

Brooke Corporation

DESCRIPTION OF BUSINESS

Nature of the Business

The Company engages primarily in the business of selling insurance and related services through franchisees. More specifically, most of the Company's revenues are currently derived from sales commissions on the sale of property and casualty insurance policies through its franchisees, although an increasing share of revenues are derived from consulting, lending and brokerage services provided to franchisees.

Franchisor Activities

The Company sells insurance and related services through franchisees that are local business owners because the Company's philosophy emphasizes the motivation provided to salespersons by business ownership. The Company's primary mission is to make local business ownership, especially insurance agency ownership, more attainable, more valuable and more liquid. Therefore, the Company makes loans to franchisees to acquire insurance agencies and consults with franchisees on the buying and selling of insurance agencies. The Company has expanded its franchise, consulting and lending activities to other services that overlap with insurance sales such as financial services and funeral services. Funeral Services, for example, involve the sales of pre-need or final expense insurance policies in addition to the sales of funeral services, cemetery services, pre-need trust accounts and pre-planned but unfunded funeral services.

For an initial franchise fee and a share of sales commissions or other revenues, the Company provides franchisor services to its franchisees in accordance with a franchise program pioneered by the Company. A basic premise of the Company's franchise program is that franchisees must outsource certain processing activities to a franchisor that can generate sufficient economies of scale to reduce administrative expenses, increase franchisees' productivity and increase availability of credit to franchisees by preserving lenders' collateral. Franchisor processing services provided by the Company to franchisees include cash management, document management and personal management. In addition to processing services, as franchisor, the Company also provides marketing assistance to franchisees. Marketing assistance includes supplier access and branding.

Facilitator Activities

The Company believes that insurance and related services are distributed more efficiently by local owners than by employees of large corporations because the success of these types of businesses generally depends on motivated sales persons. As such, the Company believes that business ownership, with the associated opportunity for wealth creation from building a business, is the ultimate tool for rewarding performance and motivating sales persons. As such, the Company assists franchisees and others in the acquisition of insurance and related businesses. Because these services facilitate the transfer of ownership, the Company refers to them as facilitator activities. Facilitator activities are generally divided into either lending, which is performed by the

Company's finance subsidiary, or consulting, which is performed by the Company's franchise subsidiary.

Brokerage Activities

The Company engages in insurance brokerage as another way to generate additional revenues from its franchising activities without additional costs to its franchisees by providing brokerage services that would otherwise be provided by a third party. Brokerage activities generally include writing insurance for those that are difficult to insure, creating insurance programs and sharing underwriting risks with insurance companies through the Company's Bermuda based subsidiaries.

Business History

The Company was incorporated under the laws of the State of Kansas on January 17, 1986, under the name of Brooke Financial Services, Inc. The Company subsequently amended its articles of incorporation, changing its name to Brooke Corporation. The Company is controlled by Brooke Holdings, Inc., which owned approximately 64.62% of the outstanding common stock of the Company as of February 29, 2004.

In the early years of the Company's operations, the Company sold its services primarily to community bank insurance agencies. However, the community bank market was limited because only the smallest banks were authorized to sell insurance, and community bankers were often not committed to insurance sales. Therefore, the Company began focusing on the sale of its services to independent insurance agents not affiliated with community banks.

In 1996, the Company adopted a "franchise" approach to expansion and developed a lending program for insurance agency acquisitions by franchisees. From 1996 to 1999, the Company spent significant resources researching and developing the processing standards and marketing plans described herein, which represent the foundation of the Company's franchise program. During this period of time, the Company also rewrote its document management and commissions reconciliation software to accommodate these processing standards and began to present document images and commission statements on the Company's web site. Since 1999, the Company has maintained a web site at www.brookecorp.com, which provides general information about the Company and hyperlinks to other related web sites. In addition, the Company maintains a web site at www.brookeprocessing.com, which the Company utilizes to provide document images and revenue information to its franchisees. The contents of such web sites (including any web site connected by hyperlink) are not incorporated into this Annual Report by reference.

In 1996, the Company leased space to establish a processing center in Phillipsburg, Kansas, and in 2002 acquired a property for renovation into a new processing center facility with increased office space and improved security.

In 1998, the Company established a national office in Overland Park, Kansas, to support the activities of the Company's state offices and to office the Company's legal, lending and consulting professionals. In 2000, a regional office approach was adopted to consolidate state office facilities and regional offices were established in the Kansas City, Missouri; Dallas, Texas; Denver,

Colorado and Nashville, Tennessee metropolitan areas. In 2003, a new regional office was established in Sacramento, California.

In 2001, customer service centers were opened in Dallas and Brownsville, Texas, to assist insurance agent franchisees, for an additional fee, in the servicing of their clients. In 2002, additional customer service centers were opened in Omaha, Nebraska; Las Vegas, Nevada; Tarpon Springs, Florida; and Phoenix, Arizona. In 2003, an additional customer service center was opened in Lake City, Florida.

Also in 2000, the Company elected to register its common stock under Section 12(g) of the Securities Exchange Act of 1934, as amended. This registration, and resulting reporting company status, enabled the Company to obtain a listing on the American Stock Exchange in 2003.

To facilitate ownership transfers, the Company established a lending division in 1996 under the name of Brooke Credit Corporation and consulting divisions in 2001 under the trade names of “Agency Business Consultants” and “Heritage Agency Consultants.”

During 2002, the Company began to tailor its franchise disclosures to accommodate franchisee specialization in businesses related to general insurance sales. As such, the Company developed a franchise specialty in financial services in 2002 and franchise specialties in funeral services and auto insurance services in 2003. Funeral specialists franchisees specialize in the sales of funeral services, cemetery services, pre-need or final expense insurance policies, pre-need trust accounts and/or pre-planned but unfunded funeral services. Auto insurance services franchisees specialize in the sale of auto insurance policies, particularly the sale of insurance to drivers with a higher risk profile.

During 2002, the Company acquired Bornstein Financial Group which is a life health agency that specializes in senior market sales and coordinates senior workshops for franchisees specializing in financial services.

The Company significantly expanded its property and casualty insurance brokerage operations in 2002 with the acquisition of CJD & Associates, LLC, which does business as Davidson-Babcock, and again in 2003 with the acquisition of Texas All Risk General Agency, Inc. Davidson-Babcock and Texas All Risk General Agency are property casualty general agencies. As a result of the CJD & Associates acquisition, the Company operates underwriting offices in Overland Park, Kansas and Omaha, Nebraska. As a result of the Texas All Risk General Agency, Inc. acquisition, the Company operates underwriting offices in Dallas, Texas and Springhill, Louisiana.

During 2003, the Company’s finance company subsidiary completed its first two securitizations of insurance agency loans. This represented a significant development in the Company’s capacity to fund loans.

Business Strategy

The Company believes that locally owned and operated businesses represent an increasingly popular means for distributing certain insurance and related services and that the Company's franchise concept will become increasingly important to the future success of those franchisees. As such, the Company expects the demand for its franchise services to grow. Accordingly, if locally owned and operated businesses become a more popular means for distributing insurance and related services, then demand for the Company's ancillary products, such as facilitator and brokerage services, should grow correspondingly.

The Company, through its franchise company subsidiary, is a franchisor that provides services in accordance with the franchise concept pioneered by the Company for the sale of insurance and related services through locally owned franchisees. Franchising is the foundation of the Company's business strategy. The Company is expanding its business by extending its franchise services to franchisees that specialize in businesses that overlap with general insurance sales including financial services, funeral services and auto insurance services. The Company is also expanding its business by increasing the geographical area that it serves.

The Company's consulting activities are relatively profitable and an important component of the Company's business strategy. The Company consults with business sellers and acquires businesses for sale to its franchisees. The Company regularly prospects for agencies for sale and operates a web site called agencies4sale.com. The contents of such web site (including any web site connected by hyperlink) are not incorporated into this Annual Report by reference. Also, many franchisees have not purchased a business before and rely on the Company to assist them during ownership transition. To do this, the Company provides a Buyers Assistance Plan ("BAP") that provides specific consulting assistance to franchisee purchasers such as: (1) inspection reports, (2) operational reports, (3) expanded training at the Brooke Academy, and (4) access to specialized marketing departments.

The Company's lending activities are also relatively profitable. Franchisee access to business acquisition loans is an important component of the Company's business strategy. The Company sells its loans to lenders as loan participation interests or as asset backed securities. The Company's strategy is to continue to grow its lender network to ensure adequate lending capacity. The Company also plans to continue securitizing a portion of its loan portfolio to help ensure adequate lending capacity.

To capitalize on the Company's franchising and lending expertise, the Company's strategy includes the eventual offering of franchises in commercial loan brokerage. The Company plans to fund these loans by selling participation interests insured by credit enhancement policies that are issued by the Company's captive insurance companies.

As part of the Company's strategy, franchisees are encouraged to share their

product expertise by networking with other franchisees through customer introductions and customer sharing. Categorizing franchisees by specialty helps promote networking because the Company believes that franchisees with different specialties do not typically compete for customers.

A new Company strategy is to directly acquire real estate for office space to lease to franchisees and to loan money to franchisees for acquisition of real estate for office space. Because franchisees specializing in insurance are usually more profitable and successful when operating from a service center, the Company expects to operate additional service centers and may acquire real estate for this purpose if circumstances warrant.

The Company's profits are highly dependent on the one-time consulting fees associated with franchisees' acquisitions of businesses which make the Company's profits less predictable. In an effort to make the Company's revenues more reliable and its profits more predictable, the Company implemented the following strategies.

Although many franchisees prefer to acquire a business and then convert to the Company's franchise, some franchisees prefer to start a business using the franchisor services provided by the Company. In these instances, it is the Company's strategy to provide a Start up Assistance Plan ("SUP") that provides specific consulting and financial assistance such as (1) access to a line of credit loan during start up, (2) expanded training at the Brooke Academy, and (3) access to specialized marketing departments.

The Company believes that local ownership of insurance agencies is important because insurance sales usually result from personal sales contacts, and the rewards of ownership provide excellent motivation for sales professionals. However, the Company's experience indicates that the sale of auto insurance, particularly the sale of insurance to drivers with a higher risk profile, is more dependent on management and organizational skills that are more characteristic of a larger organization than personal sales contacts that are more characteristic of a local business. As such, the Company recently established a separate auto insurance specialty, and the Company's strategy is to make selective acquisitions of this type of agency. These acquisitions result in regular commission based operating income and a revenue stream that is more reliable than consulting fees.

The Company plans to gradually change the lending activities so that relatively fewer profits are recorded as a "gain on sale" at the time of a loan sale, and relatively more profits are recorded as interest margins over the life of the loan which creates a more reliable revenue stream.

As part of the Company's strategy to generate additional revenues from its franchising activities without additional costs to its franchisees, the Company,

through its insurance brokerage subsidiary, sells hard to place, or excess and surplus lines, insurance and develops insurance programs. The Company's first priority is to grow its excess and surplus lines commissions because these commissions are generally more reliable than commissions from insurance programs. The Company's second priority is to develop insurance program commissions. By focusing on commissions provided by excess and surplus lines insurance, the Company plans to generate a revenue stream that is more reliable than consulting fees.

As another part of the Company's strategy to generate additional revenues from its franchising activities without additional costs to its franchisees, the Company incorporated two captive insurance companies in the country of Bermuda to share the premiums and underwriting risks for a portion of the excess and surplus lines, programs and credit enhancement insurance policies (which provide specified coverages to lenders in the event losses are incurred after a loan default and collateral liquidation) written by the Company's brokerage subsidiary. By carefully selecting the policies in which the Company assumes an underwriting risk, the Company is better able to control policy losses and thereby increases the likelihood of a reliable stream of underwriting profits.

Services and Products

The Company has three product lines. The first is its franchisor services, which the Company believes is unique to the insurance and related services industries. The Company's second line of products is its facilitator services which include lending to franchisees, consulting with franchisees and other such services to facilitate business ownership by franchisees and others. The Company's third line of products is its insurance brokerage services. Brokerage services encompass the sale of insurance by the Company on a wholesale basis through exclusive franchisees and other non-exclusive broker agents. During 2003, the Company did not develop any new product lines, but did continue to revise, expand and redefine its existing product lines. For instance, the Company has extended its franchisor services product line to include a funeral services specialty and an auto insurance specialty in addition to the existing general insurance specialty and financial services specialty.

Franchisor Services

The Company's first product line is franchisor services offered through its franchise subsidiary, Brooke Franchise Corporation. Franchisor processing services provided by the Company to franchisees include cash management, document management and personal management. The Company's cash management services include: (1) daily consolidation of all cash collected by franchisees, (2) recording customer receipts to franchisee's account statement, (3) recording customer checks to franchisee's account statement, and (4) reconciling sales commissions and other revenue to franchisee's account statement. Cash management is an important component of the Company's obligation to assist lenders with preservation of collateral. The Company's document management services include: (1) storing customer documents as electronic images for viewing via the Company's web site, and (2) maintaining customer name and address data for accurate ownership identification and reliable viewing. Document management is also an important

component of the Company's obligation to assist lenders with preservation of collateral. The Company's personal management services include: (1) personal sales training, (2) personal time management tools, and (3) a buying group for purchasing office equipment, supplies and delivery services.

In addition to processing services, as franchisor, the Company also provides marketing assistance to franchisees. Marketing assistance includes supplier access, branding, and development of professional marketing plans and materials. Supplier access is particularly important to franchisees selling property and casualty insurance because writing policies for insurance companies with competitive pricing and products is critical to insurance agents' success. Use of a trusted brand name can result in additional sales, much like additional sales that can result from a product endorsement. Although a trusted brand name may attract an Internet customer, because of the complexity of many insurance and related services, the assistance of a local franchisee to provide individualized customer support is often required. The Company believes that franchisees with a trusted brand name, local presence and franchisor support are well-positioned to compete with Internet and telephone sales of insurance and related services. The Company has a staff of marketing professionals, organized by specialty, that assists franchisees with development of marketing plans and marketing materials. In addition, the Company helps pay for a portion of franchisees' marketing costs if conducted in accordance with the Company's standards.

The Company's franchisor services include the operation of service centers to assist franchisees and their customers. The resulting economies of scale typically reduce franchisees' servicing expenses. Franchisor services also include operation of Company owned auto insurance locations.

Facilitator Services

The Company's second product line is facilitator services, which primarily encompasses the activities associated with the transfer of business ownership to franchisees. Facilitator services include lending to franchisees for the purpose of acquiring and operating businesses. The Company has developed a unique set of "Collateral Preservation" tools that has made the Company's finance company subsidiary, Brooke Credit Corporation, a leader in the area of lending for acquisitions of insurance agencies, financial services firms and funeral homes. To accommodate the unusual collateral characteristics of franchisee loans, the finance company retains the Company, as franchisor, to: (1) maintain trust accounts for customer receipts, (2) centrally store collateral (customer files), (3) control supplier relationships, (4) account for and disburse revenues, and (5) generally cooperate in preservation and, if necessary, liquidation of collateral. The Company's business includes the buying and selling of insurance agencies, financial services firms and funeral homes held in inventory. As a result of its collateral liquidation activities, insurance agencies, financial services firms and funeral homes may be purchased by the Company into inventory and sold by the Company from inventory on an ongoing basis.

Facilitator services include consulting with franchisees that purchase a business and convert it into a franchise. This service is typically performed by the Company's franchise subsidiary under the trade name of Heritage Agency Consulting. The first year of ownership for all business owners is typically the most difficult. As such, a "Buyers Assistance Plan" ("BAP") is typically provided to consult with and otherwise assist franchisees during their first months of ownership. Some of the benefits provided by a BAP include: (1) pre-closing inspection reports, (2) marketing and training plan development, and (3) operation analysis consulting. The primary benefit of a BAP is to successfully convert a business into the Company's franchise. The Company contends, and has gathered evidence to support its contention, that the value of franchisees' businesses increases as the result of successful conversion into the Company's franchise system.

The BAP services provided by the Company have been divided into three categories: (1) due diligence inspections before closing, (2) marketing and training consulting after closing, and (3) operational consulting after closing. BAP services include an inspection report that is delivered to the buyer prior to closing so it can be used as part of buyer's due diligence process. Inspection reports are the compilation of information gathered from the business seller and based on well-defined guidelines set forth in the exhibits to the BAP agreements. BAP services include marketing and training consulting. During the first 30 days after closing, a marketing plan is developed to guide the buyer's marketing and training activities during the crucial first year of business. BAP assistance includes payment for certain signage, mass media advertising and direct mail advertising expenses. During the first 30 days after execution of the BAP, an operations report is compiled to help the buyer improve business operations and historical commissions data is reconciled. BAP purchase prices have been allocated to each of the three categories of BAP services referenced above based on factors such as consulting time expended and direct cash outlays.

Facilitator services include consulting with new franchisees that elect to start a business instead of acquiring a business. This service is typically performed by the Company's franchise subsidiary under the trade name of Heritage Agency Consulting. Starting a business is often a difficult and stressful experience. As such, a "Start-up Assistance Plan" ("SUP") is typically provided to consult with and otherwise assist franchisees during the startup phase of their business. Some of the benefits provided by a SUP include: (1) access to a line of credit loan during start up, (2) expanded training at the Brooke Academy, and (3) access to specialized marketing departments.

Facilitator services include consulting with franchise and non-franchise sellers regarding the sale of their businesses. This service is typically performed by the Company's franchise subsidiary under the trade name of Agency Business Consultants. Because the selling process is typically more difficult for a

non-franchisee, Agency Business Consultants offers a variety of consulting services to non-franchisees including: (1) business profiles, (2) commission and other revenue tabulations, (3) legal agreement examples, and (4) general sale preparation. Additionally, the Company retains Agency Business Consultants, as its exclusive buyer representative, to find businesses to purchase from non-franchisees for eventual sale to franchisees.

Brokerage Services

The Company's third product line is insurance brokerage services, which includes brokerage of property casualty insurance through exclusive franchisees and non-exclusive broker agents. Brokerage services generally include writing insurance for those that are difficult to insure, creating insurance programs and sharing underwriting risks with insurance companies through the Company's Bermuda based subsidiaries.

Typical Transaction

The Company typically contracts with third party suppliers, such as insurance companies, to provide the services and products sold by franchisees. The separation or independence of franchisees from their suppliers generally increases business value. Most of the Company's transactions are currently related to the sale of insurance policies; therefore, a typical insurance transaction is described and other characteristics specific to insurance sales are discussed below. A typical transaction occurs when an insurance policy is sold by one of the Company's franchisees and the premium is paid by the customer directly to an insurance company. On a periodic (usually monthly) basis, insurance companies pay commissions to the Company for the sale of insurance policies which the Company records as commission income. The Company then pays a share of sales commissions to its franchisees which is recorded by the Company as commission expense.

The Company is solely responsible for payment to insurance companies of premiums collected from customers for the sale of insurance policies even if its franchisees mishandle premium collection. Accordingly, the Company is the recipient and owner of all commissions paid by insurance companies resulting from the sale of insurance policies by the Company's franchisees. The Company's franchisees have an exclusive contractual relationship with the Company and generally do not have any contractual relationship with the insurance companies. As such, payment of a share of sales commissions to the franchisees is an obligation of the Company and is not an obligation of any insurance company. Furthermore, for income tax purposes, the Company is required to record all commissions received from insurance companies as income and correspondingly reports to the appropriate tax authorities all commissions expense paid to franchisees.

Commission expenses as a percentage of commission income increased from approximately 77.6% in 2001 to approximately 83.0% in 2002, and decreased slightly to approximately 78.7% in 2003. The relatively high level of commission expense is primarily due to the Company's consistent practice of paying a large

share of sales commissions to its franchisees.

The typical transaction outlined above provides for the billing and collection of premiums directly by insurance companies because, when available, the Company's franchisees are required to use direct insurance company billing. However, in those instances where direct company billing is not available, the Company is responsible to the insurance company for billing and collecting the full premium from customers. The Company then remits to insurance companies the amount of the customer's premiums, net of sales commissions, when the Company is billed by insurance companies. As a result, the Company records an account receivable for the amount owed by the customer to the Company and simultaneously records a payable for the amount owed by the Company to the related insurance company.

Customer receivables are included in the balance sheet category for accounts and notes receivable. This category also includes receivables from insurance companies for commissions on direct company billed policies, and certain notes receivables held by the Company's finance company subsidiary, Brooke Credit Corporation. Customer receivables result when the Company assumes responsibility for the billing and collection of premiums that is typically the responsibility of the insurance companies. To accommodate customers when direct company billing is not available, the Company sometimes permits flexible premium payments by not requiring full premium payment prior to policy delivery. This resembles the premium payment flexibility offered by insurance companies when premiums are direct company billed. Consequences to the Company of providing this flexibility include collection risk and reduced cash balances from payment of premiums to insurance companies prior to premium collection from customers.

Customers

The Company's customers are typically entrepreneurial individuals with experience in the sale of insurance, financial services or funeral services and a desire to be business owners. Because the Company's revenues are currently derived almost exclusively from insurance sales, the Company's customers have historically been independent insurance agents. However, the Company currently sells insurance, financial services and funeral services through approximately 262 locations that employ or retain over 765 licensed insurance and financial services professionals in Arizona, California, Colorado, Florida, Georgia, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Michigan, Missouri, Nebraska, Nevada, New Mexico, Ohio, Oklahoma, Tennessee, Texas, and Utah and 8 licensed funeral professionals in Texas, Florida and Indiana.

The Company's franchise services, facilitator services and brokerage services have historically been sold to franchisees with an insurance specialty. However, these product lines are now also available to franchisees that specialize in the sale of financial services and funeral services. In addition, the Company

intends to eventually extend its franchisor services product line to include loan brokers and other such entrepreneurs.

Market

Most of the Company's revenues result from sales of insurance policies. Although the Company's revenues are comprised primarily of the sales commission portion of insurance premiums, most industry analysis is based on premiums. The Company reconciled, or allocated to franchisees and other agents, \$343 million in actual premiums during 2003; however, gross premiums for 2003, on an annualized basis, would be more as a result of agency acquisitions made during the year for which premiums were collected for only part of the year.

According to the FutureOne 2002 Agency Universe Study conducted by the Independent Insurance Agents and Brokers of America there were approximately 40,000 independent insurance agencies in the United States in 2002. The Company's insurance specialist franchisees sell insurance to both personal and commercial customers; however, as a group, the Company's insurance specialist franchisees sell more personal insurance than commercial insurance.

According to the Insurance Information Institute total premiums in the United States in the property and casualty sector totaled approximately \$312.4 billion in 2001 and \$348.2 billion in 2002. Life and health premiums totaled approximately \$584.3 billion in 2001, (most recent data available).

The market for the Company's facilitator services is largely determined by the number of independently owned insurance agencies, financial services practices and funeral homes in the United States. According to data from Dun & Bradstreet's ZAPDATA the number of independently owned financial services firms was 212,451 in 2003; the number of independently owned funeral homes was 24,815 in 2003.

Competition

Because the Company's franchise product line is relatively unique, the Company is unaware of any significant direct competitors in the United States for the franchisor services that are offered by the Company.

With regards to the Company's franchisor services that are marketed to franchisees specializing in insurance, the Company is aware of insurance agency competitors that have "vested producer" programs, but it is not aware of any such competing insurance agencies that structure their relationship in a manner that facilitates the transfer of vested ownership interests to third parties to the extent that the Company does. The Company believes the easier and safer that ownership transfers become, the more agency liquidity and value are likely to increase. The Company is also aware of insurance company principals, or

suppliers, that offer franchisor type services to insurance agents, but to the best of the Company's knowledge, such services do not allow agents exclusive agency ownership and/or require that such agents sell exclusively for one insurance company. Also, insurance company suppliers sometimes offer assistance to agents' policyholders that have purchased policies from their specific insurance company. However, there does not appear to be a service, such as the Company's unique type of franchisor services for insurance specialists, that attempts to provide a comprehensive solution to the efficiency problems encountered by independent insurance agents.

Competitors for the franchisor services that the Company markets to franchisees specializing in financial services, include independent securities brokers, life insurance brokers and securities dealers. However, the Company is not aware of any significant competitors that offer the unique type of franchisor services that the Company markets to franchisees specializing in financial services.

Competitors for the franchisor services that the Company markets to franchisees specializing in funeral services include independent, regional and multinational operators of funeral homes, crematoria and cemeteries, as well as publicly traded companies that expand through acquisitions of smaller funeral services providers. However, the Company is not aware of any significant competitors that offer the unique type of franchisor services that the Company markets to franchisees specializing in funeral services.

Competitors to the Company's facilitator product line are wide, varied and formidable. Because virtually all of the Company's facilitator activities have been related to agents specializing in insurance, the following discussion regarding competition for facilitator services focuses on competitors with an expertise in insurance and a limited number of competitors that have developed expertise in the Company's primary facilitator services of lending to insurance agents, consulting with insurance agents and matching insurance agency buyers with sellers. The competition for agency loans comes primarily from banks and other traditional lenders, many of which are larger and have more resources than that of the Company. However, the Company is not aware of any lenders that have developed the comprehensive legal and lending standards that are required to protect and preserve the intangible assets that serve as collateral for agency loans originated by the Company. Additionally, as previously noted, the Company's franchisor services are critical to collateral preservation.

The competition for consulting with buyers and sellers of insurance agencies, financial services firms and funeral homes comes from management consulting firms, accounting firms, investment banking firms and legal firms although the Company is not aware of any competitors that dominate this market.

The Company's brokerage product line is not unique; therefore, it generally has much more competition for the sale of brokerage services than it does for the

sale of services included in its franchise product line. Virtually all of the Company's brokerage services are oriented to insurance specialists. Many independent insurance agents and insurance brokers have developed insurance programs for specific market niches and provide significant competition. However, those that purchase the Company's franchisor services are considered by the Company to be a receptive audience for the Company's brokerage services which the Company believes provides a significant advantage within its franchise organization.

Sales and Marketing

Marketing of the Company's franchise and consulting services is conducted from its Kansas City, Dallas, Nashville, Denver and Sacramento regional offices. The Company's national office in Overland Park, Kansas, coordinates the sales and marketing activities of all regional offices. The Company's franchise services are marketed under the name of "Brooke Franchise Corporation" and the Company's consulting services are marketed under the trade names of "Heritage Agency Consultants" and "Agency Business Consultants." Franchising and consulting services are typically advertised through direct mailings, personal contacts, internet job sites and agencies4sales.com, a Company owned web site. The contents of such web site (including any web site connected by hyperlink) are not incorporated into this Annual Report by reference. The Company's franchise services are sold using a Uniform Franchise Offering Circular or similar offering document registered with various states.

The Company's national office markets the Company's lending services to borrowers and also markets participating interests in originated loans to investors, primarily commercial banks. However, limited advertising is directed to potential borrowers because most loan applications are originated as the result of referrals from those selling the Company's franchise and consulting services. The sale of participating interests is primarily the result of personal contacts by national office representatives.

The Company has established marketing departments at the national office that assist franchisees in marketing to their customers. The Company also pays up to 50% of franchisees advertising and marketing expenses if in accordance with Company standards for promoting a common brand.

Company owned auto insurance agencies rely primarily on local yellow pages, newspaper, radio and television advertising. These agencies typically operate from neighborhood "sales offices". If sales offices are clustered together, then they are sometimes supported by a local administrative office.

Franchisees usually market their services from office locations occupied solely by them. However, particularly as the result of the Company's SUP program, a bigger emphasis is on marketing from "service center" offices that are shared with other franchisees. In these instances, the Company manages the service center personnel and facility so franchisees can focus on sales and marketing

activities.

The Company's insurance brokerage services are marketed from four underwriting offices located in Overland Park, Kansas; Omaha, Nebraska; Dallas, Texas; and, Springhill, Louisiana. The Company markets its brokerage services primarily by personal contact and promotion of its "Easy Rater" software.

Employees

The Company currently employs a total of approximately 402 total employees. On a full-time equivalency basis (those employees who regularly work 37.5 hours or more per week), the Company employs approximately 351 individuals.

Suppliers

Most of the Company's revenues currently result from sales of insurance policies. As such, the Company's primary suppliers are insurance companies, and the Company has agency relationships with a large number of insurance companies. The Company has direct agency relationships with several of the leading writers of commercial insurance in the United States. The Company's largest suppliers include Safeco Insurance Company, Allied Insurance Company, Employers Mutual Companies, Columbia Insurance Company, Progressive Insurance Company, Hartford Insurance Company, Met Life Auto & Home and Travelers Insurance Company. The Company has entered into agency agreements with each of the suppliers listed above.

Regulations

The Company's insurance activities are generally regulated by the insurance departments of individual states. The Company must maintain valid insurance agency licenses in most of the states in which the Company transacts its insurance and financial services business. Periodically, agency insurance licenses must be renewed by and license fees must be remitted to the individual states.

The Company's finance company subsidiary's lending activities are targeted to businesses and are generally unregulated. Although the Company does not typically make consumer loans, the Company's finance company subsidiary, Brooke Credit Corporation, is licensed as a consumer finance company in Kansas. The Company's franchising activities are also regulated, to a certain extent, by the Federal Trade Commission and state regulators.

As a reporting company, the Company's reporting activities are regulated by the Securities and Exchange Commission. Offerings of the Company's securities are subject to provisions of the Kansas Securities Act and regulations administered and enforced by the Office of the Securities Commissioner of Kansas and are also subject to provisions of the federal securities laws administered by the Securities and Exchange Commission.

Although the funeral services industry is generally regulated by the states' local boards of mortuary, the insurance departments with respect to pre-need policy sales, the Federal Trade Commission and other regulatory agencies, given the Company's current business model, it is not required to maintain any funeral services related licenses other than insurance licenses needed to conduct pre-need insurance sales.

The Company believes that it is currently in material compliance with all state and federal regulations to which it is subject and is unaware of any pending or threatened investigation, action or proceeding by any state or federal regulatory agency involving the Company.

Corporate Structure

All of the Company's subsidiaries are directly or indirectly 100% owned and controlled by the Company. Subsidiaries are grouped into one of five categories that correspond to the subsidiaries' purpose: (1) operating subsidiaries, (2) acquisition subsidiaries, (3) captive subsidiaries, (4) securitization subsidiaries, and (5) other subsidiaries.

Operating Subsidiaries: Although the Company has multiple subsidiaries, the Company's business operations are typically performed by one of three operating subsidiaries: Brooke Franchise Corporation, Brooke Credit Corporation and CJD & Associates, L.L.C. Separate annual audited financial statements are typically prepared for each operating subsidiary. Each operates independently from the other two operating subsidiaries and from the Company to perform its specific business purpose. Each operating subsidiary is also responsible for its own obligations, maintains its own separate funds, generates revenue in its own right, hires its own employees and maintains separate boards of directors. The Company provides accounting, administrative and legal support for the activities of its three operating subsidiaries, and Company revenues are typically limited to dividends and administrative fees from these operating subsidiaries.

Brooke Franchise Corporation is a Missouri corporation. On November 15, 2002, the Company changed the subsidiary name from Interstate Insurance Group, LTD to Brooke Franchise Corporation so that the corporate name better identifies the subsidiary's business purpose. The primary business purpose of this subsidiary is franchising and providing consulting and other services to franchisees through its network of regional offices and service centers.

Brooke Credit Corporation is a Kansas corporation and is a licensed finance company that originates loans primarily to the Company's franchisees. To a lesser extent, this subsidiary also originates other types of loans through affiliates, independent loan brokers and loan agents. Loans originated by Brooke Credit Corporation and its loan brokers are sold on a wholesale basis to participating lenders and other investors.

CJD & Associates, L.L.C. is a Kansas limited liability company. This subsidiary is a licensed insurance agency that sells insurance programs and excess and surplus lines insurance on a wholesale basis under the trade names of Davidson-Babcock, Texas All Risk General Agency and All Risk General Agency, through the Company's network of insurance specialist franchisees and through agents not necessarily affiliated with the Company.

Acquisition Subsidiaries: The Brooke Agency, Inc. and Brooke Investments, Inc. subsidiaries are used to acquire insurance agency and real estate assets for long term investment. Separate financial statements are typically prepared for each acquisition subsidiary because each secures loans from Brooke Credit Corporation and other lenders to fund their acquisitions.

Brooke Agency, Inc. is a Kansas corporation. Brooke Agency typically acquires for investment those insurance agencies that specialize in the types of insurance sales, such as auto insurance, where local ownership is less important to success. (Note: Brooke Franchise Corporation typically acquires for resale those insurance agencies that specialize in the types of insurance sales where local ownership is important to success.) Brooke Franchise Corporation retains a share of commissions to provide personnel and facilities to this subsidiary so Brooke Agency does not typically have any employees or incur operating expenses.

Brooke Investments, Inc. is a Kansas corporation. Although no acquisitions have been made to date, Brooke Investments intends to acquire real estate for lease to franchisees and others. Although the Company provides certain administrative and legal support, Brooke Investments retains all lease payments and pays all other related expenses. Revenues from this subsidiary will be typically limited to dividends.

Captive Subsidiaries: The DB Group, LTD and DB Indemnity, LTD subsidiaries were incorporated in the country of Bermuda as captive insurance companies. Separate financial statements are typically prepared for Bermuda subsidiaries as required by the Bermuda government. Each captive insurance company subsidiary is responsible for its own obligations, maintains its own separate funds and generates revenue in its own right. The captive insurance company subsidiaries are wholly owned by CJD & Associates, LLC and revenues are typically limited to dividends.

The DB Group, LTD was incorporated for the purpose of underwriting, as a reinsurer, a small portion of the insurance written by CJD & Associates, LLC. There were no premiums written in this subsidiary in 2003.

DB Indemnity, LTD was incorporated for the purpose of insuring a portion of the professional insurance agents' liability exposure of Brooke Franchise Corporation's franchisees and for the purpose of issuing financial guaranty, or

credit enhancement, policies to Brooke Credit Corporation, its successors and assigns.

Securitization Subsidiaries: Brooke Agency Services Company LLC, Brooke Acceptance Company LLC and Brooke Captive Credit Company 2003, LLC were organized in Delaware as bankruptcy-remote special purpose entities as part of the process of securitizing Brooke Credit Corporation's loan portfolio. To the extent required by the securitization process, separate financial statements are prepared for each securitization subsidiary.

Brooke Agency Services Company LLC is licensed as an insurance agency and was created to offer property, casualty, life and health insurance through the Company's network of franchisees. Brooke Agency Services Company LLC has acquired ownership of franchise agreements from the Company and/or Brooke Franchise Corporation as part of an arrangement to preserve collateral on behalf of Brooke Credit Corporation as required by the securitization process. Brooke Agency Services Company LLC has contracted with the Company and/or Brooke Franchise Corporation for performance of any obligations to agents associated with all such franchise agreements.

Brooke Acceptance Company LLC and Brooke Captive Credit Company 2003, LLC are the purchasers of Brooke Credit Corporation loans pursuant to a true sale and the issuer of certain floating rate asset backed notes issued pursuant to various indenture agreements. The financial information of these subsidiaries is not consolidated with the Company's financial information.

Other Subsidiaries: Other subsidiaries have been established for marketing, regulatory, licensing, security or other purposes and do not typically conduct any operations or own any assets. Any revenues generated by other subsidiaries are assigned to an operating subsidiary for performance of any associated obligations. These subsidiaries include Brooke Life and Health, Inc., Brooke Bancshares, Inc., The American Agency, Inc., The American Heritage, Inc., Texas All Risk General Agency, Inc., TAR Holding Company Inc., All Risk General Agency, Inc., Brooke Funeral Services Company, LLC and First Brooke Insurance and Financial Services, Inc.