoy the important synergies and economies of scale from our scalable infrastructure. We will seek to capitalize on the quality and location of our existing portfolio of funeral homes and lower individual overhead costs by sharing common resources in clusters. When we enter the acquisition arena again, we will acquire funeral homes, using a disciplined approach, with deep heritage and tradition that are profitable and have the potential to grow revenue and operating margins.

**Acquisition Activity**

In 65 separate transactions, Keystone acquired a net total of 97 funeral homes from inception in 1996 through 2000. In connection with our acquisition activity, we have developed the following acquisition criteria: (i) operating and cultural fit, (ii) favourable community demographics and (iii) an attractive financial profile. We also seek to acquire funeral homes in geographic clusters to facilitate the management of the operations and sharing of resources. Consistent with the industry as a whole, our acquisition activity decreased after 2000 to focus on integrating our portfolio and enhancing operations.

*Hamilton Acquisition*

The acquisition of Hamilton, which will be our largest acquisition to date when it closes concurrently with this offering, fits our acquisition criteria and presents an opportunity to realize significant synergies. Management expects to realize substantial cost savings in the following areas.

- **Corporate Overhead Savings** — Reduction of Hamilton's corporate operations by leveraging Keystone's corporate head office and accounting infrastructure.
- **Procurement Savings** — Improvement of margins as a result of increased purchasing power.
- **Selling, General and Administrative Efficiencies** — Reduction of travel expense as a result of having a broader network of operating personnel; and streamlining back office systems through the elimination of duplication regarding payroll-benefit services, risk management, compliance and management and information systems.

- **Leveraging Best Practices** — Realizing gains through the utilization of best practices across the organization (*e.g.*, 'Key Memories').

Management will also continue to consider future acquisitions in accordance with our acquisition criteria and disciplined processes. Management believes that, despite the prior period of consolidation in the industry in the later 1990s, the industry remains highly fragmented and significant strategic acquisition opportunities exist at reasonable valuations.

**Currency Hedging Policy**

We will be exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar because the revenue and expenses of Keystone are in U.S. dollars and the distributions that Keystone will make to Keystone North America and Keystone ULC will be paid in Canadian dollars. In order to minimize the impact of fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar, we intend to enter into a five-year hedging arrangement at an exchange rate of C$1.2272 to US$1.00 at or prior to the closing of this offering. See "Summary of Distributable Cash Flow of the Issuer". We will convert substantially all of the amounts received by it into Canadian dollars to make distributions in Canadian dollars. We will review our hedging policy on an ongoing basis.

## INDUSTRY OVERVIEW

**Introduction**

"Death care" is the overarching term used to refer to the interrelated funeral home and cemetery industry. Funeral homes furnish goods and services relating to the preparation of the body and memorialization of the deceased. Cemeteries furnish property and goods relating to permanent disposition and remembrance.

The primary goods and services provided by funeral homes and cemeteries consist of the following:

- *Funeral homes:* Professional services related to funerals, including preparation of the body; arrangement of memorial services; use of funeral facilities and motor vehicles; sale of caskets, urns, burial vaults, burial garments; cremation.

- *Cemeteries:* Sale of interment rights associated with cemetery property including lots, lawn crypts, and mausoleum spaces; sale of related merchandise including stone and bronze memorials and burial vaults; cremation.

There are several fundamental differences between the funeral business and the cemetery business. First, the funeral business is a service business while the cemetery business is primarily an interment rights or property business. As a result, the funeral business has much greater cash flow stability as services are provided at time of need and are non-discretionary items that have predictable long-term demand. Cemetery revenue is largely derived on pre-need or advance sales that are discretionary and subject to greater volatility. Additionally, cemetery sales create an ongoing obligation between the cemetery and the customer whereas funeral services are completed at time of death. Finally, funeral homes have more stringent licensing and education requirements than cemeteries, increasing barriers to entry.

Management estimates that there are approximately 22,000 funeral homes and 10,500 cemeteries in the United States with small family-owned businesses generating approximately 80% of the death care industry's total revenue and the four major U.S. publicly listed companies in the industry (Service Corporation International, Alderwoods Group, Inc., Stewart Enterprises, Inc. and Carriage Services, Inc.) representing the remaining 20%. Total revenue for the death care industry in 2004 is expected to exceed $15 billion. Management believes that the four major U.S. public death care companies operate approximately 11% and 7% of the funeral homes and cemeteries in the United States, respectively, and serve approximately 22% of the total funeral cases in the United States.

**Attributes of the Funeral Home Business**

The funeral home business is one of the more stable industries in the U.S. Local funeral home businesses generally enjoy predictable cash flow due to a variety of favourable attributes, including:

- *Predictable and Stable Demand:* Funeral service is both stable, due to the inevitability of death, and essential, due to the legal need to properly dispose of the body and the religious and cultural need to memorialize the deceased. The U.S. Census Bureau projects a 23.2% increase in the number of deaths from 2004 to 2025 due in part to the aging of the "Baby Boom" population.

- *Significant Barriers to Entry:* Entry of a new funeral home in an established market can be difficult due to the importance of local heritage and tradition. A recent industry survey found that location, reputation, previous experience and pre-need services are the most important factors in selecting a funeral home. High barriers to entry also include significant capital investment needed to start a new funeral home and the long time needed to develop a sufficient volume of business to provide adequate returns.

- *Mature Competition Base:* The funeral industry is a very mature industry with most areas already adequately served by one or more funeral homes that through decades of operations have developed a strong reputation and heritage in their community. Since reputation and heritage are among the strongest factors influencing consumer choice, there is less incentive or opportunity to compete on price and new funeral homes tend only to open in areas of new development and population growth.

- *Attractive Margins:* The funeral home industry has demonstrated very strong operating margins, due in part to the focus of client families on heritage and tradition rather than on price, as well as the steady and predictable level of demand that most funeral homes enjoy. With a largely fixed cost structure, revenue achieved through case count increases or expansion of products and services sold typically generate substantial improvements in both margins and cash flow. Further improvements in margins have been achieved when individual facilities are clustered in a common geographic area, and are thereby able to share fixed costs such as vehicles, employees and other resources.

- *Ability to Increase Market Share through Advance Planning:* An increasing number of death care products and services are being sold prior to the time of death, or on a "pre-need" basis. Advance planning is a growing trend that is expected to continue as funeral homes expand these programs in order to increase market share and in response to consumer preference to control their own funeral arrangements. Revenue per case in the funeral home business is not materially different for sales made on a pre-need or at-need basis.

- *Highly Fragmented Ownership:* Despite forty years of funeral consolidation and a particularly active period in the 1990s, the death care industry remains highly fragmented. A significant majority of death care operators are small, family-owned businesses that control one or several funeral homes in a single community. As a result, opportunities for further consolidation and clustering exist that can result in enhanced operating efficiencies such as increased buying power and leveraging of resources.

**Market Drivers**

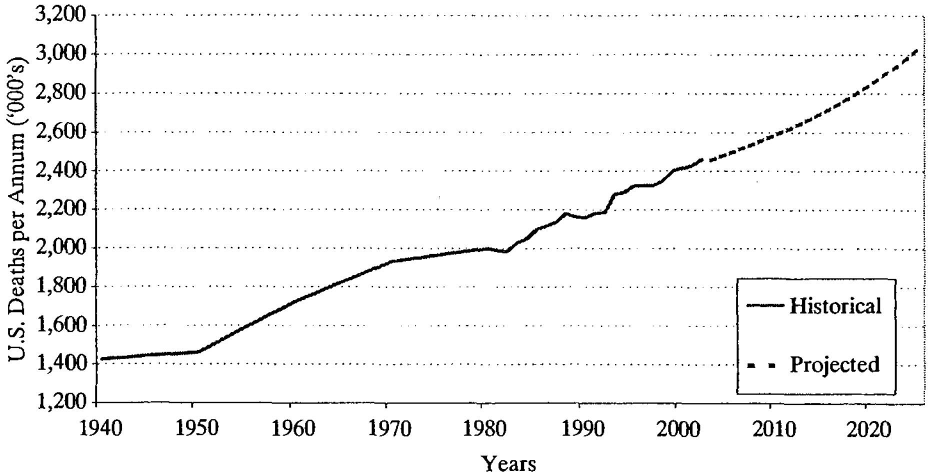
The funeral home business is subject to the following market drivers:

- *Local Heritage:* Market share is largely a function of goodwill, family heritage and tradition, all of which reflect factors that take many years to develop. Market share changes occur slowly. As such, competition among funeral homes is long-term and mostly passive based on providing good service, maintaining an attractive facility, generating positive word of mouth, offering reasonable prices, and making pre-need sales.

- *Mortality Rate:* The demand for funeral home services is a function of the number of deaths, which, in the United States, has varied slightly from year to year due to various factors. The U.S. Census Bureau projects an 8.4% increase in the number of deaths from 2004 to 2014 and a 23.2% increase from 2004 to

2025. The graph below illustrates the historical number of deaths in the United States from 1940 to 2002 and the projected number of deaths from 2003 to 2025.

**Historical and Projected Deaths per Annum in the United States**

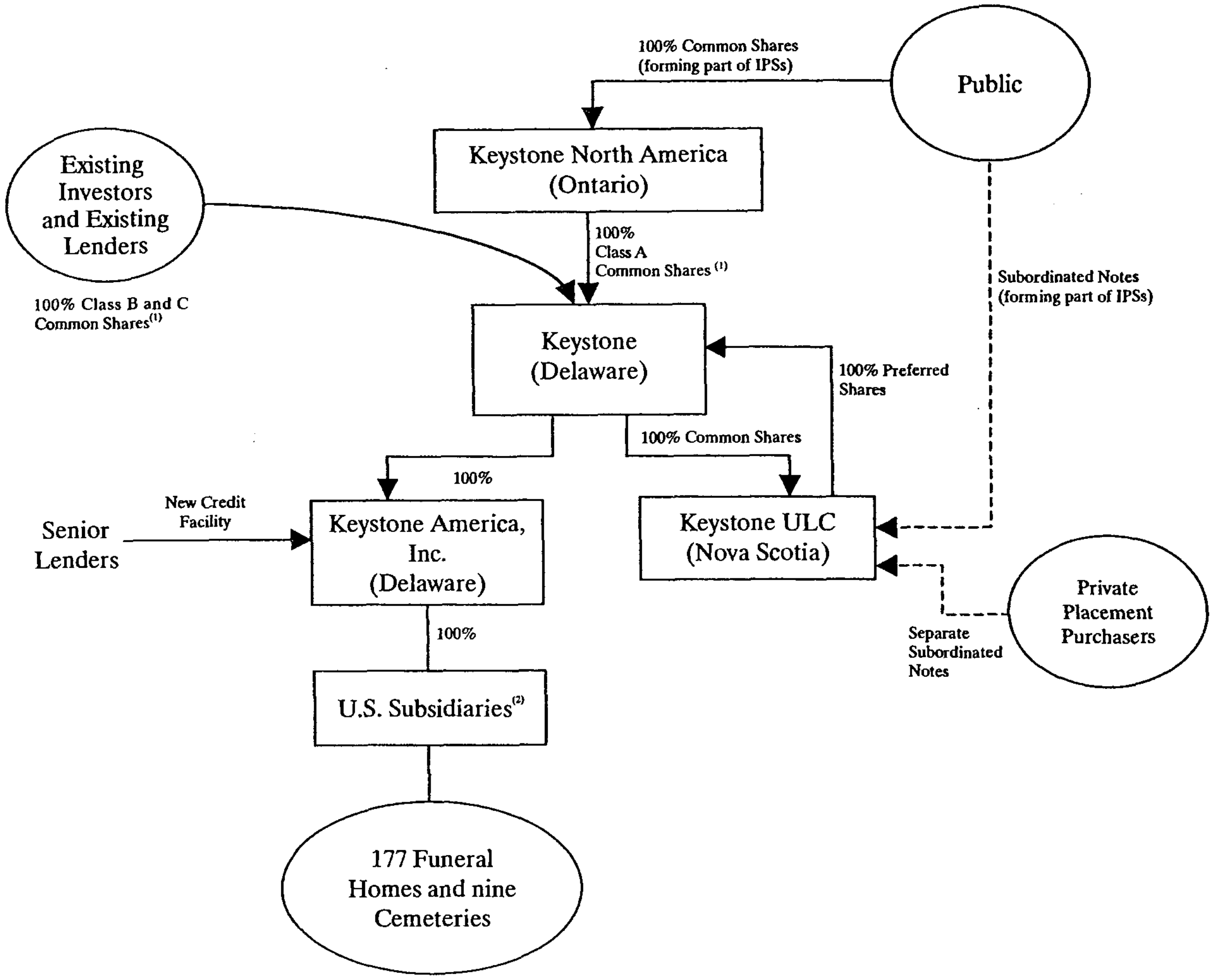



Source: Historical data — U.S. Centre for Disease Control
Projected data — U.S. Census Bureau

- *Rising Cremation Rate:* In recent years, there has been steady growth in the number of individuals and families in the United States that have chosen cremation as an alternative to a ground burial. While rates of cremation versus rates of burial are important measures, more important to the profitability of the funeral home industry is the absolute market size (*i.e.*, the total number of cremation and burial cases). In the United States, the overall population has grown substantially and is projected to continue growing. This growth has substantially muted the impact of the cremation growth rate, such that the number of burials is projected to remain roughly constant over the next twenty-five years.

## POST-CLOSING STRUCTURE

The following chart illustrates the ownership structure of the Issuer and the Company immediately after this offering and the transactions contemplated in this prospectus. See "Investment Agreement".

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(1) Upon closing, the Existing Investors (defined herein), Existing Lenders (defined herein) and certain members of management of Keystone will own all of the issued and outstanding Class B and C common shares of Keystone, representing a 14.7% voting interest in Keystone (6.3% if the over-allotment option is exercised in full). Each Class B and C common share entitles the holder to receive distributions from Keystone approximately equivalent to the distributions per IPS received by holders of IPSs. The holders of the Class B and C Common shares have the right to request that Keystone enter into good faith negotiations to repurchase their shares in certain specified circumstances. Keystone has the right to purchase for cancellation the Class B and Class C common shares in certain specified circumstances. See "Investment Agreement', "Securityholders' Agreement", "Retained Interest — Repurchase Events" and "Plan of Distribution". The Class B common shares will represent at least 10% of the aggregate value of the common shares of Keystone outstanding upon closing of the offering.

(2) The financial information of all subsidiaries is consolidated in Keystone's and Hamilton's financial statements that are contained elsewhere in this prospectus.

## SELECTED FINANCIAL AND OPERATING INFORMATION

The following table sets out selected financial and operating information for the periods indicated that has been derived from (and should be read in conjunction with) the historical financial statements of Keystone and Hamilton contained elsewhere in this prospectus:

**Financial Information**[1]

| | 12 Months Ended September 30 | Nine Months Ended September 30 | | Year Ended December 31 | | |
|---|---|---|---|---|---|---|
| | 2004 | 2004 | 2003 | 2003 | 2002 | 2001 |
| | (U.S. dollars in thousands) | | | | | |
| **Revenue** | | | | | | |
| Keystone | $48,583 | $35,856 | $36,158 | $48,885 | $50,767 | $50,852 |
| Hamilton | 37,592 | 27,564 | 27,999 | 38,026 | 40,211 | 39,337 |
| Total | $86,175 | $63,420 | $64,157 | $86,911 | $90,978 | $90,189 |
| **Cost and Expenses (including Corporate, General and Administrative)** | | | | | | |
| Keystone | $34,657 | $25,890 | $25,881 | $34,648 | $36,577 | $36,611 |
| Hamilton | 28,215 | 21,098 | 21,084 | 28,201 | 28,523 | 28,547 |
| Total | $62,872 | $46,988 | $46,965 | $62,849 | $65,100 | $65,158 |
| **EBITDA**[2] | | | | | | |
| Keystone | $14,358 | $10,328 | $10,516 | $14,546 | $14,427 | $14,795 |
| Hamilton | 9,485 | 6,626 | 8,189 | 11,083 | 13,738 | 12,913 |
| Total | $23,843 | $16,954 | $18,705 | $25,629 | $28,165 | $27,708 |
| **Capital Expenditures**[3] | | | | | | |
| Keystone | $ 1,481 | $ 1,222 | $ 1,289 | $ 1,549 | $ 1,470 | $ 1,083 |
| Hamilton | 1,247 | 587 | 962 | 1,621 | 1,415 | 1,146 |
| Total | $ 2,728 | $ 1,809 | $ 2,251 | $ 3,170 | $ 2,885 | $ 2,229 |
| **Normalized Revenue**[2] | | | | | | |
| Keystone | $47,923 | $35,410 | $35,121 | $47,634 | $47,961 | $46,949 |
| Hamilton | 37,592 | 27,564 | 27,999 | 38,026 | 40,211 | 38,607 |
| Total | $85,515 | $62,974 | $63,120 | $85,660 | $88,172 | $85,556 |
| **Normalized EBITDA**[2] | | | | | | |
| Keystone | $14,117 | $10,156 | $10,396 | $14,358 | $14,018 | $13,654 |
| Hamilton | 9,377 | 6,466 | 6,915 | 9,826 | 11,688 | 10,613 |
| Total | $23,494 | $16,622 | $17,311 | $24,184 | $25,706 | $24,267 |

## Operating Information

| | As at September 30 | | As at December 31 | | |
|---|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 | 2001 |
| **Number of funeral homes** | | | | | |
| Keystone | 97 | 101 | 101 | 106 | 107 |
| Hamilton | 80 | 86 | 86 | 92 | 93 |
| Total | 177 | 187 | 187 | 198 | 200 |
| **Number of cases** | | | | | |
| Keystone | 7,557 | 7,865 | 10,664 | 11,144 | 11,091 |
| Hamilton | 6,002 | 6,502 | 8,694 | 9,377 | 9,274 |
| Total | 13,559 | 14,367 | 19,358 | 20,521 | 20,365 |
| **Average funeral revenue per case** | | | | | |
| Keystone | $4,368 | $4,218 | $ 4,235 | $ 4,116 | $ 4,180 |
| Hamilton | 4,547 | 4,633 | 4,600 | 4,591 | 4,590 |
| Combined Average | $4,447 | $4,406 | $ 4,394 | $ 4,333 | $ 4,367 |

(1) The financial information presented in this table is derived from our Canadian GAAP based financial statements. Management does not believe that the presentation of the above financial information would be materially different if reported using accounting principles generally accepted in the United States.

(2) EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may not be comparable to similar measures presented by other companies. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash" and "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". As the Issuer intends to distribute substantially all of the Issuer's cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA and Distributable Cash are important measures in evaluating the Issuer's performance and in determining whether to invest in IPSs.

(3) Virtually all capital expenditures over the period presented represent maintenance capital expenditures. See "Our Business — Capital Expenditures".

## SUMMARY OF DISTRIBUTABLE CASH OF THE ISSUER

The following analysis has been prepared by management on the basis of the information contained in this prospectus and management's estimate of the amount of expenses and expenditures that would have been incurred by the Issuer during the 12 months ended September 30, 2004 had the Issuer been in existence during such period and had the transactions described under the caption "Investment Agreement" been completed at the beginning of that period. **This analysis is not a forecast or projection of future results. The actual results of our operations for any period whether before or after the closing of this offering will differ from the amounts set forth in the following analysis, and such differences may be material.** Additionally, our operations are subject to risks, and in reviewing the following summary of distributable cash, investors are encouraged to consider the risks described under the caption "Risk Factors".

Management believes that, upon completion of this offering, the Issuer and the Company will incur interest expenses, additional administrative expenses and taxes that will differ from those contained in the historical financial statements of Keystone and Hamilton and the *pro forma* financial statements of Keystone North America that are included elsewhere in this prospectus. In addition, we intend to continue to make maintenance capital expenditures consistent with past practices. In order to minimize the impact of fluctuations in the rate of exchange between the Canadian dollar and U.S. dollar to those currently in effect, we intend to enter into a five-year hedging arrangement to fix the rates of exchange between the Canadian dollar and U.S. dollar for substantially all of the amount of distributable cash reflected in the following table. See "Our Business — Currency Hedging Policy". Although management does not have firm commitments for all of these costs, expenses and expenditures and, accordingly, the complete financial impact of these items are not objectively determinable, management believes, based on past experience, that the following represents a reasonable estimate of the amount of cash that would have been available for distribution for the last twelve months ended September 30, 2004 had Keystone North America been in existence during such period and had the transactions described under the caption "Investment Agreement" and "Post-Closing Structure" been completed at the beginning of the period:

| *(In thousands except per IPS numbers and hedge rate)* | **Twelve months ended September 30, 2004** |
|---|---|
| Combined Normalized EBITDA(1)(2) | $23,494 |
| Management believes that the following items will increase (reduce) the amount available for distribution by the Issuer: | |
| Cost savings from Hamilton acquisition(3) | 2,187 |
| Maintenance capital expenditures | (2,900) |
| Additional administrative expenses(4) | (1,000) |
| Interest on new credit facility(5) | (3,070) |
| Interest on Separate Subordinated Notes(6) | (1,182) |
| Income taxes paid in cash | (341) |
| Distributable Cash before Cash Holdback | $17,188 |
| Distributable Cash Holdback (5%) | 859 |
| Distributable Cash | 16,329 |
| Summary of Distributable Cash: | |
| Interest on Subordinated Notes forming part of IPSs | 8,660 |
| Dividends on Common Shares forming part of IPSs | 5,274 |
| Dividends on Class B and C Shares | 2,395 |
| Distributable Cash | $16,329 |
| Hedge Rate (C$ per US$)(7) | 1.2272 |
| Distributable Cash (C$)(1) | $20,039 |
| Distributable Cash for IPS Unitholders | 13,934 |
| Distributable Cash for IPS Unitholders (C$) | 17,100 |
| Distributable Cash per IPS (C$) | $ 1.00 |

(1) EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may not be comparable to similar measures presented by other companies. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash" and "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". As the Issuer intends to distribute substantially all of the Issuer's cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA and Distributable Cash are important measures in evaluating the Issuer's performance and in determining whether to invest in IPSs.

(2) *Pro forma* for the acquisition of Hamilton and Keystone.

(3) Includes reductions in Hamilton corporate overhead costs comprised primarily of headcount reductions, elimination of their corporate offices, and related expenses (rent, travel, healthcare, etc.) and $300,000 in procurement savings related to casket purchases.

(4) Represents estimated administrative expenses to be incurred following the offering in connection with ongoing public disclosure requirements, investor relations, director fees and other expenses.

(5) Represents estimated interest on New Credit Facility based on an average of outstanding balances.

(6) Interest is payable in C$ and is calculated using the hedge rate described in the table and note (7).

(7) Based on a five-year C$/US$ hedge rate as of January 28, 2005.

Management believes that the method of determining distributable cash presented in this prospectus is comparable to cash flow from operating activities before capital expenditures, certain interest expenses and changes in working capital. In addition, the Issuer's method of determining distributable cash is derived from net income, which is a measure recognized under GAAP. Net income has been used as the basis for the calculation of Distributable Cash because a pro forma statement of cash flows for the Issuer is not available, only a pro forma of net income (or loss). This method presents cash that is intended to be distributable based on the results of the relevant period, after adjusting for the items set out in the above table. See "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash".

## THE OFFERING

**Offering:** 17,100,000 IPSs.

**Amount:** C$171,000,000

**Price:** C$10.00 per IPS.

**Over-Allotment Option:** The Issuer has granted to the Underwriters an over-allotment option to purchase up to 1,668,017 additional IPSs at a price of C$10.00 per IPS for the purpose of covering over-allotments, if any, and for market stabilization purposes. The over-allotment option is exercisable from time to time in whole or in part until 30 days following the closing of this offering. The net proceeds received from any exercise of the over-allotment option will be used by the Issuer to acquire additional Class A common shares and preferred shares of Keystone, which will in turn use such amounts to redeem Class C common shares of Keystone held by Keystone's existing equity holders and debt holders and certain of Hamilton's existing debt holders, being:

- in the case of Keystone, Golder, Thoma, Cressey, Rauner Fund V, L.P., GTCR Associates V, Robert G. Horn, Steven A. Tidwell, (collectively, the "Existing Investors") Heller Financial Inc. and Antares Capital Corporation; and
- in the case of Hamilton, TCW Leveraged Income Trust, L.P., TCW Leveraged Income Trust II, L.P., TCW/Crescent Mezzanine Partners II, L.P., TCW/Crescent Mezzanine Trust II, Massachusetts Mutual Life Insurance Company, MassMutual Corporate Investors, MassMutual Participation Investors, Berkshire Fund III, A Limited Partnership, Berkshire Investors LLC, SBIC Partners, L.P. and DFW Capital Partners L.P. (collectively and together with Heller Financial Inc. and Antares Capital Corporation, the "Existing Lenders").

If the over-allotment option is exercised in full, the Issuer will own a 93.7% voting interest in Keystone and the Existing Investors, Existing Lenders and certain members of management of Keystone will own a 6.3% voting interest. See "Plan of Distribution" and "Use of Proceeds".

**IPS Attributes:** Each IPS represents: (a) one Common Share; and (b) C$4.286 principal amount of Subordinated Notes.

The ratio of Common Shares to principal amount of Subordinated Notes represented by an IPS is subject to change in the event of a share split, consolidation or reclassification, or upon a partial redemption or repurchase of the Subordinated Notes.

Holders of IPSs will have the right to separate the IPSs into Common Shares and Subordinated Notes at any time after 45 days following the original issuance or upon the occurrence of a change of control of Keystone ULC. Separation of the IPSs will occur automatically upon a repurchase, redemption or maturity of the Subordinated Notes. Similarly, holders of Common Shares and Subordinated Notes may, at any time prior to an automatic separation of the Subordinated Notes, combine the applicable number of Common Shares and principal amount of Subordinated Notes to form IPSs. See "Description of the IPSs".

The Toronto Stock Exchange, or "TSX", has conditionally approved the listing of the IPSs and Common Shares. Listing is subject to the Issuer fulfilling all of the requirements of the TSX on or before April 22, 2005.

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| **Use of Proceeds:** | The estimated net proceeds from this offering, after deducting fees payable to the Underwriters and estimated expenses of this offering, will be approximately C$155.4 million. In addition, approximately C$10 million additional net proceeds will be raised from the sale of the Separate Subordinated Notes by Keystone ULC. Upon completion of a series of transactions, Keystone North America will acquire 100% of the Class A common shares of Keystone; Keystone ULC will acquire 100% of the preferred shares of Keystone; and the Existing Investors will acquire Class B and C common shares of Keystone and receive cash of approximately C$25.6 million. In connection with this offering, a bonus will be paid totaling approximately US$1.7 million cash and approximately 95,261 Class B common shares to 17 members of Keystone management. These amounts shall be paid with cash and shares that would otherwise be payable to the Existing Investors and Existing Lenders. In connection with the completion of this offering, Keystone expects to acquire the business of Hamilton in consideration for cash of C$69.9 million and the issuance of Class B and C common shares of Keystone. The remainder of the net proceeds, plus certain amounts to be drawn under the New Credit Facility, will be used to repay existing indebtedness of Keystone and Hamilton, establish and fund a restricted account to pay former owner obligations of Keystone and Hamilton, and pay for transition costs associated with the Hamilton acquisition. Upon closing of this offering, the Issuer will own all of the issued and outstanding Class A common shares and preferred shares of Keystone, representing a 85.3% voting interest in Keystone; and the Existing Investors, Existing Lenders and certain members of management of Keystone will own all of the issued and outstanding Class B and C common shares of Keystone, representing a 14.7% voting interest in Keystone.<br><br>If the over-allotment option is exercised, the Issuer will use the net proceeds from the exercise of the option to acquire additional Class A common shares and preferred shares of Keystone, which will in turn use such amounts to redeem Class C common shares held by the Existing Investors and Existing Lenders. If the over-allotment option is exercised in full, the Issuer will own a 93.7% voting interest in Keystone and the Existing Investors, Existing Lenders and certain members of management of Keystone will own a 6.3% voting interest in Keystone.<br><br>See "Use of Proceeds" and "Investment Agreement". |
| **Offering of Separate Subordinated Notes:** | In connection with the offering, Keystone ULC is also selling, on a private placement basis, C$10 million principal amount of Separate Subordinated Notes. The Separate Subordinated Notes will be identical in all respects to the Subordinated Notes represented by IPSs and will be issued under the same indenture. Accordingly, holders of Separate Subordinated Notes and holders of Subordinated Notes represented by IPSs will vote together as a single class, in proportion to the aggregate amount of Subordinated Notes they hold, on all matters on which they are eligible to vote under the indenture. See "Separate Subordinated Notes Offering". The completion of the offering of Separate Subordinated Notes is a condition to the Issuer's sale of IPSs. |
| **New Credit Facility:** | Keystone America, Inc., a subsidiary of Keystone, will arrange for a new credit facility (the "New Credit Facility"). Upon completion of the offering and transactions contemplated by the investment agreement, approximately $43.1 million will be drawn on the New Credit Facility under the term loan |

portion. No amounts are expected to be drawn under the $15 million revolving facility that will be available for future borrowings. See "New Credit Facility".

**Retained Interest:**

Upon closing, the Existing Investors, Existing Lenders and certain members of management will own all of the issued and outstanding Class B and C common shares of Keystone, representing a 14.7% voting interest in Keystone (6.3% if the over-allotment option is exercised in full). Each Class B and C common share entitles the holder to receive distributions from Keystone approximately equivalent to the distributions per IPS received by holders of IPSs. The holders of the Class B and C common shares have the right to request that Keystone enter into good faith negotiations to repurchase their shares in certain specified circumstances. Keystone has the right to purchase for cancellation the Class B and Class C common shares in certain specified circumstances. See "Investment Agreement", "Securityholders' Agreement", "Retained Interest — Repurchase Events" and "Plan of Distribution". The Class B common shares will represent at least 10% of the aggregate value of the common shares of Keystone outstanding upon closing of the offering.

**Distribution Policy of Keystone North America:**

The board of directors of Keystone North America will adopt a policy that Keystone North America will distribute its available cash to the maximum extent possible, subject to applicable law, by way of equal monthly distributions of dividends on the Common Shares represented by the IPSs, after:

- satisfying its debt service or other obligations, if any, under credit facilities or other agreements with third parties;
- satisfying its interest and other expense obligations, including any applicable taxes; and
- retaining reasonable working capital or other reserves as may be considered appropriate by the board of directors of Keystone North America.

The board of directors of Keystone North America may, in its discretion, amend or repeal its dividend policies in respect of the Common Shares. Keystone North America's board of directors may decrease the level of dividends provided for in any one or more of its dividend policies in respect of the Common Shares or discontinue entirely the payment of dividends in respect of the Common Shares.

See "Description of Share Capital of Keystone North America and Keystone ULC — Interest Payments and Dividend Policy".

**Dividend and Distribution Policies of Keystone:**

The board of directors of Keystone is expected to adopt dividend policies in respect of its Class A common shares pursuant to which, in the event and to the extent it has any available cash for distribution to the holders of Class A common shares of Keystone as of the dates such dividends are declared and paid, and subject to applicable law and the terms of the New Credit Facility, the indenture governing the Subordinated Notes and any other then outstanding indebtedness of and the prior payment of distributions in respect of the preferred shares, the Class B common shares and Class C common shares of Keystone, the board of directors of Keystone will declare cash dividends on the Class A common shares. Distributions in respect of and dividends on its common and preferred shares will be paid on or before the

$15^{th}$ day of each month (or the next business day if such day is not a business day).

Pursuant to the terms of the preferred shares, cumulative, preferential dividends will be paid at a rate per annum of 14.51%.

The holders of the Class B and C common shares will be entitled to receive, as and when declared by Keystone's board of directors, fixed cumulative preferential cash dividends at a rate of approximately C$0.6215 per share per annum, to be paid after the distributions in respect of the preferred shares and prior to any dividend on the Class A common shares.

After payment of the aforementioned distributions, dividends paid by Keystone shall: (i) for periods ending on or before the second anniversary of the closing of this offering, be paid *pro rata* to holders of the Class A, Class B and Class C common shares; and (ii) for periods ending after the second anniversary of the closing of this offering, be paid to the holders of Class B and Class C common shares in an amount on a per share basis equal to 1.1 times the dividend per share that the holders of the Class A common shares are entitled.

Dividend payments are not mandatory or guaranteed. The board of directors of Keystone may, in its discretion, amend or repeal its dividend policies in respect of its common shares. Keystone's board of directors may decrease the level of dividends provided for in each dividend policy in respect of its common shares or discontinue entirely the payment of dividends in respect of its common shares. In addition, Keystone's ability to pay dividends will be restricted if it does not meet certain financial tests in the New Credit Facility and the indenture governing the Subordinated Notes.

**Keystone North America Common Share Attributes:**

*Common Shares Outstanding:* 17,100,000 Common Shares will be outstanding following the completion of the offering (18,768,017 Common Shares if the Underwriters' over-allotment option is exercised in full).

*Voting Rights:* Each outstanding Common Share carries one vote per share and, subject to applicable law, the Common Shares vote as a class on all matters presented to the shareholders for a vote.

*Listing:* Closing of the offering is conditional on, among other things, the approval for listing of the Common Shares on the TSX.

**Keystone ULC Subordinated Note Attributes:**

*Subordinated Notes Outstanding:* C$73,290,600 aggregate principal amount of 14.5% Subordinated Notes will be outstanding following the completion of this offering (C$80,439,721 aggregate principal amount if the Underwriters' over-allotment is exercised in full). Such Subordinated Notes will be represented by IPSs issued under this prospectus.

*Separate Subordinated Notes Outstanding:* C$10 million aggregate principal amount of Separate Subordinated Notes will be outstanding following the completion of this offering. Such Separate Subordinated Notes are being sold on a private placement basis and do not form part of the IPSs issued under this prospectus. The distribution of the Separate Subordinated Notes is not qualified under this prospectus.

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| *Market:* | In certain circumstances, the Subordinated Notes and Common Shares represented by the IPSs will separate. There is no market through which the Subordinated Notes may be sold and purchasers may not be able to resell Subordinated Notes purchased under this prospectus. BMO Nesbitt Burns Inc., one of the Underwriters, has advised the Issuer that it currently intends to facilitate a market in the Subordinated Notes subject to customary market practice and applicable legal and regulatory requirements and limitations. |
| *Interest Rate:* | 14.5% per annum. |
| *Record and Payment Dates:* | Interest will be paid monthly in arrears on or before the 15th day of each month (or the next business day if such day is not a business day) commencing on March 15, 2005, to holders of record on the last business day of the preceding month. |
| *Interest Deferral:* | Prior to the fifth anniversary of the closing of the offering, Keystone ULC will be permitted to defer interest payments on the Subordinated Notes if and for so long as the most recently calculated interest coverage ratio of Keystone for the twelve-month period ended on the last day of any month is less than the applicable interest deferral threshold described under "Description of Notes — Certain Definitions"; *provided, however*, that no such deferral may be commenced, and any ongoing deferral shall cease, if a default in payment of interest, principal or premium, if any, on the Subordinated Notes has occurred and is continuing, or any other event of default with respect to the Subordinated Notes has occurred and is continuing and the Subordinated Notes have been accelerated as a result of the occurrence of such event of default. Interest payments will not be deferred under this provision for more than 24 months in the aggregate or beyond the fifth anniversary of the closing of the offering.<br><br>In addition, on up to eight occasions after the fifth anniversary of the closing of the offering, interest payments on the Subordinated Notes may again be deferred, at Keystone ULC's option; *provided, however*, that no such deferral may be commenced, and any ongoing deferral shall cease, if a default in payment of interest, principal or premium, if any, has occurred and is continuing, or any other event of default with respect to the Subordinated Notes has occurred and is continuing and the Subordinated Notes have been accelerated as a result of the occurrence of such event of default. Interest payments will not be deferred under this provision for more than eight months on any occasion. No interest deferral period after the fifth anniversary of the closing of the offering may commence unless and until all interest deferred pursuant to any preceding interest deferral period, together with interest thereon, has been paid in full.<br><br>Deferred interest on the Subordinated Notes will bear interest at the same rate as the stated rate on the Subordinated Notes, compounded monthly, until paid in full. Following the end of any interest deferral period, Keystone ULC will be obligated to resume monthly payments of interest on the Subordinated Notes, including interest payments on deferred interest. Keystone ULC will be obligated to repay all interest deferred prior to the fifth anniversary of the closing of the offering, including interest accrued on deferred interest, on the fifth anniversary of the closing of the offering. Pursuant to the terms of the indenture, Keystone ULC may prepay deferred interest at any time, except when an interest deferral period is in effect; however, the New Credit Facility contains limitations on Keystone ULC's |

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| | ability to prepay deferred interest. See "New Credit Facility." Keystone ULC will be obligated to repay all interest deferred after the fifth anniversary of the closing of the offering, including interest accrued on deferred interest, on or before maturity, provided that at the end of any interest deferral period following the fifth anniversary of the closing of the offering, Keystone ULC may not further defer interest unless and until all deferred interest, including interest accrued on deferred interest, is paid in full.<br><br>If interest payments on the Subordinated Notes are deferred, holders may be required to include interest in their income for Canadian federal income tax purposes on an economic accrual basis even if they do not receive any cash interest payments. |
| *Maturity Date:* | The Subordinated Notes will mature 12 years after the date of issuance. |
| *Principal Repayment:* | On maturity, Keystone ULC will repay the indebtedness represented by the Subordinated Notes by paying the indenture trustee, on behalf of the holders, an amount equal to the principal amount of the outstanding Subordinated Notes, together with accrued and unpaid interest. |
| *Optional Redemption:* | On or after the fifth anniversary of the closing of the offering, Keystone ULC may redeem the Subordinated Notes, at its option, at any time in whole and from time to time in part, upon not less than 30 nor more than 60 days' notice, for cash, at the redemption prices set forth herein together with, in each case, accrued but unpaid interest to the date of redemption. Any exercise by Keystone ULC of its option to redeem Subordinated Notes, in whole or in part, will result in an automatic separation of the IPSs into Common Shares and Subordinated Notes. |
| *Change of Control:* | Upon the occurrence of a Change of Control, as defined under "Description of Subordinated Notes — Change of Control", Keystone ULC will be required to make an offer to each holder of Subordinated Notes to repurchase that holder's Subordinated Notes at a price equal to 101% of the principal amount of the Subordinated Notes being repurchased, plus any accrued but unpaid interest to the date of repurchase. However, a holder of IPSs will not be able to have its Subordinated Notes repurchased unless such holder surrenders the IPSs to the depositary, and receives delivery of the Common Shares and Subordinated Notes represented thereby. |
| *Security and Guarantees:* | The Subordinated Notes will be an unsecured obligation of Keystone ULC and will be guaranteed by Keystone and each direct and indirect U.S. domestic subsidiary of Keystone. These guarantees will be subordinate in right of payment to all existing and future senior indebtedness of the guarantors, including under the New Credit Facility. |
| *Ranking:* | The Subordinated Notes will be unsecured senior subordinated indebtedness of Keystone ULC and will be subordinated in right of payment, as set forth in the indenture governing the Subordinated Notes, to all existing and future senior indebtedness of Keystone ULC. |
| *Restrictive Covenants:* | The indenture governing the Subordinated Notes will contain covenants with respect to Keystone and Keystone ULC that will restrict:<br>• the incurrence of additional indebtedness;<br>• the payment of dividends on, and repurchase of, common shares of Keystone;<br>• a number of other types of payments, including certain investments;<br>• specified sales of assets; |

- specified transactions with affiliates; and
- consolidations, mergers and transfers of all or substantially all of the assets of Keystone and Keystone ULC.

The limitations and prohibitions described above are subject to a number of important qualifications and exceptions described under "Description of Subordinated Notes — Certain Covenants".

**Canadian Income Tax Considerations:**

In acquiring an IPS, a holder will be acquiring ownership of a Common Share and C$4.286 aggregate principal amount of Subordinated Notes represented by such IPS. The price paid by a holder for an IPS must be allocated on a reasonable basis between the Common Share and the Subordinated Notes represented by the IPS in order to determine their respective cost to the holder for purposes of the *Income Tax Act* (Canada) and the regulations thereunder (the "Tax Act"). Keystone North America and Keystone ULC will allocate the price paid for each IPS on the basis of C$5.714 to the Common Share and C$4.286 to the Subordinated Notes represented by each IPS, and by purchasing an IPS the holder is deemed to agree to such allocation and agrees not to take a contrary position for any purpose. Since a holder who holds an IPS will own the Common Share and Subordinated Notes represented by such IPS, the Canadian federal income tax consequences of owning an IPS (including the taxation of dividends and interest on the Common Share and Subordinated Notes, respectively, and the tax treatment of disposing of the Common Share and Subordinated Notes upon the disposition of an IPS representing such securities) will not differ from those associated with owning those securities. In particular, a holder will be required to include in computing its income for a taxation year all interest on the Subordinated Notes that accrues or becomes receivable or is received by the holder in that year. Also, dividends on the Common Shares received by a holder will be required to be included in computing the holder's income for purposes of the Tax Act. See "Certain Canadian Federal Income Tax Considerations".

**U.S. Income Tax Considerations for Non-U.S. Holders:**

Ownership of IPSs should be treated for U.S. federal income tax purposes as direct ownership of the Common Shares and Subordinated Notes constituting the IPSs, and the purchase price of an IPS should be allocated between its constituent Common Share and Subordinated Note in proportion to their respective fair market values at the time of purchase. Assuming the Subordinated Notes are treated as debt for U.S. federal income tax purposes, Keystone will be treated as the issuer of the notes and will be treated as paying interest directly to IPS holders. A Non-U.S. Holder, as defined in "Certain U.S. Federal Income Tax Considerations," will generally not be subject to U.S. federal income tax or withholding tax with respect to interest paid on the Subordinated Notes or with respect to distributions on the Common Shares, provided the Non-U.S. Holder satisfies certain documentation requirements and is not a Disqualified Recipient, as defined in "Description of the Subordinated Notes — Certain Definitions", and such interest and distributions are not effectively connected with such holder's conduct of a trade or business within the U.S.

Kirkland & Ellis LLP, U.S. tax counsel to the Issuer, and Torys LLP, U.S. tax counsel to the Underwriters (together, "U.S. Tax Counsel"), have advised the Issuer and the Underwriters, as applicable, that the Subordinated Notes should be treated as debt for U.S. federal income tax purposes. Therefore, Keystone intends to deduct interest paid on the Subordinated Notes in computing its U.S. taxable income. However, there is no authority that directly addresses the tax treatment of securities similar to the Subordinated Notes that are offered in circumstances similar to this offering (*i.e.*, as part of a unit that includes Common Shares). In light of this absence of direct authority, U.S. Tax Counsel cannot conclude with certainty that the Subordinated Notes will be treated as debt for U.S. federal income tax purposes, and, although Keystone intends to take the position that the Subordinated Notes are debt for U.S. federal income tax purposes, there can be no assurance that this position will not be challenged by the Internal Revenue Service. If such a challenge were sustained, interest payments on the Subordinated Notes would be recharacterized as non-deductible distributions with respect to Keystone ULC's equity, and Keystone's net taxable income and thus its U.S. federal income tax liability would be materially increased. As a result, Keystone's after-tax cash flow would be reduced and Keystone ULC's ability to make interest payments on the Subordinated Notes and Keystone North America's ability to make distributions with respect to the Common Shares could be materially and adversely impacted. In addition, if the Subordinated Notes are treated as equity, Keystone could be liable for U.S. withholding taxes on any interest previously paid to Non-U.S. Holders.

Prospective purchasers should consult their own tax advisors regarding the U.S. federal and state tax implications of an investment in IPSs. See "Certain U.S. Federal Income Tax Considerations".

**Risk Factors:**

The risks associated with an investment in the IPSs and the underlying Common Shares and Subordinated Notes include:

With respect to the business: changes in the number of deaths are difficult to predict from market to market over the short term; our high fixed cost base makes us vulnerable to fluctuations in revenue; increasing number of cremations in the United States; we may not respond effectively to changing consumer preferences; increase in price competition in the funeral home and cemetery markets; we require access to capital resources to successfully acquire businesses and further issuances of securities could result in dilution; we may not successfully integrate Hamilton into our existing operations; increasing insurance benefits related to prearranged funeral contracts funded through life insurance or annuity contracts may not cover future increases in the cost of providing a price guaranteed funeral service; earnings from and principal of trust funds and escrow accounts could be reduced; we depend on our key personnel for the future success of the business and may have difficulty retaining or attracting such persons; increased advertising or more effective marketing by competitors could cause us to lose market share and revenue or cause us to incur increased costs in order to retain or recapture our market share; changes or increases in, or failure to comply with, regulations and licensing requirements; and environmental regulations governing our activities could become more stringent in the future and require us to expend additional funds for environmental compliance.

With respect to the capital structure: the Issuer is dependent on the Company for all cash available for distributions; a significant amount of our cash is distributed, which may restrict potential growth; the Issuer may not receive dividends from Keystone provided for in the dividend policy the board of directors of Keystone is expected to adopt or any dividends at all; subject to restrictions set forth in the indenture, the Issuer may defer the payment of interest to holders of the Subordinated Notes (including holders of IPSs) for a significant period of time; fluctuations in the exchange rate may impact the amount of cash available to the Issuer for distribution; our substantial consolidated indebtedness could negatively impact our business; Keystone ULC may not be able to make an offer to repurchase the Subordinated Notes upon a change of control as required by the indenture; changes in the Issuer's credit worthiness may affect the value of the IPSs, Common Shares and Subordinated Notes; the restrictive covenants in our New Credit Facility and the Indenture (as defined herein) could impact our business and affect our ability to pursue our business strategies; deferral of interest payments may have adverse Canadian federal income tax consequences for holders and may adversely affect the trading price of the IPSs; future sales, or the possibility of future sales of a substantial amount, of IPSs, Common Shares or Subordinated Notes may impact the price of the IPSs, the Common Shares and Subordinated Notes and could result in dilution; the U.S. Internal Revenue Service may challenge the characterization of the Subordinated Notes as debt; if the Issuer subsequently issues Subordinated Notes with significant OID (as defined herein), the Issuer may not be able to deduct all of the interest on the Subordinated Notes; an allocation of IPS purchase price that results in OID may reduce the amount a holder can recover upon an acceleration of the payment of principal due on the Subordinated Notes or in the event of the Issuer's bankruptcy; the Company or other payor may not be able to properly report OID to the holders of IPSs or Subordinated Notes and the IRS, and hence may become subject to substantial IRS penalties for such failure; the Subordinated Notes issued in this offering or Subordinated Notes issued in a subsequent offering may have OID for U.S. federal income tax purposes; certain U.S. tax considerations may discourage third parties from pursuing a tender offer, take-over bid or other change of control transaction; we may not be able to make all principal payments on the Subordinated Notes; there is no public market for the IPSs, Common Shares and Subordinated Notes and holders may have limited liquidity; the market price for the IPSs, Common Shares or Subordinated Notes may be volatile; the Company's interest deductions on the Subordinated Notes are likely "dual consolidated losses" for U.S. federal income tax purposes and may result in disallowance of interest deductions if certain "triggering events" occur; recent federal U.S. income tax legislation; ownership change will limit our ability to use certain losses for U.S. federal income tax purposes and may increase our tax liability; and because Keystone, the promoter of this offering, is organized under the laws of a foreign jurisdiction and resides outside of Canada, certain civil liabilities and judgments may not be enforceable against it.

Cash distributions on the Common Shares and payments of interest and principal on Subordinated Notes are not assured and are dependent on our financial performance, debt covenants and other contractual obligations, working capital requirements, future capital requirements and the deductibility for U.S. federal income tax purposes of interest payments on the Subordinated Notes, all of which are susceptible to a number of risks. See "Risk Factors".

## THE ISSUER AND KEYSTONE

### Keystone North America

Keystone North America is a corporation established under the laws of Ontario. Upon completion of this offering, Keystone North America will own all of the Class A common shares of Keystone. The registered head office of Keystone North America is located at Suite 2400, 250 Yonge Street, Toronto, Ontario, M5B 2M6.

### Keystone ULC

Keystone ULC is an unlimited liability company organized under the laws of Nova Scotia. Upon completion of this offering, Keystone ULC will own all of the preferred shares of Keystone. The head office of Keystone ULC is located at Suite 2400, 250 Yonge Street, Toronto, Ontario, M5B 2M6.

### Keystone

We are a leading owner and operator of funeral homes across the United States. Upon completion of this offering and Keystone's acquisition of Hamilton, we will be the owner of a funeral service business with 177 funeral homes and nine cemeteries and, in management's estimate, will be the fifth largest provider of funeral services in the United States. Generally, our funeral homes are located in the Midwest, Northeast, Southeast and Northwest regions of the continental United States with individual service markets primarily made up of non-urban areas.

Our funeral homes represent well-established businesses with an average age of the original business in excess of 50 years. In our respective markets, our funeral homes have historically provided a full range of funeral services on both an at-need (at time of death) and pre-need basis (prior to death). These services include removal of human remains, planning and coordinating personalized funerals and cremations, professional embalming, use of our funeral home facilities, merchandise sales, conducting memorial services, performing cremation and cemetery interment services.

Our executive management team consists of four seasoned funeral professionals who collectively have spent 125 years successfully acquiring, integrating and managing funeral businesses. Local management is comprised substantially of former owners, their former managers and their other key employees. We have very strong relationships with the former owners of these funeral businesses, with over 80% still actively supporting our funeral homes in some significant way.

Keystone is a corporation established under the laws of Delaware with its registered head office at 400 North Ashley Drive, Suite 1900, Tampa, Florida.

## INDUSTRY OVERVIEW

### Introduction

"Death care" is the overarching term used to refer to the interrelated funeral home and cemetery industry. Funeral homes furnish goods and services relating to the preparation of the body and memorialization of the deceased. Cemeteries furnish property and goods relating to permanent disposition and remembrance. Both funeral homes and cemeteries may offer cremation. In addition there are cremation specialists that offer, solely or primarily, cremation.

The primary goods and services provided by funeral homes and cemeteries consist of the following:

- *Funeral homes:* Professional services related to funerals, including preparation of the body; arrangement of memorial services; use of funeral facilities and motor vehicles; sale of caskets, urns, burial vaults, burial garments; cremation.
- *Cemeteries:* Sale of interment rights associated with cemetery property including lots, lawn crypts, and mausoleum spaces; sale of related merchandise including stone and bronze memorials and burial vaults; cremation.

There are several fundamental differences between the funeral business and the cemetery business. First, the funeral business is a service business while the cemetery business is primarily an interment rights or property business. As a result, the funeral business has much greater cash flow stability as services are provided at time of need and are non-discretionary items that have predictable long-term demand. Cemetery revenue is largely derived on pre-need or advance sales that are discretionary and subject to greater volatility. Additionally, cemetery sales create an ongoing obligation between the cemetery and the customer whereas funeral services are completed at time of death. Finally, funeral homes have more stringent licensing and education requirements than cemeteries, increasing barriers to entry.

Management estimates that there are approximately 22,000 funeral homes and 10,500 cemeteries in the United States with small family-owned businesses generating approximately 80% of the death care industry's total revenue and the four major U.S. publicly listed companies in the industry (Service Corporation International, Alderwoods Group, Inc., Stewart Enterprises, Inc. and Carriage Services, Inc.) comprising the remaining 20%. Total revenue for the death care industry in 2004 is expected to exceed $15 billion. Management believes that the four major U.S. public death care companies operate approximately 11% and 7% of the funeral homes and cemeteries in the United States, respectively, and serve approximately 22% of the total funeral cases in the United States.

**Attributes of the Funeral Home Business**

The funeral home business is one of the more stable industries in the U.S. Local funeral home businesses generally enjoy predictable cash flow due to a variety of favourable attributes, including:

- *Predictable and Stable Demand:* Funeral service is both stable, due to the inevitability of death, and essential, due to the legal need to properly dispose of the body and the religious and cultural need to memorialize the deceased. The U.S. Census Bureau projects a 23.2% increase in the number of deaths from 2004 to 2025 due in part to the aging of the "Baby Boom" population.
- *Significant Barriers to Entry:* Entry of a new funeral home in an established market can be difficult due to the importance of local heritage and tradition. A recent comprehensive industry survey found that location, reputation, previous experience and pre-need services are the most important factors in selecting a funeral home. High barriers to entry also include significant capital investment needed to start a new funeral home and the long time needed to develop a sufficient volume of business to provide adequate returns. Other challenges to new businesses include local zoning restrictions, regulatory burdens (including licensing) and a scarcity of prime locations.
- *Mature Competition Base:* The funeral industry is a very mature industry with most areas already adequately served by one or more funeral homes that through decades of operations have developed a strong reputation and heritage in their community. Since reputation and heritage are among the strongest factors influencing consumer choice, there is less incentive or opportunity to compete on price and new funeral homes tend only to open in areas of new development and population growth.
- *Attractive Margins:* The funeral home industry has demonstrated very strong operating margins, due in part to the focus of client families on heritage and tradition rather than on price, as well as the steady and predictable level of demand that most funeral homes enjoy. With a largely fixed cost structure, revenue achieved through case count increases typically generate substantial improvements in both margins and cash flow. In addition, due to relatively limited variable costs, incremental revenue earned through efforts to expand products and services sold, including additional services in connection with cremations, has led to superior margins at individual locations. Further improvements in margins have been achieved when individual facilities are clustered in a common geographic area, and are thereby able to share fixed costs such as vehicles, employees and other resources.
- *Ability to Increase Market Share through Advance Planning:* An increasing number of death care products and services are being sold prior to the time of death, or on a "pre-need" basis, by death care providers who have developed sophisticated marketing programs in an effort to expand their market share and secure future revenue. Advance planning is a growing trend that is expected to continue as funeral homes expand these programs in order to increase market share and in response to consumer preference to

control their own funeral arrangements. Revenue per case in the funeral home business is not materially different for sales made on a pre-need or at-need basis.

- *Highly Fragmented Ownership:* Despite forty years of funeral consolidation and a particularly active period in the 1990s, the death care industry remains highly fragmented. A significant majority of death care operators are small, family-owned businesses that control one or several funeral homes in a single community. As a result, opportunities for further consolidation and clustering exist that can result in enhanced operating efficiencies such as increased buying power and leveraging of resources.

**Differences Between Funeral Home and Cemetery Businesses**

The funeral business is primarily a service business, while the cemetery business is primarily an interment rights or property business. These fundamental differences are reflected in several ways:

- *Cash flow stability:* Goods and services provided by funeral homes and cemeteries at the time of need are basic, non-discretionary items for which there is predictable, long-term demand. Unlike funeral home services, however, cemetery services are more discretionary and cemeteries derive a significant portion of revenue from advance sales that are more subject to volatility and cancellation. Cemetary services are also continued over a long period of time following death with no opportunity to recover unanticipated cost increases. Funeral home revenue is inherently more stable and predictable because services are performed and revenue is recognized at the time of death.
- *Licensing and education requirements:* Funeral directors are trained, licensed professionals in 49 of the 50 U.S. states. In many jurisdictions, funeral directors also are required to meet certain continuing education requirements. In a number of states, funeral homes also must be licensed. Cemeterians are primarily in the business of selling interment property and typically have no minimum education requirements to operate a cemetery or to complete a sale of cemetery property.
- *Length of obligation:* Funeral directors are primarily in the business of caring for the deceased and the bereaved through preparation (embalming) of the body and arrangement and oversight of memorialization services. These services can be sold at any time but cannot be completed until after death. Once completed the funeral home has no further obligations. The sale of interment property rights is completed at the time of sale whether in advance or at the time of death and each sale creates a binding on-going obligation between the cemetery and the customer.

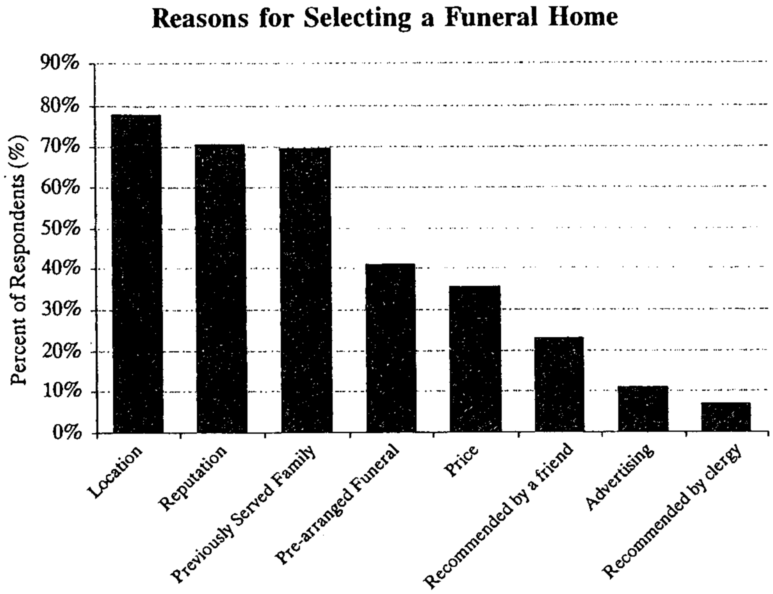
**Consolidation**

The funeral home business experienced a period of dramatic consolidation in the 1990s. Specifically, larger organizations actively pursued acquisitions of family-owned funeral services businesses. At the peak of the consolidation trend in 1999, many of the consolidators found themselves with over-leveraged balance sheets and diminished access to capital; and the competition for acquisitions had driven the price for funeral homes businesses to historic highs. As a result, following 1999, acquisition activity decreased significantly and many consolidators focused on integrating their acquired businesses and streamlining operations (including selective divestitures of funeral homes). Despite the consolidation boom in the 1990s, the industry remains highly fragmented as evidenced by the fact that the four U.S. public death care companies only operate approximately 11% of funeral homes in the United States.

**Market Drivers**

*Local Heritage*

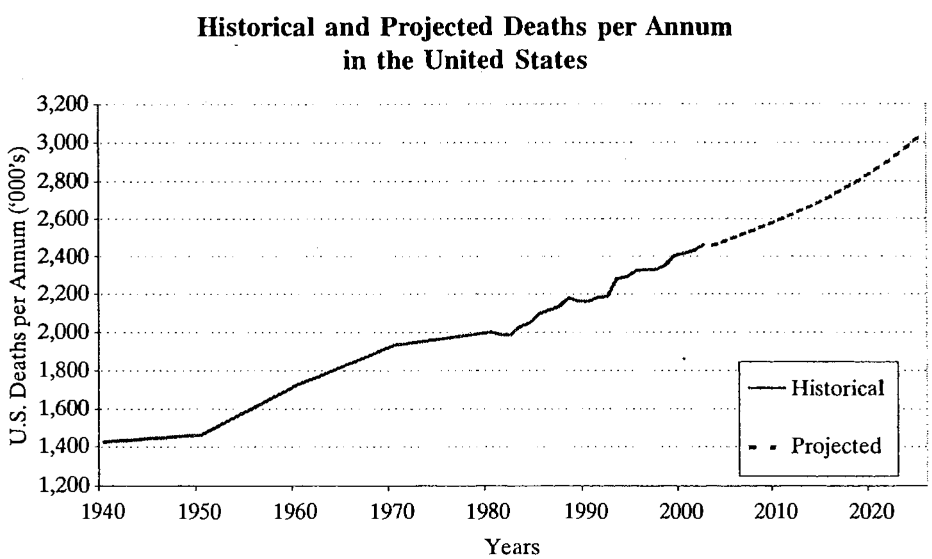
Market share is largely a function of goodwill, family heritage and tradition. A recent survey conducted by the National Funeral Directors Association, or "NFDA", which received responses from over 12,259 families in the United States, listed the top eight reasons for selecting a funeral home. The primary reasons to choose a funeral home, set out in the chart below, all reflect factors that take many years to acquire. Market share changes occur slowly. As such, competition among funeral homes is long-term and mostly passive based on providing good service, maintaining an attractive facility, generating positive word of mouth, offering reasonable prices, and making pre-need sales. Advertising is a comparatively small consideration.




Source: NFDA

***Mortality Rate***

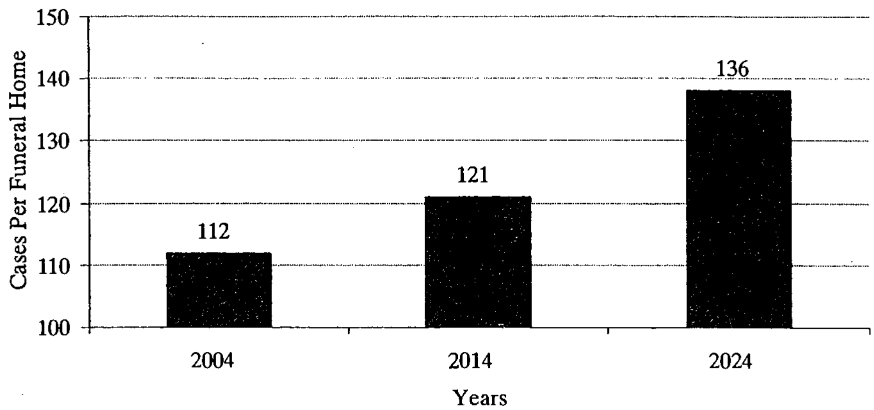
The demand for funeral home services is a function of the number of deaths. The number of deaths in the United States has varied slightly from year to year, due to factors such as the severity of the weather, outbreaks of diseases such as influenza, and fluctuations in the absolute magnitude of older age groups. The U.S. Census Bureau projects an 8.4% increase in the number of deaths from 2004 to 2014 and a 23.2% increase from 2004 to 2025. While growth in deaths is a natural result of a growing population, the projected increase in the number of deaths after 2010 is also due to the aging of the large 'Baby Boomer' demographic segment consisting of individuals born from 1946 to 1964. In 2011, the oldest 'boomers' will reach 65 years of age. The graph below illustrates the historical number of deaths in the United States from 1940 to 2002 and the projected number of deaths from 2003 to 2025.




Source: Historical data — U.S. Centre for Disease Control
Projected data — U.S. Census Bureau

The following table illustrates managements' estimate of the impact of the increase in the number of deaths will have on the average number of cases per funeral home per year based on the current number of funeral homes in the United States.

**Expected Growth in the Annual Number of Cases Per Funeral Home**



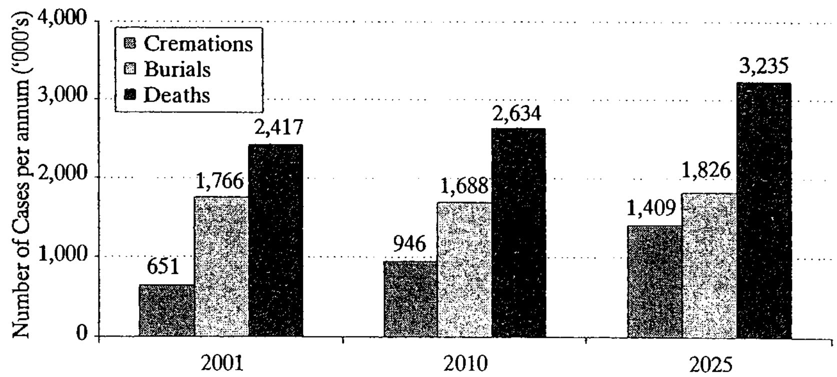

Industry studies indicate that medical advances in treating heart, cancer and other major diseases that often cause death have resulted in an increase in the age of the average population. In 2001, life expectancy reached a record high of 77.2 years in the U.S. Although death is physically inevitable, medical and other advances may continue to extend life expectancies.

***Rising Cremation Rate***

In recent years, there has been steady, gradual growth in the number of individuals and families in the United States that have chosen cremation as an alternative to a ground burial. While cremation represented approximately 10% of total dispositions in the U.S. in 1980, the Cremation Association of North America, or CANA, currently projects that cremation will account for 36% of total U.S. dispositions by 2010 and 44% by 2025. Management believes that Americans who would prefer cremation tend to be well-educated, earn higher-than-average incomes and reside in the western U.S. (states west of the Great Plains) and the state of Florida, which have the highest concentration of cremations. Areas with large retiree populations and areas with significant populations with Asian heritage also exhibit pronounced preferences for cremation. Those people that prefer burials over cremations typically live in small towns and rural communities where migration rates are lowest. For example, much of the southern and midwestern United States exhibits a significantly lower rate of cremation.

The following table illustrates CANA's projected growth in the number of cremations on an absolute scale, and relative to traditional burials.

**U.S. Cremations, Burials and Deaths**




Source: CANA

While rates of cremation versus rates of burial are important measures, more important to the profitability of the funeral home industry is the absolute market size (*i.e.*, the total number of cremation and burial cases). In the United States, the overall population has grown substantially and is projected to continue growing. This growth has substantially muted the impact of the cremation growth rate, such that the number of burials is projected to remain roughly constant over the next twenty-five years. As shown in the chart above, over the next 25 years expected growth in dispositions is almost entirely in cremation while the burial market is expected to remain at a relatively stable level of case volume.

*Seasonality*

Industry experience indicates that slightly more deaths occur in the four month period between December and March. Management believes that, on average, approximately 36% of annual deaths occur during this period. Management attributes this seasonal variation to adverse weather and certain illnesses that generally occur during the winter months.

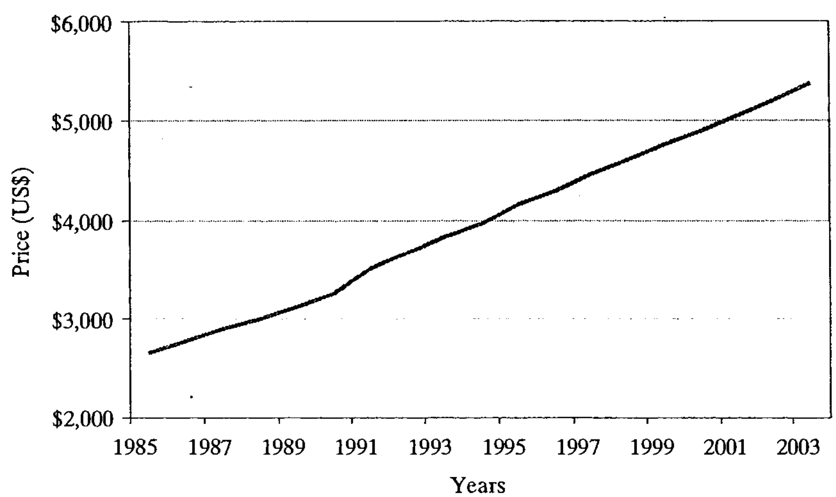
**Industry Economics**

*Revenue*

Funeral homes generate revenue through fees for services and sale of merchandise. Fees for service include basic service fees, embalming, cremation, use of facilities, use of vehicles, and transfer of remains. Merchandise sales include caskets, outer burial containers, urns, urn vaults and other enclosures and miscellaneous items such as paper goods. Ancillary revenue may be generated from commissions on pre-need insurance sales, trade embalming, trade cremation and shipping.

The average selling price for a regular adult funeral (service and casket only) in the U.S. was $5,525 in May 2004 according to the Federated Funeral Directors of America, or FFDA. FFDA calculated this average from their client base of almost 1,500 funeral homes in 44 states, which is heavily weighted toward traditional burial. The average selling price has shown a steady rise over the past twenty-five years as shown in the graph below.

**Average Selling Price for Regular Adult Funeral**




Source: FFDA

Cremation has historically been mistakenly marketed by many funeral homes as a less costly disposition alternative in the United States. Today, cremation is marketed by leading funeral homes as part of a complete package offering additional products and services that includes traditional funeral services and memorialization with an emphasis on customization. Cremations usually have higher gross profit margins than traditional funeral services but usually result in lower total revenue and gross profit dollars per service. Also, the gross dollar revenue that may be generated by a cremation case can vary greatly depending on the other services and products sold with the cremation.

The following chart illustrates the service options provided by funeral homes and management's estimates as to the different revenue and margins they generate.

| Approximate Revenue | Burial with Traditional Funeral Service $6,500 | Cremation with Traditional Funeral Service $4,800 | Cremation with Memorial Service (no casket) $2,800 | Direct Cremation $1,500 |
|---|---|---|---|---|
| **Services Provided** | Preparation | Preparation | Preparation | Preparation |
| | Visitation | Visitation | Memorial Service | Cremation |
| | Memorial Service | Memorial Service | Cremation | |
| | Transportation | Cremation | | |
| | Committal | | | |
| **Gross Margin (percent)** | Mid 80s | High 80s | Low 90s | Mid 90s |

*Advance Planning*

Although funeral services cannot be provided prior to death, funeral services can be arranged or purchased in advance of need, a process referred to in the funeral industry as 'advance planning' or 'pre-need'. The payment from pre-need sales is either placed in a 'pre-need trust' or is used to purchase a 'pre-need insurance' policy that will pay out at time of death. In either case, the funeral home has generally guaranteed to furnish the funeral at a price equal to the accrued value of the trust or the appreciated value of the insurance policy. Life insurance proceeds and principal amounts deposited in trust funds are available at the time funeral services are performed. Income earned on the trust funds is generally accumulated in the trust and is intended to cover future increases in the cost of providing price-guaranteed funeral services. Advance planning builds a book of future business that helps create an additional barrier to future competition and expand market share while building consumer awareness that strengthens local heritage and reputation.

*Operating Expenses*

Funeral homes typically exhibit predictable expense patterns. The two largest expense categories, personnel and cost of goods sold, will usually comprise 30% and 15% of revenue, respectively, with no other category alone counting for as much as 11% of the expense base assuming facilities are owned.

Savings can be created with greater facility volume or by sharing resources, such as vehicles and staff, among a group of funeral homes within a service area or cluster.

**Regulation**

Primary regulation of funeral homes operating in the United States is on the state level. Most states require licensing and supervision of individuals who provide funeral related services. Non-compliance with these regulations can result in fines or suspension of licenses.

State laws also govern the operation of pre-need trusts and establish such requirements as minimum deposit amounts (which are in some instances less than 100% of amounts received) and trust withdrawals (earnings may be permitted to be withdrawn annually rather than accumulate until the date of death in some states). State law also governs pre-need insurance operations but features of pre-need insurance are generally consistent with the sale of other insurance products. Pre-need policies are purchased with a face amount equal to the then-current retail price of contracted funeral services. The rate of appreciation on the policy is set by the insurance company and is typically based on a number of factors including the amount of the commission paid by the insurance company to the agent (usually the funeral home or an affiliate).

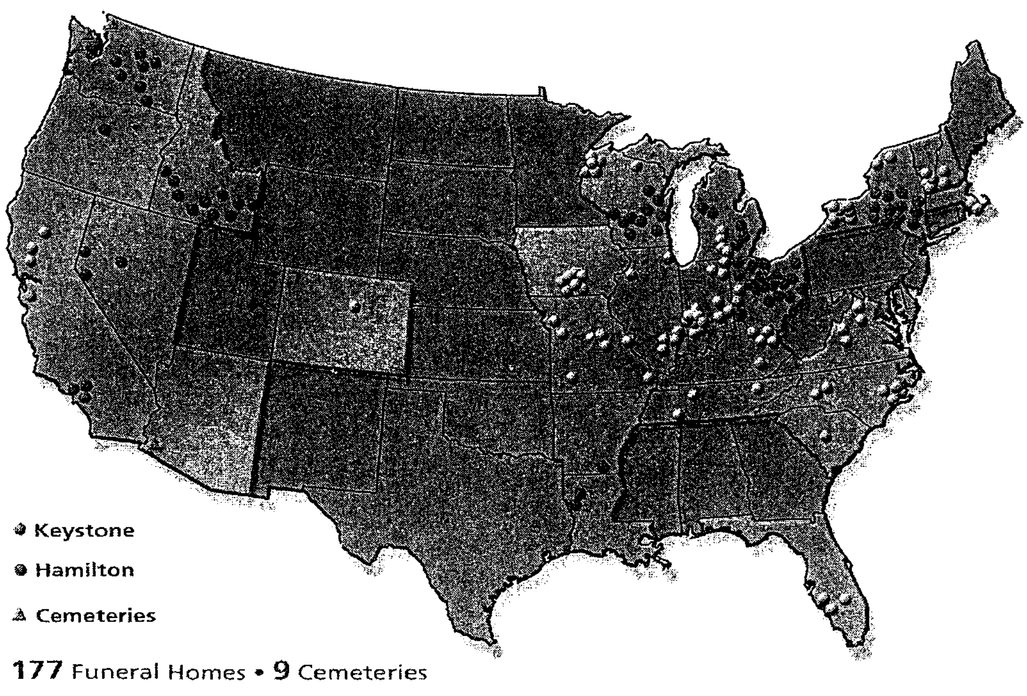
Funeral homes also must comply with federal laws and regulations. One area of U.S. federal regulation that is unique to funeral homes include the laws and regulations administered by the Federal Trade Commission, or FTC. The FTC administers the Trade Regulation Rule on Funeral Industry Practices that defines certain acts or practices as unfair or deceptive and contains certain requirements to prevent these acts or practices. The preventive measures require a funeral provider to give consumers accurate, itemized price information and various other disclosures about funeral goods and services and prohibit a funeral provider from: (1) misrepresenting legal, crematory and cemetery requirements, (2) embalming without permission, (3) requiring the purchase of a casket for direct cremation and (4) requiring consumers to buy certain funeral goods or services as a condition for furnishing other funeral goods or services. Prior to each arrangement conference and before discussing any matters relating to price of goods or service with a decedent's family, a funeral home must provide a list of goods and services offered in hardcopy and printed in a specified format. This list is known as a 'General Price List' or 'GPL' and is mandated by the FTC.

Funeral homes are also subject to U.S. federal, state and local laws and regulation related to environmental protection. Some of the areas governed by the laws and regulations include air emissions, waste water discharge, waste management and disposal, hazardous material storage and handling and workplace safety.

## OUR BUSINESS

### Business Overview

We are a leading owner and operator of funeral homes across the United States. Upon completion of this offering and our acquisition of Hamilton, we will be the owner of a funeral service business with 177 funeral homes and nine cemeteries and, in management's estimate, will be the fifth largest provider of funeral services in the United States. Generally, our funeral homes are located in the Midwest, Northeast, Southeast and Northwest regions of the continental United States with individual service markets primarily made up of non-urban areas. The following map illustrates the states in which we operate:

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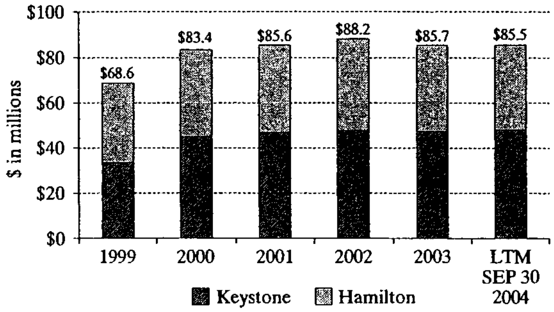
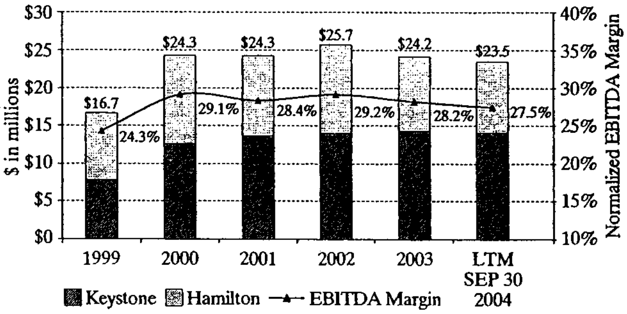
Our executive management team is comprised of four seasoned funeral professionals who collectively have spent 125 years successfully acquiring, integrating and managing funeral businesses. Local management consists substantially of former owners, their former managers and their other key employees. We have very strong relationships with the former owners of these funeral businesses, with over 80% still actively supporting our funeral homes in some significant way.

By successfully executing a business strategy that emphasizes operating efficiency and margin improvement, we have experienced stable and consistent Normalized Revenue and Normalized EBITDA, as illustrated in the following charts:

**Combined Keystone Normalized Revenue(1)**




**Combined Keystone Normalized EBITDA(1)**

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(1) EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may not be comparable to similar measures presented by other companies. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash" and "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". As the Issuer intends to distribute substantially all of the Issuer's cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA and Distributable Cash are important measures in evaluating the Issuer's performance and in determining whether to invest in IPSs.

### History of the Business

The Keystone business was founded in 1996 and developed into a leading funeral home business through 65 separate acquisition transactions from 1996 to 2000. Since its inception, the business has been run by its four key principals, who have functioned as a management team in the death care industry since 1994. Management focused its growth on non-urban areas across the eastern United States. The Hamilton business began operations in 1992, clustering its funeral homes in suburban, semi-rural markets to take advantage of less competitive markets.

Since 2000, there has been limited consolidation in the industry due to constrained access to capital. As a result, management has focused on organic growth strategies to develop market share and increase profitability. The Company now spans across the United States and has a demonstrated track record of strong and consistent cash flows.

The Company is the product of the indirect acquisition of the Hamilton business by Keystone and the combination of the two businesses under a common ownership structure. Management believes that the combination will significantly expand the capabilities of Keystone through the joining of two strong and profitable funeral home operators, creating opportunities for operating efficiencies and the ability to leverage opportunities for further consolidation in the industry.

The same individuals who have successfully led the Keystone group will bring the discipline and focus it brought to executing its business plan to the integration of Hamilton.

### Business Strengths

Our funeral home businesses have a number of attributes that promote stable revenue and EBITDA, including:

- *Strong Franchise Value:* Heritage and tradition are two of the most important factors driving client selection of a funeral home. More than 89% of our funeral homes were established before 1960. Our funeral homes are typically the largest and premier operations in their respective geographical markets. For this reason, we typically have not changed the name of acquired operations. We also typically require former owners of the acquired funeral homes to remain active in the daily operations for up to five years to facilitate the transition to corporate ownership while leveraging local heritage.

- *Focus on Stable Funeral Services:* Unlike the four U.S. publicly-traded funeral services companies that have cemetery operations providing approximately 25% to 50% of their revenue, over 95% of our revenue and 95% of our EBITDA is derived from our funeral home operations. Revenue in the funeral home business is far more stable than in the cemetery businesses, as services are provided at the time of death and therefore involve non-discretionary spending.
- *Expansion of Product Offering:* Since 2001, we have been implementing a number of value added services to increase revenue and secure market share. For example, we recently implemented the 'Key Memories' program in our funeral homes that increases family participation in the planning process, which leads to greater satisfaction and increased sales and operating margins. In addition, we have focused on adding more services to our burial and cremation options and increasing our advance planning sales.
- *Strong Supplier Relationships:* As one of the largest funeral home operators in the U.S., we enjoy preferred rates and volume discounts from many of our suppliers. Management believes that our rates from suppliers are significantly better than those available to many of our competitors.
- *High Quality Portfolio of Diverse Long-Term Sustainable Assets:* Our business includes a total of 177 funeral homes in 26 states with no one state representing more than 15% of aggregate revenue. We own a portfolio of established funeral home businesses with 99% having been in operation for more than ten years. Our average funeral home business has been in operation for over 50 years. Our clusters of funeral homes represent strong platforms for organic growth and the potential exists to further increase profit margins through selective investment to enhance existing properties. Our properties, in addition to being exceptional funeral homes, also have significant value as real estate assets.
- *Focus on Suburban and Rural Markets:* Suburban and rural markets, relative to large urban markets, offer lower migration rates, stronger community ties, less price sensitivity among consumers and a limited number of alternative service providers. In addition, our competition in such areas tends to be smaller operators that do not benefit from certain advantages that we enjoy as a national operator, including: volume discounts for merchandise and supplies, a sophisticated management team and information systems that provide strategic direction and allow us to share information across our organization, and access to capital to compete for acquisitions.
- *Experienced Management Team:* Our four founders, who comprise our executive management team, have 125 years of combined experience in funeral home and cemetery operations. Our senior management team has been in place since 1996 and the majority of whom have worked together since 1992. We have completed 65 acquisitions since 1996 and assembled a diverse pool of quality funeral home businesses, integrated the businesses under common ownership and successfully managed the businesses over a period of four to seven years. Our management team has developed expertise in identifying, executing and integrating strategic acquisitions. At the local level, our funeral homes and cemeteries are typically managed by former owners and long-time key employees with extensive care experience.

**Growth Strategies**

Our growth strategies are designed to increase market share and enhance profitability. Our organic and external growth strategies are outlined below.

*Organic Growth*

Our organic growth strategy focuses on three key areas:

- *Increase revenue per case:* We have enhanced service and merchandise packages, and developed a full line of marketing materials used in presenting burial and cremation package selections to customers, an approach that differentiates us among other death care providers in our markets. Package presentations generally generate higher revenue than customer selection of individual items. We carefully select additional merchandise and service items for inclusion in packages that provide for greater value while increasing the overall package price and margin. This strategy has been particularly successful with cremations and has increased our sales of cremations with memorial services. We support this strategy with regular training for all local managers related to effective presentation and sales techniques. In addition, we offer a range of personalized memorial programs and paper goods, again designed to increase case average while further enhancing personalization and thus value for the customer. We have historically been successful in increasing average revenue per case, even as case count has varied and cremation levels have increased from year to year.

- *Increase the volume of full service cremations:* In recognition of the growing proportion of cremations, arrangement presentations have been designed to ensure that families are well informed as to all available options and considerations when contemplating this type of service. The objective of these efforts is to increase the number of customers selecting additional service and merchandise options, thereby enhancing value and increasing revenue. Supporting marketing and advertising materials, together with best practices sales training programs, have been developed and are being utilized by our higher volume cremation facilities to increase the average revenue per case and number of cremations with memorial service. Although cremations typically generate profit margin percentages higher than those of traditional burial services, the total revenue and margin dollars of direct cremation are lower. By raising average revenue, we will be able to take full advantage of cremation's margin potential.
- *Increase market share:* Given the importance of tradition and heritage in selecting a funeral home, gains in market share are won through long-term marketing and pre-need sales. To that end, management has focused on programs such as 'Key Memories' to build awareness of the Keystone tradition and to build goodwill in the communities that we serve. Through the 'Key Memories' program we strive to be the preferred death care provider in the communities we serve. In addition, we have remained focused on increasing pre-need sales in our funeral business and ultimately strive to reach a ratio in excess of one pre-need sale for each at-need sale at a given funeral home. Growing our advance planning program at a rate faster than our competition in any given market eventually results in direct market share gains from that competition.

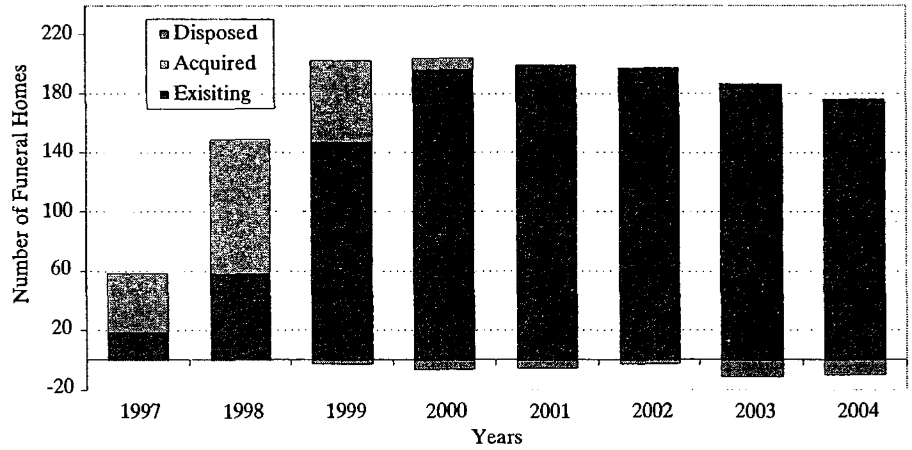
***External Growth***

Our external growth strategy focuses primarily on selective strategic acquisitions of existing funeral homes that complement our existing portfolio. We believe that growing our organization through acquisitions will continue to be a good business strategy, as we enjoy the important synergies and economies of scale from our scalable infrastructure. We will seek to capitalize on the quality and location of our existing portfolio of funeral homes and lower individual overhead costs by sharing common resources in clusters. When we enter the acquisition arena again, we will acquire funeral homes, using a disciplined approach, with deep heritage and tradition that are profitable and have the potential to grow revenue and operating margins.

**Acquisition Activity**

In 65 separate transactions, Keystone acquired a net total of 97 funeral homes from inception in 1996 through 2000. In connection with our acquisition activity, we have developed the following acquisition criteria: (i) operating and cultural fit, (ii) favourable community demographics and (iii) an attractive financial profile. We also seek to acquire funeral homes in geographic clusters to facilitate the management of the operations and sharing of resources. Consistent with the industry as a whole, our acquisition activity decreased after 2000 to focus on integrating our portfolio and enhancing operations.

**Keystone Acquisitions, Dispositions and Total Number of Funeral Homes**




*Hamilton Acquisition*

The acquisition of Hamilton, which will be our largest acquisition to date when it closes concurrently with this offering, fits our acquisition criteria and presents an opportunity to realize significant synergies. Management expects to realize substantial cost savings in the following areas.

- **Corporate Overhead Savings** — Reduction of Hamilton's corporate operations by leveraging Keystone's corporate head office and accounting infrastructure.
- **Procurement savings** — Improvement of margins as a result of increased purchasing power.
- **Selling, General and Administrative Efficiencies** — Reduction of travel expense as a result of having a broader network of operating personnel and streamlining back office systems through the elimination of duplication regarding payroll-benefit services, risk management, compliance and management and information systems.
- **Leveraging Best Practices** — Realizing gains through the utilization of best practices across the organization (*e.g.*, 'Key Memories').

Management will also continue to consider future acquisitions in accordance with our acquisition criteria and disciplined processes. Management believes that, despite the prior period of consolidation in the industry in the later 1990s, the industry remains highly fragmented and significant strategic acquisition opportunities exist at reasonable valuations.

*Acquisition Process*

Management has developed an acquisition process based on years of prior experience in funeral home acquisitions and the operation of acquired businesses. This acquisition process includes rigorous due diligence and thorough analysis of each planned acquisition. It is intended to ensure that acquired funeral home businesses can be integrated into our operating model and provide the anticipated level of financial performance. The success of this acquisition process is reflected in the strong financial performance of the acquired businesses. The acquisition process consists of three phases: qualification due diligence, business plan due diligence, and closing due diligence.

- *Qualification due diligence:* We review tax returns, income statements, and funeral service purchase agreements. Each contract is analyzed to determine case volume and revenue, a profitability examination is completed, and a pricing and market share analysis is performed. We require a detailed review of a minimum of three years of historical expenses. In addition, sellers are required to answer a series of questionnaires and provide financial statements, insurance coverage information, description of personnel and facilities, a detailed competitive analysis, pre-need analysis, and other documentation. Based on the findings and our interaction with the acquisition prospect, we determine if the owner, manager and staff are a fit for our corporate culture.

- *Business plan due diligence:* The acquisition prospect is presented internally to our management team. A detailed review is presented to the respective regional vice president. Finally, a review is performed with the existing owners and key managers. If the various groups approve, terms are negotiated, a purchase price is decided and a letter of intent is issued to the business owner.
- *Closing due diligence:* We perform the following items including: reviewing the business information questionnaires, obtaining title insurance, conducting a certified land survey, performing a Phase I environmental audit, completing a building inspection, and completing a lien search.

***Closing Process***

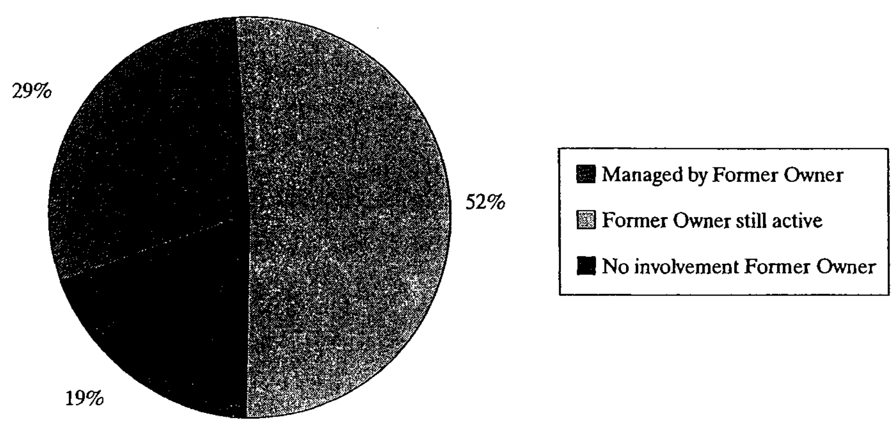
Upon reaching an agreement to acquire a funeral home business, we devote a substantial amount of resources towards integrating the new business. This integration process is outlined in a document provided to sellers, 'A Comprehensive Guide to a Keystone Merger'. This document provides guidance on managing personnel and community relations during the transition period, as well as operating procedures after the acquisition, a summary of our benefits, and an employee handbook. Our financial staff also integrate the new business into our computer systems and financial controls. Furthermore, we keep management focused on the success of the business by structuring our acquisitions such that they are incentivized to drive the success of the business.

***Former Owners***

Former owners of our businesses are usually licensed funeral directors with recognized standing in their community, typically realized through several generations of family ownership. They represent an important bridge during the transition period following acquisition. Pursuant to the acquisition terms, former owners have generally been retained to work with the funeral home for a minimum period of three to five years and are incentivized to drive the future success of the business. The specific terms typically vary depending on the former owner's age, life goals, and post acquisition position as full-time manager, funeral director or part-time consultant. The ownership transition results in minimal changes to the funeral home and is transparent to community relations and customer service. Once the initial term of the retainer agreement expires, we typically seek to extend the agreement in some form.

We believe that our excellent relations with former owners accounts for the owners' on-going involvement with the business. Of our businesses, 29% continue to be managed by one or more former owners, while another 52% have at least one former owner active or present in the community and continuing to support the business. Due to death, advanced age, health reasons or personal choice, 19% of the businesses have no former owner involvement.

**Former Owner Involvement Post Acquisition**



### Products and Services

We serve families from diverse cultural and religious backgrounds and provide a complete range of funeral and cremation services including planning and coordinating personalized disposal, removal and preparation of remains, conducting memorial services, performing interment services and transportation services. We also sell products and merchandise including caskets, urns, burial vaults, cemetery interment rights and monuments and markers.

In most non-U.S. societies, cremation is an alternative to ground burial or mausoleum entombment for the final disposition of human remains, and includes memorial services provided by the funeral home. Historically, the U.S. funeral home has presented cremation as a low-cost option only without significant memorialization.

Through training, we have demonstrated that arrangement counsellors' mindsets can be changed so as to allow cremation clients the same service options as afforded to our burial families. Beginning in 1999, we have tested marketing programs that demonstrate that cremation families desire memorialization, and will spend accordingly when offered options in which they perceive value.

Our 'Key Memories Cremation Tributes' have significantly increased revenue and margins since their introduction. Management estimates that 'Key Memories Cremation Tributes' provide the opportunity for 15-20% initial annual growth of per firm per case cremation averages upon implementation. A primary strategy for 2004-05 is to implement our 'Key Memories Cremation Tributes' at all firms, including the Hamilton firms.

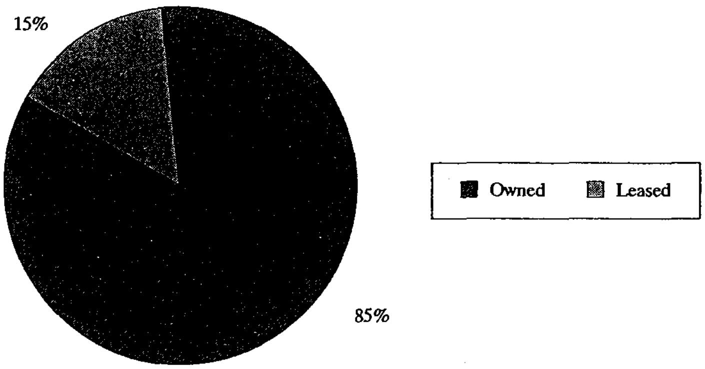
### Funeral Homes and Markets Served

Following the closing of this offering and the acquisition of Hamilton, we will own and operate 177 funeral homes and nine cemeteries in 26 states. Our funeral homes are generally located in suburban and rural markets. The average age of our funeral home businesses exceeds 50 years and only one is less than 10 years old. The table below lists each state in which we operate funeral homes, the number of funeral homes in each state, and the breakdown between owned and leased funeral homes.

| State | Number of Funeral Homes | | |
|---|---|---|---|
| | Keystone | Hamilton | Total |
| Arizona | 0 | 1 | 1 |
| Arkansas | 0 | 1 | 1 |
| California | 5 | 3 | 8 |
| Colorado | 1 | 0 | 1 |
| Florida | 3 | 0 | 3 |
| Iowa | 7 | 0 | 7 |
| Idaho | 0 | 11 | 11 |
| Illinois | 6 | 0 | 6 |
| Indiana | 17 | 0 | 17 |
| Kentucky | 5 | 0 | 5 |
| Louisiana | 0 | 2 | 2 |
| Massachusetts | 2 | 0 | 2 |
| Michigan | 4 | 5 | 9 |
| Missouri | 8 | 0 | 8 |
| North Carolina | 5 | 0 | 5 |
| Nevada | 0 | 3 | 3 |
| New Hampshire | 2 | 0 | 2 |
| New York | 11 | 12 | 23 |
| Ohio | 2 | 20 | 22 |
| Oregon | 0 | 1 | 1 |
| South Carolina | 1 | 0 | 1 |
| Tennessee | 3 | 0 | 3 |
| Virginia | 5 | 0 | 5 |
| Vermont | 4 | 0 | 4 |
| Washington | 0 | 11 | 11 |
| Wisconsin | 6 | 10 | 16 |
| **Total** **26** | **97** | **80** | **177** |

We own the vast majority of our funeral homes, as illustrated in the graph below indicating the percentage of funeral homes leased and owned.

**Owned v. Leased Funeral Homes**




**Company Operations**

Our corporate office oversees the operations of each of our funeral home businesses. Our corporate oversight consists of strategic direction, pricing, financial control, bookkeeping and operational performance. Staff accountants work intensively with funeral home staff and maintain efficiency by limiting interactions to bookkeeping and cash management and leaving all operational questions to corporate operations staff.

Our local funeral home operators are managed by individuals with extensive death care experience. The local operators continue to have responsibility for day-to-day operations, but are required to follow service and financial standards. This strategy allows each local funeral home to maintain its unique style of operation appropriate for its market and to capitalize on its reputation and heritage while we maintain supervisory controls and provide specialized services from our corporate headquarters.

Outside of day-to-day operations, there are certain areas where corporate management works jointly with funeral home staff and other areas where corporate management maintains sole responsibility. It is the sole responsibility of our corporate office to negotiate national contracts with major suppliers, in particular caskets and pre-need insurance, and selection of the professional employer organization that employs all staff and sets up employee benefits such as health care.

We have well established training programs to support the technical and managerial talent within our organization, including: Compliance, Technical Training Skills, Presentation Methods, Basic Fiscal Management, Human Resource Management, Service Delivery Models, and Risk Management. These programs are designed to be delivered in both group and individual settings as required.

**Employees**

We currently employ 526 full-time employees and 443 part-time employees. All of our funeral directors and embalmers possess licenses required by applicable regulatory agencies. We believe that relations with our employees are good. All of our employees are non-unionized except at one funeral home, where one employee is part of a union.

| Number of Employees | Keystone | Hamilton | Total |
|---|---|---|---|
| Corporate | 25 | 21 | 46 |
| Funeral Homes | 409 | 402 | 811 |
| Cemeteries | 1 | 29 | 30 |
| Advance Planning | 48 | 34 | 82 |
| **Total** | **483** | **486** | **969** |

### *Incentive Plan*

Local site-level management have a vested interest in achieving periodic operating results by virtue of a bonus program payable upon accomplishment of pre-established goals. In most cases the bonus pool equals 1% of the firm's revenues and has proven significant enough to motivate local personnel. In addition to realization of budgeted EBITDA, other significant bonus qualifiers by location could be number of days in receivables, improved average revenue per case and community involvement. Management is encouraged to share a portion of their earned bonus with key employees who were instrumental in accomplishing management's goals for the bonus period.

## Suppliers

Our primary suppliers and major vendors include providers of caskets, urns, paper products, outer burial containers, and other ancillary products. We retain a significant advantage with those suppliers permitting us to achieve preferred pricing and control costs. Due to our increased size following the Hamilton acquisition, we anticipate that relationships with these suppliers will become even more advantageous to the Company.

Our primary suppliers include the two largest casket suppliers and two large pre-need funeral insurance companies. We typically enter into supply contracts with terms ranging from one to three years pursuant to which we agree to buy certain percentages of our needs from the relevant key supplier. Management believes that in the event of a supply disruption from our key suppliers, alternative suppliers at reasonable prices are readily available.

Our main suppliers are well recognized within the industry as key providers in their respective fields. These relationships afford us significant benefits including cost savings, wide geographic distribution and support, benefit enhancements on our pre-need insurance program, current data on industry trends and product development as well as other non-monetary benefits.

## Capital Expenditures

Our capital expenditures can be categorized into two types: maintenance and growth or earnings enhancing. The table below sets out the combined historical and average maintenance and growth capital expenditures for Keystone and Hamilton for the past three years.

| | Year Ended December 31, | | | |
|---|---|---|---|---|
| | 2003 | 2002 | 2001 | Average |
| Maintenance Capital Expenditures (net) | $3,126,336 | $2,796,068 | $2,228,810 | $2,717,072 |
| Growth Capital Expenditures (net) | 43,682 | 89,195 | — | 44,292 |
| **Total** | **$3,170,018** | **$2,885,263** | **$2,228,810** | **$2,761,364** |

### *Maintenance Capital Expenditures*

Maintenance capital expenditures include those required to maintain and upgrade existing infrastructure, including the replacement of furnishings, autos and routine maintenance to existing building structures and the surrounding landscape. We believe that $2.9 million represents a conservative estimate of the annual maintenance capital expenditures required for the foreseeable future to sustain the current capacity and utilization of the facilities, infrastructure and equipment.

### *Growth Capital Expenditures*

Growth capital expenditures are those related to the acquisition of new equipment or businesses, expansion of existing infrastructure (*i.e.*, expansion of existing building facilities and/or addition of new facilities and other capital improvements). Growth capital expenditures are intended to increase productivity and cash flows, enhance margins and/or increase capacity. We will continue to consider growth capital expenditures based on the economic merit of each project and the availability of funds.

### Competition

We compete primarily with local funeral homes and cemeteries for at-need and pre-need business. The market share of a single funeral home or cemetery in any community is often a function of its name, reputation and location, and gains in market share within a community are usually achieved over a relatively long period of time.

In the 1980's and 1990's the growth strategy pursued by participants in the funeral service industry was aggressive expansion through consolidation. By 1999, high purchase price multiples, a reduced availability of financing and depressed earnings among public competitors, substantially slowed acquisition activity. Those changes led us and other death care providers to place greater emphasis on internal development rather than external consolidation.

Focused on secondary suburban and rural markets, our competitive position is strengthened by relatively low migration rates, more meaningful community ties, less price sensitivity among consumers, and a limited number of alternative service providers. Given our market focus, we compete primarily with independent operators, unable to leverage the economies of scale available to us. The publicly traded funeral home consolidators have generally concentrated on large urban markets.

### Management Information Systems

*Funeral Home:* Our funeral homes are equipped with computer systems that automate all aspects of funeral home paperwork from funeral contracts, pricing information and regulatory forms to cheque writing, cash receipt management, billing and bookkeeping. These systems provide corporate management with strong cash management controls and timely access to accounting and operating data. Various financial reports are generated weekly and monthly to facilitate management's review of each funeral home's performance. Each funeral home backs up data daily to zip drives with the disks collected monthly and stored at our corporate offices.

*Corporate:* At the corporate level, we utilize a database system for the management of detailed information from each funeral home as well as the preparation of financial statements and operating reports. Our accountants dial in to each local funeral home's computers for access to individual business information. Our corporate disaster recovery and backup procedures include a daily backup of the full system with a ten-day rotation of tapes. A monthly backup is stored in a safety deposit box off-site and is retained for two years. As a secondary backup, daily back-ups are made to network attached storage. On a monthly basis, our management information systems department tests and documents the integrity of the backup process.

### Insurance

We maintain casualty and liability insurance that is sourced and purchased by corporate staff. We realize material savings relative to the insurance costs of an independent funeral home by purchasing policies covering the entire portfolio of funeral homes. In addition, consolidation eliminates the burden of tracking separate policies. We carry insurance with coverages and coverage limits that we believe to be customary in the funeral home and cemetery industries. Although there can be no assurance that such insurance will be sufficient to protect us against all contingencies, we believe that our insurance protection is reasonable in view of the nature and scope of our operations.

### Environmental Issues

Our operations are subject to numerous environmental laws and regulations adopted by U.S. federal, state and local authorities in the jurisdictions in which we operate. Failure to comply with such laws and regulations could result in the assessment of substantial administrative, civil and criminal penalties, or the imposition of investigatory and remedial obligations. While we believe we are in substantial compliance with existing laws and regulations, we cannot assure you that we will not incur substantial costs in the future.

### Litigation

We are parties to legal proceedings from time to time that have arisen in the ordinary course of business. While the outcome of these proceedings cannot be predicted with certainty, we do not expect these matters to have a material adverse affect on us.

### Currency Hedging Policy

We will be exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar because the revenue and expenses of Keystone are in U.S. dollars and the distributions that Keystone will make to Keystone North America and Keystone ULC will be paid in Canadian dollars. In order to minimize the impact of fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar, we intend to enter into a five-year hedging arrangement at an exchange rate of C$1.2272 to US$1.00 at or prior to the closing of this offering. See "Summary of Distributable Cash Flow of the Issuer". We will convert substantially all of the amounts received by it into Canadian dollars to make distributions in Canadian dollars. We will review our hedging policy on an ongoing basis.

### Trust Funds and Escrow Accounts

We maintain three types of trust funds and escrow accounts in connection with operations relating to prearranged funeral contracts, pre-need cemetery service and merchandise sales and cemetery perpetual care. At December 31, 2003, we had approximately $48.5 million in fair value trust funds and escrow accounts (prearranged funeral funds of $44.8 million; pre-need cemetery service and merchandise funds of $2.4 million; and cemetery perpetual care funds of $0.8 million).

Prearranged funeral contracts are generally funded either through trust funds established by us from contract payments received from the customer, or through life insurance policies purchased by the customer and issued by third party insurers. We typically fund our prearranged funeral sales activities by means of life insurance policies rather than trust funds. Life insurance proceeds and principal amounts deposited in trust funds are available to us at the time funeral services are performed. Income earned on the trust funds is generally accumulated in the trust and is intended to cover future increases in the cost of providing price-guaranteed funeral services. The accumulated earnings on individual trust accounts is recognized as funeral revenue at the time funeral services are performed. Amounts held in trust are refunded to the customer in those situations when state law provides for the return of those amounts under the purchaser's option to cancel the contract.

Pursuant to applicable state law, a portion of the proceeds from the sale of pre-need cemetery merchandise and services may be required to be paid into trust funds until we deliver such merchandise or performs such services, at which time the original amount of deposits held in trust is available to us. Accumulated earnings are intended to cover future increases in the cost of providing undelivered merchandise and unperformed services and are recognized as cemetery revenue when such merchandise is delivered or the services performed.

A portion of the proceeds from the sale of cemetery interment rights is required by state law to be paid into perpetual care trust funds and therefore is not recognized as revenue by us. Earnings from these trusts are recognized as current cemetery revenue, and are used to defray ongoing cemetery maintenance costs.

## SUMMARY OF DISTRIBUTABLE CASH OF THE ISSUER

The following analysis has been prepared by management on the basis of the information contained in this prospectus and management's estimate of the amount of expenses and expenditures that would have been incurred by the Issuer during the 12 months ended September 30, 2004 had the Issuer been in existence during such period and had the transactions described under the caption "Investment Agreement" been completed at the beginning of that period. **This analysis is not a forecast or projection of future results. The actual results of our operations for any period whether before or after the closing of this offering will differ from the amounts set forth in the following analysis, and such differences may be material.** Additionally, our operations are subject to risks, and in reviewing the following summary of distributable cash, investors are encouraged to consider the risks described under the caption "Risk Factors".

Management believes that, upon completion of this offering, the Company and the Issuer will incur interest expenses, additional administrative expenses and taxes that will differ from those contained in the historical financial statements of Keystone and Hamilton and the *pro forma* financial statements of Keystone North America that are included elsewhere in this prospectus. In addition, we intend to continue to make maintenance capital expenditures consistent with past practices. In order to minimize the impact of fluctuations in the rate of exchange between the Canadian dollar and U.S. dollar to those currently in effect, we intend to enter into a five-year hedging arrangement to fix the rates of exchange between the Canadian dollar and U.S. dollar for substantially all of the amount of distributable cash reflected in the following table. See "Our Business — Currency Hedging Policy". Although management does not have firm commitments for all of these costs, expenses and expenditures and, accordingly, the complete financial impact of these items are not objectively determinable, management believes, based on past experience, that the following represents a reasonable estimate of the amount of cash that would have been available for distribution for the last twelve months ended September 30, 2004 had Keystone North America been in existence during such period and had the transactions described under the caption "Investment Agreement" and "Post-Closing Structure" been completed at the beginning of the period:

| *(In thousands except per IPS numbers and hedge rate)* | **Twelve months ended September 30, 2004** |
|---|---|
| Combined Normalized EBITDA(1)(2) | $23,494 |
| Management believes that the following items will increase (reduce) the amount available for distribution by the Issuer: | |
| Cost savings from Hamilton acquisition(3) | 2,187 |
| Maintenance capital expenditures | (2,900) |
| Additional administrative expenses(4) | (1,000) |
| Interest on new credit facility(5) | (3,070) |
| Interest on Separate Subordinated Notes(6) | (1,182) |
| Income taxes paid in cash | (341) |
| Distributable Cash before Cash Holdback | $17,188 |
| Distributable Cash Holdback (5%) | 859 |
| Distributable Cash | 16,329 |
| Summary of Distributable Cash: | |
| Interest on Subordinated Notes forming part of IPSs | 8,660 |
| Dividends on Common Shares forming part of IPSs | 5,274 |
| Dividends on Class B and C Shares | 2,395 |
| Distributable Cash | $16,329 |
| Hedge Rate (C$ per US$)(7) | 1.2272 |
| Distributable Cash (C$)(1) | $20,039 |
| Distributable Cash for IPS Unitholders | 13,934 |
| Distributable Cash for IPS Unitholders (C$) | 17,100 |
| Distributable Cash per IPS (C$) | $ 1.00 |

(1) EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable

Cash may not be comparable to similar measures presented by other companies. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash" and "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". As the Issuer intends to distribute substantially all of the Issuer's cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA and Distributable Cash are important measures in evaluating the Issuer's performance and in determining whether to invest in IPSs.

(2) *Pro forma* for the acquisition of Hamilton and Keystone.

(3) Includes reductions in Hamilton corporate overhead costs comprised primarily of headcount reductions, elimination of their corporate offices, and related expenses (rent, travel, healthcare, etc.) and $300,000 in procurement savings related to casket purchases.

(4) Represents estimated administrative expenses to be incurred following the offering in connection with ongoing public disclosure requirements, investor relations, director fees and other expenses.

(5) Represents estimated interest on New Credit Facility based on an average of outstanding balances.

(6) Interest is payable in C$ and is calculated using the hedge rate described in the table and note (7).

(7) Based on a five-year C$/US$ hedge rate as of January 28, 2005.

Management believes that the method of determining distributable cash presented in this prospectus is comparable to cash flow from operating activities before capital expenditures, certain interest expenses and changes in working capital. In addition, the Issuer's method of determining distributable cash is derived from net income, which is a measure recognized under GAAP. Net income has been used as the basis for the calculation of Distributable Cash because a pro forma statement of cash flow for the Issuer is not available, only a pro forma of net income (or loss). This method presents cash that is intended to be distributable based on the results of the relevant period, after adjusting for the items set out in the above table. See "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash".

## RECONCILIATION OF HISTORICAL RESULTS TO EBITDA, NORMALIZED EBITDA, NORMALIZED REVENUE AND DISTRIBUTABLE CASH

Because the Issuer will distribute substantially all of its cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are important measures in evaluating the performance of the Issuer and in determining whether to invest in IPSs. However, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized earnings measures under GAAP and do not have a standardized meaning prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may not be comparable to similar measures presented by other issuers. Prospective investors are cautioned that EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash should not be construed as alternatives to net income or loss determined in accordance with GAAP as indicators of performance or cash flows from operating, investing and financing activities as a measure of liquidity and cash flows. Management defines and has computed EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash as described under "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". The following table reconciles EBITDA, Normalized EBITDA, and distributable cash to net income (loss) and Normalized Revenue to revenue based on the historical financial statements of Keystone and Hamilton for the periods indicated.

**Keystone**

| | 12 Months Ended September 30, | Nine Months Ended September 30, | | Year Ended December 31, | | |
|---|---|---|---|---|---|---|
| | 2004 | 2004 | 2003 | 2003 | 2002 | 2001 |
| | | (U.S. dollars in thousands) | | | | |
| **Revenue** | $48,583 | $35,856 | $36,158 | $48,885 | $50,767 | $50,852 |
| Adjustments to revenue from homes sold[1] | (660) | (446) | (1,037) | (1,251) | (2,806) | (3,903) |
| **Normalized Revenue** | 47,923 | 35,410 | 35,121 | 47,634 | 47,961 | 46,949 |
| **Net Income (loss)** | 3,080 | 2,159 | 2,002 | 2,923 | 876 | (879) |
| Adjustments to net income (loss) | | | | | | |
| Depreciation and amortization | 3,167 | 2,355 | 2,392 | 3,204 | 3,414 | 5,345 |
| Impairment of long-lived assets | 111 | 111 | — | — | 1,149 | — |
| Interest | 6,292 | 4,607 | 4,791 | 6,476 | 7,800 | 9,871 |
| Income taxes | 1,708 | 1,096 | 1,331 | 1,943 | 1,188 | 458 |
| **EBITDA** | 14,358 | 10,328 | 10,516 | 14,546 | 14,427 | 14,795 |
| Adjustments to EBITDA from homes sold[1] | (241) | (172) | (120) | (188) | (409) | (1,141) |
| **Normalized EBITDA** | $14,117 | $10,156 | $10,396 | $14,358 | $14,018 | $13,654 |

(1) "Adjustments to revenues from homes sold" and "Adjustments to EBITDA from homes sold" reflect the elimination of the current and historical operating results for all periods presented of funeral homes that were sold as follows:

| | Businesses Sold | Funeral Homes Sold | Cemeteries Sold |
|---|---|---|---|
| 2001 | 1 | 2 | — |
| 2002 | 1 | 1 | 1 |
| 2003 | 3 | 5 | — |
| Nine Months Ended September 30, 2004 | 1 | 4 | — |
| Total | 6 | 12 | 1 |

### Hamilton

| | 12 Months Ended September 30, | Nine Months Ended September 30, | | Year Ended December 31, | | |
|---|---|---|---|---|---|---|
| | 2004 | 2004 | 2003 | 2003 | 2002 | 2001 |
| | | (U.S. dollars in thousands) | | | | |
| **Revenue** | $37,592 | $27,564 | $27,999 | $38,026 | $40,211 | $39,337 |
| Adjustments to revenue from homes sold(1) | — | — | — | — | — | 730 |
| **Normalized Revenue** | $37,592 | $27,564 | $27,999 | $38,026 | $40,211 | $38,607 |
| **Net Income (loss)** | $(9,473) | $(8,380) | $(5,092) | $(6,185) | $(4,866) | $(6,945) |
| Adjustments to net income (loss) | | | | | | |
| Noncompete expenses | 1,162 | 809 | 977 | 1,330 | 1,312 | 1,389 |
| Consulting expenses | 377 | 283 | 411 | 505 | 494 | 572 |
| Depreciation and amortization | 2,001 | 1,465 | 1,448 | 1,984 | 1,881 | 3,280 |
| Impairment of goodwill | — | — | — | — | — | 312 |
| Interest expense | 11,627 | 8,888 | 7,940 | 10,679 | 10,491 | 11,447 |
| Dividends | 42 | 31 | 31 | 42 | 42 | 42 |
| Deferred loan cost amortization | 1,881 | 1,819 | 894 | 956 | 1,619 | 951 |
| (Gain) loss on sale of property | (2) | — | (159) | (161) | — | 157 |
| Income taxes | 502 | 381 | 364 | 485 | 1,537 | — |
| (Income) loss from operations of discontinued operations | 1,260 | 1,170 | 101 | 191 | (822) | (414) |
| Adjustments to EBITDA for homes sold and classified as discontinued operations | 108 | 160 | 1,274 | 1,257 | 2,050 | 2,122 |
| **EBITDA** | 9,485 | 6,626 | 8,189 | 11,083 | 13,738 | 12,913 |
| Adjustments to EBITDA from homes sold(1) | (108) | (160) | (1,274) | (1,257) | (2,050) | (2,300) |
| **Normalized EBITDA** | $ 9,377 | $ 6,466 | $ 6,915 | $ 9,826 | $11,688 | $10,613 |

(1) "Adjustments to revenues from homes sold" and "Adjustments to EBITDA from homes sold" reflect the adjustments of the current and historical operating results for all periods presented of funeral homes that were sold and not reflected as discontinued operations as follows:

| | Businesses Sold | Funeral Homes Sold | Cemeteries Sold |
|---|---|---|---|
| 2001 (not reflected as discontinued operations) | 1 | 2 | — |
| 2002 | — | — | — |
| 2003 | 3 | 6 | — |
| Nine Months Ended September 30, 2004 | 1 | 7 | — |
| Total | 5 | 15 | — |

**Combined Keystone North America**

| | 12 Months Ended September 30, 2004 |
|---|---|
| | (In thousands except hedge rate) |
| **Net Income (loss)** | $(6,393) |
| Adjustments to Net income (loss) | |
| Noncompete expense | 1,162 |
| Consulting Expense | 377 |
| Depreciation and amortization | 5,168 |
| Interest | 17,919 |
| Impairment of long-lived assets | 111 |
| Dividends | 42 |
| Amortization of deferred loan costs | 1,881 |
| Gain (loss) on sale of property | (2) |
| Income taxes | 2,210 |
| Adjustments to EBITDA for homes sold and classified as discontinued operations | 108 |
| Income Loss from discontinued operations | 1,260 |
| **EBITDA** | 23,843 |
| Adjustments to EBITDA from funeral homes sold | (349) |
| **Normalized EBITDA** | 23,494 |
| Management believes that the following items will increase (reduce) the amount available for distribution by the Issuer: | |
| Cost savings from Hamilton acquisition(1) | 2,187 |
| Maintenance capital expenditures | (2,900) |
| Additional administrative expenses(2) | (1,000) |
| Interest on new credit facility(3) | (3,070) |
| Interest on Separate Subordinated Notes(4) | (1,182) |
| Income taxes paid in cash | (341) |
| Distributable Cash before Cash Holdback | $17,188 |
| Distributable Cash Holdback (5%) | 859 |
| Distributable Cash | $16,329 |

(1) Includes reductions in Hamilton corporate overhead costs comprised primarily of headcount reductions and related expenses (rent, travel, healthcare, etc.) and $300 in procurement savings related to casket purchases.

(2) Represents estimated administrative expenses to be incurred following the offering in connection with ongoing public disclosure requirements, investor relations, director fees and other expenses.

(3) Represents estimated interest on New Credit Facility based on an average of outstanding balances.

(4) Interest is payable in C$ and is calculated based on a five-year C$/US$ hedge rate as of January 28, 2005.

## SELECTED FINANCIAL AND OPERATING INFORMATION

The following table sets out selected financial and operating information for the periods indicated that has been derived from (and should be read in conjunction with) the historical financial statements of Keystone and Hamilton contained elsewhere in this prospectus:

**Financial Information**(1)

| | 12 Months Ended September 30 | Nine Months Ended September 30 | | Year Ended December 31 | | |
|---|---|---|---|---|---|---|
| | 2004 | 2004 | 2003 | 2003 | 2002 | 2001 |
| | (U.S. dollars in thousands) | | | | | |
| **Revenue** | | | | | | |
| Keystone | $48,583 | $35,856 | $36,158 | $48,885 | $50,767 | $50,852 |
| Hamilton | 37,592 | 27,564 | 27,999 | 38,026 | 40,211 | 39,337 |
| Total | $86,175 | $63,420 | $64,157 | $86,911 | $90,978 | $90,189 |
| **Cost and Expenses (including Corporate, General and Administrative)** | | | | | | |
| Keystone | $34,657 | $25,890 | $25,881 | $34,648 | $36,577 | $36,611 |
| Hamilton | 28,215 | 21,098 | 21,084 | 28,201 | 28,523 | 28,547 |
| Total | $62,872 | $46,988 | $46,965 | $62,849 | $65,100 | $65,158 |
| **EBITDA**(2) | | | | | | |
| Keystone | $14,358 | $10,328 | $10,516 | $14,546 | $14,427 | $14,795 |
| Hamilton | 9,485 | 6,626 | 8,189 | 11,083 | 13,738 | 12,913 |
| Total | $23,843 | $16,954 | $18,705 | $25,629 | $28,165 | $27,708 |
| **Capital Expenditures**(3) | | | | | | |
| Keystone | $ 1,481 | $ 1,222 | $ 1,289 | $ 1,549 | $ 1,470 | $ 1,083 |
| Hamilton | 1,247 | 587 | 962 | 1,621 | 1,415 | 1,146 |
| Total | $ 2,728 | $ 1,809 | $ 2,251 | $ 3,170 | $ 2,885 | $ 2,229 |
| **Normalized Revenue**(2) | | | | | | |
| Keystone | $47,923 | $35,410 | $35,121 | $47,634 | $47,961 | $46,949 |
| Hamilton | 37,592 | 27,564 | 27,999 | 38,026 | 40,211 | 38,607 |
| Total | $85,515 | $62,974 | $63,120 | $85,660 | $88,172 | $85,556 |
| **Normalized EBITDA**(2) | | | | | | |
| Keystone | $14,117 | $10,156 | $10,396 | $14,358 | $14,018 | $13,654 |
| Hamilton | 9,377 | 6,466 | 6,915 | 9,826 | 11,688 | 10,613 |
| Total | $23,494 | $16,622 | $17,311 | $24,184 | $25,706 | $24,267 |

### Operating Information

| | As at September 30 | | As at December 31 | | |
|---|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 | 2001 |
| **Number of funeral homes** | | | | | |
| Keystone | 97 | 101 | 101 | 106 | 107 |
| Hamilton | 80 | 86 | 86 | 92 | 93 |
| Total | 177 | 187 | 187 | 198 | 200 |
| **Number of cases** | | | | | |
| Keystone | 7,557 | 7,865 | 10,664 | 11,144 | 11,091 |
| Hamilton | 6,002 | 6,502 | 8,694 | 9,377 | 9,274 |
| Total | 13,559 | 14,367 | 19,358 | 20,521 | 20,365 |
| **Average funeral revenue per case** | | | | | |
| Keystone | $4,368 | $4,218 | $ 4,235 | $ 4,116 | $ 4,180 |
| Hamilton | 4,547 | 4,633 | 4,600 | 4,591 | 4,590 |
| Combined Average | $4,447 | $4,406 | $ 4,394 | $ 4,333 | $ 4,367 |

(1) The financial information presented in this table is derived from our Canadian GAAP based financial statements. Management does not believe that the presentation of the above financial information would be materially different if reported using accounting principles generally accepted in the United States.

(2) EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash may not be comparable to similar measures presented by other companies. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash" and "Reconciliation of Historical Results to EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash". As the Issuer intends to distribute substantially all of the Issuer's cash on an ongoing basis, management believes that EBITDA, Normalized EBITDA and Distributable Cash are important measures in evaluating the Issuer's performance and in determining whether to invest in IPSs.

(3) Virtually all capital expenditures over the period presented represent maintenance capital expenditures. See "Our Business — Capital Expenditures".

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS OF KEYSTONE

*Information in this management's discussion and analysis of the financial condition and results of operations of Keystone is supplemental to, and should be read in conjunction with, the financial statements of Keystone included in this prospectus. It also contains forward-looking statements, which are subject to a variety of factors that could cause actual results to differ materially from those contemplated by these statements. See "Forward-Looking Statements". Some of the factors that could cause results or events to differ from current expectations include, but are not limited to, the factors described under "Risk Factors". The financial statements included in this prospectus have been prepared in accordance with GAAP.*

*The information provided in this management's discussion and analysis of the financial condition and results of operations relates to Keystone as a stand-alone entity, prior to its acquisition of certain of Hamilton's subsidiaries that is to occur on the closing of this offering.*

### Overview

The funeral and cemetery industry in the United States generates an estimated $15 billion in total revenues annually. The funeral business is characterized by predictable and stable demand dynamics, significant barriers to entry, a mature competition base, positive operating margins, and highly fragmented ownership. The primary market drivers of the funeral industry are local heritage, the total mortality of the local service area and the mix of business between cremation and burial.

Upon completion of this offering and Keystone's acquisition of Hamilton, management believes that Keystone will be the fifth largest provider of funeral services with 177 funeral homes and nine cemeteries. These funeral homes provide a full range of funeral services on both an at-need (at time of death) and pre-need (prior to death) basis. These services include removal of human remains, planning and coordinating personalized funerals and cremations, professional embalming, use of our funeral home facilities, merchandise sales, conducting memorial services, performing cremations and cemetery interment services. Over 95% of our revenue is generated from funeral related services and products. Our two largest expense categories, personnel and costs of goods sold, comprise 30% and 15% of revenues, respectively. Certain economies of scale can be achieved by sharing resources between facilities within a service area.

Keystone funeral homes represent well-established businesses with an average age of the original businesses in excess of 50 years. Our funeral homes are located in 26 states covering the Midwest, Northeast, Southeast and Northwest regions of the continental United States. Our individual service markets are primarily made up of non-urban areas. These non-urban markets tend to experience less competition and exhibit a stronger heritage dynamic.

Our executive management team is comprised of four seasoned funeral professionals who collectively have spent 125 years successfully acquiring, integrating and managing funeral businesses. Local management consists substantially of former owners, their former managers and their other key employees. We have very strong relationships with the former owners of these funeral businesses, with approximately 80% still actively supporting our funeral homes in some significant way. Since 2000, there has been limited consolidation in the industry due to constrained access to capital. As a result, management has focused on organic growth to increase profitability. By successfully executing a business strategy that emphasizes strategic acquisition of funeral homes with strong franchise value, operating efficiency, product and service offering expansion, and margin improvement, we have experienced stable and consistent revenue and revenues net of costs and expenses and corporate, general and administrative expenses over time.

*Business Disposals:*

During 2004 and 2003 Keystone disposed of nine funeral homes that were purchased by former owners or the management team of the funeral homes for multiples of cash flow at or above market parameters. In July 2004, Keystone, in a single transaction, disposed of four funeral homes in Nebraska. Of the net proceeds of $1.7 million, $1.6 million was required to be applied to Keystone's outstanding term loan.

During 2003, in five separate transactions, Keystone disposed of five funeral homes, one each in Florida, Illinois, Iowa, Massachusetts, and Michigan. The combined net proceeds of approximately $3.1 million from the sales was required to be applied to Keystone's outstanding term loan.

During 2002, in a single transaction, Keystone disposed of one funeral home and one cemetery in Indiana. The net proceeds of $1.4 million were required to be applied to the term loan.

During 2001, Keystone disposed of two funeral homes in Kentucky in one transaction. The net proceeds of $1.7 million were required to be applied to the term loan.

**Results of Operations**

| | Nine Months Ended September 30 | | Year Ended December 31 | | |
|---|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 | 2001 |
| | (U.S. dollars in thousands) | | | | |
| Revenues | $35,856 | $36,158 | $48,885 | $50,767 | $50,852 |
| Costs and expenses | 23,460 | 23,453 | 31,460 | 32,393 | 32,768 |
| Corporate, general and administrative expenses | 2,430 | 2,427 | 3,188 | 4,184 | 3,842 |
| Depreciation and amortization | 2,355 | 2,392 | 3,204 | 3,414 | 5,345 |
| Impairment of long-lived assets | 111 | — | — | 1,149 | — |
| Income from operations | $ 7,500 | $ 7,885 | $11,033 | $ 9,626 | $ 8,896 |
| Interest expense | 4,607 | 4,791 | 6,476 | 7,800 | 9,871 |
| Other income | 363 | 239 | 310 | 238 | 554 |
| Income tax expense | 1,096 | 1,331 | 1,943 | 1,188 | 458 |
| Net Income (Loss) | $ 2,159 | $ 2,002 | $ 2,923 | $ 876 | $ (879) |
| Costs and expenses as a % of revenues | 65.4% | 64.9% | 64.4% | 63.8% | 64.4% |
| Corporate, general and administrative as a % of revenues | 6.8% | 6.7% | 6.5% | 8.2% | 7.6% |

**Consolidated Balance Sheets**

| | September 30, 2004 | December 31, 2003 | December 31, 2002 |
|---|---|---|---|
| Total assets | $142,568 | $145,523 | $151,256 |
| Total long-term liabilities[(1)] | $ 36,842 | $ 39,515 | $117,911 |

(1) Excludes $77.1 million of senior debt reclassified to current debt as of September 30, 2004 and December 31, 2003, respectively.

*Nine Months ending September 30, 2004 compared to Nine Months Ending September 30, 2003*

*Dispositions:*

Keystone disposed of four funeral homes in the period ended September 30, 2004 and five funeral homes in the period ended September 30, 2003. The results of these divested homes are as follows:

| | Nine Months Ended September 30 | |
|---|---|---|
| | 2004 | 2003 |
| | (U.S. dollars in thousands) | |
| Revenues | $446 | $1,036 |
| Costs and expenses | 250 | 795 |
| Depreciation and amortization | 22 | 83 |
| Impairment of long-lived assets | 111 | — |
| Income from operations | 63 | 158 |
| Interest expense | 107 | 255 |
| Other income (loss) | (24) | (121) |
| Income tax expense (benefit) | (23) | (87) |
| Net loss | $(45) | $ (131) |

*Revenues:*

Revenues for the period ended September 30, 2004 were $35.9 million compared to $36.2 million for the period ended September 30, 2003, representing a decrease of $0.3 million, or 0.8%. Keystone disposed of five funeral homes in 2003 and four funeral homes in 2004. Divested homes generated revenue of $0.4 million through September 30, 2004 and $1.0 million through September 30, 2003, resulting in a $0.6 million decrease in revenues period-over-period. Prices increases resulted in a slight increase in comparable funeral home revenues period-over-period. Revenues consist of the following:

| | Nine Months Ended September 30, 2004 | | Nine Months Ended September 30, 2003 | |
|---|---|---|---|---|
| | (U.S. dollars in thousands) | | | |
| Burial | $25,677 | 71.6% | $26,208 | 72.5% |
| Cremation | 5,894 | 16.4% | 5,577 | 15.4% |
| Other funeral services | 2,347 | 6.5% | 2,358 | 6.5% |
| Other | 1,938 | 5.4% | 2,015 | 5.6% |
| Total | $35,856 | 100.0% | $36,158 | 100.0% |

Burial revenues decreased $0.5 million, or 2.0% from the period ended September 30, 2003 to the period ended September 30, 2004. The decrease can be attributed to a 6.7% decrease in the number of burial services performed over the comparable period. This decrease was mitigated by a 5.0% increase in the average sales price per burial service. Burial revenues from homes that were sold accounted for a decrease of $0.5 million period-over-period.

Cremation revenues increased $0.3 million, or 5.7% from the period ended September 30, 2003 to the period ended September 30, 2004. The increase can be attributed to a 0.5% increase in the number of cremation services performed and a 5.2% increase in the average sales price per cremation service over the comparable period. Cremation revenues from homes that were sold decreased $0.1 million period-over-period.

Other funeral service revenues, which consist primarily of monument sales and shipping revenues, decreased $0.01 million from the period ended September 30, 2003 to the period ended September 30, 2004. This decrease can be primarily attributed to minimal decreases in monument sales revenue, slightly offset by a minimal increase in shipping revenue.

Other revenues, which consist of pre-need sales commissions, cemetery revenues and other ancillary revenues, decreased $0.1 million or 3.8% from the period ended September 30, 2003 to the period ended September 30, 2004. This decrease can be attributed to minor decreases in both insurance sales commissions and cemetery revenues.

Management believes that cremation rates will continue to rise modestly in future years. Additionally, our average sales price per service for all categories of services will increase over time as management's marketing initiatives have a positive impact on our funeral home operations.

*Costs and expenses:*

Costs and expenses for the interim period ending September 30, 2004 were $23.5 million, or 65.4% of sales, compared to $23.5 million, or 64.9% of sales, for the interim period ending September 30, 2003. Costs and expenses decreased period-over-period related to homes that were sold by $0.5 million, or 2.3%. Costs and expenses consist of the following:

| | Nine Months Ended September 30, 2004 | | Nine Months Ended September 30, 2003 | |
|---|---|---|---|---|
| | (U.S. dollars in thousands) | | | |
| Personnel | $11,790 | 50.3% | $11,671 | 49.8% |
| Cost of goods sold | 5,050 | 21.5% | 5,307 | 22.6% |
| Other | 6,620 | 28.2% | 6,475 | 27.6% |
| Total | $23,460 | 100.0% | $23,453 | 100.0% |

Personnel costs increased $0.1 million, or 1.0% from the period ended September 30, 2003 to the period ended September 30, 2004. This increase can be attributed to cost of living wage adjustments.

Costs of goods sold decreased $0.3 million, or 4.8% from the period ended September 30, 2003 to the period ended September 30, 2004. This decrease can be attributed to the shift in case mix from burials, which incur higher costs of goods as a percentage of revenues than cremation cases, indicated by a $0.5 million decrease in burial revenues and a $0.3 million increase in cremation revenues.

Other costs and expense increased $0.1 million, or 2.2% from the period ended September 30, 2003 to the period ended September 30, 2004. This increase can be attributed to increases in office supplies and miscellaneous funeral supplies.

Management expects costs to continue at the current percent of revenues, rising modestly with inflation.

*Corporate general and administrative expenses:*

Corporate general and administrative expenses remained constant at $2.4 million, or 6.8% of revenues, for the interim period ended September 30, 2004 compared to 6.7% of revenues for the interim period ended September 30, 2003. Management believes the corporate general and administrative costs will increase following the offering in terms of dollars due to the additional administrative cost of being a public company, but will decrease as a percentage of the increased revenue base of the combined companies.

*Depreciation and amortization:*

Depreciation and amortization remained constant at $2.4 million for the interim period ended September 30, 2004, compared to the interim period ended September 30, 2003. Depreciation and amortization will be impacted significantly by the finalization of purchase price allocation, post acquisition, by Keystone North America.

*Impairment of long-lived assets:*

A loss on impairment of $0.1 million was recorded the interim period ending September 30, 2004 related to the disposal of a funeral home. No such charge was incurred in 2003.

*Income from operations:*

Income from operations decreased to $7.5 million for the period ended September 30, 2004 from $7.9 million for the period ended September 30, 2003, as a result of a decrease of $0.3 million in revenues and a $0.1 million loss on impairment.

*Interest expense:*

Interest expense for the September 30, 2004 interim period was $4.6 million compared to $4.8 million for the September 30, 2003 interim period, a decrease of $0.2 million. Interest expense decreased due to lower interest rates paid on our existing senior debt facility and due to the overall reduction in our outstanding indebtedness. Management believes that, upon completion of this offering, additional interest expense will be incurred due to the new debt structure.

*Income tax expense:*

Income tax expense was $1.1 million for the interim period ended September 30, 2004 and $1.3 million for the interim period ended September 30, 2003. The effective rate of 40% for 2003 decreased to 34% primarily due to a reassessment of the valuation reserves that were placed on certain tax assets.

*Net income:*

Net income increased to $2.2 million for the interim period ended September 30, 2004 from $2.0 million for the interim period ended September 30, 2003 primarily as a result of reduced income tax expense and reduced interest expense offset by the impairment charge recorded in the interim period ending September 30, 2004.

***Year ended December 31, 2003 Compared to Year ended December 31, 2002***

*Dispositions:*

Keystone disposed of five funeral homes in the year ended December 31, 2003 and one funeral home *and* one cemetery in the year ended December 31, 2002. The results of these divested homes are as follows:

| | Year Ended December 31 | |
|---|---|---|
| | 2003 | 2002 |
| | (U.S. dollars in thousands) | |
| Revenues | $ 421 | $ 2,061 |
| Costs and expenses | 408 | 1,859 |
| Depreciation and amortization | 42 | 221 |
| Impairment of long-lived assets | — | 1,105 |
| Income from operations | (29) | (1,124) |
| Interest expense | 99 | 552 |
| Other income (loss) | (118) | (40) |
| Income tax benefit | (98) | (987) |
| Net Income (Loss) | $(147) | $ (729) |

*Revenues:*

Revenues for the year ended 2003 were $48.9 million compared to $50.8 million for the year ended 2002, representing a decrease of $1.9 million, or 3.7%. Keystone disposed of one funeral home and one cemetery in 2002 and five funeral homes in 2003. Divested homes generated revenue of $0.4 million in 2003 and $2.1 million in 2002, resulting in a $1.7 million decrease in revenues year-over-year. Pre-need funeral sales decreasing by approximately $0.4 million from $2.0 million in 2002 to $1.6 million in 2003 offset by price increases resulted in the net $0.2 million decrease in comparable funeral home revenues year-over-year. Revenues consist of the following:

| | Year Ended December 31, 2003 | | Year Ended December 31, 2002 | |
|---|---|---|---|---|
| | (U.S. dollars in thousands) | | | |
| Burial | $35,718 | 73.1% | $36,068 | 71.0% |
| Cremation | 7,592 | 15.5% | 7,806 | 15.4% |
| Other funeral services | 3,103 | 6.3% | 3,969 | 7.8% |
| Other | 2,472 | 5.1% | 2,924 | 5.8% |
| Total | $48,885 | 100.0% | $50,767 | 100.0% |

Burial revenues decreased $0.4 million, or 2.1% from the year ended December 31, 2002 to the year ended December 31, 2003. The decrease can be attributed to a 5.8% decrease in the number of burial services performed over the comparable period. This decrease was offset by a 5.1% increase in the average sales price per burial service. Burial revenues from homes that were sold accounted for a decrease $0.6 million year-over-year.

Cremation revenues decreased $0.2 million, or 2.7% from the year ended December 31, 2002 to the year ended December 31, 2003. The decrease was caused by a 9.2% decrease in the number of cremation services performed, which can be primarily attributed to the 2003 divesture of a home that performed 7.5% of the consolidated cremation services. The decrease in services was slightly mitigated by a 7.1% increase in the average sales price per cremation service over the comparable period. Cremation revenues from homes that were sold decreased $0.3 million year-over-year.

Other funeral service revenues, which consist of monument sales, shipping revenues, and trade revenues, decreased $0.9 million, or 21.8% from the year ended December 31, 2002 to the year ended December 31, 2003. Divested homes generated $0.4 million in trade revenues and $0.4 million in shipping revenues during 2002, due in large part to trade and shipping contracts held by one home that was divested in the first month of 2003 accounting for $0.8 million of the reduction in revenues year-over-year.

Other revenues, which consist of pre-need sales commissions, cemetery revenues and other ancillary revenues, decreased $0.5 million or 15.5% the year ended December 31, 2002 to the year ended December 31, 2003. This decrease can be attributed a $0.4 million decrease in revenues generated from pre-need sales. Other revenues from homes that were sold decreased $0.1 million year-over-year.

*Costs and expenses:*

Costs and expenses for the year ended 2003 were $31.5 million, or 64.4% of sales, compared to $32.4 million, or 63.8% of sales, for the year ended 2002, a decrease of $0.9 million or 2.9%. Costs related to the disposition of funeral homes during 2003 and 2002 resulted in a decrease in costs of $1.5 million or 4.5%. The offsetting $0.6 million increase in costs and expenses can primarily be attributed to annual salary increases of approximately $0.3 million due to cost of living wage adjustments and $0.1 million increase in utility expenses. Costs and expenses consist of the following:

| | Year Ended December 31, 2003 | | Year Ended December 31, 2002 | |
|---|---|---|---|---|
| | (U.S. dollars in thousands) | | | |
| Personnel | $15,593 | 49.6% | $16,324 | 50.4% |
| Cost of goods sold | 7,172 | 22.8% | 7,205 | 22.2% |
| Other | 8,695 | 27.6% | 8,864 | 27.4% |
| Total | $31,460 | 100.0% | $32,393 | 100.0% |

Personnel costs decreased $0.7 million, or 4.5% from the year ended December 31, 2002 to the year ended December 31, 2003. This decrease can be attributed to savings resulting from the homes that were sold slightly offset by cost of living wage increases.

Costs of goods sold remained consistent from the year ended December 31, 2002 to the year ended December 31, 2003.

Other costs and expense decreased $0.2 million, or 1.9% from the year ended December 31, 2002 to the year ended December 31, 2003. This decrease can be attributed to decreased advertising expenditures year-over-year slightly mitigated by increases utility expenses.

*Corporate, general and administrative expenses:*

Corporate, general and administrative expenses for the year ended 2003 were $3.2 million, or 6.5% of sales, compared to $4.2 million, or 8.2% of sales, for the year ended 2002, a decrease of $1.0 million or 23.8%. This decrease was primarily due to non-recurring expenditures made in 2002 such as $0.4 million incurred in conjunction with consulting services related to existing financing and non-recurring legal costs of $0.2 million associated with the legal defense of a non-compete agreement. Included in the reduction is a decrease in telecommunication spending of $0.2 million from 2002 to 2003.

*Depreciation and amortization:*

Depreciation and amortization for the year ended 2003 was $3.2 million compared to $3.4 million for the year ended 2002, a decrease of $0.2 million or 6.1% related to the impact of funeral home dispositions in 2002 and 2003.

*Impairment of long-lived assets:*

A loss on impairment of $1.1 million was recorded in the year ended 2002 related to the disposition of two funeral homes. No such charge was incurred in 2003.

*Income from operations:*

Income from operations increased to $11.0 million for the year ended 2003 from $9.6 million for the year ended 2002 primarily as a result of reduced corporate, general and administrative expenses and the 2002 impairment charge.

*Interest expense:*

Interest expense for the year ended 2003 was $6.5 million compared to $7.8 million for the year ended 2002, a decrease of $1.3 million. Interest expense decreased due to lower interest rates paid on our existing senior debt facility and due to the overall reduction in our outstanding indebtedness by approximately $9.8 million from 2002 to 2003.

*Income tax expense:*

Income tax expense was $1.9 million for the year ended 2003 compared to $1.2 million for the year ended 2002, an increase of $0.8 million. This increase in income tax expense resulted from federal loss carryforwards being exhausted during 2002.

*Net income:*

Net income increased to $2.9 million for the year ended 2003 from net income of $0.9 million for the year ended 2002. This $2.0 million increase in net income is attributed primarily to the impairment loss recorded in 2002 of approximately $1.1 million and reductions in corporate, general and administrative expenses and interest expense as noted above, offset by an increase in income tax expense.

***Year ended December 31, 2002 Compared to Year ended December 31, 2001***

*Dispositions:*

Keystone disposed of one funeral home and one cemetery in the year ended December 31, 2002 and two funeral homes in the year ended December 31, 2001. The results of these divested homes are as follows:

| | Year Ended December 31 | |
|---|---|---|
| | **2002** | **2001** |
| | (U.S. dollars in thousands) | |
| Revenues | $226 | $908 |
| Costs and expenses | 184 | 611 |
| Depreciation and amortization | 23 | 105 |
| Impairment of long-lived assets | — | — |
| Income from operations | $ 19 | $192 |
| Interest expense | 74 | 249 |
| Other income (loss) | (32) | 178 |
| Income tax expense (benefit) | (50) | 83 |
| Net Income (Loss) | $(37) | $ 38 |

*Revenues:*

Revenues for the year ended 2002 were $50.8 million compared to $50.9 million for the year ended 2001, representing a decrease of $0.1 million, or 0.2%. Keystone disposed of one funeral home and one cemetery in 2002 and two funeral homes in 2001, these homes generated revenue of $0.2 million in 2002 and $0.9 million in 2001, respectively. The impact of increased pre-need funeral sales of $0.5 million year-over-year and price increases resulted in the net increase in comparable funeral home revenues. Revenues consist of the following:

| | Year Ended December 31, 2002 | | Year Ended December 31, 2001 | |
|---|---|---|---|---|
| | (U.S. dollars in thousands) | | | |
| Burial | $36,068 | 71.0% | $37,252 | 73.3% |
| Cremation | 7,806 | 15.4% | 7,352 | 14.5% |
| Other funeral services | 3,969 | 7.8% | 3,807 | 7.5% |
| Other | 2,924 | 5.8% | 2,441 | 4.8% |
| Total | $50,767 | 100.0% | $50,852 | 100.0% |

Burial revenues decreased $1.2 million, or 3.2% from the year ended December 31, 2001 to the year ended December 31, 2002. The decrease can be attributed to a 4.1% decrease in the number of burial services performed over the comparable period. This decrease was offset by a 0.9% increase in the average sales price per burial service. Burial revenues from homes that were sold accounted for a decrease of $0.5 million year-over-year.

Cremation revenues increased $0.5 million, or 6.2% from the year ended December 31, 2001 to the year ended December 31, 2002. The increase can be attributed to a 6.0% increase in the number of cremation services performed and a 0.2% increase in the average sales price per cremation service over the comparable period. Cremation revenues from homes that were sold did not change year-over-year.

Other funeral service revenues, which consist of monument sales, shipping revenues, and trade revenues, increased $0.2 million from the year ended December 31, 2001 to the year ended December 31, 2002. This increase can be attributed to shipping revenues increasing from $2.2 million to $2.3 million.

Other revenues, which consist of pre-need sales commissions, cemetery revenues and other ancillary revenues, increased $0.5 million or 19.8% from the year ended December 31, 2001 to the year ended December 31, 2002. This increase can be attributed to increased volume of pre-need sales resulting in a $0.5 million increase slightly offset by a slight decline in year-over-year cemetery revenues.

*Costs and expenses:*

Costs and expenses for the year ended 2002 were $32.4, or 63.8% of sales, million compared to $32.8 million, or 64.4% of sales, for the year ended 2001, a decrease of $0.4 million or 1.1% related to the disposition of two funeral homes. On a comparable funeral home basis, labor costs increased approximately $0.5 million due to annual salary increases and increased health insurance and workers compensation insurance rates, which was offset by a decrease in costs related to enhanced purchase discounts and reduced merchandise costs associated with a new casket supplier beginning in 2002. Costs and expenses consist of the following:

| | Year Ended December 31, 2002 | | Year Ended December 31, 2001 | |
|---|---|---|---|---|
| | (U.S. dollars in thousands) | | | |
| Personnel | $16,324 | 50.4% | $16,033 | 48.9% |
| Cost of goods sold | 7,205 | 22.2% | 7,560 | 23.1% |
| Other | 8,864 | 27.4% | 9,175 | 28.0% |
| Total | $32,393 | 100.0% | $32,768 | 100.0% |

Personnel costs increased $0.3 million, or 1.8% from the year ended December 31, 2001 to the year ended December 31, 2002. This increase can be attributed to cost of living wage increases and increased health insurance and workers' compensation insurance rates.

Costs of goods sold decreased $0.4 million from the year ended December 31, 2001 to the year ended December 31, 2002. This decrease can be attributed to enhanced purchase discounts and reduced merchandise costs associated with a new casket supplier beginning in 2002.

Other costs and expense decreased $0.3 million, or 3.4% from the year ended December 31, 2001 to the year ended December 31, 2002. This decrease can be attributed to lower telephone expenses as a result of switching to a company-wide long distance plan.

*Corporate, general and administrative expenses:*

Corporate, general and administrative expenses for the year ended 2002 were $4.2 million, or 8.2% of sales, compared to $3.8 million, or 7.6% of sales, for the year ended 2001, an increase of $0.3 million or 8.9%. This increase was due to expenditures made in 2002 including $0.4 million incurred in conjunction with certain consulting services related to existing financing.

*Depreciation and amortization:*

Depreciation and amortization for the year ended 2002 was $3.4 million compared to $5.3 million for the year ended 2001, a decrease of $1.9 million or 36.1%. The difference is attributed to the adoption of new accounting standards that ceased the amortization of goodwill at the beginning of 2002. Keystone recorded no amortization expense for goodwill in 2002 and $1.3 million in 2001.

*Impairment of long-lived assets:*

A loss on impairment of $1.1 million was recorded in the year ended 2002 when Keystone formalized a plan to dispose of two funeral homes.

*Income from operations:*

Income from operations increased to $9.6 million for the year ended 2002 from $8.9 million for the year ended 2001 primarily as a result of amortization due to accounting changes which were offset slightly by the 2002 charge for impairment of long-lived assets.

*Interest expense:*

Interest expense for the year ended 2002 was $7.8 million compared to $9.9 million for the year ended 2001, a decrease of $2.1 million, which was a direct result of lower interest rates paid on the existing senior debt facility in addition to the reduction of overall debt levels by $4.8 million from 2001 to 2002.

*Income tax expense:*

Income tax expense was $1.2 million for the year ended 2002 compared to $0.5 million for the year ended 2001, an increase of $0.7 million. This difference pertains to the Keystone's federal net loss carryforwards that allowed the Keystone to only pay U.S. state taxes during 2001 and no U.S. federal tax. These U.S. federal benefits were exhausted during 2002 and Keystone paid both U.S. state taxes and a portion of U.S. federal taxes in fiscal 2002 that could not be offset by existing net loss carryforwards.

*Net income (loss):*

Net income increased to $0.9 million for the year ended 2002 from a net loss of $0.9 million for the year ended 2001. This $1.8 million increase can be attributed to the above items.

**Liquidity and Capital Resources**

Since its inception, Keystone has funded its acquisition growth with a combination of proceeds from debt and equity financing. We have historically funded our ongoing liquidity requirements from our operating cash flow and anticipate being able to continue to do so in the future. At September 30, 2004, Keystone had cash balances available to it of $3.3 million, which is adequate to fund short term operating needs.

The Company is currently pursuing a merger and concurrent initial public offering that will secure the capital required to retire all existing indebtedness. Management believes the Company will be able to successfully refinance or extend the Revolver and Term Loan should the offering not be completed as intended. However, if management is unable to retire through the public offering or otherwise refinance its debt obligations, the Company could be required to undertake restructuring or other changes in the business during the year ending December 31, 2005. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

*Senior Indebtedness*

The current senior credit facility was established in 1997 and expanded in 1998 to accommodate additional acquisition activity. The remaining principal and interest on this facility of $75.5 million at September 30, 2004 was due on January 31, 2004. Keystone has made payments required under the terms of the credit agreement and payments in excess of those required with proceeds from strategic dispositions. Principal payments were as follows:

| | Nine Months Ended September 30 | | Year Ended December 31 | | |
|---|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 | 2001 |
| Scheduled payments | $ — | $5,550,000 | $6,750,000 | $1,800,000 | $ 300,000 |
| Excess payments | 1,600,000 | 1,280,761 | 1,324,186 | 1,355,337 | 1,698,397 |
| Total | $1,600,000 | $6,830,761 | $8,074,186 | $3,155,337 | $1,998,397 |

In connection with this offering, we will use the proceeds to, in part, retire all existing senior indebtedness and to set aside proceeds of the transaction as restricted cash specifically to satisfy payments on the former owner obligations of both Hamilton and Keystone. See "Use of Proceeds". Management believes Keystone will be able to successfully refinance or extend the revolver and term loan under our existing credit facility should the offering not be completed as intended. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should Keystone be unable to continue as a going concern. See "Use of Proceeds".

| | Nine Months Ended September 30 | | Year Ended December 31 | |
|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 |
| | (U.S. dollars in thousands) | | | |
| Operating activities | $ 3,774 | $ 5,291 | $ 6,008 | $ 7,371 |
| Investing activities | $ 330 | $ 1,728 | $ 1,374 | $ (676) |
| Financing activities | $(2,708) | $(7,849) | $(9,208) | $(4,791) |
| Increase (decrease) in cash | $ 1,396 | $ (830) | $(1,826) | $ 1,904 |

*Net cash provided by operating activities:*

Net cash provided by operating activities for the nine months ended September 30, 2004 was $3.8 million, which represents a reduction of approximately $1.5 million in comparison to the nine months ended September 30, 2003. This reduction primarily resulted from the net reduction of accounts payable, accrued salaries and wages, and other accrued expenses.

Net cash provided by operating activities was $6.0 million for 2003, primarily due to net income of $2.9 million plus $3.8 million of non-cash depreciation and amortization, and future taxes partially offset by $1.1 million reduction in cash due to changes in working capital.

Net cash provided by operating activities was $7.4 million for 2002, primarily due to net income of $0.9 million plus $4.9 million of non-cash depreciation and amortization, loss on impairment of assets and deferred taxes. Additional cash of $1.3 million resulted from changes in working capital primarily related to increased accounts payable due to extended terms made available under a new supply arrangement for caskets.

*Net cash provided by or used in investing activities:*

For the nine months ended September 30, 2004, net cash provided by investing activities was $0.3 million down from $1.7 million for the nine months ended September 30, 2003. This net reduction of $1.4 million was a direct result of fewer dispositions in 2004 as compared to 2003.

In 2003, Keystone spent $1.5 million on purchases of property and equipment and $0.1 million on deposits in marketable securities. Proceeds of $3.1 million were received from the sale of assets and funeral homes.

In 2002, Keystone spent $1.5 million on purchases of property and equipment and $0.6 million on deposits in marketable securities. Proceeds of $1.4 million were received from the sale of assets and funeral homes.

*Net cash used in financing activities:*

For the nine months ending September 30, 2004 net cash used in financing activities was reduced to $2.7 million from $7.8 million for the nine months ending September 30, 2003. This $5.1 million reduction related primarily to reduced payments on senior debt as a result of reduced proceeds from dispositions and the fact that in 2003 we utilized cash reserves accumulated in prior years to reduce senior indebtedness.

Net cash used in financing activities was $9.2 million for 2003. Keystone borrowed $0.2 million to finance equipment, primarily autos. Cash of $8.1 million was used to make principle payments on our senior debt facility and $1.3 million was paid on obligations under agreements with former owners.

Net cash used in financing activities was $4.8 million for 2002. Keystone borrowed $0.1 million to finance equipment, primarily autos. Cash of $3.2 million was used to make principle payments on our senior debt facility and $1.8 million was paid on obligations under agreements with former owners.

**Consolidated Balance Sheets**

| | September 30, 2004 | December 31, 2003 | December 31, 2002 |
|---|---|---|---|
| Total assets | $142,568 | $145,523 | $151,256 |
| Total long-term liabilities[1] | $ 36,842 | $ 39,515 | $117,911 |

(1) Excludes $77.1 million of senior debt reclassified to current debt as of September 30, 2004 and December 31, 2003, respectively.

*Total Assets*

Total assets decreased approximately $3.0 million from December 31, 2003 to September 30, 2004. This can be primarily attributed to the disposition of a funeral home in July that had total assets of $3.1 million.

Total assets decreased approximately $5.7 million from December 31, 2002 to December 31, 2003. The primary reason for the decrease can be attributed to the dispositions made in 2003 that accounted for $4.2 million in total assets. Additionally, cash decreased $1.8 million during the year as discussed under "Liquidity and Capital Resources".

*Total Long-term Liabilities*

Total long-term liabilities decreased $2.7 million from December 31, 2003 to September 30, 2004. A disposition completed in 2004 resulted in the buyer assuming $1.4 million of long-term liabilities. The remaining $1.3 million represents the amount paid down on obligations under agreements with former owners.

Total Long-term Liabilities decreased $78.4 million from December 31, 2002 to December 31, 2003. The difference represents the reclassification of long-term debt on the senior facility to current debt.

**Capital Expenditures**

Capital expenditures have historically been primarily related to "maintenance capital expenditures" including the replacement of furnishings, autos and routine maintenance to existing building structures and the surrounding landscape.

| | Year Ended December 31 | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (U.S. dollars in thousands) | | |
| Capital Expenditures | $1,549 | $1,470 | $1,083 |

In certain circumstances, we also expend funds for items related to the acquisition of new equipment or businesses, expansion of existing infrastructure (*i.e.*, expansion of existing building facilities and/or addition of new facilities and other capital improvements), which are intended to increase productivity and cash flows, enhance margins and/or increase capacity. We will continue to consider such growth capital expenditures based on the economic merit of each project and the availability of funds.

### Commitments and Contractual Obligations

Our contractual obligations and commitments principally include obligations associated with our outstanding indebtedness, lease obligations, and former owner obligations in the form of non-competes and notes.

*Senior Indebtedness*

The current senior credit facility was established in 1997 and expanded in 1998 to accommodate additional acquisition activity. The remaining principal on this facility of $75.5 million at September 30, 2004 was due on January 31, 2004. In connection with this offering, Keystone will use the proceeds to, in part, retire all existing senior indebtedness and to establish and fund a restricted account to pay the former owner obligations of both Hamilton and Keystone. See "Use of Proceeds". Management believes Keystone will be able to successfully refinance or extend the revolver and term loan of such senior credit facility should the offering not be completed as intended. Keystone consolidated financial statements included elsewhere in the prospectus do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should Keystone be unable to continue as a going concern. See "Use of Proceeds".

We have no off-balance sheet debt or similar obligations other than the operating leases noted below.

| | Maturities | | | | | | |
|---|---|---|---|---|---|---|---|
| | | | Balance at December 31, | | | | |
| | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | Thereafter |
| Term loan | $77,056 | $77,056 | $ — | $ — | $ — | $ — | $ — |
| Obligations with former owners | 10,196 | 1,608 | 2,011 | 1,515 | 1,549 | 1,334 | 2,179 |
| Other obligations | 450 | 129 | 128 | 109 | 70 | 14 | — |
| | $87,702 | $78,793 | $2,139 | $1,624 | $1,619 | $1,348 | $2,179 |

The annual payments for operating leases (which are primarily for funeral home facilities, equipment and vehicles) at December 31, 2003 are as follows:

| | |
|---|---|
| 2004 | $ 981,314 |
| 2005 | 738,395 |
| 2006 | 656,956 |
| 2007 | 522,483 |
| 2008 | 446,237 |
| Thereafter | 616,694 |
| | $3,962,079 |

The leases for certain funeral home facilities contain contingent rental provisions based upon revenues of the related firms to be adjusted annually. The base revenue for these funeral homes did not exceed the contingent provisions; accordingly, no contingent rental has been recorded as of September 30, 2004, or December 31, 2003, 2002 or 2001.

Total rental expense for operating leases for the nine-months ended September 30, 2004 and the years ended December 31, 2003, 2002 and 2001, was $982,013, $1,224,182, $1,253,243 and $1,231,958, respectively.

### Related Party Transactions

Certain members of management, as part of their senior management agreements, have agreed to purchase 150 shares of Class B common stock and have signed promissory notes totaling $328,520 for the agreed purchase price. The stock purchased in January 1997 under these agreements vested 20% at the signing of the notes and

20% per year thereafter. The notes, originally scheduled for maturity on December 31, 2001, bear interest at 8% (payable quarterly) and are secured by the related stock. During 2002, Keystone extended these notes through December 31, 2004.

**Forward Looking Statements**

Certain statements in this management's discussion and analysis are "forward-looking statements", which reflect the expectations of management regarding the Issuer's and Keystone's future growth, results of operations, performance and business prospects and opportunities. These forward-looking statements reflect Keystone's current expectations regarding future events and operating performance and speak only as of the date of this prospectus. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not or the times at or by which such performance or results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements, including, but not limited to, the factors discussed under "Risk Factors". Although the forward-looking statements contained in this prospectus are based upon what the Issuer and Keystone believe to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. These forward-looking statements are made as of the date of this prospectus and the Issuer and Keystone assume no obligation to update or revise them to reflect new events or circumstances.

**Critical Accounting Policies**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Some of the estimates and assumptions management is required to make relate to matters that are inherently uncertain as they pertain to future events. Management bases these estimates on historical experience and on various other assumptions that we believe to be reasonable and appropriate. Actual results may differ significantly from these estimates. The following is a description of our significant critical accounting policies.

*Revenue Recognition*

The vast majority of our revenue is generated by at-need funeral sales. Funeral revenue, which includes funeral merchandise and services, is recognized when the funeral service and related merchandise is provided.

Cemetery property sales are recorded in accordance with real estate revenue recognition guidelines or when 10% of the sales price has been collected. Cemetery merchandise and service revenues are recognized when the products and services have been delivered.

*Credit Risk*

Keystone grants customers credit in the normal course of business. Procedures exist to secure accounts that include confirming a source of third-party payment such as insurance assignment, estate, group life policy or maturing pre-need trust. Keystone establishes an allowance on case-by-case basis focusing on those accounts that have not been secured and for which payments have not been received in the past 90 days. Historically, bad debts have not been significant in relation to the volume of revenues. Keystone charges interest on past due receivables in certain circumstances.

Prearranged funeral contracts do not subject Keystone to collection risk because contracts may be cancelled due to nonpayment before services are rendered.

*Funeral Accounting*

Keystone sells prearranged funeral services, whereby a customer contractually agrees to the terms of a funeral to be performed in the future. Keystone sells these price-guaranteed, prearranged funeral contracts through various programs providing for future funeral services at prices prevailing when the agreement is signed.

Prearranged funeral contracts are generally funded either through trusts established by the customer or through life insurance policies purchased by the customer and issued by third party insurers.

Keystone defers costs to obtain new prearranged funeral contracts until the related sales are recognized as revenue. Deferred obtaining costs include only those costs that vary with and are directly related to the acquisition of new prearranged contracts. Deferred obtaining costs are netted against deferred revenue on the balance sheet and are amortized based upon expected mortality of the contractholder.

Amounts paid by the customer pursuant to the prearranged funeral contracts are recognized as funeral service revenue at the time the funeral is performed. Trust earnings and increasing insurance benefits are recognized as funeral service revenues when the funeral service is performed and are intended to cover increases in the cost of providing a price-guaranteed funeral service. Prearranged funeral contract assets consist of receivables from customers, trusts or other, non-insurance accounts that will be received upon delivery of prearranged merchandise and services. Prearranged funeral contracts funded through life insurance policies purchased by the customer and issued by third party insurers are not reflected in the financial statements but are disclosed in the notes to Keystone's financial statements included elsewhere in the prospectus.

The prearranged funeral contract revenue assets are recorded at fair value, less provisions for loss in respect of individual investments where market value is below cost and this decline appears to be other than temporary.

Amounts held in trust are refunded to the customer according to U.S. state law upon cancellation of the contract. Allowances for customer cancellations are recorded using an estimated cancellation rate based on historical experience.

*Goodwill*

Goodwill represents the excess of cost over fair value of net assets acquired in business combinations accounted for under the purchase method. We apply Section 3062 of the Canadian Institute of Chartered Accountants, *Goodwill and Other Intangible Assets* ("Section 3062"). Section 3062 addresses post-acquisition financial accounting and reporting for acquired goodwill and other intangible assets. Under this statement, goodwill and other intangible assets that have indefinite useful lives will not be amortized, but rather will be tested annually for impairment based on the specific guidance of Section 3062 unless other impairment indicators are present thereby necessitating an immediate review. The Company has performed the required goodwill impairment tests and determined that no impairment exists.

*Impairment of Long-Lived Assets*

Management continually evaluates whether events or circumstances have occurred that indicate that the remaining estimated useful lives of property and equipment may warrant revision or that the remaining balances may not be recoverable. If this review indicates that the assets will not be recoverable, as determined based on the undiscounted future cash flows from the use of the assets, the carrying value of the assets will be reduced to their estimated fair value.

*Income Taxes*

Income taxes have been computed utilizing the asset and liability approach. Deferred income tax assets and liabilities arise from differences between the tax basis of an asset or liability and its reported amount in the financial statements. Deferred tax balances are determined using tax rates expected to be in effect when the taxes will actually be paid or refunds received. A valuation allowance is recorded when the expected recognition of a deferred tax asset is not considered to be more likely than not. The recorded deferred income tax liability results from a difference between book and tax basis of certain intangible assets and buildings and other fixed assets.

**Quantitative and Qualitative Disclosures About Market Risk**

In the normal course of business, we are exposed to market risks arising from adverse changes in interest rates. Market risk is defined for these purposes as the potential change in the fair market value of financial assets and liabilities resulting from an adverse movement in interest rates. As of September 30, 2004 our material variable rate borrowings included our outstanding senior credit facility. A 100 basis point increase in interest rates, applied to these borrowings as of September 30, 2004, would result in an annual increase in interest expense and a corresponding reduction in cashflow of approximately $0.8 million. We anticipate entering into a new interest rate hedge agreement for a portion of the term loan facility anticipated to be borrowed under the New Credit Facility.

In connection with this offering, Keystone will be exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar because the anticipated distributions from Keystone will be in U.S. dollars and the anticipated distributions from the Issuer will be paid in Canadian dollars. In order to minimize the impact of fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar, Keystone anticipates entering into a multi-year hedging arrangement, and to review its hedging policy on an on going basis.

**Recent Accounting Pronouncements**

In 2003, the Canadian Accounting Standards Board ("AcSB") approved Accounting Guideline 15 Consolidation of Variable Interest Entities. The guideline will be effective for the fiscal year ended December 31, 2005. Keystone is in the process of determining the effects of this guideline on its future financial statements, however, it is expected that the guideline will require consolidation of its funeral pre-need trust funds. Since Keystone's customers are the legal beneficiaries of the pre-need trust funds and Keystone does not have a legal right to access the care funds, Keystone expects to recognize non-controlling interests in its financial statements. The expected accounting changes associated with this guideline will principally affect classifications within the financial statements and will not affect cash flows or the manner in which Keystone recognizes and reports revenue or net income. The guideline also will not change the legal relationships among the trust funds, Keystone and its customers.

**Continuous Disclosure**

The Issuer has provided an undertaking to the security regulatory authorities in each of the provinces and territories of Canada that: (i) it will treat its subsidiaries as wholly-owned subsidiaries; however, if GAAP prohibits the consolidation of financial information of the subsidiaries and the Issuer and a subsidiary (including any of its significant business interests) is a significant asset of the Issuer, the Issuer will provide investors with separate financial statements for such entity; (ii) it will obtain a commitment from its subsidiaries to comply with Ontario Securities Commission Rule 61-501 — *Insider Bids, Issuer Bids, Going Private Transactions and Related Party Transactions* and Autorité des marchés financiers Q-27 — *Mesures de protection des porteurs minoritaires à l'occasion de certaines opérations*, as applicable; (iii) it will undertake to take appropriate measures to require persons who would be an insider of its subsidiaries (or operating entities) if the subsidiary (or operating entity) were a reporting issuer to file insider reports concerning trades in the Issuer's securities, subject to application of the exemptions to insider reporting provided under National Instrument 55-101 — *Exemption From Certain Insider Reporting Requirements;* and (iv) it will certify, on an annual basis, that it has complied with this undertaking.

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS OF HAMILTON

*Information in this management's discussion and analysis of the financial condition and results of operations of Hamilton is supplemental to, and should be read in conjunction with, the consolidated financial statements of Hamilton included in this prospectus. It also contains forward-looking statements, which are subject to a variety of factors that could cause actual results to differ materially from those contemplated by these statements. See "Forward-Looking Statements". Some of the factors that could cause results or events to differ from current expectations include, but are not limited to, the factors described under "Risk Factors". Hamilton's financial statements included in this prospectus have been prepared in accordance with Canadian GAAP.*

*The information provided in this management's discussion and analysis of the financial condition and results of operations of Hamilton relates to Hamilton as a stand-alone entity, prior to the acquisition of certain of its subsidiaries by Keystone on the closing of this offering.*

**Overview**

Hamilton owns and operates funeral homes, which account for approximately 98% of revenues, and cemeteries, which account for approximately 2% of revenues. Funeral homes are principally a service business that provide funeral services (burial and cremation) and sell related merchandise, such as caskets, outer enclosures and urns. Cemeteries are primarily a sales business that sells real estate (grave sites and mausoleums) and related merchandise such as markers, memorials, and outer enclosures. As of September 30, 2004, Hamilton operated 80 funeral homes and seven cemeteries in 12 states within the United States. Substantially all administrative activities are conducted from the corporate office in San Diego, California.

Factors affecting Hamilton operating results include the number of deaths in the markets served; whether its locations gain or lose market share relative to competitors in the markets served; the price at which services and merchandise are sold; and the cost of providing services, primarily the salaries and benefits expense related to professional and support staff, and the cost of merchandise. The average revenue per contract is influenced by the mix of traditional and cremation services because the average cremation service revenue is significantly less than the average revenue earned from a traditional burial service. Although cremations typically generate profit margin percentages higher than those of traditional burial services, the total revenue and margin dollars of cremations are lower. Funeral homes have a high fixed cost structure. Thus, small changes in revenues, up or down, normally cause proportionally greater changes in profitability.

*Business Disposals*

During 2004 and 2003 Hamilton disposed of a number of funeral homes that were purchased by former owners or the management team of the funeral homes for multiples of cash flow at or above market parameters. The operating results of these businesses are reported as discontinued operations as more fully disclosed in note 3 of the financial statements. Discussions which ultimately led to the sale of each of the following dispositions were in each case initiated by the acquirer. Hamilton considered the current business prospects, competition and sales price when considering the disposition of each business. Hamilton does not currently have any additional businesses targeted for sale.

In September 2004 Hamilton, in one transaction, disposed of seven funeral homes in the greater Milwaukee area. The net proceeds of $3.0 million were required to be applied to the senior secured loan indebtedness.

During 2003, in two separate transactions, Hamilton disposed of six funeral homes in two markets comprising three Michigan funeral homes and three Wisconsin funeral homes. The combined net proceeds of approximately $8.6 million from the sales were required to be applied to Hamilton's senior secured loan indebtedness.

During 2001, Hamilton disposed of two funeral homes in the greater Milwaukee area in one transaction. The net proceeds of $2.0 million were required to be applied to the senior secured loan indebtedness. Hamilton adopted the new requirements of Section 3475 of the Canadian Institute of Chartered Accountants, *Disposal of Long-lived Assets and Discontinued Operations*, to disposal activities initiated in 2003 and thereafter effective January 1, 2003. The section requires that the results related to business dispositions be reported as discontinued operations in the consolidated statements of operation. The 2001 disposition, being prior to the adoption date, could not be retroactively reclassified to discontinued operations, as Section 3475 does not allow retroactive application. To enhance analysis, normalized results of operations for the twelve months ended December 31, 2001 are presented below in addition to the audited year ended December 31, 2001. The normalized twelve months ended December 31, 2001 results of operations exclude the 2001 operating results related to the 2001 disposition from continuing operations to facilitate comparison of the retained operations.

**Results of Operations**

The following is a discussion of Hamilton's results of operations for the nine month periods ended September 30, 2004 and 2003, twelve months ended December 31, 2001, 2002 and 2003, and same store twelve months ended December 31, 2001.

| | Nine months ended September 30, (unaudited) | | Years ended December 31, | | | |
|---|---|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 | 2001 | 2001 Normalized (unaudited) |
| | | | (U.S. dollars in thousands) | | | |
| Revenues | $27,564 | $27,999 | $38,026 | $40,211 | $39,337 | $38,607 |
| Location operating costs | 18,864 | 18,534 | 24,874 | 25,177 | 25,325 | 24,773 |
| Corporate, general and administrative expenses | 2,234 | 2,550 | 3,327 | 3,346 | 3,221 | 3,221 |
| Non-compete expenses | 809 | 977 | 1,329 | 1,312 | 1,388 | 1,341 |
| Consulting expenses | 283 | 411 | 506 | 494 | 572 | 550 |
| Depreciation and amortization | 1,465 | 1,448 | 1,984 | 1,881 | 1,998 | 1,957 |
| Goodwill amortization | — | — | — | — | 1,283 | 1,262 |
| Impairment of goodwill | — | — | — | — | 312 | 312 |
| Operating income | 3,909 | 4,079 | 6,006 | 8,001 | 5,238 | 5,191 |
| Other (income) expense: | | | | | | |
| Interest expense, payable in cash | 2,290 | 2,234 | 2,886 | 4,267 | 5,828 | 5,706 |
| Interest expense, payment-in-kind | 6,597 | 5,706 | 7,793 | 6,224 | 5,619 | 5,619 |
| Dividends on retractable preferred shares | 31 | 31 | 42 | 42 | 42 | 42 |
| Deferred loan costs amortization | 1,208 | 526 | 583 | 868 | 951 | 951 |
| Loan restructuring costs | 612 | 368 | 372 | 751 | — | — |
| (Gain) loss on sale of property | — | (159) | (161) | — | 157 | (129) |
| Income taxes | 381 | 364 | 485 | 1,537 | — | — |
| (Loss) from continuing operations | (7,210) | (4,991) | (5,994) | (5,688) | (7,359) | (6,998) |
| Income (loss) from discontinued operations | (1,170) | (101) | (191) | 822 | 414 | 53 |
| Net (loss) | $(8,380) | $(5,092) | $(6,185) | $(4,866) | $(6,945) | $(6,945) |

***Nine months ended September 30, 2004 compared to nine months ended September 30, 2003:***

*Revenues:*

Revenues for the nine months ended September 30, 2004 were $27.6 million compared to $28.0 million for the nine months ended September 30, 2003, a decline of $0.4 million, or 1.4%, primarily attributable to lower per case average as a result of a shift in case mix to cremation services, which carried an overall lower average than traditional burial cases. It is expected that the shift in case mix to cremation services will continue to steadily increase.

*Location operating costs:*

Location operating costs for the nine months ended September 30, 2004 were $18.9 million compared to $18.5 million in 2003, an increase of $0.4 million. The increased costs related primarily to the hiring of a national director of prearranged sales in an effort to increase pre-need funeral sales and enhance funeral home market share, increased promotional expense expended in an effort to increase market share, increased property and liability insurance expense due to insurance industry price increases to substantially all insurance holders and slightly higher maintenance costs due to unexpected maintenance needs. It is expected that maintenance costs will decrease in future periods. Property and liability insurance costs are expected to remain constant in the next policy period.

*Corporate, general and administrative expenses:*

Corporate, general and administrative expenses for the nine months ended September 30, 2004 were $2.2 million a decrease of $0.3 million from $2.5 million in the comparable nine months of 2003, due primarily to lower personnel costs related to a restructuring of corporate operational management resulting in the elimination of two management positions. It is expected that the reductions experienced in the corporate, general and administrative expenses will continue in future periods.

*Depreciation and amortization:*

Depreciation and amortization of property and equipment for the nine months ended September 30, 2004 and 2003 remained constant at $1.5 million

*Operating income:*

Operating income for the nine months ended September 30, 2004 was $3.9 million compared to $4.1 million for the first nine months of 2003 representing a decline of $0.2 million. The decline was primarily attributable to the aforementioned revenue decline and a slight increase in operating costs that were partially offset by lower corporate, general and administrative costs.

*Interest expense:*

Interest expense payable in cash for the nine month period ended September 30, 2004 increased $0.1 million compared to the nine month period ended September 30, 2003 from $2.2 million in 2003 to $2.3 million in 2004. While the senior secured and seller debt outstanding decreased by approximately $8.2 million since December 31, 2003, there was not a significant decline in interest expense in that the current period interest expense was negatively impacted by higher interest rates associated with senior secured lender debt interest rates instituted by the lenders related to the default and subsequent forbearance agreements. Payment in kind ("PIK") interest expense increased $0.9 million due to compounded interest on Hamilton's senior subordinated PIK notes and deferred cash interest and PIK interest related to the junior subordinated notes, class A subordinated notes and class B subordinated notes.

*Deferred loan costs amortization:*

Deferred loan cost amortization for the nine months ended September 30, 2004 were $1.2 million compared to $0.5 million in 2003, an increase of $0.7 million. The increased amortization is primarily attributable to the write-off of the deferred loan costs related to the default of the subordinated debt in September 2004.

*Loan restructuring costs:*

Loan restructuring costs for the nine months ended September 30, 2004 and 2003 were $0.6 million and $0.4 million, respectively. Since June 30, 2002, Hamilton has been in default of the requirements of the senior secured debt and subordinated debt credit agreements related to principal payment and covenant compliance. Hamilton's outstanding senior secured obligations pursuant to the credit agreement became due and payable in full on June 30, 2003. The loan restructuring costs represent legal fees, financial advisor and bank fees related to negotiations regarding the default and subsequent forbearance agreements which expired in September 2004.

*Income tax expense:*

Income tax expense for the nine months ended September 30, 2004 and 2003 remain constant at $0.4 million.

*Loss from continuing operations:*

Loss from continuing operations was $7.2 million for the nine month period ended September 30, 2004 compared to $5.0 million for the first nine months of 2003. The increase in the loss from continuing operations is primarily due to a $0.2 million decrease in operating income related to the decrease in revenues mentioned above, a $0.9 million increase in non-cash PIK interest expense, a $0.1 million increase in interest expense payable in cash and a $0.7 million increase in deferred loan costs reflecting the write off of the subordinated debt's deferred loan costs in conjunction with the aforementioned default of the related subordinated debt, partially offset by lower corporate general and administrative costs mentioned above.

***Year ended December 31, 2003 compared to year ended December 31, 2002:***

*Revenues:*

Revenues for 2003 were $38.0 million compared to $40.2 million in 2002 representing a decline of $2.2 million, or 5.4%, primarily attributable to a decline in the number of funeral cases, partially offset by improved funeral case averages. In 2002 Hamilton experienced a spike in the number of families serviced in its markets with 2003 death rates returning to more normal levels.

*Location operating costs:*

Location operating costs for 2003 were $24.9 million compared to $25.2 million in 2002 representing a decrease in costs of $0.3 million. The decrease in costs relates primarily to lower variable merchandise costs relative to the decreased revenue volume mentioned above, partially offset by increased property and liability insurance costs and slightly higher personnel costs resulting from normal annual wage increases.

*Corporate general and administrative expenses:*

Corporate general and administrative expenses for 2003 and 2002 were $3.3 million, with no appreciable change from year-to-year.

*Depreciation and amortization:*

Depreciation and amortization of property and equipment remained relatively constant at $2.0 million for 2003 compared to $1.9 million in 2002.

*Operating income:*

Operating income for 2003 was $6.0 million compared to $8.0 million in 2002, a decline of $2.0 million. The decline was primarily attributable to the aforementioned revenue decline and partially offset by a decrease in operating costs as previously mentioned.

*Interest expense:*

Interest expense payable in cash for 2003 of $2.9 million compared to $4.3 million for the prior year representing a decrease of $1.4 million. Interest expense declined as a result of lower variable interest rates tied to prime and LIBOR related to the senior debt facility during 2003, and due to an overall reduction in outstanding indebtedness as a result of the application of the net proceeds to senior debt related to the sale of facilities in 2003. Interest expense paid in cash also decreased due to the restriction from making payment of senior subordinated cash interest at June 30, 2002 and subsequent due to the senior secured debt facility default at June 30, 2002. The unpaid cash interest is included in the PIK interest expense effective June 30, 2002 and subsequent. PIK interest expense increased $1.6 million reflecting the deferred cash interest and compounding of interest on Hamilton's senior subordinated PIK notes and deferred cash interest and PIK interest related to the junior subordinated notes, class A subordinated notes and class B subordinated notes.

*Deferred loan costs amortization:*

Deferred loan cost amortization for 2003 were $0.6 million compared to $0.9 million in 2002, a decrease of $0.3 million. The decreased amortization related primarily to lower senior secured loan cost amortization in that the senior secured debt reached maturity at June 30, 2003, therefore the loan costs related to this debt was fully amortized.

*Loan restructuring costs*

Loan restructuring costs for 2003 were $0.4 million compared to $0.8 million in 2002, a decrease of $0.4 million. In 2002, Hamilton employed a consultant in conjunction with the 2002 senior secured debt forbearance agreement, at Hamilton's expense, to perform a review of Hamilton which resulted in the higher 2002 expense.

*Income tax expense:*

Hamilton recorded income tax expense of $0.5 million and $1.5 million in 2003 and 2002, respectively, in conjunction with the 2002 adoption of Section 3062, which resulted in the cessation of amortization of goodwill for financial statement purposes. Under Section 3062 goodwill is no longer amortized but is tested annually for impairment, or more frequently if events or changes in circumstances indicate that assets may be impaired. For purposes of determining the valuation allowance recorded for the years ended December 31, 2003 and 2002, the future tax liabilities related to the tax deductible goodwill are excluded because their reversal is indefinite and not identifiable, absent impairment of the carrying amount of the goodwill.

*Loss from continuing operations:*

Loss from continuing operations was $6.0 million for 2003 compared to $5.7 million for 2002. The $0.3 million increase in loss from continuing operations is primarily due to a $2.0 million decline in operating income related to the decline in revenues noted above and a $1.6 million increase in non-cash PIK interest expense, offset by a $1.4 million decrease in interest expense payable in cash, a $1.0 million decrease in income taxes and decreases in deferred loan costs and loan restructuring costs.

***Year ended December 31, 2002 compared to year ended December 31, 2001:***

As is mentioned above, in 2001 Hamilton made a disposition prior to the adoption date of Section 3475, and therefore the results of operations for the operations disposed could not be reclassified to discontinued operations. To enhance analysis, comments on twelve months ended December 31, 2001 unaudited normalized results are presented below in addition to audited December 31, 2001 financial results.

*Revenues:*

Revenue for 2002 were $40.2 million compared to $39.3 million in 2001 representing an increase of $0.9 million. Normalized revenues for 2002 were $40.2 million compared to $38.6 million in 2001 representing an increase of $1.6 million, or 4.1%, primarily attributable to an increase in the number of cases performed and an increase in funeral case averages.

*Location operating costs:*

Location operating costs for 2002 were $25.2 million compared to $25.3 million in 2001, a decrease of $0.1 million. Normalized location operating costs for 2002 were $25.2 million compared to $24.8 million in 2001, an increase of $0.4 million. The increase in costs relates primarily to higher variable merchandise costs related to the increased revenue volume mentioned above and increased property and liability insurance costs.

*Corporate, general and administrative expenses:*

Corporate, general and administrative expenses for 2002 were $3.3 million compared to $3.2 million in 2001 representing an increase of $0.1 million, attributable to annual wage increases, increased workers' compensation insurance expense and earned management incentive bonuses.

*Depreciation and amortization:*

Depreciation and amortization of property and equipment remained relatively constant at $1.9 million for 2002 as compared to $2.0 million in 2001.

*Goodwill amortization:*

As a result of the adoption in 2002 of Section 3062, resulting in the cessation of amortization of goodwill for financial statement purposes, there was no amortization of goodwill for 2002, compared to $1.3 million in 2001.

*Operating income:*

Operating income for 2002 was $8.0 million compared to $5.2 million for 2001, an increase of $2.8 million. The increase in operating income was primarily attributable to the aforementioned revenue increase and the 2002 cessation of goodwill amortization, partially offset by the aforementioned increase in the operating costs.

*Interest expense:*

Interest expense payable in cash for 2002 of $4.3 million compared to $5.8 million for 2001 representing a decrease of $1.5 million. Interest expense decreased as a result of lower interest rates related to the senior debt facility and a reduction in outstanding indebtedness. Interest expense paid in cash also decreased due to the non payment of senior subordinated cash interest at June 30, 2002 and subsequent periods. PIK interest expense increased $0.6 million resulting from the compounding of interest on Hamilton's senior subordinated PIK notes and deferred cash interest and PIK interest related to the junior subordinated notes, class A subordinated notes and class B subordinated notes.

*Deferred loan costs:*

Deferred loan costs remained relatively constant at $0.9 million in 2002 compared to $1.0 million in 2001.

*Loan restructuring costs:*

2002 loan restructuring costs were $0.8 million related to the June 30, 2002 covenant and principal payment default relative to the requirements of the senior secured indebtedness that required the loan to be restructured. There were no loan defaults in 2001 requiring restructuring and accordingly no loan restructuring costs were incurred 2001.

*Income tax expense:*

Hamilton recorded income tax expense of $1.5 million in 2002 in conjunction with the 2002 adoption of Section 3062, which resulted in the cessation of amortization of goodwill for financial statement purposes. No income taxes were recorded in 2001 because future tax liabilities arising from goodwill were considered in the allowance before the adoption of Section 3062.

**Consolidated Balance Sheets**

| | September 30, 2004 | December 31, 2003 | December 31, 2002 |
|---|---|---|---|
| | (U.S. dollars in thousands) | | |
| Total assets | $116,586 | $129,336 | $136,320 |
| Total long-term liabilities | $ 28,898 | $ 31,264 | $ 30,701 |

*Total assets*

Total assets decreased approximately $12.8 million from December 31, 2003 to September 30, 2004. The decrease is primarily attributable to the 2004 disposition of funeral homes with assets of approximately $7.0 million, a reduction of cash of approximately $4.0 million, primarily resulting from the payment of senior secured debt in conjunction with the 2004 forbearance agreement, a $0.7 million write-off of deferred loan costs related to the subordinated debt default and a reduction in accounts receivables of $0.7 million.

Total assets decreased approximately $7.0 million from 2002 to 2003. The decrease is primarily attributable to the 2003 disposition of funeral homes that had assets of approximately $11.1 million, a reduction in receivables of $0.8 million, partially offset by a $3.6 million increase in cash and an increase of $0.5 million in preneed cemetery contracts.

*Total long-term liabilities*

Total long-term liabilities decreased approximately $2.4 million from December 31, 2003 to September 30, 2004. The decrease is primarily attributable to the reduction of deferred prearranged funeral contract revenues related to the 2004 disposition of funeral homes, a $0.5 million reduction in long-term debt related to normal debt amortization, partially offset by increases in future income taxes and deferred preneed cemetery contract revenues.

Total long-term liabilities increased approximately $0.6 million from 2002 to 2003. The increase is attributable to a $0.5 million increase in deferred prearranged funeral contract revenues and a $0.5 million increase in future income taxes, partially offset by $0.4 million reduction in long-term debt related to normal debt amortization.

**Liquidity and Capital Resources**

Hamilton's total debt at September 30, 2004 of $132.1 million consisted of long-term debt of $51.4 million and subordinated unsecured notes payable and deferred interest of $80.7 million. As disclosed in Note 7 to Hamilton's consolidated financial statements, except for notes payable to former owners of the acquired businesses of $2.7 million and the notes payable to a bank of $0.2 million, all debt is in default and is reflected in current liabilities.

Hamilton's outstanding obligations pursuant to the Senior Secured Credit Agreement became due and payable June 30, 2003. Effective June 4, 2004 Hamilton entered into forbearance agreements with Hamilton's senior secured lenders and subordinated debt holders. The forbearance agreements provided for a period of forbearance until November 1, 2004, providing Hamilton met certain benchmarks as provided for in the agreement. On September 28, 2004 Hamilton was advised by the agent bank for the senior secured lenders that Hamilton was in default of the Forbearance Agreement and that the forbearance period had terminated. As a condition of the default, interest is now payable at the prime rate plus 300 basis points plus an additional default rate of interest of 200 basis points.

Hamilton, with the concurrence and assistance of certain of its subordinated debt holders, is pursuing the merger with Keystone, which, if successful, would provide funds sufficient to satisfy Hamilton's obligations under its senior secured credit facility. If this merger is successfully completed, it is anticipated the funds available to repay the subordinated debt holders, which are not being assumed by Keystone, would be substantially less than the carrying value of debt and this would indicate that goodwill would be impaired and this impairment charge to Hamilton is estimated to be in excess of $10 million.

At September 30, 2004 Hamilton had cash and cash equivalent balances available to it of $2.9 million. Historically, Hamilton's net cash provided by operations has been adequate to meet its operating needs, including required principal and interest payments on seller debt and interest payments on its senior secured debt. However, Hamilton has not generated adequate cash flow from operations to meet required principal payments on its senior secured debt or pay interest on its senior subordinated debt.

Future contractual obligations are as follows:

| Contractual Obligations | Payments Due by Period as of December 31, 2003 | | | | |
|---|---|---|---|---|---|
| | Total | Less than one year | 1-3 years | 4-5 years | After 5 years |
| | (U.S dollars in thousands) | | | | |
| Senior secured credit facility | $ 54,133 | $ 54,133 | $ — | $ — | $ — |
| Secured note payable to Banks | 242 | 15 | 34 | 41 | 152 |
| Unsecured seller debt | 5,427 | 2,798 | 1,050 | 1,128 | 451 |
| Senior subordinated notes | 29,440 | 29,440 | — | — | — |
| Subordinated notes | 44,748 | 44,748 | — | — | — |
| Retractable preferred stock | 852 | 852 | — | — | — |
| Non-compete and consulting agreements | 5,049 | 1,510 | 2,294 | 1,162 | 83 |
| Employment agreements | 702 | 410 | 292 | — | — |
| Operating leases | 6,277 | 1,285 | 1,848 | 1,239 | 1,905 |
| Total contractual obligations | $146,870 | $135,191 | $5,518 | $3,570 | $2,591 |

Capital expenditures were $1.6 million, $1.4 million and $1.1 million for 2003, 2002 and 2001, respectively. Capital expenditures include those required to maintain and upgrade existing infrastructure, including the replacement of furnishings, autos and routine maintenance to existing building structures and the surrounding landscape. Capital expenditures have averaged $1.4 million over the past three years, reflecting an approximation of ongoing annual maintenance capital expenditures.

**Critical Accounting Policies and Estimates**

The preparation of the consolidated financial statements requires the use of estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an on-going basis, estimates and judgments are evaluated; including those related to revenue recognition, realization of accounts receivable, intangible assets, property and equipment and future tax assets. Estimates are based on historical experience, third party data and assumptions believed to be reasonable under the circumstances. The results of these considerations form the basis for making judgments about the amount and timing of revenues and expenses, the carrying value of assets and the recorded amounts of liabilities. Actual results may differ from these estimates and such estimates may change if the underlying conditions or assumptions change. Historical performance should not be viewed as indicative of future performance, as there can be no assurance the margins, operating income and net earnings as a percentage of revenues will be sustained consistently from year to year.

Significant accounting policies are more fully described in Note 1 to Hamilton's consolidated financial statements included in this prospectus. It is believed the following critical accounting policies affect the more significant judgments and estimates used in the preparation of Hamilton's consolidated financial statements.

*Goodwill*

The excess of the purchase price over the fair value of identifiable net assets of businesses acquired in transactions accounted for as a business combination is included in the consolidated financial statements as "Goodwill." Historically management has determined fair values used in such purchase price allocations. On January 1, 2002, Hamilton adopted Section 3062 of the Canadian Institute of Chartered Accountants, Goodwill and Other Intangible Assets. Under Section 3062 goodwill is no longer amortized but is tested annually for impairment, or more frequently if events or changes in circumstances indicate that the assets might be impaired. In assessing the recoverability of goodwill, management must make assumptions about the estimated future cash flows and other factors to determine the fair value of its reporting unit.

The annual goodwill impairment evaluation includes a comparison of the carrying value of the reporting unit (including goodwill) to that reporting unit's fair value. If the reporting unit's estimated fair value exceeds the reporting unit's carrying value, no impairment of goodwill exists. If the fair value of the reporting unit does not exceed the unit's carrying value, then an additional analysis is performed to allocate the fair value of the reporting unit to all of the assets and liabilities of that unit as if that unit had been acquired in a business combination and the fair value of the unit was the purchase price. If the excess of the fair value of the reporting unit over the fair value of the identifiable assets and liabilities is less than the carrying value of the unit's goodwill, an impairment charge is recorded for the difference.

In determining the fair market value of businesses acquired by Hamilton, a critical factor, amongst others, in determining fair market value, is the amount of cash flow that the acquired business can contribute to Hamilton. In similar fashion, in determining the value of the goodwill associated with the businesses disposed by Hamilton, management assesses the proportionate amount of cash flow contributed by the sold businesses compared to the cash flow contributed by all of its businesses in making a determination of the goodwill associated with the sold business.

Hamilton completed an assessment of its operations and has determined that it currently operates as a single operating segment with one reporting unit. The carrying value of the reporting unit is determined by allocating all applicable assets (including goodwill) and liabilities, which in a single reporting unit entity like Hamilton, is the stockholders' deficit. In order to assess impairment of goodwill, Hamilton determined that the fair value of the reporting unit is in excess of its carrying value; therefore, no impairment charge has been recorded in the consolidated statement of operations for 2003 and 2002.

*Funeral and Cemetery Operations*

Sales of funeral merchandise and services are recorded when the funeral service is performed. Pre-need cemetery interment right sales of constructed cemetery burial property are deferred until a minimum percentage of the sales price has been collected, generally 10%. Costs related to the sales of interment rights, which include property and other costs related to cemetery development activities, are charged to operations using the specific identification method in the period in which the sale of the interment right is recognized as revenue. Revenue from the sales of cemetery merchandise and services are recognized in the period in which the merchandise is delivered or the service is performed.

Allowances for customer cancellations, refunds and bad debts are provided at the date of sale based on Hamilton's historical experience. In addition, delinquency rates are monitored and additional bad debt and cancellation reserves are provided when warranted. When pre-need funeral contracts are secured by third-party life insurance policies, commissions are earned from the sale of the policies. Obtaining costs, which represent costs directly related to the acquisition of new pre-need cemetery and pre-arranged funeral business, incurred pursuant to the sale of new pre-arranged funeral and cemetery business are expensed when the related deferred prearranged contract revenues are recognized.

Hamilton sells price guaranteed prearranged funeral contracts which are funded by insurance contracts. Hamilton primarily utilizes one insurance provider nationally. Prior to the acquisition of Hamilton's locations, prior ownership sometimes utilized insurance companies other than Hamilton's national provider that provided products similar in nature to the product now offered by Hamilton. After acquisition the locations insurance funded prearranged funeral contract programs were converted to Hamilton's national preneed insurance provider. Policies in force with Hamilton's national provider currently approximates $40 million.

**Recent Accounting Pronouncements**

In 2003, the AcSB approved Accounting Guideline 15 Consolidation of Variable Interest Entities. The guideline will be effective in fiscal 2005. While still in the process of determining the effects of this guideline on its future financial statements, it is expected that the guideline will require consolidation of its funeral pre-need trust funds. Since Hamilton's customers are the legal beneficiaries of the pre-need trust funds and Hamilton does not have a legal right to access the care funds, Hamilton will recognize non-controlling interests in its financial statements. The accounting changes associated with this guideline principally affect classifications within the financial statements and do not affect cash flow or the manner in which Hamilton recognizes and reports revenue or net income. The guideline also does not change the legal relationships among the trust funds, Hamilton and its customers.

### Seasonality

Hamilton's business can be affected by seasonal fluctuations in the death rate. Generally, the rate is higher during the winter months because the incidences of deaths from influenza and pneumonia are higher during this period than other periods of the year.

### Inflation

Inflation has not had a significant impact on the results of operations of Hamilton.

### Forward-Looking Statements

In addition to historical information, management's discussion and analysis contains forward-looking statements. These statements include any projections of earnings, revenue, asset sales, cash flow, debt levels or other financial items; any statements of the plans, strategies and objectives of management for future operation; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing. Forward-looking statements may include the words "may", "will", "estimate", "intend", "believe", "expect", "project", "forecast", "plan", "anticipate" and other similar words.

These forward-looking statements reflect Hamilton's current expectations regarding future events and operating performance and speak only as of the date of this prospectus. Forward-looking statements involve significant risk and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not at the times at or by which such performance or results will be achieved. These forward-looking statements are made as of the date of this prospectus and Hamilton assumes no obligation to update or revise them to reflect events or circumstances.

## DIRECTORS, OFFICERS AND MANAGEMENT

### Keystone North America and Keystone ULC

*Directors of Keystone North America*

Keystone North America will have a minimum of three and a maximum of 20 directors. Initially, the Keystone North America board will consist of five directors. The initial directors of Keystone North America are Robert H. Byrne, Frank Cerrone, Lorie Waisberg, Robert G. Horn and George Sperzel. Frank Cerrone, Robert H. Byrne and Lorie Waisberg are unrelated to Keystone North America. Robert G. Horn, the Chief Executive Officer of Keystone, will initially be the chairman of the Keystone North America board and Lorie Waisberg will serve as its independent lead director, in which capacity he will be responsible for reviewing and commenting on the agenda for directors' meetings, acting as a liaison between the independent directors and management, leading independent sessions of the independent directors and chairing Keystone's annual meeting.

The term of office for each of the directors will expire at the time of the next annual meeting of shareholders of Keystone North America. Directors will be elected at each annual meeting of shareholders of Keystone North America; however, the articles of Keystone North America will provide that the Chief Executive Officer of Keystone North America shall be a member of the board of directors. A director may be removed by a resolution passed by a majority of the shareholders or may resign. The vacancy created by the removal of a director must be filled at the shareholder meeting at which he or she was removed. A vacancy not so filled at a shareholder meeting, or created by the resignation of a director, may be filled by a quorum of the remaining directors. A quorum for meetings of directors is a majority of the directors, provided that a majority of directors present (or one director, where a quorum is two directors) must be residents of Canada. If there is no quorum of directors, a special shareholder meeting must be called to fill vacancies.

The directors will supervise the activities and manage the affairs of Keystone North America, including acting for, voting on behalf of and representing Keystone North America as a holder of common shares in Keystone.

*Governance of Keystone North America*

In lieu of a corporate governance and compensation committee, the directors will be directly responsible for developing Keystone North America's approach to governance issues, filling vacancies among the directors and periodically reviewing the composition and effectiveness of the directors and the contribution and compensation of individual directors.

*Audit Committee*

Keystone North America will have an audit committee that will be comprised of a minimum of three directors. All of the members of the audit committee shall be unrelated and independent (for regulatory purposes) directors. Initially, the audit committee will be comprised of Robert H. Byrne, Frank Cerrone and Lorie Waisberg (Chair). The audit committee will be responsible for the oversight and supervision of the accounting and financial reporting practices and procedures of Keystone North America, the adequacy of internal accounting controls and procedures, and the quality and integrity of financial statements of Keystone North America. The independent auditors of Keystone North America will report directly to the audit committee. In addition, the audit committee will be responsible for directing the auditors' examination of specific areas and for recommending to the board of directors the selection of independent auditors of Keystone North America.

*Disclosure*

The board of directors will also be responsible for adopting and periodically reviewing and updating the written disclosure policy for Keystone North America and its subsidiaries. This policy will, among other things:

- articulate the legal obligations of Keystone North America, its affiliates and their respective directors, officers and employees with respect to confidential information;
- identify spokespersons of Keystone North America who are the only persons authorized to communicate with third parties such as analysts, media and investors;
- provide guidelines on the disclosure of forward-looking information;
- require advance review by senior executives of any selective disclosure of financial information to ensure the information is not material, to prevent the selective disclosure of material information, and to ensure that if selective disclosure does occur, a news release is issued immediately; and
- establish "black-out" periods immediately prior to and following the disclosure of quarterly and annual financial results and immediately prior to the disclosure of certain material changes, during which periods Keystone North America, its subsidiaries and its directors, managers, officers, employees and consultants, may not purchase or sell IPSs, Common Shares or Subordinated Notes or other securities of Keystone North America or its subsidiaries (including securities exchangeable for or convertible into IPSs, Common Shares or Subordinated Notes).

*Remuneration of the Directors*

Initial compensation for non-management directors of Keystone North America will be C$25,000 per year. The lead director will initially receive an additional C$10,000 per year and the chair of the audit committee will receive an additional C$5,000 per year. Directors will receive C$1,200 per meeting for attending board or committee meetings in person and C$500 per meeting for attending meetings by phone. Directors will be reimbursed for out-of-pocket expenses for attending board and committee meetings. Directors will participate in the insurance and indemnification arrangements described below under "Insurance Coverage for Keystone North America and Related Entities and Indemnification".

*Management*

Keystone North America will have two officers. Robert G. Horn will be the Chief Executive Officer and Stephen M. Shaffer will be the Chief Financial Officer, and both will hold similar positions in Keystone. Primary responsibility for managerial and executive oversight of Keystone North America's subsidiaries will be delegated to and discharged by Keystone. See "Keystone — Directors and Executive Officers of Keystone."

*Keystone ULC*

The composition of the board of directors and audit committee of Keystone ULC will be identical to those of Keystone North America. The directors of Keystone North America that serve on the board of Keystone ULC will not receive any additional compensation for such services.

**Keystone**

***Directors and Executive Officers of Keystone***

Keystone will be governed in accordance with its constating documents and its securityholders' agreement, or "Securityholders' Agreement". Its board of directors initially will be comprised of seven individuals, a majority of whom are unrelated to Keystone and are U.S. residents. On closing of this offering, the board of directors of Keystone will be comprised as follows:

- five nominees of Keystone North America (Robert H. Byrne, Frank Cerrone, Lorie Waisberg, John Heen and Robert Pierce);
- one nominee of the Existing Investors and Existing Lenders (George Sperzel); and
- the Chief Executive Officer of Keystone (Robert G. Horn).

The Existing Investors' and Existing Lenders' representation on the Keystone board of directors will be adjusted if their retained interest is increased, reduced or diluted. The board of directors of Keystone will, subject to the provisions of the Securityholders' Agreement, have full power to manage the business and affairs of Keystone, to make all decisions regarding Keystone and to bind Keystone. See "Securityholders' Agreement."

The following table sets out the name, municipality of residence, age, position(s) with Keystone and principal occupation of the individuals who will be directors and/or executive officers of Keystone on closing of this offering.

| Name and Municipality of Residence | Age | Position(s) | Principal Occupation, if not with Keystone |
|---|---|---|---|
| ROBERT H. BYRNE<br>Oakville, Ontario | 45 | Director(1)(2) | Lawyer |
| FRANK CERRONE<br>King City, Ontario | 44 | Director(1)(2) | Senior Vice-President, General Counsel and Secretary of Retirement Residences Real Estate Investment Trust |
| LORIE WAISBERG<br>Toronto, Ontario | 63 | Director(1)(2) | Corporate Director |
| JOHN HEEN<br>Lincoln, Nebraska | 65 | Director | Lawyer |
| ROBERT L. PIERCE<br>Tallahassee, Florida | 58 | Director | President, Pierce CFO |
| GEORGE SPERZEL<br>Lake Forest, Illinois | 53 | Director | Principal, GTCR Golder Rauner LLC |
| ROBERT G. HORN<br>Tampa, Florida | 63 | Director, Chairman and Chief Executive Officer | — |
| STEPHEN M. SHAFFER<br>Tampa, Florida | 40 | Chief Financial Officer | — |
| JAMES D. PRICE<br>Tampa, Florida | 55 | Chief Operating Officer | — |
| STEVEN A. TIDWELL<br>Tampa, Florida | 42 | Executive Vice President | — |

(1) Member of compensation, nominating and corporate governance committee of Keystone.

(2) Member of audit committee of each of Keystone North America and Keystone.

On closing of the offering, the directors and senior officers of Keystone as a group will beneficially own, directly or indirectly, IPSs representing 0.04% of the issued and outstanding IPSs.

*Biographies*

**Robert H. Byrne** is a corporate lawyer specializing in mergers, acquisitions and corporate finance. He acts as general counsel to the Twin Rinks Group of Companies, a builder and operator of ice sports complexes, and Roam I.T. Inc., a North America-wide medical records software provider. In 1997, Mr. Byrne co-founded publicly traded Student Transportation of America ("STA"), now the fifth largest provider of school bus transportation services in North America, where he was Senior Vice President until 2001. Mr. Byrne has completed all 17 of STA's acquisitions. He previously served as Executive Vice President with STA's predecessor, Sightseeing Tours of America, Inc. From 1992 to 1996, Mr. Byrne was in-house counsel at NYSE-listed Laidlaw Inc., completing over 80 acquisitions for Laidlaw during that span. Prior to that time, he was a partner at the Toronto law firm of Morris/Rose/Ledgett. Mr. Byrne sits on the Board of Directors of the Oakville Blades of the Ontario Junior "A" Hockey League. After studying Economics at the undergraduate level, Mr. Byrne received his Bachelor of Laws degree from the University of Windsor in 1983.

**Frank Cerrone** is Senior Vice President, General Counsel and Secretary of Retirement Residences Real Estate Investment Trust and its subsidiaries and also serves as a director of Medical Facilities Corporation. Mr. Cerrone joined Retirement REIT on April 30, 2002 on its combination with CPL Long Term Care Real Estate Investment Trust. Mr. Cerrone was Vice-President, Legal Services of CPL REIT from October 1998 to April 30, 2002. Prior to joining CPL REIT, Mr. Cerrone was Vice-President, Corporate Counsel of Investment Planning Counsel of Canada Ltd. (now IPC Financial Network Inc.). Mr. Cerrone was a partner with Gordon Traub and practiced corporate/commercial law specializing in mergers and acquisitions and corporate finance of health care facilities from 1989 to 1996.

**Lorie Waisberg** is also a director of Chemtrade Logistics Income Fund, Granby Industries Income Fund and Specialty Foods Group Income Fund. From August 2000 to October 2002, Mr. Waisberg served as Executive Vice President, Finance and Administration for Co-Steel Inc. Prior to August 2000, Lorie Waisberg was a partner at Goodmans LLP. Mr. Waisberg served as a director of McWatters Mining Inc. ("McWatters") from September 1997 to August 2004. McWatters sought protection under the *Companies Creditors Arrangement Act* ("CCAA") in February, 2001 and emerged from the protection of CCAA in April, 2002. On January 15, 2004, McWatters filed a notice of intention to make a proposal under the *Bankruptcy and Insolvency Act* and commenced disposing of its assets for the benefit of its creditors. On May 14, 2004, the TSX suspended the shares (and other listed securities) of McWatters from trading for failure to meet the continued listing requirements of the TSX. On May 26, 2004 the Ontario Securities Commission and the Autorité des marchés financiers (Quebec) issued cease trade orders against trading in the shares of McWatters by directors (including Mr. Waisberg), officers and other insiders of McWatters by reason of McWatters' failure to file audited financial statements for the year ended December 31, 2003 and interim financial statements for the three months ended March 31, 2004.

**John Heen** is a lawyer in private practise in Lincoln, Nebraska and has been for over 19 years. Mr. Heen concentrates in business law and has completed over 100 acquisitions and private and public financing transactions. In addition to his private legal practice, Mr. Heen was general counsel to Senior Technology Inc. between 1990 and 2002, a Lincoln, Nebraska manufacturer and distributor of alarm and call systems.

**Robert L. Pierce** is President of Pierce CFO, a company founded in 2003, that provides Chief Financial Officer and management services to funeral home and cemetery companies. Mr. Pierce co-founded Thomas-Pierce & Company in 1986, a company that provided brokerage services for $2 billion of cemetery and funeral home transactions. He acted as the company's Chief Financial Officer and Vice President from 1986 until his retirement in 1999, after which he continued to provide technical and valuation services to the company until 2003. Mr. Pierce was the Chief Financial Officer of Cem-a-Care of Florida, et al from 1979 until 1985, a company with seventeen cemeteries and funeral homes. Prior to that, Mr. Pierce practiced as a Certified Public Accountant with McMillan Unruh, Koehner & Pierce from 1968 to 1979. Mr. Pierce is a 1968 graduate of Florida State University with a degree in accounting and business.

**George Sperzel** is currently a principal with GTCR Golder Rauner LLC. He previously served as Senior Vice President and Chief Financial Officer of Alliant Exchange from 2000 to 2002, Chief Financial Officer of Kao America Inc. and its subsidiary the Andrew Jergens Company from 1993 to 2000. Mr. Sperzel also spent sixteen years with the General Electric Company from 1977 to 1993 in various senior financial positions, and graduated with honors from the University of Louisville with a BS in Management. Mr. Sperzel serves on the board of directors of several companies, including American Sanitary Incorporated, Cardinal Logistics Management, Inc., Synagro Technologies, Inc. and Student Transportation of America, Inc.

**Robert G. Horn** is a co-founder and the Chief Executive Officer of Keystone. Mr. Horn has 43 years of industry experience. Mr. Horn was an organizer, Partner and Chief Operating Officer of Prime Succession, Inc. from its inception until the sale of the company in 1996. Prior to Prime Succession, Mr. Horn was Executive Vice President of Pierce Brothers Holding Company, a Los Angeles based funeral home consolidator acquired by Service Corporation International, or "SCI". He was an organizer and served as Vice President for 16 years at International Funeral Services, Industries, or "IFS", the first publicly held, multi-state consolidator of funeral homes and cemeteries. He had brief experience with SCI following its merger with IFS in 1981. He began his career with a small family-owned funeral home, which was subsequently sold to IFS. Mr. Horn currently serves as a Trustee and is the Chair Elect of The National Funeral Service Foundation, is a member of the Death Care Management Council, an instructor at the ICFA Summer Executive program at Memphis University and is a Clavigerii Society Member of Loyola Marymount University, Los Angeles.

**Stephen M. Shaffer** is a co-founder and the Chief Financial Officer of Keystone. Mr. Shaffer is a CPA. Mr. Shaffer has served as Chief Financial Officer of Keystone since its inception and was previously Corporate Controller of Prime Succession, Inc. prior to its sale. Mr. Shaffer was employed as an auditor with Ernst & Young in Indianapolis from 1987 to 1994. While working at Ernst & Young, Mr. Shaffer's audit clients included two cemetery and funeral consolidation companies, Gibraltar Mausoleum Corporation and Prime Succession (inception of Prime until he joined in 1994). Mr. Shaffer graduated in 1987 from Indiana University School of Business, Bloomington, Indiana with BS in accounting.

**James D. Price** is a co-founder and the Chief Operating Officer of Keystone. Mr. Price has 37 years of industry experience. Mr. Price previously served as President and CEO of Bonny-Watson, a large Seattle based Funeral Home and Cemetary Company. He was a Southern Regional Vice President at Prime Succession, Inc. Mr. Price was a Regional Vice President for Service Corporation International. Before that, he was Operations Vice President at Pierce Brothers Holding Company. He also worked as an area manager at International Funeral Services, Industries and a local funeral home. Mr. Price is a third-generation funeral director. He is a graduate of the California College of Mortuary Science, Mira Costa College. He is a licensed Funeral Director and Embalmer in California and holds a National Board Certificate. Jim is a member of the National Funeral Directors Association, the Cremation Association of North America and the International Funeral and Cemetery Association.

**Steven A. Tidwell** is a co-founder and the Executive Vice President of Keystone. Mr. Tidwell has 24 years of industry experience including a focus on mergers and acquisitions and experience as a funeral director. He attended John A. Gupton College where he obtained an Associate of Arts in Mortuary Science. Mr. Tidwell is a licensed funeral director and embalmer and has his national certification. He was a Partner at Prime Succession, Inc. where he was Vice President of Corporate Development. Prior to Prime Succession, Mr. Tidwell was Regional Vice President covering 6 states with Thomas-Pierce & Company, a succession planning company. Mr. Tidwell was previously employed with Arlington Corporation, a funeral home consolidator and Woodlawn Funeral Home and Memorial Park. He is also a member of the NFDA and an active alumni of Sigma Chi Fraternity.

***Committees and Remuneration of the Board***

The board of directors of Keystone will have a compensation, nominating and corporate governance committee and an audit committee, which satisfy all regulatory guidelines that would apply if Keystone were a listed reporting issuer.

*Compensation, Nominating and Corporate Governance Committee.* The compensation, nominating and corporate governance committee will be comprised of, and shall not consist of fewer than, three directors (a majority of whom will be unrelated to Keystone North America and Keystone and one of whom will be nominated by the Existing Investors and Existing Lenders provided that they retain their right to nominate at least one director to the full board). Initially, the compensation, nominating and corporate governance committee will be comprised of Robert H. Byrne (Chair), Frank Cerrone and Lorie Waisberg. The committee will review and make recommendations to the directors concerning the appointment of officers of Keystone and the hiring of, compensation, benefits and termination of senior officers of Keystone. The committee will annually review the Chief Executive Officer's goals and objectives for the upcoming year and provide an appraisal of the Chief Executive Officer's performance. The committee will also make recommendations concerning the remuneration of directors. The committee will administer and make recommendations regarding the operation of any employee bonus or incentive plans, including the long-term incentive plan. The committee will also be responsible for developing Keystone's approach to corporate governance issues, advising the board on filling vacancies on the board and periodically reviewing the composition and effectiveness of the board and the contribution of individual directors, considering questions of management succession and considering and approving proposals by the directors to engage outside advisors on behalf of the directors of Keystone North America or Keystone.

*Audit Committee.* The audit committee will be comprised of, and shall not consist of fewer than, three directors, all of whom will be unrelated and independent (for regulatory purposes) of Keystone North America and Keystone and one of whom will be nominated by the Existing Investors and Existing Lenders provided that they retain their right to nominate at least one director of the full board. Initially the audit committee will be comprised of Lorie Waisberg (Chair), Robert Byrne and Frank Cerrone. The committee will assist Keystone directors in fulfilling their responsibilities of oversight and supervision of the accounting and financial reporting practices and procedures of Keystone and its subsidiaries, the adequacy of internal accounting controls and procedures and the quality and integrity of financial statements.

*Remuneration of Directors of Keystone.* Initial compensation for non-management directors of Keystone (other than directors who are also directors of Keystone North America) will be C$25,000 per year. Directors will receive C$1,200 per meeting for attending board or committee meetings in person and C$500 for attending meetings by phone. The chair of the compensation, nominating and corporate governance committee will receive an additional C$2,500. Directors will also be reimbursed for out of pocket expenses for attending board and committee meetings. Directors will participate in the insurance and indemnification arrangements described below under "Insurance Coverage for Keystone North America and Related Entities and Indemnification."

**Executive Compensation**

The following table sets forth the compensation for the Chief Executive Officer, Chief Financial Officer and Keystone's three most highly compensated executives, other than the Chief Executive Officer and Chief Financial Officer, for the year ended December 31, 2003.

| | Annual Compensation | | |
|---|---|---|---|
| **Name and Principal Position** | **Salary** | **Bonus** | **Other Annual Compensation** |
| Robert G. Horn<br>Chief Executive Officer | $176,000 | $ — | $13,837 |
| Steven A. Tidwell<br>Executive Vice-President | $176,000 | $15,000 | $ 9,536 |
| James Price<br>Chief Operating Officer | $165,600 | $20,000 | $15,186 |
| Stephen M. Shaffer<br>Chief Financial Officer | $160,000 | $21,850 | $11,027 |
| Mike Hays<br>Vice President, Advance Planning | $156,387 | $ — | $ — |

In connection with this offering, a bonus will be paid totaling approximately US$1.7 million cash and approximately 95,261 Class B common shares to 17 members of Keystone management. These amounts shall be paid with cash and shares that would otherwise be payable to the Existing Investors and Existing Lenders.

**Employment Agreements**

On the closing of this offering, Robert G. Horn, Stephen M. Shaffer, James D. Price and Steven A. Tidwell will enter into new employment agreements with Keystone. The agreements are expected to have a three year term and include non-competition provisions for a similar period.

Each employment agreement will provide that the executive will be provided with a compensation package comprised of a base salary, bonus eligibility provisions, and various perquisites. Each such executive will also be eligible to participate in the long-term incentive plan (described below).

**Long-Term Incentive Plan**

The senior management of Keystone North America and the Company will be eligible to participate in Keystone's, long-term incentive plan, or "LTIP". The purpose of the LTIP is to provide eligible participants with compensation opportunities to attract, retain and motivate key personnel and reward directors, officers and senior management by making a significant portion of their incentive compensation directly dependent upon achieving key strategic, financial and operational objectives that are crucial to ongoing growth and profitability.

Pursuant to the LTIP, Keystone will set aside a pool of funds based upon the amount, if any, by which Distributable Cash per IPS exceeds certain defined targets. One-third of the value of such funds will be paid to eligible participants upon the grant of the award. A trustee will purchase IPSs in the market with the remaining two-thirds of the funds and will hold the IPSs until such time as ownership vests to each participant. Generally, 50% of these IPSs will vest equally in each of the first two years following the grant of the awards. Upon the IPSs vesting, LTIP participants will have the option to receive the IPSs or their cash equivalents.

The compensation, nominating and corporate governance committee of Keystone will have the power to, among other things: (i) determine those individuals who will participate in the LTIP; (ii) determine the level of participation of each participant; and (iii) determine the time or times when LTIP awards are to be paid to each participant.

Initially, the LTIP will provide for awards that may be earned based on the amount by which Distributable Cash per annum per IPS exceeds a base threshold per annum equal to $1.00, or the "Base Threshold". The percentage amount of that excess which forms the LTIP incentive pool will be determined in accordance with the table below:

| Percentage by which Distributable Cash per IPS exceeds the Base Threshold | Available for LTIP Payments Maximum Proportion of Distributable Cash |
|---|---|
| 5% or less | 10% |
| over 5% to 10% | 15% of any excess over 5% to 10% |
| greater than 10% | 20% of any excess over 10% |

The Base Threshold will be set for an initial term of three years, subject to the ability of the compensation, nominating and corporate governance committee of the board of Keystone to adjust it from time to time. For the purposes of the LTIP, Distributable Cash will be calculated in a manner consistent with the definition of Distributable Cash set forth in this prospectus. See "Definition of EBITDA, Normalized EBITDA, Normalized Revenue and Distributable Cash".

**Insurance Coverage for Keystone North America and Related Entities and Indemnification**

Keystone North America will obtain or cause to be obtained a policy of insurance for directors and officers of Keystone North America and for the directors and officers of its subsidiaries. The initial aggregate limit of liability applicable to the insured directors and officers under the policy is expected to be $20 million. Under the policy, each entity will have reimbursement coverage to the extent that it has indemnified directors and officers. The policy will include securities claims coverage, insuring against any legal obligation to pay on account of any securities claims brought against Keystone North America and any of its respective subsidiaries. The total limit of liability will be shared among Keystone North America and any of its subsidiaries and its respective directors and officers so that the limit of liability will not be exclusive to any one of the entities or their respective directors and officers.

The by-laws of each of Keystone North America, Keystone and Keystone ULC provide for the indemnification of its directors and officers from and against liability and costs in respect of any action or suit brought against them in connection with the execution of their duties of office, including in respect of periods prior to the closing of this offering, subject to certain limitations.

## USE OF PROCEEDS

The table below sets forth, as of January 31, 2005, our estimate of the sources and uses of funds required to effect the transactions described in this prospectus. The estimated sources and uses are based on an assumed initial offering price of C$10.00 per IPS, and an initial public offering price of 100% of the stated principal amount of each Separate Subordinate Note. Actual amounts will vary from the amounts shown below. Certain amounts in the table have been converted from US Dollars to Canadian Dollars at an assumed exchange rate of $1.2272 per Canadian Dollar, which represents exchange rates in effect as of January 28, 2005.

### Sources and Uses

| | (in millions) |
|---|---|
| **Sources** | |
| IPSs sold hereby(1) | C$171.0 |
| Separate Subordinated Notes | 10.0 |
| New Credit Facility | 52.9 |
| Total sources of funds | C$233.9 |
| **Uses** | |
| Acquisition of Keystone(2) | C$119.4 |
| Acquisition of Hamilton(3) | 69.9 |
| Funding of former owner obligations(4) | 23.4 |
| Integration costs(5) | 2.8 |
| Fees and expenses(6) | 18.4 |
| Total uses of funds | C$233.9 |

(1) Includes approximately C$97.7 million of proceeds allocated to the sale of Common Shares represented by such IPSs and approximately C$73.3 million of proceeds allocated to the Subordinated Notes represented by such IPSs. The amount of proceeds assumes that the over-allotment option is not exercised. If the over-allotment option is exercised, the Issuer will use the net proceeds from the exercise of the option to acquire additional Class A common shares and preferred shares of Keystone, which will in turn use such amounts to redeem Class C common shares held by the Existing Investors and Existing Lenders. If the over-allotment option is exercised in full, the Issuer will own a 93.7% voting interest in Keystone and the Existing Investors, Existing Lenders and certain members of management of Keystone will own a 6.3% voting interest in Keystone.

(2) As part of the Keystone acquisition:

- Approximately C$91.8 million of the proceeds of the offering and Keystone cash on hand above a minimum level will be used to retire all existing indebtedness of Keystone under Keystone's existing credit facility.
- Approximately C$25.6 million will be paid to the Existing Investors.
- Approximately C$2.1 million will be paid to certain members of management of Keystone as a bonus for completing the offering.

(3) As part of the Hamilton acquisition:

- Approximately C$55.0 million of the proceeds of the offering and Hamilton cash on hand above a minimum level will be used to retire the existing senior indebtedness of Hamilton under its term loan and revolver.
- The Existing Lenders will receive C$14.9 million (before payment of certain fees and expenses and other specified items) and Class B and Class C common shares equal to approximately 35% of the aggregate issued and outstanding Class B and C common shares in exchange for the cancellation of their debt.

(4) Approximately C$23.4 million will be placed into a restricted account to satisfy the existing unsecured former owner obligations of Keystone and Hamilton.

(5) Certain integration costs associated with the purchase of Hamilton of approximately C$2.8 million will be paid.

(6) Includes an estimated C$9.8 million payable to the Underwriters of IPSs, approximately C$5.7 million payable in connection with the offering, approximately C$0.4 million payable in connection with the private placement of Separate Subordinated Notes and approximately C$2.5 million payable to the arrangers and lenders under the New Credit Facility.

## INVESTMENT AGREEMENT

Keystone North America, Keystone ULC, Keystone and the Existing Investors will enter into the Investment Agreement pursuant to which, immediately prior to the closing of this offering, the following series of transactions will be undertaken that will result in the Issuer acquiring a 85.3% voting interest in Keystone in the form of Class A common shares and preferred shares of Keystone:

- The proceeds of the offering received by Keystone North America in connection with the issuance of its Common Shares (net of certain expenses incurred by Keystone North America) will be used by Keystone North America to subscribe for common shares of its wholly owned subsidiary, Keystone Merger Corporation ("Mergersub"), a Delaware corporation.
- The gross proceeds of the offering received by Keystone ULC in connection with the issuance of the Subordinated Notes will be used by Keystone ULC to subscribe for preferred shares of Mergersub.
- Mergersub will merge into Keystone with Keystone being the surviving corporation (the "Merger").
- In connection with the Merger (and related transactions):
    - (i) The current shareholders of Keystone will exchange their shares of Keystone for newly issued Class B and Class C common shares of Keystone and cash.
    - (ii) The common shares of Mergersub held by Keystone North America will be converted into Class A common shares of Keystone.
    - (iii) The preferred shares of Mergersub held by Keystone ULC will be converted into preferred shares of Keystone.
- Concurrent with the closing of the Merger, Keystone America, Inc. will purchase certain subsidiaries of Hamilton pursuant to an acquisition agreement (the "Hamilton Acquisition Agreement") in consideration for C$69.9 million (before payment of certain fees and expenses and other specified items) and Class B and Class C common shares equal to 35% of the aggregate issued and outstanding Class B and Class C common shares. Hamilton will, in turn, use that cash and Class B and C common shares to, among other things, retire the indebtedness held by the Existing Lenders of Hamilton. The Hamilton Acquisition Agreement will provide for an escrow of $2 million from the cash that would otherwise be paid to the Existing Lenders to satisfy potential claims associated with the representations and warranties provided to Keystone America, Inc. in the Hamilton Acquisition Agreement. The escrow funds will be held until the earlier of (i) 10 days following the delivery of Keystone North America's 2006 audited financial statements and (ii) April 30, 2007.

• Upon the closing of this offering and the other transactions described in this prospectus, the Existing Investors will hold Class B and Class C common shares and receive net cash proceeds, and the Existing Lenders will hold Class B and Class C common shares, as set out below:

| | Class B common shares(1) | Class C common shares(1) | Net Cash Proceeds (C$)(1) |
|---|---|---|---|
| **Existing Investors and Existing Lenders** | | | |
| Golder, Thoma, Cressey, Rauner Fund V, L.P. | 621,199 | 1,023,816 | 24,158,603 |
| GTCR Associates V | 1,085 | 1,789 | 42,206 |
| Robert G. Horn | 75,424 | — | — |
| Steven A. Tidwell | 35,487 | — | — |
| Heller Financial, Inc. | 17,780 | 29,303 | 691,448 |
| Antares Capital Corporation | 17,780 | 29,303 | 691,448 |
| TCW Leveraged Income Trust, L.P. | 12,701 | 17,514 | — |
| TCW Leveraged Income Trust II, L.P. | 12,701 | 17,514 | — |
| TCW/Crescent Mezzanine Partners II, L.P. | 183,852 | 253,530 | — |
| TCW/Crescent Mezzanine Trust II | 44,763 | 61,727 | — |
| Massachusetts Mutual Life Insurance Company | 49,216 | 67,867 | — |
| MassMutual Corporate Investors | 49,216 | 67,867 | — |
| MassMutual Participation Investors | 28,577 | 39,407 | — |
| Berkshire Fund III, A Limited Partnership | 13,409 | 18,490 | — |
| Berkshire Investors LLC | 703 | 970 | — |
| SBIC Partners, L.P. | 14,112 | 19,460 | — |
| DFW Capital Partners, L.P. | 14,112 | 19,460 | — |
| Other Management(2) | 78,847 | — | — |

(1) To the extent that the amount of proceeds and related expenses of this offering exceeds or is less than the amount asserted, the net cash proceeds to be received by the Existing Investors and the number of Class B and C common shares the Existing Investors and Existing Lenders will receive will be increased or decreased correspondingly.

(2) In connection with this offering, a bonus will be paid totaling approximately US$1.7 million cash and approximately 95,261 Class B common shares to 17 members of Keystone management (including Robert G. Horn and Steven A. Tidwell). These amounts shall be paid with cash and shares that would otherwise be payable to the Existing Investors and Existing Lenders.

• The net proceeds received by Keystone North America from any exercise of the over-allotment option will be used by Keystone North America to subscribe for Class A common shares of Keystone. The gross proceeds received by Keystone ULC will be used by Keystone ULC to subscribe for preferred shares of Keystone. Keystone will contribute to Keystone ULC an amount equal to the fees and expenses payable by Keystone ULC in connection with the exercise of the over-allotment option. Keystone will use the net proceeds remaining to redeem a corresponding number of the Class C common shares of Keystone held by the Existing Investors and Existing Lenders.

For an illustration of the Issuer's ownership interest in Keystone see "Post Closing Structure".

The Investment Agreement will contain customary representations and warranties, which will survive 24 months from the closing of this offering, and related indemnities from Keystone in favour of Keystone North America and Keystone ULC as to various matters, including organization and status, power and due authorization, capital structure, approvals, non-contravention, financial statements, environmental issues, conduct of business, litigation, tax status, title to assets, employees and benefits, material contracts, real property, accounts receivable and content of public disclosure.

The Investment Agreement will also contain a representation and warranty (the "Prospectus Representation") from Golder, Thoma Cressy, Rauner Fund V, L.P., GTCR Associates V, Robert G. Horn and Steven A. Tidwell, in each case on a several basis, in favour of Keystone North America and Keystone ULC that this prospectus contains full, true and plain disclosure of all material facts relating to the IPSs, the Common Shares, and the Subordinated Notes and does not omit to state a material fact that is required to be stated or necessary to make a statement not misleading in light of the circumstances in which it was made. The Prospectus Representation will survive for three years from the date of the closing of this offering or termination of distribution of this offering, whichever is later. The Prospectus Representation will be made to the respective knowledge of the Existing Investors making such representation. For this purpose, knowledge will mean the actual knowledge of those certain Existing Investors after reasonable investigation (which, for an entity, will be a specified individual or individuals) and in any event each such Existing Investor will be deemed to have the knowledge of each of the other Existing Investors (excluding members of management). The several obligations of each of the Existing Investors that give the Prospectus Representation in respect of a breach of the Prospectus Representation will be limited to 100% of the proceeds received by such Existing Investors. To the extent that a claim exceeds the net cash proceeds received by any such Existing Investor, the Existing Investor's liability for such excess will be limited to the then value of their respective Class B and C common shares, if any, which can be satisfied by the surrender of all or a portion of such shares. Investors should note that they may not have a direct statutory right of action against each of the Existing Investors for a misrepresentation in this prospectus.

All representations, warranties and indemnities shall be subject to an initial deductible of $500,000 and each set of claims thereafter must aggregate at least $250,000, subject to the cap on liability discussed above.

The completion of the Issuer's investment in Keystone will be conditional upon the completion of this offering, the receipt of certain consents and approvals (including the listing of the IPSs and Common Shares on the TSX), and the New Credit Facility being available to Keystone America, Inc. If the investment is not completed as provided by the Investment Agreement, the Issuer will refund to purchasers in this offering the consideration paid in respect of the IPSs offered by this prospectus.

## SECURITYHOLDERS' AGREEMENT

Keystone North America, Keystone ULC, Keystone, the Existing Investors, the Existing Lenders and certain members of management of Keystone will enter into the Securityholders' Agreement governing, among other things, their securityholdings in, and the business and affairs of, Keystone. The following is a summary of certain provisions of the Securityholders' Agreement, which summary is not intended to be complete. Reference is made to the Securityholders' Agreement for a complete description and the text of its provisions.

### *Directors*

Initially, the board of directors of Keystone will be comprised of seven persons, a majority of whom shall be residents of the United States. The Securityholders' Agreement requires that the articles of Keystone are to provide that the Chief Executive Officer of Keystone shall be nominated as a director and that the Existing Investors, the Existing Lenders and Keystone North America may nominate individuals to the board of directors of Keystone as follows:

- if at any time the Existing Investors, the Existing Lenders and certain members of management of Keystone, together, own 20% or more of the voting rights of the then outstanding common shares of Keystone, the Existing Investors, the Existing Lenders and certain members of management of Keystone shall have the right to nominate two individuals and the board of Keystone North America shall have the right to nominate four individuals; and
- so long as (i) none of the Existing Investors, the Existing Lenders or certain members of management of Keystone has exercised its Negotiation Right regarding its Class B common shares of Keystone (defined herein), or (ii) the Existing Investors, the Existing Lenders and certain members of management of Keystone, as a group, own 5% or more of the voting rights of the then outstanding common shares of Keystone, they shall have the right to nominate one individual and the board of Keystone North America shall have the right to nominate five individuals.

Keystone's articles will provide that, for so long as the requisite level of ownership is held by a party, the nominees of such party may not be removed without the written consent of such party. In addition, the Securityholders' Agreement provides that the Keystone North America nominees shall be comprised of the members of the board of directors of Keystone North America (other than the nominees of the Existing Investors, the Existing Lenders and certain members of management of Keystone, if any).

*Approval of Certain Actions*

Certain actions that may be taken by Keystone or its subsidiary companies require the approval of: (a) the Existing Investors, the Existing Lenders and certain members of management of Keystone so long as they hold no less than 20% of the voting rights of the then outstanding common shares of Keystone and (b) a majority of the board of directors of Keystone. The actions requiring this approval include: (i) entering into a merger, consolidation, business combination, joint venture or other material corporate transaction; (ii) selling, assigning, conveying or otherwise disposing of all or substantially all of its assets; (iii) adopting any plan or proposal for the liquidation, dissolution, reorganization or recapitalization or commencement of any action seeking relief under any laws relating to bankruptcy, insolvency, conservatorship or relief of debtors; (iv) authorizing or issuing new equity securities except for limited exceptions; (v) consummating an acquisition or acquisitions in excess of certain thresholds; (vi) entering into lines of business other than those concurrently carried on; (vii) changing its fiscal year or making a material change in its accounting policies or procedures unless required under the applicable generally accepted accounting principles; (viii) taking, or permitting, any action which would prevent the business from continuing on an ongoing basis; (ix) making or committing to make any capital expenditures in excess of $5 million; (x) creating, incurring or suffering to exist certain indebtedness or certain liens; (xi) modifying or amending, or permitting such changes, to the terms of the IPSs, Common Shares or Subordinated Notes (any amendment to the terms of the Subordinated Notes will be governed by the terms thereof including the requirement, in certain circumstances, for the unanimous approval of all holders of the Subordinated Notes then outstanding); (xii) modifying, amending or taking any action in contravention of its constating documents including the terms of any securities held by the Existing Investors, the Existing Lenders and certain members of management of Keystone; (xiii) commingling funds; or (xiv) agreeing to do any of the preceding.

***Pre-Emptive Rights***

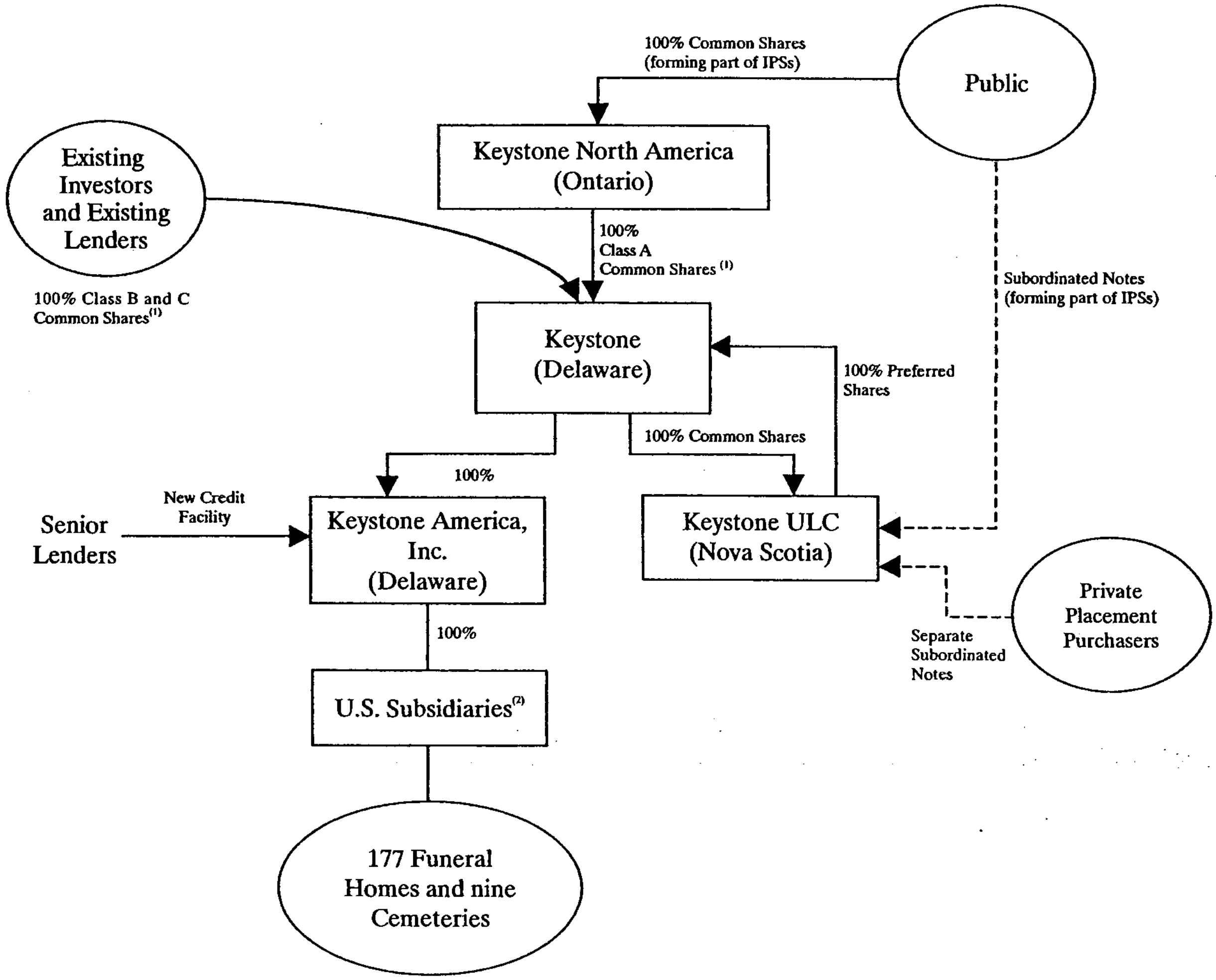
The Securityholders' Agreement will also provide that the Existing Investors, the Existing Lenders and certain members of management of Keystone will have pre-emptive rights to purchase IPSs or Class B or C common shares of the Issuer or Keystone, as applicable, to maintain their *pro rata* ownership of Keystone in the event that Keystone decides to issue common shares or the Issuer decides to issue IPSs, subject to certain exceptions. Any Existing Investor, Existing Lender or certain members of management of Keystone exercising this right will be entitled to participate in the issuance of common shares or IPSs by Keystone or the Issuer, as applicable, in either case, through the purchase of Class C common shares of Keystone at the most favourable price and on the most favourable terms as the applicable securities are to be offered to a third party. The pre-emptive rights may be waived, as to all Existing Investors, Existing Lenders and certain members of management of Keystone, by the holders of 66⅔% of all equity securities of Keystone then outstanding and held by the Existing Investors, the Existing Lenders and certain members of management of Keystone.

***Tag-Along Rights***

The Securityholders' Agreement will also provide that on or after the second anniversary of this offering, in the event that a person offers to purchase more than 10% of the Class A common shares in Keystone held by Keystone North America pursuant to an agreement with Keystone North America, directly or indirectly, or in the case of an indirect purchase, pursuant to a non-exempt take-over bid in respect of which Keystone North America proposes to enter into a support agreement with such person, then it will be a condition of any such agreement or support agreement that the person will offer to purchase a *pro rata* portion of the Class B and C common shares, on the same terms and subject to the same conditions as are applicable to the direct or indirect purchase of the Class A common shares of Keystone held by Keystone North America, with appropriate adjustments to reflect the Liquidation Amount (as defined below) payable on the Class B and C common shares in accordance with the formula and restrictions set out in the Securityholders' Agreement. For the purposes of the foregoing, an offer to purchase Common Shares shall be considered to be an indirect offer to purchase that portion of the common shares of Keystone held by Keystone North America equal to the portion of Common Shares subject to the offer.

## POST-CLOSING STRUCTURE

The following chart illustrates the ownership structure of the Issuer and the Company immediately after this offering and the transactions contemplated in this prospectus. See "Investment Agreement".




(1) Upon closing, the Existing Investors, Existing Lenders and certain members of management of Keystone will own all of the issued and outstanding Class B and C common shares of Keystone, representing a 14.7% voting interest in Keystone (6.3% if the over-allotment option is exercised in full). Each Class B and C common share entitles the holder to receive distributions from Keystone approximately equivalent to the distributions per IPS received by holders of IPSs. The holders of the Class B and C Common shares have the right to request that Keystone enter into good faith negotiations to repurchase their shares in certain specified circumstances. Keystone has the right to purchase for cancellation the Class B and Class C common shares in certain specified circumstances. See "Investment Agreement', "Securityholders' Agreement", "Retained Interest — Repurchase Events" and "Plan of Distribution". The Class B common shares will represent at least 10% of the aggregate value of the common shares of Keystone outstanding upon closing of the offering.

(2) The financial information of all subsidiaries is consolidated in Keystone's and Hamilton's financial statements that are contained elsewhere in this prospectus.

## RETAINED INTEREST

Upon closing of this offering, the Existing Investors, Existing Lenders and certain members of management of Keystone will hold a 14.7% voting interest in Keystone (6.3% if the over-allotment option is exercised in full) represented by 1,270,964 Class B common shares and 1,668,017 Class C common shares. The Class B and C common shares entitle the holders to receive dividends equivalent to the distributions paid on the IPSs. The Class B common shares will represent at least 10% of the aggregate value of the common shares of Keystone outstanding upon closing of the offering.

### Repurchase Events

The Securityholders' Agreement will provide that each holder of Class B and/or C common shares has the right (the "Negotiation Right"), exercisable at any time and from time to time and subject to the limits described below, to request Keystone to enter into good faith negotiations with such holder to purchase for cancellation, all or any portion of the Class B or C common shares owned by such holder. Upon delivery of a notice by a holder of Class B or C common shares to Keystone requesting that Keystone enter into good faith negotiations with such holder to purchase, for cancellation, all or a portion of such holder's Class B and/or C common shares, Keystone is required to use its best efforts to negotiate the purchase of such Class B and/or C common shares.

The Negotiation Right in respect of the Class B common shares may not be exercised for a period of two years from the date of closing of the offering. In addition, the Existing Investors and Existing Lenders have agreed not to exercise the Negotiation Right in respect of the Class C common shares for a period of 180 days from the date of the closing of the offering without the prior written consent of BMO Nesbitt Burns Inc., on behalf of the Underwriters. The Negotiation Right may only be exercised if, at the time of its exercise: (i) none of Keystone ULC, Keystone or their respective subsidiaries is in default under the indenture related to the Subordinated Notes or any other indebtedness other than indebtedness to affiliates, and (ii) interest on the Subordinated Notes is not being deferred in accordance with the interest deferral provisions in the indenture related to the Subordinated Notes and no interest deferred during any Interest Deferral Period (including interest thereon) remains unpaid.

The terms of the Class B and C common shares provide that Keystone has the right (the "Redemption Right"), exercisable at any time and from time to time following the second anniversary of the closing of the offering and subject to the limits described below, to purchase for cancellation from the holders of Class B and C common shares, all or any portion of the outstanding Class B and/or C common shares. Upon delivery of a notice to all of the holders of Class B and/or C common shares, as the case may be, (the "Redemption Notice") requesting the holders to sell to Keystone all or a portion of each such holder's Class B and/or C common shares (each such share, a "Subject Interest" and collectively the "Subject Interests"), on a *pro rata* basis, the holders are required to sell to Keystone such interests. The repurchase of the Subject Interests will occur on such date as is specified by Keystone in the Redemption Notice (provided such date shall not be prior to the 30th day following receipt by the holders of the Redemption Notice).

The Redemption Right may only be exercised if, at the time of its exercise: (i) none of Keystone ULC, Keystone or their respective subsidiaries is in default under the indenture related to the Subordinated Notes or any other indebtedness other than indebtedness to affiliates, and (ii) interest on the Subordinated Notes is not being deferred in accordance with the interest deferral provisions in the indenture related to the Subordinated Notes and no interest deferred during any Interest Deferral Period (including interest thereon) remains unpaid.

The amount which shall be paid by Keystone for the purchase of each Subject Interest pursuant to the Redemption Right will be equal to the fair market value of the Subject Interest at the time of the purchase, without regard to: (i) the liquidity of the Subject Interest and (ii) the Enhanced Dividend (as defined below).

Any repurchase by Keystone of Class B and/or C common shares, including pursuant to the exercise by a holder of the Negotiation Right or the exercise by Keystone of the Redemption Right, shall be referred to in this prospectus as a "Repurchase Event".

## DESCRIPTION OF IPSs

### General

The Issuer is offering 17,100,000 IPSs in this offering. Each IPS represents:

- one Common Share; and
- C$4.286 aggregate principal amount of Subordinated Notes.

The ratio of Common Shares to principal amount of Subordinated Notes represented by an IPS is subject to change in the event of a stock split, recombination or reclassification, or upon a partial redemption or repurchase of the Subordinated Notes.

### Voluntary Separation and Recombination

At any time after the 45th day following the date of original issuance or upon the occurrence of a change of control of Keystone ULC, holders of IPSs may separate their IPSs into the Common Shares and Subordinated Notes represented thereby through their broker or other financial institution. Similarly, any holder of Common Shares and Subordinated Notes may recombine the applicable number of Common Shares and principal amount of Subordinated Notes to form IPSs through their broker or other financial institution, at any time prior to an automatic separation of the Subordinated Notes. See "Book-Entry Settlement and Clearance" below for more information on the method by which delivery and surrender of IPSs and delivery of Common Shares and Subordinated Notes will be effected.

### Automatic Separation

Upon the occurrence of any of the following, the IPSs will be automatically separated into the Common Shares and Subordinated Notes represented thereby:

- with respect to any holder of IPSs, acceptance by such holder of Keystone ULC's offer to repurchase the Subordinated Notes represented by that holder's IPSs in connection with a change of control of Keystone ULC;
- exercise by Keystone ULC of its right to redeem all or a portion of the Subordinated Notes which may be represented by IPSs at the time of such redemption;
- the date on which the outstanding principal amount of the Subordinated Notes becomes due and payable, whether at the stated maturity date or upon acceleration thereof;
- if CDS is unwilling or unable to continue as securities depository with respect to the IPSs and the Issuer is unable to find a successor depository; or
- the continuance (without cure) of a payment default on the Subordinated Notes for 90 days.

### Book-Entry Settlement and Clearance

#### *General*

CDS will act as securities depository for the IPSs, the Subordinated Notes and the Common Shares represented by the IPSs, which are referred to collectively as the "Securities". The IPSs and the Subordinated Notes and the Common Shares represented by the IPSs will be represented by one or more global notes and global share certificates. The global notes and global share certificates will be issued as fully-registered in book-entry only form in the name of CDS or its nominee, CDS & Co. If an investor intends to purchase IPSs or Subordinated Notes sold separately in the manner provided by this prospectus an investor must do so through direct and indirect CDS participants. The participant through which a purchase is made will receive a credit for the applicable number of IPSs on CDS's records. The ownership interest of each actual purchaser of the applicable security, referred to as a "beneficial owner", is to be recorded on the participant's records. Beneficial owners will not receive written confirmation from CDS of their purchases, but beneficial owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the CDS participant through which the beneficial owner entered into the transaction.

All interests in the Securities will be subject to the operations and procedures of CDS. The following is a summary of those operations and is provided by the Issuer solely for convenience. The operations and procedures of each settlement system may be changed at any time. The Issuer is not responsible for those operations and procedures.

To facilitate subsequent transfers, all Securities deposited by direct CDS participants are registered in the name of CDS. The deposit of Securities with CDS and their registration in the name of CDS effect no change in beneficial ownership. CDS has no knowledge of the actual beneficial owners of the Securities. CDS's records reflect only the identity of the direct CDS participants to whose accounts such Securities are credited, which may or may not be the beneficial owners. The CDS participants will remain responsible for keeping account of their holdings on behalf of their customers.

Transfers of ownership interests in the Securities are effected by entries made on the books of the CDS participants acting on behalf of beneficial owners. Beneficial owners will not receive certificates representing their ownership interests in the applicable Security except in the event that use of the book-entry only system for the Securities is discontinued.

Cross-market transfers between CDS participants, on the one hand, and the Depositary Trust Company or "DTC", participants, on the other hand, will be effected within CDS through DTC. To deliver or receive an interest in Securities held in a DTC account, an investor must send transfer instructions to DTC under the rules and procedures of that system and within the established deadlines of that system. If the transaction meets its settlement requirements, DTC will send instructions to its CDS depositary to take action to effect final settlement by delivering or receiving interests in the Securities in CDS and making or receiving payment under normal procedures for same-day funds settlement applicable to CDS. DTC participants may not deliver instructions directly to the CDS depositary that is acting for DTC.

Conveyance of notices and other communications by CDS to direct participants, by direct participants to indirect CDS participants, and by CDS participants to beneficial owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

CDS will not consent or vote with respect to the Securities. Under its usual procedures, CDS would mail an omnibus proxy to the Issuer as soon as possible after the record date. The omnibus proxy assigns CDS's consent or voting rights to those direct participants to whose accounts the Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

The Issuer and the trustee under the Subordinated Note indenture will make any payments on the Common Shares and Subordinated Notes to CDS. CDS's practice is to credit direct CDS participants' accounts on the payment date in accordance with their respective holdings shown on CDS's records unless CDS has reason to believe that it will not receive payment on the payment date. Payments by CDS participants to beneficial owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such participant and not of CDS, Keystone North America, Keystone ULC or the trustee, subject to any statutory or regulatory requirements as may be in effect from time to time.

Keystone North America and the trustee under the Subordinated Note indenture will be responsible for the payment of all amounts to CDS. CDS will be responsible for the disbursement of those payments to its participants, and the participants will be responsible for disbursements of those payments to beneficial owners.

CDS may discontinue providing its service as securities depository with respect to the IPSs, the Common Shares or the Subordinated Notes at any time by giving reasonable notice to Keystone North America, Keystone ULC and the trustee under the Subordinated Note indenture. If CDS discontinues providing its service as securities depository with respect to the IPSs and Keystone North America and Keystone ULC are unable to obtain a successor securities depository, an investor will automatically take a position in the component securities and Keystone North America and Keystone ULC will print and deliver certificates representing the IPSs. If CDS discontinues providing its service as securities depository with respect to the Common Shares or Subordinated Notes and Keystone North America and Keystone ULC are unable to obtain a successor securities depository, Keystone North America and Keystone ULC will print and deliver to the investor certificates for those securities and Keystone North America and Keystone ULC will automatically take a position in the securities and Keystone North America and Keystone ULC will print and deliver certificates for the Common Shares and Subordinated Notes.

Also, in the event that Keystone North America or Keystone ULC decide to discontinue use of the system of book-entry only transfers through CDS (or a successor securities depository) Keystone North America or Keystone ULC will print and deliver to the investor certificates for the Common Shares and Subordinated Notes the investor may own.

The information in this section concerning CDS and CDS' book-entry only system has been obtained from sources that the Issuer believes to be reliable, including CDS, but neither the Issuer, nor the Underwriters take responsibility for its accuracy.

Neither the Issuer nor any trustee nor the Underwriters will have any responsibility or obligation to participants, or the persons for whom they act as nominees, with respect to:

- the accuracy of the records of CDS, its nominee, or any participant, any ownership interest in the securities; or
- any payments to, or the providing of notice, to participants or beneficial owners.

***Separation and Recombination.***

Any voluntary or automatic separation of IPSs, and any subsequent recombination of IPSs from Subordinated Notes and Common Shares, are to be accomplished by entries made by the CDS participants on behalf of beneficial owners. In any such case, the participant's account through which a separation or recombination is effected will be credited and debited for the applicable securities on CDS's records.

***Procedures relating to subsequent issuances.***

The Indenture and the agreements with CDS will provide that, in the event there is a subsequent issuance of Subordinated Notes, the terms of the newly issued Subordinated Notes (including interest and maturity) will be identical in all material respects to the previously issued Subordinated Notes and all such Subordinated Notes will be traded under the same CUSIP number. Any such subsequently issued Subordinated Notes may be issued at a discount or premium to the principal amount of Subordinated Notes offered in this offering. See "Description of Subordinated Notes — Additional Issuances of Subordinated Notes".

## DESCRIPTION OF SUBORDINATED NOTES

The Subordinated Notes are to be issued under an indenture, to be dated as of the Closing Date (the "Indenture"), between Keystone ULC, Keystone, each Guarantor and Computershare Trust Company of Canada, as trustee (the "Trustee"). The following is a description of the terms of the Indenture, a copy of the form of which will be filed with the Canadian securities regulatory authorities. Capitalized terms used in this "Description of Subordinated Notes" section and not otherwise defined have the meanings set forth in the Indenture and in the section "Certain Definitions" below, as applicable. The following summary of certain provisions of the Indenture is subject to, and is qualified in its entirety by reference to, all the provisions of the Indenture.

### General

The Indenture will provide for the issuance of the Subordinated Notes, represented by the IPSs, and the issuance of the Separate Subordinated Notes. The Indenture will also provide for the issuance of an unlimited aggregate principal amount of additional Subordinated Notes having substantially identical terms and conditions to the Subordinated Notes offered hereby (the "Additional Subordinated Notes"), subject to compliance with the covenants contained in the Indenture. Any Additional Subordinated Notes will be part of the same issue as the Subordinated Notes offered pursuant to this prospectus and the Separate Subordinated Notes and will vote on all matters with the Subordinated Notes offered pursuant to this prospectus and the Separate Subordinated Notes.

The Subordinated Notes will be registered in book-entry only form. See "Description of IPSs — Book-Entry Settlement and Clearance". The Subordinated Notes will not be listed or traded on any exchange or market and therefore the holders may not be able to resell the Subordinated Notes. BMO Nesbitt Burns Inc. has advised Keystone ULC that it currently intends to facilitate a market in the Subordinated Notes subject to customary market practice and applicable legal and regulatory requirements and limitations. However, BMO Nesbitt Burns Inc. is not obligated to do so and may discontinue any such activities, if commenced, at any time and without notice. Moreover, if and to the extent that BMO Nesbitt Burns Inc. facilitates a market for the Subordinated Notes, there can be no assurance that such market would provide sufficient liquidity for any holder of any such securities.

The Subordinated Notes will be an unsecured senior subordinated obligation of Keystone ULC and each Guarantor will guarantee the Subordinated Notes on an unsecured basis. See "Security and Guarantees" below.

None of the Separate Subordinated Notes sold concurrently with this offering may be purchased, directly or indirectly, by Persons who are also purchasing IPSs in this offering. Prior to the Closing Date, certain representations will be made to the Company in connection with these restrictions.

**Maturity**

The Subordinated Notes will mature on the 12th anniversary of the Closing Date. On maturity, Keystone ULC will repay the indebtedness represented by the Subordinated Notes by paying the Trustee, on behalf of the Holders, in lawful money of Canada an amount equal to the principal amount of the outstanding Subordinated Notes, together with accrued and unpaid interest.

**Interest**

The Subordinated Notes will bear interest at a rate of 14.5% per annum from the Closing Date, or from the most recent date to which interest has been paid or provided for, payable monthly in arrears, subject to any permissible interest deferral, less any tax required to be withheld, on the fifteenth day following the end of each month (or the next Business Day, if such day is not a Business Day) to holders of record at the close of business on the last Business Day of the preceding month commencing March 15, 2005. The interest and principal on the Subordinated Notes will be payable in lawful money of Canada by wire transfer or banker's draft at any branch in Canada of the bank to be specified in the Indenture.

**Interest Deferral**

Prior to the fifth anniversary of the closing of this offering, Keystone ULC will be permitted, at its election, to defer interest payments on the Subordinated Notes, if and for so long as the Interest Coverage Ratio of the Company for the most recently ended twelve-month period ending on the last day of any month, is less than the Interest Deferral Threshold, unless a default in payment of interest, principal or premium, if any, on the Subordinated Notes has occurred and is continuing, or any other Event of Default with respect to the Subordinated Notes has occurred and is continuing and the Subordinated Notes have been accelerated as a result of the occurrence of such Event of Default (any such period, an "Interest Deferral Period"). Interest payments on the Subordinated Notes will not be deferred under this provision for more than 24 months in the aggregate or beyond the fifth anniversary of the closing of this offering.

In addition, after the fifth anniversary of the closing of this offering, Keystone ULC may at its election defer interest on the Subordinated Notes on not more than eight occasions for not more than eight months per occasion (each, an "Interest Deferral Period") by delivering to the Trustee a copy of a resolution of Keystone ULC's board of directors certified by an officer's certificate of Keystone ULC to the effect that, based upon a good faith determination of Keystone ULC's board of directors, such deferral is reasonably necessary for *bona fide* cash management purposes, or to reduce the likelihood of or avoid a default on any Senior Indebtedness; *provided* no such deferral may be commenced and any ongoing deferral shall cease, if a default in payment of interest, principal or premium, if any, on the Subordinated Notes has occurred and is continuing or any other Event of Default with respect to the Subordinated Notes has occurred and is continuing and the Subordinated Notes have been accelerated as a result of the occurrence of such Event of Default. No Interest

Deferral Period may commence unless and until all interest deferred pursuant to any preceding Interest Deferral Period, together with interest thereon, has been paid in full.

Deferred interest on the Subordinated Notes shall bear interest at the same rate as the stated rate on the Subordinated Notes, compounded monthly, until paid in full. Following the end of any Interest Deferral Period, Keystone ULC shall be obligated to resume monthly payments of interest on the Subordinated Notes, including interest on deferred interest. All interest deferred prior to the fifth anniversary of the closing of this offering, including interest accrued on deferred interest, must be repaid on or before the fifth anniversary of the closing of this offering. All interest deferred after the fifth anniversary of the closing of this offering, including interest accrued on deferred interest, must be repaid on or before maturity, provided that Keystone ULC must pay all deferred interest and accrued interest thereon in full prior to deferring interest on a subsequent occasion. Keystone ULC may prepay all or part of the deferred interest, at any time other than during an Interest Deferral Period.

During any Interest Deferral Period, or so long as any deferred interest remains unpaid, and under other circumstances described below, Keystone shall not pay any dividends or make any distribution to holders of its common shares, or make certain other Restricted Payments. See "Certain Covenants — Limitation on Restricted Payments". The New Credit Facility contains limitations on Keystone's ability to make distributions to Keystone ULC to enable it to prepay deferred interest on the Subordinated Notes. See "New Credit Facility".

**Additional Amounts for U.S. Withholding Tax**

All amounts paid or credited by Keystone ULC under or with respect to the Subordinated Notes or by any Guarantor under or in respect of its Guarantee will be made free and clear of and without withholding or deduction for or on account of any present or future tax, duty, levy, impost, assessment or other government charge (including penalties, interest and any other liabilities or expenses related thereto) imposed or levied by or on behalf of the government of the United States or any government of any political subdivision, state or territory of the United States or any authority or agency therein or thereof having power to tax (hereinafter, "Taxes"), unless Keystone ULC or such Guarantor is required to withhold or deduct any amount for or on account of Taxes by law or by interpretation or administration of law. If Keystone ULC or any Guarantor is required to withhold or deduct any amount for or on account of Taxes from any amounts paid or credited under or with respect to the Subordinated Notes or the Guarantees of the Subordinated Notes, Keystone ULC or such Guarantor will pay such additional amounts ("Additional Amounts") as may be necessary so that the net amount received by each owner of Subordinated Notes (an "owner" for purposes of this "Additional Amounts for U.S. Withholding Tax" section) including Additional Amounts, after such withholding or deduction (including any withholding or deduction in respect of Additional Amounts) will not be less than the amount the owner would have received if such Taxes had not been withheld or deducted; provided that Additional Amounts will only be payable with respect to a payment made to a person if:

(a) the person is a Non-U.S. Holder that is not a Disqualified Recipient,

(b) either: (i) the Non-U.S. Holder certifies to Keystone ULC or its agent on IRS Form W-8BEN (or a suitable substitute or successor form) executed under penalties of perjury that such Non-U.S. Holder is not a "United States person" (as defined in the Code) and provides its name and address; or (ii) a "qualified intermediary" (as defined in applicable Treasury Regulations) receives documentation upon which it can rely to treat the Non-U.S. Holder as not a United States person and provides the Issuer with an IRS Form W-8IMY (or a suitable substitute or successor form), and

(c) the payment is not effectively connected with such person's conduct of a trade or business within the U.S.

Keystone ULC and any Guarantors will also:

(a) make such withholding or deduction; and

(b) remit the full amount deducted or withheld to the relevant authority;

in accordance with and in the time required under applicable law.

At least 30 days or as soon as otherwise practicable prior to each date on which any payment under or with respect to the Subordinated Notes is due and payable, on which Keystone ULC or any Guarantor will be obligated to pay Additional Amounts with respect to such payment, Keystone ULC or such Guarantor will deliver to the Trustee an officers' certificate stating the fact that such Additional Amounts will be payable and specifying the amounts so payable and will set forth such other information necessary to enable the Trustee to pay such Additional Amounts to holders of notes or owners on the payment date. Whenever in the Indenture or in this prospectus there is mentioned, in any context, principal, premium, if any, interest or any other amount payable under or with respect to any Subordinated Note, such mention will be considered to include the payment of Additional Amounts to the extent that, in such context, Additional Amounts are, were or would be payable in respect thereof.

Keystone ULC or a Guarantor will pay any present or future stamp, court, documentary or other similar taxes, charges or levies that arise in any taxing jurisdiction from the execution, delivery or registration of, or enforcement of rights under, the Subordinated Notes, the Indenture or any related document ("Documentary Taxes").

The obligation to pay Additional Amounts (and any reimbursement) and Documentary Taxes under the terms and conditions described above will survive any termination, defeasance or discharge of the Indenture.

**Canadian Withholding Tax**

Keystone ULC will be entitled to deduct and withhold any applicable withholding taxes pursuant to the Tax Act from any payment to be made on the Subordinated Notes and the amount of any such deduction or withholding will be considered an amount paid in satisfaction of Keystone ULC's obligation under such Subordinated Notes and there is no obligation on Keystone ULC to gross-up amounts paid to a Holder of the Subordinated Notes in respect of such deductions or withholding.

**Optional Redemption**

Except for a tax redemption described below, Keystone ULC may not redeem the Subordinated Notes at its option prior to the fifth anniversary of the Closing Date.

On or after the fifth anniversary of the Closing Date, Keystone ULC may redeem the Subordinated Notes, at its option, at any time in whole and from time to time in part, upon not less than 30 nor more than 60 days notice to Holders, for cash, at a redemption price (expressed as percentages of principal amount) set forth below, plus accrued and unpaid interest on the Subordinated Notes redeemed to the applicable redemption date, if redeemed during the twelve-month period beginning on the anniversary of the date of closing of the offering in the years indicated below:

| Year | Percentage |
|---|---|
| 2010 | 104% |
| 2011 | 103% |
| 2012 | 102% |
| 2013 | 101% |
| 2014 and thereafter | 100% |

Keystone ULC may, at its option, redeem all, but not less than all, of the Subordinated Notes, at any time upon not less than 30 nor more than 60 days' prior notice, at a redemption price equal to 100% of the principal amount of the Subordinated Notes plus accrued and unpaid interest to the redemption date, during any period that for U.S. federal income tax purposes Keystone ULC: (i) is not, or would not be, in the opinion of nationally recognized tax counsel, permitted to deduct all or a substantial portion of the interest payable on the Subordinated Notes from its income; or (ii) is required to withhold or deduct any amount for or on account of Taxes from any amounts paid or credited under or with respect to the Subordinated Notes and Keystone ULC is required to pay Additional Amounts. See "— Additional Amounts for U.S. Withholding Tax".

In the case of any partial redemption, selection of the Subordinated Notes for redemption will be made by the Trustee on a *pro rata* basis, by lot or by such other method as the Trustee deems fair and appropriate (and in such manner as complies with the applicable legal and regulatory requirements). If any Subordinated Note is to be redeemed in part only, the notice of redemption relating to such subordinated note will state the portion of the principal amount thereof to be redeemed. A new Subordinated Note in principal amount equal to the unredeemed portion thereof will be issued in the name of the holder thereof upon cancellation of the original Subordinated Note. On and after the redemption date, interest will cease to accrue on Subordinated Notes or portions thereof called for redemption, so long as Keystone ULC has deposited with the depositary funds sufficient to pay the principal of, plus accrued and unpaid interest and the premium (if any) on, the Subordinated Notes to be redeemed.

**Ranking**

The Subordinated Notes will be unsecured senior subordinated indebtedness of Keystone ULC and will be subordinated in right of payment, as set forth in the Indenture, to all existing and future Senior Indebtedness of Keystone ULC including the guarantee provided by Keystone ULC pursuant to the New Credit Facility.

Keystone ULC may not pay principal of, premium (if any) or interest on, the Subordinated Notes or make any deposit pursuant to the provisions described under "— Defeasance" below and may not otherwise purchase, redeem or otherwise retire any Subordinated Notes (except that Holders may receive and retain (a) Permitted Junior Securities and (b) payments made from the trust described under "— Defeasance" below so long as, on the date or dates the respective amounts were paid into the trust, such payments were made with respect to the Subordinated Notes without violating the subordination provisions described herein or any other material agreement binding on Keystone ULC, including the New Credit Facility) (collectively, "pay the Subordinated Notes") if:

- a default in the payment of the principal of, premium, if any, or interest on any Designated Senior Indebtedness occurs and is continuing or any other amount owing in respect of any Designated Senior Indebtedness has not been paid when due, or
- any other default on any Designated Senior Indebtedness has occurred and the maturity of such Designated Senior Indebtedness has been accelerated in accordance with its terms,

unless, in either case, the default has been cured or waived and any such acceleration has been rescinded or such Designated Senior Indebtedness has been paid or discharged in full.

However, Keystone ULC may pay the Subordinated Notes without regard to the foregoing if Keystone ULC and the Trustee receive written notice approving such payment from the Representative of each series of the Designated Senior Indebtedness with respect to which either of the events set forth in either of the bullet points of the immediately preceding sentence has occurred and is continuing. During the continuance of any default (other than a default described in either of the bullet points of the second preceding sentence) with respect to any Designated Senior Indebtedness pursuant to which the maturity thereof may be accelerated immediately without further notice (except such notice as may be required to effect such acceleration) or upon the expiration of any applicable grace periods, Keystone ULC may not pay the Subordinated Notes for a period (a "Payment Blockage Period") commencing upon the receipt by the Trustee (with a copy to Keystone ULC) of written notice (a "Blockage Notice") of such default from the Representative of such defaulted Designated Senior Indebtedness specifying an election to effect a Payment Blockage Period and ending on the earliest to occur of the following events:

- 179 days shall have elapsed since the receipt of such Blockage Notice;
- such Payment Blockage Period is terminated by written notice to the Trustee and Keystone ULC from the Person or Persons who gave such Blockage Notice;
- the repayment or discharge in full of such defaulted Designated Senior Indebtedness; or
- the default giving rise to such Blockage Notice is no longer continuing, or is waived by the holders of the defaulted Designated Senior Indebtedness or the Representative of such holders.

Notwithstanding the provisions described in the immediately preceding sentence (but subject to the provisions contained in the succeeding paragraph), unless the holders of such defaulted Designated Senior Indebtedness or the Representative of such holders have accelerated the maturity of such defaulted Designated Senior Indebtedness, Keystone ULC may resume payments on the Subordinated Notes after the end of such Payment Blockage Period. In no event may the total number of days during which any Payment Blockage Period or Periods is in effect exceed 179 days in the aggregate during any 360 consecutive day period. For purposes of this provision, no default or event of default that existed or was continuing on the date of the commencement of any Payment Blockage Period with respect to the Designated Senior Indebtedness initiating such Payment Blockage Period shall be, or be made, the basis of the commencement of a subsequent Payment Blockage Period by the Representative of such Designated Senior Indebtedness, unless such default or event of default shall have been cured or waived for a period of not less than 90 consecutive days.

Upon any payment or distribution of the assets of Keystone upon a total or partial liquidation or dissolution, bankruptcy, reorganization, insolvency, receivership or similar proceeding relating to Keystone or its property, or an assignment for the benefit of its creditors or any marshalling of Keystone's assets or liabilities, the holders of Senior Indebtedness will be entitled to receive payment of all the Senior Indebtedness before the holders of the Subordinated Notes are entitled to receive any payment, and until the Senior Indebtedness is paid in full, any payment or distribution to which holders of the Subordinated Notes would be entitled but for the subordination provisions of the Indenture will be made to holders of the Senior Indebtedness as their interests may appear. However, the holders of Subordinated Notes may receive and retain Permitted Junior Securities, and payments made from the trust described under "— Defeasance" so long as, on the date or dates the respective amounts were paid into the trust, such payments were made with respect to the Subordinated Notes without violating the subordination provisions described herein or any other material agreement binding on Keystone, including the New Credit Facility. If a distribution is made to holders of the Subordinated Notes that due to the subordination provisions of the Indenture should not have been made to them, such holders of the Subordinated Notes are required to hold it in trust for the holders of Senior Indebtedness and pay it over to them as their interests may appear.

After the occurrence of an Event of Default, Keystone or the Trustee shall promptly notify the holders of each series of the Designated Senior Indebtedness (or their respective Representative) of such occurrence. If any Designated Senior Indebtedness is outstanding, Keystone may not make any payments then due on the Subordinated Notes until five Business Days after the holders or the Representative of such Designated Senior Indebtedness receive notice of such occurrence and, thereafter, may pay the Notes only if the subordination provisions of the Indenture otherwise permit payment at that time.

By reason of such subordination provisions contained in the Indenture, in the event of insolvency, creditors of Keystone who are holders of Senior Indebtedness may recover more, ratably, than the holders of the Subordinated Notes and, because of the obligation on the part of the holders of the Subordinated Notes to turn over distributions to the holders of Senior Indebtedness, to the extent required to pay Senior Indebtedness in full, trade creditors of Keystone and Guarantors may recover more, ratably, than the holders of the Subordinated Notes.

The Indenture will contain identical subordination provisions relating to each Guarantor's obligations under its Guarantee.

Notwithstanding the above provisions, nothing shall prevent an Event of Default from occurring or otherwise impair, as between Keystone ULC (and the Guarantors) and the holders of the Subordinated Notes, the obligation of Keystone ULC and the Guarantors, which is unconditional and absolute, to make payments on the Subordinated Notes as and when the same shall become due and payable in accordance with their terms, nor shall the holders of Subordinated Indebtedness be prohibited from immediately enforcing any of their default remedies permitted by applicable law upon default under the Subordinated Notes, subject, however, to the Acceleration Forbearance Period.

**Security and Guarantees**

The Subordinated Notes will be an unsecured obligation of Keystone ULC, guaranteed by Keystone and each of its Subsidiaries on an unsecured basis pursuant to guarantees to be entered into by each Guarantor. The indebtedness evidenced by each Guarantee will be subordinated in right of payment, as set forth in the Indenture, to all existing and future Senior Indebtedness of such Guarantor, including the Senior Indebtedness of Keystone and its affiliates under the New Credit Facility.

**Additional Issuances of IPSs and Subordinated Notes**

Subject to certain covenants on the Incurrence of Indebtedness, the Indenture provides for the additional issuances of Subordinated Notes. The terms of any Additional Subordinated Notes will be identical in all material respects to the Subordinated Notes distributed as part of IPSs under this prospectus. Keystone ULC may issue Additional Subordinated Notes at a discount or premium to the principal amount. The issuance of Additional Subordinated Notes upon the exercise of the underwriters' over-allotment option is expressly authorized in the Indenture.

**Acceleration Forbearance Periods**

The principal amount of the Subordinated Notes will not be due and payable during any Acceleration Forbearance Period; *provided, however*, the Acceleration Forbearance Period shall not prevent an Event of Default from occurring or otherwise impair, as between Keystone ULC (and the Guarantors) and the holders of the Subordinated Notes, the obligation of Keystone ULC and the Guarantors, which is unconditional and absolute, to make payments on the Subordinated Notes as and when the same shall become due and payable in accordance with their terms, nor shall the holders of Subordinated Debt be prohibited from immediately enforcing any of their other default remedies permitted by applicable law (including the right to sue) during the Acceleration Forbearance Period. "Acceleration Forbearance Period" means, so long as Keystone ULC has Senior Indebtedness outstanding which requires subordinated debt of Keystone ULC to have a forbearance provision, the period beginning on the date when the Trustee or the Holders of at least 25% in principal amount of the outstanding Subordinated Notes (or Holders of a Reduced Threshold Amount for a Reduced Threshold Default) provide Keystone ULC with a notice of acceleration and ending on the earliest of: (a) 179 days after the commencement of such period, *provided, however,* that in the event that there has been any prior Acceleration Forbearance Period in the immediately preceding 12-month period, the duration of the Acceleration Forbearance Period will be automatically reduced by the cumulative duration of all prior Acceleration Forbearance Periods that occurred during the preceding 12-month period; (b) the date the holders of Indebtedness under the New Credit Facility accelerate the Senior Indebtedness thereunder or any enforcement or collection action shall have been commenced with respect thereto; (c) the occurrence or existence of an Event of Default described in clause (vii) under "Defaults under the Indenture"; (d) the maturity of the Subordinated Notes; and (e) the holders of Senior Indebtedness consent in writing to the termination of the Acceleration Forbearance Period.

The Indenture will contain substantially equivalent forbearance provisions relating to each Guarantor's Obligations under its Guarantee.

**Change of Control**

Upon the occurrence of any of the following events (each, a "Change of Control"), Keystone ULC will have the obligation to make an offer to repurchase all or any part of a Holder's Subordinated Notes at a purchase price in cash equal to 101% of the principal amount thereof, plus accrued and unpaid interest, if any, to the date of repurchase (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date): (i) the adoption of a plan relating to the liquidation or dissolution of Keystone ULC, Keystone North America or Keystone, (ii) the acquisition by any Person or group of a direct or indirect interest in securities representing more than 50% of the voting power of the Voting Stock of Keystone ULC, Keystone North America or Keystone, by way of purchase, merger or consolidation or otherwise (other than the creation of a holding company that does not involve a change in the beneficial ownership of Keystone ULC, Keystone North America or Keystone, as the case may be, as a result of such transaction), or (iii) the merger or consolidation of Keystone ULC, Keystone North America or Keystone with or into another Person or the merger of another Person into Keystone ULC, Keystone North America or Keystone with the effect that immediately after such transaction the shareholders of Keystone ULC, Keystone North America or Keystone, as the case may be, immediately prior to such transaction hold, directly or indirectly, less than 50% of the total voting rights of all securities generally entitled to vote in the election of directors, managers, or trustees of the Person surviving such merger or consolidation, in each case other than the creation of a holding company that does not involve a change in the beneficial ownership of Keystone ULC, Keystone North America or Keystone as a result of such transaction.

Future Senior Indebtedness of Keystone ULC may contain prohibitions on certain events which would constitute a Change of Control or require Keystone ULC to repay or repurchase, or to make an offer to repurchase, such Senior Indebtedness upon a Change of Control. The Senior Indebtedness may prohibit any purchase by Keystone ULC of the Subordinated Notes. Moreover, the exercise by the Holders of their right to require Keystone ULC to repurchase the Subordinated Notes could cause a default under other Senior Indebtedness, even if the Change of Control itself does not, due to the financial effect of such repurchase on Keystone ULC. Keystone ULC's ability to pay cash to the Holders upon a repurchase may be limited by Keystone ULC's then existing financial resources and the terms of any Senior Indebtedness then in effect. There can be no assurance that sufficient funds will be available when necessary to make any repurchases. See "Risk Factors".

If at the time of such Change of Control the terms of any Senior Indebtedness restrict or prohibit the repurchase by Keystone ULC of Subordinated Notes pursuant to this covenant, then prior to the mailing of the notice to Holders provided for in the immediately following paragraph but in any event within 30 days following any Change of Control, Keystone ULC shall (i) repay in full all Senior Indebtedness or offer to repay in full all Senior Indebtedness and repay the Senior Indebtedness of each lender who has accepted such offer, or (ii) obtain the requisite consent under the agreements governing the Senior Indebtedness to permit Keystone ULC to make an offer to repurchase the Subordinated Notes as provided for in the immediately following paragraph.

Within 30 days following any Change of Control, unless Keystone ULC has exercised its right to redeem all of a particular Holder's Subordinated Notes as described above under "— Optional Redemption", in which case the following provisions shall not apply to such Holder (an "Excluded Holder") Keystone ULC will mail a notice (a "Change of Control Offer") to each Holder with a copy to the Trustee stating: (i) that a Change of Control has occurred, together with an offer to purchase the Subordinated Notes of each Holder who is not an Excluded Holder at a purchase price in cash equal to 101% of the principal amount thereof, plus accrued and unpaid interest, if any, to the date of purchase (subject to the right of Holders of record on a record date to receive interest on the relevant interest payment date); (ii) the circumstances and relevant facts and financial information regarding such Change of Control; (iii) the repurchase date (which will be no earlier than 30 days nor later than 60 days from the date such notice is mailed); and (iv) the instructions determined by Keystone ULC, consistent with this covenant, that a Holder must follow in order to have its Subordinated Notes purchased. A holder of IPSs will not be able to have its Subordinated Notes purchased unless the Holder surrenders the IPSs to the applicable depositary and receives delivery of the Common Shares and Subordinated Notes represented thereby.

Keystone ULC will not be required to make a Change of Control Offer upon a Change of Control if (i) a third party makes the Change of Control Offer in the manner, at the times and otherwise in compliance with the requirements set forth in the Indenture applicable to a Change of Control Offer made by Keystone ULC and purchases all Subordinated Notes validly tendered and not withdrawn under such Change of Control Offer, or (ii) issues a redemption notice in compliance with the requirements set forth in the Indenture with respect to all of the Subordinated Notes and redeems such Subordinated Notes on the redemption date specified in the redemption notice.

**Recombination of Notes and Common Shares into IPSs**

The Indenture will provide that as long as any Subordinated Notes are outstanding, any Holder of Subordinated Notes and Common Shares may after the 45th day following the Closing Date, at any time and from time to time prior to an automatic separation of the IPSs, recombine these securities to form IPSs.

**Certain Covenants**

The Indenture will contain covenants including, among others, the covenants listed below.

*Limitation on Incurrence of Indebtedness and Issuance of Disqualified Stock and Preferred Stock.* The Indenture will provide that Keystone ULC and Keystone will not, and will not permit any of their Subsidiaries to, directly or indirectly, Incur any Indebtedness or issue any shares of Disqualified Stock or Preferred Stock; *provided, however*, that Keystone ULC and Keystone or any of their Subsidiaries may Incur Indebtedness or issue shares of Disqualified Stock or Preferred Stock if the ratio of Total Funded Debt at the end of the most recently ended full fiscal quarter to Adjusted EBITDA for the most recently ended four full fiscal quarters of Keystone for which internal financial statements are available immediately preceding the date on which such additional Indebtedness is Incurred or such Disqualified Stock or Preferred Stock is issued would have been less than 5.5 to 1.0 ( the "Debt-to-EBITDA Ratio") determined on a *pro forma* basis (including a *pro forma* application of the net proceeds therefrom), as if the additional Indebtedness had been Incurred or the Disqualified Stock or Preferred Stock had been issued, as the case may be, and the application of proceeds therefrom had occurred at the beginning of such four-quarter period.

The foregoing limitations will not apply to:

(a) the Incurrence by Keystone ULC, Keystone or any Subsidiary of Indebtedness pursuant to the New Credit Facility in an amount not to exceed $85 million;

(b) the Incurrence by Keystone ULC and the Guarantors of Indebtedness represented by the Subordinated Notes and Separate Subordinated Notes issued on Closing and the Guarantees and in connection with the exercise by the Underwriters of the over-allotment option;

(c) Indebtedness, Disqualified Stock or Preferred Stock existing on the Closing Date;

(d) Indebtedness to be issued in the form of Additional Subordinated Notes (and the related issuance by Keystone of preferred shares) upon the repurchase of any Class B or C common shares of Keystone;

(e) Indebtedness arising from agreements of Keystone ULC, Keystone or any Subsidiary providing for indemnification, adjustment of purchase price, earn out or similar obligations, in each case, Incurred in connection with the acquisition or disposition of any business, assets or a Subsidiary of Keystone ULC or Keystone in accordance with the terms of the Indenture, other than guarantees of Indebtedness Incurred by any Person acquiring all or any portion of such business, assets or Subsidiary for the purpose of financing such acquisition;

(f) the Incurrence by Keystone or any of its Subsidiaries of any Indebtedness in the form of Seller Debt in an amount not to exceed $5 million, provided that such Seller Debt shall be unsecured and subordinated to the Obligations of Keystone or any of its Subsidiaries under the New Credit Facility;

(g) Indebtedness of Keystone ULC or Keystone to a Subsidiary; provided that any such Indebtedness is subordinated in right of payment to the Subordinated Notes; *provided further* that any subsequent issuance or transfer of any Capital Stock or any other event which results in any such Subsidiary ceasing to be a Subsidiary or any other subsequent transfer of any such Indebtedness (except to Keystone ULC, Keystone, or another Subsidiary) will be deemed, in each case, to be an Incurrence of such Indebtedness;

(h) Indebtedness of a Subsidiary of Keystone ULC or Keystone to Keystone ULC or Keystone or another Subsidiary; *provided* that (i) any such Indebtedness is made pursuant to an intercompany note, and (ii) if a Guarantor Incurs such Indebtedness to a Subsidiary that is not a Guarantor such Indebtedness is subordinated in right of payment to the Guarantee of such Guarantor; *provided further* that any subsequent issuance or transfer of any Capital Stock or any other event which results in any Subsidiary lending such Indebtedness ceasing to be a Subsidiary or any other subsequent transfer of any such Indebtedness (except to Keystone ULC, Keystone or another Subsidiary) will be deemed, in each case, to be an Incurrence of such Indebtedness;

(i) Hedging Obligations that are incurred in the ordinary course of business (i) for the purpose of fixing or hedging interest rate risk with respect to any Indebtedness that is permitted by the terms of the

Indenture to be outstanding, (ii) for the purpose of fixing or hedging currency exchange rate risk with respect to any currency exchanges, or (iii) for the purpose of fixing or hedging commodity price risk with respect to any commodity purchases;

(j) any guarantee by Keystone ULC, Keystone or a Guarantor of Indebtedness or other obligations of Keystone ULC, Keystone or any Subsidiary so long as the Indebtedness by Keystone ULC, Keystone or such Subsidiary is permitted under the terms of the Indenture; provided that if such Indebtedness is by its express terms subordinated in right of payment to the Subordinated Notes or the Guarantee of such Subsidiary, as applicable, any such guarantee of such Guarantor with respect to such Indebtedness will be subordinated in right of payment to such Guarantor's Guarantee with respect to the Subordinated Notes substantially to the same extent as such Indebtedness is subordinated to the Subordinated Notes or the Guarantee of such Subsidiary, as applicable;

(k) the Incurrence by Keystone ULC, Keystone or any Subsidiary of any of Indebtedness which serves to refund or refinance any Indebtedness Incurred as permitted under the first paragraph of this covenant and clauses (a), (b), (c) and (d) above and (l) and (p) below, or any Indebtedness issued to so refund or refinance such Indebtedness (subject to the following proviso, "Refinancing Indebtedness") prior to its respective maturity, *provided, however*, that such Refinancing Indebtedness:

  (i) has a Weighted Average Life to Maturity at the time such Refinancing Indebtedness is Incurred which is not less than the remaining Weighted Average Life to Maturity of the Indebtedness being refunded or refinanced;

  (ii) has a Stated Maturity which is no earlier than the Stated Maturity of the Indebtedness being refunded or refinanced or the Stated Maturity of the Notes;

  (iii) to the extent such Refinancing Indebtedness refinances Indebtedness *pari passu* with the Subordinated Notes or the Guarantees, is *pari passu* with or subordinated to the Subordinated Notes or Guarantees, as applicable; and

  (iv) is Incurred in an aggregate amount (or if issued with original issue discount, an aggregate issue price) that is equal to or less than the aggregate principal amount (or if issued with original issue discount, the aggregate accreted value) then outstanding of the Indebtedness being refinanced plus premium, prepayment penalties, costs, expenses and fees Incurred in connection with such refinancing;

provided that clauses (i) and (ii) of this sub-paragraph (k) shall not apply to any refunding of the New Credit Facility;

(l) Indebtedness of Persons that are acquired by Keystone ULC, Keystone or a Subsidiary merged into a Subsidiary in accordance with the terms of the Indenture; *provided, however*, that such Indebtedness is not Incurred in contemplation of such acquisition or to provide all or a portion of the funds or credit support required to consummate such acquisition or merger; *provided further, however*, that after giving effect to such acquisition and the Incurrence of such Indebtedness on a *pro forma* basis either (i) Keystone would be permitted to Incur at least $1.00 of additional Indebtedness pursuant to the Debt-to-EBITDA Ratio set forth in this covenant or (ii) the Interest Coverage Ratio for the preceding period on a *pro forma* basis, after giving effect to such acquisition and the Incurrence of such Indebtedness, would be greater than the actual Interest Coverage Ratio for such period without giving effect to such acquisition;

(m) the incurrence by Keystone ULC, Keystone or any of its Subsidiaries of Indebtedness represented by Capital Lease Obligations, mortgage financings or purchase money obligations, or other Indebtedness in each case, incurred for the purpose of financing all or any part of the purchase price or cost of construction or improvement of property (real or personal), plant, vehicles or equipment used in the business of Keystone ULC, Keystone or such Subsidiary (whether through the direct purchase of assets or the Capital Stock of any Person owning such assets), in an aggregate principal amount, including all Refinancing Indebtedness incurred to refund, refinance or replace any Indebtedness incurred pursuant to this clause (m), not to exceed at any time outstanding $25 million;

(n) the incurrence by Keystone ULC, Keystone or any of its Subsidiaries of Indebtedness constituting reimbursement obligations with respect to letters of credit issued in the ordinary course of business, including, without limitation, letters of credit in respect of workers' compensation claims of self-insurance, or other Indebtedness with respect to reimbursement type obligations regarding workers' compensation claims or self insurance; *provided, however*, that, in each case, upon the drawing of such letters of credit or the incurrence of such Indebtedness, such obligations are reimbursed within 30 days following such drawing or incurrence;

(o) the incurrence by Keystone ULC, Keystone or any of its Subsidiaries of obligations in respect of performance and surety bonds and completion guarantees provided by Keystone ULC, Keystone or such Subsidiaries in the ordinary course of business;

(p) the incurrence by Keystone ULC, Keystone or any of its Subsidiaries of additional Indebtedness in an aggregate amount (or accreted value, as applicable) at any time outstanding, including all Refinancing Indebtedness incurred to refund, refinance or replace any Indebtedness incurred pursuant to this clause (p), not to exceed $20 million; and

(q) Indebtedness arising from the honouring by a bank or other financial institution of a check, draft or similar instrument inadvertently drawn against insufficient funds in the ordinary course of business; *provided, however*, that such Indebtedness is extinguished within five business days of incurrence.

For purposes of determining compliance with this covenant, in the event that an item of Indebtedness meets the criteria of more than one of the categories of permitted Indebtedness described in clauses (a) through (q) above or is entitled to be Incurred pursuant to this covenant, Keystone ULC will, in its sole discretion, classify or reclassify such item of Indebtedness in any manner that complies with this covenant and such item of Indebtedness will be treated as having been Incurred pursuant to only one of such clauses. Accrual of interest, the accretion of accreted value or amortization at original issue discount, the payment of interest on any Indebtedness in the form of additional Indebtedness with the same terms, and the payment of dividends on Disqualified Stock in the form of additional shares of the same class of Disqualified Stock will not be deemed to be an Incurrence of Indebtedness for purposes of this covenant.

*Limitation on Restricted Payments.* The Indenture will provide that Keystone ULC and Keystone will not, and shall not permit any of their Subsidiaries to, directly or indirectly:

(i) declare or pay any dividend or make any distribution on account of Keystone ULC's, Keystone's or any Subsidiary's Equity Interests, including any payment made in connection with any merger or consolidation involving Keystone ULC or Keystone (other than (A) dividends or distributions by Keystone ULC or Keystone payable solely in Equity Interests (other than Disqualified Stock) of Keystone ULC or Keystone or (B) dividends or distributions by a Subsidiary so long as, in the case of any dividend or distribution payable on or in respect of any class or series of securities issued by a Subsidiary other than a Wholly-Owned Subsidiary, Keystone ULC or Keystone or a Subsidiary receives at least its *pro rata* share of such dividend or distribution in accordance with the terms of such Equity Interests), provided that for the purposes of the foregoing, Keystone shall be considered to be a Subsidiary of Keystone ULC; or

(ii) purchase or otherwise acquire or retire for value any Equity Interests of Keystone ULC or Keystone, other than repurchases of the Class B or C common shares by the Company in connection with a Repurchase Event and/or any redemption of the preferred shares of Keystone held by Keystone ULC; or

(iii) make a Restricted Investment;

(all such payments and other actions set forth in clauses (i), (ii) and (iii) above being collectively referred to as "Restricted Payments"), unless, at the time of such Restricted Payment:

(a) no Default or Event of Default will have occurred and be continuing or would occur as a consequence thereof;

(b) (i) no Interest Deferral Period with respect to the Subordinated Notes is in effect and (ii) there is no interest deferred during any Interest Deferral Period (including interest thereon) that remains unpaid; and

(c) such Restricted Payment, together with the aggregate amount of all other Restricted Payments made by Keystone ULC, Keystone and their Subsidiaries after the Closing Date (including Restricted Payments permitted by clauses (1), (3), (4), (5) and (6) of the next succeeding paragraph, but excluding all other Restricted Payments permitted by the next succeeding paragraph), is less than the sum of, without duplication:

(i) 100% of the Excess Cash of Keystone (calculated in accordance with the Indenture) for the period (taken as one accounting period) from the first date of the fiscal quarter in which the Closing Date occurs to the end of Keystone's most recently ended fiscal quarter for which internal financial statements are available at the time of such Restricted Payment, plus

(ii) 100% of the aggregate net proceeds, including cash and the Fair Market Value (as determined in accordance with the next paragraph) of property other than cash, received by Keystone after the Closing Date from the issue or sale of Equity Interests of Keystone (subject to certain exceptions), including Equity Interests issued upon conversion of Indebtedness or upon exercise of warrants or options (other than an issuance or sale to a Subsidiary of Keystone or to Keystone ULC or to Keystone North America), plus

(iii) 100% of the aggregate amount of contributions to the capital of Keystone received in cash and the Fair Market Value (as determined in accordance with the next paragraph) of property other than cash received by Keystone as a contribution to capital after the Closing Date (subject to certain exceptions), plus

(iv) 100% of the aggregate amount received in cash and the Fair Market Value (as determined in accordance with the next paragraph) of property other than cash received from (A) the sale or other disposition (other than to Keystone ULC, Keystone, Keystone North America or a Subsidiary) of Restricted Investments made by Keystone and any Subsidiary and from repurchases and redemptions of such Restricted Investments from Keystone and any Subsidiary by any Person (other than Keystone ULC, Keystone, Keystone North America or a Subsidiary) and from repayments of loans or advances which constituted Restricted Investments, and (B) the sale (other than to Keystone ULC, Keystone, Keystone North America or a Subsidiary) of the Capital Stock of a Subsidiary.

The Fair Market Value of property other than cash referred to in clauses (ii), (iii) and (iv) above will be determined in good faith by Keystone ULC and (A) in the case of property with a Fair Market Value in excess of $5 million, shall be set forth in an officers' certificate or (B) in the case of property with a Fair Market Value in excess of $10 million, shall be set forth in a resolution approved by at least a majority of the board of directors.

The foregoing provisions of this covenant will not prohibit:

1. the payment of any dividend or distribution within 60 days after the date of declaration thereof, if at the date of declaration such payment would have been permitted under the provisions of the Indenture;

2. (a) the repurchase, retirement or other acquisition of any Equity Interests ("Retired Capital Stock") or Subordinated Indebtedness of Keystone ULC in exchange for, or out of the proceeds of the substantially concurrent sale of, Equity Interests of Keystone ULC or Keystone or any of their respective Subsidiaries or contributions to the equity capital of Keystone ULC, the Company or any of their respective Subsidiaries (other than any Disqualified Stock or any Equity Interests sold to a Subsidiary or to an employee stock ownership plan or any trust established by Keystone ULC or Keystone or any of their respective Subsidiaries) (collectively, including any such contributions, "Refunding Capital Stock"); and (b) the declaration and payment of accrued dividends on the Retired Capital Stock out of the proceeds of the substantially concurrent sale (other than to a Subsidiary of the Issuer or to an employee stock ownership plan or any trust established by Keystone ULC, the Company or any of their respective Subsidiaries) of Refunding Capital Stock;

3. the declaration and payment of dividends or distributions to holders of any class or series of Disqualified Stock of Keystone ULC, Keystone or any of their respective Subsidiaries issued or incurred in accordance with the covenant entitled "— Limitation on Incurrence of Indebtedness and Issuance of Disqualified Stock and Preferred Stock";

4. the declaration and payment of dividends or distributions to holders of any class or series of Preferred Stock issued in accordance with the covenant entitled "— Limitation on Incurrence of Indebtedness and Issuance of Disqualified Stock and Preferred Stock" or on the preferred shares of Keystone held by Keystone ULC;

5. other Restricted Payments in an aggregate amount specified in the Indenture which may not exceed $5 million, provided that any amounts paid pursuant to this clause that subsequently would have become eligible to be paid out pursuant to clause (7), may be excluded from this calculation at that time;

6. repurchases of Equity Interests deemed to occur upon exercise of stock options if such Equity Interests represent a portion of the exercise price of such options;

7. the payment of dividends on the common shares of Keystone to the extent permitted but not previously paid;

8. the repurchase, redemption or other acquisition or retirement for value of any Equity Interests held by any, or any pension entitlement of, former or current employees, officers, directors or consultants of Keystone ULC, Keystone or any of their Subsidiaries or their respective estates, spouses or family members under any management equity plan or stock option or other management or employee benefit plan, in an aggregate amount not to exceed $5 million in any calendar year pursuant to this clause (8); *provided* that Keystone ULC, Keystone or any of their Subsidiaries may carry forward and make in a subsequent calendar year, in addition to the amounts permitted for such calendar year, the amount of such purchases, redemptions or other acquisitions or retirements for value permitted to have been made but not made in any preceding calendar year up to a maximum of $5 million in any calendar year pursuant to this clause (8); and *provided further*, that such amount in any calendar year may be increased by the cash proceeds of key man life insurance policies received by Keystone ULC, Keystone and their Subsidiaries after the date of the Indenture less any amount previously applied to the payment of Restricted Payments pursuant to this clause (8); *provided further*, that cancellation of the Indebtedness owing to Keystone ULC, Keystone or any of their Subsidiaries from employees, officers, directors and consultants of Keystone or any of its Subsidiaries in connection with a repurchase of Equity Interests from such Persons will not be deemed to constitute a Restricted Payment for purposes of this covenant or any other provisions of the Indenture;

9. dividends or distributions solely in the form of Equity Interests or repurchases of Equity Interests which may be deemed to occur upon exchange or exercise of other outstanding Equity Interests;

10. the redemption, repurchase or other acquisition for value of Capital Stock of Keystone representing fractional shares of such capital stock in connection with a merger, consolidation, amalgamation or other combination involving Keystone; and

11. any Restricted Payment made in connection with the transactions as described in this prospectus, including, without limitation, any restricted payment made in connection with the exercise of the underwriters of the over-allotment option;

*provided, however* that at the time of and after giving effect to, any Restricted Payment permitted under clauses (1), (3), (4), (5), (6), (7) and (9), no Default or Event of Default shall have occurred and be continuing or would occur as a consequence thereof, no Interest Deferral Period with respect to the Subordinated Notes is in effect, and there is not any interest deferred during any Interest Deferral Period (including interest thereon) that remains unpaid.

*Dividend and Other Payment Restrictions Affecting Subsidiaries.* The Indenture will provide that Keystone ULC and Keystone will not, and will not permit (to the extent that any of their indirect approval rights are triggered) any of their Subsidiaries to, directly or indirectly, create or otherwise cause or suffer to exist or become effective any consensual encumbrance or consensual restriction on the ability of their respective Subsidiaries to:

(a) (i) pay dividends or make any other distributions to Keystone ULC, Keystone or any Subsidiary (1) on its Capital Shares, or (2) with respect to any other interest or participation in, or measured by, its profits, or (ii) pay any Indebtedness owed to Keystone ULC, the Company or any Subsidiary;

(b) make loans or advances to Keystone ULC, Keystone or any Subsidiary; or

(c) sell, lease or transfer any of its properties or assets to Keystone ULC, Keystone or any Subsidiary;

except in each case for such encumbrances or restrictions existing under or by reason of:

(i) contractual encumbrances or restrictions in effect on the Closing Date, including pursuant to the New Credit Facility;

(ii) the Indenture and the Subordinated Notes;

(iii) applicable law or any applicable rule, regulation or order;

(iv) any agreement or other instrument relating to Indebtedness of a Person acquired by Keystone ULC, Keystone or any Subsidiary which was in existence at the time of such acquisition (but not created in contemplation thereof or to provide all or any portion of the funds or credit support utilized to consummate such acquisition), which encumbrance or restriction is not applicable to any Person, or the properties or assets of any Person, other than the Person, or the property or assets of the Person, so acquired;

(v) any restriction with respect to a Subsidiary imposed pursuant to an agreement entered into for the sale or disposition of all or substantially all the Capital Stock or assets of such Subsidiary pending the closing of such sale or disposition;

(vi) Secured Indebtedness otherwise permitted to be Incurred pursuant to the covenants described under "— Limitations on Incurrence of Indebtedness and Issuance of Disqualified Stock and Preferred Stock" that limit the right of the debtor to dispose of the assets securing such Indebtedness;

(vii) restrictions on cash or other deposits or net worth imposed by customers under contracts entered into in the ordinary course of business;

(viii) customary provisions in joint venture agreements, limited partnership agreements and other similar agreements entered into in the ordinary course of business;

(ix) customary provisions contained in leases and other similar agreements entered into in the ordinary course of business;

(x) purchase money obligations for property acquired in the ordinary course of business that impose restrictions on that property of the nature described in clause (c) of the preceding paragraph;

(xi) Refinancing Indebtedness, provided that the restrictions contained in the agreements governing such Refinancing Indebtedness are no more restrictive, taken as a whole, than those contained in the agreements governing the Indebtedness being refinanced;

(xii) Indebtedness incurred after the date of the Indenture in accordance with the terms of the Indenture; provided that the restrictions contained in the agreements governing the new Indebtedness are, in the good faith judgment of the board of directors of Keystone, not materially less favourable, taken as a whole, to the Holders of the Subordinated Notes than those contained in the agreements governing Indebtedness that were in effect on the date of the Indenture; or

(xiii) any encumbrances or restrictions of the type referred to in clauses (a), (b) and (c) above imposed by any amendments, modifications, restatements, renewals, increases, supplements, refundings, replacements or refinancings of the contracts, instruments or obligations referred to in clauses (i) through (xii) above; provided that such amendments, modifications, restatements, renewals, increases, supplements, refundings, replacements or refinancings are, in the good faith judgment of the board of directors, no more restrictive with respect to such dividend and other payment restrictions than those contained in the dividend or other payment restrictions prior to such amendment, modification, restatement, renewal, increase, supplement, refunding, replacement or refinancing.

*Asset Sales.* The Indenture will provide that Keystone ULC and Keystone will not, and will not permit any of their Subsidiaries to cause or make an Asset Sale, unless Keystone ULC, Keystone or such Subsidiary, as the case may be, receives consideration at the time of such Asset Sale at least equal to the Fair Market Value (as determined in good faith by Keystone ULC, the Company or such Subsidiary, as the case may be) of the assets sold.

Within 18 months after the receipt of the net proceeds of any Asset Sale, Keystone ULC, Keystone or such Subsidiary shall apply the net proceeds from such Asset Sale, at its option:

(i) to permanently reduce Obligations under Senior Indebtedness or Indebtedness of a Subsidiary, in each case other than Indebtedness owed to Keystone ULC, Keystone or an affiliate of Keystone ULC or Keystone;

(ii) to make an investment in any one or more businesses, capital expenditures or acquisitions of other assets in each case used or useful in a similar business; and/or

(iii) to make an investment in properties or assets that replace the properties and assets that are the subject of such Asset Sale.

Pending the final application of any such net proceeds, Keystone ULC, Keystone or such Subsidiary may temporarily reduce Indebtedness under a revolving credit facility, if any, or otherwise invest such net proceeds in cash equivalents or Investment Grade Securities. The Indenture will provide that any net proceeds from any Asset Sale that are not applied as provided and within the time period set forth in the first sentence of the prior paragraph will be deemed to constitute "Excess Proceeds". When the aggregate amount of Excess Proceeds exceeds $15 million, Keystone ULC will have the obligation to make an offer to all Holders of Subordinated Notes (an "Asset Sale Offer") to purchase the maximum principal amount of Subordinated Notes that may be purchased out of the Excess Proceeds at an offer price in cash in an amount equal to the lesser of (i) 105% of the principal amount, and (ii) the redemption amount at such date, plus accrued and unpaid interest, if any, to but not including the date fixed for the closing of such offer, in accordance with the procedures set forth in the Indenture. A holder of IPSs will not be able to have its Subordinated Notes purchased under an Asset Sale Offer unless the Holder separates the IPS and receives delivery of the Common Shares and Subordinated Notes represented thereby.

Notices of an Asset Sale Offer shall be mailed by first class mail, postage prepaid, at least 30 but not more than 60 days before the purchase date to each Holder of Subordinated Notes at such Holder's registered address. If any subordinated note is to be purchased in part only, any notice of purchase that relates to such subordinated note shall state the portion of the principal amount thereof that has been or is to be purchased.

A new subordinated note in principal amount equal to the unpurchased portion of any subordinated note purchased in part will be issued in the name of the Holder thereof upon cancellation of the original subordinated note. On and after the purchase date, unless the Issuer defaults in payment of the purchase price, interest shall cease to accrue on Subordinated Notes or portions thereof purchased.

The terms of any Senior Indebtedness of Keystone ULC, Keystone or their Subsidiaries may prohibit the completion of sales and/or the application of the proceeds of sales as provided in the Indenture.

*Transactions with Affiliates.* The Indenture will provide that Keystone ULC and Keystone will not, and will not permit any of their Subsidiaries to, directly or indirectly, make any payment to, or sell, lease, transfer or otherwise dispose of any of its properties or assets to, or purchase any property or assets from, or enter into or make or amend any transaction or series of transactions, contract, agreement, understanding, loan, advance or guarantee with, or for the benefit of, any affiliate of Keystone ULC or Keystone (each of the foregoing, an "Affiliate Transaction") involving aggregate consideration in excess of $2 million, unless:

(a) such Affiliate Transaction is on terms that are not materially less favourable to Keystone ULC or Keystone or the relevant Subsidiary than those that could have been obtained in a comparable transaction by Keystone ULC or Keystone or such Subsidiary with an unrelated Person; and

(b) with respect to any Affiliate Transaction or series of related Affiliate Transactions involving aggregate consideration in excess of $5 million, Keystone ULC delivers to the Trustee a resolution adopted by the majority of the board of directors of Keystone ULC, approving such Affiliate Transaction and an officers' certificate certifying that such Affiliate Transaction complies with clause (a) above.

The foregoing provisions will not apply to the following:

(i) Permitted Investments and Restricted Payments permitted by the provisions of the Indenture described above under the covenant "— Limitation on Restricted Payments";

(ii) the payment of reasonable and customary fees paid to, and indemnity provided on behalf of, officers, directors, employees or consultants of Keystone ULC, Keystone, or any Subsidiary;

(iii) transactions in which Keystone ULC, Keystone, or any of their Subsidiaries, as the case may be, delivers to the Trustee a letter from an independent financial advisor of recognized standing stating that such transaction is fair to Keystone ULC, Keystone, or such Subsidiary from a financial point of view or meets the requirement of clause (a) of the preceding paragraph (provided that the requirements of clause (b) must be met, if applicable);

(iv) payments or loans to employees or consultants in the ordinary course of business which are approved by a majority of the board of directors of Keystone or Keystone ULC in good faith;

(v) any agreement as in effect as of the Closing Date or any amendment thereto (so long as any such amendment is not disadvantageous to the Holders of the Subordinated Notes in any material respect) or any transaction contemplated thereby;

(vi) the existence of, or the performance by Keystone ULC, Keystone, or any Subsidiary of its obligations under the terms of, any shareholders agreement (including any registration rights agreement or purchase agreement related thereto) to which it is a party as of the Closing Date and any similar agreements (including any operating agreements or limited partnership agreements) which it may enter into thereafter; *provided, however* that the existence of, or the performance by Keystone ULC, Keystone, or any Subsidiary of its obligations under any future amendment to any such existing agreement or under any similar agreement entered into after the Closing Date shall only be permitted by this clause (vi) to the extent that the terms of any such amendment or new agreement are not otherwise disadvantageous to the Holders of the Subordinated Notes in any material respect;

(vii) any employment agreement or other compensation arrangements or agreements entered into by Keystone or any of its Subsidiaries in the ordinary course of business of Keystone or such Subsidiary;

(viii) transactions between or among Keystone, Keystone ULC and any of their Subsidiaries;

(ix) transactions with a Person that is an Affiliate of Keystone ULC, Keystone or any of their Subsidiaries solely because Keystone, Keystone ULC or one or more of its Subsidiaries owns an Equity Interest in, or controls, such Person;

(x) issuances of Equity Interests (other than Disqualified Stock) to affiliates of Keystone; and

(xi) transactions entered into in connection with the transactions described in this prospectus.

*Liens.* The Indenture will provide that Keystone ULC and Keystone will not and will not permit any Subsidiary to, directly or indirectly, create, Incur or suffer to exist any Lien on any asset or property of Keystone ULC, Keystone, or such Subsidiary, or any income or profits therefrom, or assign or convey any right to receive income therefrom, that secures any obligations of Keystone ULC, Keystone, or any of their

Subsidiaries or any other Person (other than Senior Indebtedness) unless the subordinated notes are equally and ratably secured with (or on a senior basis to, in the case of obligations subordinated in right of payment to the subordinated notes) the obligations so secured or until such time as such obligations are no longer secured by a Lien. The preceding sentence will not require Keystone ULC, Keystone or any Subsidiary to secure the subordinated notes if the Lien consists of a Permitted Lien.

The Indenture will provide that no Guarantor will directly or indirectly create, Incur or suffer to exist any Lien on any asset or property of such Guarantor or any income or profits therefrom, or assign or convey any right to receive income therefrom, that secures any obligation of such Guarantor or any other Person (other than Senior Indebtedness) unless the Guarantee of such Guarantor of the Subordinated Notes is equally and ratably secured with (or on a senior basis to, in the case of obligations subordinated in right of payment to such Guarantor's Guarantee of the Subordinated Notes) the obligations so secured or until such time as such obligations are no longer secured by a Lien. The preceding sentence will not require any Guarantor to secure its Guarantee of the Subordinated Notes, if the Lien consists of a Permitted Lien.

*Reporting Obligations.* The Indenture will provide that Keystone ULC deliver to the Trustee within 90 days after the end of each fiscal year of Keystone ULC and 45 days after the end of each fiscal quarter (other than the last fiscal quarter) of each fiscal year, a consolidated balance sheet of Keystone North America and related statements of income and changes in financial position for the fiscal year or fiscal quarter and year-to-date, as applicable in accordance with Canadian GAAP (audited with respect to annual financial statements). Keystone ULC will also be subject to other customary reporting obligations including the delivery of officer's certificates in respect of the occurence of default under the Indenture.

**Merger, Consolidation, or Sale of All or Substantially All Assets**

The Indenture will provide that Keystone ULC and Keystone may not consolidate or merge with or into or wind up into (whether or not Keystone ULC or Keystone is the surviving corporation), or sell, assign, transfer, lease, convey or otherwise dispose of all or substantially all of its properties or assets in one or more related transactions, to any Person unless:

(i) Keystone ULC or Keystone, as the case may be, is the surviving corporation or the Person formed by or surviving any such consolidation or merger (if other than Keystone ULC) or to which such sale, assignment, transfer, lease, conveyance or other disposition will have been made is a corporation, partnership or limited liability company organized or existing under the laws of Canada or any province or territory thereof (Keystone ULC, Keystone or such Person, as the case may be, being herein called the "Successor Issuer");

(ii) the Successor Issuer (if other than Keystone ULC or Keystone) expressly assumes all the obligations of Keystone ULC or Keystone, as the case may be, under the Indenture and the Subordinated Notes pursuant to a supplemental indenture or other documents or instruments in form reasonably satisfactory to the Trustee;

(iii) immediately after giving effect to such transaction (and treating any Indebtedness which becomes an obligation of the Successor Issuer or any of its Subsidiaries as a result of such transaction as having been Incurred by the Successor Issuer or such Subsidiary at the time of such transaction) no Default or Event of Default will have occurred and be continuing;

(iv) immediately after giving *pro forma* effect to such transaction, as if such transaction had occurred at the beginning of the applicable four-quarter period, either (A) the Successor Issuer would be permitted to Incur at least $1.00 of additional Indebtedness pursuant to the Debt-to-EBITDA Ratio or (B) the Interest Coverage Ratio for the Successor Issuer and its Subsidiaries would be greater than or equal to such ratio for the Company and its Restricted Subsidiaries immediately prior to such transaction;

(v) each party to the Subordinated Notes and Guarantees, unless they are the other party to the transactions described above, will have by supplemental notes and guarantees confirmed that such notes and guarantees will apply to such Person's obligations under the Subordinated Notes and

Guarantees (or, such parties will have entered into guarantees of the Subordinated Notes in form and substance substantially the same as the Guarantees); and

(vi) Keystone ULC will have delivered to the Trustee an officers' certificate or an opinion of legal counsel stating that such consolidation, merger or transfer and such supplemental notes and guarantees (or guarantees of the Subordinated Notes) comply with the Indenture.

The Successor Issuer will succeed to, and be substituted for, Keystone ULC or Keystone under the Indenture and the Subordinated Notes. Notwithstanding the foregoing clauses (iii) and (iv), (a) any Subsidiary may consolidate with, merge into or transfer all or part of its properties and assets to Keystone ULC or to another Subsidiary and (b) Keystone ULC or Keystone may merge with an affiliate incorporated solely for the purpose of reincorporating Keystone ULC or Keystone in another province or territory of Canada so long as the amount of Indebtedness of Keystone ULC and its Subsidiaries is not increased thereby.

The Indenture will further provide that, subject to certain limitations described in the Indenture governing release of a Guarantee upon the sale or disposition of a Guarantor, each Guarantor will not, and Keystone ULC and Keystone will not permit a Guarantor to, consolidate or merge with or into or wind up into (whether or not such Guarantor is the surviving corporation), or sell, assign, transfer, lease, convey or otherwise dispose of all or substantially all of its properties or assets in one or more related transactions to, any Person unless:

(i) such Guarantor is the surviving corporation or the Person formed by or surviving any such consolidation or merger (if other than such Guarantor) or to which such sale, assignment, transfer, lease, conveyance or other disposition will have been made is a corporation, partnership or limited liability company organized or existing under the laws of Canada or the United States, or any province or territory of Canada or state of the United States (such Guarantor or such Person, as the case may be, being herein called the "Successor Guarantor");

(ii) the Successor Guarantor (if other than such Guarantor) expressly assumes all the obligations of such Guarantor under the Indenture and such Guarantor's guarantee pursuant to a supplemental indenture or other documents or instruments in form reasonably satisfactory to the Trustee;

(iii) immediately after giving effect to such transaction (and treating any Indebtedness which becomes an obligation of the Successor Guarantor or any of its Subsidiaries as a result of such transaction as having been Incurred by the Successor Guarantor or such Subsidiary at the time of such transaction) no Default or Event of Default shall have occurred and be continuing; and

(iv) the Guarantor shall have delivered or caused to be delivered to the Trustee an officers' certificate and opinion of legal counsel, stating that such consolidation, merger or transfer and such supplemental indenture (if any) comply with the Indenture.

Subject to certain limitations described in the Indenture, the Successor Guarantor will succeed to, and be substituted for, such Guarantor under the Indenture and such Guarantor's guarantee. Notwithstanding the foregoing clause (iii), a Guarantor may merge with an affiliate incorporated solely for the purpose of reincorporating such Guarantor in another state of the United States or province or territory of Canada so long as the amount of Indebtedness of the Guarantor is not increased thereby.

The Indenture shall not prohibit the merger of Mergersub with Keystone undertaken in connection with the closing of the transactions described under the headings "Investment Agreement" and "Post-Closing Structure".

**Defaults Under the Indenture**

An Event of Default will be defined in the Indenture as:

(i) a default in any payment of interest on any Subordinated Notes when due and continuing for 30 days, subject to the interest deferral provisions contained in the Indenture; *provided, however,* that a default in any payment of deferred interest on the Subordinated Notes required to be made on the fifth anniversary of the closing of the offering shall immediately constitute an Event of Default (without regard to length of time for which such default continues);

(ii) a default in the payment of principal or premium, if any, of any Subordinated Note when due at its maturity date, upon optional redemption, upon required repurchase, upon acceleration or otherwise or upon any extensions of the maturity date in accordance with the Indenture;

(iii) the failure by Keystone ULC or Keystone to comply with their respective obligations under the covenant described under "— Merger, Consolidation or Sale of All or Substantially All Assets" above, subject to certain grace and cure periods, as applicable;

(iv) the failure by Keystone ULC or Keystone to comply for 30 days after notice with any of their respective obligations under the covenants described under "— Change of Control" or "— Certain Covenants" above (in each case, other than a failure to purchase Subordinated Notes);

(v) the failure by Keystone ULC or Keystone to comply for 60 days after notice with its other agreements contained in the Subordinated Notes or the Indenture;

(vi) the failure by Keystone ULC, Keystone or any Major Subsidiary to pay any Indebtedness (other than Indebtedness owing to Keystone ULC, Keystone or a Subsidiary) within any applicable grace period after final maturity or the acceleration of any such Indebtedness by the holders thereof because of a default if the total amount of such Indebtedness unpaid or accelerated exceeds $10 million or its foreign currency equivalent (the "cross acceleration provision");

(vii) certain events of bankruptcy, insolvency or reorganization of Keystone ULC, Keystone or a Major Subsidiary (the "bankruptcy provisions");

(viii) the rendering of any judgment or decree for the payment of money (other than judgments which are covered by enforceable insurance policies issued by solvent carriers) in excess of $10 million or its foreign currency equivalent against Keystone ULC, Keystone or a Major Subsidiary if (A) an enforcement proceeding thereon is commenced and not discharged or stayed within 90 days thereafter or (B) such judgment or decree remains outstanding for a period of 60 days following such judgment and is not discharged, waived or stayed (the "judgment default provision");

(ix) the Subordinated Notes or any Guarantee therefor cease to be in full force and effect, except as contemplated by the terms thereof, or Keystone ULC, Keystone or any Guarantor denies or disaffirms its obligations under the Subordinated Notes or any Guarantee or any Security therefor, except as contemplated by the terms thereof, and the Default continues for 10 days;

(x) except as expressly provided by clause 1 under "— Limitation on Restricted Payments," Keystone pays any dividend on shares of its Capital Stock or purchases or otherwise acquires or retires for value any Equity Interests of Keystone ULC, Keystone or any other Subsidiary, other than the repurchase of the Class B or C common shares by Keystone in connection with a Repurchase Event (A) when, based on the then-available financial statements presented to the Board of Directors, such Restricted Payment exceeds the amount available to be paid pursuant to paragraph (c) or clauses 2 through 11 of the "— Limitation on Restricted Payments" covenant or (B) during any Interest Deferral Period or period when any interest deferred during any Interest Deferral Period (including interest thereon) remains unpaid or the continuance of a Default or an Event of Default; or

(xi) Keystone ULC fails to make an offer to repurchase as required under "— Asset Sales" or "Change of Control" above.

The foregoing will constitute Events of Default whatever the reason for any such Event of Default and whether it is voluntary or involuntary or is effected by operation of law or pursuant to any judgment, decree or order of any court or any order, rule or regulation of any administrative or governmental body.

However, a default under clause (iv) or (v) will not constitute an Event of Default until the Trustee or the Holders of 25% in principal amount of the outstanding Subordinated Notes (or Holders of a Reduced Threshold Amount in the case of a Reduced Threshold Default) notify Keystone ULC of the default and Keystone ULC does not cure such default within the time specified in clauses (iv) or (v) hereof after receipt of such notice.

If an Event of Default occurs and is continuing, the Subordinated Notes will bear an additional 2% of interest per annum until such time as the Event of Default has been cured.

Subject to any Acceleration Forbearance Periods during which the principal amount of the Subordinated Notes will not be due and payable by Keystone ULC or any Guarantor (see "Acceleration Forbearance Periods" above), if an Event of Default (other than a Default relating to certain events of bankruptcy, insolvency or reorganization of Keystone ULC or Keystone for which acceleration is automatic) occurs and is continuing, the Trustee or the Holders of at least 25% in principal amount of the outstanding Subordinated Notes (or Holders of a Reduced Threshold Amount for a Reduced Threshold Default) by notice to Keystone ULC may declare the principal of, premium, if any, and accrued but unpaid interest on all the Subordinated Notes to be due and payable. Upon such a declaration, such principal, premium and interest will be due and payable immediately. If an Event of Default relating to certain events of bankruptcy, insolvency or reorganization of Keystone ULC or Keystone occurs, the principal of, premium, if any, and interest on all the Subordinated Notes will become immediately due and payable without any declaration or other act on the part of the Trustee or any Holders. Under certain circumstances, the holders of a majority in principal amount of the outstanding Subordinated Notes may rescind any such acceleration with respect to the Subordinated Notes and its consequences.

Subject to the provisions of the Indenture relating to the duties of the Trustee, if an Event of Default occurs and is continuing, the Trustee will be under no obligation to exercise any of the rights or powers under the Indenture at the request or direction of any of the Holders unless such Holders have offered to the Trustee reasonable security and indemnification satisfactory to the Trustee against any loss, liability or expense. Except to preserve or enforce the right to receive payment of principal, premium (if any) or interest when due, no Holder may pursue any remedy with respect to the Indenture or the Subordinated Notes unless (i) such Holder has previously given the Trustee notice that an Event of Default is continuing, (ii) holders of at least 25% in principal amount of the outstanding Subordinated Notes (or at least a Reduced Threshold Amount in respect of a remedy (other than acceleration) for a Reduced Threshold Default) have requested the Trustee to pursue the remedy, (iii) such Holders have offered the Trustee reasonable security or indemnity against any loss, liability or expense, (iv) the Trustee has not complied with such request within 60 days after the receipt of the request and the offer of security or indemnity, and (v) except for a remedy (other than an acceleration) for a Reduced Threshold Default, the Holders of a majority in principal amount of the outstanding Subordinated Notes have not given the Trustee a direction inconsistent with such request within such 60-day period. Subject to certain restrictions, the holders of a majority in principal amount of the outstanding Subordinated Notes are given the right to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee or of exercising any trust or power conferred on the Trustee. The Trustee, however, may refuse to follow any direction that conflicts with law or the Indenture or that the Trustee determines is unduly prejudicial to the rights of any other Holder or that would involve the Trustee in personal liability. Prior to taking any action under the Indenture, the Trustee will be entitled to indemnification satisfactory to it in its sole discretion against all losses and expenses caused by taking or not taking such action.

The Indenture will provide that if a Default occurs and is continuing and is actually known to the Trustee, the Trustee must mail to each Holder notice of the Default within the earlier of 90 days after it occurs or 30 days after written notice of it is received by the Trustee. Except in the case of a Default in the payment of principal or premium, if any, or interest on any Subordinated Note or in the case of a Reduced Threshold Default, the Trustee may withhold notice if and so long as it in good faith determines that withholding notice is in the interests of the Holders. In addition, Keystone ULC is required to deliver to the Trustee, within 90 days after the end of each fiscal year, a certificate indicating whether the signers thereof know of any Default that occurred during the previous year. Keystone ULC also is required to deliver to the Trustee, within 30 days after the occurrence thereof, written notice of any event which would constitute certain Defaults, their status and what action the Issuer is taking or proposes to take in respect thereof.

**Amendments and Waivers**

Subject to certain exceptions, the Indenture may be amended with the consent of the Holders of a majority in principal amount of the Subordinated Notes then outstanding of all series affected by such amendment and any past default in compliance with any provisions may be waived with the consent of the Holders of a majority in principal amount of the Subordinated Notes then outstanding. However, without the consent of all of the Holders of the Subordinated Notes then outstanding, no amendment or waiver may, among other things:

(i) reduce the amount of Subordinated Notes whose Holders must consent to an amendment,

(ii) reduce the rate of or extend the time for payment of interest on any Subordinated Note,

(iii) reduce the principal of or reduce or extend the Stated Maturity of any Subordinated Note,

(iv) reduce the premium payable upon the redemption of any Subordinated Note or change the time at which any Subordinated Note may be redeemed as described under "Optional Redemption" above,

(v) make any Subordinated Note payable in a currency other than that stated in the Subordinated Note,

(vi) make any change to the subordination provisions of the Indenture that adversely affects the rights of any Holder,

(vii) impair the right of any Holder to receive payment of principal or premium, if any, and interest on such Holder's Subordinated Notes on or after the due dates therefor or to institute suit for the enforcement of any payment on or with respect to such Holder's Subordinated Notes,

(viii) modify the Guarantees or any related security in any manner adverse to the Holders,

(ix) (A) make a change to paragraph (c) under "— Limitation on Restricted Payments" that would have the effect of increasing the amounts of Restricted Payments in respect of Keystone ULC's or Keystone's Capital Stock, (B) make any change to the provisions of the indenture that prohibits the payment of Restricted Payments during an Interest Deferral Period or while any interest deferred during any Interest Deferral Period (including interest thereon) remains unpaid, or during the continuance of any Default or Event of Default or (C) waive an Event of Default under clause (x) under "— Defaults under the Indenture",

(x) waive a Default or an Event of Default under clause (i) or (ii) under "— Defaults under the Indenture",

(xi) make any change in the amendment provisions which require all of the Holder's consent or in the waiver provisions, or

(xii) (A) waive a Reduced Threshold Default; or (B) amend the covenants described above under "— Certain Covenants — Limitation on Restricted Payments" in any way that would permit a Reduced Threshold Default or that would permit the Issuer to take any action described in clause (ii) of the first paragraph of such covenant when it would not have otherwise been permitted to take such action under the terms of such covenant as in effect on the date of the Indenture.

Without the consent of any Holder, Keystone ULC and the Trustee may amend the Indenture to cure any ambiguity, omission, defect or inconsistency, to provide for the assumption by a successor corporation, partnership or limited liability company of the obligations of Keystone ULC under the Indenture, to provide for uncertificated Subordinated Notes in addition to or in place of certificated Subordinated Notes, to add guarantees with respect to the Subordinated Notes, to add to the covenants of Keystone ULC for the benefit of the holders or to surrender any right or power conferred upon Keystone ULC, to make any change that does not adversely affect the rights of any Holder, or to make certain changes to the Indenture to provide for the issuance of Additional Subordinated Notes. However, no amendment may be made to the subordination provisions of the Indenture that adversely affects the rights of providers of the Senior Indebtedness then outstanding unless the holders of such Senior Indebtedness (or any group or representative thereof authorized to give a consent) consent to such change. Notwithstanding the foregoing, no amendment shall be required to issue Additional Subordinated Notes in connection with the exercise by the Underwriters of the over-allotment option.

The consent of all of the Holders is not necessary under the Indenture to approve the particular form of any proposed amendment. It is sufficient if such consent approves the substance of the proposed amendment.

Under future Senior Indebtedness, Keystone ULC may not be permitted to effect any amendment or modification if the effect would be to (i) increase the interest rate applicable to the Subordinated Notes, (ii) change to an earlier date the scheduled dates of payment on any component of principal, interest or other amounts on the Subordinated Notes, (iii) alter the redemption, prepayment or subordination provisions of the Subordinated Notes, (iv) add to or alter the covenants (including, without limitation, the financial covenants), defaults and Events of Defaults set forth in the Indenture in a manner that would make such provisions more onerous or restrictive to Keystone ULC, or (v) otherwise increase the Obligations of Keystone ULC, Keystone or any Guarantor in respect of the Subordinated Notes or confer additional rights upon the holders thereof which individually or in the aggregate would be adverse to the Issuer, any Guarantor or the lenders of the Senior Indebtedness.

**Defeasance**

Keystone ULC at any time may terminate all of its Obligations under the Subordinated Notes and the Indenture ("legal defeasance"), except for certain Obligations, including those respecting the defeasance trust and Obligations to register the transfer or exchange of the Subordinated Notes, to replace mutilated, destroyed, lost or stolen Subordinated Notes and to maintain a registrar and paying agent in respect of the Subordinated Notes. Keystone ULC at any time may terminate its Obligations under the covenants described under "Certain Covenants" and "Change of Control", the operation of the cross acceleration provision, the bankruptcy provisions with respect to Major Subsidiaries and the judgment default provision described under "— Defaults Under the Indenture" above and the limitations contained in clause (iv) of the first paragraph under "Merger, Consolidation or Sale of All or Substantially All Assets" above and certain other covenants ("covenant defeasance"). If Keystone ULC exercises its legal defeasance option or its covenant defeasance option, each Guarantor will be released from all of its Obligations with respect to its Guarantee.

If Keystone ULC exercises its legal defeasance option, payment of the Subordinated Notes may not be accelerated because of an Event of Default with respect thereto. If Keystone ULC exercises its covenant defeasance option, payment of the Subordinated Notes may not be accelerated because of an Event of Default specified in clause (iv), (vi), (vii) with respect only to Major Subsidiaries or (viii) with respect only to Major Subsidiaries under "— Defaults Under the Indenture" above or because of the failure of Keystone ULC to comply with clause (iv) of the first paragraph under "— Merger, Consolidation or Sale of All or Substantially All Assets" above. Keystone ULC may exercise its legal defeasance option notwithstanding its prior exercise of its covenant defeasance option.

In order to exercise either defeasance option, Keystone ULC must irrevocably deposit in trust (the "defeasance trust") with the Trustee money or Government of Canada obligations for the payment of principal, premium (if any) and interest on the Subordinated Notes to redemption or maturity, as the case may be, and must comply with certain other conditions, including (i) delivery to the Trustee of an opinion of counsel to the effect that Holders of the Subordinated Notes will not recognize income, gain or loss for U.S. federal or Canadian income tax purposes as a result of such deposit and defeasance and will be subject to U.S. federal or Canadian income tax on the same amounts and in the same manner and at the same times as would have been the case if such deposit and defeasance had not occurred (and, in the case of legal defeasance only, such opinion of counsel must be based on a ruling of the Internal Revenue Service or the Canada Customs and Revenue Agency, and (ii) so long as, on the date or dates the respective amounts were paid into the trust, such payments were made with respect to the Subordinated Notes without violating the subordination provisions of the Indenture or any other material agreement binding on Keystone ULC.

**Meetings of Holders**

The Indenture provides that meetings of the Holders may be convened at any time and for any purpose and must be convened if (i) requested by Keystone ULC or the Holders representing not less than 25% of the principal amount of all outstanding Subordinated Notes, and (ii) the Trustee receives funding and is indemnified by Keystone ULC or Holders requesting the meeting against the costs which may be incurred in calling and holding such a meeting. Notice of any meeting must be provided to the Holders at least 21 days before the meeting is held.

Holders may be present and vote at any meeting of Holders either in person or by proxy and a proxyholder need not be a Holder. Holders present in person or by proxy and representing at least 25% in principal amount of the outstanding Subordinated Notes shall constitute a quorum for the transaction of business at all such meetings. At any meeting where a quorum is not present within one-half hour from the time fixed for the holding of such meeting, the meeting, if summoned by the Holders or pursuant to a request of the Holders, shall be dissolved, but in any other case the meeting shall be adjourned to the same day in the next week at the same time and (if reasonably practicable) place with no notice required to be given in respect of such adjourned meeting or at such other time and place as the chair of the meeting may decide and notice shall be given to Holders at least five days prior to such day. At such adjourned meeting, the Holders present in person or by proxy shall constitute a quorum and may transact the business for which the meeting was originally convened whether or not they represent 25% of the principal amount of the outstanding Securities.

Voting at any such meeting can be taken by way of a show of hands or by a poll. On a show of hands every person who is present and entitled to vote, whether as a Holder or as proxy for one or more Holders, shall have one vote. On a poll each Holder present in person or represented by a proxy is entitled to one vote for each $10.00 principal amount of Subordinated Notes for which they are the holder where any fractional amount shall be rounded to the nearest $10.00. Except for business which requires an Extraordinary Resolution, every question submitted to a meeting shall be decided by a majority of the votes.

The Indenture provides that, subject to certain exceptions (including a Reduced Threshold Default), certain powers are exercisable only by way of an Extraordinary Resolution which must be passed by not less then 66⅔% of the principal amount of the Subordinated Notes present or represented by proxy at the meeting and voted upon on a poll on such resolution. Holders have the following powers exercisable by Extraordinary Resolution, among other things: (i) power to sanction any change or arrangement of their rights or those of the Trustee against Keystone ULC or against its property or assets, (ii) subject to certain requirements, the power to assent to any change to the provisions of the Indenture, the Subordinated Notes, the Guarantees or any security therefor that is agreed to by Keystone ULC and/or the Guarantors, as applicable, (iii) power to sanction the reconstruction, reorganization or recapitalization of Keystone ULC or the consolidation, amalgamation or merger of the Issuer with any Person or for the sale, leasing, transfer or other disposition of all of the undertaking, property and assets of Keystone ULC, (iv) power to authorize the Trustee or any other person to bid at any sale of Keystone ULC's properties or assets and to borrow money in connection with such bid and to mortgage the property or assets so purchased as security for the repayment of the money so borrowed and to hold the property or assets so purchased in trust for all the Holders, or (v) power to remove the Trustee and appoint a new Trustee or Trustees.

### Concerning the Trustee

Computershare Trust Company of Canada is to be the Trustee under the Indenture.

### Governing Law

The Indenture will provide that it and the Subordinated Notes will be governed by, and construed in accordance with, the laws of the Province of Ontario.

### Certain Definitions

Certain definitions used in this section "Description of the Subordinated Notes" will have the following meanings as they pertain to the Indenture and if not otherwise defined shall have the meanings as set out in the "Glossary of Terms":

"Adjusted EBITDA" means for any period, the earnings of the Person before interest, taxes in respect of earnings and profits, depreciation and amortization, plus any non-cash charges reducing earnings and minus all non-cash charges increasing earnings plus expected EBITDA attributable to acquisitions determined on a consolidated basis.

"affiliate" of any specified Person means any other Person directly or indirectly controlling or controlled by or under direct or indirect common control with such specified Person. For purposes of this definition, "control" (including, with correlative meanings, the terms "controlling", "controlled by" and "under common control with"), as used with respect to any Person, means the possession, directly or indirectly, of the power to direct or cause the direction of the management or policies of such Person, whether through the ownership of voting securities, by agreement or otherwise.

"Asset Sale" means:

(a) the sale, conveyance, transfer or other disposition (whether in a single transaction or a series of related transactions) of property or assets (including by way of a Sale/Leaseback Transaction) of Keystone ULC, Keystone or any Subsidiary (each referred to in this definition as a "disposition"); or

(b) the issuance or sale of Equity Interests of any Subsidiary (other than to Keystone ULC, Keystone or another Wholly-Owned Subsidiary) (whether in a single transaction or a series of related transactions),

in each case other than:

(i) a disposition of cash equivalents or Investment Grade Securities or obsolete or worn out equipment in the ordinary course of business;

(ii) the disposition of all or substantially all of the assets of Keystone ULC or Keystone in a manner permitted in the Indenture or any disposition that constitutes a Change of Control;

(iii) any Restricted Payment or Permitted Investment that is permitted to be made, and is made;

(iv) any disposition of property or assets by a Subsidiary to Keystone ULC or Keystone or a Subsidiary to a Subsidiary;

(v) any exchange of like property for use in a similar business;

(vi) sales of assets received by Keystone ULC or Keystone upon the foreclosure on a Lien;

(vii) sales of inventory in the ordinary course of business consistent with past practices and sales of equipment upon termination of a contract with a client entered into in the ordinary course of business pursuant to the terms of such contract;

(viii) any single transaction or series of related transactions that involves assets or Capital Stock, as the case may be, having a fair market value of less than $20 million; and

(ix) the licensing of intellectual property to third Persons on customary terms as determined by the board of directors in good faith.

"Business Day" means a day other than a Saturday, Sunday or other day on which banking institutions in the Province of Ontario are authorized or required by law to close.

"Capital Stock" means:

(a) in the case of a corporation, corporate shares or equity interests, including, without limitation, corporate shares represented by IPSs and corporate shares outstanding upon the separation of IPSs into the securities represented thereby;

(b) in the case of an association or business entity, any and all shares, interests, participations, rights or other equivalents (however designated) of corporate shares;

(c) in the case of a partnership or limited liability company, partnership or membership interests (whether general or limited); and

(d) any other interest or participation that confers on a Person the right to receive a share of the profits and losses of, or distributions of assets of, the issuing Person.

"Capitalized Lease Obligation" means, at the time any determination thereof is to be made, the amount of the liability in respect of a capital lease that would at such time be required to be capitalized and reflected as a liability on a balance sheet (excluding the footnotes thereto) in accordance with GAAP.

"Closing Date" means the date of the Indenture.

"Debt-to-EBITDA Ratio" has the meaning set forth in the covenant described under " — Limitations on Incurrence of Indebtedness and Issuance of Disqualified Stock and Preferred Stock".

"Default" means any event which is, or after notice or passage of time or both would be, an Event of Default.

"Designated Senior Indebtedness" means (i) the Senior Indebtedness under the New Credit Facility and (ii) any other Senior Indebtedness of the Company with a principal amount in excess of $25 million and designated by the Company as Designated Senior Indebtedness.

"Disqualified Recipient" means (i) any person that owns, directly or indirectly (through ownership of IPSs or otherwise) and after application of the constructive ownership rules described in Code section 871(h)(3), 10% or more of the total combined voting power of all classes of equity of the Issuer entitled to vote, (ii) a controlled foreign corporation, within the meaning of Code section 957(a), related, within the meaning of Code section 864(d)(4), to the Issuer through stock ownership, or (iii) a bank described in Code section 881(c)(3)(A) with respect to the Subordinated Notes.

"Disqualified Stock" means, with respect to any Person, any Capital Stock of such Person which, by its terms (or by the terms of any security into which it is convertible or for which it is redeemable or exchangeable), or upon the happening of any event:

(a) matures or is mandatorily redeemable, pursuant to a sinking fund obligation or otherwise;

(b) is convertible or exchangeable for Indebtedness or Disqualified Stock; or

(c) is redeemable at the option of the holder thereof, in whole or in part;

in each case prior to the first anniversary of the maturity date of the Subordinated Notes; *provided, however* that only the portion of Capital Stock which so matures or is mandatorily redeemable, is so convertible or exchangeable or is so redeemable at the option of the holder thereof prior to such first anniversary will be deemed to be Disqualified Stock; *provided further, however*, that if such Capital Stock is issued to any director, manager, officer, employee or to any plan for the benefit of such parties of Keystone ULC, Keystone or their Subsidiaries or by any such plan to such parties, such Capital Stock will not constitute Disqualified Stock solely because it may be required to be repurchased by Keystone ULC in order to satisfy applicable statutory or regulatory obligations or as a result of such parties' termination, death or disability; *provided further, however*, that the Class B and Class C common shares in the capital of Keystone and any other securities having similar characteristics to the Class B or Class C common shares in the capital of Keystone that are used to finance repurchases of Class B or Class C common shares in the capital of Keystone and the preferred shares in the capital of Keystone will be deemed to constitute Disqualified Stock.

"Equity Interests" means Capital Stock and all warrants, options or other rights to acquire Capital Stock (but excluding any debt security that is convertible into, or exchangeable for, Capital Stock).

"Excess Cash" means, with respect to any period, EBITDA minus the sum of (i) cash interest expense (including dividends on Disqualified Stock and Preferred Stock), (ii) income tax expense, and (iii) unfinanced capital investments and repayments of principal, in each case, for such period.

"Fair Market Value" means, with respect to any asset or property, the price which could be negotiated in an arm's-length, free market transaction, for cash, between a willing seller and a willing and able buyer, neither of whom is under undue pressure or compulsion to complete the transaction.

"Former Owner Obligations" means all obligations and liabilities of Keystone or any of its Subsidiaries outstanding on the Closing Date or issued to the seller in connection with an Investment that constitutes a Permitted Investment by virtue of clause (c) of the definition of Permitted Investments representing a deferred purchase price for such Investment to the extent amounts sufficient to pay all principal and other obligations together with interest thereon are on deposit in the Restricted Account.

"GAAP" means generally accepted accounting principles from time to time approved by the Canadian Institute of Chartered Accountants.

"guarantee" means a guarantee (other than by endorsement of negotiable instruments for collection in the ordinary course of business) direct or indirect, in any manner (including, letters of credit and reimbursement agreements in respect thereof), of all or any part of any Indebtedness or other obligations.

"Guarantee" means any guarantee of the obligations of Keystone ULC under the Indenture and the Subordinated Notes by any Person.

"Guarantor" means any Person that Incurs a Guarantee; provided that upon the release or discharge of such Person from its Guarantee in accordance with the Indenture or the applicable Guarantee, such Person ceases to be a Guarantor.

"Hedging Obligations" means, with respect to any Person, the obligations of such Person under (i) currency exchange, interest rate or commodity swap agreements, currency exchange, interest rate or commodity cap agreements and currency exchange, interest rate or commodity collar agreements, and (ii) other agreements or arrangements designed to manage or hedge fluctuations in currency exchange, interest rates or commodity prices.

"Holder" means a holder of Subordinated Notes.

"Incur" means issue, assume, guarantee, incur or otherwise become liable for; *provided, however*, that any Indebtedness or Capital Stock of a Person existing at the time such Person becomes a Subsidiary (whether by merger, consolidation, acquisition or otherwise) will be deemed to be Incurred by such Person at the time it becomes a Subsidiary, and "Incurred" or "Incurrence" will have a corresponding meaning.

"Indebtedness" means, with respect to any Person:

(a) the principal of any indebtedness of such Person, whether or not contingent:

(i) in respect of borrowed money,

(ii) evidenced by bonds, notes, debentures or similar instruments or letters of credit or bankers' acceptances (or, without duplication, reimbursement agreements in respect thereof),

(iii) representing the deferred and unpaid purchase price of any property, except any such balance that constitutes a trade payable or similar obligation to a trade creditor due within six months from the date on which it is Incurred, and Incurred in the ordinary course of business, which purchase price is due more than six months after the date of placing the property in service or taking delivery and title thereto, or

(iv) in respect of Capitalized Lease Obligations;

(b) to the extent not otherwise included, any obligation of such Person to be liable for, or to pay, as obligor, guarantor or otherwise, on the Indebtedness of another Person (other than by endorsement of negotiable instruments for collection in the ordinary course of business); and

(c) to the extent not otherwise included, Indebtedness of another Person secured by a Lien on any asset owned by such Person (whether or not such Indebtedness is assumed by such Person); *provided, however*, that the amount of such Indebtedness will be the lesser of (i) the Fair Market Value of such asset at such date of determination, and (ii) the amount of such Indebtedness of such other Person;

*provided, further*, that any obligation of Keystone ULC, Keystone or any Subsidiary in respect of account credits or participants under any employee, director or officer compensation plan, will be deemed not to constitute Indebtedness, *provided, further*, that the Former Owner Obligations will be deemed not to constitute Indebtedness, and *provided, further*, that the Class B and Class C common shares in the capital of Keystone and any other securities having similar characteristics to the Class B or Class C common shares in the capital of Keystone that are used to finance repurchases of Class B or Class C common shares in the capital of Keystone and the preferred shares in the capital of Keystone will be deemed not to constitute Indebtedness.

"Interest Coverage Ratio" means, for any period of twelve consecutive fiscal months of the Company, the ratio of (a) Adjusted EBITDA for such period to (b) the sum of (i) Interest Expense paid or payable in cash during such period (other than deferred interest and dividends paid or payable on the Class B and Class C common shares in the capital of Keystone and any other securities having similar characteristics to the Class B or Class C common shares in the capital of Keystone that are used to finance repurchases of Class B or Class C common shares in the capital of Keystone and the preferred shares in the capital of Keystone) and (ii) interest deferred on the Subordinated Notes during such period each determined on a consolidated basis.

"Interest Deferral Threshold" means an Interest Coverage Ratio of 1.70 to 1.00.

"Interest Expense" means, in respect of any Person, for any period, the total cash interest expense (including that attributable to Capitalized Lease Obligations) of such Person for such period with respect to all outstanding Indebtedness of such Person (including, without limitation, all commissions, discounts and other fees and charges owed by such Person with respect to letters of credit and bankers' acceptance financing and net costs made or payments received of such Person under hedge agreements in respect of interest rates to the extent such net costs are allocable to such period in accordance with GAAP but excluding any interest charges in respect of the Former Owner Obligations).

"Investment Grade Securities" means (i) securities issued or directly and fully guaranteed or insured by the United States or Canadian government or any agency or instrumentality thereof (other than Cash Equivalents), (ii) debt securities or debt instruments with a rating of BBB – or higher by S&P or Baa3 or higher by Moody's or the equivalent of such rating by such rating organization, or if no rating of S&P or Moody's then exists, the equivalent of such rating by any other nationally recognized securities rating agency, but excluding any debt securities or instruments constituting loans or advances among the Issuer and its Subsidiaries, and (iii) investments in any fund that invests exclusively in investments of the type described in clauses (i) and (ii) which fund may also hold immaterial amounts of cash pending investment and/or distribution.

"Investments" means, with respect to any Person, all investments by such Person in other Persons (including affiliates) in the form of loans (including guarantees), advances or capital contributions (excluding accounts receivable, trade credit and advances to customers and commission, travel and similar advances to officers, employees and consultants made in the ordinary course of business), purchases or other acquisitions for consideration (including agreements providing for the adjustment or deferral of purchase price and non-competition agreements, consulting agreements, unsecured notes, earn-outs or other similar agreements) of Indebtedness, Equity Interests (or other securities) issued by any other Person or any business or all or substantially all of the assets of any other Person whether through purchase of assets, merger or otherwise and investments that are required by GAAP to be classified on the balance sheet of the Issuer in the same manner as the other investments included in this definition to the extent such transactions involve the transfer of cash or other property.

"Lien" means, with respect to any asset, any mortgage, lien, pledge, charge, security interest or encumbrance of any kind in respect of such asset, whether or not filed, recorded or otherwise perfected under applicable law (including any conditional sale or other title retention agreement, any lease in the nature thereof, any option or other agreement to sell or give a security interest in and any filing of or agreement to give any financing statement under the *Personal Property Security Act* (Ontario) (or equivalent statutes) of any jurisdiction); provided that in no event will an operating lease be deemed to constitute a Lien.

"Major Subsidiary" means a Subsidiary of the Issuer if the cash flow of the Subsidiary for the 12-month period ended on the last day of the most recent fiscal quarter, on a consolidated basis, is equal to or greater than 20% of the consolidated cash flow of the Issuer for such period.

"Moody's" means Moody's Investors Service, Inc.

"New Credit Facility" means the credit agreement to be entered into by and among Harris Trust Savings Bank and a syndicate of financial institutions together with the related documents thereto (including the term loans and revolving loans thereunder, any guarantees and security documents), as amended, extended, renewed, restated, supplemented or otherwise modified (in whole or in part, and without limitation as to amount, terms, conditions, covenants and other provisions) from time to time (including by adding Subsidiaries of Keystone as additional borrowers or Guarantors thereunder), and any agreement (and related document) governing Indebtedness Incurred to refinance (including one or more debt facilities, receivables, financing facilities or commercial paper facilities or indentures with banks or other institutional lenders or a trustee providing for revolving credit loans, term loans, receivables financing (including through the sale of receivables to such lenders or to special purpose entities formed to borrow from such lenders against such receivables) or letters of credit or issuance of debt securities to institutional investors, or one or more Sale/Leaseback Transactions with counterparties thereto), in whole or in part, the borrowings and commitments then outstanding or permitted to be outstanding under such New Credit Facility or a successor New Credit Facility.

"Non-U.S. Holder" means any person that is not: (i) an individual who is a citizen or resident of the U.S. for U.S. federal tax purposes, (ii) a corporation (or other entity taxable as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the U.S. or a political subdivision thereof, (iii) an estate, the income of which is subject to U.S. federal income tax regardless of the source, or (iv) a trust, if it (A) is subject to the primary supervision of a court within the U.S. and one or more U.S. persons have the authority to control all substantial decisions of the trust and one or more U.S. persons have the authority to control all of its substantial decisions, or (B) the trust was in existence on August 20, 1996 and has properly elected under applicable Treasury Regulations to continue to be treated as a United States person.

"Obligations" means any principal, interest, penalties, fees, indemnifications, reimbursements (including, reimbursement obligations with respect to letters of credit and bankers' acceptances), damages and other liabilities payable under the documentation governing any Indebtedness; provided that Obligations with respect to the Subordinated Notes will not include fees or indemnifications in favour of the Trustee and other third parties other than the Holders of the Subordinated Notes.

"Permitted Investments" means:

(a) any Investment in Keystone ULC, Keystone or any Subsidiary;

(b) any Investment in Cash Equivalents or Investment Grade Securities;

(c) any Investment by Keystone ULC, Keystone or any Subsidiary in a Person that is primarily engaged in a similar business if as a result of such Investment: (a) such Person becomes a Subsidiary; or (b) such Person, in one transaction or a series of related transactions, is merged, consolidated or amalgamated with or into, or transfers or conveys substantially all of its assets to, or is liquidated into, Keystone ULC, Keystone or any of their Subsidiaries;

(d) any Investment in securities or other assets not constituting Cash Equivalents and received in connection with an Asset Sale permitted under to the Indenture or any other disposition of assets not constituting an Asset Sale;

(e) any Investment existing on the Closing Date;

(f) advances to employees of Keystone ULC, Keystone or any Subsidiary not in excess of $5 million outstanding at any one time in the aggregate;

(g) any Investment acquired by Keystone ULC, Keystone or any Subsidiaries (a) in exchange for any other Investment or accounts receivable held by Keystone ULC, Keystone or any Subsidiary in connection with or as a result of a bankruptcy, workout, reorganization or recapitalization of the issuer of such other Investment or accounts receivable, or (b) as a result of a foreclosure by Keystone ULC, Keystone or any Subsidiaries with respect to any secured Investment or other transfer of title with respect to any secured Investment in default;

(h) Hedging Obligations permitted under the Indenture;

(i) additional Investments having an aggregate Fair Market Value, taken together with all other Investments made pursuant to this clause that are at that time outstanding, not to exceed the greater of 7.5% of total assets of the Company on a consolidated basis or $5 million at the time of such Investment (with the Fair Market Value of each Investment being measured at the time made and without giving effect to subsequent changes in value);

(j) loans and advances to officers, directors and employees for business-related travel expenses, moving expenses and other similar expenses, in each case Incurred in the ordinary course of business, and account credits and payments to participants under the long-term incentive plan or any successor or similar compensation plan;

(k) Investments the payment for which consists of Equity Interests of Keystone ULC or Keystone (other than Disqualified Stock) ("Equity Payment Investments");

(l) Guarantees incurred in accordance with the Indenture;

(m) any Investment by Subsidiaries in other Subsidiaries and any Investments held by a Person prior to that Person becoming a Subsidiary of Keystone;

(n) Investments consisting of purchases and acquisitions of inventory, supplies, materials and equipment or purchases of contract rights or licenses or leases of intellectual property, in each case in the ordinary course of business;

(o) loans, advances and payments to current or former management personnel of Keystone ULC or the Company and/or any entity in which any current or former management personnel of Keystone ULC or the Company has a beneficial or equity interest pursuant to any management equity plan or stock option plan or any other management or employee benefit or incentive plan or agreement or any other agreement pursuant to which stock is held for the benefit of such Persons not to exceed $10 million in aggregate principal amount at any time outstanding, the proceeds of which will be used to purchase or redeem, directly or indirectly, shares of Capital Stock of Keystone ULC or Keystone; and

(p) Investments consisting of securities, insurance policies or other assets acquired in accordance with entering into preneed funeral arrangements established with customers in the ordinary course of business and in accordance with respective laws governing such arrangements in the state of origin. Further, any such investments required by state law in conjunction with the operation of a cemetery owned by the Issuer for pre-construction of cemetery property, deferred merchandise liability, and perpetual care.

"Permitted Junior Securities" shall mean debt or equity securities of Keystone ULC or any successor corporation issued pursuant to a plan of reorganization or readjustment of Keystone ULC that are subordinated to the payment of all then outstanding Senior Indebtedness of Keystone ULC at least to the same extent that the Subordinated Notes are subordinated to the payment of all Senior Indebtedness of Keystone ULC on the Issue Date, so long as to the extent that any Senior Indebtedness of Keystone ULC outstanding on the date of consummation of any such plan of reorganization or readjustment is not paid in full on such date, either (a) the holders of any such Senior Indebtedness not so paid in full have consented to the terms of such plan of reorganization or readjustment or (b) such holders receive securities which constitute Senior Indebtedness and which have been determined by the relevant court to constitute satisfaction in full of any Senior Indebtedness not paid in full.

"Permitted Liens" means, with respect to any Person:

(a) pledges or deposits by such Person under workmen's compensation laws, unemployment insurance laws or similar legislation, or good faith deposits in connection with bids, tenders, contracts (other than for the payment of Indebtedness) or leases to which such Person is a party, or deposits to secure public or statutory obligations of such Person or deposits of cash or Canadian or United States government bonds to secure surety or appeal bonds to which such Person is a party, or deposits as security for contested taxes or import duties or for the payment of rent, in each case Incurred in the ordinary course of business;

(b) Liens imposed by law, such as carriers', warehousemen's and mechanics' Liens, in each case for sums not yet due or being contested in good faith by appropriate proceedings or other Liens arising out of judgments or awards against such Person with respect to which such Person will then be proceeding with an appeal or other proceedings for review;

(c) Liens for taxes, assessments or other governmental charges not yet due or payable or subject to penalties for non-payment or which are being contested in good faith by appropriate proceedings;

(d) Liens in favour of issuers of performance and surety bonds or bid bonds or completion guarantees or with respect to other regulatory requirements or letters of credit issued pursuant to the request of and for the account of such Person in the ordinary course of its business;

(e) minor survey exceptions, minor encumbrances, easements or reservations of, or rights of others for, licenses, rights-of-way, sewers, electric lines, telegraph and telephone lines and other similar purposes, or zoning or other restrictions as to the use of real properties or Liens incidental to the conduct of the business of such Person or to the ownership of its properties which were not Incurred in connection with Indebtedness and which do not in the aggregate materially adversely affect the value of said properties or materially impair their use in the operation of the business of such Person;

(f) Liens on property or shares of stock of a Person at the time such Person becomes a Subsidiary; *provided, however,* that such Liens are not created or Incurred in connection with, or in contemplation of, such other Person becoming such a Subsidiary; *provided, further, however,* that such Liens may not extend to any other property owned by Keystone ULC or the Company or a Subsidiary;

(g) Liens on property at the time Keystone ULC, Keystone or a Subsidiary acquired the property, including any acquisition by means of a merger or consolidation with or into Keystone ULC, Keystone or a Subsidiary; *provided, however,* that such Liens are not created or Incurred in connection with, or in contemplation of, such acquisition; *provided, further, however*, that the Liens may not extend to any other property owned by Keystone ULC, Keystone or a Subsidiary;

(h) Liens securing Indebtedness or other obligations of a Subsidiary owing to Keystone ULC, Keystone or a Subsidiary permitted to be Incurred in accordance with the Indenture;

(i) Liens securing Hedging Obligations so long as the related Indebtedness is, and is permitted to be under this Indenture, secured by a Lien on the same property securing such Hedging Obligations;

(j) Leases and subleases of real property which do not materially interfere with the ordinary conduct of the business of Keystone ULC, Keystone or a Subsidiary;

(k) Liens arising from Personal Property Registry filings or Uniform Commercial Code financing statement filings regarding operating leases entered into by Keystone ULC, Keystone or a Subsidiary in the ordinary course of business;

(l) Liens in favour of Keystone ULC or Keystone;

(m) Liens on equipment of Keystone ULC or Keystone granted in the ordinary course of business to Keystone ULC's or Keystone's client at which such equipment is located;

(n) Liens encumbering deposits made in the ordinary course of business to secure obligations arising from statutory, regulatory, contractual or warranty requirements, including rights of offset and set-off; and

(o) Liens to secure any refinancing, refunding, extension, renewal or replacement or successive refinancings, refundings, extensions, renewals or replacements, as a whole, or in part, of any Indebtedness secured by any Lien referred to in the foregoing clauses (g), (h), (i), (j), and (l); *provided, however,* that (A) such new Lien will be limited to all or part of the same property that secured the original Lien (plus improvements on such property) and (B) the Indebtedness secured by such Lien at such time is not increased to any amount greater than the sum of (x) the outstanding principal amount or, if greater, committed amount of the Indebtedness described under clauses (g), (h), (i), (j), and (l) at the time the original Lien became a Permitted Lien under the Indenture and (y) an amount necessary to pay any fees and expenses, including premiums, related to such refinancing, refunding, extension, renewal or replacement.

"Person" means any individual, corporation, partnership, business trust, limited liability company, joint venture, association, joint-stock company, trust, unincorporated organization, government or any agency or political subdivision thereof or any other entity.

"Preferred Stock" means any Equity Interest with preferential right of payment of dividends or upon liquidation, dissolution, or winding up; *provided, however,* that the Class B and Class C common shares in the capital of Keystone and any other securities having similar characteristics to the Class B or Class C common shares in the capital of Keystone that are used to finance repurchases of Class B or Class C common shares in the capital of Keystone and the preferred shares in the capital of Keystone will be deemed not to constitute Preferred Stock.

"Reduced Threshold Amount" means an amount equal to 10% of the aggregate outstanding principal amount of Subordinated Notes.

"Reduced Threshold Default" means a Default arising from a failure to comply with clause (i) under "— Certain Covenants — Limitations on Restricted Payments" and such failure continues for 30 days after the notice specified in "Defaults Under the Indenture".

"Representative" means the trustee, agent or representative (if any) for an issue of Senior Indebtedness.

"Restricted Account" means the account established by Keystone or any of its Subsidiaries with Harris Trust and Savings Bank (or one of its affiliates) in which it will deposit cash from time to time for the purpose of paying Former Owner Obligations.

"Restricted Investment" means an Investment other than a Permitted Investment.

"Restricted Payment" has the meaning ascribed to it under "— Certain Covenants — Limitation on Restricted Payments".

"Seller Debt" means all obligations and liabilities of Keystone or any of its Subsidiaries issued in connection with an Investment that constitutes a Permitted Investment by virtue of clause (c) of the definition of Permitted Investments representing a deferred purchase price for such Investment, other than Former Owner Obligations.

"Senior Indebtedness" means, with respect to Keystone ULC, Keystone or any Guarantor, all secured Indebtedness of Keystone ULC, Keystone or any Guarantor, including interest thereon (including interest accruing on or after the filing of any petition in bankruptcy or for reorganization relating to Keystone ULC, Keystone or any Guarantor whether or not a claim for post-filing interest is allowed in such proceeding) and other amounts (including make-whole, fees, expenses, reimbursement obligations under letters of credit and indemnities) owing in respect thereof, all Hedging Obligations and all obligations in respect of cash management services, in each case whether outstanding on the Closing Date or thereafter Incurred, unless in the instrument creating or evidencing the same or pursuant to which the same is outstanding it is provided that such obligations are not superior in right of payment to the Subordinated Notes or such Guarantor's Guarantee, as applicable; *provided, however*, that Senior Indebtedness shall not include, as applicable, (i) any obligation of Keystone ULC, Keystone or any Guarantor to any of their respective Subsidiaries or of any such Subsidiary to Keystone ULC, Keystone or such Guarantor, (ii) any liability for federal, state, provincial, local or other taxes owed or owing by Keystone ULC, Keystone or such Guarantor, (iii) any accounts payable or other liability to trade creditors arising in the ordinary course of business (including guarantees thereof or instruments evidencing such liabilities), and (iv) any obligations with respect to any Capital Stock.

"Subordinated Indebtedness" means, with respect to Keystone ULC, the Company or any Guarantor, all Indebtedness which is not Senior Indebtedness or pari passu Indebtedness.

"Subsidiary" means, with respect to any Person,

(a) any corporation, association or other business entity (other than a partnership, joint venture or limited liability company) of which 50% or more of the total voting power of shares of Capital Stock entitled (without regard to the occurrence of any contingency) to vote in the election of directors, managers or trustees thereof is at the time of determination owned or controlled, directly or indirectly, by such Person or one or more of the other Subsidiaries of that Person or a combination thereof; and

(b) any partnership, joint venture or limited liability company of which 50% or more of the capital accounts, distribution rights, total equity and voting interests or general and limited partnership interests, as applicable, are owned or controlled, directly or indirectly, by such Person or one or more of the other Subsidiaries of that Person or a combination thereof, whether in the form of membership, general, special or limited partnership interests or otherwise and any such Person owns or controls, directly or indirectly, 50% or more of the total equity and voting rights of the general partner of such entity.

"Total Funded Debt" means all Indebtedness (based on average revolving credit facility usage), letters of credit and guarantees of same of a Person, determined on a consolidated basis.

"Voting Stock" of any Person as of any date means the Capital Stock of such Person that is at the time entitled to vote in the election of the board of directors or equivalent body or Person of such Person.

"Weighted Average Life to Maturity" means, when applied to any Indebtedness or Disqualified Stock, as the case may be, at any date, the quotient obtained by dividing (i) the sum of the products of the number of years from the date of determination to the date of each successive scheduled principal payment of such Indebtedness or redemption or similar payment with respect to such Disqualified Stock multiplied by the amount of such payment, by (ii) the sum of all such payments.

"Wholly-Owned Subsidiary" of any Person means a Subsidiary of such Person 100% of the outstanding Capital Stock on other ownership interests of which will at the time be owned by such Person or by one or more Wholly-Owned Subsidiaries of such Person.

## EARNINGS COVERAGE RATIOS

The Issuer's interest requirements, after giving effect to the issue of the Subordinated Notes as a component of the IPSs and the Separate Subordinated Notes and other obligations, would have amounted to $13.4 million for the 12 months ended December 31, 2003 and $13.4 million for the 12 months ended September 30, 2004. The Issuer's *pro forma* earnings before minority interest, interest and income tax for the 12 months ended December 31, 2003 would have been $18.2 million which is 1.36 times the interest requirements for this period. The Issuer's *pro forma* earnings before minority interest, interest and income tax for the 12 months ended September 30, 2004 would have been $16.3 million, which is 1.22 times the interest requirements for this period.

## CONSOLIDATED CAPITALIZATION

The following table sets out the consolidated capitalization of Keystone North America as at August 27, 2004 and as at January 28, 2005, both before and after giving effect to this offering and the transactions contemplated by the Investment Agreement.

| Designation | Authorized | At August 27, 2004 | At August 27, 2004 before giving effect to this offering and the Transaction Contemplated in the Investment Agreement | At January 31, 2005, after giving effect to this offering and the Transaction Contemplated in the Investment Agreement (in thousands of dollars)(2) |
|---|---|---|---|---|
| Common Shares | Unlimited | C$10.00<br>(1 Common Share)(1) | C$10.00<br>(1 Common Share) | C$97,709<br>(17,100,000 Common Shares) |
| Preferred Shares | Unlimited | — | — | — |
| Long-term Indebtedness | | — | — | C$160,085 |

(1) Keystone North America was incorporated on August 27, 2004 and issued one Common Share for C$10.00. This share will be cancelled at the time of the Offering.

(2) Does not include Underwriters' fee of C$9.8 million and other fees and expenses in connection with the offering of C$5.7 million.

## SEPARATE SUBORDINATED NOTES OFFERING

In connection with the offering, Keystone ULC is also selling, on a private placement basis, approximately C$10 million principal amount of Subordinated Notes (not part of the IPSs). Holders of the Separate Subordinated Notes may, at any time, through their broker or other financial institution, combine the applicable number of Common Shares and principal amount of Separate Subordinated Notes to form IPSs. The completion of the offering of Separate Subordinated Notes is a condition to the Issuer's sale of IPSs.

## NEW CREDIT FACILITY

Capitalized terms used in this "New Credit Facility" section and not otherwise defined have the meanings set forth in the New Credit Facility.

Keystone America, Inc. has arranged for a new senior credit facility (the "New Credit Facility") with a syndicate of financial institutions in the form of a $15 million secured revolving credit facility (of which none is expected to be drawn at the closing of this offering) and a $43.1 million secured term loan. The New Credit Facility will be guaranteed by Keystone America, Inc. and all of its and Keystone's existing and future subsidiaries. The obligations in respect of the New Credit Facility will be secured by: (i) a first priority security interest in the assets of Keystone America, Inc. and all of its subsidiaries; and (ii) a pledge of the shares of Keystone America, Inc. and all of its subsidiaries. The New Credit Facility will have a term of three years from the closing of this offering.

Loans under the New Credit Facility will bear interest at a rate equal to LIBOR or a U.S. Base Rate, plus an applicable margin to those rates. Base Rate committed advances may be prepaid at any time with same day written notice in a minimum amount of $500,000. LIBOR committed advances may not be paid prior to the last day of the applicable interest period without payment of breakage costs and required minimum amount must remain outstanding.

The New Credit Facility will contain customary representations, warranties, covenants (including restrictions on incurring additional indebtedness), conditions to funding and events of default. Among other things, no cash distributions shall be permitted during the existence of a default or an event of default under the New Credit Facility. Any change of control is an event of default under the New Credit Facility. The New Credit Facility will contain restrictive covenants that will limit the discretion of management with respect to certain business matters. The New Credit Facility will also be subject to financial covenants regarding a maximum ratio of: Senior Funded Debt to Adjusted EBITDA of 2.25; Total Funded Debt to Adjusted EBITDA of 5.35, and, for any twelve month period, Adjusted EBITDA to the sum of Interest Expensed and deferred interest on the Subordinated Notes of 1.50.

The New Credit Facility is with, and guaranteed by, entities from which Keystone receives its cash distributions and as a result, the amounts owing under the credit facility and any interest thereon will be payable in priority to any cash distributions to holders of IPSs, Common Shares and Subordinated Notes.

## DESCRIPTION OF SHARE CAPITAL OF KEYSTONE NORTH AMERICA AND KEYSTONE ULC

### Share Capital of Keystone North America

The authorized share capital of Keystone North America will consist of an unlimited number of common and preferred shares. Upon closing of this offering, all of the issued and outstanding Common Shares of Keystone North America will be represented by the IPSs sold pursuant to this offering.

Holders of Common Shares of Keystone North America will be entitled to receive dividends as and when declared by the board of directors and are entitled to one vote per Common Share on all matters to be voted on at all meetings of shareholders. Upon the voluntary or involuntary liquidation, dissolution or winding-up of Keystone North America, the holders of Common Shares are entitled to share ratably in the remaining assets available for distribution, after payment of liabilities.

### Share Capital of Keystone ULC

The authorized share capital of Keystone ULC will consist of 1,000,000,000 common shares. Immediately after closing of the offering, all of the outstanding common shares of Keystone ULC will be owned by Keystone. Holders of common shares of Keystone ULC will be entitled to receive dividends as and when declared by the board of directors and are entitled to one vote per share on all matters to be voted on at all meetings of shareholders. Upon the voluntary or involuntary liquidation, dissolution or winding-up of Keystone ULC, the holders of common shares are entitled to share ratably in the remaining assets available for distribution, after payment of liabilities and subject to the prior rights of preferred shares (if any).

The shareholders of Keystone ULC may, by special resolution, alter the share capital of Keystone ULC and, without prejudice to any special rights previously conferred on the existing shareholders at the time, issue preferred shares with such designations, powers, preferences, privileges and relative, participating, optional or special rights, including any qualifications, limitations or restrictions. Special rights which may be granted to a series of preferred shares may include dividend rights, conversion rights, voting rights, terms of redemption and liquidation preferences, any of which may be superior to the rights of the common shares.

**Interest Payments and Dividend Policy**

Keystone ULC will pay interest on the Subordinated Notes and Keystone North America will pay dividends on the Common Shares (if declared) on the 15th day of each month (or the next business day, if such day is not a business day) to holders of record at the close of business on the last business day of the preceding month commencing March 15, 2005.

The dividends on the Common Share represented by an IPS will be paid, if and to the extent dividends are declared by the Keystone North America's board of directors and permitted by applicable law. Keystone North America has currently adopted a dividend policy that contemplates an annual dividend of approximately C$0.3785 per Common Share. Keystone North America will generally declare dividends of its available cash after satisfying its debt service obligations under any credit facilities or other agreements with third parties, if any, satisfying its other expense obligations, including withholding and other applicable taxes and retaining reasonable reserves as may be considered appropriate by its board of directors.

Keystone North America may make additional distributions in excess of monthly distributions during the year, as the board of directors may determine in its sole discretion.

The board of directors of Keystone North America may, in its discretion, modify or repeal Keystone North America's current dividend policy. No assurances can be made that Keystone North America will pay dividends at the level contemplated in the future or at all. Assuming that Keystone ULC makes the scheduled interest payments on the Subordinated Notes and Keystone North America pays dividends on the Common Shares in the amount contemplated by the current dividend policy, an investor would receive, in the aggregate, approximately C$1.00 per year per IPS in dividends on the Common Shares and interest on the Subordinated Notes.

The initial cash distribution on both the Subordinated Notes and Common Shares for the period from closing to February 28, 2005 is expected to be paid on March 15, 2005 (assuming closing occurs on February 8, 2005). The first monthly distribution is expected to be C$0.0625 per IPS.

## DESCRIPTION OF SHARE CAPITAL OF KEYSTONE

Keystone is a Delaware corporation.

**Capital of Keystone**

The authorized capital of Keystone will consist of 25,000,000, 2,000,000 and 2,000,000 Class A, B and C common shares, respectively, and 25,000,000 preferred shares. Upon closing of this offering and the transactions contemplated under "Investment Agreement", 17,100,000 Class A common shares of Keystone will be owned by Keystone North America and 1,270,964 Class B and 1,668,017 Class C common shares will be owned by the Existing Investors, Existing Lenders and certain members of management of Keystone; and 19,433,178 preferred shares will be owned by Keystone ULC. The Class B common shares will represent at least 10% of the aggregate value of the common shares of Keystone outstanding upon closing of the offering.

**Class A Common Shares**

Each Class A common share will carry one vote on all matters to be voted on at all meetings of shareholders. Holders of Class A common shares will be entitled to receive dividends as and when declared by the board of directors. In the event of the liquidation, dissolution or winding-up of Keystone or other distribution of assets of the Company among shareholders for the purpose of winding-up its affairs, the holders of Class A common shares shall be entitled to share ratably with the holders of Class B and C common shares in the remaining assets available for distribution, after payment of liabilities, including the portion of the amounts owing on the Class B and C common shares that are preferential to payments on the Class A common shares, as described below.

### Class B and C Common Shares

The holders of the Class B and C common shares will be entitled to receive, as and when declared by the board of directors of Keystone, fixed cumulative preferential cash dividends at a rate of 14.5% of the Liquidation Amount thereof (as defined below) or approximately C$0.6215 per share, per annum, to be paid after the distributions in respect of the preferred shares described below and before any dividend on the Class A common shares of Keystone. Dividends on the Class B and C common shares will be paid on a monthly basis in Canadian dollars or the U.S. dollar equivalent thereof on the 15th day of the following month (or the next business day if such day is not a business day). Monthly dividends will be paid after advances in respect of the preferred shares. Any dividends paid by Keystone in excess of the dividends at a rate of 14.5% or approximately C$0.6215 per share shall: (i) for periods ending on or before the second anniversary of the closing of this offering, be paid pro rata to the holders of Class A common shares of Keystone and the holders of Class B and C common shares (subject to adjustment to increase dividends to the holders of Class A common shares of Keystone in order to support payment of Keystone North America's expenses) and (ii) for periods ending after the second anniversary of the closing of this offering, be paid to the holders of Class B and C common shares (subject to the subordination provisions described below) in an amount per share equal to 1.1 times the dividend per share to which the holders of the Class A common shares are entitled (such enhanced dividend entitlement of holders of the Class B and C common shares over the dividend entitlement of the Class A common shares is referred to as the "Enhanced Dividend"). The Enhanced Dividend will be non-cumulative and may only be paid to holders of the Class B and C common shares in respect of any month if Keystone has declared and paid dividends on the Class A common shares at no less than the monthly amount of C$0.0315 per share for such month (not taking into account any dividend to the holders of Class A common shares in respect of the expenses of Keystone North America).

Upon the closing, all of the outstanding Class B and C common shares will be held by Existing Investors, Existing Lenders and certain members of management of Keystone. On the redemption of the Class C common shares by Keystone in connection with the exercise by the Underwriters of the over-allotment option, any accrued and unpaid dividends on such shares will be paid.

In the event of the liquidation, dissolution or winding-up of Keystone or other distribution of assets of Keystone among shareholders for the purpose of winding-up its affairs, the holders of Class B and C common shares shall be entitled to receive from the assets of Keystone, in cash, the sum of C$4.286 (the "Liquidation Amount") for each Class B and C common share held, together with all accrued and unpaid (whether or not declared) cumulative dividends thereon calculated up to the date of distribution (which for such purposes shall be calculated as if such dividends, to the extent unpaid, were accruing for the period from the expiration of the last period for which dividends thereon were paid in full up to the date of distribution) after payment to holders of the preferred shares, as described below, and before any amount shall be paid or any assets of Keystone distributed to holders of any other class of shares ranking junior to the Class B and C common shares. After payment to the holders of preferred shares of the amount so payable to them as described below and payment to the holders of the Class B and C common shares of the amount so payable to them as provided above, the remaining assets and funds of Keystone available for distribution to shareholders shall be distributed ratably among the holders of Class A, B or C common shares.

The holders of Class B and C common shares shall be entitled to one vote per share on all matters to be voted on at all meetings of shareholders.

### Preferred Shares

The preferred shares will consist of 25,000,000 authorized shares designated as preferred shares. The holders of the preferred shares shall be entitled to receive, as and when declared by the board of directors of Keystone, out of the assets of Keystone, fixed cumulative preferential cash dividends at the rate of 14.51% or approximately C$0.6219 per share, per annum in addition to any dividends in excess of such preferential dividend declared by the board of directors of Keystone from time to time in its sole discretion. Dividends will be paid on an annual basis in Canadian dollars at the end of each year, but will accrue on a monthly basis. Keystone will lend amounts on a monthly basis to holders of preferred shares until the annual dividend is paid, at which time the loaned amounts will be paid and satisfied. Such advances will enable Keystone ULC to pay the monthly interest obligation on the Subordinated Notes until the annual dividend is paid. Upon closing, all of the outstanding preferred shares will be held by Keystone ULC.

In the event of the liquidation, dissolution or winding-up of Keystone or other distribution of assets of Keystone among shareholders for the purpose of winding-up its affairs, the holders of preferred shares shall be entitled to receive from the assets of Keystone, in cash, the sum of C$4.286 for each preferred share held, together with all accrued and unpaid (whether or not declared) cumulative dividends thereon calculated up to the date of distribution (which for such purpose shall be calculated as if such dividends, to the extent unpaid, were accruing for the period from the expiration of the last period for which dividends thereon were paid in full up to the date of distribution) before an amount shall be paid or any assets of Keystone distributed to the holders of any common shares or shares of any other class ranking junior to the preferred shares, including the Class B and C common shares. After payment to the holders of the preferred shares of the amount so payable to them as provided above, all of the remaining assets and funds of Keystone available for distribution to shareholders shall be distributed among the holders of the Class A, B and C common shares in the manner described above.

Except as otherwise required by law, the holders of preferred shares shall not have any voting rights.

Holders of preferred shares may cause Keystone to redeem or Keystone may redeem, in either case at any time, all or any of the outstanding preferred shares of Keystone for an amount equal to C$4.286 per share.

**Distribution Policy**

Keystone will adopt a policy to distribute all of its available cash, subject to applicable law and the terms of the New Credit Facility, the Indenture and any other then outstanding indebtedness by way of monthly dividends and/or loans on its common shares, preferred shares or other distributions on its securities, after:

- satisfaction of its debt service or other obligations, if any, under credit facilities or other agreements with third parties;
- satisfaction of its interest and other expense obligations, including any applicable taxes;
- making any redemptions in respect of any preferred shares; and
- retaining reasonable working capital or other reserves as may be considered appropriate by the board of directors of Keystone.

Distributions in respect of and dividends on its common shares and preferred shares will be paid on or prior to the 15th day of each month (or the next business day if such day is not a business day).

Dividend payments are not mandatory or guaranteed. The board of directors of Keystone may, in its discretion, amend or repeal its dividend policies in respect of its common shares. Keystone's board of directors may decrease the level of dividends provided for in each dividend policy in respect of its common shares or discontinue entirely the payment of dividends in respect of its common shares.

## PRINCIPAL HOLDERS OF IPSs (COMMON SHARES)

To the Issuer's knowledge, no person or company will, as at closing, own beneficially, directly or indirectly, more than 10% of the Common Shares.

## INDEBTEDNESS OF DIRECTORS AND EXECUTIVE OFFICERS

The following table outlines all indebtedness (other than routine indebtedness), which totals $328,520 in the aggregate, to the Company of each individual who is, or at any time during the most recently completed financial year of the Company was, a director or executive officer of the Company, and each associate of such individual:

| Name and Principal Position | Involvement of the company | Largest Amount Outstanding during Fiscal 2004 | Amount Outstanding as at November 30, 2004(2) | Security for Indebtedness |
|---|---|---|---|---|
| Stephen M. Shaffer .......... Chief Financial Officer of Keystone | Loan(1) | $ 56,250 | $ 56,250 | Pledge of shares in Keystone |
| James D. Price ............. Chief Operating Officer of Keystone | Loan(1) | $ 87,500 | $ 87,500 | Pledge of shares in Keystone |
| Steven A. Tidwell ........... Executive Vice President of Keystone | Loan(1) | $184,770 | $184,770 | Pledge of shares in Keystone |

(1) Promissory notes that bear interest at a rate of 8% were issued to Keystone and are secured by a pledge of shares in Keystone.

(2) These loans will be cancelled prior to the closing of this offering.

## PRIOR ISSUANCES

The only issuances of securities by Keystone North America in the 12 months prior to the date of this prospectus was the issuance of one Common Share upon incorporation at a price of $10.00. This Common Share will be repurchased by Keystone North America for $10.00 and cancelled in connection with the closing of this offering.

## RISK FACTORS

An investment in the IPSs and the underlying Common Shares and Subordinated Notes under this prospectus involves a number of risks. In addition to the other information contained in this prospectus, prospective investors should give careful consideration to the following factors. The risks described below are not the only risks facing the Company and the Issuer. Additional risks and uncertainties not currently known or that are currently considered to be immaterial may also materially and adversely affect the Company and the Issuer's operations. If any of these or other risks actually occur, the Company and the Issuer's business, financial conditions, results of operations and cash flow could be adversely affected, in which case, the trading prices of the IPSs and the underlying Common Shares and Subordinated Notes would decline and you could lose all or part of your investment.

### Risks Related to the Business

***Declines in the number of deaths in our markets can cause a decrease in revenue and margins. Changes in the number of deaths are difficult to predict from market to market over the short term.***

Declines in the number of deaths could cause at-need sales of funeral and cemetery services, property and merchandise to decline, which could decrease revenue and margins. Although the United States Census Bureau estimates that the number of deaths in the United States will increase, longer lifespans could reduce the rate of deaths. If the number of deaths declines, the number of funeral services and interments performed by us will decrease and our financial condition, results of operations and our future cash flows may be materially adversely affected. In addition, changes in the number of deaths can vary among local markets and from quarter to quarter, and variations in the number of deaths in our markets or from quarter to quarter are not predictable. However, generally the number of deaths fluctuates with the seasons with more deaths occurring during the winter months primarily resulting from pneumonia and influenza. These variations can cause revenue to fluctuate over short periods of time.

***Our high fixed cost base makes us vulnerable to fluctuations in revenue.***

Companies in the funeral home and cemetery business must incur many of the costs of operating and maintaining facilities, land and equipment regardless of the level of sales in any given period. For example, we must pay salaries, utilities, property taxes, insurance and maintenance costs on funeral homes regardless of the number of funeral services or interments performed. Because we cannot decrease these costs significantly or rapidly when we experience declines in sales, declines in sales can cause margins, profits and cash flow to decline at a greater rate than the decline in revenue.

***The increasing number of cremations in the United States could cause revenue to decline because basic cremations generally produce lesser funeral revenue and limited revenue for cemetery operations.***

Our traditional cemetery and funeral service operations face the challenge of the increasing number of cremations in the United States. Industry studies indicate that the percentage of cremations has steadily increased and that cremations will represent approximately 36 percent of the United States burial market by the year 2010, compared to 27 percent in 2001. While we have focused our efforts on providing cremation with services, cremations without services usually result in lower total revenue and gross profit dollars than traditional services. A substantial increase in the rate of cremations without services that we perform could have a material adverse effect on our financial condition, results of operations and cash flows.

***If we are not able to respond effectively to changing consumer preferences, our market share, revenue and profitability could decrease.***

Future market share, revenue and profit will depend in part on our ability to anticipate, identify and respond to changing consumer preferences. Although we continually monitor consumer preferences, we may not correctly anticipate or identify trends in consumer preferences, or we may identify them later than our competitors do. In addition, any strategies we may implement to address these trends may prove incorrect or ineffective, which could have a material adverse effect on our financial condition, results of operations and cash flows.

***Increase in price competition in the funeral home and cemetery markets in which we operate could reduce our market share or cause us to reduce prices to retain or recapture market share, either of which could reduce our revenue and margins.***

To compete successfully, our funeral service locations and cemeteries must maintain good reputations and high professional standards in the industry, as well as offer attractive products and services at competitive prices. In a few markets, we have experienced price competition primarily from family run funeral home and cemetery operators, and from monument dealers, casket retailers, low cost funeral providers and other non-traditional providers of services or product. Recently, certain retailers and discounters have experimented with casket sales. From time to time, competition has resulted in losing market share in some markets. In other markets, we have had to reduce prices to retain or recapture market share. If we are unable to successfully compete, our company, our financial condition, results of operations and cash flows could be materially adversely affected.

***We require access to capital resources to successfully acquire businesses and further issuances of securities could result in dilution.***

Our growth strategies include the acquisition of additional funeral homes. Any such acquisitions will require additional capital that may be funded through additional debt or equity financings. To the extent that financing is raised through the issuance of IPSs or other securities of the Issuer, current holders of IPSs may experience ownership dilution. To the extent debt is incurred, either the Issuer or the Company may incur significant interest expense and may be subject to covenants in the related debt agreements that affect the conduct of business. Without sufficient capital resources to implement this strategy, our future growth could be limited and operations impaired. There can be no assurance that additional financing will be available to fund our growth strategies or that, if available, the financing will be on terms that are acceptable to the Company and the Issuer.

***We may not successfully integrate Hamilton into our existing operations.***

The acquisition of Hamilton materially increases the scope of our operations. Our operations and those of Hamilton have been conducted as separate and distinct businesses, each with its own management team and operations. We have developed an integration plan that includes the consolidation of certain purchasing, administrative and management functions, however we are not retaining all of the senior management personnel of Hamilton. The cost savings anticipated by management following the acquisition of Hamilton reflect numerous assumptions as to purchasing and other efficiencies and we cannot be sure that actual cost savings will be consistent with these assumptions. While we believe, based on our history with prior acquisitions, that we can successfully integrate the operations of Hamilton, there can be no assurance that this will be the case, in part, because we have never integrated an acquisition of this size. Further, the integration may require substantial attention from and place substantial demands upon our senior management, as well as require the cooperation of the employees of the Hamilton companies. In addition, we could face contractual and other restrictions on our ability to implement the cost reductions. Following our acquisition of Hamilton, we may discover that we have undisclosed liabilities. Although we have conducted what we believe to be a prudent investigation in connection with our acquisition of Hamilton, an unavoidable level of risk remains regarding any undisclosed or unknown liabilities or issues concerning Hamilton. Our failure to successfully integrate the operations of Hamilton or realize the anticipated benefits of the acquisition of Hamilton could have a material adverse effect on our financial position, results of operations and cash flows.

***Increasing insurance benefits related to prearranged funeral contracts funded through life insurance or annuity contracts may not cover future increases in the cost of providing a price guaranteed funeral service.***

We sell price guaranteed prearranged funeral contracts through various programs providing for future funeral services at prices prevailing when the agreements are signed. For prearranged funeral contracts funded through life insurance or annuity contracts, there is no guarantee that the increasing insurance benefit will cover future increases in the cost of providing a price guaranteed funeral service, which could materially adversely affect our financial condition, results of operations and cash flows.

***Earnings from and principal of trust funds and escrow accounts could be reduced by changes in stock and bond prices and interest and dividend rates or by a decline in the size of the funds.***

We maintain three types of trust funds and escrow accounts: (1) pre-need funeral merchandise and services, (2) pre-need cemetery merchandise and services and (3) perpetual care. Earnings and investment gains and losses on trust funds and escrow accounts are affected by financial market conditions that are not within our control. Earnings are also affected by the mix of fixed-income and equity securities that we choose to maintain in the funds, and we may not choose the optimal mix for any particular market condition. The size of the funds depends upon the level of pre-need sales and maturities, the amount of ordinary income and investment gains or losses and funds added through acquisitions, if any. In addition, any significant or sustained investment losses could result in there being insufficient funds in the trusts to cover the cost of delivering services and merchandise or maintaining cemeteries in the future. Any such deficiency would have to be covered by cash flow, which could have a material adverse effect on our financial condition, results of operations and cash flows.

Under our current accounting practices, unrealized gains and losses in the funeral trust funds and cemetery trust funds have no immediate impact on our earnings or cash flow, unless the fair market value of the funds were to decline below the estimated costs to deliver the underlying products and services. If that were to occur, we would record a charge to earnings to record a liability for the expected losses on the delivery of the associated contract. Over time, gains and losses realized in the funds are allocated to underlying pre-need contracts and affect the amount of the trust fund earnings we record when we deliver the underlying product or service. Accordingly, if current market conditions do not improve, the funds may eventually realize losses, and our revenue, margins, earnings and cash flow would be negatively affected by the reduced revenue when we deliver the underlying products and services. We project that with approximately 1.0 percent to 3.0 percent annualized returns in the funds over the estimated lives of the associated pre-need contracts, our trust and escrow funds would recover the net unrealized depreciation currently in the funds by the time the underlying products and services are delivered. Unrealized gains and losses in the perpetual care trust fund do not affect earnings but could limit the capital gains available to us and could result in lower returns and lower current revenue than we have historically achieved.

***We depend on our key personnel for the future success of the business and may have difficulty retaining or attracting such persons.***

Our future success and our ability to manage future growth depend, in large part, upon the continued services of our senior management and former funeral home owners and the ability to attract and retain key officers and other highly qualified personnel. Competition for such personnel is intense. There can be no assurance that we will continue to be successful in attracting and retaining qualified personnel, and the loss of the services of any of these individuals could have a material adverse effect on our revenue, financial performance and results of operations.

***Increased advertising or more effective marketing by competitors, including over the Internet, could cause us to lose market share and revenue or cause us to incur increased costs in order to retain or recapture our market share.***

In recent years, the marketing of pre-need funeral services through television, radio and print advertising, direct mailings and personal sales calls has increased. Extensive advertising or effective marketing by competitors in local markets could cause us to lose market share and revenue or cause us to increase marketing costs. In addition, competitors may change the types or mix of products or services offered. These changes may attract customers, causing us to lose market share and revenue or to incur costs in response to competition in order to vary the types or mix of products or services offered by us. Also, increased use of the Internet by customers to research and/or purchase products and services could cause us to lose market share to competitors offering to sell products or services over the Internet.

***Changes or increases in, or failure to comply with, regulations and licensing requirements applicable to our business could increase costs or decrease cash flows.***

The death care industry is subject to regulation and licensing requirements under federal, state and local laws. For example, the funeral home industry is regulated by the U.S. Federal Trade Commission, which requires funeral homes to take actions designed to protect consumers. State laws impose licensing requirements and regulate pre-need sales. Embalming facilities are subject to environmental and health regulations. Compliance with these regulations can be burdensome, and we are always at risk of not complying with the regulations or facing costly and burdensome investigations from regulatory authorities.

***Environmental regulations governing our activities could become more stringent in the future and require us to expand additional funds for environmental compliance.***

Our operations are subject to environmental laws and regulations adopted by federal, state and local authorities in the jurisdictions in which we operate. Failure to comply with such laws and regulations could result in the assessment of substantial administrative, civil and criminal penalties, or the imposition of investigatory and remedial obligations. While we believe we are in substantial compliance with existing laws and regulations, we cannot assure you that we will not incur costs in the future.

**Risks Related to the Capital Structure**

***The Issuer is Dependent on the Company for all cash available for distributions***

Keystone North America and Keystone ULC are dependent on the operations and assets of the Company through the ownership of common and preferred shares, respectively. Cash distributions to the holders of IPSs, Common Shares and Subordinated Notes will be dependent on the ability of the Company to make dividend payments on its common shares held by Keystone North America and on its preferred shares held by Keystone ULC. The actual amount of cash available for payments to holders of Subordinated Notes and distribution to holders of the IPSs, or Common Shares or Subordinated Notes will depend upon numerous factors relating to the business of the Company, including profitability, changes in revenue, fluctuations in working capital, capital expenditure levels, applicable laws, compliance with contracts and contractual restrictions contained in the instruments governing any indebtedness. Any reduction in the amount of cash available for distribution, or actually distributed, by the Company will reduce the amount of cash available for Keystone ULC to make payments to holders of Subordinated Notes and to Keystone North America for distributions to holders of Common Shares. While Keystone ULC is contractually obligated to make interest payments on the Subordinated Notes, cash distributions by Keystone North America on the Common Share component of an IPS are not guaranteed and will fluctuate with the performance of the business of the Company.

***A significant amount of our cash is distributed, which may restrict potential growth.***

The payout of substantially all of our operating cash flow will make additional capital and operating expenditures dependent on increased cash flow or additional financing in the future. Lack of these funds could limit our future growth and our cash flow. In addition, we may be precluded from pursuing otherwise attractive acquisitions or investments because they may not be accretive on a short-term basis.

***The Issuer may not receive dividends from Keystone provided for in the dividend policy the board of directors of the Company is expected to adopt or any dividends at all.***

Keystone North America's only source of cash flow for payment of dividends on the Common Shares is distributions on its equity ownership of the Company. The board of directors of the Company may, in its discretion, amend or repeal the initial dividend policy it is expected to adopt upon the closing of this offering. The Company's board of directors may decrease the level of dividends provided for in this initial dividend policy or entirely discontinue the payment of dividends. Future dividends with respect to the common shares of the Company, if any, will depend on, among other things, the results of operations, cash requirements, financial condition, contractual restrictions, business opportunities, provisions of applicable law and other factors that the board of directors of the Company may deem relevant. The Indenture and the New Credit Facility contain significant restrictions on the Company's ability to make dividend payments, including, if the Company defers interest on the Subordinated Notes under the indenture, restrictions on the payment of dividends until the Company has paid all deferred interest, together with accrued interest thereon.

In addition, the Company's after-tax cash flow available for dividend and interest payments would be reduced if the Subordinated Notes were treated as equity rather than debt for U.S. federal income tax purposes. In that event, the stated interest on the Subordinated Notes could be treated as a dividend and would not be deductible by the Company for U.S. federal income tax purposes. The Company's inability to deduct interest on the Subordinated Notes could materially increase the Company's taxable income and, thus, the Company's U.S. federal and applicable state income tax liability. If this were to occur, the Company's after-tax cash flow available for dividend and interest payments may be reduced.

***Subject to restrictions set forth in the indenture, the Issuer may defer the payment of interest to holders for a significant period of time.***

Prior to the fifth anniversary of the closing of the offering, the Issuer may, subject to restrictions set forth in the indenture, defer interest payments on the Subordinated Notes on one or more occasions for up to an aggregate period of 24 months. In addition, after the fifth anniversary of the closing of the offering, the Issuer may, subject to certain restrictions, defer interest payments on the Subordinated Notes on eight occasions for up to eight months on each occasion. Deferred interest will bear interest at the same rate as the Subordinated Notes. For any interest deferred during the first five years, the Issuer is not obligated to pay any deferred interest until the fifth anniversary of the closing of the offering, so a holder of IPSs or Subordinated Notes may be owed a substantial amount of deferred interest that will not be due and payable until such time. For any interest deferred after the fifth anniversary of the closing of the offering, the Issuer is not obligated to pay all of the deferred interest until maturity, so a holder of IPSs or Subordinated Notes may be owed a substantial amount of deferred interest that will not be due and payable until such time.

*Fluctuations in the exchange rate may impact the amount of cash available to the Issuer for distribution.*

The distributions to holders of IPSs and the underlying Common Shares and Subordinated Notes will be denominated in Canadian dollars. Conversely, all of the Issuer's revenue and expenses, together with distributions received from the Company will be denominated in U.S. dollars. As a result, the Issuer will be exposed to currency exchange rate risks.

Although the Issuer intends to directly or indirectly enter into hedging arrangements to mitigate this exchange rate risk, there can be no assurance that these arrangements will be sufficient to fully protect against this risk. If hedging transactions do not fully protect against this risk, changes in the currency exchange rate between U.S. and Canadian dollars could have a material adverse effect on the Issuer's financial condition, results of operations and cash flow and may adversely affect cash distributions.

*Our substantial consolidated indebtedness could negatively impact our business.*

After the offering, we will have a substantial amount of indebtedness. On September 30, 2004, after giving *pro forma* effect to the offering and the application of the net proceeds from the offering and the replacement of certain of our existing indebtedness with our New Credit Facility, which will be consummated concurrently at the closing of the offering, we would have had total indebtedness (including C$83.3 million indebtedness to IPS holders and to holders of the Separate Subordinated Notes issued by Keystone ULC) of $130.4 million. In addition, the indenture under which Subordinated Notes are issued will permit future further indebtedness provided that certain covenants are satisfied.

The degree to which we are leveraged on a consolidated basis could have important consequences to the holders of IPSs and the underlying Common Shares and Subordinated Notes, including:

- our ability in the future to obtain additional financing for working capital, capital expenditures or other purposes may be limited;
- we may be unable to refinance indebtedness on terms acceptable to us or at all;
- our ability to make distributions to Keystone ULC may be limited, which may make it more difficult for Keystone ULC to satisfy its obligations on the Subordinated Notes;
- a significant portion of our cash flow (on a consolidated basis) is likely to be dedicated to the payment of the principal of and interest on our indebtedness, including the Subordinated Notes, thereby reducing funds available for future operations, capital expenditures and/or dividends on our common shares;
- we may be more vulnerable to economic downturns and be limited in our ability to withstand competitive pressures;
- we may be limited on our ability to plan for or react to changes in our business or the industry in which we operate; and
- we may be at a competitive disadvantage to our competitors that have less indebtedness.

The Indenture will not limit Keystone ULC's ability to issue additional Subordinated Notes to be represented by additional IPSs in connection with the repurchase of any Class B or C common shares of Keystone in connection with a Repurchase Event.

*Keystone ULC may not be able to repurchase the Subordinated Notes upon a change of control as required by the Indenture.*

Upon the occurrence of certain specific kinds of change of control events, Keystone ULC will be required to offer to repurchase outstanding Subordinated Notes at 101% of their principal amount plus accrued and unpaid interest, if any, to the date of repurchase. However, it is possible that Keystone ULC will not have sufficient funds at the time of the change of control to make any required repurchases or the restrictions in our New Credit Facility may not allow such repurchases. Failure to purchase tendered Subordinated Notes would constitute a default under the Indenture, which, in turn, would constitute a default under our New Credit Facility. See "Description of Subordinated Notes — Change of Control".

*Changes in the Issuer's creditworthiness may affect the value of the IPSs, Common Shares and Subordinated Notes.*

The perceived creditworthiness of the Issuer, the Company and their respective subsidiaries that have guaranteed the Subordinated Notes may affect the market price or value and the liquidity of the IPSs, Common Shares and Subordinated Notes.

*The restrictive covenants in our New Credit Facility and the Indenture could impact our business and affect our ability to pursue our business strategies.*

The agreements in our New Credit Facility and the Indenture are both expected to feature restrictive covenants that limit our ability, among other things, to:

- incur additional indebtedness;
- pay dividends and make distributions in respect of the Issuer's equity interest or to make certain other restrictive payments or investments;
- sell assets;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets;
- enter into transactions with our affiliates;
- create liens; and
- enter into new lines of businesses.

In addition, the New Credit Facility will include other and more restrictive covenants and will prohibit Keystone and certain of its affiliates from prepaying our other indebtedness, including Keystone ULC prepaying the Subordinated Notes, while debt under our New Credit Facility is outstanding. The agreement governing our New Credit Facility will also require us to achieve specified financial and operating results and maintain compliance with specified financial ratios. Our ability to comply with these ratios may be affected by events beyond our control.

A breach of any of the restrictive covenants in our New Credit Facility or in our ability to comply with the required financial ratios could result in a default under the New Credit Facility. If a default occurs, the lenders under the New Credit Facility may elect to clear all borrowings outstanding under that facility together with accrued interest and other fees, to be immediately due and payable which would result in an Event of Default under the Indenture.

*Deferral of interest payments may have adverse Canadian federal income tax consequences for holders and may adversely affect the trading price of the IPSs.*

If interest payments on the Subordinated Notes are deferred, holders may be required to recognize interest income for Canadian federal income tax purposes in respect of the Subordinated Notes before receiving any cash payment of this interest. See "Certain Canadian Federal Income Tax Considerations — Taxation of Dividends, Interest and Capital Gains — Interest on the Subordinated Notes". In addition, a holder will not receive this cash payment if the holder sells the IPSs or the Subordinated Notes, as the case may be, before the end of any deferral period or before the record date relating to interest payments that are to be paid.

If the Issuer defers interest payments, the IPSs and the Subordinated Notes may trade at a price that does not fully reflect the value of accrued but unpaid interest on the Subordinated Notes. In addition, the existence of the Issuer's right to defer payments of interest on the Subordinated Notes under certain circumstances may mean that the market price for the IPSs or the Subordinated Notes may be more volatile than other securities that do not have these restrictions.

*Future sales, or the possibility of future sales of a substantial amount, of IPSs, Common Shares or Subordinated Notes may impact the price of the IPSs, the Common Shares and Subordinated Notes and could result in dilution.*

Future sales, or the possibility of future sales of a substantial amount, of IPSs, Common Shares or Subordinated Notes in the public market could adversely affect the prevailing market price of the Issuer's IPSs, the Common Shares and Subordinated Notes and could impair the Issuer's ability to raise capital through future sales of those securities. Additionally, the issuance of additional IPSs or Common Shares may dilute an investor's investment in the Issuer and reduce distributable cash per Common Share or per IPS.

The Issuer may issue Common Shares and Subordinated Notes, which may be in the form of IPSs, or other securities from time to time in order to raise capital or as consideration for future acquisitions and investments. If an acquisition or investment is significant, the number of Common Shares or the aggregate principal amount of Subordinated Notes, which may be in the form of IPSs, or the number or aggregate principal amount, as the case may be, of other securities that may be issued may in turn be significant. In addition, the Issuer may also grant registration rights covering those IPSs, Common Shares, Subordinated Notes or other securities in connection with any acquisitions or investments.

***Investment eligibility and foreign property.***

There can be no assurance that the Common Shares and Subordinated Notes represented by the IPSs will continue to be qualified investments for trusts governed by registered retirement savings plans, registered retirement income funds, deferred profit sharing plans and registered education savings plans or that the Common Shares and Subordinated Notes represented by the IPSs will not be foreign property under the *Income Tax Act* (Canada) and the regulations thereunder (the "Tax Act") (see "Eligibility for Investment" below). The Tax Act imposes penalties for the acquisition or holding of non-qualified investments and on excess holdings of foreign property. In particular, if either Keystone North America or Keystone ULC ceases to have a "substantial Canadian presence" (as that term is understood for the purposes of the Tax Act), the Common Shares and Subordinated Notes represented by the IPSs may become foreign property. There can be no assurance that either Keystone North America or Keystone ULC will continue to have a substantial Canadian presence.

On March 23, 2004, the Minister of Finance (Canada) proposed amendments to the *Income Tax Act* (Canada) (the "Budget Proposals") to restrict direct and indirect holdings in "business income trusts" (as defined in the Budget Proposals) by certain tax exempt investors. On May 18, 2004, the Minister of Finance (Canada) suspended the Budget Proposals pending consultation with representatives of the pension fund industry, the investment industry, provincial governments and other interested parties. The Department of Finance has indicated that it will continue to evaluate the development of the income trust market as part of its ongoing monitoring and assessment of Canadian financial markets and the Canadian tax system. While the Budget Proposals did not reference ownership of subordinated notes and common shares of a company as represented by IPSs, IPSs share many characteristics of income trust units. Accordingly, further changes in this area, in addition to the Budget Proposals, are possible. Such changes could result in the income tax considerations described under the heading "Certain Canadian Federal Income Tax Considerations" being materially different in certain respects.

***The U.S. Internal Revenue Service may challenge the characterization of the Subordinated Notes as debt.***

There can be no assurance that U.S. federal income tax laws and IRS administrative policies respecting the U.S. federal income tax consequences described in this prospectus will not be changed in a manner which adversely affects Non-U.S. Holders. See "Certain U.S. Federal Income Tax Considerations".

No statutory, judicial or administrative authority directly addresses the treatment of the IPSs or the Subordinated Notes, or instruments similar to the IPSs or the Subordinated Notes, for U.S. federal income tax purposes. As a result, the U.S. federal income tax consequences of the purchase, ownership and disposition of IPSs and the Subordinated Notes are uncertain. The Company will receive an opinion from the Company's counsel, Kirkland & Ellis LLP and the Underwriters will receive an opinion from their counsel, Torys LLP, to the effect that the acquisition of an IPS should be treated as the acquisition of the Common Share and Subordinated Notes as separate securities, and that the Subordinated Notes should be classified as debt for U.S. federal income tax purposes. The Company intends to deduct interest on such Subordinated Notes for tax purposes. However, the IRS or the courts may take the position that the IPSs are a single security classified as equity, or that the Subordinated Notes are properly classified as equity for U.S. federal income tax purposes or that the interest rate on the Subordinated Notes is in excess of an arm's length interest rate, which could adversely affect the amount, timing and character of income, gain or loss in respect of a holder's investment in IPSs or

Subordinated Notes, and materially increase the Company's taxable income and, thus, the Company's U.S. federal and applicable state income tax liability. This would adversely affect the Company's financial position, cash flow, and liquidity, and could affect the Company's ability to make interest or dividend payments on the Subordinated Notes and the common shares owned by Keystone North America and may affect the Company's ability to continue as a going concern.

In addition, if the Subordinated Notes are reclassified as equity for U.S. federal income tax purposes, Non-U.S. Holders, as defined in "Certain U.S. Federal Income Tax Considerations" below may be subject to U.S. federal withholding or estate taxes with respect to the Subordinated Notes and the Company could be liable for withholding taxes on any interest payments previously made to Non-U.S. Holders. Payments to foreign holders would not be grossed-up for any such taxes. The Company's tax deduction for interest may be put at risk in the future as a result of a change in law or administrative or judicial rulings issued in the future and, in such event, the Company may need to consider the effect of such developments on the determination of the Company's future tax provisions and obligations. For discussion of these tax-related risks, see "Certain U.S. Federal Income Tax Considerations."

***If the Issuer subsequently issues Subordinated Notes with significant OID, the Issuer may not be able to deduct all of the interest on the Subordinated Notes.***

Subordinated Notes issued in a subsequent issuance may be issued at a discount to their face value and, accordingly, such notes may have "significant OID" and thus be classified as "applicable high yield discount obligations" for U.S. federal income tax purposes. If any such Subordinated Notes were so treated, a portion of the OID on such notes would be non-deductible by the Company and the remainder would be deductible only when paid. It is also possible that Subordinated Notes issued in a subsequent issuance will be treated as equity for tax purposes. If any such Subordinated Notes were so treated, the interest payable on such Subordinated Notes would be non-deductible by the Company. Any limit on the Company's ability to deduct interest for tax purposes would have the effect of increasing the Company's taxable income and may adversely affect the Company's cash flow available for interest payments and distributions to the Company's shareholders.

***An allocation of IPS purchase price that results in OID may reduce the amount a holder can recover upon an acceleration of the payment of principal due on the Subordinated Notes or in the event of the Issuer's bankruptcy.***

Under New York and U.S. federal bankruptcy law, if the Subordinated Notes are treated as issued with OID because the allocation of the purchase price is not respected, holders of such Subordinated Notes having OID may not be able to collect the portion of the principal face amount of such Subordinated Notes that represents unamortized OID as of the acceleration or filing date, as the case may be, in the event of an acceleration of the Subordinated Notes or in the event of the Issuer's bankruptcy prior to the maturity date of the Subordinated Notes. As a result, a treatment of the Subordinated Notes as having been issued with OID could have the effect of ultimately reducing the amount such holder can recover from us in the event of an acceleration or bankruptcy.

***The Company or other payor may not be able to properly report OID to the holders of IPSs or Subordinated Notes and the IRS, and hence may become subject to substantial IRS penalties for such failure.***

The Internal Revenue Code generally requires that the payor of interest and OID to report to its payees and the IRS the amounts of interest and OID includable in income with respect to such payees, unless an exception to reporting applies. If the IPSs or Subordinated Notes issued in this offering are issued with OID and there is a subsequent issuance of Subordinated Notes or if any subsequent issuance of IPSs or Subordinated Notes is issued with OID and, in either case, no exception to reporting applies, the Company or other payor may not be able to properly report the amount of OID to the proper payee because all of the Subordinated Notes are being issued and will be traded under the same CUSIP number and will be held in book-entry form in the name of the CDS or its nominee, CDS & Co. As a result, the identity of the holders of the Subordinated Notes issued with OID may not be known, and hence the Company or other payor may not be able to properly report OID to the IRS and to the proper payees.

In such circumstances, the Company or other payor may choose to report such OID to all holders of Subordinated Notes regardless of whether such holders acquired the Subordinated Notes in this offering or a subsequent issuance, unless an exception to reporting applies. The Company believes that such reporting may satisfy the OID reporting requirements and hence reduce or eliminate any exposure of Keystone to penalties for not properly reporting. Non-U.S. Holders who qualify for the Portfolio Interest Exemption generally should not be subject to OID reporting, and hence generally should not be impacted by such reporting.

As a result, a holder subject to OID reporting may be required to report OID even though such holder purchased Subordinated Notes having no OID unless such holder can establish to the IRS that its Subordinated Notes do not have OID. The IRS might assert that, unless a holder can establish that it is not holding Subordinated Notes with OID, all Subordinated Notes held by such holder will have OID. Prospective investors should consult their own tax advisor to determine the particular U.S. federal income tax consequences of OID, including the proper reporting of OID in these circumstances and the applicability and effect of U.S. state and local tax laws.

The penalties for failure to properly file and report such OID amounts to the IRS is generally capped at $250,000 for all such failures during any calendar year, but if such failure is due to the intentional disregard of the filing requirement, the penalty is the greater of $100 for each return with respect to which a failure occurs or 10% of the aggregate amount of items required to be reported correctly. The penalties for failure to properly furnish and report such amounts to a payee of OID is generally capped at $100,000 for all such failures during any calendar year, but if such failure is due to the intentional disregard of the filing requirement, the penalty is the greater of $100 for each return with respect to which a failure occurs or 10% of the aggregate amount of items required to be reported correctly. A failure is due to intentional disregard if it is a knowing or willful failure to file timely or to include the correct information, which determination is made based on all the facts and circumstances of the particular case. A failure by the Company or other payor to properly report OID in the case of the IPSs and Subordinated Notes may be treated as due to an intentional disregard, and therefore could result is substantial penalties.

***The Subordinated Notes issued in this offering or Subordinated Notes issued in a subsequent offering may have OID for U.S. federal income tax purposes.***

The Subordinated Notes issued in this offering and Subordinated Notes issued in a subsequent offering may be treated as having been issued with OID for U.S. federal income tax purposes in certain circumstances, *e.g.*, if the allocation of the purchase price of each IPS to the subordinated notes were determined to be too high or if the likelihood of a deferral of interest payments on the Subordinated Notes were determined not to be "remote" or an interest deferral actually occurred.

A Non-U.S. Holder generally would not be subject to U.S. federal income tax with respect to such OID so long as such OID is not effectively connected with such holder's conduct of a trade or business within the U.S. and such holder qualifies for the Portfolio Interest Exemption. See "Certain U.S. Federal Income Tax Considerations — Taxation of Non-U.S. Holders — Subordinated Notes". If the Non-U.S. Holder failed to satisfy these requirements, a holder generally would be required to include OID in income in advance of the receipt of cash attributable to that income, and such OID may be subject to U.S. federal income or withholding taxes, see "Certain U.S. Federal Income Tax Considerations." Prospective investors should consult their own tax advisor to determine the particular U.S. federal income tax consequences of OID, including the applicability and effect of U.S. state and local tax laws.

The requirement to include OID in income in advance of the receipt of cash attributable to that income may discourage U.S. persons and those Non-U.S. Holders subject to U.S. federal income tax on OID from acquiring Subordinated Notes and may adversely affect the liquidity of the IPSs and Subordinated Notes.

***Certain U.S. tax considerations may discourage third parties from pursuing a tender offer or other change of control transaction.***

Under certain circumstances, Code Section 163(j) limits a corporation's deductions for interest paid to related foreign persons exempt from U.S. tax. For these purposes, a corporation and a creditor of the corporation will generally be "related" if the creditor owns, directly or by attribution, more than 50% of the corporation by vote or value. The purchase of an IPS will be treated for U.S. tax purposes as a purchase of both an equity interest and a creditor's interest in the Issuer. As a result, a purchase by any non-U.S. person of more than 50% of the IPSs could result in Keystone's interest deductions being limited with respect to the Subordinated Notes represented by those IPSs or otherwise owned by such person. This could discourage third parties from pursuing a tender offer or other change of control transaction with respect to the Issuer, which otherwise might have led to a premium being paid for IPSs.

***We may not be able to make all principal payments on the Subordinated Notes.***

The Subordinated Notes will mature 12 years after the date of issuance. Keystone ULC may not be able to refinance the principal amount of the Subordinated Notes in order to repay the principal outstanding or may not have generated enough cash from operations to meet this obligation. There is no guarantee that Keystone ULC will be able to repay the outstanding principal amount upon maturity of the Subordinated Notes.

As a result of the subordinated nature of the guarantees of the Subordinated Notes, upon any distribution to creditors of the Company in a bankruptcy, liquidation or reorganization or similar proceeding relating to the Company or its property or assets, the holders of the Company's senior indebtedness will be entitled to be paid in full in cash before any payment may be made with respect to the Subordinated Notes under the guarantee provided by the Company.

***There is no public market for the IPSs, Common Shares and Subordinated Notes and holders may have limited liquidity.***

Neither the IPSs, the Common Shares nor the Subordinated Notes have a public market history. No assurance can be made that an active trading market for the IPSs will develop in the future, and we currently do not expect that an active trading market for the Common Shares will develop until the Subordinated Notes mature. If the Subordinated Notes represented by the IPSs mature or are redeemed or repurchased, the IPSs will be automatically separated. There is no intention to list the Subordinated Notes on any stock exchange. BMO Nesbitt Burns Inc. has advised us that it currently intends to make a market in the Subordinated Notes subject to customary market practice and applicable legal and regulatory requirements and limitations. However, BMO Nesbitt Burns Inc. is not obligated to do so and may discontinue any such activities, if commenced, at any time and without notice. Moreover, if and to the extent that BMO Nesbitt Burns Inc. makes a market for the Subordinated Notes, there can be no assurance that such market would provide sufficient liquidity for any holder of any such securities.

***The Market Price for the IPSs, Common Shares or Subordinated Notes may be volatile.***

Prior to the offering, there has been limited public market for income participating securities. The offering price of the IPSs offered in the offering has been determined by negotiations between us, the Existing Investors and the Underwriters of the offering and may not be indicative of the market price of the IPSs after the offering is completed. Factors such as variations in our financial results, announcements by us or others, developments affecting our business or the death care industry, general interest rate levels, the market price of the Common Shares and general market volatility could cause the market price of the IPSs, the Common Shares or the Subordinated Notes to fluctuate significantly.

In addition, future sales or the availability for sale of substantial amounts of IPSs or Common Shares or a significant principal amount of Subordinated Notes in the public market could adversely affect the prevailing market price of the IPSs, the Common Shares and the Subordinated Notes and could impair our ability to raise capital through future sales of our securities.

***Keystone's interest deductions on the Subordinated Notes are likely "dual consolidated losses" for U.S. federal income tax purposes and may result in disallowance of interest deductions if certain "triggering events" occur.***

Pursuant to Code section 1503(d) and the Treasury Regulations thereunder, the interest deductions generated on the Subordinated Notes will likely generate a "dual consolidated loss" ("DCL") for U.S. federal income tax purposes and will therefore be deductible by Keystone only if Keystone and Keystone ULC make the election provided by Treasury Regulation 1.1503-2(g)(2) and comply with all applicable requirements, including annual reporting and certification requirements. Keystone and Keystone ULC intend to make such election and comply with all applicable requirements. Even if such an election is made, however, if any of several "triggering events" occurs (*e.g.*, the use of such losses to offset the income of any other non-U.S. person, or, in certain circumstances, a disposition of Keystone ULC stock or assets), Keystone will generally be required to report the amount of any prior interest deductions on the subordinated notes (plus interest thereon) as gross income in the year of the triggering event. Keystone and Keystone ULC intend to comply with all of the DCL reporting and certification requirements and to conduct their affairs such that no DCL triggering event occurs. However, if Keystone and Keystone ULC fail to satisfy such reporting and certification requirements, or if a DCL triggering event occurs and no exception applies, Keystone's taxable income and thus its U.S. federal income tax liability would be materially increased. This would adversely affect Keystone's financial position, cash flow, and liquidity, and could affect the Company's ability to make interest or dividend payments on the Subordinated Notes and the Common Shares and may affect the Company's ability to continue as a going concern.

***Recent U.S. federal income tax legislation***

Recently enacted U.S. federal income tax legislation dealing with corporate "inversions" (*e.g.*, certain transactions in which a non-U.S. corporation acquires substantially all of the equity interests in, or the assets of, a U.S. corporation or partnership, if, after the transaction, former equity owners of the U.S. corporation or partnership own a specified level of stock in the non-U.S. corporation) provides in certain cases that a non-U.S. corporation may be treated as a U.S. corporation for U.S. federal income tax purposes. As enacted, this legislation does not apply to Keystone North America, because the shareholders of Keystone will not own any stock in Keystone North America as a result of the offering and related transactions. The legislation grants authority to the Internal Revenue Service to write implementing regulations, which could, if exercised broadly and retroactively, cause the new provisions to apply to Keystone North America and result in U.S. withholding taxes being imposed on dividends paid on the Common Shares to Non-U.S. Holders. Certain advisors of Keystone may have discussions with U.S. tax authorities to explain why such regulations should not extend to a number of transactions, including transactions such as this one. The outcome of such discussions is uncertain.

***Ownership change will limit our ability to use certain losses for U.S. federal income tax purposes and may increase our tax liability.***

The transactions contemplated herein will result in an "ownership change" within the meaning of the U.S. federal income tax laws addressing net operating loss carryforwards, alternative minimum tax credits and other similar tax attributes. As a result of such ownership change, as well as any prior ownership changes (if any), there will be specific limitations on our ability to use our net operating loss carryforwards and other tax attributes from periods prior to this offering. It is possible in the future that such limitations could limit our ability to utilize such tax attributes and, therefore, result in an increase in our U.S. federal income tax liability. Such an increase would reduce the funds available for the payments of dividends on the Class A common shares and interest on the Subordinated Notes.

***Because Keystone, the promoter of this offering, is organized under the laws of a foreign jurisdiction and resides outside of Canada, certain civil liabilities and judgments may not be enforceable against it.***

Keystone is the promoter of this offering and is organized under the laws of a foreign jurisdiction and resides outside Canada. All of its directors and officers and certain of the experts named elsewhere in this prospectus are residents of countries other than Canada. All of Keystone's assets and the assets of these persons are located outside of Canada. As a result, although Keystone has appointed Keystone North America as its agent for service of process in Ontario, it may be difficult for IPS holders to initiate a lawsuit within Canada against these non-Canadian residents. In addition, it may not be possible for holders of IPSs to collect from Keystone or these other non-Canadian residents judgements obtained in courts in Canada predicated on the civil liability provisions of securities legislation of certain of the provinces and territories of Canada. It may also be difficult for IPS holders to succeed in a lawsuit in the United States, based solely on violations of Canadian securities laws.

## PLAN OF DISTRIBUTION

Pursuant to an underwriting agreement dated January 28, 2005, among Keystone North America, Keystone ULC, Keystone, the Existing Investors, and the Underwriters, we have agreed to sell 17,100,000 IPSs and the Underwriters have agreed to purchase, as principals, on closing, subject to the conditions stipulated in the underwriting agreement, all but not less than all of such IPSs at a price of C$10.00 per IPS payable in cash. The underwriting agreement provides that the Underwriters will be paid a fee of C$0.575 per IPS purchased in consideration for services performed in connection with the offering.

The obligations of the Underwriters under the underwriting agreement are conditional and may be terminated at their discretion on the basis of their assessment of the state of the financial markets and may also be terminated in certain stated circumstances and upon the occurrence of certain stated events. The Underwriters are, however, severally obligated to take up and pay for all offered IPSs that they have obliged themselves to purchase if any of the offered IPSs are purchased under the underwriting agreement.

The Issuer has granted the Underwriters an over-allotment option, to cover over-allotments, if any, and for market stabilization purposes. This prospectus also qualifies the distribution of the over-allotment option and the distribution of up to 1,668,017 IPSs issuable upon exercise of the over-allotment option.

The underwriting agreement contains customary representations and warranties and related indemnities from Keystone North America, Keystone ULC and Keystone in favour of the Underwriters as to various matters.

Subscriptions for IPSs will be received subject to rejection or allotment in whole or in part and the right is reserved to close the subscription books at any time without notice.

The IPSs have not been and will not be registered under the United States *Securities Act of 1933*, as amended (the "U.S. Securities Act") and, subject to certain exemptions, may not be offered or sold in the United States or to, or for the account or benefit of, U.S. Persons (as defined by Regulation S under the U.S. Securities Act). The Underwriters have agreed that, except in accordance with Rule 144A and Regulation S under the U.S. Securities Act, they will not offer or sell the IPSs within the United States or to, or for the account or benefit of, U.S. Persons.

In addition, until 40 days after the closing, an offer or sale of IPSs within the United States by a dealer (whether or not participating in this offering) may violate the registration requirements of the U.S. Securities Act if that offer or sale is made otherwise than in accordance with Rule 144A.

Pursuant to policy statements of the Ontario Securities Commission and the Autorité des marchés financiers, the Underwriters may not, throughout the period of distribution, bid for or purchase IPSs. The foregoing restriction is subject to exceptions, on the condition that the bid or purchase is not engaged in for the purpose of creating actual or apparent active trading in, or raising the price of, IPSs. These exceptions include a bid or purchase permitted under the by-laws and rules of the TSX relating to market stabilization and passive market-making activities and a bid or purchase made for and on behalf of a customer where the order was not solicited during the period of distribution. Under the first-mentioned exception, in connection with this offering, the Underwriters may over-allot or effect transactions which stabilize or maintain the market price of the IPSs at levels other than those which might otherwise prevail in the open market. Those transactions, if commenced, may be discontinued at any time.

Each of Keystone North America and Keystone ULC has agreed not to, directly or indirectly, sell or issue, or negotiate or enter into an agreement to sell or issue, any of its securities and each Existing Investor and Existing Lender has agreed not to, directly or indirectly, (i) exercise the Negotiation Right for a period of 180 days following the date of closing, or (ii) sell, contract to sell, grant any option to purchase, transfer, assign or otherwise dispose of any IPSs, Common Shares, Subordinated Notes and Class B and Class C common shares, without the prior consent of BMO Nesbitt Burns Inc., on behalf of the Underwriters, other than in connection with specific types of transactions.

**There is currently no market through which the IPSs, and the Common Shares and Subordinated Notes represented thereby, may be sold and purchasers may not be able to resell securities purchased under this prospectus.** The TSX has conditionally approved the listing of the IPSs and the Common Shares. Listing is subject to the Issuer fulfilling all of the requirements of the TSX on or before April 22, 2005. While it is a condition of Closing that the Common Shares be listed on the TSX, the Common Shares will not be posted for trading on the TSX until there exists a sufficient public distribution (for the purposes of the listing requirements of the TSX) of Common Shares that are held separately from Subordinated Notes. For the purposes of the listing requirements of the TSX, a sufficient public distribution of Common Shares will exist when at least one million freely tradeable Common Shares having an aggregate market value of C$4 million are held by at least 300 public holders, each holding one board lot or more. The terms of the distribution, including the price and number of IPSs offered, were determined by negotiation between Keystone North America, Keystone ULC, and the Underwriters.

The Separate Subordinated Notes, which will constitute at least 10% of the aggregate principal amount of the Subordinated Notes at closing, will be issued other than as part of the IPSs on a private placement basis concurrently with the closing of the offering. The offering of the IPSs is conditional upon the closing of the offering of the Separate Subordinated Notes.

An affiliate of BMO Nesbitt Burns Inc. has arranged to make credit facilities available to a subsidiary of the Issuer. As a result, the Issuer may be considered a "connected issuer" of BMO Nesbitt Burns Inc. See "New Credit Facility".

## AUDITORS, TRANSFER AGENT AND REGISTRAR

Our auditors are Ernst & Young LLP, Tampa, FL.

The transfer agent and registrar for the IPSs and the Common Shares is Computershare Trust Company of Canada at its principal office in Toronto, Ontario.

## CURRENCY AND EXCHANGE RATE INFORMATION

In this prospectus, references to "C$" and "Canadian dollars" are to the lawful currency of Canada and references to "$", "US$" and "U.S. dollars" are to the lawful currency of the United States. **All dollar amounts herein are in U.S. dollars, unless otherwise stated. The translation exchange rate used in this prospectus is the hedge rate of US$1.00 = C$1.2272.**

Our business is conducted primarily in the United States and our revenue and expenses are denominated, earned and incurred primarily in U.S. dollars. Accordingly, the *pro forma* consolidated financial statements and the financial statements of the Company and Hamilton included in this prospectus are presented in U.S. dollars. The following table sets forth, for each period indicated, the high and low exchange rates for one U.S. dollar, expressed in Canadian dollars, the average of such exchange rates on the last day of each month during such period and the exchange rate at the end of such period, based on the noon rate in Canadian dollars as quoted by the Bank of Canada (the "Noon Buying Rate"). On January 28, 2005, the Noon Buying Rate was US$1.00 = C$1.2421.

| | Nine Months Ended September 30, | | Twelve Months Ended December 31, | | |
|---|---|---|---|---|---|
| | 2004 | 2003 | 2003 | 2002 | 2001 |
| High | 1.3968 | 1.5747 | 1.5747 | 1.6132 | 1.6021 |
| Low | 1.2639 | 1.3342 | 1.2924 | 1.5110 | 1.4936 |
| Average(1) | 1.3290 | 1.4209 | 1.3914 | 1.5699 | 1.5513 |
| Period End | 1.2639 | 1.3504 | 1.2924 | 1.5796 | 1.5926 |

(1) The average of the exchange rates on the last day of each month during each period.

## ELIGIBILITY FOR INVESTMENT

In the opinion of Goodmans LLP, Canadian counsel to the Issuer and Keystone, and of Torys LLP, counsel to the Underwriters, on the date of this prospectus, the Common Shares and Subordinated Notes represented by the IPSs if, as and when the Common Shares are listed on a prescribed stock exchange (which currently includes the TSX) will be qualified investments under the *Income Tax Act* (Canada) and the regulations thereunder (the "Tax Act") for trusts governed by registered retirement savings plans, registered retirement income funds, deferred profit sharing plans (except that the Subordinated Notes will not be qualified investments for trusts governed by a deferred profit sharing plan to which contribution payments are made by Keystone ULC or a person with whom Keystone ULC does not deal at arm's length within the meaning of the Tax Act) and registered education savings plans (collectively, the "plans") at that time. Based, in part, on certificates of the Issuer as to certain factual maters, the Common Shares and the Subordinated Notes represented by the IPSs will not constitute "foreign property" for the purposes of the tax imposed under Part XI of the Tax Act on those plans (other than registered education savings plans), registered investments and other tax exempt entities including most registered pension funds and registered pension plans. Registered education savings plans are not subject to the foreign property rules. See "Certain Canadian Federal Income Tax Considerations".

## MATERIAL CONTRACTS

The only material contracts, other than contracts entered into in the ordinary course of business, to which the Issuer or the Company will become a party prior to or at closing of this offering are as follows:

- the Hamilton Acquisition Agreement referred to under "Investment Agreement";
- the Investment Agreement referred to under "Investment Agreement";
- the LTIP referred to under "Directors, Officers and Management — Long-Term Incentive Plan";
- the New Credit Facility referred to under "New Credit Facility";
- the Securityholders' Agreement referred to under "Securityholders' Agreement";
- the Subordinated Note Indenture referred to under "Description of Subordinated Notes"; and
- the Underwriting Agreement referred to under "Plan of Distribution".

Copies of these agreements may be examined at the head and principal office of Keystone North America during normal business hours.

## LEGAL PROCEEDINGS

In the ordinary course of business, we may, from time to time, be subject to various pending and threatened lawsuits in which claims for monetary damages are asserted. We are not involved in any legal proceedings that we expect to have a material effect on us. To our knowledge, no legal proceedings of a material nature involving us have been pending or threatened by any individuals, entities or governmental authorities.

## PROMOTER

Keystone is considered to be a promoter of the Issuer by reason of its initiative in organizing the business and affairs of the Issuer.

## EXPERTS

The matters referred to under "Eligibility for Investment" and "Certain Canadian Federal Income Tax Considerations" and certain other legal matters relating to the IPSs offered by this prospectus will be passed upon at the date of closing on behalf of us by Goodmans LLP and on behalf of the Underwriters by Torys LLP. The matters referred to under "Certain U.S. Federal Income Tax Considerations" will be passed upon at the date of closing on behalf of us by Kirkland & Ellis LLP and on behalf of the Underwriters by Torys LLP.

As of the date hereof, the partners and associates of Goodmans LLP, Torys LLP and Kirkland & Ellis LLP, did not beneficially own, directly or indirectly, any of our outstanding securities.

## CERTAIN CANADIAN FEDERAL INCOME TAX CONSIDERATIONS

In the opinion of Goodmans LLP, Canadian counsel to the Issuer and the Company and Torys LLP, counsel to the Underwriters, the following is, as of the date of this prospectus, a summary of the principal Canadian federal income tax considerations generally applicable under the Income Tax Act (Canada) and the regulations thereunder (the "Tax Act") to a holder who acquires Common Shares and Subordinated Notes as represented by IPSs pursuant to this offering and who, for purposes of the Tax Act and at all relevant times, is resident or is deemed to be resident in Canada, holds the Common Shares and Subordinated Notes represented by IPSs as capital property and deals at arm's length and is not affiliated with the Issuer or the Company (a "Holder" for the purposes of this section only). Generally, the Common Shares and Subordinated Notes represented by the IPSs will be considered to be capital property to a Holder provided that the Holder does not hold such securities in the course of carrying on a business of buying and selling securities and has not acquired them in one or more transactions considered to be an adventure in the nature of trade. Certain Holders who might not otherwise be considered to hold their Common Shares and Subordinated Notes represented by IPSs as capital property may, in certain circumstances, be entitled to have them treated as capital property by making the irrevocable election permitted by subsection 39(4) of the Tax Act.

This summary is not applicable to a Holder that is a "financial institution" (as defined in the Tax Act for purposes of the mark-to-market rules), a "specified financial institution" or a Holder an interest in which is a "tax shelter investment" (all as defined in the Tax Act).

This summary is based upon the facts set out in this prospectus, the provisions of the Tax Act in force on the date of this prospectus, counsels' understanding of the current published administrative policies and assessing practices of the Canada Customs and Revenue Agency (the "CCRA") and certificates from the Issuer as to certain factual matters. This summary takes into account all specific proposals to amend the Tax Act which have been publicly announced by or on behalf of the Minister of Finance (Canada) prior to the date of this prospectus. There can be no assurance that any such tax proposals will be implemented in their current form or at all. This summary does not otherwise take into account or anticipate any changes in law, whether by legislative, governmental or judicial decision or action, or administrative policies or assessing practices, and does not take into account any provincial, territorial or foreign tax legislation or considerations which may differ significantly from those discussed in the prospectus.

**This summary is of a general nature only and is not exhaustive of all possible Canadian federal income tax considerations applicable to an investment in Common Shares and Subordinated Notes represented by IPSs. Moreover, the income or other tax consequences of acquiring, holding or disposing of Common Shares and Subordinated Notes represented by IPSs will vary depending on the Holder's particular circumstances, including the province or territory or provinces or territories in which the Holder resides or carries on business. Accordingly, this summary is of a general nature only and is not intended to be legal or tax advice to any prospective purchaser of Common Shares and Subordinated Notes represented by IPSs. Investors should consult their own tax advisors for advice with respect to the tax consequences of an investment in Common Shares and Subordinated Notes represented by IPSs based on their particular circumstances.**

### Nature of IPSs

In acquiring an IPS, a Holder will be acquiring ownership of the Common Share and Subordinated Notes represented by such IPS. The Common Share and Subordinated Notes represented by an IPS are separate properties and, accordingly, the price paid by a Holder for an IPS must be allocated on a reasonable basis between the Common Share and Subordinated Notes represented by the IPS in order to determine their respective cost to the Holder for purposes of the Tax Act. Such cost will establish a Holder's initial adjusted cost base of the Common Share and Subordinated Notes represented by the Holder's IPS. The Issuer proposes to allocate the price paid for each IPS on the basis of C$5.714 to the Common Share and C$4.286 to the Subordinated Notes and, by purchasing an IPS, a Holder is deemed to agree to such allocation. Although the Issuer believes this allocation to be reasonable, such allocation is not binding on the CCRA.

In disposing of an IPS, a Holder will be disposing of the Common Share and Subordinated Notes represented by such IPS. Any proceeds from the disposition (or deemed disposition) of an IPS must be allocated on a reasonable basis between the Common Share and Subordinated Notes represented by such IPS.

The separation by a Holder of an IPS into the Common Share and Subordinated Notes represented by such IPS will not be a disposition for purposes of the Tax Act, and, as such, the Holder will not realize a gain or loss upon such separation of the IPS into a Common Share and Subordinated Notes. The Holder's adjusted cost base of the Common Share and Subordinated Notes represented by an IPS will not be affected by such separation of an IPS into a Common Share and Subordinated Notes. Similarly, the combination by a Holder of a Common Share and Subordinated Notes into an IPS representing such Common Share and Subordinated Notes will not be a disposition for purposes of the Tax Act, and, as such, the Holder will not realize a gain or loss upon such delivery of the Common Share and Subordinated Notes in return for an IPS representing such Common Share and Subordinated Notes. The Holder's adjusted cost base of the Common Share and Subordinated Notes will not be affected by such delivery of the Common Share and Subordinated Notes in return for an IPS representing such Common Share and Subordinated Notes.

**Taxation of Keystone North America and Keystone ULC**

The Company will be a "foreign affiliate" and a "controlled foreign affiliate" of both Keystone North America and Keystone ULC for Canadian income tax purposes. Dividends paid by the Company to Keystone North America and Keystone ULC will be included in computing the income of Keystone North America and Keystone ULC. However, to the extent that such dividends are considered to have been paid out of the "exempt surplus" of the Company with respect to Keystone North America and Keystone ULC the amount of such dividends will be deductible in computing the taxable income of Keystone North America and Keystone ULC. Dividends that are not paid out of "exempt surplus" will be generally considered to have been paid out of the "pre-acquisition surplus" of the Company with respect to Keystone North America and Keystone ULC. The amount of such dividends will also be deductible in computing the taxable income of Keystone North America and Keystone ULC. The adjusted cost base to Keystone North America of its Common Shares in the Company and adjusted cost base to Keystone ULC of its preferred shares in the Company will be reduced to the extent that dividends paid by the Company are considered to have been paid out of the "pre-acquisition surplus" of the Company with respect to Keystone North America and Keystone ULC. If the adjusted cost base to Keystone North America or Keystone ULC of their shares in the Company becomes a negative amount, Keystone North America or Keystone ULC will be deemed to realize a capital gain equal to such amount for that year. To the extent that the Company or any direct or indirect wholly owned subsidiary thereof earns income that qualifies as "foreign accrual property income" ("FAPI"), the FAPI allocable to Keystone North America and Keystone ULC must be included in computing the income of Keystone North America and Keystone ULC for Canadian income tax purposes, whether or not Keystone North America and Keystone ULC actually receive a distribution of FAPI. Any amount so included will increase the adjusted cost base to Keystone North America and Keystone ULC of their shares in the Company. At such time as Keystone North America and Keystone ULC receives a dividend of this type of income that was previously treated as FAPI, that dividend will effectively not be taxable to Keystone North America and Keystone ULC and there will be a corresponding reduction in the adjusted cost base to Keystone North America and Keystone ULC of their shares in the Company.

Keystone ULC generally will be entitled to deduct the interest paid by it on the Subordinated Notes in computing its income to the extent such amount is reasonable in the circumstances. To the extent that the deduction for interest on the Subordinated Notes (and other deductible expenses of Keystone ULC) creates a loss in a taxation year of Keystone ULC, that loss will be a non-capital loss which may be carried back for three taxation years and forward for ten taxation years and applied against the income of Keystone ULC (including taxable capital gains) for such years subject to the detailed rules in the Tax Act in that regard. Tax proposals (the "Tax Proposals") applicable to taxation years that begin after 2004 will only allow a taxpayer to recognize a loss for a taxation year from a source which is a business or property if, in the taxation year in question, it is reasonable to expect the taxpayer to realize a cumulative profit from that business or property during the time that the taxpayer has carried on, or can reasonably be expected to carry on that business, or has held, or can reasonably be expected to hold, that property. Profit, for these purposes, is intended to mean profit determined in accordance with generally accepted commercial principles. Keystone ULC has advised counsel that it reasonably expects to realize a cumulative profit from its properties during the period it reasonably expects to hold such properties. Keystone ULC will continue to monitor the Tax Proposals as their proposed effective date approaches.

**Taxation of Dividends, Interest and Capital Gains**

Since a Holder who holds an IPS will own the Common Share and Subordinated Notes represented by such IPS, the income tax consequences under the Tax Act of owning and disposing of an IPS (including the taxation of dividends and interest on the Common Share and Subordinated Notes, respectively, and the tax treatment of disposing of the Common Share and Subordinated Notes upon the disposition of an IPS representing such securities) will not differ from those associated with owning and disposing of those securities as is described below.

***Interest on the Subordinated Notes***

A Holder that is a corporation, partnership, unit trust or a trust of which a corporation or partnership is a beneficiary will be required to include in computing its income for a taxation year all interest that accrues to such Holder on the Subordinated Notes to the end of that year or that becomes receivable or is received by the Holder before the end of that year, except to the extent that such interest was included in computing the Holder's income for a preceding taxation year. Any other Holder, including an individual, will be required to include in computing its income for a taxation year all interest on the Subordinated Notes that is received or receivable by such Holder in that year (depending on the method regularly followed by the Holder in computing income) to the extent that such interest was not included in computing the Holder's income for a preceding taxation year. In addition, a Holder may be required to include in computing its income for a taxation year any interest that accrues to the Holder on the Subordinated Notes up to any "anniversary day" (as defined in the Tax Act) of the Subordinated Notes in the year to the extent that such amount was not otherwise included in the Holder's income for that or a preceding taxation year. If interest on the Subordinated Notes is deferred, a Holder will be required to include such amount in computing its income in accordance with the foregoing even though the Holder has not received a cash interest payment.

A Holder that is a "Canadian-controlled private corporation" (as defined in the Tax Act) may be liable to pay a refundable tax of 6⅔% on investment income, including interest income on the Subordinated Notes.

The amount of interest on the Subordinated Notes to be included in a Holder's income as described above will include United States withholding tax, if any, imposed in respect of the interest. To the extent that United States withholding tax is imposed in respect of interest on the Subordinated Notes, the amount of such tax generally will be eligible for foreign tax credit or deduction treatment where applicable, subject to the detailed rules and limitations under the Tax Act. Holders are advised to consult their own tax advisors with respect to the availability of a credit or deduction to them having regard to their particular circumstances.

***Disposition of Subordinated Notes***

On a disposition or a deemed disposition (which will include a redemption of the Subordinated Notes or repayment at maturity) of Subordinated Notes, a Holder will generally be required to include in computing its income for the taxation year in which the disposition occurs the amount of interest accrued on the Subordinated Notes from the date of the last interest payment to the date of disposition, except to the extent that such interest has otherwise been included in computing the Holder's income for that year or a preceding taxation year.

Any amount paid by the Issuer as a penalty or bonus because of early repayment of all or part of the principal amount of the Subordinated Notes will be deemed to be received by the Holder as interest on the Subordinated Notes and included in computing the Holder's income as described above, to the extent such amount can reasonably be considered to relate to, and does not exceed the value at the time of payment of, interest that would otherwise have been payable on the Subordinated Notes for periods ending after the payment of such amount.

In general, a disposition or a deemed disposition of a Subordinated Note by a Holder will give rise to a capital gain (or a capital loss) equal to the amount by which the proceeds of disposition, net of any amount included in computing the Holder's income as interest and any reasonable costs of disposition, exceed (or are exceeded by) the adjusted cost base of the Subordinated Note to the Holder immediately before the disposition. See "— Capital Gains and Losses" below.

### *Dividends on the Common Shares*

Dividends received or deemed to be received by a Holder on the Common Shares will be required to be included in computing the Holder's income for purposes of the Tax Act. Dividends received or deemed to be received by a Holder who is an individual will be subject to the gross-up and dividend tax credit rules generally applicable to taxable dividends received by an individual from taxable Canadian corporations. A Holder that is a corporation generally will be entitled to deduct the amount of the dividend received or deemed to be received in computing its taxable income. A Holder that is a "private corporation" or "subject corporation" (as such terms are defined in the Tax Act) will generally be liable under Part IV of the Tax Act to pay a refundable tax of 33⅓% of the dividends received or deemed to be received on the Common Shares to the extent that such dividends are deductible in computing the Holder's taxable income.

### *Disposition of the Common Shares*

A disposition or deemed disposition of Common Shares by a Holder will generally give rise to a capital gain (or capital loss) to the extent that the proceeds of disposition, net of any reasonable costs of disposition, exceed (or are less than) the adjusted cost base to the Holder of the Common Shares immediately before the disposition. See "— Capital Gains and Losses" below.

### *Capital Gains and Losses*

One-half of the amount of any capital gain (a "taxable capital gain") realized by a Holder in a taxation year must be included in computing such Holder's income for that year, and one-half of any capital loss (an "allowable capital loss") realized by a Holder in a taxation year may be deducted from any taxable capital gains realized by the Holder in the year. Allowable capital losses in excess of taxable capital gains realized in a taxation year may be carried back and deducted in any of the three preceding taxation years or carried forward and deducted in any following taxation year against taxable capital gains realized in such years, subject to and in accordance with the provisions of the Tax Act. A capital loss realized by certain Holders in respect of the disposition or deemed disposition of Common Shares may be reduced in certain circumstances by the amount of any dividends, including deemed dividends, that have been received by such Holders on the Common Shares to the extent and in the manner provided for in the Tax Act.

A holder that is a Canadian-controlled private corporation (as defined in the Tax Act) may be liable to pay an additional refundable tax of 6⅔% on investment income, including taxable capital gains.

### *Alternative Minimum Tax*

Individuals, including certain trusts, are subject to an alternative minimum tax. Dividends received or deemed to be received on the Common Shares and capital gains realized on a disposition or deemed disposition of Common Shares or Subordinated Notes may increase a Holder's liability for alternative minimum tax. Holders should consult their own advisors with respect to alternative minimum tax.

## CERTAIN U.S. FEDERAL INCOME TAX CONSIDERATIONS

In the opinion of Kirkland & Ellis LLP, U.S. tax counsel to the Issuer and Torys LLP, U.S. tax counsel to the Underwriters, together, "U.S. Tax Counsel", the following summary describes, as of the date of this prospectus, the material U.S. federal income tax considerations applicable to Non-U.S. Holders, as defined below, with respect to the purchase, ownership and disposition of IPSs, Subordinated Notes or Common Shares. Such opinion is based in part on facts described in this prospectus and on various assumptions, representations and determinations. Any alteration or incorrectness of such facts, assumptions, representations or determinations could adversely affect such opinion. This summary is directed only to prospective purchasers of IPSs or the Subordinated Notes sold separately in this offering who are Non-U.S. Holders. In addition to this summary, see "Risk Factors — Risks Related to the Capital Structure".

This summary is of a general nature only and is not intended to be legal or tax advice to any prospective purchaser of IPSs or Subordinated Notes sold separately, and is not a substitute for careful tax planning and advice. Prospective purchasers should consult their own tax advisors in determining the application to them of the U.S. federal income tax consequences set forth below and any other U.S. federal, state, local, foreign or other tax consequences to them of the purchase, ownership and disposition of IPSs, Subordinated Notes or Common Shares.

This summary addresses only IPSs, Subordinated Notes and Common Shares held as capital assets by Non-U.S. Holders who acquired IPSs upon their original issuance at their initial offering price in this offering or Subordinated Notes (not represented by IPSs) upon their original issuance at their initial offering price. This summary is not exhaustive of all possible U.S. federal income tax considerations that may be relevant to the acquisition, ownership or disposition of IPSs, Subordinated Notes and Common Shares by prospective investors in light of their particular circumstances. In particular, this summary does not address all of the tax considerations that may be relevant to certain types of investors subject to special treatment under U.S. federal income tax laws. Special rules may apply to certain Non-U.S. Holders, such as:

- U.S. expatriates,
- controlled foreign corporations,
- passive foreign investment companies,
- foreign personal holding companies,
- corporations that accumulate earnings to avoid U.S. federal income tax,
- investors in pass-through entities that are subject to special treatment under the Code, and
- Non-U.S. Holders that are engaged in the conduct of a U.S. trade or business.

This summary is based upon the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), the Treasury Regulations promulgated thereunder and administrative and judicial interpretations thereof, all as currently in effect, and all subject to change or differing interpretations, possibly on a retroactive basis. Except to the extent specified with respect to U.S. federal estate tax, this summary does not address any U.S. federal estate or gift, state, local or non-U.S. tax considerations.

For purposes of this summary, a "Non-U.S. Holder" means beneficial owner of IPSs, Subordinated Notes or Common Shares, other than an entity or arrangement treated as a partnership for U.S. federal income tax purposes, that for U.S. federal income tax purposes is not:

- an individual who is a citizen or resident of the U.S.;
- a corporation (or other entity taxable as a corporation for U.S. federal income tax purposes) created or organized in or under the laws of the U.S. or of any political subdivision thereof;
- an estate, the income of which is subject to U.S. federal income taxation regardless of its source; or
- a trust if it (i) is subject to the primary supervision of a court within the U.S. and one or more U.S. persons have the authority to control all substantial decisions of the trust or (ii) was in existence on

August 20, 1996 and has properly elected under applicable U.S. Treasury Regulations to be treated as a U.S. person.

If a partnership or other entity or arrangement treated as a partnership for U.S. federal income tax purposes holds IPSs, Subordinated Notes or Common Shares, the tax treatment of the partner will generally depend upon the status of the partner and the activities of the partnership. Non-U.S. Holders who are partners of a partnership holding IPSs, Subordinated Notes or Common Shares, should consult their own tax advisors.

For purposes of this discussion, unless otherwise provided, references to Subordinated Notes include Subordinated Notes as part of an IPS. This discussion does not address the tax treatment of any subsequent issuance of Subordinated Notes, as more fully described in "Description of Subordinated Notes — Additional Issuances of IPSs and Subordinated Notes", including in connection with the repurchase of Class B and C common shares by Keystone on a Repurchase Event; the classification of subsequently issued Subordinated Notes as debt or equity for U.S. federal income tax purposes will depend on the facts and circumstances at the time of the subsequent issuance and thereafter.

No statutory, administrative or judicial authority directly addresses the treatment of IPSs or instruments similar to IPSs for U.S. federal income tax purposes, and neither the Issuer nor the Company have not sought any ruling from the IRS with respect to the statements made and the conclusions reached in the following discussion. As a result, the Internal Revenue Service ("IRS") or the courts may not agree with the tax consequences described below. A different treatment from that described below could adversely affect the amount, timing and character of income, gain or loss in respect of an investment in the IPSs or Subordinated Notes, and could subject them to U.S. federal estate taxes and subject payments to them to U.S. federal withholding taxes. Payments to Non-U.S. Holders would not be grossed-up for any such taxes. In addition, a different treatment could result in the loss by the Company of all or part of the Company's deduction for interest paid by Keystone ULC on the Subordinated Notes and could result in the Company being liable for U.S. federal withholding tax on interest paid to Non-U.S. Holders.

**Taxation of Non-U.S. Holders**

*Allocation of Purchase Price*

As discussed in more detail below, in the opinion of U.S. Tax Counsel, a Non-U.S. Holder's acquisition of an IPS should be treated for U.S. federal income tax purposes as the acquisition of the Common Share and the Subordinated Notes constituting the IPS. Accordingly, the Issuer and the Company will treat the acquisition of IPSs in this manner, and, by purchasing an IPS, a Non-U.S. Holder agrees to treat the acquisition of IPSs in this manner. However, there is no authority that directly addresses the tax treatment of securities with terms substantially similar to the terms of the IPSs (that is, securities structured as a unit consisting of Subordinated Notes and Common Share). In light of the absence of direct authority, neither the Issuer nor U.S. Tax Counsel can conclude with certainty that the IPSs should be so treated. If that treatment is not respected, then the acquisition of IPSs may be treated as an acquisition only of an equity interest, in which case the Subordinated Notes would be treated in effect as equity rather than as debt for U.S. federal income tax purposes. See "— Subordinated Notes — Characterization of Subordinated Notes." The remainder of this discussion assumes that the acquisition of an IPS will be treated as an acquisition of the one Common Share and the Subordinated Notes constituting the IPS.

The purchase price of each IPS will be allocated between the Common Share and the Subordinated Notes constituting the IPS in proportion to their respective fair market values at the time of purchase. Such allocation will establish a Non-U.S. Holder's initial tax bases in the Common Share and the Subordinated Notes. The Issuer and the Company will report the initial fair market value of each Common Share as C$4.286 and the initial fair market value of each Subordinated Notes as C$5.714, and by purchasing an IPS, a Non-U.S. Holder agrees to such allocation and agrees to not take a contrary position for any purpose, including tax reporting purposes. However, this allocation is not binding on the IRS and the IRS may challenge it.

If this allocation is not respected, it is possible that the Subordinated Notes will be treated as having been issued with original-issue discount ("OID"). Assuming a Non-U.S. Holder satisfies the Portfolio Interest Exemption requirements described below under "U.S. Federal Withholding Tax," such Non-U.S. Holder would not be subject to withholding with respect to such OID. If a Non-U.S. Holder failed to satisfy those requirements, OID on the Subordinated Notes would be subject to a 30% U.S. withholding tax, unless such Non-U.S. Holder otherwise establishes an exemption from or reduced rate of withholding under a tax treaty and satisfies certain documentation requirements. In general, under the Canada-United States Income Tax Convention, Canadian residents would be entitled to a 10% withholding tax rate. The remainder of this discussion assumes that the agreed upon allocation of the purchase price will be respected for U.S. federal income tax purposes.

***Separation and Combination***

If a Non-U.S. Holder separates an IPS into the Common Share and Subordinated Notes or combines a Common Share and Subordinated Notes to form an IPS, such holder will not recognize gain or loss upon such separation or combination for U.S. federal income tax purposes. In such case, a Non-U.S. Holder will continue to take into account items of income otherwise includible with respect to the Common Share and the Subordinated Notes, and such holder's tax bases and holding period in the Common Share and the Subordinated Note will not be affected by such separation or combination.

***Subordinated Notes***

*Characterization of Subordinated Notes*

As discussed more fully below under "Taxation of the Company — Deductibility of Interest," in the opinion of U.S. Tax Counsel, the Subordinated Notes should be treated as debt for U.S. federal income tax purposes. If the Subordinated Notes were treated as equity rather than debt for U.S. federal income tax purposes, payments of interest on the Subordinated Notes to Non-U.S. Holders could be subject to U.S. federal withholding taxes. In addition, there can be no assurance that the IRS will not assert that the interest rate on the Subordinated Notes is in excess of an arm's length interest rate. If the IRS were successful in such a challenge, then any excess of the interest paid on the Subordinated Notes over the deemed arm's length amount would not be deductible by the Company and could be recharacterized as a payment with respect to equity instead of an interest payment for U.S. federal income tax purposes. In such case, Non-U.S. Holders could be subject to U.S. federal withholding tax with respect to the excess amount paid on the Subordinated Notes.

Except where stated otherwise, the remainder of this discussion assumes the Subordinated Notes are treated as debt for U.S. federal income tax purposes.

*U.S. Federal Withholding Tax*

Subject to the discussion below concerning backup withholding, no withholding of U.S. federal income tax should be required with respect to the payment of interest on a Subordinated Note owned by a Non-U.S. Holder under the "Portfolio Interest Exemption," provided that:

- the interest is not effectively connected with such holder's conduct of a trade or business within the U.S.;
- such Non-U.S. Holder does not actually or constructively own 10 percent or more of the total combined voting power of all classes of the Company's stock entitled to vote, within the meaning of section 871(h)(3) of the Code;
- such Non-U.S. Holder is not a controlled foreign corporation, within the meaning of section 957(a) of the Code, that is related, within the meaning of section 864(d)(4) of the Code, to the Company through stock ownership;
- such Non-U.S. Holder is not a bank whose receipt of interest on a note is an extension of credit made pursuant to a loan agreement entered into in the ordinary course of its trade or business; and
- such Non-U.S. Holder satisfies the statement requirement (described generally below) set forth in section 871(h) and section 881(c) of the Code and the regulations thereunder.

To satisfy the statement requirement referred to in the final bullet above, a Non-U.S. Holder, or a securities clearing organization, bank or other financial institution that holds customers' securities in the ordinary course of its trade or business (a "Financial Institution") holding the note on a Non-U.S. Holder's behalf, must provide the withholding agent in accordance with specified procedures, a statement to the effect that such holder is not a U.S. person. Currently, these requirements will be met if (1) a Non-U.S. Holder provides such holder's name and address, and certifies, under penalties of perjury, that such holder is not a U.S. person (which certification may be made on an IRS Form W-8BEN), or (2) a Financial Institution holding the note on behalf of a Non-U.S. Holder certifies, under penalties of perjury, that such statement has been received by it and furnishes the withholding agent with a copy thereof.

If a Non-U.S. Holder cannot satisfy the requirements of the Portfolio Interest Exemption described above, payments of interest (including payments in respect of OID, if any, on the Subordinated Notes) made to a Non-U.S. Holder will be subject to a 30 percent withholding tax, unless such Non-U.S. Holder provides the withholding agent with a properly executed:

- IRS Form W-8BEN claiming an exemption from or reduction in withholding under an applicable income tax treaty; or
- IRS Form W-8ECI stating that interest paid on the note is not subject to withholding tax because it is effectively connected with such holder's conduct of a trade or business in the U.S.

Applicable Treasury Regulations provide alternative methods for satisfying the requirement to provide IRS Forms, as set forth above. Under these Treasury Regulations, in the case of Subordinated Notes held by a foreign intermediary (other than a "qualified intermediary") or a foreign partnership (other than a "withholding foreign partnership"), the foreign intermediary or partnership, as the case may be, generally must provide an IRS Form W-8IMY and attach thereto an appropriate certification by each beneficial owner or partner.

*U.S. Federal Income Tax*

If a Non-U.S. Holder is engaged in a trade or business in the U.S. and interest on a Subordinated Note is effectively connected with the conduct of such holder's trade or business in the U.S., although exempt from the U.S. federal withholding tax discussed above (provided the certification requirements described above are satisfied), such holder will be subject to U.S. federal income tax on such interest on a net income basis in the same manner as if such holder were not a Non-U.S. Holder. In addition, if a Non-U.S. Holder is a foreign corporation, such holder may be subject to a branch profits tax equal to 30 percent (or lesser rate under an applicable income tax treaty) of its effectively connected earnings and profits for the taxable year, subject to adjustments.

*Sale, Exchange or Other Disposition of Subordinated Notes*

Upon the sale, exchange, or other disposition of an IPS, a Non-U.S. Holder will be treated as having sold, exchanged, or disposed of the Subordinated Note represented by the IPS. Any gain realized upon the sale, exchange or other disposition of a Subordinated Notes generally will not be subject to U.S. federal income tax, unless:

- such gain is effectively connected with a conduct of a trade or business in the U.S.; or
- the Non-U.S. Holder is an individual present in the U.S. for 183 days or more in the taxable year of such sale, exchange, retirement or other disposition, and has a "tax home" in the U.S.

If a Non-U.S. Holder is an individual and is described in the first bullet above, such Non-U.S. Holder will be subject to tax on any gain derived from the sale, exchange or other disposition under regular graduated U.S. federal income tax rates. If a Non-U.S. Holder is an individual and is described in the second bullet above, such Non-U.S. Holder will be subject to a flat 30 percent tax on any gain derived from the sale, exchange or other disposition, which may be offset by U.S. source capital losses (even though such holder is not considered a resident of the U.S.). If a Non-U.S. Holder is a corporation and is described in the first bullet above, such Non-U.S. Holder will be subject to tax on any gain under regular graduated U.S. federal income tax rates and, in addition, may be subject to the branch profits tax equal to 30 percent (or lesser rate under an applicable income tax treaty) on such holder's effectively connected earnings and profits for the taxable year, subject to adjustments.

*U.S. Federal Estate Tax*

If a Non-U.S. Holder is an individual, any Subordinated Notes owned by such Non-U.S. Holder at the time of a holder's death should not be subject to U.S. federal estate tax, provided that any payment of interest to such holder on such Subordinated Notes would be eligible for the portfolio interest exemption from the 30% U.S. federal withholding tax under the rules described above under "U.S. Federal Withholding Tax" without regard to the statement requirement described therein.

***Common Shares***

*Dividends*

Dividends paid on the Common Shares to a Non-U.S. Holder should not be subject to withholding of U.S. federal income tax and should not otherwise be subject to U.S. federal income tax unless such dividends are effectively connected with a Non-U.S. Holder's conduct of a trade or business within the U.S. and are paid out of the Keystone North America's current or accumulated earnings and profits (as determined under U.S. federal income tax principles). Such dividends would be subject to U.S. federal income tax on a net income basis at applicable graduated individual or corporate rates. In addition, if a Non-U.S. Holder is a foreign corporation with effectively connected dividends, such holder may be subject to a branch profits tax equal to 30 percent (or lesser rate under an applicable income tax treaty) of such holder's effectively connected earnings and profits for the taxable year, subject to adjustments.

Recently enacted U.S. federal income tax legislation dealing with corporate "inversions" (*e.g.*, certain transactions in which a non-U.S. corporation acquires substantially all of the equity interests in, or the assets of, a U.S. corporation or partnership, if, after the transaction, former equity owners of the U.S. corporation or partnership own a specified level of stock in the non-U.S. corporation) provides in certain cases that a non-U.S. corporation may be treated as a U.S. corporation for U.S. federal income tax purposes. As enacted, this legislation does not apply to Keystone because the shareholders of the Company will not own any stock in Keystone as a result of the offering and related transactions. The legislation grants authority to the IRS to write implementing regulations, which could, if exercised broadly and retroactively, cause the new provisions to apply to Keystone and result in U.S. withholding taxes being imposed on dividends paid on the Common Shares to Non-U.S. Holders. Certain advisors to Keystone may have discussions with U.S. tax authorities to explain why such regulations should not extend to a number of transactions, including transactions such as this one. The outcome of such discussions is uncertain.

*Sale, Exchange or Other Disposition of Common Shares*

Upon the sale, exchange or other taxable disposition of an IPS, a Non-U.S. Holder will be treated as having sold, exchanged or disposed of the Common Shares represented by the IPS. Any gain realized upon the sale, exchange, retirement or other disposition of a Common Shares generally will not be subject to U.S. federal income tax unless:

- such gain is effectively connected with such Non-U.S. Holder's conduct of a trade or business in the U.S., or
- such Non-U.S. Holder is an individual present in the U.S. for 183 days or more in the taxable year of such sale, exchange or other disposition, and has a "tax home" in the U.S.

If a Non-U.S. Holder is an individual and is described in the first bullet above, such holder will be subject to tax on any gain derived from the sale, exchange or other disposition under regular graduated U.S. federal income tax rates. If a Non-U.S. Holder is an individual and is described in the second bullet above, such holder will be subject to a flat 30 percent tax on any gain derived from the sale, exchange or other disposition, which may be offset by U.S. source capital losses (even though such holder is not considered a resident of the U.S.). If a Non-U.S. Holder is a corporation and is described in the first bullet above, such holder will be subject to tax on any gain under regular graduated U.S. federal income tax rates and, in addition, may be subject to the branch profits tax equal to 30 percent (or lesser rate under an applicable income tax treaty) on such holder's effectively connected earnings and profits for the taxable year, subject to adjustments.

*Information Reporting and Backup Withholding*

A Non-U.S. Holder may be subject to information reporting requirements and backup withholding with respect to interest and principal payments on, and the proceeds from dispositions of, IPSs or Subordinated Notes, unless such holder complies with certain reporting procedures (usually satisfied by providing an IRS Form W-8BEN) or otherwise establish an exemption. Additional information reporting requirements and backup withholding with respect to the payment of proceeds from the disposition of IPSs or Subordinated Notes are as follows:

- If the proceeds are paid to or through the U.S. office of a broker, they generally will be subject to backup withholding and information reporting unless the Non-U.S. Holder certifies that such holder is not a U.S. person under penalties of perjury (usually on an IRS Form W-8BEN) or otherwise establishes an exemption.
- If the proceeds are paid to or through a non-U.S. office of a broker that is not a U.S. person and is not a foreign person with certain specified U.S. connections (a "U.S. Related Person"), they will not be subject to backup withholding or information reporting.
- If the proceeds are paid to or through a non-U.S. office of a broker that is a U.S. person or a U.S. Related Person, they generally will be subject to information reporting (but not backup withholding) unless a Non-U.S. Holder certifies that such holder is not a U.S. person under penalties of perjury (usually on an IRS Form W-8BEN) or otherwise establish an exemption.

In addition, the amount of interest paid to a Non-U.S. Holder and the amount of tax, if any, withheld from such payment must generally be reported annually to such holder and the IRS unless an exception applies. The IRS may make such information available under the provisions of an applicable income tax treaty to the tax authorities in the country in which a Non-U.S. Holder is resident. Any amounts withheld under the backup withholding rules will be allowed as a refund or a credit against such holder's U.S. federal income tax liability, provided the required information is furnished by such holder to the IRS.

*Taxation of Keystone North America*

Distributions paid by the Company to Keystone North America will be considered dividends, to the extent of the Company's current and accumulated earnings and profits, and generally will be subject to a 30% U.S. federal withholding tax, subject to a potential reduction under an applicable tax treaty. In general, under the Canada-U.S. Income Tax Convention, dividends paid to a Canadian resident corporation that owns 10% or more of the voting stock of the corporation paying the dividends are subject to a 5% withholding rate thus, any dividends paid to Keystone North America by the Company should be eligible for the 5% withholding rate. The Company intends to withhold at that rate. Keystone North America does not intend to conduct a trade or business in the U.S. or otherwise create a permanent establishment in the U.S. Therefore, it is generally not expected that Keystone North America would be subject to U.S. federal income tax.

*Taxation of Keystone ULC*

The Treasury Regulations under Section 7701 of the Code provide that a foreign eligible entity will be disregarded as an entity separate from its owner if it has a single owner and such owner has unlimited liability for the obligations of the foreign entity. For U.S. federal income tax purposes, assuming the Subordinated Notes issued by Keystone ULC are treated as debt for U.S. federal income tax purposes (see discussion below "Taxation of the Company — Deductibility of Interest"), Keystone ULC should be disregarded as an entity separate from the Company. In such case, interest payments made by Keystone ULC will be considered interest payments made by the Company directly to holders of the Subordinated Notes, and the payment of dividends by the Company on the shares of preferred shares of the Company held by Keystone ULC will be disregarded. The Company intends to take the position that Keystone ULC should be disregarded as an entity separate from the Company for U.S. federal income tax purposes.

*Taxation of the Company*

*Deductibility of Interest*

As discussed in more detail in the following paragraphs, in the opinion of U.S. Tax Counsel the Subordinated Notes issued in this offering should be treated as debt for U.S. federal income tax purposes. Such opinion is based in part on facts described in this prospectus and on various assumptions, representations and determinations (including those described below). Any alteration or incorrectness of such facts, assumptions, representations or determinations could adversely affect such opinions. In addition, such opinion is not binding on the IRS or the courts, and no ruling on this issue has been requested from the IRS. The IRS may challenge the Issuer's and Company's position and such challenge may be successful. The Issuer and the Company will treat, and, by acquiring an IPS or a note (not represented by an IPS), all holders agree to treat, the Subordinated Notes as indebtedness for all tax purposes.

The determination of whether an instrument is treated as debt or as equity for U.S. federal income tax purposes is based on all relevant facts and circumstances. There is no clear statutory definition of debt and the characterization of an instrument as debt or equity treatment is governed by principles developed in the case law, which analyzes numerous factors (with no one factor being dispositive) that are intended to identify the economic substance of the investor's interest in the issuer of the instrument. The opinion of U.S. Tax Counsel referred to above is based upon the terms of the Subordinated Notes and the IPSs and, in addition, relies upon certain representations and determinations by the Issuer and the Company, and an independent appraisal firm. The representations and determinations by the Issuer, the Company and/or the independent appraisal firm will be substantially to the effect that:

- after 45 days from the closing of the offering, an investor holding IPSs may separate the IPS into Subordinated Notes and Common Shares, and an investor holding Subordinated Notes and Common Shares may create IPSs, in each case without material market impediments;
- the term, interest rate, issue price, and other material provisions of the Subordinated Notes, including, *inter alia*, restrictions on incurrence of debt and payment of dividends are commercially reasonable and are substantially similar to those terms to which an unrelated third party lender not otherwise owning equity in Keystone North America or the Company, bargaining at arm's length with Keystone North America and the Company, would reasonably agree, where such lender would ordinarily be considered by knowledgeable corporate finance experts to be a lender or investor in the corporate bond market or other market for corporate debt and not primarily an investor in preferred stock;
- after giving effect to the offering, the ratio of the aggregate amount of indebtedness of the Company and its subsidiaries to the fair market value of the Company's equity is commercially reasonable under the circumstances and is reasonably comparable to that of similarly situated corporate bond issuers;
- based on the pricing of the IPSs (and the resulting implied valuation of the Company) and immediately after and giving effect to the Offering, the ratio of (A) the sum of (I) the principal amount of the Subordinated Notes, (II) the amount outstanding under the New Credit Facility, to (B) the fair market value of Keystone's equity (including retained interest) is approximately 1.3 to 1:
- based on the detailed financial forecasts provided by the Company (and assuming without verifying that those forecasts are correct), the Company and Keystone ULC should be able to pay interest on the Subordinated Notes and, assuming that market conditions in 2017 are substantially similar to current market conditions, to repay the principal amount of the Subordinated Notes at their maturity date, and it is reasonable to expect that the Company would be able to obtain debt financing in the bank or corporate bond markets (on a senior unsubordinated basis) in an amount sufficient to enable it to repay the principal amount of the Subordinated Notes at such maturity date.

In light of the representations and determinations described above and their relevance to several of the factors analyzed in the case law, and taking into account the facts and circumstances relating to the issuance of the Subordinated Notes, U.S. Tax Counsel is of the opinion that the Subordinated Notes issued in this offering should be treated as debt for U.S. federal income tax purposes. However, there is no authority that directly addresses the tax treatment of securities with terms substantially similar to the terms of the Subordinated Notes or offered under circumstances such as the offering (*i.e.*, offered as a unit consisting of Subordinated Notes and Common Shares). In light of this absence of direct authority, U.S. Tax Counsel cannot conclude with certainty that the Subordinated Notes issued in this offering will be treated as debt for U.S. federal income tax purposes.

If the Subordinated Notes were treated as equity rather than debt for U.S. federal income tax purposes, interest on the Subordinated Notes would not be deductible by the Company for U.S. federal income tax purposes. The Company's inability to deduct interest on the Subordinated Notes would materially increase the Company's taxable income and, thus, could increase the Company's U.S. federal income tax liability. Furthermore, if the Subordinated Notes were treated as equity, then payment of the stated interest paid on the Subordinated Notes may be subject to U.S. federal withholding tax. The Company could also be liable for failing to properly withhold U.S. federal withholding taxes on any interest payments previously made to Non-U.S. Holders. As a result, if the Subordinated Notes were treated as equity for U.S. federal income tax purposes, the Company's after-tax cash flow could be reduced, thereby adversely affecting the Company's ability to make payments on the Subordinated Notes and its common shares owned by Keystone North America, and Keystone North America's ability to pay dividends on the Common Shares.

In addition, there can be no assurance that the IRS will not assert that the interest rate on the Subordinated Notes is in excess of an arm's length interest rate. If the IRS were successful in such a challenge, then any excess of the interest paid on the Subordinated Notes over the deemed arm's length amount would not be deductible by the Company and could be recharacterized as a payment with respect to equity instead of an interest payment for U.S. federal income tax purposes. In such case, the Company's taxable income and, thus, its U.S. federal income tax liability could be materially increased. The Company could also be liable for U.S. federal withholding taxes on any interest payments previously made to Non-U.S. Holders. In addition, if a portion of the interest were recharacterized as a payment with respect to equity, Keystone ULC may not be disregarded as an entity separate from the Company, and may be treated as a partnership for U.S. federal income tax purposes. Such characterization could result in the disallowance of the interest deductions generated by Keystone ULC on the Subordinated Notes under the dual consolidated loss rules discussed below and could result in a material increase in the Company's taxable income and income tax liability.

*Earnings Stripping Rules — Section 163(j)*

Code section 163(j) is another potentially limiting factor on the Company's ability to deduct interest paid on the Subordinated Notes. In general, Code section 163(j) limits a corporation's deductions for interest paid to related foreign persons exempt from U.S. tax in years that: (i) the debt-to-equity ratio of the U.S. corporate taxpayer exceeds 1.5 to 1 (based on the tax basis of assets), and (ii) the corporation's net interest expense (*i.e.*, the excess of interest expense over interest income) exceeds 50% of "adjusted taxable income". Adjusted taxable income is generally defined as the corporation's taxable income before net interest expense, depreciation, and amortization. For purposes of Code section 163(j), a corporation and a creditor of the corporation will generally be "related" if the creditor owns, directly or by attribution, more than 50% of the corporation by vote or value. Under current law, assuming no Non-U.S. Holder owns more than 50%, directly or by attribution, of the Company's stock by vote or value, Code Section 163(j) should not apply to limit the Company's ability to deduct interest paid on the Subordinated Notes.

Various proposals have been introduced in the U.S. Congress to amend Code section 163(j). Prospects for the enactment of such legislation are uncertain. Although U.S. Tax Counsel believes that none of the current proposals to amend Code section 163(j) would affect the deductibility of interest paid on the Subordinated Notes, the ultimate form of legislation amending Code section 163(j), if any is enacted, is uncertain. In addition, the recently enacted *American Jobs Creation Act of 2004* requires a comprehensive study of the earnings stripping provisions of Code Section 163(j) to be completed by June 30, 2005.

*Dual Consolidated Losses*

Pursuant to Code section 1503(d) and the Treasury Regulations thereunder, the interest deductions generated by Keystone ULC on the Subordinated Notes will likely generate a "dual consolidated loss" ("DCL") and will therefore be deductible by the Company only if the Company and Keystone ULC make the election provided by Treasury Regulation 1.1503-2(g)(2) and comply with all applicable requirements, including annual reporting and certification requirements. The Company and Keystone ULC intend to make such election and comply with all applicable requirements. Even if such an election is made, however, if any of several "triggering events" occurs (*e.g.*, the use of Keystone ULC losses to offset the income of any other non-U.S. person, or, in certain circumstances, a disposition of Keystone ULC stock or assets), the Company will generally be required to report the amount of any prior Keystone ULC interest deductions (plus interest thereon) as gross income in the year of the triggering event. The Company and Keystone ULC intend to comply with all of the DCL reporting and certification requirements and to conduct their affairs such that no DCL triggering event occurs. However, if the Company and Keystone ULC fail to satisfy such reporting and certification requirements, or if a DCL triggering event occurs and no exception applies, the Company's taxable income and thus its U.S. federal income tax liability would be materially increased. This would reduce the Company's after-tax income available for distribution, and consequently would reduce the cash available for distributions.

*Penalties for Failing to Properly Report OID*

The Code generally requires that the payor of interest and OID to report to its payees and the IRS the amounts of interest and OID includable in income with respect to such payees, unless an exception to reporting applies. If the Subordinated Notes issued as part of an IPS or issued separately in this offering are issued with OID and there is a subsequent issuance of Subordinated Notes or if any subsequent issuance of Subordinated Notes issued as part of an IPS or separately are issued with OID and, in either case, no exception to reporting applies, the Company or other payor may not be able to properly report the amount of OID to the proper payee because all of the Subordinated Notes are being issued and will be traded under the same CUSIP number and will be held in book-entry form in the name of the CDS or its nominee, CDS & Co. As a result, the identity of the holders of the Subordinated Notes issued with OID may not be known, and hence the Company or other payor may not be able to properly report OID to the IRS and to the proper payees.

In such circumstances, the Company or other payor may choose to report such OID to all holders of Subordinated Notes regardless of whether such holders acquired the Subordinated Notes in this offering or a subsequent issuance, unless an exception to reporting applies. The Company believes that such reporting may satisfy the OID reporting requirements and hence reduce or eliminate any exposure of the Company to penalties for not properly reporting. Non-U.S. Holders who qualify for the Portfolio Interest Exemption generally should not be subject to OID reporting, and hence generally should not be impacted by such reporting.

As a result, a holder subject to OID reporting may be required to report OID even though such holder purchased Subordinated Notes having no OID unless such holder can establish to the IRS that its Subordinated Notes do not have OID. The IRS might assert that, unless a holder can establish that it is not holding Subordinated Notes with OID, all Subordinated Notes held by such holder will have OID. Prospective investors should consult their own tax advisor to determine the particular U.S. federal income tax consequences of OID, including the proper reporting of OID in these circumstances and the applicability and effect of U.S. state and local tax laws.

The penalties for failure to properly file and report such OID amounts to the IRS is generally capped at $250,000 for all such failures during any calendar year, but if such failure is due to the intentional disregard of the filing requirement, the penalty is the greater of $100 for each return with respect to which a failure occurs or 10% of the aggregate amount of items required to be reported correctly. The penalties for failure to properly furnish and report such amounts to a payee of OID is generally capped at $100,000 for all such failures during any calendar year, but if such failure is due to the intentional disregard of the filing requirement, the penalty is the greater of $100 for each return with respect to which a failure occurs or 10% of the aggregate amount of items required to be reported correctly. A failure is due to intentional disregard if it is a knowing or willful failure to file timely or to include the correct information, which determination is made based on all the facts and circumstances of the particular case. A failure by the Company or other payor to properly report in the case of the IPSs and Subordinated Notes may be treated as due to an intentional disregard, and therefore could result is substantial penalties.

## PURCHASERS' STATUTORY RIGHTS OF WITHDRAWAL AND RESCISSION

Securities legislation in certain of the provinces and territories of Canada provides purchasers with the right to withdraw from an agreement to purchase securities. This right may be exercised within two business days after receipt or deemed receipt of a prospectus and any amendment. In several of the provinces and territories, the securities legislation further provides a purchaser with remedies for rescission or damages in some jurisdictions if the prospectus or any amendment contains a misrepresentation or is not delivered to the purchaser, provided that the remedies for rescission or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of the purchaser's province or territory. The purchaser should refer to any applicable provisions of the securities legislation of the purchaser's province or territory for the particulars of these rights or consult with a legal adviser.

## INDEX TO FINANCIAL STATEMENTS

## AUDITORS' CONSENT

We have read the prospectus of Keystone North America Inc. (the "Company") dated January 31, 2005 relating to the issue and sale of income participating securities of the Company. We have complied with Canadian generally accepted standards for an auditor's involvement with offering documents.

We consent to the use in the above-mentioned prospectus of our report to the directors of the Company on the balance sheet of the Company as at August 27, 2004. Our report is dated December 2, 2004.

We also consent to the use in the above-mentioned prospectus of our report to the directors of Keystone Group Holdings, Inc. ("Keystone") on the consolidated balance sheets of Keystone as at December 31, 2003 and 2002 and the consolidated statements of income, shareholders' equity and cash flows for each of the years in the three-year period ended December 31, 2003. Our report is dated April 7, 2004 (except for Note 15, which is as of January 31, 2005).

Tampa, Florida
January 31, 2005

(Signed) ERNST & YOUNG LLP
Certified Public Accountants

# KEYSTONE NORTH AMERICA INC.

## AUDITED BALANCE SHEET

# REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors,
Keystone North America Inc.

We have audited the accompanying balance sheet of Keystone North America Inc. as at August 27, 2004. The balance sheet is the responsibility of the Company's management. Our responsibility is to express an opinion on the balance sheet based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the balance sheet is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the balance sheet. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall balance sheet presentation.

In our opinion, the balance sheet presents fairly, in all material respects, the financial position of Keystone North America Inc. as at August 27, 2004 in accordance with Canadian generally accepted accounting principles.

Tampa, Florida
December 2, 2004

(Signed) ERNST & YOUNG LLP
Certified Public Accountants

**KEYSTONE NORTH AMERICA INC.**

**BALANCE SHEET**

**As at August 27, 2004**

| | |
|---|---|
| **Assets** | (US $ ) |
| Cash | **$ 8** |
| **Shareholders' equity** | (US $ ) |
| Capital Stock: | |
| Common share, no par value, authorized unlimited shares, 1 share issued and outstanding | **$ 8** |

On behalf of the Board:

(Signed) ROBERT G. HORN
Director

(Signed) FRANK CERRONE
Director

*See accompanying notes.*

**KEYSTONE NORTH AMERICA, INC.**

**NOTES TO FINANCIAL STATEMENTS**

**August 27, 2004**

## 1. FORMATION

Keystone North America Inc. (the "Company") was incorporated on August 27, 2004 under the laws of the Province of Ontario. The Company's authorized capital consists of an unlimited number of Common Shares and an unlimited number of Class A Preferred Shares. One Common Share was issued on August 27, 2004. No Class A Preferred Shares have been issued.

## 2. SUBSEQUENT EVENTS

The Company indirectly incorporated a wholly owned subsidiary, Keystone Newport ULC, on September 9, 2004 as an unlimited liability corporation pursuant to the laws of the Province of Nova Scotia.

The Company and Keystone Newport ULC are in the process of filing a preliminary prospectus for an initial public offering (the "Offering") of Income Participating Securities ("IPSs").

The Company will use the proceeds of the Offering to acquire an ownership interest in Keystone Group Holdings, Inc. ("Keystone"). In addition, on the date of the closing of the Offering, Keystone Newport ULC will acquire the preferred shares of Keystone. Keystone Newport ULC will be a subsidiary of Keystone upon closing of the Offering.

The acquisition of Keystone will be accounted for using the purchase method.

## KEYSTONE GROUP HOLDINGS, INC.

## AUDITED ANNUAL FINANCIAL STATEMENTS

## REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors,
Keystone Group Holdings, Inc.

We have audited the accompanying consolidated balance sheets of Keystone Group Holdings, Inc. and Subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Keystone Group Holdings, Inc. and Subsidiaries at December 31, 2003 and 2002, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2003, in conformity with Canadian generally accepted accounting principles.

The accompanying financial statements have been prepared assuming that Keystone Group Holdings, Inc. will continue as a going concern. As more fully described in Note 14, the Company's Term Loan and Revolver were due on January 31, 2004, and have been classified as current liabilities, which results in a working capital deficiency. This condition raises substantial doubt about the Company's ability to continue as a going concern. Management's plans in regards to these matters are also described in Note 14. Management's plans describe that the Company is currently pursuing a merger and concurrent initial public offering that, if successful, the Company expects will secure the capital required to retire all existing indebtedness. The accompanying financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

April 7, 2004 (except for Note 15, which is as of
January 31, 2005)

(Signed) ERNST & YOUNG LLP
Certified Public Accountants

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES
## CONSOLIDATED BALANCE SHEETS

| | December 31, 2003 (US $) | December 31, 2002 (US $) |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | **$ 1,929,722** | $ 3,756,059 |
| Marketable securities | **699,064** | 560,835 |
| Accounts receivable, less allowance for doubtful accounts of $1,054,049 and $895,881 at December 31, 2003 and 2002, respectively | **5,166,609** | 4,684,782 |
| Inventories | **1,801,873** | 1,834,553 |
| Prepaids and other current assets | **358,747** | 160,416 |
| Future income taxes | **486,000** | 465,000 |
| Assets held for sale | **—** | 2,034,892 |
| Total current assets | **10,442,015** | 13,496,537 |
| Prearranged funeral contracts | **25,286,729** | 24,303,838 |
| Property and equipment, net | **34,261,208** | 36,276,561 |
| Goodwill, net | **69,980,668** | 70,350,047 |
| Covenants not to compete, net | **5,401,074** | 6,673,515 |
| Other assets | **151,454** | 155,043 |
| Total assets | **$145,523,148** | $151,255, 541 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | **$ 1,390,136** | $ 1,344,442 |
| Accrued salaries and wages | **536,108** | 648,753 |
| Other accrued expenses | **1,242,966** | 845,231 |
| Income taxes payable | **250,574** | 573,310 |
| Current maturities of long-term debt and obligations under agreements with former owners | **78,741,569** | 8,583,779 |
| Liabilities associated with assets held for sale | **—** | 425,631 |
| Total current liabilities | **82,161,353** | 12,421,146 |
| Deferred prearranged funeral contract revenues | **25,454,760** | 24,522,028 |
| Deferred revenues | **43,212** | 126,497 |
| Long-term debt, less current maturities | **—** | 78,379,938 |
| Obligations under agreements with former owners, less current maturities | **8,639,435** | 10,183,080 |
| Future income taxes | **5,056,000** | 4,411,000 |
| Other long-term obligations | **321,174** | 288,091 |
| Total liabilities | **121,675,934** | 130,331,780 |
| Shareholders' equity: | | |
| Share capital | **32,818,677** | 32,818,677 |
| Notes receivable-common stock | **(328,520)** | (328,520) |
| Accumulated deficit | **(8,642,943)** | (11,566,396) |
| Total shareholders' equity | **23,847,214** | 20,923,761 |
| Total liabilities and shareholders' equity | **$145,523,148** | $151,255,541 |

*See accompanying notes.*

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES

## CONSOLIDATED INCOME STATEMENTS

| | Year ended December 31 | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (US $) | (US $) | (US $) |
| Revenues: | | | |
| Funeral services | **$46,412,870** | $47,843,590 | $48,411,601 |
| Other | **2,472,304** | 2,923,653 | 2,440,605 |
| Total revenues | **48,885,174** | 50,767,243 | 50,852,206 |
| Costs and expenses | **31,459,588** | 32,393,070 | 32,768,481 |
| Gross profit | **17,425,586** | 18,374,173 | 18,083,725 |
| Other operating expenses: | | | |
| Corporate, general and administrative expenses | **3,188,445** | 4,184,409 | 3,842,234 |
| Depreciation | **2,092,594** | 2,252,204 | 2,227,921 |
| Amortization | **1,111,882** | 1,162,236 | 3,117,300 |
| Impairment of long-lived assets | **—** | 1,148,970 | — |
| Income from operations | **11,032,665** | 9,626,354 | 8,896,270 |
| Interest expense | **6,476,443** | 7,800,056 | 9,871,411 |
| Other income | **310,231** | 237,934 | 554,239 |
| Income (loss) before income taxes | **4,866,453** | 2,064,232 | (420,902) |
| Income tax expense | **1,943,000** | 1,188,000 | 458,000 |
| Net income (loss) | **$ 2,923,453** | $ 876,232 | $ (878,902) |

*See accompanying notes.*

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (US $)

| | Share Capital | Notes Receivable — Common Stock | Accumulated Deficit | Total |
|---|---|---|---|---|
| Balance at January 1, 2001 | $32,818,677 | $(328,520) | $(11,563,726) | $20,926,431 |
| Net loss | — | — | (878,902) | (878,902) |
| Balance at December 31, 2001 | 32,818,677 | (328,520) | (12,442,628) | 20,047,529 |
| Net income | — | — | 876,232 | 876,232 |
| Balance at December 31, 2002 | 32,818,677 | (328,520) | (11,566,396) | 20,923,761 |
| Net income | — | — | 2,923,453 | 2,923,453 |
| Balance at December 31, 2003 | $32,818,677 | $(328,520) | $ (8,642,943) | $23,847,214 |

*See accompanying notes.*

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES
## CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Year ended December 31, | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| | (US $) | (US $) | (US $) |
| **Operating activities** | | | |
| Net income (loss) | **$ 2,923,453** | $ 876,232 | $ (878,902) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | | |
| Depreciation | **2,092,594** | 2,252,204 | 2,227,921 |
| Amortization | **1,111,882** | 1,162,236 | 3,434,532 |
| Impairment of long-lived assets | **—** | 1,148,970 | — |
| Gain on cancellation of notes payable | **—** | — | (190,231) |
| Loss (gain) on sale of assets | **26,635** | 30,526 | (70,630) |
| Provision for doubtful accounts | **378,722** | 301,102 | 363,755 |
| Provision for future income taxes | **624,000** | 329,000 | 244,000 |
| Changes in operating assets and liabilities, net of effects of dispositions of subsidiaries: | | | |
| Accounts receivable | **(703,289)** | 211,929 | 1,226,049 |
| Prepaids and other current assets | **(180,755)** | 177,834 | (72,042) |
| Deferred preneed funeral contracts | **(48,511)** | 178,240 | (171,870) |
| Accounts payable, accrued salaries and wages, and other accrued expenses | **(217,590)** | 1,027,453 | (1,307,742) |
| Other | **808** | (324,932) | (190,362) |
| Net cash provided by operating activities | **6,007,949** | 7,370,794 | 4,614,478 |
| **Investing activities** | | | |
| Net deposits in marketable securities | **(138,229)** | (560,835) | — |
| Purchases of property and equipment | **(1,548,621)** | (1,470,442) | (1,083,041) |
| Proceeds from sale of assets and business | **3,060,865** | 1,355,337 | 1,698,397 |
| Net cash provided by (used in) investing activities | **1,374,015** | (675,940) | 615,356 |
| **Financing activities** | | | |
| Proceeds from long-term debt | **204,948** | 138,329 | 52,225 |
| Payments on long-term debt | **(8,074,186)** | (3,155,337) | (1,998,397) |
| Payments on obligations under agreements with former owners | **(1,339,063)** | (1,774,330) | (2,127,253) |
| Net cash used in financing activities | **(9,208,301)** | (4,791,338) | (4,073,425) |
| (Decrease) increase in cash and cash equivalents | **(1,826,337)** | 1,903,516 | 1,156,409 |
| Cash and cash equivalents at beginning of year | **3,756,059** | 1,852,543 | 696,134 |
| Cash and cash equivalents at end of year | **$ 1,929,722** | $ 3,756,059 | $ 1,852,543 |
| **Supplement disclosure of cash flow information:** | | | |
| Cash paid for income taxes | **$ 1,642,109** | $ 124,420 | $ 336,202 |

*See accompanying notes.*

# KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES
## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
### December 31, 2003

## 1. CORPORATE ORGANIZATION

Keystone Group Holdings, Inc. and Subsidiaries (collectively, "Keystone" or the "Company") was organized under the laws of the state of Delaware on October 18, 1996. Keystone's primary focus is to deliver funeral and cemetery services and products to its client families throughout the United States. At December 31, 2003, the Company, which is headquartered in Tampa, Florida, owns and manages 1 cemetery and 101 funeral homes throughout the United States.

The funeral service locations and cemetery operations consist of Keystone's funeral homes, cemetery, crematoria and related businesses. Funeral-related merchandise is sold at funeral service locations and certain funeral service locations contain crematoria. Keystone's cemetery provides cemetery interment rights (including mausoleum spaces and lawn crypts) and certain merchandise, including stone and bronze memorials and burial vaults. These items are sold on an at-need or pre-need basis.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of Presentation**

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles.

**Principles of Consolidation**

The consolidated financial statements include the accounts of Keystone Group Holdings, Inc. and all majority-owned subsidiaries. Intercompany balances and transactions have been eliminated in consolidation. All amounts are shown in U.S. dollars.

**Cash and Cash Equivalents**

Keystone considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. As of December 31, 2003 and 2002, there were no cash equivalents.

**Marketable Securities**

The carrying values of marketable securities are stated at lower of cost or market, as determined by quoted market prices, as they are classified as temporary investments. Marketable securities include gross unrealized losses of $1,017 and $78 as of December 31, 2003 and 2002, respectively. Realized investment and interest income is included in the cost basis of these securities.

**Inventories**

Inventories, which consist primarily of caskets and cremation urns, are carried at the lower of cost, determined on a first-in, first-out method, and net realizable value.

**Property and Equipment**

Property and equipment is recorded at cost and is depreciated on a straight-line basis over the estimated useful lives of the assets as follows:

| | |
|---|---|
| Buildings and related improvements | 15 to 40 years |
| Furniture, fixtures and equipment | 7 to 10 years |

**Revenue Recognition**

Funeral revenue, which includes funeral merchandise and services, is recognized when the funeral service is performed. The Company's trade receivables result from funeral services already performed. An allowance for doubtful accounts is established based on historical experience.

**Credit Risk**

The Company grants customers credit in the normal course of business. Procedures exist to secure accounts that include confirming a source of third-party payment such as insurance assignment, estate, group life policy or maturing pre-need trust. The Company focuses on those accounts which have not been secured and for which payments have not been received in the past 90 days and establishes an allowance on case-by-case basis. To date, bad debts have not been significant in relation to the volume of revenues. The Company charges interest on past due receivables in certain circumstances.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Prearranged funeral contracts do not subject the Company to collection risk because contracts may be canceled due to nonpayment before services are rendered. Prearranged funeral contracts that the customer funds by purchasing insurance-funded contracts are subject to supervision by state insurance departments and are protected in the majority of states by insurance guarantee acts.

### Advertising Costs

The Company expenses advertising costs as incurred. In 2003, 2002, and 2001, Keystone expensed advertising costs of $1,188,487, $1,453,592, and $1,416,568, respectively.

### Goodwill

Goodwill represents the excess of purchase price over the fair value of identifiable net assets acquired. Beginning in 2002, goodwill is tested for impairment annually based on the fair value of the Company's reporting units or more frequently if impairment indicators arise. The Company has not recorded any impairment loss.

Prior to January 1, 2002, the Company amortized its goodwill on a straight-line basis over 40 years. As of January 1, 2002, goodwill is no longer amortized. The following is a reconciliation of net income (loss) for the years ended December 31, 2003, 2002 and 2001, adjusted for the elimination of goodwill amortization:

| | Year ended December 31 | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| Net income (loss) | $2,923,453 | $876,232 | $ (878,902) |
| Goodwill amortization, net of tax | — | — | 1,276,458 |
| Adjusted net income | $2,923,453 | $876,232 | $ 397,556 |

### Covenants not to Compete

The covenants not to compete represent amounts prepaid or the present value of amounts to be paid under noncompetition agreements with certain key management personnel of acquired funeral operations. Amortization of such covenants not to compete is provided on a straight-line basis over the term of the agreements, generally ten years.

### Prearranged Funeral Accounting

Keystone sells prearranged funeral services, whereby a customer contractually agrees to the terms of a funeral to be performed in the future. The Company sells these price-guaranteed, prearranged funeral contracts through various programs providing for future funeral services at prices prevailing when the agreement is signed. Prearranged funeral contracts are generally funded either through trusts established by the customer or through life insurance policies purchased by the customer and issued by third party insurers. The Company, in accordance with certain state laws, may retain a portion of the payments on prearranged contracts funded through trust. The Company defers costs to obtain new prearranged funeral contracts until the related sales are recognized as revenue. Deferred obtaining costs include only those costs that vary with and are directly related to the acquisition of new prearranged contracts. Deferred obtaining costs are netted against deferred revenue on the balance sheet.

Amounts paid by the customer pursuant to the prearranged funeral contracts are recognized as funeral service revenue at the time the funeral is performed. Trust earnings and increasing insurance benefits are recognized as funeral service revenues when the funeral service is performed and are intended to cover increases in the cost of providing a price-guaranteed funeral service. Prearranged funeral contract revenue assets consist of receivables from customers, trusts or other, non-insurance accounts that will be received upon delivery of prearranged merchandise and services. Prearranged funeral contracts funded through life insurance policies purchased by the customer and issued by third party insurers are not reflected in the financial statements but are disclosed in Footnote 12. The prearranged funeral contract assets are recorded at fair value, less provisions for loss in respect of individual investments where market value is below cost and this decline appears to be other than temporary.

Amounts held in trust are refunded to the customer according to state law upon cancellation of the contract. Allowances for customer cancellations are recorded using an estimated cancellation rate based on historical experience.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Impairment or Disposal of Long-Lived Assets

The Company reviews its long-lived assets for impairment when changes in circumstances indicate that the carrying amount of the asset may not be recoverable. An impairment in the carrying value of a long-lived asset is recognized when the expected future operating cash flow derived from the asset is less than its carrying value. Impairment of long-lived assets are based on a fair value assessment, derived from a cash flow analysis, as compared to the related carrying value of the assets. Long-lived assets to be held and used are reported at the lower of carrying amount or fair value. Assets to be disposed of and assets not expected to provide any future service potential to the Company are recorded at the lower of carrying amount or fair value less estimated cost to sell.

### Financial Instruments

The Company's financial instruments include cash, marketable securities, accounts receivable, prearranged funeral contracts, accounts payable and accrued expenses, deferred prearranged funeral contract revenues, long-term debt and obligations under agreements with former owners. The carrying amounts of its financial instruments approximate fair value.

### Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from these estimates.

### Recent Accounting Pronouncements

In 2003, the Canadian Accounting Standards Board ("AcSB") approved Accounting Guideline 15 on the consolidation of variable interest entities. The guideline will be effective for the Company in fiscal 2005. Management is in the process of determining the effects of this guideline on its future financial statements, however, it is expected that the guideline will require consolidation of its funeral pre-need trust funds. Since the Company's customers are the legal beneficiaries of the pre-need trust funds and the Company does not have a legal right to access the care funds, the Company will recognize non-controlling interests in its financial statements. Management believes that the accounting changes associated with this guideline principally affect classifications within the financial statements and do not affect cash flow or the manner in which the Company recognizes and reports revenue or net income. The guideline also does not change the legal relationships among the trust funds, Keystone and its customers.

## 3. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

| | Cost | | Accumulated Depreciation | | Net Book Value | |
|---|---|---|---|---|---|---|
| | 2003 | 2002 | 2003 | 2002 | 2003 | 2002 |
| Land | $ 6,394,996 | $ 6,434,343 | $ — | $ — | $ 6,394,996 | $ 6,434,343 |
| Buildings and related improvements | 29,454,235 | 30,256,130 | 4,352,290 | 3,622,275 | 25,101,945 | 26,633,855 |
| Furniture, fixtures and equipment | 9,388,478 | 8,843,498 | 6,624,211 | 5,635,135 | 2,764,267 | 3,208,363 |
| | $45,237,709 | $45,533,971 | $10,976,501 | $9,257,410 | $34,261,208 | $36,276,561 |

## 4. GOODWILL

The changes in carrying amounts in goodwill for the years ended December 31, 2003 and 2002 are as follows:

| | 2003 | 2002 |
|---|---|---|
| Beginning balance | $70,350,047 | $71,272,686 |
| Dispositions | (369,379) | (853,376) |
| Other | — | (69,263) |
| Ending balance | $69,980,668 | $70,350,047 |

Amortization of goodwill charged against operations was $1,934,028 for 2001.

## 5. COVENANTS NOT TO COMPETE

| | 2003 | 2002 |
|---|---|---|
| Covenants not to compete | **$11,109,421** | $11,421,165 |
| Accumulated amortization | **(5,708,347)** | (4,747,650) |
| | **$ 5,401,074** | $ 6,673,515 |

The amortization of covenants not to compete charged against operations was $1,111,882, $1,162,236, and $1,183,272 in 2003, 2002 and 2001, respectively.

Future amortization of the Company's covenants not to compete at December 31, 2003, is as follows:

| | |
|---|---|
| 2004 | $1,110,942 |
| 2005 | 1,102,684 |
| 2006 | 1,084,713 |
| 2007 | 971,142 |
| 2008 | 731,384 |
| Thereafter | 400,209 |
| | $5,401,074 |

## 6. DEBT

In 1998, Keystone entered into a term loan (the Term Loan) and revolving line of credit (the Revolver) with Antares Leveraged Capital Corporation and Heller Financial, Inc. (the Lenders), which was originally due on December 31, 2001, and was subsequently extended through August 15, 2002. In April 2003, the parties amended that agreement to convert all borrowings to the Term Loan eliminating the Revolver and extending the Term Loan through January 31, 2004, and accordingly, the outstanding balances as of December 31, 2003, have been classified as current liabilities on the accompanying consolidated balance sheet as of December 31, 2003. The Term Loan is secured by substantially all of the assets of Keystone.

The Term Loan included provisions for principal reduction of varying amounts monthly through December 2003. Under the extension, a principal payment of $2.35 million was paid on April 3, 2003. Principal payments ranging from $200,000 to $400,000 were paid monthly through December 31, 2003. Additionally, two principal payments totaling a minimum of $1.75 million were paid under the agreement by November 15, 2003, from the proceeds of dispositions. Interest is paid monthly with the remaining principal due January 31, 2004.

The original terms of the Term Loan provided for interest at either the prime rate plus 1.75% or the London Inter Bank Offered Rate (LIBOR) plus 3.75%. The amendment redefined the interest terms of the Term Loan and provided for interest at either the prime rate plus 2.50% or the LIBOR plus 4.50%.

Under the terms of the amended agreement, Keystone was required to maintain specified financial ratios related to fixed charge and interest coverage during the year ending December 31, 2003. Additionally, Keystone was required to meet certain EBITDA levels throughout 2003. The Company met all requirements under the amended agreement.

Interest paid on long-term debt in 2003, 2002, and 2001 was $5,178,102, $6,523,470, and $8,231,797, respectively.

In addition to the Term Loan of $77.1 million, which is classified as current, Keystone has entered into other debt primarily for the purchase of equipment. Obligations under these agreements are as follows:

| | 2003 | 2002 |
|---|---|---|
| Other obligations | **$ 449,972** | $ 401,284 |
| Less current portion | **(128,798)** | (113,193) |
| Long-term portion | **$ 321,174** | $ 288,091 |

## 7. OBLIGATIONS UNDER AGREEMENTS WITH FORMER OWNERS

Keystone has entered into consulting and noncompetition agreements (generally for ten years) with former owners and key employees of acquired funeral homes and cemeteries and has financed certain portions of the purchase price with owners. Obligations under these agreements are as follows:

| | 2003 | 2002 |
|---|---|---|
| Obligations under covenants not to compete, principal and interest payable monthly or quarterly at various dates through 2018. Obligations have been discounted at 10%. Amount shown is net of $2,358,762 and $3,007,491 in unamortized discount for 2003 and 2002, respectively. | $ 6,605,902 | $ 7,712,467 |
| Notes payable to former owners, discounted at 10% per annum, payable at various dates through 2014. Amount shown is net of $1,050,384 and $1,365,354 in unamortized discount for 2003 and 2002, respectively. | 2,600,056 | 2,850,369 |
| Class C program notes, discounted at 10% per annum, payable quarterly beginning 2003 through 2005. Amount shown is net of $107,036 in unamortized discount for 2002. | 522,496 | 492,994 |
| Consulting obligations to former owners, discounted at 10% per annum, payable at various dates through 2018. Amount shown is net of $129,970 and $192,867 in unamortized discount for 2003 and 2002, respectively. | 467,999 | 847,836 |
| | 10,196,453 | 11,903,666 |
| Less current portion | (1,557,018) | (1,720,586) |
| Long-term portion | $ 8,639,435 | $10,183,080 |

Future maturities of these agreements at December 31, 2003, are as follows:

| | |
|---|---|
| 2004 | $2,781,204 |
| 2005 | 2,626,410 |
| 2006 | 2,122,088 |
| 2007 | 2,001,674 |
| 2008 | 1,631,603 |
| Thereafter | 2,572,590 |
| Gross payments | 13,735,569 |
| Less amounts representing interest | 3,539,116 |
| Obligations under agreements with former owners | 10,196,453 |
| Less current portion | 1,557,018 |
| Long-term portion | $8,639,435 |

Interest expense related to these obligations in 2003, 2002 and 2001 was $1,271,359, $1,249,653 and $1,578,653, respectively.

## 8. LEASES

The annual payments for operating leases (which are primarily for funeral home facilities, equipment and vehicles) at December 31, 2003 are as follows:

| | |
|---|---|
| 2004 | $ 981,314 |
| 2005 | 738,395 |
| 2006 | 656,956 |
| 2007 | 522,483 |
| 2008 | 446,237 |
| Thereafter | 616,694 |
| | $3,962,079 |

The leases for certain funeral home facilities contain contingent rental provisions based upon revenues of the related firms to be adjusted annually. The base revenue for these homes did not exceed the contingent provisions; accordingly, no contingent rental has been recorded as of December 31, 2003, 2002 or 2001.

Total rental expense for operating leases for the years ended December 31, 2003, 2002 and 2001, was $1,224,182, $1,253,243 and $1,231,958, respectively.

## 9. LOSS ON IMPAIRMENT OF LONG-LIVED ASSETS

During December 2002, the Company adopted a formal plan to sell two funeral homes. Based on its progress at that time and management's decision to proceed with the sales of these locations if acceptable prices and terms could be obtained, in December of 2002 the Company wrote down the aggregate value of these assets to their estimated fair value, which was based upon the actual sales price of the assets after year-end, less cost to sell. As a result, the Company incurred an aggregate pretax noncash charge to earnings of $1,105,375.

Additionally, the Company recorded impairment charges of $43,595 for noncompetition agreements with deceased key management personnel during the year ended December 31, 2002.

In the consolidated statements of operations, the impairment charges related to these writedowns and the writedowns of the noncompetition agreements are reflected as loss on impairment of long-lived assets. The related assets and liabilities associated with assets held for sale are shown in separate line items in the consolidated balance sheets titled assets held for sale and liabilities associated with assets held for sale.

A summary of the assets and liabilities included in these accounts at December 31, 2002, is as follows:

| | 2002 |
|---|---|
| **Assets** | |
| Accounts receivable | $ 31,107 |
| Inventories | 38,140 |
| Prepaids and other current assets | 2,212 |
| Prearranged funeral contracts | 345,429 |
| Property and equipment, net | 1,436,967 |
| Intangible assets | 181,037 |
| Assets held for sale | $2,034,892 |
| **Liabilities** | |
| Accounts payable | $ 1,667 |
| Other accrued expenses | 4,747 |
| Deferred prearranged funeral contract revenues | 345,429 |
| Obligations under agreements with former owners | 40,378 |
| Other long-term liabilities | 33,410 |
| Liabilities associated with assets held for sale | $ 425,631 |

## 9. LOSS ON IMPAIRMENT OF LONG-LIVED ASSETS (Continued)

The operating results of assets sold and held for sale included in the consolidated statements of operations for the years ended December 31, 2003, 2002 and 2001, were as follows:

| | 2003 | 2002 | 2001 |
|---|---|---|---|
| Revenues | **$ 143,302** | $1,265,889 | $1,443,505 |
| Net loss | **$(101,189)** | $ (687,794) | $ (770,501) |

For the year ended December 31, 2002, loss from operations included an impairment loss of $1,105,375 recognized on assets held for sale.

In 2003, the Company completed the sale of the two homes previously identified as held for sale for a total purchase price of $1,537,185, which resulted in a loss of $43,361 recorded in other income (expense) in the consolidated income statement.

## 10. INCOME TAXES

Future income tax assets and liabilities are determined based upon differences between financial reporting and tax bases of assets and liabilities and are measured using the enacted or substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse.

The components of income tax expense are as follows:

| | 2003 | 2002 | 2001 |
|---|---|---|---|
| Federal: | | | |
| Current | **$1,073,000** | $ 532,000 | $ — |
| Future | **544,000** | 287,000 | 213,000 |
| | **$1,617,000** | 819,000 | 213,000 |
| State: | | | |
| Current | **246,000** | 327,000 | 214,000 |
| Future | **80,000** | 42,000 | 31,000 |
| | **326,000** | 369,000 | 245,000 |
| | **$1,943,000** | $1,188,000 | $458,000 |

A reconciliation of the differences between the effective income tax rate and the statutory federal tax rate follows:

| | December 31 | | |
|---|---|---|---|
| | 2003 | 2002 | 2001 |
| Tax at U.S. statutory rate | **$1,655,000** | $ 701,000 | $(144,000) |
| State taxes, net of federal benefit | **133,000** | 35,000 | 70,000 |
| Goodwill amortization | **51,000** | 228,000 | 471,000 |
| Valuation allowance | **132,000** | 130,000 | 45,000 |
| Other | **(28,000)** | 94,000 | 16,000 |
| | **$1,943,000** | $1,188,000 | $ 458,000 |

## 10. INCOME TAXES (Continued)

Significant components of the Company's future tax assets and liabilities are as follows:

| | December 31 | |
|---|---|---|
| | 2003 | 2002 |
| Future tax assets: | | |
| Noncompete agreements | $ 1,793,000 | $ 1,728,000 |
| Acquisition costs | 207,000 | 229,000 |
| Allowance for doubtful accounts | 411,000 | 349,000 |
| State net operating loss carryforwards | 735,000 | 781,000 |
| Accrued expenses | 75,000 | 116,000 |
| Other | 6,000 | 4,000 |
| Gross future tax asset | 3,227,000 | 3,207,000 |
| Less valuation allowance | (636,000) | (504,000) |
| | 2,591,000 | 2,703,000 |
| Future tax liabilities: | | |
| Property and equipment | (4,891,000) | (5,187,000) |
| Goodwill | (2,270,000) | (1,462,000) |
| Net future tax liability | $(4,570,000) | $(3,946,000) |
| Classified as follows: | | |
| Current | $ 486,000 | $ 465,000 |
| Noncurrent | (5,056,000) | (4,411,000) |
| | $(4,570,000) | $(3,946,000) |

Generally accepted accounting principles require a valuation allowance to reduce the deferred tax assets reported if, based on the weight of the evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. After consideration of all the evidence, both positive and negative, management has determined that a valuation allowance of $636,000 is necessary at December 31, 2003.

The Company does not have net operating loss carryforwards for federal tax purposes as of December 31, 2003. The state net operating loss carryforwards range from $60,000 to $4.5 million and expire in various amounts through 2023.

## 11. SHAREHOLDERS' EQUITY

In connection with the formation of Keystone in October 1996, two executive officers of the Company and a venture capital firm (the Founders) agreed there would be two classes of common stock, Class A and Class B. On January 10, 1997, the founding agreement was amended to add the Lenders and two additional members of senior management of Keystone. At that time, all authorized Class B shares were issued and outstanding.

The founding agreement, as amended, provides that the Founders and the Lenders will be required to purchase additional Class A common shares based on the ownership levels of Class B shares. In prior years, the Founders and the Lenders agreed to purchase an additional 56 Class A shares at $100,000 per share.

Effective November 19, 1998, Keystone authorized 1 million shares of Class C common stock to be issued. As a class, the shares of Class C will participate in ownership of 10% of the Company on a pro rata basis as issued. The Class C shares contain certain provisions restricting the transfer of share; allowing repurchase by Keystone; and governing procedures in the event of a public offering of Keystone stock or sale of Keystone to a third party. As of December 31, 2003 65,000 shares of Class C common stock were issued and outstanding.

The rights of the Class A, Class B and Class C common stock differ with respect to dividends and number of votes per share. In the event a dividend is declared by Keystone, it will be paid first to holders of Class A common stock in an amount equal to the sum of the shares' unreturned original cost plus any unpaid yield (defined as 5% per annum on unreturned original cost plus accumulated unpaid yield). Any dividends in excess of the amount due to the Class A shareholders will then be paid to the holders of Class C, Class B, and Class A common stock in direct relation to the percentage ownership of Keystone.

## 11. SHAREHOLDERS' EQUITY (Continued)

Certain members of management, as part of their senior management agreements, have agreed to purchase 150 shares of Class B common stock and have signed promissory notes (bearing interest at 8%) for the agreed purchase price. The stock purchased in January 1997 under these agreements vested 20% at the signing of the notes and 20% per year thereafter. The notes, originally scheduled for maturity on December 31, 2001, bear interest at 8% (payable quarterly) and are secured by the related stock. During 2002, the Company extended these notes through December 31, 2004.

The following represents the Company's classes of stock:

| | December 31 | |
|---|---|---|
| | 2003 | 2002 |
| Class A, par value $.01 per share; 360 shares authorized, 304 issued and outstanding | $30,788,231 | $30,788,231 |
| Class B, par value $.01 per share; 2,348 shares authorized, issued and outstanding | 1,685,026 | 1,685,026 |
| Class C, par value $.01 per share; 1,000,000 shares authorized, 65,000 issued and outstanding | 16,900 | 16,900 |
| Share capital | $32,490,157 | $32,490,157 |

## 12. PREARRANGED FUNERAL CONTRACTS

Prearranged funeral contracts represent receivables due from customers, trust funds and other non-insurance accounts related to unperformed, prearranged funeral contracts. The components of prearranged funeral contracts in the consolidated balance sheets are as follows at December 31:

| | 2003 | 2002 |
|---|---|---|
| Receivables from trusts and other accounts | $25,802,685 | $24,806,885 |
| Allowance for cancellation | (515,956) | (503,047) |
| Total prearranged funeral contracts | $25,286,729 | $24,303,838 |

Prearranged funeral contract amounts deposited in trust funds and other accounts are available to the Company when the services are performed. A portion of trust funded amounts are withdrawn by the Company pursuant to various state laws. Trust and other account assets consist of the following at December 31:

| | 2003 | 2002 |
|---|---|---|
| Cash and term deposits | $ 5,666,644 | $ 5,883,795 |
| Money market and other | 19,468,853 | 19,268,519 |
| Mutual funds | 634,989 | — |
| Contract cost plus realized appreciation | 25,770,486 | 25,152,314 |
| Net unrealized appreciation | 32,199 | — |
| Total fair value | 25,802,685 | 25,152,314 |
| Less trust funds of assets held for sale | — | (345,429) |
| Total prearranged funeral contracts | $25,802,685 | $24,806,885 |

The Company has other arrangements under which customers purchase insurance policies, which are assigned to the Company at the time of death. The Company does not have control of these policies and is obligated to deliver these services at a fixed price only if the insurance policy proceeds are delivered. Approximate proceeds due from third-party insurers for the years ended December 31, 2003 and 2002, was $63,688,000 and $58,844,000, respectively, which represent both future assets and obligations of the Company.

## 13. PROFIT-SHARING PLAN

Keystone has a defined contribution, 401(k) plan for the benefit of its employees. All full-time employees who have reached the age of 21 and have completed one year of service are eligible to enroll. Employees may defer up to 15% of their salary and Keystone will

## 13. PROFIT-SHARING PLAN (Continued)

match up to 25% of the employee's elective deferral up to 1% of their salary. Total expense recognized by Keystone for 2003, 2002 and 2001 was $50,904, $50,657 and $51,194, respectively.

## 14. ABILITY TO CONTINUE AS A GOING CONCERN

The remaining principal and interest on the Company's Revolver and Term Loan of $77,055,753 were due on January 31, 2004. The Company is currently pursuing a merger and concurrent initial public offering that will secure the capital required to retire all existing indebtedness. The pending status of the public offering raises substantial doubt as to the Company's ability to operate as a going concern. Management believes the Company will be able to successfully refinance or extend the Revolver and Term Loan should the offering not be completed as intended. However, if management is unable to retire through public offering or otherwise refinance its debt obligations, the Company could be required to undertake restructuring or other changes in the business during the year ending December 31, 2004. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

## 15. PENDING MERGER WITH HFSC HOLDINGS, INC. AND INITIAL PUBLIC OFFERING

The Company has entered into agreements to explore the sale of the Company through an initial public offering ("IPO") of Income Participating Securities in Canada. In conjunction with this offering, the Company has also entered into negotiation of the acquisition of the operating subsidiaries of Hamilton Funeral Services, Inc., a funeral service provider based in San Diego, California. The potential IPO and acquisition would occur simultaneously, with the acquisition being funded from proceeds of the IPO.

The Company filed a final prospectus related to the IPO on January 31, 2005.

# KEYSTONE GROUP HOLDINGS, INC.

## UNAUDITED INTERIM FINANCIAL STATEMENTS

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES
## UNAUDITED CONSOLIDATED BALANCE SHEETS

| | September 30, 2004 | December 31, 2003 |
|---|---|---|
| | (US $) | (US $) |
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 3,325,579 | $ 1,929,722 |
| Marketable securities | 841,746 | 699,064 |
| Accounts receivable, less allowance for doubtful accounts of $1,080,091 and $1,054,049 at September 30, 2004 and December 31, 2003, respectively | 4,019,588 | 5,166,609 |
| Inventories | 1,751,201 | 1,801,873 |
| Income tax receivable | 682,907 | — |
| Prepaids and other current assets | 324,448 | 358,747 |
| Future income taxes | 465,000 | 486,000 |
| Total current assets | 11,410,469 | 10,442,015 |
| Prearranged funeral contracts | 24,150,589 | 25,286,729 |
| Property and equipment, net | 33,232,639 | 34,261,208 |
| Goodwill, net | 68,925,231 | 69,980,668 |
| Covenants not to compete, net | 4,466,428 | 5,401,074 |
| Other assets | 382,979 | 151,454 |
| Total assets | $142,568,335 | $145,523,148 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 1,152,526 | $ 1,390,136 |
| Accrued salaries and wages | 765,591 | 536,108 |
| Other accrued expenses | 652,906 | 1,242,966 |
| Income taxes payable | — | 250,574 |
| Current maturities of long-term debt and obligations under agreements with former owners | 77,148,903 | 78,741,569 |
| Total current liabilities | 79,719,926 | 82,161,353 |
| Deferred prearranged funeral contracts | 24,197,881 | 25,454,760 |
| Deferred revenues | — | 43,212 |
| Obligations under agreements with former owners, less current maturities | 7,251,745 | 8,639,435 |
| Future income taxes | 5,023,611 | 5,056,000 |
| Other long-term obligations | 368,560 | 321,174 |
| Total liabilities | 116,561,723 | 121,675,934 |
| Shareholders' equity: | | |
| Share capital | 32,818,677 | 32,818,677 |
| Notes receivable — common stock | (328,520) | (328,520) |
| Accumulated deficit | (6,483,545) | (8,642,943) |
| Total shareholders' equity | 26,006,612 | 23,847,214 |
| Total liabilities and shareholders' equity | $142,568,335 | $145,523,148 |

*See accompanying notes.*

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES
## UNAUDITED CONSOLIDATED INCOME STATEMENTS

| | Nine Months Ended September 30, 2004 (US $) | Nine Months Ended September 30, 2003 (US $) |
|---|---|---|
| Revenues: | | |
| Funeral services | **$33,917,890** | $34,142,813 |
| Other | **1,937,816** | 2,014,706 |
| Total revenues | **35,855,706** | 36,157,519 |
| Costs and expenses | **23,459,516** | 23,453,161 |
| Gross profit | **12,396,190** | 12,704,358 |
| Other operating expenses: | | |
| Corporate, general and administrative expenses | **2,429,994** | 2,427,485 |
| Depreciation | **1,509,487** | 1,554,146 |
| Amortization of covenants not to compete | **845,701** | 837,807 |
| Impairment of long-lived assets | **111,343** | — |
| Income from operations | **7,499,665** | 7,884,920 |
| Interest expense | **4,606,766** | 4,791,155 |
| Other income | **362,621** | 239,188 |
| Income before income taxes | **3,255,520** | 3,332,953 |
| Income tax expense | **1,096,122** | 1,330,848 |
| Net income | **$ 2,159,398** | $ 2,002,105 |

*See accompanying notes.*

## KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES

## UNAUDITED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (US $)

| | Share Capital | Notes Receivable — Common Stock | Accumulated Deficit | Total |
|---|---|---|---|---|
| Balance at December 31, 2003 | $32,818,677 | $(328,520) | $(8,642,943) | $23,847,214 |
| Net income | — | — | 2,159,398 | 2,159,398 |
| Balance at December 31, 2003 | $32,818,677 | $(328,520) | $(6,483,545) | $26,006,612 |

*See accompanying notes.*

**KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES**

**UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | Nine Months ended September 30 | |
|---|---|---|
| | 2004 | 2003 |
| | (US $) | (US $) |
| **Operating activities** | | |
| Net income | $ 2,159,398 | $ 2,002,105 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 1,509,487 | 1,554,146 |
| Amortization of covenants not to compete | 845,701 | 837,807 |
| Impairment of long-lived assets | 111,343 | — |
| Loss (gain) on sale of assets | 7,066 | (68,566) |
| Provision for doubtful accounts | 181,649 | 210,035 |
| Provision for future income taxes | (11,389) | 468,000 |
| Changes in operating assets and liabilities, net of effects of dispositions of subsidiaries: | | |
| Accounts receivable | 872,981 | 202,809 |
| Prepaids and other current assets | 54,448 | (216,521) |
| Deferred preneed funeral contracts | 2,207 | 3,526 |
| Accounts payable, accrued salaries and wages, and other accrued expenses | (1,726,586) | 292,552 |
| Other | (232,182) | 4,718 |
| Net cash provided by operating activities | 3,774,123 | 5,290,611 |
| **Investing activities** | | |
| Net deposits in marketable securities | (142,682) | — |
| Purchases of property and equipment | (1,221,525) | (1,289,117) |
| Proceeds from sale of assets and business | 1,694,319 | 3,017,440 |
| Net cash provided by investing activities | 330,112 | 1,728,323 |
| **Financing activities** | | |
| Proceeds from long-term debt | 153,189 | 186,782 |
| Payments on long-term debt | (1,600,000) | (6,830,761) |
| Payments on obligations under agreements with former owners | (1,261,567) | (1,205,067) |
| Net cash used in financing activities | (2,708,378) | (7,849,046) |
| Decrease (increase) in cash and cash equivalents | 1,395,857 | (830,112) |
| Cash and cash equivalents at beginning of the period | 1,929,722 | 3,756,059 |
| Cash and cash equivalents at end of the period | $ 3,325,579 | $ 2,925,947 |
| **Supplement disclosure of cash flow information:** | | |
| Cash paid for interest | $ 5,204,288 | $ 4,281,050 |
| Cash paid for income taxes | $ 2,040,992 | $ 1,066,493 |

*See accompanying notes.*

# KEYSTONE GROUP HOLDINGS, INC. AND SUBSIDIARIES
# NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
## September 30, 2004

### 1. BASIS OF PRESENTATION

**The Company**

Keystone Group Holdings, Inc. and Subsidiaries (collectively, "Keystone" or the "Company") was organized under the laws of the state of Delaware on October 18, 1996. Keystone's primary focus is to deliver funeral and cemetery services and products to its client families throughout the United States. At September 30, 2004, the Company, which is headquartered in Tampa, Florida, owns and manages 1 cemetery and 99 funeral homes throughout the United States.

The funeral service locations and cemetery operations consist of Keystone's funeral homes, cemetery, crematoria and related businesses. Funeral-related merchandise is sold at funeral service locations and certain funeral service locations contain crematoria. Keystone's cemetery provides cemetery interment rights (including mausoleum spaces and lawn crypts) and certain merchandise, including stone and bronze memorials and burial vaults. These items are sold on an at-need or pre-need basis.

The consolidated financial statements include the accounts of Keystone Group Holdings, Inc. and all majority-owned subsidiaries. Intercompany balances and transactions have been eliminated in consolidation. All amounts are shown in U.S. dollars.

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

**Interim Disclosures**

The information as of September 30, 2004, and for the nine months ended September 30, 2004 and 2003, is unaudited and, in the opinion of management, reflects all adjustments which are of a normal recurring nature and necessary for a fair presentation of financial position and results of operations for the interim periods. These financial statements have been prepared in accordance with GAAP for interim financial statements and do not include all information and footnotes required for annual financial statements. As a result, the accompanying unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes for the fiscal year ended December 31, 2003 presented elsewhere in this prospectus.

The results of operations for the nine months ended September 30, 2004 are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2004.

### 2. LOSS ON IMPAIRMENT OF LONG-LIVED ASSETS

In July 2004, the Company sold a funeral home for a total purchase price of $1,694,319. As a result, the Company incurred an aggregate pretax noncash charge to earnings of $111,343.

The operating results of this home included in the unaudited consolidated income statements for the nine months ended September 30, 2004 and 2003, were as follows:

| | Nine Months ended September 30, | |
|---|---|---|
| | **2004** | **2003** |
| Revenues | **$445,919** | $614,953 |
| Net income (loss) | **$ (40,693)** | $ 10,623 |

For the nine months ended September 30, 2004, loss from operations included an impairment loss of $111,343 recognized on assets held for sale.

### 3. OTHER SIGNIFICANT EVENTS

The remaining principal and interest on the Company's Revolver and Term Loan of $77,055,753 were due on January 31, 2004. The Company is currently pursuing a merger and concurrent initial public offering that will secure the capital required to retire all existing indebtedness. The pending status of the public offering raises substantial doubt as to the Company's ability to operate as a going concern. Management believes the Company will be able to successfully refinance or extend the Revolver and Term Loan should the offering not be completed as intended. However, if management is unable to retire through public offering or otherwise refinance its debt obligations, the Company could be required to undertake restructuring or other changes in the business. The consolidated financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

**3. OTHER SIGNIFICANT EVENTS (Continued)**

As of this report, the Company has entered into agreements to explore the sale of the Company through an initial public offering ("IPO") of Income Participating Securities. In conjunction with this offering, the Company has also entered into negotiations for the acquisition of the operating subsidiaries of Hamilton Funeral Services, Inc., a funeral service provider based in San Diego, California. The IPO and acquisition will occur simultaneously, with the acquisition being funded from proceeds of the IPO.

The Company filed a prospectus related to the IPO on January 31, 2005.

**HFSC HOLDINGS, INC.**

**AUDITED ANNUAL FINANCIAL STATEMENTS**
**AND UNAUDITED INTERIM FINANCIAL STATEMENTS**

## INDEPENDENT AUDITORS' REPORT

To the Board of Directors
HFSC Holdings, Inc.

We have audited the accompanying consolidated balance sheets of HFSC Holdings, Inc. and subsidiaries as of December 31, 2003 and 2002, and the related consolidated statements of operations, stockholders' deficit and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion the consolidated financial statements referred to above present fairly, in all material respects, the financial position of HFSC Holdings, Inc. and subsidiaries as of December 31, 2003 and 2002, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2003 in conformity with Canadian generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, the Company changed its method of accounting for goodwill on January 1, 2002 to be in conformity with Section 3062 of the Canadian Institute of Chartered Accountants, *Goodwill and Other Intangible Assets*. An analysis of goodwill in accordance with Section 3062 does not indicate that goodwill is impaired. However, there is the likelihood, as described in Note 15, that as a result of a contemplated merger, goodwill may be impaired and that the impairment charge would be material.

As further discussed in Note 1, the Company adopted the new requirements of Section 3475 (Section 3475) of the Canadian Institute of Chartered Accountants, *Impairment of Long-Lived Assets*, as of January 1, 2003. As described in Note 3, the consolidated financial statements for all periods presented have been prepared to present the disposition of certain business operations in 2004 and 2003 as discontinued operations.

The accompanying financial statements have been prepared assuming that HFSC Holdings, Inc. will continue as a going concern. The Company has suffered recurring losses from operations, its total liabilities exceed its total assets, and, as more fully described in Note 15, the Company's Senior Secured credit facility and subordinated notes are in default, due on demand, and have been classified as current liabilities, which results in a working capital deficiency. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regards to these matters are also described in Note 15. The accompanying financial statements do not include any adjustments to reflect the possible future effects on the recoverability and classification of assets or the amounts and classification of liabilities that may result from the outcome of this uncertainty.

San Diego, California
November 15, 2004, except for Note 16
as to which the date is December 23, 2004
and the last sentence of Note 11 as to which the
date is January 21, 2005.

(Signed) McGLADREY & PULLEN LLP
Certified Public Accountants

## HFSC HOLDINGS, INC. AND SUBSIDIARIES
## CONSOLIDATED BALANCE SHEETS
### (Amounts in U.S. Dollars)

| | December 31, 2003 | December 31, 2002 | September 30, 2004 (Unaudited) |
|---|---|---|---|
| **Assets** (Note 7) | | | |
| Current Assets | | | |
| Cash and cash equivalents | $ 6,845,096 | $ 3,209,067 | $ 2,893,385 |
| Receivables, net (Note 6) | 3,830,801 | 4,652,018 | 3,158,623 |
| Inventories (Note 6) | 1,995,580 | 2,063,815 | 2,044,223 |
| Prepaid expenses and other assets | 1,092,945 | 740,236 | 1,166,011 |
| **Total current assets** | 13,764,422 | 10,665,136 | 9,262,242 |
| Prearranged Funeral Contracts (Note 4) | 19,160,056 | 18,620,693 | 16,687,373 |
| Preneed Cemetery Contracts (Note 5) | 2,942,370 | 2,961,442 | 3,084,414 |
| Property and Equipment, net (Note 6) | 38,895,495 | 43,325,261 | 34,865,674 |
| Cemetery Property, at cost (Note 6) | 2,084,838 | 2,106,167 | 2,072,304 |
| Goodwill, net (Note 2) | 47,486,634 | 52,951,706 | 46,398,597 |
| Deferred Charges and Other Assets, net (Note 6) | 5,002,456 | 5,689,646 | 4,215,838 |
| | $129,336,271 | $136,320,051 | $116,586,442 |
| **Liabilities and Stockholders' Deficit** | | | |
| Current Liabilities | | | |
| Excess of outstanding checks over bank balance | $ 470,548 | $ — | $ 115,197 |
| Current maturities of long-term debt (Note 7) | 56,945,925 | 65,831,685 | 49,113,504 |
| Subordinated notes payable and deferred interest (Note 7) | 74,188,244 | 66,497,279 | 80,664,772 |
| Accounts payable and accrued expenses (Note 9) | 2,571,358 | 3,264,668 | 2,236,028 |
| Retractable preferred stock (Note 9) | 852,000 | 810,000 | 883,500 |
| Income taxes payable | 25,240 | 11,175 | 36,743 |
| **Total current liabilities** | 135,053,315 | 136,414,807 | 133,049,744 |
| Long-term debt, less current maturities (Note 7) | 2,857,311 | 3,259,169 | 2,304,769 |
| Deferred Prearranged Funeral Contract Revenues (Note 4) | 20,049,012 | 19,562,915 | 17,600,251 |
| Deferred Preneed Cemetery Contract Revenues (Note 5) | 6,361,452 | 6,353,527 | 6,584,589 |
| Future Income Taxes (Note 13) | 1,996,220 | 1,525,541 | 2,408,220 |
| **Total liabilities** | 166,317,310 | 167,115,959 | 161,947,573 |
| Commitments and Contingencies (Notes 8, 12 and 15) | | | |
| Stockholders' Deficit (Notes 7, 10 and 11) | | | |
| Class A common stock | 2,050,572 | 2,050,572 | 2,050,572 |
| Contributed surplus | 1,547,854 | 1,232,854 | 1,547,854 |
| Put warrant | — | 315,000 | — |
| Accumulated Deficit | (40,579,465) | (34,394,334) | (48,959,557) |
| **Total stockholders' deficit** | (36,981,039) | (30,795,908) | (45,361,131) |
| | $129,336,271 | $136,320,051 | $116,586,442 |

*See Notes to Consolidated Financial Statements.*

**HFSC HOLDINGS, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

**(Amounts in U.S. Dollars)**

| | Years Ended December 31, | | | Nine Months Ended September 30, (Unaudited) | |
|---|---|---|---|---|---|
| | **2003** | **2002** | **2001** | **2004** | **2003** |
| Revenues: | | | | | |
| Funeral | $36,978,276 | $39,104,687 | $38,197,459 | $26,857,223 | $27,185,849 |
| Cemetery | 1,048,182 | 1,106,383 | 1,139,872 | 706,532 | 812,742 |
| | 38,026,458 | 40,211,070 | 39,337,331 | 27,563,755 | 27,998,591 |
| Location operating costs | 24,873,603 | 25,176,566 | 25,325,295 | 18,864,347 | 18,533,813 |
| | 13,152,855 | 15,034,504 | 14,012,036 | 8,699,408 | 9,464,778 |
| Other operating expenses: | | | | | |
| Corporate general and administrative expenses | 3,326,907 | 3,346,621 | 3,221,432 | 2,233,433 | 2,549,785 |
| Noncompete expenses | 1,329,755 | 1,311,631 | 1,388,157 | 809,293 | 976,915 |
| Consulting expenses | 505,567 | 494,159 | 572,004 | 283,013 | 411,053 |
| Depreciation and amortization of property and equipment | 1,984,021 | 1,880,892 | 1,997,711 | 1,464,545 | 1,448,180 |
| Goodwill amortization | — | — | 1,282,833 | — | — |
| Impairment of goodwill (Note 2) | — | — | 312,399 | — | — |
| | 7,146,250 | 7,033,303 | 8,774,536 | 4,790,284 | 5,385,933 |
| **Operating income** | 6,006,605 | 8,001,201 | 5,237,500 | 3,909,124 | 4,078,845 |
| Other income (expense): | | | | | |
| Interest expense, payable in cash | (2,885,310) | (4,267,404) | (5,827,856) | (2,290,339) | (2,233,976) |
| Interest expense, payment-in-kind | (7,793,530) | (6,223,633) | (5,619,249) | (6,597,658) | (5,706,044) |
| Dividends on retractable preferred shares (Note 9) | (42,000) | (42,000) | (42,000) | (31,500) | (31,500) |
| Deferred loan costs amortization (Note 7) | (583,453) | (867,989) | (950,585) | (1,207,740) | (525,675) |
| Loan restructuring costs | (372,764) | (751,261) | — | (611,565) | (367,847) |
| Gain (loss) on sale of property | 161,271 | — | (157,157) | — | 159,014 |
| | (11,515,786) | (12,152,287) | (12,596,847) | (10,738,802) | (8,706,028) |
| Loss from continuing operations before income taxes | (5,509,181) | (4,151,086) | (7,359,347) | (6,829,678) | (4,627,183) |
| Income taxes (Note 13) | 484,744 | 1,536,716 | — | 380,500 | 363,558 |
| **Loss from continuing operations** | (5,993,925) | (5,687,802) | (7,359,347) | (7,210,178) | (4,990,741) |
| Income (loss) from discontinued operations (Note 3) | (191,206) | 821,915 | 414,630 | (1,169,914) | (100,907) |
| **Net loss** | $(6,185,131) | $(4,865,887) | $(6,944,717) | $(8,380,092) | $(5,091,648) |

*See Notes to Consolidated Financial Statements.*

## HFSC HOLDINGS, INC. AND SUBSIDIARIES
## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIT
### (Amounts in U.S. Dollars)

| | Class A Common Stock | | Contributed Surplus | Put Warrant | Accumulated Deficit | Total |
|---|---|---|---|---|---|---|
| | Shares | Amount | | | | |
| Balance, December 31, 2000 | 2,982,488 | $2,036,580 | $1,232,854 | $ 315,000 | $(22,583,730) | $(18,999,296) |
| Issuance of common stock | 699,606 | 13,992 | — | — | — | 13,992 |
| Net loss | — | — | — | — | (6,944,717) | (6,944,717) |
| Balance, December 31, 2001 | 3,682,094 | 2,050,572 | 1,232,854 | 315,000 | (29,528,447) | (25,930,021) |
| Net loss | — | — | — | — | (4,865,887) | (4,865,887) |
| Balance, December 31, 2002 | 3,682,094 | 2,050,572 | 1,232,854 | 315,000 | (34,394,334) | (30,795,908) |
| Put warrant expiration (Note 7) | — | — | 315,000 | (315,000) | — | — |
| Net loss | — | — | — | — | (6,185,131) | (6,185,131) |
| Balance, December 31, 2003 | 3,682,094 | 2,050,572 | 1,547,854 | — | (40,579,465) | (36,981,039) |
| Net loss (unaudited) | — | — | — | — | (8,380,092) | (8,380,092) |
| Balance, September 30, 2004 (unaudited) | 3,682,094 | $2,050,572 | $1,547,854 | $ — | $(48,959,557) | $(45,361,131) |

*See Notes to Consolidated Financial Statements.*

**HFSC HOLDINGS, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

**(Amounts in U.S. Dollars)**

| | Years Ended December 31, | | | Nine Months Ended September 30, (Unaudited) | |
|---|---|---|---|---|---|
| | **2003** | **2002** | **2001** | **2004** | **2003** |
| Cash Flows from Operating Activities | | | | | |
| Net loss | $(6,185,131) | $(4,865,887) | $(6,944,717) | $(8,380,092) | $(5,091,648) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | | | | |
| Depreciation and amortization of property and equipment | 2,213,839 | 2,151,405 | 2,195,749 | 1,565,742 | 1,647,026 |
| Amortization and impairment of goodwill | — | — | 1,797,492 | — | — |
| Amortization of deferred charges and other | 583,452 | 867,989 | 950,585 | 1,207,906 | 525,675 |
| Loss on disposal of businesses | 540,773 | — | — | 1,060,875 | 544,245 |
| (Gain) loss on sale of property | (161,271) | — | 157,157 | — | (159,014) |
| Future income taxes | 470,679 | 1,525,541 | — | 412,000 | 410,510 |
| Dividends on retractable stock | 42,000 | 42,000 | 42,000 | 31,500 | 31,500 |
| Changes in working capital components, net of effects of purchases and sales of businesses: | | | | | |
| (Increase) decrease in: | | | | | |
| Receivables | 821,217 | (891,296) | 675,277 | 673,364 | 1,537,597 |
| Inventories and cemetery property | (66,949) | 41,627 | (79,829) | (75,378) | (68,296) |
| Prepaid expenses, deferred charges and other assets | (601,259) | (861,362) | (524,091) | (605,573) | 29,667 |
| Preneed funeral and cemetery contracts | (520,291) | (904,822) | (1,509,696) | 2,330,639 | 200,604 |
| Increase (decrease) in: | | | | | |
| Accounts payable and accrued expenses | (692,242) | (334,554) | (1,805,753) | (348,089) | (651,058) |
| Deferred preneed funeral and cemetery contract revenues | 472,587 | 1,004,480 | 1,681,209 | (2,225,624) | (207,979) |
| Deferred interest | 7,690,965 | 6,525,457 | 5,507,137 | 6,476,526 | 5,675,936 |
| Income taxes payable | 14,065 | 11,175 | — | 11,503 | 10,549 |
| **Net cash provided by operating activities** | 4,622,434 | 4,311,753 | 2,142,520 | 2,135,299 | 4,435,314 |
| Cash Flows from Investing Activities | | | | | |
| Proceeds from sale of property, equipment and businesses | 9,452,062 | 198,403 | 2,430,577 | 3,056,716 | 9,399,094 |
| Purchase of property and equipment | (1,621,397) | (1,414,821) | (1,145,769) | (586,806) | (961,587) |
| **Net cash provided by (used in) investing activities** | 7,830,665 | (1,216,418) | 1,284,808 | 2,469,910 | 8,437,507 |
| Cash Flows from Financing Activities | | | | | |
| Net increase (decrease) in excess of outstanding checks over bank balance | 470,548 | — | — | (355,351) | — |
| Payments on senior secured credit facility | (9,038,189) | (587,219) | (4,009,373) | (7,921,981) | (9,006,418) |
| Payments on other borrowings | (249,429) | (287,659) | (342,175) | (279,588) | (207,994) |
| Proceeds from exercised stock options | — | — | 13,992 | — | — |
| **Net cash (used in) financing activities** | (8,817,070) | (874,878) | (4,337,556) | (8,556,920) | (9,214,412) |
| **Net increase (decrease) in cash and cash equivalents** | 3,636,029 | 2,220,457 | (910,228) | (3,951,711) | 3,658,409 |
| Cash and Cash Equivalents | | | | | |
| Beginning | 3,209,067 | 988,610 | 1,898,838 | 6,845,096 | 3,209,067 |
| Ending | $ 6,845,096 | $ 3,209,067 | $ 988,610 | $ 2,893,385 | $ 6,867,476 |

*See Notes to Consolidated Financial Statements.*

## HFSC HOLDINGS, INC.
## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
### (Amounts in U.S. Dollars)

### 1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES

**Nature of business:** HFSC Holdings, Inc. and its wholly owned subsidiaries (individually or collectively, the Company) owns funeral homes and cemeteries that provide death care services and products in the communities in which the Company's operations are located. The Company also sells prearranged funeral services whereby a customer contractually agrees to the terms of a funeral to be performed in the future. The Company's cemeteries sell cemetery property, merchandise and services on both an at-need and preneed basis. At December 31, 2003, the Company operated 87 funeral homes and 7 cemeteries located in 12 states within the United States.

**Basis of presentation:** The accompanying financial statements have been prepared in accordance with Canadian generally accepted accounting principles and assume that the Company will continue as a going concern. As discussed in Note 7 to the financial statements, the Company is in default on various of their long-term debt instruments due to failure to make certain principal payments and meet various restrictive and financial covenants. As a result, the respective long-term debt instruments have been classified as current. This raises substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are described in Note 15. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. All amounts are denominated in U.S. dollars.

**Discontinued operations:** As a result of the Company's sales of funeral homes in 2004 and 2003, the Company's consolidated financial statements for all periods presented have been prepared to present the discontinued operations separate from continuing operations, with no effect on net loss or stockholders' deficit (Note 3).

**Unaudited interim financial information:** The interim financial information presented herein as of and for the nine months ended September 30, 2004 and 2003 is unaudited. The unaudited interim financial information has been prepared on the same basis as the annual financial statements and reflect all adjustments which are, in the opinion of management, necessary for a fair presentation for the periods presented. Such adjustments are of a normal recurring nature. The interim financial information is not intended to be a complete presentation in accordance with generally accepted accounting principles. The September 30, 2004 interim financial statements are not necessarily indicative of the results in the entire fiscal year ending December 31, 2004, or any subsequent period.

**A summary of the Company's significant accounting policies follows:**

**Principles of consolidation:** The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated in consolidation.

**Use of estimates:** The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The Company's operations are affected by numerous factors including changes in death rates, competition and new federal, state and local laws and regulations. The Company cannot predict if any of these factors might have a significant impact on the funeral and cemetery death care industry in the future, nor can it predict what impact, if any, the occurrence of these or other events might have on the Company's operations. Significant estimates and assumptions made by management are used for, but not limited to, the receivable allowances, the estimated useful lives of long-lived assets, the recoverability of such assets by their estimated future undiscounted cash flows, the purchase price allocation used in the Company's business acquisitions, the deferred obtaining costs for amounts incurred to date on the acquisition of new preneed cemetery and prearranged funeral business, the deferred trust income related to deferred prearranged contracts that have not been recognized, the deferred prearranged funeral and deferred preneed cemetery contract revenue and deferred land sales, the realizability of deferred tax assets and the fair market value of the Company's outstanding equity instruments.

**Cash and cash equivalents:** The Company maintains its cash accounts in various financial institutions located throughout the United States. Accounts at these banks are insured by the Federal Deposit Insurance Corporation up to $100,000. While the Company's accounts at these institutions, at times, may exceed the federally insured limit, management believes that the risk of loss is not significant. The Company has not experienced any losses in such accounts. For purposes of reporting cash flows, the Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Cash equivalents consist primarily of U.S. government securities.

**Credit risk:** The Company grants customers credit in the normal course of business. Procedures are in effect to determine the source of payment for services and the credit worthiness of customers. The Company generally does not require collateral and establishes an allowance for doubtful accounts based upon factors surrounding the credit risk of customers, historical trends, and on a case-by-case basis of all accounts overdue over 90 days. To date, bad debts have not been significant in relation to the volume of revenues. No interest is charged to customers on overdue balances.

## 1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

Prearranged funeral and preneed cemetery contracts generally do not subject the Company to collection risk because contracts may be canceled due to nonpayment before services are rendered. Prearranged funeral contracts that the customer funds by purchasing insurance-funded contracts are subject to supervision by state insurance departments and are protected in the majority of states by insurance guarantee acts.

**Disclosures about fair value of financial instruments:** The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

- Long-term debt is generally stated at the face amount of the notes. Due to the complexity of the Company's capital structure and the inherent uncertainties involved in valuing securities underlying warrants issued in connection with the notes, embedded conversion options and other features, it is not practical for management to determine the fair value of the Company's debt securities.
- Retractable preferred stock is stated at redemption value. Due to the inherent uncertainties regarding the ability and ultimate timing of either the redemption or conversion of these preferred shares and the accretion method used, it is not practical for management to determine their fair value.

The carrying amounts of financial instruments, including cash, cash equivalents, receivables, accounts payable and accrued expenses, and excess of outstanding checks over bank balance, approximates fair value because of the short-term maturity of those instruments.

**Inventories:** Merchandise and supplies inventories are stated at the lower of cost (first-in first-out method) or market.

**Property and equipment:** Property and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the various classes of assets ranging from three to ten years for furniture, fixtures, equipment and automobiles. Leasehold improvements are amortized on the straight-line method over the terms of the lease or the estimated useful lives, whichever is shorter. Buildings are depreciated on the straight-line method over the estimated useful lives ranging from 30 to 40 years.

Effective January 1, 2003, the Company early adopted the new accounting standard issued by the Canadian Institute of Chartered Accountants Section 3063, *Impairment of Long-Lived Assets*, which established new requirements for recognition, measurement and disclosure of the impairment of long-lived assets. Also effective January 1, 2003, the Company adopted the new requirements of Section 3475, *Disposal of Long-lived Assets and Discontinued Operations*, to disposal activities initiated in 2003 and thereafter.

Long-lived assets and asset groups are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Long-lived assets evaluated for impairment are grouped with other assets to the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities. If the sum of the projected undiscounted cash flows (excluding interest) is less than the carrying value of the assets, the assets will be written down to the estimated fair value in the period in which the determination is made. Certain long-lived assets to be disposed of by sale are reported at the lower of carrying amount or fair value less cost for sale. Fair value is determined by management based on either projected discounted cash flows, or multiples of earnings before interest, taxes, depreciation and amortization.

The assumptions used by management in determining the future cash flows are critical. In the event these expected cash flows are not realized, future impairment losses may be recorded. Management has determined that no impairment of long-lived assets currently exists.

**Goodwill:** The excess of the purchase price over the fair value of identifiable net assets of businesses acquired in transactions accounted for as a business combination is included in the consolidated financial statements as "Goodwill." Historically management has determined fair values used in such purchase price allocations.

On January 1, 2002, the Company adopted Section 3062 (Section 3062) of the Canadian Institute of Chartered Accountants, *Goodwill and Other Intangible Assets*, (Note 2). Under Section 3062 goodwill is no longer amortized but is tested annually for impairment, or more frequently if events or changes in circumstances indicate that the assets might be impaired. Reported net loss for the year ended December 31, 2001 would have been $1,485,000 less before income taxes had Section 3062 been adopted effective January 1, 2001.

The annual goodwill impairment evaluation includes a comparison of the carrying value of the reporting unit (including goodwill) to that reporting unit's fair value. If the reporting unit's estimated fair value exceeds the reporting unit's carrying value, no impairment of goodwill exists. If the fair value of the reporting unit does not exceed the unit's carrying value, then an additional analysis is performed to allocate the fair value of the reporting unit to all of the assets and liabilities of that unit as if that unit had been acquired in a business combination and the fair value of the unit was the purchase price. If the excess of the fair value of the reporting unit over the fair value of the identifiable assets and liabilities is less than the carrying value of the unit's goodwill, an impairment charge is recorded for the difference.

## 1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

In assessing the recoverability of goodwill, the Company must make assumptions about the estimated future cash flows and other factors to determine the fair value of its reporting units. Assumptions about future cash flows require significant judgment. If the expected cash flows are not realized, impairment losses may be recorded in the future. Because the Company currently operates as a single reporting unit entity and the Company has a stockholders' deficit, further analysis is not currently required. If as a result of future profitable operations or restructuring of its debt the Company has positive stockholders' equity, or upon restructuring of the Company's operations into more than one reporting unit, further analysis may be required which could potentially result in impairment.

**Deferred charges and other assets:** Loan costs are being amortized over the lives of the actual or expected borrowings of the underlying debt instrument. Consulting and noncompetition agreements, primarily with former owners of businesses acquired, are expensed over the lives of the respective agreements. Obtaining costs, which represent costs directly related to the acquisition of new preneed cemetery and prearranged funeral business, incurred pursuant to the sale of new prearranged funeral and cemetery business are expensed when the related deferred prearranged contract revenues are recognized.

**Funeral operations:** The Company recognizes revenue on funeral sales at the time the services are performed. An allowance for doubtful accounts has been provided relative to trade receivables based on historical experience.

The Company also sells price guaranteed prearranged funeral contracts through various programs providing for future funeral services at prices prevailing when the agreements are signed. Revenues associated with sales of prearranged funeral contracts (which include accumulated trust investment earnings) are deferred until such time that the funeral services are performed and there can be no assurance that the revenues recognized when services are performed will approximate prevailing prices. Prearranged funeral contracts are generally funded either through trust funds established by the Company from contract payments received from the customer, or through life insurance policies purchased by the customer and issued by third party insurers. A portion of the payments on prearranged contracts may be retained by the Company in accordance with applicable state law. Principal amounts deposited in trust funds and proceeds from life insurance policies are available to the Company as funeral services are performed. Amounts held in trust are refunded to the customer in those situations when state law provides for the return of those amounts under the purchaser's option to cancel the contract. The Company defers investment earnings on prearranged funeral trust funds until the prearranged funeral service is provided. Prearranged funeral contracts funded through life insurance policies purchased by the customer and issued by third party insurers are not reflected in the accompanying consolidated financial statements. As of December 31, 2003 prearranged funeral contracts funded through life insurance policies underwritten by the Company's national insurance provider approximated $40 million.

**Cemetery operations:** The Company's cemetery revenues are generated primarily through the sale of cemetery interment rights, merchandise and services. Preneed cemetery interment right sales of constructed cemetery burial property are deferred until a minimum percentage of the sales price has been collected, generally 10%. Revenues related to the preneed sale of unconstructed cemetery burial property are deferred until such property is constructed and a minimum percentage of the sales price has been collected. Revenues related to the preneed sale of merchandise and services are deferred until the merchandise is delivered and the service is performed.

Costs related to the sales of interment rights include property and other costs related to cemetery development activities, and are charged to operations using the specific identification method. Costs related to merchandise and services are based on actual costs incurred.

Pursuant to state law, all or a portion of the proceeds from cemetery merchandise or services sold on a preneed basis may be required to be paid into trust funds until such merchandise is delivered or the services performed. The Company defers realized investment earnings related to these merchandise and service trusts until the associated merchandise is delivered or services are performed.

A portion of the proceeds from the sale of cemetery property is required by state law to be paid into perpetual care trust funds. Earnings from these trusts are recognized in current cemetery revenues and are intended to defray cemetery maintenance costs, which are expensed as incurred. The principal of such perpetual care trust funds generally cannot be withdrawn by the Company and therefore is not included in the consolidated balance sheets.

Operating costs in the consolidated statements of operations include, but are not limited to property and merchandise costs, personnel costs, costs of funeral and cemetery services, automotive costs, selling, facility and administrative expenses.

**Future Income taxes:** Future income taxes are provided on a liability method whereby future tax assets are recognized for deductible temporary differences and future tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Future tax assets are recognized when it is determined to be more likely than not that some portion or all of the future tax assets will be realized. Future tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

(Amounts in U.S. Dollars)

## 1. NATURE OF BUSINESS AND SIGNIFICANT ACCOUNTING POLICIES (Continued)

**Stock-based compensation:** The Company has stock-based compensation plans, which are described in Note 11. During 2002, the Company adopted Handbook Section 3870 "Stock-Based Compensation and Other Stock-Based Payments" which requires the use of a fair value-based method to account for such arrangements. In regards to the Company's plans currently in existence, then new standard applies prospectively to options and warrants issued on or after January 1, 2002 and has such, there has been no effect to the financial statements on adoption of the standard.

## 2. GOODWILL

The Company completed an assessment of its operations and has determined that it currently operates as a single operating segment with one reporting unit. The carrying value of the reporting unit is determined by allocating all applicable assets (including goodwill) and liabilities, which in a single reporting unit entity like the Company, is the stockholders' deficit. In order to assess impairment of goodwill, the Company determined that the fair value of the reporting unit is in excess of its carrying value; therefore, no impairment charge has been recorded in the consolidated statement of operations for 2003 and 2002.

During the year ended December 31, 2001, management determined that an impairment of goodwill of approximately $312,000 existed relating to certain locations that were not generating sufficient cash flows to recover the assets and recorded a charge in the accompanying consolidated financial statements.

The carrying value of goodwill was reduced during the periods presented as a result of the funeral home sales further described in Note 3. Accumulated goodwill amortization was approximately $4,767,000 and $5,314,000 as of December 31, 2003 and December 31, 2002, respectively.

The change in the carrying amount of goodwill for each of the three years ended December 31, 2003 and nine months ended September 30, 2004 and 2003 are as follows:

| | Years Ended December 31, | | | Nine Months Ended September 30, (Unaudited) | |
|---|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2004 | 2003 |
| Beginning of year | $52,951,706 | $52,951,706 | $55,766,828 | $47,486,634 | $52,951,706 |
| Amortization — continuing operations | — | — | (1,282,833) | — | — |
| Amortization — discontinued operations | — | — | (202,260) | — | — |
| Impairment | — | — | (312,399) | — | — |
| Funeral home sales | (5,465,072) | — | (1,017,630) | (1,088,037) | (5,465,072) |
| End of year | $47,486,634 | $52,951,706 | $52,951,706 | $46,398,597 | $47,486,634 |

## 3. BUSINESS DISPOSALS

In June 2004, the Company evaluated certain of its operating locations and concluded to dispose of certain locations. On September 30, 2004, the Company disposed of seven funeral homes located in Milwaukee. The net proceeds from the transaction of approximately $3,009,000 were required to be applied to the Company's senior secured loan indebtedness.

During 2003, in two separate transactions, the Company disposed of six funeral homes in two markets comprising three Michigan funeral homes and three Wisconsin funeral homes. The combined net proceeds of approximately $8,550,000 from the sales were applied to the Company's senior secured loan indebtedness.

The Company has not made any allocation of corporate expenses to discontinued operations.

(Amounts in U.S. Dollars)

### 3. BUSINESS DISPOSALS (Continued)

Summarized operating results of the 2004 and 2003 discontinued operations for each of the three years ended December 31 and the nine months ended September 30, 2004 and 2003 are as follows:

| | Years Ended December 31, | | | Nine Months Ended September 30, (Unaudited) | |
|---|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2004 | 2003 |
| Revenues | $4,141,188 | $5,469,467 | $5,801,262 | $ 1,173,000 | $3,816,065 |
| Operating Costs | | | | | |
| Location operating costs | 2,884,340 | 3,419,554 | 3,679,140 | 1,012,917 | 2,541,630 |
| Corporate general and administrative expenses | — | — | — | — | — |
| Noncompete expenses | 116,000 | 150,990 | 150,998 | 10,750 | 113,250 |
| Consulting expenses | 54,183 | 66,500 | 68,200 | 17,200 | 43,183 |
| Depreciation and amortization of property and equipment | 229,817 | 270,513 | 254,873 | 101,361 | 203,229 |
| Goodwill amortization | — | — | 202,260 | — | — |
| Total operating costs | 3,284,340 | 3,907,557 | 4,355,471 | 1,142,228 | 2,901,292 |
| Operating income | 856,848 | 1,561,910 | 1,445,791 | 30,772 | 914,773 |
| Interest expense allocated to discontinued operations | 507,281 | 739,995 | 1,031,161 | 139,811 | 471,435 |
| Income (loss) from discontinued operations | 349,567 | 821,915 | 414,630 | (109,039) | 443,338 |
| Loss on disposal of discontinued operations | (540,773) | — | — | (1,060,875) | (544,245) |
| Net income (loss) from discontinued operations | $ (191,206) | $ 821,915 | $ 414,630 | $(1,169,914) | $ (100,907) |

During 2001 the Company disposed of two funeral homes that under accounting standards in place in 2001 are not presented as discontinued operations but are included in continuing operations in the consolidated statement of operations. Revenues and expenses for 2001 for the two funeral homes disposed of amounted to approximately $726,000 and $548,000, respectively. A net loss of approximately $287,000 was recognized in 2001 related to the disposals and is included in loss on sale of property in the 2001 consolidated statement of operations.

### 4. PREARRANGED FUNERAL ACTIVITIES

Prearranged funeral contracts represents customer receivables and amounts held in trust funds related to unperformed, price guaranteed prearranged funeral contracts. Accumulated earnings from trust funds have been included to the extent that they have been earned through December 31, 2003, 2002 and 2001. Such accumulated earnings are intended to cover future increases in the cost of providing price-guaranteed funeral services. The cumulative trust funded amount has been reduced by allowable cash withdrawals for trust earnings and amounts retained by the Company pursuant to various state laws. The components of prearranged funeral contracts in the consolidated balance sheets are as follows at December 31:

| | 2003 | 2002 |
|---|---|---|
| Receivables from customers | $ 165,104 | $ 241,742 |
| Receivables from trusts | 18,994,952 | 18,378,951 |
| Total prearranged funeral contracts | $19,160,056 | $18,620,693 |

(Amounts in U.S. Dollars)

**4. PREARRANGED FUNERAL ACTIVITIES (Continued)**

Prearranged funeral contract amounts deposited in trust funds are available to the Company when the services are performed. The cost and market value of invested funds held in trust consist of the following at December 31:

| | 2003 | 2002 |
|---|---|---|
| U.S. government, U.S. agencies and municipalities | $ 2,063,072 | $ 1,842,756 |
| Mutual funds, primarily government obligations | 1,457,291 | 1,871,337 |
| Money market funds and other investments | 15,474,588 | 14,664,858 |
| Total value at cost | 18,994,951 | 18,378,951 |
| Net unrealized appreciation (depreciation) | 41,026 | (2,247) |
| Total value at market | $19,035,977 | $18,376,704 |

U.S. government, U.S. agencies and municipal debt securities generally mature within one year.

Deferred prearranged funeral contract revenues generally represents the original contract price of unperformed prearranged funeral sales and accumulated trust earnings relative to unperformed funeral contracts funded by trust.

**5. PRENEED CEMETERY ACTIVITIES**

Preneed cemetery contracts represent customer receivables and amounts held in trust funds related to sales of preneed cemetery property, merchandise and services. Accumulated earnings from trust funds have been included in receivables from trusts to the extent that they have been earned through December 31, 2003 and 2002, respectively. Such accumulated earnings are intended to cover future increases in the cost of providing undelivered merchandise and unperformed services. The components of preneed cemetery contracts in the consolidated balance sheets are as follows at December 31:

| | 2003 | 2002 |
|---|---|---|
| Receivables from customers | $ 558,972 | $ 720,567 |
| Receivables from trusts | 2,383,398 | 2,240,875 |
| Total prearranged cemetery contracts | $2,942,370 | $2,961,442 |

Preneed cemetery contract amounts deposited in trust funds are available to the Company when the cemetery merchandise has been delivered and the services are performed. The cost and market value of invested funds held in cemetery merchandise and service trust funds consist of the following at December 31:

| | 2003 | 2002 |
|---|---|---|
| U.S. government, U.S. agencies and municipalities | $1,239,749 | $1,246,926 |
| Mutual funds, primarily government obligations | 509,027 | 143,891 |
| Money market funds and other short-term investments | 634,622 | 850,058 |
| Total value at cost | 2,383,398 | 2,240,875 |
| Net unrealized appreciation (depreciation) | 268 | (23,753) |
| Total value at market | $2,383,666 | $2,217,122 |

U.S. government, U.S. agencies and municipal debt securities generally mature within one year.

Included in deferred preneed cemetery contract revenue at December 31, 2003, 2002 and 2001 is approximately $1,110,000, $1,208,000 and $1,224,000, respectively, of estimated costs to deliver merchandise related to preneed cemetery contract obligations assumed in conjunction with business acquisitions.

(Amounts in U.S. Dollars)

## 5. PRENEED CEMETERY ACTIVITIES (Continued)

The following summary reflects the Company's perpetual care trust fund balances at December 31, 2003 and 2002. Because the principal generally cannot be withdrawn, these balances are not reflected in the accompanying consolidated financial statements.

| | 2003 | 2002 |
|---|---|---|
| Mutual funds, primarily government obligations | $694,628 | $452,393 |
| Money market funds and other short-term investments | 112,263 | 326,394 |
| Debt securities | — | 18,534 |
| Total value at cost | 806,891 | 797,321 |
| Net unrealized appreciation | 10,687 | 497 |
| Total value at market | $817,578 | $797,818 |

Investment earnings related to perpetual care trust funds recognized in cemetery revenues were approximately $10,000, $9,000 and $14,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

## 6. SUPPLEMENTARY INFORMATION

The detail of certain consolidated balance sheet accounts consisted of the following at December 31:

| | 2003 | 2002 |
|---|---|---|
| Receivables, net: | | |
| Trade accounts | $ 4,387,694 | $ 5,276,484 |
| Less allowance for doubtful accounts | (556,893) | (624,466) |
| | $ 3,830,801 | $ 4,652,018 |
| Inventories: | | |
| Merchandise and supplies | $ 1,935,580 | $ 2,003,815 |
| Developed cemetery property to be sold within one year | 60,000 | 60,000 |
| | $ 1,995,580 | $ 2,063,815 |
| Property and equipment: | | |
| Land and improvements | $ 9,837,064 | $10,941,219 |
| Less accumulated depreciation and amortization | (510,206) | (417,739) |
| | 9,326,858 | 10,523,480 |
| Buildings and improvements | 31,602,989 | 34,122,330 |
| Less accumulated depreciation and amortization | (5,727,997) | (5,155,673) |
| | 25,874,992 | 28,966,657 |
| Leasehold improvements | 898,435 | 862,426 |
| Less accumulated depreciation and amortization | (400,662) | (326,788) |
| | 497,773 | 535,638 |
| Furniture, fixtures, equipment and vehicles | 9,570,142 | 9,240,911 |
| Less accumulated depreciation and amortization | (6,374,270) | (5,941,425) |
| | 3,195,872 | 3,299,486 |
| Net property and equipment | $38,895,495 | $43,325,261 |

(Amounts in U.S. Dollars)

## 6. SUPPLEMENTARY INFORMATION (Continued)

| | 2003 | 2002 |
|---|---|---|
| Cemetery property: | | |
| Mausoleums | $ 262,092 | $ 272,070 |
| Developed cemetery land | 654,450 | 665,506 |
| Undeveloped cemetery land | 1,168,296 | 1,168,591 |
| | $ 2,084,838 | $ 2,106,167 |
| Deferred charges and other assets: | | |
| Deferred loan costs | $ 3,620,299 | $ 5,342,899 |
| Less accumulated amortization | (2,381,058) | (3,520,205) |
| Deferred obtaining costs | 1,775,344 | 1,703,263 |
| Noncompetition agreements, net | 1,835,756 | 2,024,287 |
| Other | 152,115 | 139,402 |
| | $ 5,002,456 | $ 5,689,646 |

## 7. LONG-TERM DEBT

As of December 31, 2003, the senior secured, subordinated, and certain seller debt are in default. Long-term debt consists of the following at December 31:

| | 2003 | 2002 |
|---|---|---|
| Senior secured credit facility[a][f] | $54,133,448 | $63,171,637 |
| Notes payable to bank, due in monthly payments of approximately $3,000 through April 2014, including adjustable interest rate at 9%, collateralized by deeds of trust on real estate and assets of a funeral home with a net book value of approximately $886,000 | 242,573 | 276,112 |
| Unsecured notes payable to former owners of acquired businesses, due through June 2009, including interest ranging from 5.5% to 8.0%, subordinated to all other debt[e] | 5,427,215 | 5,643,105 |
| | 59,803,236 | 69,090,854 |
| Less current maturities | 56,945,925 | 65,831,685 |
| | $ 2,857,311 | $ 3,259,169 |

Subordinated unsecured notes payable and deferred interest consists of the following at December 31:

| | 2003 | 2002 |
|---|---|---|
| Senior subordinated notes[b][f] | $29,440,349 | $29,440,349 |
| Junior subordinated notes[d][f] | 26,573,063 | 24,806,241 |
| Class A subordinated notes[c][f] | 3,020,057 | 3,020,057 |
| Class B convertible subordinated notes[c][f] | 2,000,000 | 2,000,000 |
| Deferred interest payable[c][d] | 13,154,775 | 7,230,632 |
| | $74,188,244 | $66,497,279 |

(a) The Company has defaulted on the senior secured credit facility (the facility) principal payments and is in default of various restrictive and financial covenants. In May 2004, the Company entered into a Forbearance Agreement and Fifth Amendment to Second Amended and Restated Credit Agreement (2004 forbearance agreement), with the lenders under the facility whereby the lenders agreed to forbear from exercising their default-related rights against the Company for a limited time period while the Company seeks financial restructuring, provided the Company complies with the terms of the forbearance agreement. The 2004 forbearance agreement expires on November 1, 2004. Among other rights and remedies under events of default, the interest rate spreads have been increased for LIBOR loans to LIBOR plus 4.50% and for prime rate loans to prime rate plus 3.00%. The Company must comply with various covenants with respect to the 2004 forbearance agreement. The Company is not in compliance with certain covenants (Note 15).

**7. LONG-TERM DEBT (Continued)**

The Company is in the process of seeking to amend the facility, but because it was all due in June 2003, and the Company did not pay off the facility, it has been classified as current. The Company incurred debt restructuring costs totaling approximately $373,000 and $751,000, which were charged to expense during 2003 and 2002, respectively.

The loans are collateralized by substantially all the assets and capital stock of the Company's wholly owned subsidiaries and contain acceleration clauses upon a change in control of the Company.

Under the initial and first amendment to the credit agreement, the Company granted warrants to the initial lender to purchase in aggregate 1,424,904 shares of Class B common stock at $.01 per share. Upon grant, the Company allocated $315,000 to the value of these puttable warrants. These warrants expired on June 30, 2003.

(b) In January 1999, the Company entered into a $30,000,000, 15% senior subordinated securities purchase agreement, to be used initially to repay senior secured borrowings, and then for working capital and permitted acquisitions. In connection with the securities purchase agreement, the Company granted warrants to the investors to purchase up to an aggregate of 3,491,919 shares of Class A common stock at an exercise price of $.01 per share which became exercisable as senior subordinated notes are purchased. During 1999, the investors purchased $22,500,000 of 15% Senior Subordinated Notes due in January 2007, and warrants for 2,618,941 shares of Class A common stock became exercisable and expire January 25, 2009. Warrants that did not become exercisable were cancelled on October 31, 2000. Quarterly interest only payments on the notes are payable 10% in cash and 5% Pay-In-Kind. The Company may call the notes at any time after January 25, 2002, at a price equal to the outstanding balance of the notes. In connection with and as a condition of this securities purchase agreement, the Company, the junior subordinated lenders and Class A and Class B subordinated lenders (see subparagraphs (c) and (d) below) entered into an amendment under the securities purchase agreement which formally extended the Class A and B subordinated and the 1996 junior subordinated notes to April 2007 and subordinated such debt to the 1999 senior subordinated lenders. The Class A and B subordinated and junior subordinated notes extended due date is subject to the earlier due date of January 23, 2006 under certain circumstances as described in the agreement.

In November 2000, the Company entered into a Note Premium Payment Agreement in connection with the 1999 purchase agreement. The agreement requires the Company to pay the holders of the Senior Subordinated notes, concurrently with any payments (except for (i) payments-in-kind of accrued interest, and (ii) issuance of common stock of the Company valued at fair market as full or partial satisfaction of principal or interest accrued) made to the Junior Subordinated note holders, an amount determined as specified in the agreement.

The Company is in default of various restrictive and financial covenants under this agreement and has defaulted on certain interest payments. In connection therewith, a default rate of interest has been imposed. The lenders granted a waiver dated August 2002 related to deferral of the cash interest payments due and payable July 1 and October 1, 2002. The waiver expired October 2002 and no other amendments regarding the agreement have been executed to date.

Interest expense on these notes totaled approximately $5,293,000, $4,631,000 and $4,419,000 for the years ended December 31, 2003, 2002 and 2001, respectively. No additional notes were issued in 2003 for deferred interest. Additional notes in the amount of $1,990,523 were issued in 2002 for deferred interest. At December 31, 2003 and 2002, $8,744,000 and $3,451,000, respectively, are accrued and included with deferred interest payable.

(c) The Class A and Class B subordinated notes bear interest at 7%, and are due no later than April 23, 2007 (subparagraph (b) above). Interest accrues and compounds quarterly and is payable in full on April 23, 2007.

The Class B convertible subordinated notes are convertible at the holders' option into 8,556,458 shares of Class A common stock at a price of $.2337416 per share at any time prior to maturity.

The Company is in default of certain restrictive and financial covenants under these note agreements.

Interest expense on these notes totaled approximately $584,000, $545,000 and $522,000 in 2003, 2002 and 2001, respectively. At December 31, 2003 and 2002, $3,693,000 and $3,109,000, respectively, is accrued and included with deferred interest payable.

(d) In 1996, the Company entered into an agreement with three investors for $9,000,000 of 7% Pay-In-Kind Senior Subordinated Notes (the "Junior Subordinated Notes" as amended) due no later than April 2007 (subparagraph (b) above). Interest on the Junior Subordinated Notes accrues and compounds semiannually on January 15 and July 15, at which time additional notes are issued in a principal amount equal to the aggregate accrued interest thereon. Such additional notes ($4,647,681 and $3,740,258 at December 31, 2003 and 2002, respectively) also accrue interest compounded semiannually and are due no later than 2007.

**7. LONG-TERM DEBT (Continued)**

In connection with the original 1996 Junior Subordinated Notes, the Company granted warrants to the investors to purchase an aggregate of 14,368,299 shares of Class A common stock at an exercise price of $.00001 per share. At December 31, 2003, the warrants are exercisable and expire January 23, 2006.

In 1998, the Company sold an additional $9,100,000 of 7% Pay-In-Kind Junior Subordinated Notes due on June 15, 2008, $9,000,000 to the original three investors and $100,000 to certain officers. Interest on these junior subordinated notes accrues similar to those issued in 1996. Such additional notes ($3,825,383 and $2,965,984 at December 31, 2003 and 2002, respectively) also accrue interest compounded semiannually and are due in 2008.

In connection with the 1998 Junior Subordinated Notes, the Company granted warrants to the investors to purchase an aggregate of 7,263,975 shares of Class A common stock at an exercise price of $.00001 per share. At December 31, 2003, the warrants are exercisable and expire in June 2008.

In connection with the Junior Subordinated Note agreements, none of the creditors' representatives are currently members of the Company's Board, of which there are currently three members. The creditors may appoint up to four directors at their discretion.

The Company is in default of certain restrictive and financial covenants under these note agreements.

Interest expense on these notes totaled approximately $1,814,000, $1,707,000 and $1,581,000 in 2003, 2002 and 2001, respectively. At December 31, 2003 and 2002, $718,000 and $671,000, respectively, is accrued and included with deferred interest payable.

(e) In 1998, the Company issued approximately $4,141,000 of notes payable to former owners. Notes totaling approximately $2,250,000 require interest only payments at 5.5% through 2003, and include an automatic conversion feature for $1,000,000 of common stock upon consummation of an IPO. An additional $1,000,000 of the unpaid balance (depending upon amounts outstanding) may be converted into common stock at that time at the option of the holder. The number of shares for conversion is determined by dividing the unpaid principal balance to be converted by 80% of the per-share price of the offering. The notes are not convertible under any other circumstance. The notes stipulate that in the event the Company has not completed an IPO by October 2003, the unpaid principal balance and any unpaid interest are due. As the Company has not completed an IPO or paid off the principal balances of the notes as of December 31, 2003, the Company is in default under these notes.

During 1999, the Company issued notes payable to former owners of approximately $2,506,000. Notes totaling $1,325,000 require interest only payments at 8% through 2004, and automatically convert into shares of common stock upon consummation of an IPO. The number of shares issuable upon conversion is determined by dividing the unpaid principal balance to be converted by a predetermined percentage of the per-share price of the offering. Of the $1,325,000, the unpaid principal balance of $1,125,000 and $200,000, at December 31, 2003, are to be converted by 85% and 90%, respectively. The notes are not convertible under any other circumstance. In the event the Company has not completed an IPO by 2004, the unpaid principal balance is to be amortized and paid over the five-year period thereafter.

Approximate aggregate maturities of former owner notes are as follows: 2004 $2,798,000; 2005 $542,000; 2006 $508,000; 2007 $550,000; 2008 $578,000; thereafter $451,000.

(f) These credit and note purchase agreements contain various restrictive covenants which include, among other things, restrictions on capital expenditures, additional indebtedness, and disposal of assets. The covenants also restrict or prohibit additional investments, payments for dividends, issuance of options, warrants or rights, changes in corporate structure, changes in subordinated debt, disposal of subsidiary stock, engagement in other businesses, or change in the Company's fiscal year. The Company is also required to maintain certain minimum and maximum financial ratios. Certain of the covenants are generally less restrictive during the early years of the loans and become increasingly more restrictive in the later years. The Company is in default under certain of the covenants at December 31, 2003.

The prime rate of interest and LIBOR were 4.00% and 1.12%, respectively, at December 31, 2003.

Except for unsecured notes payable to former owners of acquired businesses of approximately $2,857,000 and a note payable to bank collateralized by real estate of approximately $243,000, all debt is in default and is recorded as current liabilities. In addition to the forbearance agreement on the senior credit facility, the Company had forbearance agreements with the subordinated note holders.

At December 31, 2003, unamortized loan costs of approximately $1,239,000, including the original issue discount, were being amortized over the actual and expected borrowings under the terms of the senior and junior subordinated, and subordinated debt. The remaining unamortized loan costs were written off in September 2004 upon default of the forbearance agreements (Note 15).

(Amounts in U.S. Dollars)

## 8. COMMITMENTS

**Operating leases:** The Company leases several of its funeral homes under operating leases which currently require aggregate monthly payments of approximately $79,000 and expire at various dates through May 2014. Certain leases include escalation clauses and fair market value purchase options exercisable after specified periods.

The Company also leases vehicles under noncancelable operating leases. The leases require monthly aggregate rents of approximately $52,000 and expire at various dates through May 2008.

Total approximate future minimum rental commitments under the above operating leases are as follows:

| Years Ending December 31, | Amount |
|---|---|
| 2004 | $1,285,000 |
| 2005 | 1,011,000 |
| 2006 | 837,000 |
| 2007 | 700,000 |
| 2008 | 539,000 |
| Thereafter | 1,905,000 |
| | $6,277,000 |

Total rent expense for 2003, 2002 and 2001 was approximately $1,466,000, $1,464,000 and $1,388,000, respectively.

**Legal matters:** The Company is involved in various legal matters arising in the normal course of business. Management believes that any liability as a result of these matters would not have a material effect on the Company's consolidated financial position, results of operations or cash flows.

**Employment agreements:** The Company has entered into various employment agreements with former owners of businesses acquired and certain other key employees. The employment agreements are for periods of one to five years and expire through 2006. Total approximate future minimum commitments under the above agreements are as follows:

| Years Ending December 31, | Amount |
|---|---|
| 2004 | $410,000 |
| 2005 | 224,000 |
| 2006 | 68,000 |
| | $702,000 |

**Noncompetition agreements:** The Company has entered into various noncompetition and consulting agreements with former owners of businesses acquired. If all such commitments are fulfilled by all parties, these agreements provide for approximate future payments as follows:

| Years Ending December 31, | Amount |
|---|---|
| 2004 | $1,510,000 |
| 2005 | 1,215,000 |
| 2006 | 1,079,000 |
| 2007 | 778,000 |
| 2008 | 384,000 |
| Thereafter | 83,000 |
| | $5,049,000 |

### 9. RETRACTABLE PREFERRED STOCK

The Company's Board of Directors is authorized to issue 10,000,000 shares of preferred stock with such rights, preferences, privileges and restrictions as they alone may determine, without approval by the common stockholders. The issuance of additional stock is restricted under the senior secured and subordinated credit agreements (Note 7).

During 1998 the Company created, authorized and issued 6,000 shares of Class A preferred stock. The stock was issued in connection with an acquisition of a business, at its stated value of $100 per share. The stock is nonvoting, provides for cumulative dividends at 7% per annum on the stated value, and is automatically convertible into shares of common stock in the event of an IPO at 85% of the IPO stock price. Beginning in 2003, the stock is redeemable by the Company, or at the option of the holders, subject to certain restrictions imposed by State of California statutes, at $100 per share. Dividends in arrears at December 31, 2003 and 2002 totaled $252,000 and $210,000, respectively, and are included in the carrying value of the retractable preferred stock in the accompanying consolidated balance sheets.

### 10. COMMON STOCK

The Company has 90,000,000 shares of no par value common stock authorized, of which 80,000,000 shares are designated as Class A and 10,000,000 are designated as Class B. There are 3,682,094 shares of Class A common stock issued and outstanding as of December 31, 2003 and 2002. There are no Class B shares issued.

The Class B common stock is convertible at the option of the holder at any time at the rate of one share of Class A common stock for each share of Class B common stock. The Class B common stock has principally the same rights and privileges as Class A common stock excluding voting rights.

### 11. STOCK OPTIONS AND WARRANTS

In 1992 the Company adopted a stock option plan under which options to purchase up to 343,500 shares of the Company's Class A common stock may be granted to officers, directors and consultants providing services to the Company. Both "incentive" and "nonqualified" options may be granted under the plan. Incentive options may be granted at an exercise price equal to the fair market value of the shares at the date of grant while nonqualified options may be granted at 85% or more of the then-current fair market value. Individual option agreements will contain such additional terms as may be determined by the Board of Directors at the time of grant. The plan provides for grants of options with a term of up to ten years. No options have been granted under this plan through December 31, 2003.

In 1993 the Company has granted nonqualified options to purchase 1,081,210 shares of Class A common stock to certain officers at an option price of $.02 per share. During 2001 699,606 nonqualified options were exercised. The remaining 381,604 options expired in 2003.

In connection with the issuance of Junior Subordinated Notes in January 1996 (Note 7), the Company adopted a Management Stock Option Plan, under which options may be granted to purchase up to 3,157,040 shares of Class A common stock. Up to 878,764 of such options (Base Options) may be granted to current and future operating management, which become exercisable ratably over five years. The options expire if not exercised ten years from the date of grant. The remaining 2,278,276 options (IRR Options) may be granted to management, but will become exercisable only if the purchasers of the Junior Subordinated Notes realize stipulated returns on their investments. As of December 31, 2003, 652,000 Base Options and 1,661,000 IRR Options are outstanding and an additional 218,764 of Base Options and 625,276 of IRR Options are available for grant to management as a result of the past issuance of Junior Subordinated Notes.

(Amounts in U.S. Dollars)

## 11. STOCK OPTIONS AND WARRANTS (Continued)

A summary of the status of the stock option plans is as follows at December 31:

| | 2003 | | 2002 | | 2001 | |
|---|---|---|---|---|---|---|
| | Shares | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price | Shares | Weighted Average Exercise Price |
| Outstanding at beginning of period | 3,204,604 | $0.02 | 3,221,804 | $0.02 | 3,934,210 | $0.02 |
| Granted | — | — | — | — | — | — |
| Exercised | — | — | — | — | (699,606) | 0.02 |
| Forfeited | (400,600) | 0.02 | (17,200) | 0.02 | (12,800) | — |
| Expired | (491,004) | 0.02 | — | — | — | — |
| Outstanding at end of period | 2,313,000 | $0.02 | 3,204,604 | $0.02 | 3,221,804 | $0.02 |
| Exercisable at end of period | 652,200 | $0.02 | 1,093,204 | $0.02 | 1,010,604 | $0.02 |

A further summary of options outstanding at December 31, 2003 is as follows:

| Options Outstanding | | | Options Exercisable | |
|---|---|---|---|---|
| Number Outstanding | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price | Number Exercisable | Weighted Average Exercise Price |
| 184,000 | 5 years | $0.02 | 31,200 | $0.02 |
| 719,000 | 4 years | 0.02 | 211,000 | 0.02 |
| 310,000 | 3 years | 0.02 | 90,000 | 0.02 |
| 1,100,000 | 2 years | 0.02 | 320,000 | 0.02 |
| 2,313,000 | | | 652,200 | |

At December 31, 2003, the Company also has warrants outstanding and exercisable which were issued in connection with various debt agreements as follows:

| Number Outstanding and Exercisable | Weighted Average Remaining Contractual Life | Weighted Average Exercise Price |
|---|---|---|
| 2,618,941 | 5.1 years | $ 0.01 |
| 14,368,299 | 3.3 years | 0.01 |
| 7,263,975 | 4.5 years | 0.0001 |
| 24,251,215 | | |

On January 21, 2005, warrants were exercised to purchase approximately 3.2 million shares of common stock at $0.00001 per share.

## 12. EMPLOYEE BENEFIT PLAN

The Company has a qualified 401(k) profit sharing and savings plan (the Plan) for all eligible employees. Under the Plan, employees may defer from 1% to 15% of their compensation each year based on provisions as outlined in the Plan. The Plan allows the Company to make matching contributions on behalf of those who actively participate equal to 25% of the employees' salary deferrals, up to 5% of the employees' voluntary deferral. The Plan also provides for discretionary additional matching employer contributions which may be made at the end of any Plan year. Company contributions vest ratably pro rata over five years. For the years ended December 31, 2003, 2002 and 2001, the Company contributed approximately $82,000, $89,000 and $98,000, respectively, to the Plan.

(Amounts in U.S. Dollars)

## 13. INCOME TAX MATTERS

The provision for income taxes consisted of the following:

| | 2003 | 2002 | 2001 |
|---|---|---|---|
| Current: | | | |
| Federal | $ — | $ — | $ — |
| State | 14,065 | 11,175 | — |
| | 14,065 | 11,175 | — |
| Future: | | | |
| Federal | 444,436 | 1,301,352 | — |
| State | 26,243 | 224,189 | — |
| | 470,679 | 1,525,541 | — |
| Total provision for income taxes | $484,744 | $1,536,716 | $ — |

The provision for income taxes on earnings subject to income taxes differs from the statutory federal rate at December 31 due to the following:

| | 2003 | 2002 | 2001 |
|---|---|---|---|
| Taxes at U.S. statutory rate (34%) | $(1,923,852) | $(1,117,638) | $(2,346,924) |
| State income taxes, net of federal benefit | (130,449) | (118,817) | (201,807) |
| Effect of valuation allowance | 1,822,594 | 2,756,026 | 2,092,014 |
| Permanent book-tax differences | 702,011 | 4,754 | 456,717 |
| Other items | 14,440 | 12,391 | — |
| Total provision for income taxes | $ 484,744 | $ 1,536,716 | $ — |

Future income taxes reflect the net tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

Significant components of the Company's future tax assets and liabilities were as follows:

| | 2003 | 2002 |
|---|---|---|
| Future tax assets: | | |
| Net operating loss carryforwards | $ 10,239,000 | $ 9,111,000 |
| Prearranged contracts | 886,000 | 879,000 |
| Intangible assets | 783,000 | 715,000 |
| Capital loss carryforward | 750,000 | — |
| Other | 399,000 | 1,243,000 |
| Total future tax assets | 13,057,000 | 11,948,000 |
| Valuation allowance | (10,227,000) | (8,771,000) |
| Net future tax assets | 2,830,000 | 3,177,000 |
| Future tax liabilities: | | |
| Property and equipment | (2,728,000) | (3,074,000) |
| Goodwill | (1,996,000) | (1,526,000) |
| Other | (102,220) | (102,541) |
| Total future tax liabilities | (4,826,220) | (4,702,541) |
| Net future tax asset (liability) | $ (1,996,220) | $ (1,525,541) |

The future tax amounts have been classified in the accompanying consolidated balance sheets as non-current liabilities.

(Amounts in U.S. Dollars)

## 13. INCOME TAX MATTERS (Continued)

The Company has federal net operating loss carry-forwards of approximately $27.9 million at December 31, 2003, all of which expire in various years from 2007 to 2024, unless previously utilized. The Company also has state net operating loss carryforwards of approximately $20.6 million at December 31, 2003, all of which expire in various years from 2004 to 2024, unless previously utilized. As of December 31, 2003, the Company has a federal capital loss carry-forward of approximately $750,000. The capital loss carry-forward expires in 2008. Pursuant to Internal Revenue Code Sections 382 and 383, annual use of the Company's net operating loss and capital loss carryforwards may be limited because of cumulative changes in ownership.

A valuation allowance is recorded when it is more likely than not that some portion or all of the future tax assets will not be realized. The ultimate realization of the future tax assets depends on the ability to generate sufficient taxable income of the appropriate character in the future and in the appropriate taxing jurisdictions. As the generation of sufficient taxable income is uncertain, the Company has recorded a valuation allowance.

In connection with the adoption of Section 3062 on January 1, 2002, the Company ceased amortizing goodwill for financial statement purposes. The Company has tax basis in certain of its goodwill that continues to be amortized for tax purposes. Accordingly, future tax liabilities are recorded for the temporary difference between the book and tax basis of such tax deductible goodwill. For purposes of determining the valuation allowance recorded for the years ended December 31, 2003 and 2002, the future tax liabilities related to the tax deductible goodwill are excluded because their reversal is indefinite and not identifiable, absent impairment of the carrying amount of goodwill.

## 14. SUPPLEMENTAL CASH FLOWS INFORMATION

| | December 31, | | | Nine Months Ended September 30, (Unaudited) | |
|---|---|---|---|---|---|
| | 2003 | 2002 | 2001 | 2004 | 2003 |
| Supplemental Disclosures of Cash Flow Information | | | | | |
| Cash payments for interest | $ 2,940,875 | $4,267,404 | $5,827,856 | $ 2,290,339 | $ 1,970,099 |
| Supplemental Schedule of Noncash Investing and Financing Activities | | | | | |
| Sale of business, cash sales price (Note 3) | $ 8,550,000 | $ — | $2,059,168 | $ 3,009,000 | $ 8,550,000 |
| Working capital: | | | | | |
| Inventories | $ 127,513 | $ — | $ 54,886 | $ 39,269 | $ 127,513 |
| Other | 8,857 | — | 82,409 | 60,320 | 12,329 |
| Accounts payable and accrued expenses | (37,705) | — | — | (12,759) | (37,705) |
| Net Working Capital | 98,665 | — | 137,295 | 86,830 | 102,137 |
| Prearranged funeral contracts | 2,006,657 | — | — | 2,600,049 | 2,006,657 |
| Deferred prearranged funeral contract revenue | (2,006,657) | — | — | (2,600,049) | (2,006,657) |
| Net prearranged funeral contracts | — | — | — | — | — |
| Subordinated debt | — | — | — | (183,394) | — |
| Net book value of assets sold: | | | | | |
| Property and equipment | 3,322,670 | — | 1,151,440 | 3,014,238 | 3,322,670 |
| Goodwill | 5,465,072 | — | 1,017,630 | 1,088,037 | 5,465,072 |
| Other intangibles | 204,366 | — | 39,384 | 64,164 | 204,366 |
| Total net book value of assets sold | 8,992,108 | — | 2,208,454 | 4,166,439 | 8,992,108 |
| Loss on sale of business | (540,773) | — | (286,581) | (1,060,875) | (544,245) |
| | $ 8,550,000 | $ — | $2,059,168 | $ 3,009,000 | $ 8,550,000 |
| Junior subordinated and subordinated notes issues for interest | $ 1,766,822 | $3,639,871 | $4,848,964 | $ 1,897,940 | $ 1,766,822 |

Substantially all cash received from the sale of business was used to repay senior secured loan indebtedness.

## 15. MANAGEMENT PLANS

The Company's senior secured credit agreement facility expired on June 30, 2003, and as a result of the Company's inability thus far to make payment of the balloon payment amount due at the facilities expiration, or to refinance the obligation, the Company is in both payment and financial covenant default of the agreement (Note 7).

The Company had previously entered into a forbearance agreement with its senior secured and subordinated lenders, but on September 28, 2004, was notified by its senior secured lenders of a default of the agreement, thereby terminating the forbearance period. The senior secured lenders further advised that they were not initiating any further immediate action, but were reserving all of their rights relative to the senior secured credit agreement.

Capital and credit market parameters have materially shifted since the establishment of the Company's senior secured credit agreement facility in 1998. Senior and subordinated leveraging levels have tightened significantly since the establishment of the credit facility. As a result, albeit the Company generates significant cash flow available for repayment of indebtedness, the current credit market parameters represent challenges to simply renegotiating or refinancing the now reduced senior secured indebtedness, requiring the Company to seek additional capital in the form of subordinated indebtedness or equity to refinance the senior debt.

The Company has engaged an investment banking firm to assist the Company in seeking capital to refinance the outstanding senior secured indebtedness and work with the Company's subordinated debt holders to restructure their indebtedness and the Company's capital structure in conjunction with a refinancing. The Company, with the concurrence and assistance of certain of its subordinated debt holders, is simultaneously pursuing a merger with a Company in the industry, which, if successful, would provide funds sufficient to satisfy the Company's obligations under its senior secured credit facility. If this merger is successfully completed, it is anticipated the funds available to repay the subordinated debt holders would be substantially less than the carrying value of debt and this would indicate that goodwill would be impaired and this impairment charge is estimated to be in excess of $10 million.

The Company is in ongoing discussions with its lenders pursuing a refinancing and restructuring of the Company's capital structure while simultaneously pursuing a merger opportunity. Although no assurances can be given, management believes that it will have adequate cash flow and liquidity to fund its operations, as well as maintain bank relationships, until one of those alternatives is finalized. If management is unsuccessful, or if the debt holders demand acceleration of the debt under the default provisions, the Company may need to seek protection from the courts.

## 16. SUBSEQUENT EVENT

On December 23, 2004, the Company entered into an agreement for the sale of substantially all of its assets to Keystone Group Holdings, Inc., a funeral service provider based in Tampa Florida. Keystone Group Holdings, Inc. is planning to facilitate the acquisition through an initial public offering ("IPO") of Income Participating Securities.

KEYSTONE NORTH AMERICA INC.

UNAUDITED *PRO FORMA* CONSOLIDATED FINANCIAL STATEMENTS

## COMPILATION REPORT ON *PRO FORMA* CONSOLIDATED FINANCIAL STATEMENTS

The Board of Directors
Keystone North America Inc.

We have read the accompanying unaudited *pro forma* consolidated balance sheet of Keystone North America Inc. ("KNA") as at September 30, 2004 and the unaudited pro forma consolidated income statements for the nine months ended September 30, 2004 and the year ended December 31, 2003 and have performed the following procedures:

1. Compared the figures in the column captioned Keystone North America Inc. to the audited balance sheet of KNA as at August 27, 2004 and found them to be in agreement.
2. Compared the figures in the columns captioned Keystone Group Holdings, Inc. to the unaudited financial statements of Keystone Group Holdings, Inc. and Subsidiaries for the nine months ended September 30, 2004 and the audited financial statements the year ended December 31, 2003 and found them to be in agreement.
3. Compared the figures in the column captioned HFSC Holdings, Inc. to the unaudited financial statements of HFSC Holdings, Inc. for the nine months ended September 30, 2004 and the audited financial statements for the year ended December 31, 2003 and found them to be in agreement.
4. Made enquiries of certain officials of KNA who have responsibility for financial and accounting matters about:
   (a) the basis for determination of the pro forma adjustments; and
   (b) whether the *pro forma* consolidated financial statements comply as to form in all material respects with the published requirements of Canadian securities legislation.

   The officials:

   (c) described to us the basis for determination of the *pro forma* adjustments; and
   (d) stated that the *pro forma* consolidated financial statements comply as to form in all material respects with the published requirements of Canadian securities legislation.
5. Read the notes to the unaudited *pro forma* consolidated financial statements, and found them to be consistent with the basis described to us for determination of the pro forma adjustments.
6. Recalculated the application of the Pro Forma Adjustments to the aggregate amount in columns entitled Keystone North America, Inc., Keystone Group Holdings, Inc. and HFSC Holdings, Inc. at September 30, 2004 and for the nine months ended September 30, 2004 and the year ended December 31, 2003 and found the amounts in the column captioned Pro Forma Consolidated Financials to be arithmetically correct.

A *pro forma* financial statement is based on management assumptions and adjustments which are inherently subjective. The foregoing procedures are substantially less than either an audit or a review, the objective of which is the expression of assurance with respect to management's assumptions, the *pro forma* adjustments, and the application of the adjustments to the historical financial information. Accordingly, we express no such assurance. The foregoing procedures would not necessarily reveal matters of significance to the *pro forma* consolidated financial statements, and we therefore make no representation about the sufficiency of the procedures for the purposes of a reader of such statements.

Tampa, Florida
January 28, 2005

(Signed) ERNST & YOUNG LLP
Certified Public Accountants

## KEYSTONE NORTH AMERICA INC.

## UNAUDITED *PRO FORMA* CONSOLIDATED BALANCE SHEET

### (in thousands of U.S. Dollars)
### As of September 30, 2004

| | Keystone North America Inc. (US $) | Keystone Group Holdings, Inc. (US $) | HFSC Holdings, Inc. (US $) | *Pro Forma* Adjustments (US $) | Note 3 | *Pro Forma* Consolidated Financials (US $) |
|---|---|---|---|---|---|---|
| **ASSETS** | | | | | | |
| Current Assets: | | | | | | |
| Cash and cash equivalents | $ — | $ 3,326 | $ 2,893 | $ (3,719) | a,b,c,d | $ 2,500 |
| Maketable securities | — | 842 | — | — | | 842 |
| Accounts receivable, less allowance for doubtful accounts | — | 4,019 | 3,159 | — | | 7,178 |
| Inventories | — | 1,751 | 2,044 | — | | 3,795 |
| Income tax receivable | — | 683 | — | — | | 683 |
| Prepaid and other current assets | — | 324 | 1,166 | 2,300 | a | 3,790 |
| Future income taxes | — | 465 | — | — | | 465 |
| Total current assets | — | 11,410 | 9,262 | (1,419) | | 19,253 |
| Prearranged funeral contracts | — | 24,151 | 16,687 | — | | 40,838 |
| Preneed cemetery contracts | — | — | 3,085 | — | | 3,085 |
| Property and equipment, net | — | 33,233 | 34,865 | — | | 68,098 |
| Cemetery property | — | — | 2,072 | — | | 2,072 |
| Goodwill, net | — | 68,925 | 46,399 | (14,787) | c,d | 100,537 |
| Tradenames | — | — | — | 16,760 | d | 16,760 |
| Covenants not to compete, net | — | 4,466 | — | 2,378 | d | 6,844 |
| Restricted cash | — | — | — | 18,980 | a | 18,980 |
| Deferred charges and other assets | — | 383 | 4,216 | 7,534 | a,b,c | 12,133 |
| Total assets | $ — | $142,568 | $116,586 | $ 29,446 | | $288,600 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)** | | | | | | |
| Current Liabilities: | | | | | | |
| Outstanding checks | $ — | $ — | $ 115 | $ — | | $ 115 |
| Accounts payable | — | 1,152 | 2,236 | — | | 3,388 |
| Accrued salaries and wages | — | 766 | — | — | | 766 |
| Other accrued expenses | — | 653 | — | 2,300 | a | 2,953 |
| Retractable preferred stock | — | — | 883 | (883) | c | — |
| Income taxes payable | — | — | 37 | — | | 37 |
| Current maturities of long-term debt and obligations under agreements with former owners | — | 77,149 | 49,114 | (126,134) | c,d | 129 |
| Current maturities of subordinated notes payable and deferred interest | — | — | 80,665 | (80,665) | c | — |
| Total current liabilities | — | 79,720 | 133,050 | (205,382) | | 7,388 |
| Long-term debt less current maturities | — | — | 2,305 | 40,795 | b,c | 43,100 |
| Deferred prearranged funeral contracts | — | 24,198 | 17,600 | — | | 41,798 |
| Obligations under agreements with former owners, less current maturities | — | 7,252 | — | 11,728 | c,d | 18,980 |
| Other long-term obligations | — | 368 | — | — | | 368 |
| Subordinated notes | — | — | — | 67,870 | a | 67,870 |
| Deferred preneed cemetery contract revenues | — | — | 6,584 | — | | 6,584 |
| Future income taxes | — | 5,024 | 2,408 | — | c,d | 7,432 |
| Minority interest | — | — | — | 22,704 | c,d | 22,704 |
| Total liabilities | — | 116,562 | 161,947 | (62,285) | | 216,224 |
| Shareholders' equity (deficit) | | | | | | |
| Share capital | — | 32,819 | 3,598 | 35,959 | a,c,d | 72,376 |
| Notes receivable — common stock | — | (329) | — | 329 | d | — |
| Accumulated deficit | — | (6,484) | (48,959) | 55,443 | c,d | — |
| Total shareholders' equity (deficit) | — | 26,006 | (45,361) | 91,731 | | 72,376 |
| Total liabilities and shareholders' equity | $ — | $142,568 | $116,586 | $ 29,446 | | $288,600 |

*See accompanying notes.*

## KEYSTONE NORTH AMERICA INC.

## UNAUDITED *PRO FORMA* CONSOLIDATED INCOME STATEMENTS

### (in thousands of U.S. Dollars except per share amount)
### Year Ended December 31, 2003

| | Keystone North America Inc. (US $) | Keystone Group Holdings, Inc. (US $) | HFSC Holdings, Inc. (US $) | *Pro Forma* Adjustments (US $) | Note 3 | *Pro Forma* Consolidated Financials (US $) |
|---|---|---|---|---|---|---|
| **Revenues** | | | | | | |
| Funeral services | $ — | $46,413 | $36,978 | $ — | | $83,391 |
| Cemetery | — | — | 1,048 | — | | 1,048 |
| Other | — | 2,473 | — | — | | 2,473 |
| Total revenues | — | 48,886 | 38,026 | — | | 86,912 |
| Cost and expenses | — | 31,460 | 24,874 | — | | 56,334 |
| Gross profit | — | 17,426 | 13,152 | — | | 30,578 |
| Other operating expenses | | | | | | |
| Corporate, general and administrative expenses | — | 3,188 | 3,327 | — | l,m,n | 6,515 |
| Depreciation | — | 2,093 | 1,984 | — | h | 4,077 |
| Amortization of covenants not to compete | — | 1,112 | — | 257 | h | 1,369 |
| Non-compete expenses | — | — | 1,330 | (1,330) | g | — |
| Consulting expenses | — | — | 505 | (505) | g | — |
| Income from operations | — | 11,033 | 6,006 | 1,578 | | 18,617 |
| Other (income) expense: | | | | | | |
| Interest expense | — | 6,477 | 2,884 | 3,550 | i | 12,911 |
| Interest expense — payment in kind | — | — | 7,794 | (7,794) | i | — |
| Interest expense — owner obligations | — | — | — | 497 | i | 497 |
| Deferred loan cost amortization | — | — | 583 | 570 | j | 1,153 |
| Dividend on retractable preferred stock | — | — | 42 | (42) | k | — |
| Loan restructuring costs | — | — | 373 | (373) | k | — |
| Other income | — | (310) | (161) | (497) | i | (968) |
| Income (loss) before taxes | — | 4,866 | (5,509) | 5,667 | | 5,024 |
| Income tax expense | — | 1,943 | 485 | (418) | e | 2,010 |
| Minority interest | — | — | — | 442 | f | 442 |
| Income (loss) from continuing operations | — | 2,923 | (5,994) | 5,643 | | 2,572 |
| Loss from discontinued operations | — | — | (191) | — | | (191) |
| Net income (loss) | $ — | $ 2,923 | $(6,185) | $ 5,643 | | $ 2,381 |
| Net income per share | | | | | | $ 0.14 |

*See accompanying notes.*

## KEYSTONE NORTH AMERICA INC.

## UNAUDITED *PRO FORMA* CONSOLIDATED INCOME STATEMENTS

### (in thousands of U.S. Dollars except per share amount)
### Nine Months Ended September 30, 2004

| | Keystone North America Inc. (US $) | Keystone Group Holdings, Inc. (US $) | HFSC Holdings, Inc. (US $) | *Pro Forma* Adjustments (US $) | Note 3 | *Pro Forma* Consolidated Financials (US $) |
|---|---|---|---|---|---|---|
| **Revenues** | | | | | | |
| Funeral services | $ — | $33,918 | $26,857 | $ — | | $60,775 |
| Cemetery | — | — | 707 | — | | 707 |
| Other | — | 1,938 | — | — | | 1,938 |
| Total revenues | — | 35,856 | 27,564 | — | | 63,420 |
| Cost and expenses | — | 23,460 | 18,864 | — | | 42,324 |
| Gross profit | — | 12,396 | 8,700 | — | | 21,096 |
| Other operating expenses | | | | | | |
| Corporate, general and administrative expenses | — | 2,430 | 2,233 | — | l,m,n | 4,663 |
| Depreciation | — | 1,509 | 1,466 | — | h | 2,975 |
| Amortization of covenants not to compete | — | 846 | — | 181 | h | 1,027 |
| Non-compete expenses | — | — | 809 | (809) | g | — |
| Consulting expenses | — | — | 283 | (283) | g | — |
| Impairment of long-lived assets | — | 111 | — | — | | 111 |
| Income from operations | — | 7,500 | 3,909 | 911 | | 12,320 |
| Other (income) expense: | | | | | | |
| Interest expense | — | 4,607 | 2,290 | 2,787 | i | 9,684 |
| Interest expense- payment in kind | — | — | 6,597 | (6,597) | i | — |
| Interest expense- owner obligations | — | — | — | 373 | i | 373 |
| Deferred loan cost amortization | — | — | 1,208 | (343) | j | 865 |
| Dividend on retractable preferred stock | — | — | 32 | (32) | k | — |
| Loan restructuring costs | — | — | 612 | (612) | k | — |
| Other income | — | (363) | — | (373) | i | (736) |
| Income (loss) before taxes | — | 3,256 | (6,830) | 5,708 | | 2,134 |
| Income tax expense | — | 1,097 | 380 | (758) | e | 719 |
| Minority Interest | — | — | — | 208 | f | 208 |
| Income (loss) from continuing operations | — | 2,159 | (7,210) | 6,258 | | 1,207 |
| Loss from discontinued operations | — | — | (1,170) | — | | (1,170) |
| Net income (loss) | $ — | $ 2,159 | $ (8,380) | $ 6,258 | | $ 37 |
| Net income per share | | | | | | $ 0.00 |

*See accompanying notes.*

# KEYSTONE NORTH AMERICA INC.

## NOTES TO THE UNAUDITED *PRO FORMA* CONSOLIDATED FINANCIAL STATEMENTS

### As at and for the nine-month period ended September 30, 2004 and for the year ended December 31, 2003

**1. BASIS OF PRESENTATION**

Keystone North America Inc. ("Keystone North America") was incorporated on August 27, 2004 under the laws of the Province of Ontario. Keystone North America indirectly incorporated a wholly owned subsidiary, Keystone Newport ULC (and together with Keystone North America, the "Issuer") on August 27, 2004 as an unlimited liability corporation pursuant to the laws of the Province of Nova Scotia. The Issuer will issue income participating securities ("IPSs") for cash pursuant to an initial public offering (the "Offering"). Each IPS consists of one common share of Keystone North America and Cdn$4.286 of aggregate principal amount of 14.5% subordinated notes of Keystone Newport ULC.

The pro forma consolidated balance sheet as at September 30, 2004 and the pro forma consolidated income statements for the nine months ended September 30, 2004 and for the year ended December 31, 2003 have been prepared from the audited opening balance sheet of Keystone North America as of August 27, 2004, the unaudited interim consolidated financial statements of Keystone Group Holdings, Inc. ("Keystone") as of and for the nine months ended September 30, 2004, the unaudited interim consolidated financial statements of HFSC Holdings. Inc. ("HFSC") as of and for the nine months ended September 30, 2004, the audited consolidated financial statements of Keystone for the year ended December 31, 2003, and the audited consolidated financial statements of HFSC for the year ended December 31, 2003. These financial statements are included elsewhere in this prospectus.

The pro forma consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The audited consolidated financial statements of Keystone and HFSC have been prepared in accordance with Canadian generally accepted accounting principles.

The pro forma consolidated balance sheet gives effect to the transactions in Note 2 as if they had occurred on September 30, 2004. The pro forma consolidated income statements for the nine months ended September 30, 2004 and the year ended December 31, 2003 give effect to the transactions in Note 2 as if the transactions occurred on January 1, 2003.

The pro forma consolidated financial statements are not necessarily indicative of the results that would have actually occurred had the transactions been consummated at the dates indicated nor are they necessarily indicative of future operating results or the financial position of Keystone North America.

**2. THE ACQUISITION**

The Issuer will use the net proceeds of the Offering to acquire indirectly an 85.3% voting equity ownership in Keystone. Keystone will have acquired assets, liabilities and stock of certain subsidiaries of HFSC at the time of the Offering. Existing investors and members of management of Keystone and HFSC will hold the remaining 14.7% of Keystone voting equity. The estimated net proceeds from the IPSs, after deducting fees payable to the underwriters of the Offering (the "Underwriters") and estimated expenses of the Offering, will be approximately $126.7 million. In addition to the $59.7 million of 14.5% subordinated notes that will be represented by IPSs following the completion of the Offering, $8.1 million of subordinated notes will be separately sold by Keystone Newport ULC (the "Separate Subordinated Notes"). Keystone North America will also arrange for a new credit facility in the aggregate amount of $58.0 million (the "New Credit Facility"), of which $43.1 million is expected to be drawn as of the close.

Upon completion of the offering, Keystone North America will acquire 100% of the Class A common shares of Keystone; Keystone ULC will acquire 100% of the preferred shares of Keystone; and the existing investors of Keystone and HFSC will acquire Class B and C common shares of Keystone and receive cash. The remainder of the net proceeds, plus certain amounts to be drawn under the New Credit Facility, will be used to repay existing indebtedness of Keystone and HFSC, fund future payments of former owner obligations of Keystone and Hamilton, and pay for transition costs associated with the Hamilton acquisition. Existing investors of Keystone will distribute a portion of their cash proceeds and Class B common shares to members of Keystone management upon completion of the Offering.

The Issuer has granted the Underwriters an over-allotment option (the "Over-Allotment Option") to purchase up to a total of 1,688,017 additional IPSs for the purpose of covering over-allotments, if any, and for market stabilization purposes. If the Over-Allotment Option is exercised, the Issuer will use the net proceeds to acquire additional Class A common stock and preferred stock of Keystone North America, which in turn will use such amounts to redeem all or a portion of the Class C common stock of Keystone North America held by existing investors and members of management of the Company. If the Over-Allotment Option is exercised in full, the Issuer will own 93.7% of the voting equity of Keystone and existing investors and members of management of the Company will own 6.3% of the voting equity of Keystone. The pro forma financial statements do not reflect the potential Over-Allotment Option.

## 3. PRO FORMA ADJUSTMENTS

### (a) Initial Public Offering

The Issuer will issue 17,100,000 IPSs pursuant to the Offering for net proceeds of approximately Cdn$155 million on closing of the Offering after deducting estimated expenses of the Offering and underwriters' fees.

The U.S. dollar equivalent of the Offering, based on the exchange rate of Cdn$1.2272 per $US, is:

| | |
|---|---|
| IPS subordinated notes | $ 59.7 |
| IPS common shares | 79.6 |
| Subtotal | 139.3 |
| Total expenses related to IPS issuance | 12.6 |
| Net total | $126.7 |

Of the $12.6 million of expenses, $5.4 million will be treated as deferred financing costs, and be amortized over the term of the related debt as interest expense, and $7.2 million will be charged directly against share capital for a net amount of share capital of $72.4 million.

Additionally, Keystone Newport ULC will issue Cdn$10.0 million of Separate Subordinated Notes. The U.S. dollar equivalent of the Offering, based on the exchange rate of 1.2272 per U.S. dollar is $8.1 million. Fees associated with the issuance of the Separate Subordinated Notes of $0.3 million will be treated as deferred financing costs and amortized over the term of the Separate Subordinated Notes.

Offering proceeds of $19.0 million were used to fund restricted accounts that secure former owner obligations. Offering proceeds of $2.3 million were segregated to pay for Hamilton transition costs.

### (b) Credit Facilities

Keystone America, Inc., a subsidiary of Keystone North America will arrange for a senior credit facility in the amount of $58.0 million with a total amount drawn on the facilities of $43.1 million at closing as part of the initial structuring transaction. A fee of approximately $1.5 million will be recorded related to this facility as deferred financing costs and amortised over 3 years. Additionally, the $0.6 million cost to secure a 2.95% (plus applicable margin not to exceed 4%) interest rate cap will be amortized over 3 years.

### (c) Acquisition of assets, liabilities and certain subsidiaries of HFSC

The acquisition of assets, liabilities and stock of certain subsidiaries of HFSC will be accounted for using the purchase method. The purchase price of $57.1 million has been preliminarily allocated on a pro forma basis to the assets and liabilities of HFSC at September 30, 2004 as follows:

| | |
|---|---|
| Current assets, less current liabilities | $ 2.6 |
| Property and equipment | 36.9 |
| Other assets and intangibles | 23.8 |
| Future income taxes | (2.4) |
| Other obligations | (41.1) |
| Subtotal | 19.8 |
| Goodwill | 37.3 |
| Total | $ 57.1 |

The actual determination and allocation of the purchase price will be based upon the assets purchased and the liabilities assumed at the effective date of the acquisition and other information available at that date. Accordingly, the actual amounts for each of the assets will vary from the pro forma amounts and the variations may be material. The Issuer will obtain a third party valuation to assist in determining the purchase price allocation.

Other assets and intangibles principally represent the prearranged funeral and cemetery contracts of $19.8 million. Other obligations principally represent deferred prearranged funeral contract and deferred preneed cemetery contract revenues of $24.2 million, former owner obligations of $9.0 million and minority interest of $7.9 million.

**3. PRO FORMA ADJUSTMENTS (Continued)**

Keystone North America intends to make certain tax elections with respect to the acquisition of HFSC subsidiary stock. These elections will allow certain stock purchases to be treated as a purchase of assets for U.S. federal tax purposes. As the timing and scope of this election has not been finalized, Keystone North America has not reflected the results of this election within the pro forma financial statements.

Keystone North America did not acquire the following assets and liabilities shown on the accompanying historical HFSC balance sheet as of September 30, 2004:

| | |
|---|---|
| Deferred charges and other assets | $ 0.2 |
| Retractable preferred stock | $ 0.9 |
| Long-term debt | $51.4 |
| Subordinated notes payable and deferred interest | $80.7 |

Immediately preceding the acquisition Hamilton paid down $1.3 million on existing debt out of cash reserves.

(d) **Acquisition of Keystone**

The acquisition of Keystone will be accounted for using the purchase method. The purchase price of $97.3 million has been preliminarily allocated to the assets and liabilities of Keystone at September 30, 2004 as follows:

| | |
|---|---|
| Current assets, less current liabilities | $ 7.0 |
| Property and equipment | 33.2 |
| Other assets and intangibles | 48.1 |
| Future income taxes, non-current | (5.0) |
| Other obligations | (49.3) |
| Subtotal | 34.0 |
| Goodwill | 63.3 |
| Total | $ 97.3 |

The actual determination and reallocation will be based upon the assets purchased and the liabilities assumed at the effective date of the acquisition and other information available at that date. Accordingly, the actual amounts for each of the assets will vary from the pro forma amounts and the variations may be material. The Issuer will obtain a third party valuation to assist in determining the purchase price allocation.

Other assets and intangibles represent the prearranged funeral contracts of $24.2 million, tradenames of $16.8 million, covenants not to compete of $6.8 million that will be amortized over length of the agreement and other assets of $0.3 million. Other obligations represent prearranged funeral contract revenues of $24.2 million, former owner obligations of $10.0 million, other long-term obligations of $0.3 million and minority interest of $14.8 million.

Immediately preceding the acquisition Keystone paid down $0.7 million on existing debt out of cash reserves. Keystone retired $74.8 million of debt obligations in connection with its acquisition by Keystone North America.

(e) **Tax Provision**

Reflects the tax impact of pro forma adjustments and the pro forma utilization of HFSC tax losses.

(f) **Minority Interests**

The minority interest pro forma adjustments on the pro forma consolidated income statements represents the minority interest portion of consolidated net income.

(g) **Noncompete and consulting expenses**

Eliminates the noncompete and consulting payments expensed by HFSC during the year.

(h) **Depreciation and Amortization**

Depreciation and amortization have not been adjusted on HFSC assets because the preliminary fair value adjustment to property and equipment and intangible assets equals existing carrying value. Additionally, any changes to asset useful lives have not yet been

**3. PRO FORMA ADJUSTMENTS (Continued)**

determined. Preliminary adjustments have been made to Keystone intangible assets. As a result, intangible asset amortization of $1.0 million and $1.4 million for the nine months ended September 30, 2004 and the twelve months ended December 31, 2003, respectively, has been recorded.

(i) **Interest Expense**

Historical interest expense of $13.5 million and $17.2 million for the nine months ended September 30, 2004 and the twelve months ended December 31, 2003, respectively, has been eliminated.

Interest expense has been adjusted to reflect interest expense of $9.7 million and $12.9 million, for the nine months ended September 30, 2004 and the twelve months ended December 31, 2003, respectively, on the Subordinated Notes, Separate Subordinated Notes and New Credit Agreement, at a rates of 14.5%, 14.5%, and 6.95% respectively.

Interest expense of $0.4 million and $0.5 million, for the nine months ended September 30, 2004 and the twelve months ended December 31, 2003, respectively, relate to imputed interest on the former owner obligations. Other income in the same amount was recorded related to interest income earned on restricted cash investments.

(j) **Deferred Loan Costs**

The adjustments to loan cost amortization reflects amortization on loan costs from new indebtness of $0.9 million and $1.1 million for the nine months ended September 30, 2004 and the twelve months ended December 31, 2003, respectively.

(k) **Preferred Stock Dividends and Loan Restructuring Costs**

Eliminates expensing of loan restructuring costs and dividends on preferred stock made by HFSC.

(l) **General and Administrative Expenses**

Estimated administrative expenses in the amount of $1.0 million to be incurred by the Issuer in connection with reporting to shareholders, investor relations, directors' fees and insurance and other expenses have **not** been reflected in the pro forma consolidated income statements.

(m) **Corporate Synergies**

With the combination of the two companies, HFSC and Keystone, certain duplicative functions of the existing corporate offices will be eliminated, generating estimated cost savings upon combination of $1.8 million. These savings have **not** been presented in the pro forma financial statements.

(n) **Purchase Discounts**

Estimated purchase discounts of $0.3 million resulting from increased volume commitments from key suppliers has **not** been included in the pro forma financial statements.

**4. PRO FORMA NET INCOME PER SHARE**

The calculation of pro forma net income per share on the pro forma consolidated income statements is based on the pro forma number of Common Shares outstanding for the year ended December 31, 2003 and for the nine months ended September 30, 2004 as if the issuance had taken place on January 1, 2003.

## CERTIFICATE OF THE ISSUER, THE PROMOTER AND THE CREDIT SUPPORTERS

Date: January 31, 2005

The foregoing constitutes full, true and plain disclosure of all material facts relating to the securities offered by this prospectus as required by Part 9 of the *Securities Act* (British Columbia), by Part 9 of the *Securities Act* (Alberta), by Part XI of *The Securities Act* (Saskatchewan), by Part VII of *The Securities Act* (Manitoba), by Part XV of the *Securities Act* (Ontario), by Part 6 of the *Securities Act* (New Brunswick), by Section 63 of the *Securities Act* (Nova Scotia), by Part II of the *Securities Act* (Prince Edward Island), by Part XIV of *The Securities Act* (Newfoundland and Labrador), by the *Securities Act* (Yukon Territory), by the *Securities Act* (Northwest Territories) and by the *Securities Act* (Nunavut) and the respective regulations under those acts. This prospectus, as required by the *Securities Act* (Québec) and the regulations under that act, does not contain any misrepresentation that is likely to affect the value or the market price of the securities to be distributed.

**KEYSTONE NORTH AMERICA INC.**

By: (Signed) ROBERT G. HORN
Chief Executive Officer

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

On behalf of the Board of Directors

By: (Signed) GEORGE SPERZEL
Director

By: (Signed) FRANK CERRONE
Director

**KEYSTONE NEWPORT ULC**

By: (Signed) ROBERT G. HORN
Chief Executive Officer

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

On behalf of the Board of Directors

By: (Signed) GEORGE SPERZEL
Director

By: (Signed) FRANK CERRONE
Director

The Promoter

**KEYSTONE GROUP HOLDINGS, INC.**

By: (Signed) ROBERT G. HORN
Chief Executive Officer

**The Credit Supporters**

**FOR EACH OF THE ENTITIES LISTED ON SCHEDULE "A" HERETO**

By: (Signed) ROBERT G. HORN

On behalf of the Board of Directors

By: (Signed) ROBERT G. HORN
President
(Acting as Chief Executive Officer)

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

**KEYSTONE AMERICA, INC.**

By: (Signed) STEVEN A. TIDWELL

By: (Signed) ROBERT G. HORN

On behalf of the Board of Directors

By: (Signed) ROBERT G. HORN
Chief Executive Officer

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

**KEYSTONE MICHIGAN, INC.**

By: (Signed) JAMES R. STARKS

On behalf of the Board of Directors

By: (Signed) ROBERT G. HORN
Chief Executive Officer

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

**NICKERSON BOURNE FUNERAL HOMES, INC.**

By: (Signed) JAMES D. PRICE

By: (Signed) STEVEN A. TIDWELL

On behalf of the Board of Directors

By: (Signed) ROBERT G. HORN
Chief Executive Officer

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

**MEMORIAL CHAPEL, INC.**

By: (Signed) ROBERT G. HORN

By: (Signed) STEVEN A. TIDWELL

On behalf of the Board of Directors

By: (Signed) ROBERT G. HORN
Chief Executive Officer

By: (Signed) STEPHEN M. SHAFFER
Chief Financial Officer

## SCHEDULE "A"

Keystone Advance Planning, Inc.

Keystone California, Inc.

Keystone Colorado, Inc.

Keystone Florida, Inc.

Keystone Illinois, Inc.

Keystone Indiana, Inc.

Keystone Iowa, Inc.

Keystone Kentucky, Inc.

Keystone Massachusetts, Inc.

Keystone Missouri, Inc.

Keystone New Hampshire, Inc.

Keystone New York, Inc.

Keystone North Carolina, Inc.

Keystone Ohio, Inc.

Keystone Tennessee, Inc.

Keystone Texas, Inc.

Keystone South Carolina, Inc.

Keystone Vermont, Inc.

Keystone Virginia, Inc.

Keystone Wisconsin, Inc.

Rice Funeral Homes, Inc.

Webb-Freer Funeral Homes, Inc.

Ker-Westerlund Funeral Home, Inc.

## CERTIFICATE OF THE UNDERWRITERS

Date: January 31, 2005

To the best of our knowledge, information and belief, the foregoing constitutes full, true and plain disclosure of all material facts relating to the securities offered by this prospectus as required by Part 9 of the *Securities Act* (British Columbia), by Part 9 of the *Securities Act* (Alberta), by Part XI of *The Securities Act* (Saskatchewan), by Part VII of the *Securities Act* (Manitoba), by Part XV of the *Securities Act* (Ontario), by Part 6 of the *Securities Act* (New Brunswick), by Section 64 of the *Securities Act* (Nova Scotia), by Part II of the *Securities Act* (Prince Edward Island), by Part XIV of the *Securities Act* (Newfoundland and Labrador), by the *Securities Act* (Yukon Territory), by the *Securities Act* (Northwest Territories) and by the *Securities Act* (Nunavut) and the respective regulations under those acts. To the best of our knowledge, this prospectus, as required by the *Securities Act* (Québec) and the regulations under that act, does not contain any misrepresentation that is likely to affect the value or the market price of the securities to be distributed.

**BMO NESBITT BURNS INC.**

By: (Signed) JEFFREY P. WATCHORN

**SCOTIA CAPITAL INC.**

By: (Signed) PETER L. SLAN

**CIBC WORLD MARKETS INC.**

By: (Signed) DANIEL J. MCCARTHY

**RBC DOMINION SECURITIES INC.**

By: (Signed) WILLIAM WONG

**NATIONAL BANK FINANCIAL INC.**

By: (Signed) MICHELLE FIEBIG

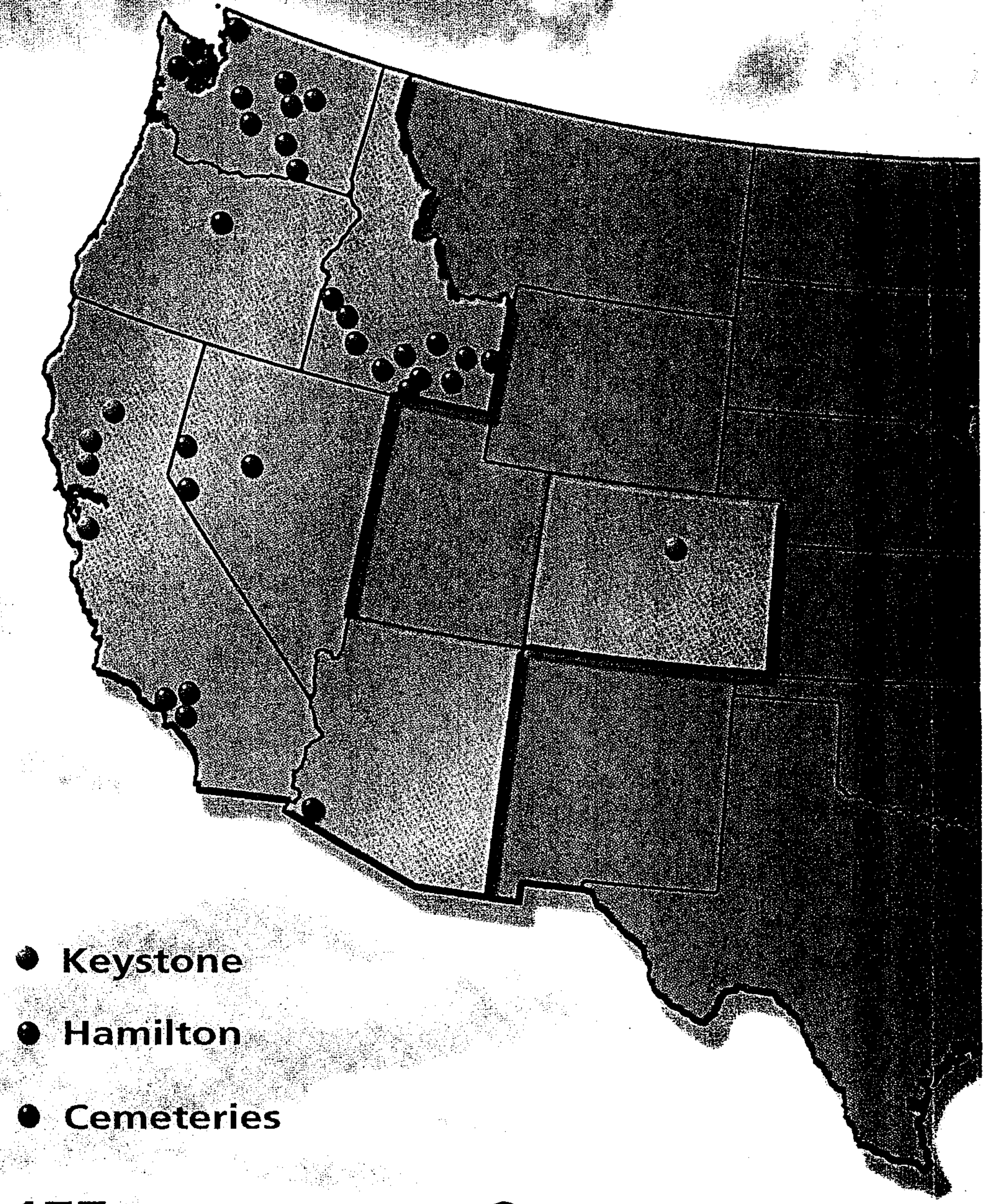
**TD SECURITIES INC.**

By: (Signed) STEVE DUMANSKI

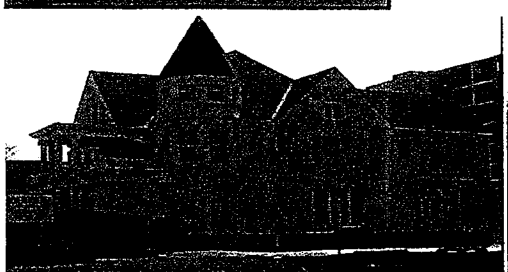
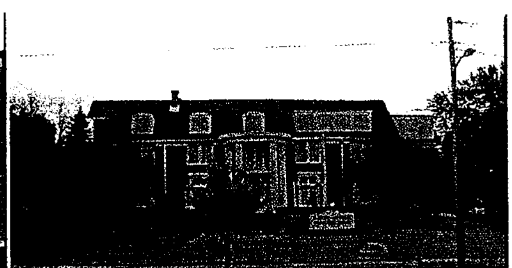





K E Y S T




**177** Funeral Homes • **9** Cemeteries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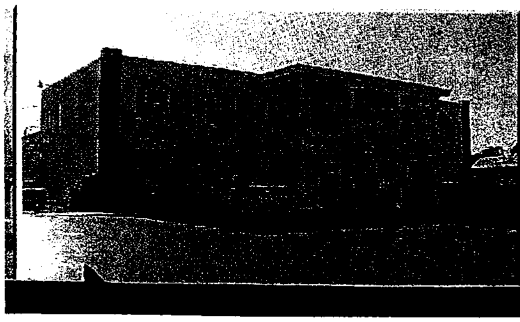

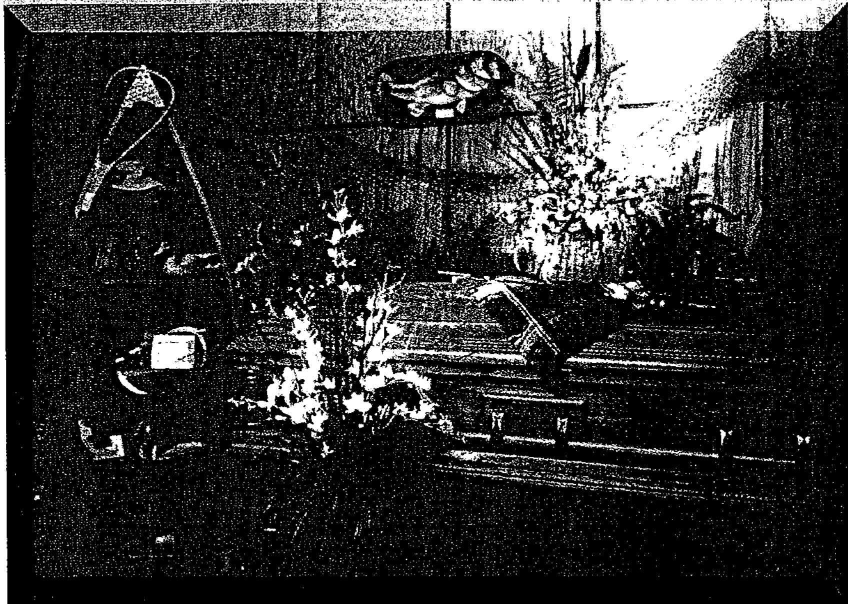

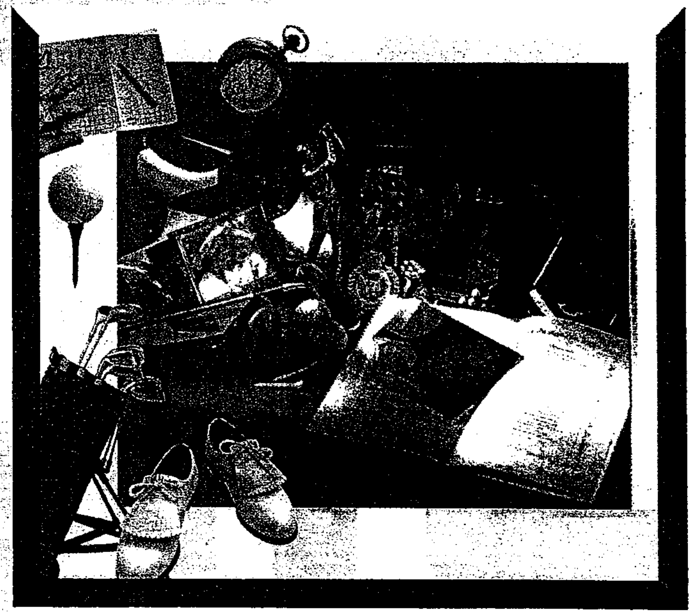

# Personalizing a Funeral Through Experiences, Service, and Merchandise

KEY Memories™

KEYSTONE

# EXHIBIT C

KEYSTONE

# KEYSTONE NORTH AMERICA INC.

# AUDITED FINANCIAL STATMENTS AND MANAGEMENT'S DISCUSSION AND ANALYSIS

# PERIOD FROM FEBRUARY 8, 2005 TO DECEMBER 31, 2005

KEYSTONE

# KEYSTONE NORTH AMERICA INC.

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

PERIOD FROM FEBRUARY 8, 2005 TO DECEMBER 31, 2005

*The following management discussion and analysis of the financial condition and results of operations of Keystone North America Inc. (the "Company") is supplemental to, and should be read in conjunction with the consolidated financial statements of the Company for the period ended December 31, 2005. The Company's financial statements are prepared in accordance with accounting principles generally accepted in Canada ("GAAP"). The information in this Management's Discussion and Analysis of the Financial Condition and Results of Operations is effective March 24, 2006. Substantially all of the Company's operating cash flows are in U.S. dollars, accordingly, all amounts presented herein are stated in U.S. dollars, unless indicated otherwise.*

## FORWARD LOOKING STATEMENTS

Certain statements in this management's discussion and analysis are "forward-looking statements", which reflect the expectations of management regarding the Company's future growth, results of operations, performance and business prospects and opportunities. These forward-looking statements reflect management's current reasonable expectations regarding future events and operating performance and speak only as of December 31, 2005. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not or the times at or by which such performance or results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements. Although the forward-looking statements contained in this management's discussion and analysis are based upon what management believes to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. These forward-looking statements are made as of the date of this Management Discussion and Analysis and, except as otherwise required by law, the Company assumes no obligation to update or revise them to reflect new events or circumstances.

## DEFINITION OF EBITDA AND DISTRIBUTABLE CASH

References to ''EBITDA'' are to earnings before interest, taxes, depreciation, amortization and certain other adjustments listed in the reconciliation table provided herein. References to "Distributable Cash" are to EBITDA, as adjusted for: capital expenditures, interest on the senior credit facility, interest on the separate subordinated notes, proceeds from debt, payments on debt, proceeds from investments, cash taxes and minority interest. EBITDA and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Distributable Cash may not be comparable to similar measures presented by other issuers. Management believes that EBITDA and Distributable Cash are important measures in evaluating the Company's performance. Distributable Cash is not intended to be representative of cash flow or results of operations determined in accordance with GAAP.

## PRESENTATION OF FINANCIAL INFORMATION

The Company began operations on February 8, 2005, the same day as the Company and Keystone Newport ULC ("Keystone ULC") completed an initial public offering of income participating securities ("IPSs"). The period ended December 31, 2005 (part of fiscal year 2005) includes three hundred twenty-seven days of operations, and there are no financial statements for the 2004 fiscal year for the Company that can be used on a comprehensive basis for comparing the current 327-day period operating results to the comparative period in the prior period. The comparison difficulty is compounded by the fact that at the time of the Company's initial public offering, it acquired two distinct businesses: Keystone Group Holdings, Inc. ("Keystone") and certain assets, liabilities and stock of certain subsidiaries of HFSC Holdings, Inc. ("Hamilton").

In order to enhance its usefulness, this management discussion and analysis includes a summary of the operating results of the Company for the 327-day period subsequent to the public offering of IPSs and for the period from January 1, 2005 through February 7, 2005 of Keystone and Hamilton on a pro forma combined basis to arrive at pro forma combined operating results for the year ended December 31, 2005. These pro forma combined results have been compared to the pro forma combined operating results of Keystone and Hamilton for the year ended December 31, 2004. Additionally, the operating results for the three-month period ended December 31, 2005 have been compared to the pro forma combined operating results of Keystone and Hamilton for the three-month period ended December 31, 2004. As the periods, or portions thereof, are prior to the purchase by the Company of Keystone and Hamilton, this information is provided for reference purposes only, and is not intended as a comprehensive comparison of financial results.

Readers are cautioned that as a result of the initial public offering, the operating results for periods prior to February 8, 2005 may not necessarily be indicative of the revenues and expenses that would have resulted had the Company operated on a combined basis during these periods.

**General**

The Company is the fifth largest provider of funeral services in the United States with 173 funeral homes and six cemeteries. The Company's funeral homes are located in 26 states primarily in the Midwest, Northeast, Southeast and Northwest regions of the continental United States.

The funeral and cemetery industry in the United States generates an estimated $15 billion in total revenues annually. The primary market drivers of the funeral industry are local heritage, the total mortality of a local service area and the mix of business between cremation and burial.

The Company's funeral homes have historically provided a full range of funeral services on both an at-need (at time of death) and preneed basis (prior to death). These services include removal of human remains, planning and coordinating personalized funerals and cremations, professional embalming, use of our funeral home facilities, merchandise sales, conducting memorial services, performing cremation and cemetery interment services.

Corporate, general and administrative expenses primarily include costs associated with Keystone's corporate office in Tampa, Florida. As the Company continues to implement its business and growth strategies, it expects that there will be a modest increase in the Company's general and administrative expenses. However, because these expense increases will be incurred in connection with an increase in its revenue base, the Company anticipates that the expense increases will be relatively smaller, as a percentage of revenues, as it realizes economies of scale and the costs are spread over a larger revenue base.

Income from operations for the pro forma combined year ended December 31, 2005 and for the three months ended December 31, 2005 exceeded the results for the same period on a pro forma combined basis for the prior year. Higher income from operations for the year was principally the result of higher volume of funeral services performed and increased average revenue per funeral. Higher income for the final three months of 2005 was higher due to increased averages despite performing fewer services compared the same period on a pro forma combined basis for the prior year.

The Company posted a net loss for the fourth quarter of $0.9 million and net income for the 327-day period ending December 31, 2005 of $3.1 million. The net loss for the fourth quarter includes and unrealized loss on foreign currency exchange contracts of $0.8 million and the net income for the 327-day period ending December 31, 2005 includes an unrealized gain on foreign currency exchange contracts of $4.6 million, representing the change in market value of those contracts for the period. The Company does not intend to liquidate the foreign exchange contracts, as it would expose future distributions to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar. The change in market value of the foreign currency exchange contracts does not impact the cash flows of the Company or the ability of the Company to make cash distributions. It is management's intention to continue to roll forward these contracts on a quarterly basis as they expire; however, such extensions will be at the discretion of the board of directors.

Management remains confident of the Company's business model and ability to meet the anticipated annual distribution target of C$1.00 per IPS.

There is a seasonal component to the operation of a funeral business. Case volume, revenue and, as a result, cash flows are typically higher in the first and fourth quarters. To illustrate the significance of the seasonal component to our business, we have provided the following pro forma combined seasonal data for the past five years:

**Percentage of Annual EBITDA generated by Quarter**
**Pro Forma Combined before consideration of Corporate, General and Administrative Expenses**

| Trailing Twelve Months Ended | Q1 | Q2 | Q3 | Q4 | Q2 & Q3 | Q1 &Q4 |
|---|---|---|---|---|---|---|
| December 31, 2001 | 28.0% | 24.6% | 21.2% | 26.2% | 45.8% | 54.2% |
| December 31, 2002 | 30.4% | 23.2% | 21.8% | 24.6% | 45.0% | 55.0% |
| December 31, 2003 | 27.0% | 24.0% | 21.6% | 27.4% | 45.6% | 54.4% |
| December 31, 2004 | 30.6% | 21.3% | 23.1% | 25.0% | 44.4% | 55.6% |
| December 31, 2005 | 31.7% | 22.4% | 20.5% | 25.4% | 42.9% | 57.1% |
| **Five Year Average** | **29.5%** | **23.1%** | **21.6%** | **25.8%** | **44.7%** | **55.3%** |

As demonstrated in the table above, the funeral homes during the second and third quarters generate, on average, approximately 11% less EBITDA than the first and fourth quarters due to decreased case volume. Given that Keystone North America commenced operations in February of 2005, our year to date operations do not include results from the period January 1, 2005 to February 7, 2005 which is historically our strongest seasonal period.

**Results of Operations (in 000's of US$, except per share data and where the context requires)**

| | Three Months Ended December 31, | | Year Ended December 31, | | | |
|---|---|---|---|---|---|---|
| | Actual 2005 | Pro forma Combined 2004 (Note 1) | Actual 327 Days 2/8/05-12/31/05 | Pro forma Combined 38 Days 1/1/05-2/7/05 (Note 1) | Pro forma Combined 2005 (Note 1) | Pro forma Combined 2004 (Note 1) |
| Revenues | $21,619 | $20,624 | $76,527 | $9,848 | $86,376 | $81,588 |
| Costs and expenses | | | | | | |
| Costs and expenses | 14,133 | 13,378 | 49,952 | 6,318 | 56,271 | 53,341 |
| Corporate, general and administrative | 1,777 | 1,617 | 5,482 | 653 | 6,135 | 6,280 |
| Depreciation | 682 | 857 | 2,387 | 366 | 2,753 | 3,730 |
| Amortization and other | 773 | 1,300 | 2,898 | 301 | 3,199 | 4,113 |
| Total operating expenses | 17,365 | 17,152 | 60,719 | 7,638 | 68,358 | 67,464 |
| Income from operations | 4,254 | $3,472 | 15,808 | $2,210 | $18,018 | $14,124 |
| Interest expense | 4,096 | | 14,259 | | | |
| Unrealized gain (loss) on foreign currency exchange contracts | (758) | | 4,627 | | | |
| Other income | 400 | | 736 | | | |
| Income (loss) from continuing operations before income taxes and minority interest | (200) | | 6,912 | | | |
| Income tax expense | 209 | | 3,032 | | | |
| Minority interest | 527 | | 797 | | | |
| Income from continuing operations | (936) | | 3,083 | | | |
| Income from discontinued operations | 57 | | 55 | | | |
| Net income (loss) | $(879) | | $3,138 | | | |
| Basic and diluted income (loss) from continuing operations | $ (0.05) | | $ 0.16 | | | |
| Basic and diluted income from discontinued operations | $ 0.00 | | $ 0.00 | | | |
| Basic and diluted income (loss) per share | $ (0.05) | | $ 0.17 | | | |

*Note 1: Results for all periods prior to February 8, 2005 are based on combined, pro forma same funeral home operating results as presented in internally prepared financial statements for Keystone and Hamilton. These amounts do not include pro forma adjustments for the change in treatment of consulting and non-compete payments expensed in the Hamilton historical financial statements.*

**Distributable Cash Summary (in 000's of US$, except per share data and where the context requires)**

| | Period Ended December 31, 2005 | |
|---|---|---|
| | 3 Months | 327 Days |
| Net income (loss) | $(879) | $3,138 |
| Plus: | | |
| Depreciation | 682 | 2,387 |
| Amortization | 773 | 2,898 |
| Interest expense | 4,096 | 14,259 |
| Unrealized loss (gain) on foreign currency exchange contracts | 758 | (4,627) |
| Income tax expense | 209 | 3,032 |
| Minority interest | 527 | 797 |
| Loss (gain) from disposals | (78) | 196 |
| Discontinued Operations EBITDA adjustments | 90 | 218 |
| **EBITDA** (Note 2) | **$6,178** | **$22,298** |
| Less: | | |
| Capital expenditures of property and equipment | 810 | 2,223 |
| Proceeds from debt | (179) | (222) |
| Payments on long term debt | 922 | 4,272 |
| Proceeds from investments | (1,012) | (4,801) |
| Interest on other loans | 187 | 561 |
| Interest on senior credit facility | 783 | 2,790 |
| Interest on separate subordinated notes | 309 | 1,075 |
| Minority interest distributions | 363 | 945 |
| Cash taxes | 78 | 821 |
| **Distributable cash** (Notes 2 and 3) | **$3,917** | **$14,634** |
| **Per IPS unit** | **$ 0.21** | **$ 0.78** |
| | | |
| Interest accrued on IPS distributions | 2,486 | 8,661 |
| Declared dividends on IPS distributions | 1,509 | 5,252 |
| **Total IPS distributions** | **$3,995** | **$13,913** |
| **Per IPS unit** | **$ 0.21** | **$ 0.74** |

*Note 2- EBITDA and Distributable Cash are not recognized measures under generally accepted accounting principals ("GAAP") and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Distributable Cash may not be comparable to similar measures presented by other issuers. Keystone intends to distribute substantially all of its cash on an ongoing basis, management believes that EBITDA and Distributable Cash are important measures in evaluating Keystone's performance. Distributable Cash is not intended to be representative of cash flow or results of operations determined in accordance with GAAP. Management believes that Distributable Cash is a useful financial measure as it provides investors with an indication of cash available for distribution and is a measure generally used by Canadian income funds as an indicator of financial performance. Keystone's method of determining distributable cash is derived from EBITDA, which in turn is derived from net earnings, a measure recognized under GAAP.*

*Note 3- **Reconciliation of cash from operating activities to distributable cash:***

| | Period Ended December 31, 2005 | |
|---|---|---|
| | 3 Months | 327 Days |
| **Cash from operating activities** | **$1,793** | **$10,225** |
| Capital expenditures of property and equipment | (810) | (2,223) |
| Proceeds from debt | 179 | 222 |
| Payments on long term debt | (922) | (4,272) |
| Proceeds from investments | 1,012 | 4,801 |
| Current tax expense | 1,140 | 188 |
| Non-cash interest expense | 333 | 1,177 |
| Class B distributions declared | (363) | (945) |
| Changes in working capital | (853) | (2,379) |
| IPS unit interest | 2,486 | 8,661 |
| Cash taxes | (78) | (821) |
| **Distributable cash** | **$3,917** | **$14,634** |

***327 Days Ended December 31, 2005***

For the 327 days ended December 31, 2005, revenue totaled $76.5 million. Cost and expenses totaled $50.0 million or 65.3% of revenues; corporate, general and administrative expenses totaled $5.5 million or 7.2% of revenues; and depreciation and amortization totaled $5.3 million. Interest expense totaled $14.3 million and unrealized gain on foreign currency exchange contracts totaled $4.6 million for the 327-day period. Income tax expense totaled $3.0 million. Minority interest was $0.8 million. The Company also recorded a gain on discontinued operations of $0.1 million.

The unrealized gain on foreign currency exchange contracts of $4.6 million relates to changes in the fair value of the outstanding foreign currency exchange contracts. The Company does not intend to liquidate the foreign exchange contracts, as it would expose future distributions to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar. The change in market value of on the foreign currency exchange contracts does not impact the cash flows of the Company or the ability of the Company to make cash distributions.

In 2005, the Company disposed of three funeral homes and three cemeteries for net cash proceeds of $3.2 million. Summarized operating results for the period are as follows:

| | 327 Day Period ended December 31, 2005 |
|---|---|
| Revenues | $ 2,272 |
| Costs and expenses | 1,954 |
| Gross profit | 318 |
| Depreciation | 84 |
| Amortization | 81 |
| Interest expense | 4 |
| Other income | (62) |
| Income tax expense | 92 |
| Minority interest | 4 |
| Income on discontinued operations | 115 |
| Loss on disposal of discontinued operations | 60 |
| Net income from discontinued operations | $ 55 |

Total assets and liabilities disposed were $8.8 million and $5.5 million respectively. Goodwill disposed of for all dispositions was a combined $0.9 million.

Distributable Cash for the 327-day period ending December 31, 2005 was $14.6 million or $0.78 per unit, which exceeded distributions declared in respect of this period by $0.7 million. The excess Distributable Cash was directly related to the higher volume of funeral services performed and increased average revenue per case in the 327-day period ending December 31, 2005 offset by related variable expenses. Excess Distributable Cash was also due to reduced maintenance capital expenditure rates for the period in comparison to management's anticipated annual level of $2.9 million. As indicated in the seasonality discussion above, funeral home operations for the second and third quarters typically generate approximately 11% less EBITDA for the company than during the first and fourth quarters. As the company commenced operations in February, the majority of our 327 days of operation have been during the seasonally slower quarters.

The Company's monthly distribution rate of C$0.08333333 per IPS unit was established at the time of its IPS Offering and was, in large part, based upon the historical results for Keystone and Hamilton (adjusted for certain factors in connection with the change in capital structure, additional expense as a result of becoming a reporting issuer, and synergies anticipated from the business combination). At this time, the Company has not identified any reason to adjust the monthly distribution rate or the assumptions utilized in developing that distribution rate.

***Comparison of the three month period ended December 31, 2005 to the pro forma combined results for the three month period ended December 31, 2004***

*Revenues:* Revenues for the fourth quarter of fiscal year 2005 were $21.6 million, compared to pro forma combined revenues of $20.6 million for the fourth quarter of fiscal year 2004, representing an increase of $1.0 million, or 4.8%. The primary driver of this increased revenue was the increasing the average revenue per funeral service approximately $196, a 4.1% increase, offset slightly by performing 28 less funeral services in 2005 as compared to the same period in 2004, a 0.7% decrease.

*Cost and expenses:* Cost and expenses for the fourth quarter of fiscal 2005 were $14.1 million or 65.4% of revenues, compared to $13.4 million or 64.9% of revenues, for the pro forma combined fourth quarter of 2004, an increase of $0.8 million or 5.6%. This increase was primarily related to increases in labor costs over the prior period associated with cost of living increases, health benefits and year end bonuses.

The principal elements of the cost and expenses include salaries and wages and direct costs of goods sold. These two significant categories comprise 32% and 13% of fourth quarter 2005 revenues, respectively. These categories historically represent approximately the same percentage of revenues over time.

The funeral service industry is subject to seasonal variations in deaths with historically higher revenues and cash flows in the winter months. The fourth quarter of the year has traditionally been the second strongest period of the year for the company. On a trailing twelve-month basis, the seasonal impact for the fourth quarter was consistent with historical patterns discussed earlier.

*Corporate, general and administrative expense:* Corporate, general and administrative expense was $1.8 million for the fourth quarter of 2005 which compares to $1.6 million for the pro forma combined fourth quarter of 2004. The increase relates to additional performance based bonus expense recorded in the fourth quarter of 2005.

*Depreciation expense:* Depreciation expense for the fourth quarter of fiscal year 2005 was $0.7 million compared to $0.9 million for the pro forma combined fourth quarter of fiscal year 2004, a decrease of $0.2 million related directly to the impact of the valuation of assets and useful lives in purchase accounting.

*Amortization and other expense:* Amortization and other expense was $0.8 million for the fourth quarter of 2005 compared to $1.3 million for the pro forma combined fourth quarter of fiscal year 2004, a decrease of $0.5 million. Amortization expense represents the amortization of trade names and covenants not to compete related to the acquisition of Keystone and Hamilton. In connection with these acquisitions, these intangible assets were valued at fair value and are being amortized over their estimated useful lives.

*Income from operations:* Income from operations was $4.3 million for the fourth quarter compared to income from operations of $3.5 million for the pro forma combined fourth quarter of fiscal year 2004, an increase of $0.8 million due primarily to the net effect of items noted above.

***Comparison of the pro forma combined results for the year ended December 31, 2005 to the pro forma combined results for the year ended December 31, 2004***

*Revenues:* Pro forma combined revenues for 2005 were $86.4 million, compared to $81.6 million for the pro forma combined year 2004, representing an increase of $4.8 million or 5.9%. The primary driver of this increased revenue was the performance of 492 additional funeral services in 2005 as compared to the same period in 2004, a 3.0% increase. Additionally, average revenue per funeral service increased by approximately $84 per service or 1.8% from 2004 to 2005.

*Cost and expenses:* Cost and expenses for the pro forma combined year 2005 was $56.3 million or 65.1% of revenues, compared to $53.3 million or 65.4% of revenues, for the pro forma combined year 2004, an increase of $2.9 million or 5.5%. This increase was primarily related to additional cost of sales and labor costs directly related to the increased service volume in 2005. The decrease of cost and expenses as a percentage of revenues reflects the relatively fixed nature of the cost of operations in comparison to the increased revenues generated from additional case volume, which increased operating margins disproportionately.

The principal elements of the cost and expenses include salaries and wages and direct costs of goods sold. These two significant categories comprise 32% and 14% of 2005 revenues respectively. These categories represent approximately the same percentage of revenues over time.

*Corporate, general and administrative expense:* Corporate, general and administrative expense for the pro forma combined year 2005 was $6.1 million compared to $6.3 million for the pro forma combined year 2004, a decrease of $0.1 million or 2.3%. The decrease is primarily attributable to corporate general and administrative savings resulting from the combination of Keystone and Hamilton for the period after the combination offset by the additional costs of operating as a public company.

*Depreciation expense:* Depreciation expense for the pro forma combined year 2005 was $2.8 million compared to $3.7 million for the pro forma combined year 2004, a decrease of $1.0 million related directly to the impact of the valuation of assets and useful lives in purchase accounting.

*Amortization and other expense:* Amortization and other expense for the pro forma combined year 2005 was $3.2 million compared to $4.1 million for the pro forma combined year 2004, a decrease of $0.9 million. Amortization expense represents the amortization of trade names and covenants not to compete related to the acquisition of Keystone and Hamilton. In connection with these acquisitions, these intangible assets were valued at fair value and are being amortized over their estimated useful lives.

*Income from operations:* Income from operations was $18.0 million for the pro forma combined year 2005 compared to income from operations of $14.1 million for the pro forma combined year 2004, an increase of $3.9 million due primarily to the net effect of items noted above.

**Outstanding Share Data**

At December 31, 2005, the Company had 18,768,017 IPSs outstanding. Each IPS represents one Common Share of the Company, and C$4.286 principal amount of 14.5% Subordinated Notes.

**Liquidity and Capital Resources**

The Company completed the IPS Offering on February 8, 2005 through the issuance of 17,100,000 IPSs for net proceeds of $71.4 million related to the Common Share portion of the IPSs, and $59.7 million related to the Subordinated Notes portion of the IPSs. In addition, upon closing of the IPS Offering, Keystone ULC issued $8.0 million (C$10.0 million) of Subordinated Notes on a private placement basis (the "Separate Subordinated Notes") and a subsidiary of the Company borrowed $43.1 million under the new credit agreement (the "Credit Agreement"). The Company incurred $8.2 million in deferred financing costs related to the issuance of this debt. The Company used the net proceeds from the IPS Offering to purchase an 85.3% interest in Keystone.

On February 17, 2005, the underwriters of the IPS Offering exercised an over-allotment option granted in connection with the IPS Offering. As part of the exercise of the over-allotment option, the Issuer completed a subsequent issuance of 1,668,017 IPSs for net proceeds of $8.9 million (C$10.9 million). The net proceeds from this subsequent issuance were used to purchase additional Class A common shares and preferred shares of Keystone. Keystone in turn used such amounts to purchase all of its Class C common shares. Upon the purchase of all of the Class C common shares, the Company's ownership percentage in Keystone increased to 93.7%, resulting in a reduction of minority interest from the issuance of additional IPS units.

During the 327-day period ended December 31, 2005, the Company generated $10.2 million in cash flow from operations.

At December 31, 2005, debt under the Credit Agreement was $43.1 million, with $15.0 million in borrowings available for acquisitions and working capital purposes under the revolving credit facility. There were no amounts drawn or outstanding on the revolving credit facility at December 31, 2005. In addition, at December 31, 2005, outstanding debt included $12.4 million in obligations to former owners and equipment financing, and $77.6 million in Subordinated Notes and Separate Subordinated Notes. The Credit Agreement has a maturity date of February 8, 2008, while the Subordinated Notes and Separate Subordinated Notes have a 12-year term and are due and payable on February 8, 2017. The obligations due to former owners have various maturity dates through the fiscal year 2018.

The Company determines its dividend declarations, which it intends to pay in equal monthly amounts, based on periodic reviews of its estimated annual earnings and related estimated annual cash flows. The Company expects to remain in a position to continue distributions of C$0.08333333 per IPS per month. A portion of that distribution represents interest on the Subordinated Notes with the remainder representing a dividend on the Common Shares.

The Company intends to selectively acquire funeral homes to the extent that it is able to finance these from available financing under the Credit Agreement, proceeds reinvested from dispositions, and the potential additional issuance of IPSs.

**Commitments and Contractual Obligations**

Contractual obligations and commitments principally include obligations associated with outstanding indebtedness and lease obligations. The following table shows contractual obligations and commitments related to outstanding indebtedness as of December 31, 2005 and the related payment by period due.

Maturities of long-term debt are as follows (in 000's):

| | December 31, 2005 Balance | Year Ending December 31, 2006 | 2007 | 2008 | 2009 | 2010 | Thereafter |
|---|---|---|---|---|---|---|---|
| Term Loan Facility | $ 43,100 | $ - | $ - | $43,100 | $ - | $ - | $ - |
| Equipment Financing | 562 | 189 | 161 | 102 | 77 | 33 | - |
| Due to Former Owners and Employees | 11,863 | 3,302 | 3,061 | 2,482 | 1,231 | 428 | 1,359 |
| Subordinated Debt | 77,571 | - | - | - | - | - | 77,571 |
| | $ 133,096 | $ 3,491 | $3,222 | $45,684 | $ 1,308 | $ 461 | $ 78,930 |

The Company expects to be able to renew or refinance the various loan facilities as they become due at then current market rates.

Capital expenditures were $2.2 million for the 327-day period ended December 31, 2005 and $0.8 million for the three-month period ended December 31, 2005. Capital expenditures include those required to maintain and upgrade existing infrastructure, including the replacement of furnishings, autos and routine maintenance to existing building structures and the surrounding landscape. Management anticipates an annual capital expenditure level of $2.9 million.

The Company has no off-balance sheet debt or similar obligations. The Company has arrangements under which customers purchase insurance policies, which are assigned to the Company at the time of death. The Company does not have control of these policies and is obligated to deliver services at a fixed price only if the insurance policy proceeds are delivered. Approximate proceeds due from third party insurers $136.3 million at December 31, 2005 were which represent both future assets and obligations of the Company.

The Company leases certain facilities, vehicles and other equipment under operating leases. Rent expense was $2.3 million for the period from February 8, 2005 to December 31, 2005.

The following represents the future minimum lease payments under the operating leases:

| | |
|---|---|
| Year ending December 31: | |
| 2006 | $2,203 |
| 2007 | 1,859 |
| 2008 | 1,479 |
| 2009 | 920 |
| 2010 | 548 |
| Thereafter | 1,665 |
| | $13,173 |

**Quantitative and Qualitative Disclosures About Market Risk**

In the normal course of business, the Company is exposed to market risks arising from adverse changes in interest rates and the C$/US$ foreign currency exchange rate. Market risk is defined for these purposes as the potential change in the fair market value of financial assets and liabilities resulting from an adverse movement in these rates.

As of December 31, 2005 the Company's material variable rate borrowings included outstanding borrowings under the Credit Agreement. At inception of the Credit Agreement, the Company put in place interest rate cap agreements. The notional amount of the interest rate cap agreement equals the outstanding term loan and, in accordance with the terms of the interest rate cap agreement, limits the interest rate on the outstanding term loan amount. As of December 31, 2005 the Company had $43.1 million in outstanding indebtedness related to the term loan facility. Without considering the effect of the interest rate cap, a 100 basis point increase in interest rates, applied to these borrowings as of December 31, 2005, would result in an annual increase in interest expense and a corresponding reduction in cash flow of approximately $0.4 million.

The Company is exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar because the anticipated distributions from Keystone to the Company and Keystone

ULC will be paid in U.S. dollars and the anticipated distributions on the IPSs and Separate Subordinated Notes will be paid in Canadian dollars. In order to minimize the impact of fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar, the Company has entered into Canadian dollar/U.S. dollar exchange contracts for the total amount of anticipated IPS distributions and Separate Subordinated Note interest. The agreements consist of monthly forward foreign exchange contracts. Under the terms of the contracts, the Company is required to deliver approximately $1.4 million U.S. dollars on or around the 14th day of each month in exchange for approximately $1.7 million Canadian dollars. It is management's intention to continue to roll forward these contracts on a quarterly basis as they expire; however, such extensions will be at the discretion of the board of directors.

As of December 31, 2005, the following contracts remain open:

- 50 contracts through February 2010 at $1.2272 Canadian dollar/U.S. dollar,
- 3 contracts from March 2010 through May 2010 at $1.2225 Canadian dollar/U.S. dollar,
- 3 contracts from June 2010 through August 2010 at $1.1570 Canadian dollar/U.S. dollar,
- 3 contracts from September 2010 through November 2010 at $1.1330 Canadian dollar/U.S. dollar, and
- 3 contracts from December 2010 through February 2011 at $1.1202 Canadian dollar/U.S. dollar.

At December 31, 2005, the Company had unrealized gains on the open forward currency exchange contracts totaling $4.6 million. If the Company had liquidated the contracts and realized a gain, it would be exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar with respect to distributions on the IPSs. Such fluctuations in foreign currency exchange contracts have no impact on current cash flows of the Company or evaluation of the Company's distributions given the long-term maturity horizon of those obligations.

**Summary of Quarterly Results**

| | 1st Quarter 2005 | 2nd Quarter 2005 | 3rd Quarter 2005 | 4th Quarter 2005 | Period from 2/8/05 to 12/31/05 |
|---|---|---|---|---|---|
| **Revenues** | **$14,017** | **$20,785** | **$20,106** | **$21,619** | **$76,527** |
| **Net income (loss)** | **2,433** | **(354)** | **1,939** | **(879)** | **3,138** |
| **Net income (loss) per share** | **0.13** | **(0.02)** | **0.10** | **(0.05)** | **0.17** |

**Critical Accounting Estimates**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Some of the estimates and assumptions management is required to make relate to matters that are inherently uncertain as they pertain to future events. Management bases these estimates on historical experience and on various other assumptions that it believes to be reasonable and appropriate. Actual results may differ significantly from these estimates. The following is a description of the Company's accounting policies that management believes require subjective and complex judgments, and could potentially have a material effect on reported financial condition and results of operations.

*Concentration of Credit Risk*
The Company grants customers credit in the normal course of business. Procedures exist to secure accounts and include confirming a source of third-party payment such as insurance assignment, estate, group life policy or maturing preneed trust. To date, bad debts have not been significant in relation to the volume of revenues. The Company charges interest on past due receivables in certain circumstances.

Preneed funeral contracts do not subject the Company to significant collection risk because contracts may be cancelled due to nonpayment before services are rendered. Preneed funeral contracts that the customer funds by purchasing insurance-funded contracts are subject to supervision by state insurance departments and are protected in the majority of states by insurance guarantee acts.

*Preneed Funeral Accounting*
The Company sells preneed funeral services, whereby a customer contractually agrees to the terms of a funeral to be performed in the future. The Company sells these price-guaranteed, prearranged funeral contracts through various programs providing for future funeral services at prices prevailing when the agreement is signed. Preneed funeral contracts are generally funded either through trusts established by the customer or through life insurance policies purchased by the customer and issued by third party insurers. The Company, in accordance with certain state laws, may retain a portion of the payments on preneed contracts funded through trust. The Company records costs as incurred.

Amounts paid by the customer pursuant to the preneed funeral contracts are recognized as funeral service revenue at the time the funeral is performed. Trust earnings and increasing insurance benefits are recognized as funeral service revenues when the funeral service is performed and are intended to protect the margin associated with providing a price-guaranteed funeral service in the future.

Preneed receivables and funds consist of receivables from customers, trusts or other, non-insurance accounts that will be received upon delivery of preneed merchandise and services. Preneed funeral contracts funded through life insurance policies purchased by the customer and issued by third party insurers are not reflected as assets or liabilities in the financial statements.

The preneed receivables and funds are recorded at cost, less provisions for loss in respect of individual investments where market value is below cost and this decline appears to be other than temporary.

Amounts held in trust are refunded to the customer according to state law upon cancellation of the contract.

*Property and Equipment*
Property and equipment is recorded at cost or at fair value if obtained as part of a business acquisition, less accumulated depreciation. Ordinary maintenance and repairs are expensed as costs are incurred. Depreciation on property and equipment is computed on the straight-line basis

over the estimated useful lives of the assets, which range from 5 to 40 years. Leasehold improvements are amortized over the shorter of the lease term or the estimated useful lives of the assets. In conjunction with the acquisition of Keystone and Hamilton, management engaged an independent third party valuation firm to value the building and land values and has revalued property and equipment to market value in conjunction with recording the acquisition under the purchase method.

*Goodwill and Other Identifiable Intangibles*
Goodwill represents the excess of cost over fair value of net assets acquired in business combinations accounted for under the purchase method. Other identifiable intangible assets consist of covenants not to compete and tradenames. Covenants not to compete represent the value of non-competition agreements with certain key management personnel of acquired funeral operations. Amortization of such covenants not to compete is provided on a straight-line basis over the term of the agreements. Tradenames represent the value assigned to the acquired business names under which the entities do business.

*Impairment of Long-Lived Assets*
Management continually evaluates whether events or circumstances have occurred that indicate that the remaining estimated useful lives of property and equipment may warrant revision or that the remaining balances may not be recoverable. If this review indicates that the assets will not be recoverable, as determined based on the undiscounted future cash flows from the use of the assets, the carrying value of the assets are reduced to their estimated fair value.

*Income Taxes*
Income taxes have been computed utilizing the liability approach. Future income tax assets and liabilities arise from differences between the tax basis of an asset or liability and its reported amount in the financial statements. Future tax balances are determined by using tax rates expected to be in effect when the taxes will actually be paid or refunds received. A valuation allowance is recorded when the expected recognition of a future tax income asset is not considered to be more likely than not. The recorded future income tax liability results from a difference between the book and tax basis of certain assets.

*Accounting for Derivatives and Hedging Activities*
Derivative financial instruments are utilized by the Company in the management of its foreign currency and interest rate exposures. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows or hedged items.

The Company accounts for its interest rate cap and interest rate collar on an accrual basis whereby interest payable and interest expense under the Credit Agreement is limited to 6.95%. The interest rate collar is not effective until 2006. The interest rate cap and interest rate collar agreements require the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based.

Derivatives that are not designated hedges for accounting purposes, such as the foreign currency exchange contracts, are recorded at fair value on the balance sheet. Changes in fair value are recorded in the statement of operations.

**Disclosure controls and procedures**

Under the supervision and participation of our management, including the chief executive officer and the chief financial officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings) as of December 31, 2005. Based on that evaluation, the chief executive officer and the chief financial officer concluded that the Company's disclosure controls and procedures are effective in making known to them material information relating to the Company required to be disclosed in our reports filed or submitted under the Multilateral Instrument.

**Risk Factors**

**Risks Related to the Business**

***Declines in the number of deaths in our markets can cause a decrease in revenue and margins. Changes in the number of deaths are difficult to predict from market to market over the short term.***

Declines in the number of deaths could cause at-need sales of funeral and cemetery services, property and merchandise to decline, which could decrease revenue and margins. Although the United States Census Bureau estimates that the number of deaths in the United States will increase, longer lifespans could reduce the rate of deaths. If the number of deaths declines, the number of funeral services and interments performed by us will decrease and our financial condition, results of operations and our future cash flows may be materially adversely affected. In addition, changes in the number of deaths can vary among local markets and from quarter to quarter, and variations in the number of deaths in our markets or from quarter to quarter are not predictable. However, generally the number of deaths fluctuates with the seasons with more deaths occurring during the winter months primarily resulting from pneumonia and influenza. These variations can cause revenue to fluctuate over short periods of time.

***Our high fixed cost base makes us vulnerable to fluctuations in revenue.***

Companies in the funeral home and cemetery business must incur many of the costs of operating and maintaining facilities, land and equipment regardless of the level of sales in any given period. For example, we must pay salaries, utilities, property taxes, insurance and maintenance costs on funeral homes regardless of the number of funeral services or interments performed. Because we cannot decrease these costs significantly or rapidly when we experience declines in sales, declines in sales can cause margins, profits and cash flow to decline at a greater rate than the decline in revenue.

***The increasing number of cremations in the United States could cause revenue to decline because basic cremations generally produce lesser funeral revenue and limited revenue for cemetery operations.***

Our traditional cemetery and funeral service operations face the challenge of the increasing number of cremations in the United States. Industry studies indicate that the percentage of cremations has steadily increased and that cremations will represent approximately 36 percent of the United States burial market by the year 2010, compared to 27 percent in 2001. While we have focused our efforts on providing cremation with services, cremations without services usually result in lower total revenue and gross profit dollars than traditional services. A substantial increase in the rate of cremations without services that we perform could have a material adverse effect on our financial condition, results of operations and cash flows.

***If we are not able to respond effectively to changing consumer preferences, our market share, revenue and profitability could decrease.***
Future market share, revenue and profit will depend in part on our ability to anticipate, identify and respond to changing consumer preferences. Although we continually monitor consumer preferences, we may not correctly anticipate or identify trends in consumer preferences, or we may identify them later than our competitors do. In addition, any strategies we may implement to address these trends may prove incorrect or ineffective, which could have a material adverse effect on our financial condition, results of operations and cash flows.

***Increase in price competition in the funeral home and cemetery markets in which we operate could reduce our market share or cause us to reduce prices to retain or recapture market share, either of which could reduce our revenue and margins.***
To compete successfully, our funeral service locations and cemeteries must maintain good reputations and high professional standards in the industry, as well as offer attractive products and services at competitive prices. In a few markets, we have experienced price competition primarily from family run funeral home and cemetery operators, and from monument dealers, casket retailers, low cost funeral providers and other non-traditional providers of services or product. Recently, certain retailers and discounters have experimented with casket sales. From time to time, competition has resulted in losing market share in some markets. In other markets, we have had to reduce prices to retain or recapture market share. If we are unable to successfully compete, our company, our financial condition, results of operations and cash flows could be materially adversely affected.

***We require access to capital resources to successfully acquire businesses and further issuances of securities could result in dilution.***
Our growth strategies include the acquisition of additional funeral homes. Any such acquisitions will require additional capital that may be funded through additional debt or equity financings. To the extent that financing is raised through the issuance of IPSs or other securities of the Issuer, current holders of IPSs may experience ownership dilution. To the extent debt is incurred, either the Issuer or the Company may incur significant interest expense and may be subject to covenants in the related debt agreements that affect the conduct of business. Without sufficient capital resources to implement this strategy, our future growth could be limited and operations impaired. There can be no assurance that additional financing will be available to fund our growth strategies or that, if available, the financing will be on terms that are acceptable to the Company and the Issuer.

***Increasing insurance benefits related to preneed funeral contracts funded through life insurance or annuity contracts may not cover future increases in the cost of providing a price guaranteed funeral service.***
We sell price guaranteed preneed funeral contracts through various programs providing for future funeral services at prices prevailing when the agreements are signed. For preneed funeral contracts funded through life insurance or annuity contracts, there is no guarantee that the increasing insurance benefit will protect the margin associated with providing a price-guaranteed funeral service in the future, which could materially adversely affect our financial condition, results of operations and cash flows.

***Earnings from and principal of trust funds and escrow accounts could be reduced by changes in stock and bond prices and interest and dividend rates or by a decline in the size of the funds.***
We maintain three types of trust funds and escrow accounts: (1) preneed funeral merchandise and services, (2) preneed cemetery merchandise and services and (3) perpetual care. Earnings and investment gains and losses on trust funds and escrow accounts are affected by financial market conditions that are not within our control. Earnings are also affected by the mix of fixed-income and equity securities that we choose to maintain in the funds, and we may not choose the optimal mix for any particular market condition. The size of the funds depends upon the level of preneed sales and maturities, the amount of ordinary income and investment gains or losses and funds added through acquisitions, if any. In addition, any significant or sustained investment losses could result in there being insufficient funds in the trusts to cover the cost of delivering services and merchandise or maintaining cemeteries in the future. Any such deficiency would have to be covered by cash flow, which could have a material adverse effect on our financial condition, results of operations and cash flows. Under our current accounting practices, unrealized gains and losses in the funeral trust funds and cemetery trust funds have no immediate impact on our earnings or cash flow, unless the fair market value of the funds were to decline below the estimated costs to deliver the underlying products and services. If that were to occur, we would record a charge to earnings to record a liability for the expected losses on the delivery of the associated contract. Over time, gains and losses realized in the funds are allocated to underlying preneed contracts and affect the amount of the trust fund earnings we record when we deliver the underlying product or service. In times of adverse market conditions, the funds may eventually realize losses, and our revenue, margins, earnings and cash flow would be negatively affected by the reduced revenue when we deliver the underlying products and services. We project that with approximately 1.0 percent to 3.0 percent annualized returns in the funds over the estimated lives of the associated preneed contracts, our trust and escrow funds would recover the net unrealized depreciation currently in the funds by the time the underlying products and services are delivered. Unrealized gains and losses in the perpetual care trust fund do not affect earnings but could limit the capital gains available to us and could result in lower returns and lower current revenue than we have historically achieved.

***We depend on our key personnel for the future success of the business and may have difficulty retaining or attracting such persons.***
Our future success and our ability to manage future growth depend, in large part, upon the continued services of our senior management and former funeral home owners and the ability to attract and retain key officers and other highly qualified personnel. Competition for such personnel is intense. There can be no assurance that we will continue to be successful in attracting and retaining qualified personnel, and the loss of the services of any of these individuals could have a material adverse effect on our revenue, financial performance and results of operations.

***Increased advertising or more effective marketing by competitors, including over the Internet, could cause us to lose market share and revenue or cause us to incur increased costs in order to retain or recapture our market share.***
In recent years, the marketing of preneed funeral services through television, radio and print advertising, direct mailings and personal sales calls has increased. Extensive advertising or effective marketing by competitors in local markets could cause us to lose market share and revenue or cause us to increase marketing costs. In addition, competitors may change the types or mix of products or services offered. These changes may attract customers, causing us to lose market share and revenue or to incur costs in response to competition in order to vary the types or mix of products or services offered by us. Also, increased use of the Internet by customers to research and/or purchase products and services could cause us to lose market share to competitors offering to sell products or services over the Internet.

***Changes or increases in, or failure to comply with, regulations and licensing requirements applicable to our business could increase costs or decrease cash flows.***
The death care industry is subject to regulation and licensing requirements under federal, state and local laws. For example, the funeral home industry is regulated by the U.S. Federal Trade Commission, which requires funeral homes to take actions designed to protect consumers. State laws impose licensing requirements and regulate preneed sales. Embalming facilities are subject to environmental and health regulations. Compliance with these regulations can be burdensome, and we are always at risk of not complying with the regulations or facing costly and burdensome investigations from regulatory authorities.

***Environmental regulations governing our activities could become more stringent in the future and require us to expand additional funds for environmental compliance.***
Our operations are subject to environmental laws and regulations adopted by federal, state and local authorities in the jurisdictions in which we operate. Failure to comply with such laws and regulations could result in the assessment of substantial administrative, civil and criminal penalties, or the imposition of investigatory and remedial obligations. While we believe we are in substantial compliance with existing laws and regulations, we cannot assure you that we will not incur costs in the future.

**Risks Related to the Capital Structure**

***The Issuer is dependent on the Company for all cash available for distributions***
Keystone North America and Keystone ULC are dependent on the operations and assets of the Company through the ownership of common and preferred shares, respectively. Cash distributions to the holders of IPSs, Common Shares and Subordinated Notes will be dependent on the ability of the Company to make dividend payments on its common shares held by Keystone North America and on its preferred shares held by Keystone ULC. The actual amount of cash available for payments to holders of Subordinated Notes and distribution to holders of the IPSs, or Common Shares or Subordinated Notes will depend upon numerous factors relating to the business of the Company, including profitability, changes in revenue, fluctuations in working capital, capital expenditure levels, applicable laws, compliance with contracts and contractual restrictions contained in the instruments governing any indebtedness. Any reduction in the amount of cash available for distribution, or actually distributed, by the Company will reduce the amount of cash available for Keystone ULC to make payments to holders of Subordinated Notes and to Keystone North America for distributions to holders of Common Shares. While Keystone ULC is contractually obligated to make interest payments on the Subordinated Notes, cash distributions by Keystone North America on the Common Share component of an IPS are not guaranteed and will fluctuate with the performance of the business of the Company.

***A significant amount of our cash is distributed, which may restrict potential growth.***
The payout of substantially all of our operating cash flow makes additional capital and operating expenditures dependent on increased cash flow or additional financing in the future. Lack of these funds could limit our future growth and our cash flow. In addition, we may be precluded from pursuing otherwise attractive acquisitions or investments because they may not be accretive on a short-term basis.

***The Issuer may not receive dividends from Keystone provided for in the dividend policy the board of directors of the Company is expected to adopt or any dividends at all.***
Keystone North America's only source of cash flow for payment of dividends on the Common Shares is distributions on its equity ownership of the Company. The board of directors of the

Company may, in its discretion, amend or repeal the initial dividend policy it is expected to adopt upon the closing of this offering. The Company's board of directors may decrease the level of dividends provided for in this initial dividend policy or entirely discontinue the payment of dividends. Future dividends with respect to the common shares of the Company, if any, will depend on, among other things, the results of operations, cash requirements, financial condition, contractual restrictions, business opportunities, provisions of applicable law and other factors that the board of directors of the Company may deem relevant. The Indenture and the Credit Facility contain significant restrictions on the Company's ability to make dividend payments, including, if the Company defers interest on the Subordinated Notes under the indenture, restrictions on the payment of dividends until the Company has paid all deferred interest, together with accrued interest thereon. In addition, the Company's after-tax cash flow available for dividend and interest payments would be reduced if the Subordinated Notes were treated as equity rather than debt for U.S. federal income tax purposes. In that event, the stated interest on the Subordinated Notes could be treated as a dividend and would not be deductible by the Company for U.S. federal income tax purposes. The Company's inability to deduct interest on the Subordinated Notes could materially increase the Company's taxable income and, thus, the Company's U.S. federal and applicable state income tax liability. If this were to occur, the Company's after-tax cash flow available for dividend and interest payments may be reduced.

***Subject to restrictions set forth in the indenture, the Issuer may defer the payment of interest to holders for a significant period of time.***

Prior to the fifth anniversary of the closing of the offering, the Issuer may, subject to restrictions set forth in the indenture, defer interest payments on the Subordinated Notes on one or more occasions for up to an aggregate period of 24 months. In addition, after the fifth anniversary of the closing of the offering, the Issuer may, subject to certain restrictions, defer interest payments on the Subordinated Notes on eight occasions for up to eight months on each occasion. Deferred interest will bear interest at the same rate as the Subordinated Notes. For any interest deferred during the first five years, the Issuer is not obligated to pay any deferred interest until the fifth anniversary of the closing of the offering, so a holder of IPSs or Subordinated Notes may be owed a substantial amount of deferred interest that will not be due and payable until such time. For any interest deferred after the fifth anniversary of the closing of the offering, the Issuer is not obligated to pay all of the deferred interest until maturity, so a holder of IPSs or Subordinated Notes may be owed a substantial amount of deferred interest that will not be due and payable until such time.

***Fluctuations in the exchange rate may impact the amount of cash available to the Issuer for distribution.***

The distributions to holders of IPSs and the underlying Common Shares and Subordinated Notes are denominated in Canadian dollars. Conversely, all of the Issuer's revenue and expenses, together with distributions received from the Company will be denominated in U.S. dollars. As a result, the Issuer will be exposed to currency exchange rate risks. Although the Issuer intends to directly or indirectly enter into hedging arrangements to mitigate this exchange rate risk, there can be no assurance that these arrangements will be sufficient to fully protect against this risk. If hedging transactions do not fully protect against this risk, changes in the currency exchange rate between U.S. and Canadian dollars could have a material adverse effect on the Issuer's financial condition, results of operations and cash flow and may adversely affect cash distributions.

***Our substantial consolidated indebtedness could negatively impact our business.***

We have a substantial amount of indebtedness. In addition, the indenture under which Subordinated Notes are issued permits future further indebtedness provided that certain covenants are satisfied. The degree to which we are leveraged on a consolidated basis could have important consequences to the holders of IPSs and the underlying Common Shares and Subordinated Notes, including:

• our ability in the future to obtain additional financing for working capital, capital expenditures or other purposes may be limited;

• we may be unable to refinance indebtedness on terms acceptable to us or at all;

• our ability to make distributions to Keystone ULC may be limited, which may make it more difficult for Keystone ULC to satisfy its obligations on the Subordinated Notes;

• a significant portion of our cash flow (on a consolidated basis) is dedicated to the payment of the principal of and interest on our indebtedness, including the Subordinated Notes, thereby reducing funds available for future operations, capital expenditures and/or dividends on our common shares;

• we may be more vulnerable to economic downturns and be limited in our ability to withstand competitive pressures;

• we may be limited on our ability to plan for or react to changes in our business or the industry in which we operate; and

• we may be at a competitive disadvantage to our competitors that have less indebtedness.

The Indenture does not limit Keystone ULC's ability to issue additional Subordinated Notes to be represented by additional IPSs in connection with the repurchase of any Class B or C common shares of Keystone in connection with a Repurchase Event.

***Keystone ULC may not be able to repurchase the Subordinated Notes upon a change of control as required by the Indenture.***

Upon the occurrence of certain specific kinds of change of control events, Keystone ULC will be required to offer to repurchase outstanding Subordinated Notes at 101% of their principal amount plus accrued and unpaid interest, if any, to the date of repurchase. However, it is possible that Keystone ULC will not have sufficient funds at the time of the change of control to make any required repurchases or the restrictions in our Credit Facility may not allow such repurchases. Failure to purchase tendered Subordinated Notes would constitute a default under the Indenture, which, in turn, would constitute a default under our Credit Facility.

***We may not be able to make all principal payments on the Subordinated Notes.***

The Subordinated Notes mature 12 years after the date of issuance. Keystone ULC may not be able to refinance the principal amount of the Subordinated Notes in order to repay the principal outstanding or may not have generated enough cash from operations to meet this obligation. There is no guarantee that Keystone ULC will be able to repay the outstanding principal amount upon maturity of the Subordinated Notes. As a result of the subordinated nature of the guarantees of the Subordinated Notes, upon any distribution to creditors of the Company in a bankruptcy, liquidation or reorganization or similar proceeding relating to the Company or its property or assets, the holders of the Company's senior indebtedness will be entitled to be paid in full in cash before any payment may be made with respect to the Subordinated Notes under the guarantee provided by the Company.

***Changes in the Issuer's creditworthiness may affect the value of the IPSs, Common Shares and Subordinated Notes.***

The perceived creditworthiness of the Issuer, the Company and their respective subsidiaries that have guaranteed the Subordinated Notes may affect the market price or value and the liquidity of the IPSs, Common Shares and Subordinated Notes.

***The restrictive covenants in our Credit Facility and the Indenture could impact our business and affect our ability to pursue our business strategies.***

The agreements in our Credit Facility and the Indenture feature restrictive covenants that limit our ability, among other things, to:

- incur additional indebtedness;
- pay dividends and make distributions in respect of the Issuer's equity interest or to make certain other restrictive payments or investments;
- sell assets;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets;
- enter into transactions with our affiliates;
- create liens; and
- enter into new lines of businesses.

In addition, the Credit Facility includes other and more restrictive covenants and prohibits Keystone and certain of its affiliates from prepaying our other indebtedness, including Keystone ULC prepaying the Subordinated Notes, while debt under our Credit Facility is outstanding. The agreement governing our Credit Facility also requires us to achieve specified financial and operating results and maintain compliance with specified financial ratios. Our ability to comply with these ratios may be affected by events beyond our control. A breach of any of the restrictive covenants in our Credit Facility or in our ability to comply with the required financial ratios could result in a default under the Credit Facility. If a default occurs, the lenders under the Credit Facility may elect to clear all borrowings outstanding under that facility together with accrued interest and other fees, to be immediately due and payable which would result in an Event of Default under the Indenture.

***Deferral of interest payments may have adverse Canadian federal income tax consequences for holders and may adversely affect the trading price of the IPSs.***

If interest payments on the Subordinated Notes are deferred, holders may be required to recognize interest income for Canadian federal income tax purposes in respect of the Subordinated Notes before receiving any cash payment of this interest. In addition, a holder will not receive this cash payment if the holder sells the IPSs or the Subordinated Notes, as the case may be, before the end of any deferral period or before the record date relating to interest payments that are to be paid.

If the Issuer defers interest payments, the IPSs and the Subordinated Notes may trade at a price that does not fully reflect the value of accrued but unpaid interest on the Subordinated Notes. In addition, the existence of the Issuer's right to defer payments of interest on the Subordinated Notes under certain circumstances may mean that the market price for the IPSs or the Subordinated Notes may be more volatile than other securities that do not have these restrictions.

***Future sales, or the possibility of future sales of a substantial amount, of IPSs, Common Shares or Subordinated Notes may impact the price of the IPSs, the Common Shares and Subordinated Notes and could result in dilution.***

Future sales, or the possibility of future sales of a substantial amount, of IPSs, Common Shares or Subordinated Notes in the public market could adversely affect the prevailing market price of the Issuer's IPSs, the Common Shares and Subordinated Notes and could impair the Issuer's ability to raise capital through future sales of those securities. Additionally, the issuance of additional IPSs or Common Shares may dilute an investor's investment in the Issuer and reduce distributable cash per Common Share or per IPS. The Issuer may issue Common Shares and Subordinated Notes, which may be in the form of IPSs, or other securities from time to time in order to raise capital or as consideration for future acquisitions and investments. If an acquisition or investment is significant, the number of Common Shares or the aggregate principal amount of Subordinated Notes, which may be in the form of IPSs, or the number or aggregate principal amount, as the case may be, of other securities that may be issued may in turn be significant. In addition, the Issuer may also grant registration rights covering those IPSs, Common Shares, Subordinated Notes or other securities in connection with any acquisitions or investments.

***Changes may occur in classification of IPS investments.***

There can be no assurance that the Common Shares and Subordinated Notes represented by the IPSs will continue to be qualified investments for trusts governed by registered retirement savings plans, registered retirement income funds, deferred profit sharing plans and registered education savings plans or that the Common Shares and Subordinated Notes represented by the IPSs will not be foreign property under the *Income Tax Act* (Canada) and the regulations thereunder (the ''Tax Act''). On March 23, 2004, the Minister of Finance (Canada) proposed amendments to the *Income Tax Act* (Canada) (the ''Budget Proposals'') to restrict direct and indirect holdings in ''business income trusts'' (as defined in the Budget Proposals) by certain tax exempt investors. On May 18, 2004, the Minister of Finance (Canada) suspended the Budget Proposals pending consultation with representatives of the pension fund industry, the investment industry, provincial governments and other interested parties. The Department of Finance has indicated that it will continue to evaluate the development of the income trust market as part of its ongoing monitoring and assessment of Canadian financial markets and the Canadian tax system. While the Budget Proposals did not reference ownership of subordinated notes and common shares of a company as represented by IPSs, IPSs share many characteristics of income trust units. Accordingly, further changes in this area, in addition to the Budget Proposals, are possible. Such changes could result in the income tax considerations being materially different in certain respects.

***The U.S. Internal Revenue Service may challenge the characterization of the Subordinated Notes as debt.***

There can be no assurance that U.S. federal income tax laws and IRS administrative policies respecting the U.S. federal income tax consequences described herein will not be changed in a manner which adversely affects Non-U.S. Holders. No statutory, judicial or administrative authority directly addresses the treatment of the IPSs or the Subordinated Notes, or instruments similar to the IPSs or the Subordinated Notes, for U.S. federal income tax purposes. As a result, the U.S. federal income tax consequences of the purchase, ownership and disposition of IPSs and the Subordinated Notes are uncertain. The Company received an opinion from the Company's counsel, Kirkland & Ellis LLP and the Underwriters received an opinion from their counsel, Torys LLP, to the effect that the acquisition of an IPS should be treated as the acquisition of the Common Share and Subordinated Notes as separate securities, and that the Subordinated Notes should be classified as debt for U.S. federal income tax purposes. The Company has deducted interest on such Subordinated Notes for tax purposes. However, the IRS or the courts may take the position that the IPSs are a single security classified as equity, or that the Subordinated Notes are properly classified as equity for U.S. federal income tax purposes or that the interest rate on the Subordinated Notes is in excess of an arm's length interest rate, which could adversely affect the amount, timing and character of income, gain or loss in respect of a holder's investment in IPSs or Subordinated Notes, and materially increase the Company's taxable income and, thus, the Company's U.S. federal and applicable state income tax liability. This would adversely affect the Company's financial position, cash flow, and liquidity, and could affect the Company's ability to make interest or dividend payments on the Subordinated Notes and the common shares owned by Keystone North America and may affect the Company's ability to continue as a going concern. In addition, if the Subordinated Notes are reclassified as equity for U.S. federal income tax purposes, Non-U.S. Holders, may be subject to U.S. federal withholding or estate taxes with respect to the Subordinated Notes and the Company could be liable for withholding taxes on any interest payments previously made to Non-U.S. Holders. Payments to foreign holders would not be grossed-up for any such taxes. The Company's tax deduction for interest may be put at risk in the future as a result of a change in law or administrative or judicial rulings issued in the future and, in such event, the Company may need to consider the effect of such developments on the determination of the Company's future tax provisions and obligations.

***If the Issuer subsequently issues Subordinated Notes with significant OID, the Issuer may not be able to deduct all of the interest on the Subordinated Notes.***

Subordinated Notes issued in a subsequent issuance may be issued at a discount to their face value and, accordingly, such notes may have "significant OID" and thus be classified as "applicable high yield discount obligations" for U.S. federal income tax purposes. If any such Subordinated Notes were so treated, a portion of the OID on such notes would be non-deductible by the Company and the remainder would be deductible only when paid. It is also possible that Subordinated Notes issued in a subsequent issuance will be treated as equity for tax purposes. If any such Subordinated Notes were so treated, the interest payable on such Subordinated Notes would be non-deductible by the Company. Any limit on the Company's ability to deduct interest for tax purposes would have the effect of increasing the Company's taxable income and may adversely affect the Company's cash flow available for interest payments and distributions to the Company's shareholders.

***The Company or other payor may not be able to properly report OID to the holders of IPSs or Subordinated Notesand the IRS, and hence may become subject to substantial IRS penalties for such failure.***

The Internal Revenue Code generally requires that the payor of interest and OID to report to its payees and the IRS the amounts of interest and OID includable in income with respect to such payees, unless an exception to reporting applies. If the IPSs or Subordinated Notes issued in this offering are issued with OID and there is a subsequent issuance of Subordinated Notes or if any subsequent issuance of IPSs or Subordinated Notes is issued with OID and, in either case, no exception to reporting applies, the Company or other payor may not be able to properly report the amount of OID to the proper payee because all of the Subordinated Notes are being issued and will be traded under the same CUSIP number and will be held in book-entry form in the name of the CDS or its nominee, CDS & Co. As a result, the identity of the holders of the Subordinated Notes issued with OID may not be known, and hence the Company or other payor may not be able to properly report OID to the IRS and to the proper payees. In such circumstances, the Company or other payor may choose to report such OID to all holders of Subordinated Notes regardless of whether such holders acquired the Subordinated Notes in this offering or a subsequent issuance, unless an exception to reporting applies. The Company believes that such reporting may satisfy the OID reporting requirements and hence reduce or eliminate any exposure of Keystone to penalties for not properly reporting. Non-U.S. Holders who qualify for the Portfolio Interest Exemption generally should not be subject to OID reporting, and hence generally should not be impacted by such reporting. As a result, a holder subject to OID reporting may be required to report OID even though such holder purchased Subordinated Notes having no OID unless such holder can establish to the IRS that its Subordinated Notes do not have OID. The IRS might assert that, unless a holder can establish that it is not holding Subordinated Notes with OID, all Subordinated Notes held by such holder will have OID. Prospective investors should consult their own tax advisor to determine the particular U.S. federal income tax consequences of OID, including the proper reporting of OID in these circumstances and the applicability and effect of U.S. state and local tax laws. The penalties for failure to properly file and report such OID amounts to the IRS is generally capped at $250,000 for all such failures during any calendar year, but if such failure is due to the intentional disregard of the filing requirement, the penalty is the greater of $100 for each return with respect to which a failure occurs or 10% of the aggregate amount of items required to be reported correctly. The penalties for failure to properly furnish and report such amounts to a payee of OID is generally capped at $100,000 for all such failures during any calendar year, but if such failure is due to the intentional disregard of the filing requirement, the penalty is the greater of $100 for each return with respect to which a failure occurs or 10% of the aggregate amount of items required to be reported correctly. A failure is due to intentional disregard if it is a knowing or willful failure to file timely or to include the correct information, which determination is made based on all the facts and circumstances of the particular case. A failure by the Company or other payor to properly report OID in the case of the IPSs and Subordinated Notes may be treated as due to an intentional disregard, and therefore could result is substantial penalties.

***The Subordinated Notes issued or Subordinated Notes issued in a subsequent offering may have OID for U.S. federal income tax purposes.***

The Subordinated Notes issued and Subordinated Notes issued in a subsequent offering may be treated as having been issued with OID for U.S. federal income tax purposes in certain circumstances, *e.g.*, if the allocation of the purchase price of each IPS to the subordinated notes were determined to be too high or if the likelihood of a deferral of interest payments on the Subordinated Notes were determined not to be "remote" or an interest deferral actually occurred. A Non-U.S. Holder generally would not be subject to U.S. federal income tax with respect to such OID so long as such OID is not effectively connected with such holder's conduct of a trade or business within the U.S. and such holder qualifies for the Portfolio Interest Exemption. If the Non-U.S. Holder failed to satisfy these requirements, a holder generally would be required to include OID in income in advance of the receipt of cash attributable to that income, and such OID may be subject to U.S. federal income or withholding taxes. Prospective investors should consult their own tax advisor to determine the particular U.S. federal income tax consequences of OID, including the applicability and effect of U.S. state and local tax laws. The requirement to include OID in income in advance of the receipt of cash attributable to that income may discourage U.S. persons and those Non-U.S. Holders subject to U.S. federal income tax on OID from acquiring Subordinated Notes and may adversely affect the liquidity of the IPSs and Subordinated Notes.

***Certain U.S. tax considerations may discourage third parties from pursuing a tender offer or other change of control transaction.***

Under certain circumstances, Code Section 163(j) limits a corporation's deductions for interest paid to related foreign persons exempt from U.S. tax. For these purposes, a corporation and a creditor of the corporation will generally be "related" if the creditor owns, directly or by attribution, more than 50% of the corporation by vote or value. The purchase of an IPS will be treated for U.S. tax purposes as a purchase of both an equity interest and a creditor's interest in the Issuer. As a result, a purchase by any non-U.S. person of more than 50% of the IPSs could result in Keystone's interest deductions being limited with respect to the Subordinated Notes represented by those IPSs or otherwise owned by such person. This could discourage third parties from pursuing a tender offer or other change of control transaction with respect to the Issuer, which otherwise might have led to a premium being paid for IPSs.

***Keystone's interest deductions on the Subordinated Notes are likely "dual consolidated losses" for U.S. federal income tax purposes and may result in disallowance of interest deductions if certain "triggering events" occur.***

Pursuant to Code section 1503(d) and the Treasury Regulations thereunder, the interest deductions generated on the Subordinated Notes will likely generate a "dual consolidated loss" ("DCL") for U.S. federal income tax purposes and will therefore be deductible by Keystone only if Keystone and Keystone ULC make the election provided by Treasury Regulation 1.1503-2(g)(2) and comply with all applicable requirements, including annual reporting and certification requirements. Keystone and Keystone ULC intend to make such election and comply with all applicable requirements. Even if such an election is made, however, if any of several "triggering events" occurs (*e.g.*, the use of such losses to offset the income of any other non-U.S. person, or, in certain circumstances, a disposition of Keystone ULC stock or assets), Keystone will generally be required to report the amount of any prior interest deductions on the subordinated notes (plus interest thereon) as gross income in the year of the triggering event. Keystone and Keystone ULC intend to comply with all of the DCL reporting and certification requirements and to conduct their affairs such that no DCL triggering event occurs. However, if Keystone and Keystone ULC fail to satisfy such reporting and certification requirements, or if a DCL triggering event occurs and no exception applies, Keystone's taxable income and thus its U.S. federal income tax liability would be materially increased. This would adversely affect Keystone's financial position, cash flow, and liquidity, and could affect the Company's ability to make interest or dividend payments on the Subordinated Notes and the Common Shares and may affect the Company's ability to continue as a going concern.

***Recent U.S. federal income tax legislation could lead to the Company being treated as a U.S. corporation for U.S. federal income tax purposes.***

Recently enacted U.S. federal income tax legislation dealing with corporate "inversions" (*e.g.*, certain transactions in which a non-U.S. corporation acquires substantially all of the equity interests in, or the assets of, a U.S. corporation or partnership, if, after the transaction, former equity owners of the U.S. corporation or partnership own a specified level of stock in the non-U.S. corporation) provides in certain cases that a non-U.S. corporation may be treated as a U.S. corporation for U.S. federal income tax purposes. As enacted, this legislation does not apply to Keystone North America, because the shareholders of Keystone will not own any stock in Keystone North America as a result of the offering and related transactions. The legislation grants authority to the Internal Revenue Service to write implementing regulations, which could, if exercised broadly and retroactively, cause the new provisions to apply to Keystone North America and result in U.S. withholding taxes being imposed on dividends paid on the Common Shares to Non-U.S. Holders. Certain advisors of Keystone may have discussions with U.S. tax authorities to explain why such regulations should not extend to a number of transactions, including transactions such as this one. The outcome of such discussions is uncertain.

**Outlook**

The Company has operated as a recent combination of two sizable funeral service companies for 327 days as of December 31, 2005. For this 327-day period, the Company's revenues remain strong based on better than expected funeral service volume combined with higher per service revenue. Management expects that continued increases in average funeral service revenue as a result of the Company's operational programs will continue to exceed the anticipated increases in operating costs.

The funeral service industry is subject to seasonal variations with historically higher revenues in the winter months. For example, EBITDA generated for the pro forma combined three-month period ending December 31, 2005 represented 25.4% of the pro forma results for the trailing twelve-month period then ended. This is consistent with similar trends over the last five years and Management does not anticipate any significant changes to this annual trend for fiscal year 2006 or further into the future.

The Company's monthly distribution rate of C$0.08333333 per IPS unit was established at the time of its IPS Offering and was, in large part, based upon the historical results for Keystone and Hamilton (adjusted for certain factors in connection with the change in capital structure, expense as a reporting issuer, and synergies anticipated from the business combination). Management remains confident of the Company's business model and ability to meet the anticipated annual distribution target of C$1.00 per IPS.

In addition, the Company has identified and is pursuing strategic, accretive acquisition opportunities with a focus on those that would provide the most synergies with its existing homes.

**Additional Information**

Additional information relating to the Company, including the financial statements for the period from February 8, 2005 to December 31, 2005 is available on SEDAR at www.sedar.com.

KEYSTONE

# KEYSTONE NORTH AMERICA INC.

## CONSOLIDATED FINANCIAL STATEMENTS

## PERIOD FROM FEBRUARY 8, 2005 TO DECEMBER 31, 2005

Keystone North America Inc.

Consolidated Financial Statements

December 31, 2005

## Contents

AUDITOR'S REPORT

To the Shareholders of Keystone North America Inc.

We have audited the consolidated balance sheet of Keystone North America Inc. as at December 31, 2005 and the consolidated statements of operations and accumulated deficit and cash flows for the period from February 8, 2005 to December 31, 2005. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2005 and the results of its operations and its cash flows for the period from February 8, 2005 to December 31, 2005 in accordance with Canadian generally accepted accounting principles.

Ernst + Young LLP

Ernst & Young LLP
Certified Public Accountants
Tampa, Florida
March 10, 2006 (except for Note 16 which is as at March 14, 2006).

Keystone North America Inc.

Consolidated Balance Sheet
December 31, 2005
(000's of U.S. Dollars)

| | | |
|---|---|---|
| **Assets** | | |
| Current assets: | | |
| Cash and cash equivalents | **$** | **6,614** |
| Marketable securities | | **350** |
| Restricted short-term investments (Note 7) | | **3,331** |
| Trade receivables, less allowance for doubtful accounts of $1,795 | | **7,350** |
| Inventories | | **3,816** |
| Income tax receivable | | **1,102** |
| Prepaid and other current assets (Note 12) | | **2,564** |
| Future income taxes (Note 11) | | **2,308** |
| Total current assets | | **27,435** |
| | | |
| Preneed receivables and funds (Note 10) | | **43,100** |
| Restricted cemetery care funds | | **552** |
| Restricted long-term investments (Note 7) | | **8,525** |
| Property and equipment, net (Note 6) | | **67,546** |
| Goodwill | | **86,741** |
| Tradenames | | **24,652** |
| Covenants not to compete, less accumulated amortization of $2,898 | | **11,713** |
| Foreign currency exchange contracts (Note 12) | | **3,597** |
| Other assets (Note 2) | | **7,653** |
| Total assets | **$** | **281,514** |

*See accompanying notes.*

On behalf of the board

R. G. Horn
Robert Horn
Director

L Waisberg
Lorie Waisberg
Director

Keystone North America Inc.

Consolidated Balance Sheet
December 31, 2005
(000's of U.S. Dollars)

| | | |
|---|---|---|
| **Liabilities and shareholders' equity** | | |
| Current liabilities: | | |
| Accounts payable and accrued expenses | $ | 7,532 |
| Dividends payable | | 599 |
| Current maturities of long-term debt (Note 7) | | 3,491 |
| Total current liabilities | | 11,622 |
| | | |
| Deferred revenue | | 6,461 |
| Long-term debt (Note 7) | | 129,605 |
| Future income taxes (Note 11) | | 10,926 |
| Other long-term liabilities | | 84 |
| | | |
| Non-controlling interests in preneed funds (Note 2) | | 41,251 |
| Non-controlling interests in cemetery care funds | | 552 |
| Minority interest (Note 9) | | 9,513 |
| | | |
| Shareholders' equity: | | |
| Share capital (Note 8) | | 78,312 |
| Accumulated deficit | | (2,114) |
| Cumulative currency translation adjustments | | (4,698) |
| Total shareholders' equity | | 71,500 |
| Total liabilities and shareholders' equity | $ | 281,514 |

*See accompanying notes.*

On behalf of the board

Robert Horn
Director

Lorie Waisberg
Director

Keystone North America Inc.

Consolidated Statement of Operations and Accumulated Deficit
Period from February 8, 2005 to December 31, 2005
(000's of U.S. Dollars – except per share amounts)

| | | |
|---|---|---|
| Revenues: | | |
| Funeral services | $ | 73,118 |
| Other | | 3,409 |
| Total revenues | | 76,527 |
| Costs and expenses | | 49,952 |
| Gross profit | | 26,575 |
| | | |
| Other operating expenses: | | |
| Corporate, general and administrative expenses | | 5,482 |
| Depreciation | | 2,387 |
| Amortization | | 2,898 |
| Income from operations | | 15,808 |
| | | |
| Interest expense | | 14,259 |
| Unrealized gain on foreign currency exchange contracts (Note 12) | | 4,627 |
| Other income | | 736 |
| Income from continuing operations before income taxes and minority interest | | 6,912 |
| | | |
| Income tax expense (Note 11) | | 3,032 |
| Minority interest | | 797 |
| Net income from continuing operations | | 3,083 |
| Net income from discontinued operations (Note 5) | | 55 |
| Net income | | 3,138 |
| | | |
| Accumulated deficit– beginning of period | | - |
| Dividends | | 5,252 |
| Accumulated deficit – end of period | $ | (2,114) |
| | | |
| | | 18,768,017 |
| Basic and diluted net income from continuing operations | $ | 0.16 |
| Basic and diluted net income from discontinued operations | $ | 0.00 |
| Basic and diluted net income per common share | $ | 0.17 |

*See accompanying notes.*

Keystone North America Inc.

Consolidated Statement of Cash Flows
Period from February 8, 2005 to December 31, 2005
(000's of U.S. Dollars)

| | | |
|---|---|---|
| Operating activities: | | |
| Net income | $ | 3,138 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Minority interest | | 801 |
| Provision for future income taxes | | 2,888 |
| Unrealized gain on foreign currency exchange contracts | | (4,627) |
| Amortization expense | | 2,979 |
| Depreciation expense | | 2,471 |
| Loss on sale of businesses and assets | | 196 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | | 1,775 |
| Prepaid and other current assets | | (950) |
| Deferred preneed funeral contracts | | (40) |
| Accounts payable, accrued salaries and wages, and other accrued expenses | | 665 |
| Other | | 929 |
| *Net source of cash from operating activities* | | 10,225 |
| Investing activities: | | |
| Business acquisitions, net of cash acquired of $2,539 | | (153,415) |
| Purchase of Class B Minority Interest Shares related to the exercise of the over-allotment option | | (12,691) |
| Purchases of property and equipment | | (2,223) |
| Cash paid for transition costs | | (3,162) |
| Proceeds from sale of businesses and assets | | 3,303 |
| Proceeds from restricted investments | | 4,801 |
| Proceeds invested to fund indebtedness to former owners and employees | | (16,393) |
| *Net use of cash from investing activities* | | (179,780) |
| Financing activities: | | |
| Initial public offering and over-allotment proceeds of common shares, net of expenses | | 78,312 |
| Initial public offering and over-allotment proceeds of 14.5% Subordinated Notes, net of expenses | | 64,492 |
| Issuance of 14.5% Separate Subordinated Notes, net of expenses | | 8,005 |
| Proceeds from New Credit Facility, at closing of IPS transactions | | 43,100 |
| Deferred financing costs | | (8,085) |
| Borrowings on long-term debt | | 222 |
| Payments on long-term debt | | (4,272) |
| Cash paid for Class A dividends | | (4,751) |
| Cash paid for Class B dividends | | (854) |
| *Net source of cash from financing activities* | | 176,169 |
| *Net source of cash* | | 6,614 |
| Cash and cash equivalents, beginning of period | | - |
| Cash and cash equivalents, end of the period | $ | 6,614 |

**Supplement disclosure of cash flow information:**

| | | |
|---|---|---|
| Cash paid for interest | $ | 12,959 |
| Cash paid for income taxes | $ | 821 |

*See accompanying notes.*

Keystone North America Inc.

Notes to the Consolidated Financial Statements

*(000's of U.S. Dollars, except percentages and where the context requires)*

December 31, 2005

## 1. General

Keystone North America Inc. (the "Company") was incorporated on August 27, 2004 under the laws of the Province of Ontario. The Company's authorized capital consists of an unlimited number of common shares ("Common Shares") and an unlimited number of Class A preferred shares. No Class A preferred shares have been issued. Holders of Common Shares are entitled to receive dividends as and when declared by the board of directors and are entitled to one vote per Common Share on all matters to be voted on at all meetings of shareholders of the Company. From the time period August 27, 2004 to February 8, 2005, the Company was inactive. The Company and its indirect subsidiary, Keystone Newport ULC (together, the "Issuer"), completed an initial public offering (the "IPS Offering") on February 8, 2005 through the issuance of 17,100,000 income participating securities ("IPSs") for gross proceeds of $136,887 (C$171,000). Each IPS consists of one Common Share and C$4.286 principal amount of 14.5% subordinated notes of Keystone Newport ULC ("Subordinated Notes"). In connection with the IPS Offering, the Company acquired an 85.3% interest in Keystone Group Holdings, Inc. ("Keystone"). Simultaneous to the IPS Offering, the Company indirectly acquired assets, liabilities and stock of certain subsidiaries of HFSC Holdings, Inc. ("Hamilton").

On February 17, 2005, the underwriters of the IPS Offering exercised an over-allotment option granted in connection with the IPS Offering. As part of the exercise of the over-allotment option, the Issuer completed a subsequent issuance of 1,668,017 IPSs for gross proceeds of $13,522 (C$16,680). The Issuer used the net proceeds from this subsequent issuance to increase its ownership percentage in Keystone to 93.7%, resulting in a reduction of minority interest. Keystone Newport ULC, both prior and subsequent to the purchase of additional shares of preferred stock, owns 100% of the issued and outstanding preferred stock of Keystone. The Common Shares issued in connection with the over-allotment participated fully in the distribution for the month of February paid on March 15, 2005.

At any time after the 45th day following the date of original issuance or upon the occurrence of a change of control of Keystone Newport ULC, holders of IPSs may separate their IPSs into the Common Shares and Subordinated Notes represented thereby through their broker or other financial institution. Similarly, any holder of Common Shares and Subordinated Notes may recombine the applicable number of Common Shares and principal amount of Subordinated Notes to form IPSs through their broker or other financial institution, at any time. The IPSs will

**1. General (continued)**

be automatically separated into the Common Shares and Subordinated Notes upon the occurrence of any of the following: (i) with respect to any holder of IPSs, acceptance by such holder of Keystone Newport ULC's offer to repurchase the Subordinated Notes represented by that holder's IPSs in connection with a change of control of the Company or Keystone Newport ULC; (ii) exercise by Keystone Newport ULC of its right to redeem all or a portion of the Subordinated Notes that may be represented by IPSs at the time of such redemption; (iii) the date on which the outstanding principal amount of the Subordinated Notes becomes due and payable, whether at the stated maturity date or upon acceleration thereof; (iv) if The Canadian Depository for Securities Limited is unwilling or unable to continue as securities depository with respect to the IPSs and the Issuer is unable to find a successor depository; or (v) the continuance (without cure) of a payment default on the Subordinated Notes for 90 days.

Simultaneous to the IPS Offering, Keystone Newport ULC issued, on a private placement basis, \$8,149 (C\$10,000) of separate 14.5% subordinated notes (the "Separate Subordinated Notes" and together with the Subordinated Notes, the "Notes") and the Issuer, through a subsidiary, entered into a bank credit facility (the "Credit Agreement") with a group of lenders consisting of a \$43,100 term loan and a \$15,000 revolving credit commitment (together with the IPS Offering, the "IPS Transactions"). In connection with the IPS Offering, \$43,100 was drawn on the Credit Agreement.

These audited consolidated financial statements present the results of operations of the Company from the close of the IPS Offering on February 8, 2005 to December 31, 2005. The Company had no active operations in the period prior to February 8, 2005, and thus, no comparative figures are presented.

**2. Basis of Presentation**

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. These consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany transactions and balances have been eliminated on consolidation. The significant accounting policies are described below:

**2. Basis of Presentation (continued)**

*Foreign Currency Translation*

The functional currency of the Company and Keystone Newport ULC is the Canadian dollar. The functional currency of the Company's operations in the United States is the U.S. dollar. The Company's financial statements are reported in U.S. dollars, as the principal operations and cash flows of its subsidiaries are conducted in U.S. dollars. As a result, the assets and liabilities of the Company and Keystone Newport ULC, including the Notes of Keystone Newport ULC, which are denominated in Canadian dollars, are translated into U.S. dollars using the exchange rate in effect at the period end and revenues and expenses are translated at the average rate during the period. Exchange gains or losses on translation are deferred as a separate component of shareholders' equity.

Monetary assets and liabilities denominated in a currency other than the functional currency are translated at the rate of exchange prevailing at the balance sheet date. Transactions denominated in a currency other than the functional currency are translated at the rate of exchange prevailing on the transaction date. Gains and losses on translation of these items are included in the consolidated statement of operations.

*Cash and Cash Equivalents*

Cash and cash equivalents include all cash balances and highly liquid investments with original maturities of three months or less from the date of purchase. At December 31, 2005, there were no cash equivalents.

*Concentration of Credit Risk*

The Company grants customers credit in the normal course of business. Procedures exist to secure accounts and include confirming a source of third-party payment such as insurance assignment, estate, group life policy or maturing pre-need trust. To date, bad debts have not been significant in relation to the volume of revenues. The Company charges interest on past due receivables in certain circumstances.

**2. Basis of Presentation (continued)**

Preneed funeral contracts do not subject the Company to significant collection risk because contracts may be cancelled due to nonpayment before services are rendered. Preneed funeral contracts that the customer funds by purchasing insurance-funded contracts are subject to supervision by state insurance departments and are protected in the majority of states by insurance guarantee acts.

*Use of Estimates*

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Company bases its estimates and judgments on historical experience and on various other assumptions that it believes are reasonable under the circumstances. Amounts reported that are affected by these assumptions include, but are not limited to accounts receivable, income taxes, goodwill and other long-lived assets.

*Marketable Securities*

The carrying values of marketable securities are stated at the lower of cost or market, as determined by quoted market prices, as they are classified as temporary investments. Realized investment and interest income is included in the cost basis of these securities.

*Inventories*

Inventories, which consist primarily of caskets and cremation urns, are carried at the lower of cost, determined on a first-in, first-out method, and net realizable value.

**2. Basis of Presentation (continued)**

*Restricted Investments*

Restricted investments represent funds from the IPS Offering proceeds set aside to satisfy acquired former owner obligations and equipment financing. The restricted investment account has been established with the administrative agent of the Credit Agreement and is restricted under terms of the Credit Agreement to investments that are the direct obligations of the U.S. Government. Proceeds from this account are restricted to use solely for the payment of existing former owner obligations and equipment financing. The Company cannot modify the payment instructions under the related custodial agreement without the approval of the administrative agent. The carrying values of the investments are stated at cost, less provisions for loss in respect of individual investments where market value is below cost and this decline appears to be other than temporary. Realized investment and interest income is included in the carrying amount of these securities. At December 31, 2005 the Company has concluded that the declines in the market values of the restricted investments are temporary and primarily relate to discounts and premiums related to the purchase of bonds. Total market value for restricted investments is $11,821 at December 31, 2005.

*Property and Equipment*

Property and equipment is recorded at cost and is depreciated on a straight-line basis over the estimated useful lives of the assets as follows:

| | |
|---|---|
| Buildings and related improvements | 15 to 40 years |
| Furniture, fixtures and equipment | 7 to 10 years |

*Goodwill and Other Identifiable Intangibles*

Goodwill represents the excess of cost over fair value of net assets acquired in business combinations accounted for under the purchase method. Other identifiable intangible assets consist of covenants not to compete and tradenames. Covenants not to compete represent the value of non-competition agreements with certain key management personnel of acquired funeral operations. Amortization of such covenants not to compete is provided on a straight-line basis over the term of the agreements. Tradenames represent the value assigned to the acquired business names under which the entities do business.

**2. Basis of Presentation (continued)**

Tradenames have an indefinite life and are not amortized. Goodwill and tradenames are tested for impairment annually on October 1, by comparing their fair values with their book values. Goodwill and tradenames are required to be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of an intangible asset below its carrying amount. Covenants not to compete are tested for impairment in accordance with our policy for long-lived assets.

*Deferred Financing Costs*

The Company incurred costs related to obtaining debt financing. These costs have been capitalized and are being amortized to interest expense over the term of the related debt. The Company has capitalized approximately $8,085 of costs related to its indebtedness incurred in connection with the IPS Offering and the Credit Agreement. As of December 31, 2005, the amortization expense of those costs for the year totaled approximately $1,177. Deferred financing costs are included in other assets in the consolidated balance sheet.

*Preneed Funeral Accounting*

The Company sells preneed funeral services, whereby a customer contractually agrees to the terms of a funeral to be performed in the future. The Company sells these price-guaranteed, prearranged funeral contracts through various programs providing for future funeral services at prices prevailing when the agreement is signed. Preneed funeral contracts are generally funded either through trusts established by the customer or through life insurance policies purchased by the customer and issued by third party insurers. The Company, in accordance with certain state laws, may retain a portion of the payments on preneed contracts funded through trust. The Company records costs as incurred. As of December 31, 2005, the Company has deferred revenue related to $2,278 of sales commissions and $2,995 of retained cemetery funds contracts that do not yet meet the criteria for revenue recognition.

Amounts paid by the customer pursuant to the preneed funeral contracts are recognized as funeral service revenue at the time the funeral is performed. Trust earnings and increasing insurance benefits are recognized as funeral service revenues when the funeral service is performed and are intended to protect the margin associated with providing a price-guaranteed funeral service in the future.

**2. Basis of Presentation (continued)**

Preneed receivables and funds consist of receivables from customers, trusts or other, non-insurance accounts that will be received upon delivery of preneed merchandise and services. Preneed funeral contracts funded through life insurance policies purchased by the customer and issued by third party insurers are not reflected as assets or liabilities in the financial statements. The Company does not have control of these policies and is obligated to deliver services at a fixed price only if the insurance policy proceeds are delivered.

The preneed receivables and funds are recorded at cost, less provisions for loss in respect of individual investments where market value is below cost and this decline appears to be other than temporary.

Amounts held in trust are refunded to the customer according to state law upon cancellation of the contract.

*Revenue Recognition*

Funeral revenue, which includes funeral merchandise and services, is recognized when the funeral service is performed. Revenue associated with cemetery merchandise and services, is recorded when the merchandise has been delivered or the service has been performed. Revenue associated with cemetery property interment rights (cemetery burial property) is not recognized until a minimum percentage (10%) of the sales price has been collected. Commission revenue is generated through sales of preneed insurance contracts and is deferred until realized, generally one year. Cemetery and commission revenue is reported as other revenue on the income statement. The Company's trade receivables primarily result from funeral services already performed. An allowance for doubtful accounts is established primarily based on historical experience.

*Impairment of Long-Lived Assets*

Management continually evaluates whether events or circumstances have occurred that indicate that the remaining estimated useful lives of long-lived assets, such as property, plant and equipment and covenants not to compete, may warrant revision or that the remaining balances may not be recoverable. If this review indicates that the assets will not be recoverable, as determined based on the undiscounted future cash flows from the use of the assets, the carrying value of the assets will be reduced to their estimated fair value.

**2. Basis of Presentation (continued)**

*Income Taxes*

Income taxes have been computed utilizing the liability approach. Future income tax assets and liabilities arise from differences between the tax basis of an asset or liability and its reported amount in the financial statements. Future tax assets and liabilities are determined by using substantively enacted tax rates expected to be in effect when the temporary differences are expected to reverse. A valuation allowance is recorded when the expected realization of a future income tax asset is not considered to be more likely than not.

*Accounting for Derivatives and Hedging Activities*

Derivative financial instruments are utilized by the Company in the management of its foreign currency and interest rate exposures. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives to specific assets and liabilities on the balance sheet or to specific firm commitments or forecasted transactions. The Company also formally assesses, both at the hedge's inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows or hedged items.

The Company accounts for its interest rate cap and interest rate collar on an accrual basis whereby interest payable and interest expense under the Credit Agreement is limited to 6.95% (see Note 7). The interest rate cap and interest rate collar agreements require the periodic exchange of payments without the exchange of the notional principal amount on which the payments are based. The interest rate collar is not effective until 2006.

Derivatives that are not designated hedges for accounting purposes, such as the foreign currency exchange contracts, are recorded at fair value on the balance sheet. Changes in fair value are recorded in the statement of operations (see Note 12).

**2. Basis of Presentation (continued)**

*Segment Reporting*

The Company through its subsidiaries is a nationwide funeral home operator in the United States. The Company operates as one operating segment.

*Earnings per Share*

Earnings per share is calculated by dividing the net income or loss by the weighted average number of Common Shares that includes the 17,100,000 Common Shares issued at the IPS Offering and 1,668,017 Common Shares issued upon exercise of the over-allotment.

*Seasonality*

Funeral service revenue has historically been seasonal, peaking in the winter months.

*Consolidation of Variable Interest Entities*

Accounting Guideline 15 "Consolidation of Variable Interest Entities" (AcG-15) outlines consolidation principles for certain entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. As a result of AcG-15, the Company has consolidated its preneed cemetery trust funds, preneed funeral trust funds and cemetery care funds. The preneed funds and cemetery care funds are considered variable interest entities because as a group, the equity investors (if any) do not have sufficient equity at risk and do not have the direct or indirect ability through voting or similar rights to make decisions about the funds' activities that have a significant effect on the success of the funds. AcG-15 requires the Company to consolidate any funds for which the Company is the primary beneficiary. The Company is the primary beneficiary of all of its preneed funds and cemetery care funds in that the Company absorbs the majority of the funds' expected losses.

The Company has also recognized non-controlling financial interests of third parties in the preneed funds and cemetery care funds to the extent that the Company's customers are the legal beneficiaries of the funds and the Company does not have a legal right to access the principal amount of the funds.

## 2. Basis of Presentation (continued)

Also, as a result of AcG-15, the Company recognizes realized earnings of its preneed funds and cemetery care funds in Other Income in its statements of operations. The Company also recognizes expenses within Other Income equal to the realized earnings of these funds attributable to the non-controlling interest holders and defers the realized earnings of the funds attributable to the Company when such earnings have not been earned by the Company through the performance of services or delivery of merchandise.

The Company recognizes as revenues, amounts removed from the pre-need funds upon the performance of services and delivery of merchandise including realized earnings accumulated in the funds. The accounting associated with AcG-15 principally affects classifications within the financial statements and do not affect cash flow or the manner in which the Company recognizes and reports revenue or net income. AcG-15 also does not change the legal relationships among the funds, the Company and its customers.

*Fair Value of Financial Instruments*

The carrying amounts of cash, trade receivables, foreign currency contracts, accounts payable and accrued expenses approximate fair value because of the short maturity of these items. The carrying amount of debt outstanding pursuant to bank credit agreements approximates fair value as interest rates on these instruments approximate current market rates. The fair value of the subordinated notes payable is not readily determinable due to a lack of trading history and other economic variables. The fair value of the foreign currency contracts approximates their carrying value on the financials statements, see note 12 for further discussion.

## 3. Acquisition of assets, liabilities and certain subsidiaries of Hamilton

Simultaneous with the IPS Offering, Keystone indirectly acquired assets, liabilities and stock of certain subsidiaries of Hamilton. The acquisition of these assets, liabilities and the stock of certain subsidiaries of Hamilton have been accounted for under the purchase method of accounting. The net purchase price of the Hamilton acquisition was approximately $58,000, which included a contribution of approximately $8,000 of equity interest in Keystone. The allocation of the purchase price to the fair values of assets acquired and liabilities assumed is as follows:

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

### 3. Acquisition of assets, liabilities and certain subsidiaries of Hamilton (continued)

| | |
|---|---|
| Current assets, less current liabilities | $ 229 |
| Property and equipment | 34,352 |
| Preneed receivables and funds | 20,721 |
| Cemetery care funds | 849 |
| Other assets | 546 |
| Intangible assets | 19,031 |
| Future income taxes | 2,128 |
| Long-term debt | (6,415) |
| Deferred revenue | (9,566) |
| Other long-term liabilities | (140) |
| Non-controlling interest in preneed funds | (17,391) |
| Non-controlling interest in cemetery care funds | (849) |
| Minority interest of Keystone | (7,827) |
| Subtotal | 35,668 |
| Goodwill | 22,163 |
| Total | $ 57,831 |

The allocation of the purchase price is based on internal management and third party valuations and anticipated tax basis elections. The purchase price allocation represents the fair value of assets acquired and liabilities assumed, pending any changes in estimates of anticipated tax basis elections. Intangible assets represent covenants not to compete of $7,627 that are amortized over the life of the agreements and tradenames of $11,404 with indefinite lives. The minority interest amount included in the purchase allocation does not reflect the exercise of the over-allotment option.

In conjunction with the acquisition of assets, liabilities and stock of certain subsidiaries of Hamilton, Keystone has established a reserve for transition and other costs to eliminate the corporate office and certain associated corporate administrative functions. The costs anticipated in this reserve include severance and termination costs of personnel and other assumed liabilities. The total provision for these costs was approximately $4,000 in 2005. At December 31, 2005 the reserve has been reduced to approximately $1,000 as a result of cash payments for anticipated items.

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

**4. Acquisition of Keystone**

Simultaneous with the IPS Offering, the Company acquired all of the issued and outstanding common shares of Keystone representing an 85.3% interest in Keystone and Keystone Newport ULC acquired all of the preferred shares of Keystone. Upon the closing of the over-allotment, the Company acquired an additional 8.4% interest in Keystone. Existing investors in Keystone retained all of the issued and outstanding shares of Class B common stock of Keystone representing a 6.3% minority interest in Keystone at December 31, 2005.

The acquisition of the common shares of Keystone has been accounted for under the purchase method of accounting. The net purchase price of the Keystone acquisition was approximately $98,000. The preliminary allocation of the purchase price to the fair values of assets acquired and liabilities assumed is as follows:

| | |
|---|---|
| Current assets, less current liabilities | $ 7,311 |
| Property and equipment | 37,242 |
| Preneed receivables and funds | 25,766 |
| Other assets | 1,012 |
| Intangible assets | 21,391 |
| Future income taxes | (7,716) |
| Long-term debt | (10,163) |
| Deferred revenue | (1,869) |
| Non-controlling interest in preneed funds | (25,766) |
| Minority interest | (14,536) |
| Subtotal | 32,672 |
| Goodwill | 65,451 |
| Total | $ 98,123 |

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

## 4. Acquisition of Keystone (continued)

The allocation of the purchase price is based on internal management and third party valuations. The purchase price allocation represents the fair value of assets acquired and liabilities assumed. Intangible assets represent covenants not to compete of $7,180 that are amortized over the life of the agreements and tradenames of $14,211 with indefinite lives. The minority interest amount included in the purchase allocation does not reflect the exercise of the over-allotment option.

## 5. Discontinued Operations

On September 28, 2005, the Company disposed of one funeral home located in Washington for net cash proceeds of approximately $532. On December 29, 2005, the Company disposed of two funeral homes in Florida for net cash proceeds of approximately $2,346. On December 31, 2005, the Company disposed of three cemeteries in Ohio for net cash proceeds of approximately $312.

Summarized operating results for the period from February 8, 2005 to December 31, 2005 are as follows:

| | |
|---|---|
| Revenues | $ 2,272 |
| Costs and expenses | 1,954 |
| Gross profit | 318 |
| Depreciation | 84 |
| Amortization | 81 |
| Interest expense | 4 |
| Other income | (62) |
| Income tax expense | 92 |
| Minority interest | 4 |
| Income from discontinued operations | 115 |
| Loss on disposal of discontinued operations, net of tax benefit | 60 |
| Income from discontinued operations | $ 55 |

Total assets and liabilities disposed were $8,795 and $5,501 respectively. Goodwill disposed of for all dispositions was a combined $873. Tradenames and covenants not to compete disposed of for all dispositions were a combined $963 and $220 respectively.

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

## 6. Property and Equipment

Property and equipment consisted of the following at December 31, 2005:

| | Cost | Accumulated Depreciation | Total |
|---|---|---|---|
| Land | $ 13,288 | $ – | $ 13,288 |
| Buildings and improvements | 49,281 | (1,350) | 47,931 |
| Furniture, fixtures and equipment | 6,979 | (1,030) | 5,949 |
| Undeveloped cemetery property | 378 | – | 378 |
| | $ 69,926 | $ (2,380) | $ 67,546 |

## 7. Debt

Indebtedness of the Company at December 31, 2005 includes the following:

| | Current | Long-Term |
|---|---|---|
| Subordinated notes | $ – | $ 77,571 |
| Term loan facility | – | 43,100 |
| Obligations under covenants not to compete | 2,320 | 4,885 |
| Notes payable to former owners | 889 | 3,406 |
| Obligations under consulting agreements | 93 | 270 |
| Equipment financing | 189 | 373 |
| | $ 3,491 | $129,605 |

Maturities of long-term debt are as follows:

| Year ending December 31: | Term Loan Facility | Equipment Financing | Due to Former Owners & Employees | Subordinated Notes |
|---|---|---|---|---|
| 2006 | $ – | $ 189 | $ 3,302 | $ – |
| 2007 | – | 161 | 3,061 | – |
| 2008 | 43,100 | 102 | 2,482 | – |
| 2009 | – | 77 | 1,231 | – |
| 2010 | – | 33 | 428 | – |
| Thereafter | – | – | 1,359 | 77,571 |
| | $ 43,100 | $ 562 | $ 11,863 | $ 77,571 |

**7. Debt (continued)**

*Credit Agreement*

The Credit Agreement includes a $43,100 term loan and a $15,000 revolving credit commitment. Borrowings under the Credit Agreement may be Base Rate Loans or Eurodollar Loans, as defined in the Credit Agreement. Base Rate Loans bear interest at the base rate, as defined in the Credit Agreement (7.25% at December 31, 2005), plus the applicable margin, which ranges from 2.00% to 2.50% depending on Keystone's leverage ratio on the pricing date. Eurodollar Loans bear interest at the adjusted LIBOR rate, as defined in the Credit Agreement (4.38% at December 31, 2005), plus the applicable margin, which ranges from 3.50% to 4.00% depending on Keystone's leverage ratio on the pricing date (4.00% at December 31, 2005). Borrowings under the Credit Agreement are collateralized by assets of Keystone and its U.S. domestic subsidiaries, and certain shares of the capital stock of Keystone and the capital stock of each of its subsidiaries. In addition, payment and performance of the obligations under the Credit Agreement are guaranteed by each of Keystone's subsidiaries. The Credit Agreement contains various covenants that, among other things, require Keystone to maintain certain defined leverage and coverage ratios. The credit agreement has a term loan maturity date of February 8, 2008, at which time the entire principal balance of and all accrued interest shall mature and become due.

In connection with the IPS Offering, the Company entered into an interest rate cap agreement (the "Interest Rate Cap") and an interest rate collar agreement (the "Interest Rate Collar") to set limits on its interest rate exposure on the term loan facility ($43,100 notional amount). The term for the Interest Rate Cap is effective through February 10, 2006 and the term of the Interest Rate Collar is effective from February 11, 2006 through the credit agreement's maturity date. At December 31, 2005 the Interest Rate Cap had an effective LIBOR rate of 6.95% (2.95% base rate plus the applicable margin of 4.00%). The Interest Rate Cap does not have a floor rate. The Interest Rate Collar will have a floor rate of 2.90% and a ceiling rate of 4.00% and be based upon LIBOR plus an applicable margin of 4.00%.

The maturity dates and other significant terms of the Interest Rate Cap and Interest Rate Collar match those of the underlying indebtedness. The Interest Rate Cap and Interest Rate Collar are designated as cash flow hedges, and are highly effective hedges of the interest rate risk. Any changes in the fair value of the cash flow hedges are deferred and not recognized until the hedged transactions are recorded in income. The fair value of the Interest Rate Cap and Interest Rate Collar were approximately $800 at December 31, 2005.

**7. Debt (continued)**

*The Subordinated Notes*

The Subordinated Notes (the "Notes") were issued pursuant to a note indenture dated as of February 8, 2005 (the "Note Indenture") and are denominated in Canadian dollars with an aggregate principal amount of C$90.4 million. Interest on the Notes accrues at the rate of 14.5% per annum and the Notes are due on February 8, 2017. Interest on the Notes is payable monthly, and commenced on March 15, 2005. On or after the fifth anniversary of the issuance of the Notes, the Company may redeem the Notes for the principal amount plus a premium that declines over time.

Prior to the fifth anniversary of the closing of the IPS Offering, Keystone Newport ULC will be permitted, at its election, to defer interest payments on the Notes, if and for so long as the Interest Coverage Ratio (as defined in the Note Indenture), of the Company for the most recent twelve-month period ending on the last day of any month, is less than the Interest Deferral Threshold (as defined in the Note Indenture), unless a default in payment of interest, principal or premium, if any, on the Notes has occurred and is continuing, or any other Event of Default (as defined in the Note Indenture) with respect to the Notes has occurred and is continuing and the Notes have been accelerated as a result of the occurrence of such Event of Default (any such period, an "Interest Deferral Period"). Interest payments on the Notes will not be deferred under this provision for more than 24 months in the aggregate or beyond the fifth anniversary of the closing of the IPS Offering.

In addition, after the fifth anniversary of the closing of the IPS Offering, Keystone Newport ULC may at its election, defer interest on the Notes on not more than eight occasions for not more than eight months per occasion (each, an "Interest Deferral Period") by delivering to the Trustee (as defined in the Note Indenture) a copy of a resolution of Keystone Newport ULC's board of directors certified by an officer's certificate of Keystone Newport ULC to the effect that, based upon a good faith determination of Keystone Newport ULC's board of directors, such deferral is reasonably necessary for *bona fide* cash management purposes, or to reduce the likelihood of, or avoid a default on, any Senior Indebtedness (as defined in the Note Indenture); provided no such deferral may be commenced and any ongoing deferral shall cease, if a default in payment of interest, principal or premium, if any, on the Notes has occurred and is continuing or any other Event of Default with respect to the Notes has occurred and is continuing and the Notes have been accelerated as a result of the occurrence of such Event of Default. No Interest Deferral Period may commence unless and until all interest deferred pursuant to any preceding Interest Deferral Period, together with interest thereon, has been paid in full.

**7. Debt (continued)**

Deferred interest on the Notes will bear interest at the same rate as the stated rate on the Notes, compounded monthly, until paid in full. Following the end of any Interest Deferral Period, Keystone Newport ULC will be obligated to resume monthly payments of interest on the Notes, including interest on deferred interest. All interest deferred prior to the fifth anniversary of the closing of the IPS Offering, including interest accrued on deferred interest, must be repaid on the fifth anniversary of the closing of the IPS Offering. All interest deferred after the fifth anniversary of the closing of the IPS Offering, including interest accrued on deferred interest, must be repaid on or before maturity, provided that Keystone Newport ULC must pay all deferred interest and accrued interest thereon in full prior to deferring interest on a subsequent occasion. Keystone Newport ULC may prepay all or part of the deferred interest, at any time other than during an Interest Deferral Period.

During any Interest Deferral Period, or so long as any deferred interest remains unpaid, and under other circumstances described below, the Company will not be permitted to pay any dividends or make any distribution to holders of its Common Shares, or make certain other restricted payments. The Credit Agreement contains limitations on the Company's ability to make distributions to Keystone Newport ULC to enable it to prepay deferred interest on the Notes.

*Obligations Due to Former Owners and Former Employees*

Notes payable to former owners represent notes issued by Keystone in connection with its prior acquisitions of various businesses. Keystone also entered into consulting and noncompetition agreements (generally for ten years) with former owners and former key employees of acquired funeral homes and cemeteries.

In the event of liquidation of the Company, payment of principal and interest on indebtedness to the former owners and former employees are subordinate to the payment of any senior debt of the Company. Proceeds of approximately $16,000 from the IPS Offering were invested into marketable securities accounts to satisfy these former owner and employee obligations that existed as of the closing of the IPS Offering date as they come due in future years through 2018. These amounts are carried on the balance sheet as restricted investments and have been discounted at their net present value based on the corresponding interest rates of the restricted investments estimated at approximately 3%.

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

## 8. Common Shares

On February 8, 2005, the Company issued 17,100,000 Common Shares for net proceeds of $71.4 million (C$89.3 million) as part of the IPS Offering. On February 17, 2005, the over-allotment option was exercised resulting in the issuance of 1,668,017 Common Shares for net proceeds of $6.9 million (C$8.4 million).

## 9. Minority Interest

Minority interest at December 31, 2005 represents the Class B common shares of Keystone retained by the existing investors in Keystone upon the closing of the IPS Offering and the exercise of the over-allotment option. The Class B common shares represent a 6.3% interest in Keystone at December 31, 2005. Each Class B common share entitles the holder to receive distributions from Keystone approximately equivalent to the distributions per IPS received by holders of IPSs. Two years from the date of closing of the IPS Offering, the holders of the Class B common shares of Keystone have the right to request that Keystone enter into good faith negotiations to repurchase their shares. Also at the two year anniversary, dividends are to be paid to Class B share holders at a rate of 1.1 times the dividend per share to which the holders of the Class A common shares are entitled. Keystone has the right to purchase for cancellation the Class B common shares in certain circumstances.

## 10. Preneed Receivables and Funds

Preneed receivables and funds represent receivables due from customers, trust funds and other non-insurance accounts related to unperformed, prearranged funeral contracts. The components of preneed receivables and funds in the consolidated balance sheets are as follows:

| | |
|---|---|
| Funeral trust fund receivables | $ 41,922 |
| Cemetery trust fund receivables | 1,731 |
| | 42,982 |
| Cemetery preneed customer receivables due to trusts | 118 |
| | $ 43,100 |

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

**10. Preneed Receivables and Funds (continued)**

Trust funds held by third parties become available to the Company when the related merchandise and services have been delivered. Amounts due from funeral and cemetery trust funds consist of investments with fixed and floating rates and equity securities as follows:

| | Book Value | Fair Value |
|---|---|---|
| Cash and term deposits | $ 37,119 | $ 37,119 |
| Bonds | 247 | 246 |
| Equities | 1,307 | 1,337 |
| Equity mutual funds | 4,309 | 4,239 |
| | $ 42,982 | $ 42,941 |

The Company considers various factors when considering if a decline in fair value of an asset is other than temporary, including but not limited to the length of time and magnitude of the unrealized loss; the volatility of the investment; the credit ratings of the issuers of the investments; and the Company's intentions to sell or ability to hold the investments. At December 31, 2005 the Company has concluded that the declines in the fair values of the Company 's investments in bonds, equities and equity mutual funds are temporary.

Preneed funeral contracts funded through life insurance policies purchased by the customer and issued by third party insurers are not reflected as assets or liabilities in the financial statements.

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

## 11. Income Taxes

The tax provision for continuing operations reported in the consolidated financial statements for the period from February 8, 2005 to December 31, 2005 is made up of the following components:

| | |
|---|---|
| Federal: | |
| Current | $ – |
| Deferred | 2,354 |
| State: | |
| Current | 188 |
| Deferred | 535 |
| Total provision | 3,077 |
| Less: provision from discontinued operations | 45 |
| Provision from continuing operations | $ 3,032 |

The difference between the effective rate reflected in the provision for income taxes and the amount determined by applying the statutory rate to income before income taxes for the period February 8, 2005 to December 31, 2005 is analyzed below:

| | |
|---|---|
| Tax at U.S. statutory rate | $ 2,385 |
| State taxes, net of federal benefit | 658 |
| Other | 34 |
| | $ 3,077 |

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

**11. Income Taxes (continued)**

The components of future income tax balances are as follows:

| | |
|---|---|
| Future tax liabilities: | |
| Property and equipment | $ (5,184) |
| Tradenames | (6,905) |
| Goodwill | (1,016) |
| Foreign currency exchange contracts | (1,816) |
| Total future tax liabilities | $ (14,921) |
| | |
| Future tax assets: | |
| Covenants not to compete | $ 2,278 |
| Acquisition related transition costs | 164 |
| Allowance for doubtful accounts | 705 |
| Net operating loss carry-forward | 1,515 |
| Accrued expenses | 702 |
| Deferred revenue / commissions | 974 |
| Other | 41 |
| Gross future tax assets | 6,379 |
| Less: Valuation allowance | (76) |
| Total future tax assets | 6,303 |
| Total net future tax liabilities | $ (8,618) |

Net future tax assets (liabilities) are classified as:

| | |
|---|---|
| Current | $ 2,308 |
| Noncurrent | (10,926) |
| | $ (8,618) |

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

**11. Income Taxes (continued)**

Generally accepted accounting principles require a valuation allowance to reduce the future tax assets reported if, based on the weight of the evidence, it is more likely than not that some portion or all of the future tax assets will not be realized. After consideration of all the evidence, both positive and negative, management has determined that a valuation allowance of $76 is necessary at December 31, 2005. This valuation allowance relates to state net operating losses in certain state and local tax jurisdictions that may not be utilized before they expire.

Keystone North America, Inc. has a federal net operating loss carry-forward for tax purposes of $4.1 million as of December 31, 2005. This federal net operating loss carry-forward will expire in 2025. The company also has state net operating loss carry-forwards of $2.9 million as of December 31, 2005. These state net operating loss carry-forward amounts will expire between 2010 and 2025.

**12. Foreign Currency Exchange Contracts**

Keystone has entered into foreign currency exchange flat forward contracts (the "Forward Contracts"). The Canadian dollars will be used to fund interest and dividend distributions to the IPS unit and separate subordinate note holders. Keystone was not required to deposit any collateral with regard to these contracts. At December 31, 2005 the Company had the following Forward Contracts outstanding:

| Contract Dates | # Contracts | US$ to be delivered monthly | C$ to be received monthly | C$ per US$ |
|---|---|---|---|---|
| Jan 2006-Feb 2010 | 50 | $1,361 | $1,670 | 1.2272 |
| Mar 2010-May 2010 | 3 | $1,361 | $1,663 | 1.2225 |
| Jun 2010-Aug 2010 | 3 | $1,443 | $1,670 | 1.1570 |
| Sept 2010-Nov 2010 | 3 | $1,473 | $1,663 | 1.1330 |
| Dec 2010-Feb 2011 | 3 | $1,443 | $1,617 | 1.1202 |

The Forward Contracts do not qualify as hedges for accounting purposes and the change in the fair value of the Forward Contracts is recorded in income. The fair value of the Forward Contracts was $4,627 at December 31, 2005, of which $1,030 is recorded in other current assets.

*(000's of U.S. Dollars, except percentages, share amounts and where the context requires)*

The Forward Contracts have been entered into with a major Canadian bank as counterparty. The risk associated with the Forward Contracts is the cost of replacing these instruments in the event of default by the counterparty. Management believes that this risk is remote.

**13. Retirement Plan**

Keystone has a defined contribution plan for the benefit of its employees. Total expense recognized by Keystone related to this plan for the period from February 8, 2005 to December 31, 2005 was $102.

**14. Lease Commitments**

The leases for certain funeral home facilities contain contingent rental provisions based upon revenues of the related firms to be adjusted annually.

The Company leases certain facilities, vehicles and other equipment under operating leases. Rent expense was $2,315 for the period from February 8, 2005 to December 31, 2005.

The following represents the future minimum lease payments under the operating leases:

| | |
|---|---|
| Year ending December 31: | |
| 2006 | $ 2,203 |
| 2007 | 1,859 |
| 2008 | 1,479 |
| 2009 | 920 |
| 2010 | 548 |
| Thereafter | 1,665 |
| | $ 13,173 |

**15. Contingencies**

The Company is a party to various litigation matters, investigations and proceedings. For each of its outstanding legal matters, the Company evaluates the merits of the case, its exposure to the matter, possible legal or settlement strategies and the likelihood of an unfavorable outcome. If the Company determines that an unfavorable outcome is probable and can be reasonably estimated, it establishes the necessary accruals. Certain insurance policies held by the Company may reduce cash outflows with respect to an adverse outcome of certain of these litigation matters.

**16. Subsequent Events**

In March of 2006, the Company acquired a funeral home in Iowa for cash proceeds of $975, deferred cash proceeds of $25 and seller financing of approximately $150.

In March of 2006, the Company acquired three funeral homes and a cemetery in Indiana in exchange for two of its funeral homes in Missouri, three funeral homes in California and paid $540 in cash.

# EXHIBIT D

KEYSTONE

Keystone North America Inc.

Third Quarter Report
September 30, 2006

KEYSTONE

# Keystone North America Inc.

## Management's Discussion and Analysis of Financial Condition and Results of Operations

### Three Months and Nine Months Ended September 30, 2006

*The following management discussion and analysis of the financial condition and results of operations of Keystone North America Inc. (the "Company") is supplemental to, and should be read in conjunction with the consolidated financial statements of the Company for the period ended September 30, 2006 and with the consolidated financial statements and Management's Discussion and Analysis of the Company for the period ended December 31, 2005. Additional information regarding the Company, including copies of our continuous disclosure materials such as our Annual Information Form dated March 24, 2006, is available through the SEDAR website at www.sedar.com. The Company's financial statements are prepared in accordance with accounting principles generally accepted in Canada ("GAAP"). The information in this Management's Discussion and Analysis of the Financial Condition and Results of Operations is effective as of November 8, 2006. Substantially all of the Company's operating cash flows are in U.S. dollars, accordingly, all amounts presented herein are stated in U.S. dollars, unless indicated otherwise.*

## FORWARD LOOKING STATEMENTS

Certain statements in this Management's Discussion and Analysis are "forward-looking statements", which reflect the expectations of management regarding the Company's future growth, results of operations, performance and business prospects and opportunities. These forward-looking statements reflect management's current reasonable expectations regarding future events and operating performance and speak only as of September 30, 2006. Forward-looking statements involve significant risks and uncertainties, should not be read as guarantees of future performance or results, and will not necessarily be accurate indications of whether or not or the times at or by which such performance or results will be achieved. A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements including, among others, those factors set out in the "Risk Factors" section of the Company's Annual Information Form dated March 24, 2006, which factors are incorporated herein by reference. However, the risk factors set out therein are not exhaustive of the factors that may affect any of the Company's forward-looking statements. Although the forward-looking statements contained in this Management's Discussion and Analysis are based upon what management believes to be reasonable assumptions, investors cannot be assured that actual results will be consistent with these forward-looking statements, and the differences may be material. These assumptions, which include, management's current expectations, estimates and assumptions about the markets the Company operates in, mix of funeral services, interest rates, exchange rates and the Company's ability to attract and retain customers and to manage its assets and operating costs, may prove to be incorrect. Further information regarding these and other factors is included in the Company's public filings with Canadian securities regulatory authorities. These forward-looking statements are made as of the date of this Management Discussion and Analysis and, except as otherwise required by law, the Company assumes no obligation to update or revise them to reflect new events or circumstances.

## DEFINITION OF EBITDA AND DISTRIBUTABLE CASH

References to ''EBITDA'' are to earnings before interest, taxes, depreciation, amortization and certain other adjustments listed in the reconciliation table provided herein. References to "Distributable Cash" are to EBITDA, as adjusted for: capital expenditures, interest on the senior credit facility, interest on other loans, interest on the separate subordinated notes, proceeds from debt (equipment financing), payments on debt, proceeds from investments, cash taxes and Class B distributions declared. EBITDA and Distributable Cash are not recognized measures under GAAP and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Distributable Cash may not be comparable to similar measures presented by other issuers. Management believes that EBITDA and Distributable Cash are important measures in evaluating the Company's performance because the Company intends to distribute substantially all of its cash on an ongoing basis. Distributable Cash is not intended to be representative of cash flow or results of operations determined in accordance with GAAP.

## PRESENTATION OF FINANCIAL INFORMATION

The Company began operations on February 8, 2005, the same day as the Company and Keystone Newport ULC ("Keystone ULC") completed an initial public offering of income participating securities ("IPSs"). The period ended September 30, 2005 includes only 235 days of operations. Comparisons to historical periods are therefore difficult. In addition, at the time of the Company's initial public offering, it acquired two distinct businesses: Keystone Group Holdings, Inc. ("Keystone") and certain assets, liabilities and stock of certain subsidiaries of HFSC Holdings, Inc. ("Hamilton").

In order to enhance its usefulness, this Management Discussion and Analysis includes a summary of the operating results of the Company for the 235-day period subsequent to the public offering of IPSs and for the period from January 1, 2005 through February 7, 2005 of Keystone and Hamilton on a pro forma combined basis to arrive at pro forma combined operating results for the nine month period ended September 30, 2005. These pro forma combined results have been compared to the actual operating results of the Company for the nine month period ended September 30, 2006. As a portion of the period is prior to the purchase by the Company of Keystone and Hamilton, this information is provided for reference purposes only, and is not intended as a comprehensive comparison of financial results. The 2005 pro forma combined results do not consider the pro forma effects of any acquisitions subsequent to the acquisition of Keystone and Hamilton.

Readers are cautioned that as a result of the initial public offering, the operating results for periods prior to February 8, 2005 may not necessarily be indicative of the revenues and expenses that would have resulted had the Company operated on a combined basis during these periods.

## General

The Company is the fifth largest provider of funeral services in the United States with 177 funeral homes and 10 cemeteries as of the effective date of this Management Discussion and Analysis. The Company's funeral homes are located in 27 states and the province of Ontario as of September 30, 2006.

The funeral and cemetery industry in the United States generates an estimated $15 billion in total revenues annually. The primary market drivers of the funeral industry are local heritage, the total mortality of a local service area and the mix of business between cremation and burial.

The Company's funeral homes have historically provided a full range of funeral services on both an at-need (at time of death) and preneed basis (prior to death). These services include removal of human remains, planning and coordinating personalized funerals and cremations, professional embalming, use of our funeral home facilities, merchandise sales, conducting memorial services, performing cremation and cemetery interment services.

Corporate, general and administrative expenses primarily include costs associated with the Company's corporate office in Tampa, Florida. As the Company continues to implement its business and growth strategies, it expects that there will be a modest increase in general and administrative expenses. However, because these expense increases will be incurred in connection with an increase in its revenue base, the Company anticipates that the expense increases will be relatively smaller, as a percentage of revenues, as it realizes economies of scale and the costs are spread over a larger revenue base.

Income from operations for the nine-month period ended September 30, 2006 trailed the pro forma combined results for the same period of the prior year due to a lower volume of funeral services performed by same store locations and higher corporate costs. This is partially offset by income from operations generated by new acquisitions. Income from operations for the three-month period ended September 30, 2006 exceed the results for the same period of the prior year due to the performance of firms acquired in 2006. Based on internal and external data management has assembled, total deaths in our markets appear to have decreased for the nine-month period ended September 30, 2006 compared to the nine-month period ended September 30, 2005. Based on management's experience, total deaths often occur in cyclical trends such as this.

The Company posted a net loss for the quarter of $0.7 million and net income for the nine-month period ended September 30, 2006 of $0.3 million. The net loss for the quarter includes an unrealized loss on derivative contracts of $1.1 million. The net income for the nine month period ended September 30, 2006 includes an unrealized gain on derivative contracts of $1.8 million, representing the change in market value of those contracts for the period.

Management remains confident of the Company's ability to meet the anticipated annual distribution target of C$1.00 per IPS.

There is a seasonal component to the operation of a funeral business. Case volume, revenue and, as a result, cash flows are typically higher in the first and fourth quarters. To illustrate the significance of the seasonal component to our business, we have provided the following pro forma combined seasonal data for the past five years:

**Percentage of Annual EBITDA generated by Quarter**
**Pro Forma Combined before consideration of Corporate, General and Administrative Expenses**

| Trailing Twelve Months Ended | Q1 | Q2 | Q3 | Q4 | Q2 & Q3 | Q1 &Q4 |
|---|---|---|---|---|---|---|
| December 31, 2001 | 28.0% | 24.6% | 21.2% | 26.2% | 45.8% | 54.2% |
| December 31, 2002 | 29.9% | 23.1% | 22.0% | 25.0% | 45.1% | 54.9% |
| December 31, 2003 | 27.0% | 23.0% | 22.7% | 27.3% | 45.7% | 54.3% |
| December 31, 2004 | 30.4% | 21.0% | 22.8% | 25.8% | 43.8% | 56.2% |
| December 31, 2005 | 31.7% | 22.5% | 20.6% | 25.2% | 43.1% | 56.9% |
| **Average** | **29.4%** | **22.8%** | **21.9%** | **25.9%** | **44.7%** | **55.3%** |

As demonstrated in the table above, the funeral homes during the second and third quarters generate, on average, approximately 11% less EBITDA than the first and fourth quarters due to decreased case volume.

Based on seasonality, the first nine months of 2006 are generally consistent with past trends of EBITDA before consideration of Corporate, General and Administrative Expenses (after eliminating the effects of new acquisitions). The third quarter of 2006 was consistent with the historical seasonality trend.

## Results of Operations (in 000's of US$, except per share data and where the context requires)

| | Three Months Ended September 30, 2005 | Three Months Ended September 30, 2006 | Pro forma Combined 38 Days 1/1/05-2/7/05 (Note 1) | 235 Days 2/8/05-9/30/05 | Nine Months Ended September 30, Pro forma Combined 2005 (Note 1) | Nine Months Ended September 30, 2006 |
|---|---|---|---|---|---|---|
| Revenues | $19,442 | $22,017 | $9,558 | $53,062 | $62,620 | $65,796 |
| Costs and expenses | | | | | | |
| Costs and expenses | 13,042 | 14,795 | 6,044 | 34,363 | 40,407 | 43,342 |
| Corporate, general and administrative | 1,455 | 2,049 | 653 | 3,639 | 4,292 | 5,770 |
| Depreciation | 708 | 749 | 356 | 1,655 | 2,011 | 2,169 |
| Amortization and other | 745 | 697 | 287 | 2,074 | 2,361 | 2,482 |
| Total operating expenses | 15,950 | 18,290 | 7,340 | 41,731 | 49,071 | 53,763 |
| Income from operations | $3,492 | $3,727 | $2,218 | $11,331 | $13,549 | $12,033 |
| Interest expense | 3,961 | 4,070 | | 10,154 | | 12,391 |
| Unrealized gain (loss) on derivative contracts | 4,056 | (1,060) | | 5,385 | | 1,787 |
| Other income | 7 | 648 | | 320 | | 1,370 |
| Income (loss) from continuing operations before income taxes and minority interest | 3,594 | (755) | | 6,882 | | 2,799 |
| Income tax expense (benefit) | 1,422 | (293) | | 2,730 | | 1,210 |
| Minority interest | 137 | 135 | | 262 | | 590 |
| Net income (loss) from continuing operations | 2,035 | (597) | | 3,890 | | 999 |
| Net income (loss) from discontinued operations | (96) | (132) | | 128 | | (707) |
| Net income (loss) | $1,939 | $(729) | | $4,018 | | $292 |
| Basic and diluted net income (loss) from continuing operations | $ 0.11 | $ (0.03) | | $ 0.21 | | $ 0.05 |
| Basic and diluted net income (loss) from discontinued operations | $ (0.01) | $ (0.01) | | $ 0.01 | | $ (0.04) |
| Basic and diluted net income (loss) per share | $ 0.10 | $ (0.04) | | $ 0.21 | | $ 0.02 |

*Note 1: Results for all periods prior to February 8, 2005 are based on combined, pro forma same funeral home operating results as presented in internally prepared financial statements for Keystone and Hamilton. These amounts do not include pro forma adjustments for the change in treatment of consulting and non-compete payments expensed in the Hamilton historical financial statements.*

**Distributable Cash Summary (in 000's of US$, except per share data and where the context requires)**

| | Three Months Ended September 30, 2006 | Nine Months Ended September 30, 2006 |
|---|---|---|
| Net income (loss) | $(729) | $292 |
| Adjustments: | | |
| Depreciation | 749 | 2,169 |
| Amortization | 697 | 2,482 |
| Interest expense | 4,070 | 12,391 |
| Unrealized loss (gain) on derivative contracts | 1,060 | (1,787) |
| Income tax expense (benefit) | (293) | 1,210 |
| Minority interest | 135 | 590 |
| Loss from disposals | 163 | 202 |
| Discontinued operations EBITDA adjustments | (97) | 636 |
| **EBITDA** (Note 2) | **$5,755** | **$18,185** |
| Adjustments: | | |
| Capital expenditures for property and equipment | (1,267) | (2,606) |
| Revolving facility draw for land purchase | 700 | 700 |
| Proceeds from debt | 109 | 606 |
| Payments on long term debt | (1,145) | (3,298) |
| Proceeds from restricted investments | 926 | 3,004 |
| Interest on other loans | (77) | (338) |
| Interest on senior credit facility | (876) | (2,628) |
| Interest on separate subordinated notes | (323) | (960) |
| Class B distributions declared | (284) | (847) |
| Cash taxes recovered (paid) | (59) | 717 |
| **Distributable cash US$** (Notes 2 and 3) | **$3,459** | **$12,535** |
| Average rate of C$ to US$ | 1.122 | 1.133 |
| **Distributable cash C$** | **$3,880** | **$14,199** |
| **Per IPS unit in C$** | **$ 0.21** | **$ 0.76** |
| | | |
| Interest accrued on IPS units in C$ | 2,916 | 8,748 |
| Declared dividends on IPS units in C$ | 1,776 | 5,328 |
| **Total IPS distributions in C$** | **$4,692** | **$14,076** |
| **Per IPS unit in C$** | **$ 0.25** | **$ 0.75** |

*Note 2- EBITDA and Distributable Cash are not recognized measures under generally accepted accounting principles ("GAAP") and do not have standardized meanings prescribed by GAAP. Therefore, EBITDA and Distributable Cash may not be comparable to similar measures presented by other issuers. The Company intends to distribute substantially all of its cash on an ongoing basis, management believes that EBITDA and Distributable Cash are important measures in evaluating the Company's performance. Distributable Cash is not intended to be representative of cash flow or results of operations determined in accordance with GAAP. Management believes that Distributable Cash is a useful financial measure as it provides investors with an indication of cash available for distribution and is a measure generally used by Canadian income funds as an indicator of financial performance. The Company's method of determining distributable cash is derived from EBITDA, which in turn is derived from net earnings, a measure recognized under GAAP. Average rates used represent the average market rates of Canadian currency per US$1 over the periods presented.*

*Note 3-* ***Reconciliation of cash from operating activities to distributable cash:***

| | Three Months Ended September 30, 2006 | Nine Months Ended September 30, 2006 |
|---|---|---|
| **Cash from operating activities** | **$2,133** | **$8,148** |
| Capital expenditures of property and equipment | (1,267) | (2,606) |
| Revolving facility draw for land purchase | 700 | 700 |
| Proceeds from debt | 109 | 606 |
| Payments on long term debt | (1,145) | (3,298) |
| Proceeds from investments | 926 | 3,004 |
| Current tax expense | 40 | 98 |
| Non-cash interest expense | 192 | 742 |
| Class B distributions declared | (284) | (847) |
| Changes in working capital | (486) | (2,453) |
| IPS unit interest | 2,600 | 7,724 |
| Cash taxes recovered (paid) | (59) | 717 |
| **Distributable cash** | **$3,459** | **$12,535** |

*Nine Months Ended September 30, 2006*

- Revenues totaled $65.8 million
- Cost and expenses totaled $43.3 million or 65.9% of revenues
- Corporate, general and administrative expenses totaled $5.8 million or 8.8% of revenues
- Depreciation and amortization totaled $4.7 million
- Interest expense totaled $12.4 million
- Unrealized gains on derivative contracts totaled $1.8 million
- Income tax expense totaled $1.2 million
- Minority interest was $0.6 million

The unrealized gain on derivative contracts of $1.8 million relates to changes in the fair value of the outstanding foreign currency exchange contracts and interest rate swap agreements. The Company does not intend to liquidate the contracts, as it would expose future distributions to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar and expose the Company to market fluctuations in the interest rates applied to its Term Loan. The change in market value of the contracts does not impact the cash flows of the Company or the ability of the Company to make cash distributions.

**Acquisitions**

The Company acquired nine funeral homes and four cemeteries during the first nine months of 2006. The operating results of these acquisitions have been included since their respective acquisition dates. Although management anticipates the acquisitions to be accretive in future periods, the cash flow impact to the nine months ended September 30, 2006 was limited because the acquisitions were completed throughout the year.

The net purchase price of these acquisitions was approximately $15.5 million, which consisted of the transfer of ownership of five funeral homes and net cash of $10.5 million. The preliminary allocation of the purchase price to the fair value of assets acquired and liabilities assumed is as follows (in thousands):

| | |
|---|---|
| Current assets, less current liabilities | $ 3,240 |
| Property and equipment | 8,041 |
| Preneed receivables and funds | 13,118 |
| Cemetery care funds | 2,735 |
| Intangible assets | 3,594 |
| Long-term debt | (2,459) |
| Deferred revenue | (9,190) |
| Non-controlling interest in preneed funds | (6,871) |
| Non-controlling interest in cemetery care funds | (2,735) |
| Subtotal | 9,473 |
| Goodwill | 6,065 |
| Total | $ 15,538 |

The preliminary allocation of the purchase price is based on preliminary internal management and third-party valuations. The purchase price allocation may change upon final determination of the fair value of assets acquired and liabilities assumed. Intangible assets represent covenants not to compete of $1.5 million that are amortized over the life of the agreements and tradenames of $2.0 million with indefinite lives. Approximately $4.0 million of goodwill will be deductible for tax purposes.

**Dispositions**

The Company disposed of four funeral homes and three cemeteries during 2005 and seven funeral homes during the first nine months of 2006.

The operating results of these dispositions are shown as results from discontinued operations on the statements of operations. Summarized operating results for the periods from February 8, 2005 to September 30, 2005 and the first nine months of 2006 are as follows (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Revenues | $ 671 | $ 3,581 |
| Costs and expenses | 757 | 2,944 |
| Gross profit | (86) | 637 |
| Other expenses | 621 | 509 |
| Income (loss) from discontinued operations | $ (707) | $ 128 |

The value of total assets disposed in the first nine months of 2006 was approximately $9.2 million. The value of total liabilities disposed in first nine months of 2006 was approximately $4.0 million. The total value of goodwill dispositions in the first nine months of 2006 was a combined $2.2 million. The total value of tradenames and non-compete agreements dispositions in the first nine months of 2006 was a combined $0.9 million and $0.2 million, respectively.

The value of total assets disposed in the first nine months of 2005 was approximately $0.8 million. The value of total liabilities disposed in first nine months of 2005 was approximately $42,000. The total value of goodwill dispositions in the first nine months of 2005 was a combined $0.1 million. The total value of tradenames and non-compete agreements dispositions in the first nine months of 2005 was a combined $0.1 million and $40,000, respectively.

**Distributable Cash**

Distributable Cash for the nine month period ended September 30, 2006 was C$14.2 million (US$12.5 million) or C$0.76 per unit, which exceeded distributions declared by C$0.1 million. The excess Distributable Cash can be attributed to the higher case volume from a seasonally strong period and the recovery of previous paid taxes offset by certain corporate expenses. Management intends to retain excess distributable cash to fund working capital needs of the company. The shortage in distributable cash for the quarter was funded via distributable cash reserves generated during the first six months of the year.

***Comparison of the three month period ended September 30, 2006 to the results for the three month period ended September 30, 2005***

*Revenues:* Revenues for the third quarter of fiscal year 2006 were $22.0 million compared to revenues of $19.4 million for the third quarter of fiscal year 2005, representing an increase of $2.6 million, or 13.2%. Acquisitions closed in 2006 contributed $1.6 million in revenues in the third quarter. As a result of these acquisitions, the number of funeral services performed increased from 3,718 during the third quarter of 2005 to 3,901 in the third quarter of 2006, an increase of 4.9%. Additionally, the average revenue per funeral service increased from $4,808 in the third quarter of 2005 to $5,078 in the third quarter of 2006, a $270 or 5.6% increase. The number of funeral services performed by same store locations decreased by 64 from the prior quarter of 2005. Management believes, based on its information gathered internally combined with available external resources, that total deaths in our markets are down from the prior period and the decrease in services performed is not indicative of a loss of market share for the Company as a whole.

The funeral service industry is subject to seasonal variations in deaths with historically higher revenues and cash flows in the winter months. The third quarter of the year has traditionally been the weakest period of the year for the Company.

*Cost and expenses:* Cost and expenses for the third quarter of fiscal 2006 were $14.8 million, 67.2% of revenues, compared to $13.0 million, 67.1% of revenues, for the third quarter of 2005, an increase of $1.8 million. Costs and expenses as a percent of revenues are consistent over the periods. The increase in gross dollars can be attributed to the new acquisitions that generated $1.1 million (67.0% of revenues) in additional cost and expenses during the quarter and inflationary increases year over year in cost items such as merchandise and labor.

The principal elements of the cost and expenses include direct salaries and wages and costs of goods sold. These two significant categories comprise 33% and 14% of third quarter 2006 revenues, respectively and historically they represent approximately the same percentage of revenues over time.

*Corporate, general and administrative expense:* Corporate, general and administrative expense was $2.0 million for the third quarter of 2006 compared to $1.5 million for the third quarter of 2005. The primary increase is attributable to expense recorded on board approved incentive plans; this totaled $0.3 million during the third quarter. The remaining increase is attributable to accounting and legal services rendered in connection with acquisitions, dispositions and operating a public company.

*Depreciation expense:* Depreciation expense was $0.7 million for both the third quarter of 2006 and the third quarter of 2005.

*Amortization and other expense:* Amortization and other expense was $0.7 million for both the third quarter of 2006 and the third quarter of 2005. Amortization expense represents the amortization of covenants not to compete.

*Income from operations:* Income from operations was $3.7 million for the third quarter of 2006 and $3.5 million for the third quarter of 2005, an increase of $0.2 million primarily to the net effect of items noted above.

*Interest expense:* Interest expense was $4.1 million for the third quarter of 2006 and $4.0 million for the third quarter of 2005. The increase is attributed to the interest paid on the additional senior facility draws partially offset by rate savings related to the completed refinancing.

*Unrealized gain (loss) on derivative contracts:* The unrealized loss on derivative contracts for the third quarter of 2006 was $1.1 million compared to an unrealized gain of $4.1 million for the third quarter of 2005. Unrealized gain (loss) on derivative contracts relates to changes in the fair value of the outstanding foreign currency exchange contracts and interest rate swap agreements.

*Other income:* Other income was $0.6 million for the third quarter of 2006. Other income consists primarily of realized translation gains or losses, interest income, rental income and trust income.

*Income (loss) from continuing operations before income taxes and minority interest:* Loss from continuing operations before income taxes and minority interest was $0.8 million for the third quarter of 2006 and income of $3.6 million for the third quarter of 2005, a decrease of $4.3 million primarily to the net effect of the items noted above.

*Income tax expense (benefit):* Income tax benefit was $0.3 million for the third quarter of 2006 and expense of $1.4 million for the third quarter of 2005. Income tax expense (benefit) is calculated based on the income (loss) from continuing operations before income taxes and minority interest for the period.

*Minority interest:* Minority interest for both the third quarter of 2006 and the third quarter of 2005 was $0.1 million. These amounts represent the minority portion of the consolidated loss before minority interest and interest expense associated with the IPS units.

*Net income (loss) from continuing operations:* Net loss from continuing operations was $0.6 million for the third quarter of 2006 and net income from continuing operations was $2.0 million for the third quarter of 2005, a decrease of $2.6 million primarily to the net effect of the items noted above.

*Net loss from discontinued operations:* Net loss from discontinued operations was $0.1 million for both the third quarter of 2006 and the third quarter of 2005. This loss represents the net of the operations, loss on disposition, and related taxes attributed to all discontinued operations for the periods presented.

*Net income (loss):* Net loss for the third quarter of 2006 was $0.7 million and net income for the third quarter of 2005 was $1.9 million, a decrease of $2.7 million primarily to the net effect of the items noted above.

***Comparison of the nine month period ended September 30, 2006 to the pro forma combined results for the nine month period ended September 30, 2005***

*Revenues:* Revenues for the first nine months of fiscal year 2006 were $65.8 million compared to pro forma combined revenues of $62.6 million for the first nine months of fiscal year 2005, representing an increase of $3.2 million, or 5.1%. Acquisitions closed in 2006 contributed $3.5 million in revenues through the first nine months of 2006. This increase in new acquisition revenue was offset by a decrease in revenue in the same homes held year over year. The number of services performed decreased from 12,069 during the pro forma combined first nine months of 2005 to 11,877 in the first nine months of 2006, a decrease of 192 or 1.6%. This decrease in services was offset by an increase in the average revenue per funeral service from $4,855 per service in the pro forma combined first nine months of 2005 to $5,059 in the first nine months of 2006, a $204 or 4.2% increase. Management believes, based on its information gathered internally combined with available external resources, that total deaths in our markets are down from the prior period and the decrease in services performed is not indicative of a loss of market share for the Company as a whole.

The funeral service industry is subject to seasonal variations in deaths with historically higher revenues and cash flows in the winter months.

*Cost and expenses:* Cost and expenses for the first nine months of fiscal 2006 were $43.3 million, 65.9% of revenues, compared to $40.4 million, 64.5% of revenues, for the pro forma combined first nine months of 2005, an increase of $2.9 million. The increase as a percent of revenue is due to the number of services being down at the homes owned year over year and replacing those services with new acquisitions and their fully loaded costs. The new acquisitions generated $2.3 million (66.4% of revenues) in additional cost and expenses during the first nine months of 2006.

The principal elements of the cost and expenses include direct salaries and wages and costs of goods sold. These two significant categories comprise 32% and 14% of first nine months 2006 revenues, respectively and historically they represent approximately the same percentage of revenues over time.

*Corporate, general and administrative expense:* Corporate, general and administrative expense was $5.8 million for the first nine months of 2006 compared to $4.3 million for the pro forma combined first nine months of 2005. The increase is primarily attributable to costs incurred in relation to accounting and legal services rendered in connection with operating a public company and acquisitions. Additionally, expense of $0.3 million was recorded during the third quarter on board approved incentive plans. Management anticipates that its 2006 annual overhead will exceed the original anticipated $6.7 million.

*Depreciation expense:* Depreciation expense was $2.2 million for the first nine months of 2006 and $2.0 million for the pro forma combined first nine months of 2005. This increase can be attributed to depreciation expense recorded on the fixed assets of the acquisitions.

*Amortization and other expense:* Amortization and other expense was $2.5 million for the first nine months of 2006 compared to $2.4 million for the pro forma combined first nine months of 2005, an increase of $0.1 million. Amortization expense represents the amortization of covenants not to compete.

*Income from operations:* Income from operations was $12.0 million for the first nine months of 2006 compared to income from operations of $13.5 million for the pro forma combined first nine months of 2005, a decrease of $1.5 million due primarily to the net effect of items noted above.

**Outstanding Share Data**

At September 30, 2006, the Company had 18,768,017 IPSs outstanding. Each IPS represents one Common Share of the Company, and C$4.286 principal amount of 14.5% Subordinated Notes.

**Liquidity and Capital Resources**

At September 30, 2006, debt under the senior credit facilities was $50.3 million, with $22.7 million in borrowings available for acquisitions and working capital purposes under the revolving credit facility. There was $7.2 million drawn and outstanding on the revolving credit facility at September 30, 2006. These draws were to fund acquisitions. The Company also has a letter of credit of $0.1 million, which reduces the funds available under the revolving credit facility, in order to conduct insurance business in various states. In addition, at September 30, 2006, outstanding debt included $11.6 million in notes payable to former owners, obligations under covenants not to compete, obligations under consulting agreements and amounts owing under equipment financing contracts, and $80.9 million in Subordinated Notes and Separate Subordinated Notes. The senior credit facilities have a maturity date of February 8, 2011, while the Subordinated Notes and Separate Subordinated Notes have a 12-year term and are due and payable on February 8, 2017. The notes payable to former owners, obligations under covenants not to compete, obligations under consulting agreements and amounts owing under equipment financing contracts have various maturity dates through the fiscal year 2026.

On April 21, 2006, the Company finalized an amendment to its senior credit facilities to (i) provide for an additional $15 million in capacity, (ii) reduce the interest rate by 200 basis points with an additional 50 basis point reduction contingent on achieving certain covenant levels, (iii) extend the term from February 8, 2008 to February 8, 2011 and (iv) allow for favorable adjustments to certain debt covenant ratios.

In conjunction with the senior credit facilities amendment, the Company also entered into an agreement to convert its existing two-year collar, which capped interest rates on $43.1 million at 8.0% to a four-year interest rate swap fixing interest rates at 6.68%. Management estimates the annual net interest savings of the rate reduction and the swap based on current outstanding amounts under the facility is estimated at approximately US$669,000.

The Company determines its dividend declarations (which it intends to pay in equal monthly amounts) based on periodic reviews of its estimated annual earnings and related estimated annual cash flows. The Company expects to remain in a position to continue distributions of C$0.08333333 per IPS per month. A portion of that distribution represents interest on the Subordinated Notes with the remainder representing a dividend on the Common Shares.

### Commitments and Contractual Obligations

Contractual obligations and commitments principally include obligations associated with outstanding indebtedness and lease obligations. The following table shows contractual obligations and commitments related to outstanding indebtedness as of September 30, 2006 and the related payment by period due. Maturities of long-term debt are as follows (in 000's):

| | | Year Ending December 31, | | | | | |
|---|---|---|---|---|---|---|---|
| | September 30, 2006 | 2006 | 2007 | 2008 | 2009 | 2010 | Thereafter |
| Term Loan Facility | $ 43,100 | $ - | $ - | $ - | $ - | $ - | $ 43,100 |
| Revolving Loan Facility | 7,200 | - | - | - | - | - | 7,200 |
| Equipment Financing | 990 | 59 | 247 | 191 | 173 | 99 | 221 |
| Due to Former Owners and Employees | 10,597 | 726 | 3,158 | 2,608 | 1,405 | 619 | 2,081 |
| Subordinated Debt | 80,916 | - | - | - | - | - | 80,916 |
| | $142,803 | $785 | $3,405 | $2,799 | $1,578 | $ 718 | $133,518 |

The Company expects to be able to renew or refinance the various loan facilities as they become due at then current market rates. Capital expenditures were $2.6 million for the nine month period ended September 30, 2006, this includes a parcel of land that was purchased by drawing $0.7 million on the revolving credit facility. Capital expenditures historically include those required to maintain and upgrade existing infrastructure, including the replacement of furnishings, automobiles and routine maintenance to existing building structures and the surrounding landscape. Management anticipates an annual capital expenditure level of $2.9 million. Management in certain instances finances capital expenditure items in order to spread the cash impact over time and more closely associate the use of cash with the benefit of the capital expenditures. During the first nine months of 2006, management financed $0.6 million of capital expenditure items.

The Company has no off-balance sheet debt or similar obligations. The Company has arrangements under which customers purchase insurance policies, which are assigned to the Company at the time of death. The Company does not have control of these policies and is obligated to deliver services at a fixed price only if the insurance policy proceeds are delivered.

### Quantitative and Qualitative Disclosures About Market Risk

In the normal course of business, the Company is exposed to market risks arising from adverse changes in interest rates and the C$/US$ foreign currency exchange rate. Market risk is defined for these purposes as the potential change in the fair market value of financial assets and liabilities resulting from an adverse movement in these rates.

As of September 30, 2006, the Company's material variable rate borrowings included outstanding borrowings under the senior credit facilities. Upon amending the senior credit facilities, the Company put in place an interest rate swap agreement. The notional amount of the interest rate swap agreement equals the outstanding term loan and, in accordance with the terms of the interest rate swap agreement, limits the interest rate on the outstanding term loan amount. As of September 30, 2006, the Company had $43.1 million in outstanding indebtedness related to the term loan facility and $7.2 million in outstanding indebtedness related to the revolving credit facility. Without considering the effect of the interest rate swap, a 100 basis point increase in interest rates, applied to these borrowings as of September 30, 2006, would result in an annual increase in interest expense and a corresponding reduction in cash flow of approximately $0.5 million.

The Company is exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar because the anticipated distributions from Keystone to the Company and Keystone ULC will be paid in U.S. dollars and the anticipated distributions on the IPSs and Separate Subordinated Notes will be paid in Canadian dollars. In order to minimize the impact of fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar, the Company has entered into Canadian dollar/U.S. dollar exchange contracts for the total amount of anticipated IPS distributions and Separate Subordinated Note interest payments. The agreements consist of monthly forward foreign exchange contracts. Under the terms of the contracts, the Company receives approximately $1.7 million Canadian dollars on or around the 14th day of each month. It is management's intention to continue to roll forward these contracts on a quarterly basis as they expire; however, such extensions will be at the discretion of the board of directors.

As of September 30, 2006, the following contracts remain open:

- 41 contracts through February 2010 at $1.2272 Canadian dollar/U.S. dollar
- 3 contracts from March 2010 through May 2010 at $1.2225 Canadian dollar/U.S. dollar
- 3 contracts from June 2010 through August 2010 at $1.1570 Canadian dollar/U.S. dollar
- 3 contracts from September 2010 through November 2010 at $1.1330 Canadian dollar/U.S. dollar
- 3 contracts from December 2010 through February 2011 at $1.1202 Canadian dollar/U.S. dollar
- 3 contracts from March 2011 through May 2011 at $1.0805 Canadian dollar/U.S. dollar
- 3 contracts from June 2011 through August 2011 at $1.0750 Canadian dollar/U.S. dollar
- 3 contracts from September 2011 through November 2011 at $1.0695 Canadian dollar/U.S. dollar

At September 30, 2006, the Company's open forward currency exchange contracts had a market value totaling $6.9 million. If the Company had liquidated the contracts, it would be exposed to fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar with respect to distributions on the IPSs. Such fluctuations in the value of the foreign currency exchange contracts have no adverse impact on current cash flows of the Company and enhance the ability of the Company to continue distributions despite short-term market volatility in the exchange rate. Given the long-term maturity horizon of Canadian denominated obligations, due in 2017, there is no short term impact to cash flows from changes in the notional value of the subordinated notes due to changes in the exchange rate.

**Critical Accounting Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Some of the estimates and assumptions management is required to make relate to matters that are inherently uncertain as they pertain to future events. Management bases these estimates on historical experience and on various other assumptions that it believes to be reasonable and appropriate. Actual results may differ significantly from these estimates.

Management believes that certain of the Company's accounting policies require subjective and complex judgments and could potentially have a material effect on reported financial condition and results of operations. For a full description of the Company's accounting policies, see our Audited Annual Financial Statements dated March 27, 2006, which can be found at www.sedar.com. There were no changes during the quarter.

**Risk Factors**

See our Company's Annual Information Form dated March 24, 2006, which factors are incorporated herein by reference which can be found at www.sedar.com, for a full description of the Company's risk factors. There were no changes during the quarter.

**Outlook**

The first nine months of 2006 saw the Company's distributable cash exceed its distribution requirements. Additionally, new acquisitions have increased revenues over the prior year totals despite lower case volume in existing markets. Management believes that the total number of deaths was down from the exceptionally strong prior year, which moderated growth. Management does not believe the fundamental assumptions have changed and there is no change to our business plan. Management expects acquisitions to continue to be accretive from a distributable cash standpoint and expects to continue to realize significant savings from the senior credit facility amendment.

The funeral service industry is subject to seasonal variations with historically higher revenues in the winter months. Management does not anticipate any significant changes to these trends for the final quarter of fiscal year 2006 or further into the future.

The Company's monthly distribution rate of C$0.08333333 per IPS unit was established at the time of its IPS Offering and was, in large part, based upon the historical results for Keystone and Hamilton (adjusted for certain factors in connection with the change in capital structure, the additional expenses incurred as a result of being a reporting issuer, and synergies anticipated from the business combination). Management remains confident in the Company's business model and ability to meet the anticipated annual distribution target of C$1.00 per IPS.

**Additional Information**

Additional information relating to the Company, including the financial statements for the period ended September 30, 2006 is available on SEDAR at www.sedar.com. Readers may also obtain information by visiting our new investor website at http://www.keystonenorthamerica.ca/.

KEYSTONE

# Keystone North America Inc.

## Consolidated Financial Statements

## For the Three and Nine Months Ended September 30, 2006

Keystone North America Inc.

Unaudited Consolidated Financial Statements

September 30, 2006

## Contents

Keystone North America Inc.

Unaudited Consolidated Balance Sheets
(000's of U.S. Dollars)

| | | As at September 30, 2006 | | As at December 31, 2005 |
|---|---|---|---|---|
| **Assets** | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | $ | **3,092** | $ | 6,614 |
| Marketable securities | | **188** | | 350 |
| Restricted short-term investments | | **3,615** | | 3,331 |
| Trade receivables, less allowances for doubtful accounts of $1,738 and $1,795 at September 30, 2006 and December 31, 2005, respectively | | **7,448** | | 7,350 |
| Inventories | | **5,989** | | 3,816 |
| Income tax receivable | | **-** | | 1,102 |
| Prepaid and other current assets | | **2,819** | | 2,564 |
| Future income taxes | | **2,087** | | 2,308 |
| Total current assets | | **25,238** | | 27,435 |
| Preneed receivables and funds | | **52,389** | | 43,100 |
| Restricted cemetery care funds | | **3,312** | | 552 |
| Restricted long-term investments | | **5,385** | | 8,525 |
| Property and equipment, net | | **73,961** | | 67,546 |
| Goodwill | | **90,343** | | 86,741 |
| Tradenames | | **25,877** | | 24,652 |
| Covenants not to compete, less accumulated amortization of $4,487 and $2,898 at September 30, 2006 and December 31, 2005, respectively | | **10,544** | | 11,713 |
| Derivative contracts | | **5,508** | | 3,597 |
| Other assets | | **6,815** | | 7,653 |
| Total assets | $ | **299,372** | $ | 281,514 |

*See accompanying notes.*

Keystone North America Inc.

Unaudited Consolidated Balance Sheets
(000's of U.S. Dollars)

| | As at September 30, 2006 | As at December 31, 2005 |
|---|---|---|
| **Liabilities and shareholders' equity** | | |
| Current liabilities: | | |
| Accounts payable and accrued expenses | $ **6,906** | $ 7,532 |
| Dividends payable | **624** | 599 |
| Current maturities of long-term debt (Note 6) | **3,464** | 3,491 |
| Total current liabilities | **10,994** | 11,622 |
| | | |
| Deferred revenue | **15,155** | 6,461 |
| Long-term debt (Note 6) | **139,339** | 129,605 |
| Future income taxes | **13,248** | 10,926 |
| Other long-term liabilities | **415** | 84 |
| | | |
| Non-controlling interests in preneed funds | **43,656** | 41,251 |
| Non-controlling interests in cemetery care funds | **3,312** | 552 |
| Minority interest | **9,203** | 9,513 |
| | | |
| Shareholders' equity: | | |
| Share capital | **78,312** | 78,312 |
| Accumulated deficit | **(6,495)** | (2,114) |
| Cumulative currency translation adjustments | **(7,767)** | (4,698) |
| Total shareholders' equity | **64,050** | 71,500 |
| Total liabilities and shareholders' equity | $ **299,372** | $ 281,514 |

*See accompanying notes.*

Keystone North America Inc.

Unaudited Consolidated Statements of Operations and Retained Earnings (Accumulated Deficit )
(000's of U.S. Dollars – except per share amounts)

| | Three months ended September 30, 2006 | Three months ended September 30, 2005 | Nine months ended September 30, 2006 | Period from February 8, 2005 to September 30, 2005 |
|---|---|---|---|---|
| Revenues: | | | | |
| Funeral services | $ 20,792 | $ 18,455 | $ 62,255 | $ 50,583 |
| Other | 1,225 | 987 | 3,541 | 2,479 |
| Total revenues | 22,017 | 19,442 | 65,796 | 53,062 |
| Costs and expenses | 14,795 | 13,042 | 43,342 | 34,363 |
| Gross profit | 7,222 | 6,400 | 22,454 | 18,699 |
| Other operating expenses: | | | | |
| Corporate, general and administrative expenses | 2,049 | 1,455 | 5,770 | 3,639 |
| Depreciation | 749 | 708 | 2,169 | 1,655 |
| Amortization | 697 | 745 | 2,482 | 2,074 |
| Income from operations | 3,727 | 3,492 | 12,033 | 11,331 |
| Interest expense | 4,070 | 3,961 | 12,391 | 10,154 |
| Unrealized gain (loss) on derivative contracts | (1,060) | 4,056 | 1,787 | 5,385 |
| Other income | 648 | 7 | 1,370 | 320 |
| Income (loss) from continuing operations before income taxes and minority interest | (755) | 3,594 | 2,799 | 6,882 |
| Income tax expense (benefit) | (293) | 1,422 | 1,210 | 2,730 |
| Minority interest | 135 | 137 | 590 | 262 |
| Net income (loss) from continuing operations | (597) | 2,035 | 999 | 3,890 |
| Net income (loss) from discontinued operations (Note 5) | (132) | (96) | (707) | 128 |
| Net income (loss) | (729) | 1,939 | 292 | 4,018 |
| (Accumulated deficit) – beginning of period | (4,212) | (182) | (2,114) | - |
| Dividends | 1,554 | 1,482 | 4,673 | 3,743 |
| Retained earnings (accumulated deficit) – end of period | $ (6,495) | $ 275 | $ (6,495) | $ 275 |
| Weighted average number of shares outstanding | 18,768,017 | 18,768,017 | 18,768,017 | 18,768,017 |
| Basic and diluted net income (loss) from continuing operations | $ (0.03) | $ 0.11 | $ 0.05 | $ 0.21 |
| Basic and diluted net income (loss) from discontinued operations | $ (0.01) | $ (0.01) | $ (0.04) | $ 0.01 |
| Basic and diluted net income (loss) per common share | $ (0.04) | $ 0.10 | $ 0.02 | $ 0.21 |

*See accompanying notes.*

Keystone North America Inc.

Unaudited Consolidated Statements of Cash Flows
(000's of U.S. Dollars)

| | Three months ended September 30, 2006 | Three months ended September 30, 2005 | Nine months ended September 30, 2006 | Period from February 8, 2005 to September 30, 2005 |
|---|---|---|---|---|
| Operating activities: | | | | |
| Net income (loss) | $ (729) | $ 1,939 | $ 292 | $ 4,018 |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: | | | | |
| Minority interest | 127 | 130 | 543 | 270 |
| Provision for future income taxes (benefit) | (424) | 2,130 | 1,755 | 3,772 |
| Unrealized loss (gain) on derivative contracts | 1,060 | (4,056) | (1,787) | (5,385) |
| Amortization expense | 699 | 778 | 2,503 | 2,188 |
| Depreciation expense | 751 | 766 | 2,187 | 1,769 |
| Loss on sale of businesses and assets | 163 | 274 | 202 | 274 |
| Changes in operating assets and liabilities | 486 | (609) | 2,453 | 1,526 |
| *Net cash provided by operating activities* | 2,133 | 1,352 | 8,148 | 8,432 |
| Investing activities: | | | | |
| Business acquisitions, net of cash acquired | (2,019) | - | (10,508) | (153,415) |
| Purchase of Class B Minority Interest Shares related to the exercise of the over-allotment option | - | - | - | (12,692) |
| Purchases of property and equipment | (1,267) | (658) | (2,606) | (1,413) |
| Proceeds from dispositions of businesses | 197 | 645 | 197 | 645 |
| Cash paid for transition costs | (23) | (221) | (673) | (2,728) |
| Proceeds from restricted investments | 926 | 1,238 | 3,004 | 3,789 |
| Proceeds invested to fund indebtedness to former owners and employees | - | - | - | (16,393) |
| *Net cash provided by (used in) investing activities* | (2,186) | 1,004 | (10,586) | (182,207) |
| Financing activities: | | | | |
| Initial public offering and over-allotment proceeds of common shares, net of expenses | - | - | - | 78,312 |
| Initial public offering and over-allotment proceeds of 14.5% Subordinated Notes, net of expenses | - | - | - | 64,492 |
| Issuance of 14.5% Separate Subordinated Notes, net of expenses | - | - | - | 8,005 |
| Proceeds from new credit facility | 2,200 | - | 7,200 | 43,100 |
| Deferred financing costs | - | - | (403) | (8,085) |
| Borrowings on long-term debt | 109 | - | 606 | 43 |
| Payments on long-term debt | (1,145) | (1,085) | (3,298) | (3,350) |
| Cash paid for Class A dividends | (1,449) | (1,457) | (4,346) | (3,237) |
| Cash paid for Class B dividends | (284) | (263) | (843) | (583) |
| *Net cash provided by (used in) financing activities* | (569) | (2,805) | (1,084) | 178,697 |
| *Net increase (decrease) in cash* | (622) | (449) | (3,522) | 4,922 |
| Cash and cash equivalents, beginning of period | 3,714 | 5,371 | 6,614 | - |
| Cash and cash equivalents, end of the period | $ 3,092 | $ 4,922 | $ 3,092 | $ 4,922 |
| **Supplement disclosure of cash flow information:** | | | | |
| Cash paid for interest | $ 3,832 | $ 3,941 | $ 11,223 | $ 8,909 |
| Cash paid (recovered) for income taxes | $ 59 | $ 93 | $ (717) | $ 743 |

*See accompanying notes.*

Keystone North America Inc.

Notes to the Unaudited Consolidated Financial Statements

September 30, 2006

**1. General**

Keystone North America Inc. (the "Company") was incorporated on August 27, 2004 under the laws of the Province of Ontario. The Company's authorized capital consists of an unlimited number of common shares ("Common Shares") and an unlimited number of Class A preferred shares. No Class A preferred shares have been issued. Holders of Common Shares are entitled to receive dividends as and when declared by the board of directors and are entitled to one vote per Common Share on all matters to be voted on at all meetings of shareholders of the Company. From August 27, 2004 to February 8, 2005, the Company was inactive. The Company and its indirect subsidiary, Keystone Newport ULC (together, the "Issuer"), completed an initial public offering (the "IPS Offering") on February 8, 2005. Each Income Participating Share ("IPS") consists of one Common Share and C$4.286 principal amount of 14.5% subordinated notes of Keystone Newport ULC ("Subordinated Notes").

Concurrent with the IPS Offering, Keystone Newport ULC issued, on a private placement basis, $8.1 million (C$10 million) of separate 14.5% subordinated notes (the "Separate Subordinated Notes" and together with the Subordinated Notes, the "Notes") and the Issuer, through a subsidiary, entered into a bank credit facility (the "Credit Agreement") with a group of lenders consisting of a $43.1 million term loan and a $15 million revolving credit commitment (together with the IPS Offering, the "IPS Transactions"). In connection with the IPS Offering, $43.1 million was drawn on the Credit Agreement. The credit agreement has since been amended which increased the revolving credit commitment to $30 million (see Note 6).

These interim consolidated financial statements present the results of operations of the Company for the three and nine month periods ended September 30, 2006 compared with the results of operations for the three month period ended September 30, 2005 and from the close of the IPS Offering on February 8, 2005 to September 30, 2005, respectively.

**2. Basis of Presentation**

The unaudited interim consolidated financial statements of the Company contain all adjustments, consisting only of normal recurring adjustments, which, in the opinion of management, are necessary for a fair presentation of the results for the interim period presented. The financial statement results for the interim periods presented are not necessarily indicative of financial results for the full year. The Company's operations are subject to seasonality and industry experience indicates that slightly more deaths occur between December and March, which management attributes to seasonal variation due to adverse weather and certain illnesses that generally occur during the winter months. These unaudited interim consolidated financial

**2. Basis of Presentation (continued)**

statements include the accounts of the Company and its subsidiaries. All significant intercompany transactions and balances have been eliminated upon consolidation. These unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada for interim financial statements and do not contain all of the disclosures required for annual financial statements. As a result, these financial statements should be read in conjunction with the Company's most recent financial statements dated December 31, 2005. These interim financial statements follow the same accounting policies and methods of application as the most recent annual financial statements.

*Reclassifications*

Certain 2005 revenues and expenses have been reclassified from other income to other revenue to conform with the 2006 presentation.

*Derivative Contracts*

The Company records the fair value of their interest rate swap and foreign currency forward contracts on the balance sheets in derivative contracts and records the change in fair value of the unsettled contracts in the statements of operations as unrealized gain/loss on derivative contracts.

**3. Acquisitions in 2005**

In conjunction with the acquisition of assets, liabilities and stock of certain subsidiaries, the Company established a reserve for transition and other costs to eliminate a corporate office and certain associated corporate administrative functions. The costs anticipated in this reserve included severance and termination costs of personnel and other assumed liabilities. In the first nine months of 2006, the total liability decreased by approximately $0.7 million as a result of cash payments for anticipated items. The accrual was reduced by approximately $0.4 million when the Company revised the estimate of anticipated income tax liabilities. The adjustment reduced Goodwill.

**4. Acquisitions in 2006**

The Company acquired nine funeral homes and four cemeteries during the first nine months of 2006. The operating results of these acquisitions have been included since their respective dates of acquisition. The following funeral homes and cemeteries were acquired:

**4. Acquisitions in 2006 (continued)**

| Dates Acquired | Name | Location | Entity |
|---|---|---|---|
| March 10, 2006 | Lange | Iowa | Funeral Home |
| March 14, 2006 | Roselawn Group | Indiana | Cemetery and Funeral Homes |
| April 1, 2006 | Lahaie Group | Ontario | Funeral Homes |
| April 10, 2006 | Green | Connecticut | Funeral Home |
| September 12, 2006 | Missouri Group | Missouri | Cemeteries and Funeral Homes |

The net purchase price of these acquisitions was approximately $15.5 million, which consisted of the transfer of ownership of five funeral homes (see Note 5) and net cash of $10.5 million. The preliminary allocation of the purchase price to the fair value of assets acquired and liabilities assumed is as follows (in thousands):

| | |
|---|---|
| Current assets, less current liabilities | $ 3,240 |
| Property and equipment | 8,041 |
| Preneed receivables and funds | 13,118 |
| Cemetery care funds | 2,735 |
| Intangible assets | 3,594 |
| Long-term debt | (2,459) |
| Deferred revenue | (9,190) |
| Non-controlling interest in preneed funds | (6,871) |
| Non-controlling interest in cemetery care funds | (2,735) |
| Subtotal | 9,473 |
| Goodwill | 6,065 |
| Total | $ 15,538 |

The preliminary allocation of the purchase price is based on preliminary internal management and third-party valuations. The purchase price allocation may change upon final determination of the fair value of assets acquired and liabilities assumed. Intangible assets represent covenants not to compete of $1.5 million that are amortized over the life of the agreements and tradenames of $2.0 million with indefinite lives. Approximately $4.0 million of goodwill will be deductible for tax purposes.

**5. Discontinued Operations**

The Company disposed of four funeral homes and three cemeteries during 2005 and seven funeral homes during the first nine months of 2006.

The operating results of these dispositions are shown as results from discontinued operations on the statements of operations. Summarized operating results for the periods from February 8, 2005 to September 30, 2005 and the first nine months of 2006 are as follows (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Revenues | $ 671 | $ 3,581 |
| Costs and expenses | 757 | 2,944 |
| Gross profit | (86) | 637 |
| Depreciation | 17 | 114 |
| Amortization | 20 | 115 |
| Interest expense | 3 | 12 |
| Other income (expense) | (1) | 24 |
| Income tax expense (benefit) | (50) | 167 |
| Minority interest | (47) | 8 |
| Income (loss) from discontinued operations | (30) | 245 |
| Loss on disposal of discontinued operations, net of tax expense | (677) | (117) |
| Income (loss) from discontinued operations | $ (707) | $ 128 |

The transaction on March 14, 2006 consisted of the exchange of five funeral homes and approximately $500,000 in cash for three funeral homes and a cemetery. The transaction was valued at the fair market value, which was approximately $5.5 million, and resulted in a gain on disposition of approximately $186,000. The gain was offset by tax expense largely related to the disposal of goodwill not deductible for tax purposes.

The value of total assets disposed in the first nine months of 2006 was approximately $9.2 million. The value of total liabilities disposed in first nine months of 2006 was approximately $4.0 million. The total value of goodwill dispositions in the first nine months of 2006 was a combined $2.2 million. The total value of tradenames and non-compete agreements dispositions in the first nine months of 2006 was a combined $0.9 million and $0.2 million, respectively.

The value of total assets disposed in the first nine months of 2005 was approximately $0.8 million. The value of total liabilities disposed in first nine months of 2005 was approximately $42,000. The total value of goodwill dispositions in the first nine months of 2005 was a combined $0.1 million. The total value of tradenames and non-compete agreements dispositions in the first nine months of 2005 was a combined $0.1 million and $40,000, respectively.

## 6. Debt

*Amended Credit Agreement*

In February 2005, the Company entered into a credit agreement in connection with the IPS Offering that included a $43.1 million term loan facility and a $15 million revolving loan facility. On April 21, 2006, the Company amended the credit agreement to (i) provide for an additional $15 million of capacity under the revolving loan facility, (ii) extend the Revolving Credit Termination Date and Term Loan Maturity Date as defined therein three years from February 8, 2008 to February 8, 2011, and (iii) secured an interest rate reduction (applicable margin reduction) of 200 basis points with an additional 25 basis point reduction contingent upon the leverage ratio.

Borrowings under the new Credit Agreement may be Base Rate Loans or Eurodollar Loans, as defined in the Credit Agreement. Base Rate Loans bear interest at the Base Rate, as defined in the Credit Agreement (8.25% at September 30, 2006), plus the applicable margin, which ranges from 0.25% to 0.75% depending on Keystone's leverage ratio on the pricing date. Eurodollar Loans bear interest at the Adjusted LIBOR Rate, as defined in the Credit Agreement (5.37% at September 30, 2006), plus the applicable margin, which ranges from 1.75% to 2.25% depending on the Company's leverage ratio on the pricing date (2.00% at September 30, 2006). The Company has an interest rate swap agreement that fixes LIBOR at 4.68%, which, including the applicable margin, yields an effective rate of 6.68% on $43.1 million notional amount of debt. Borrowings under the Credit Agreement are collateralized by assets of the Company and its U.S. domestic subsidiaries, and certain shares of the capital stock of the Company and the capital stock of each of its subsidiaries. In addition, payment and performance of the obligations under the Credit Agreement are guaranteed by each of the Company's U.S. subsidiaries. The Credit Agreement contains various covenants that, among other things, require the Company to maintain certain defined leverage and coverage ratios. The credit agreement has a term loan maturity date of February 8, 2011, at which time the entire principal balance and all accrued interest shall mature and become due.

Indebtedness of the Company at September 30, 2006 includes the following:

| | Current | Long-Term |
|---|---|---|
| Subordinated notes | $ – | $ 80,916 |
| Term loan facility | – | 43,100 |
| Revolving loan facility | – | 7,200 |
| Obligations under covenants not to compete | 2,103 | 3,763 |
| Notes payable to former owners | 1,022 | 3,277 |
| Obligations under consulting agreements | 100 | 332 |
| Equipment financing | 239 | 751 |
| | $ 3,464 | $139,339 |

**6. Debt (continued)**

Maturities of long-term debt are as follows:

| | Term Loan Facility | Revolving Loan Facility | Equipment Financing | Due to Former Owners & Employees | Subordinated Notes |
|---|---|---|---|---|---|
| Year ending December 31: | | | | | |
| 2006 (10/1/2006 to 12/31/2006) | $ – | $ – | $ 59 | $ 726 | $ – |
| 2007 | – | – | 247 | 3,158 | – |
| 2008 | – | – | 191 | 2,608 | – |
| 2009 | – | – | 173 | 1,405 | – |
| 2010 | – | – | 99 | 619 | – |
| Thereafter | 43,100 | 7,200 | 221 | 2,081 | 80,916 |
| | $ 43,100 | $ 7,200 | $ 990 | $ 10,597 | $ 80,916 |

*Subordinated Notes and Separate Subordinated Notes*

The Subordinated Notes issued as part of the IPSs, along with the Separate Subordinated Notes are unsecured obligations of Keystone ULC, guaranteed by Keystone Group Holdings and each of its subsidiaries on an unsecured basis pursuant to guarantees that were entered into by each of the guarantor subsidiaries at the time of the IPS Offering.

In April 2006, the Company formed a subsidiary, Keystone Canada Funeral Homes Inc. ("KCFH"). KCFH acquired the Lahaie group in April 2006. KCFH has not guaranteed Keystone ULC's obligations under the Notes. The consolidated financial statements of the Company include the financial results of KCFH. Summary consolidating financial information of both the guarantor and non-guarantor subsidiaries of the Issuer for the nine months ended September 30, 2006 is as follows:

**6. Debt (continued)**

| | Keystone ULC | Keystone North America and Guarantor Subsidiaries | Non-Guarantor Subsidiaries Combined | Total Consolidated Amounts |
|---|---|---|---|---|
| Revenue | $ - | $ 64,997 | $ 799 | $ 65,796 |
| Income from operations | - | 11,827 | 206 | 12,033 |
| Net income (loss) | (8,383) | 8,489 | 186 | 292 |
| Current assets | - | 24,443 | 795 | 25,238 |
| Non-current assets, excluding preneed funds | 5,176 | 214,331 | 7,659 | 227,166 |
| Current liabilities | 978 | 9,957 | 59 | 10,994 |
| Non-current liabilities, excluding minority interest and preneed interests | 80,916 | 79,546 | 7,695 | 168,157 |

**7. Retirement Plan**

The Company has a defined contribution plan for the benefit of its employees. Total expense recognized by the Company related to this plan for the three months and nine months ended September 30, 2006 was approximately $31,000 and $95,000, respectively.

**8. Subsequent Event**

On October 31, 2006, the Company entered into a contingent asset sale agreement to acquire eight funeral home and four cemetery businesses for the purchase price of $13.6 million. The agreement is contingent upon the satisfaction by the seller of certain conditions, including the completion of the pending combination of Service Corporation International (SCI) and Alderwoods Group Inc., US Federal Trade Commission (FTC) approval and other closing conditions typical for transactions of this nature.