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## Evaluating Non-Insurance Ultimate Parents

Understanding the potential effect on a rated entity from the activities of the ultimate parent/holding company is an important component in developing a comprehensive view of the risk profile. The financial flexibility of an insurance company's owner(s), management effectiveness and strategy, and the importance of the insurance company compared with other subsidiary organizations and businesses within the consolidated organization all are incorporated into the published rating of the insurance company. It is important to understand the owner's ability and willingness to support the insurance company during times of stress. This analysis becomes potentially more complex when the insurance company is owned by a parent that is engaged primarily in a business other than insurance.

This criteria procedure outlines a two-step rating process that is employed when a rated insurer has a non-insurance owner and describes how non-insurance ultimate parents are evaluated by A.M. Best. The first step contemplates gathering information to derive a stand-alone assessment of the insurance company that is to be rated. This stand-alone assessment utilizes many of the analytical procedures and techniques used to analyze any insurer that A.M. Best rates. The second step contemplates whether an adjustment is necessary to distill a published rating to be assigned to the insurer, after incorporating information related to the non-insurance parent and its intended incorporation of the insurance company in the consolidated organization's business plan. With this information, A.M. Best determines whether or not the individual insurance subsidiary qualifies for enhancement or drag to its stand-alone assessment,

The analysis of the non-insurance owner of a rated insurer includes assessment of publicly available credit measures, market-based credit measures and independently performed financial analysis. The relative weight of the approaches utilized to generate an assessment of the non-insurance owner is assessed at the rating committee.

The publicly available credit measures of non-insurance owners include the credit ratings assigned to the company or group by other credit rating agencies (CRAs) that have developed expertise in that particular industry. The credit analysis performed by major CRAs is a tool that incorporates quantitative and qualitative information from public and nonpublic sources, in addition to the CRA's proprietary expertise derived from the processes and people involved in assigning a rating. A.M. Best utilizes major credit ratings publically available to form an opinion of the creditworthiness of a non-insurance ultimate parent.

The market-based credit measures of non-insurance owners incorporate tracking and use of market-based measures of default risk indicated by credit default swap (CDS) prices ("spreads"), as an example. If credit default swaps are not available, the credit spreads on issued debt instruments may be utilized. CDS spreads contain valuable and timely information regarding the market's perception of an issuer's credit quality. While they can be volatile and need to be monitored over an extended period, CDS spreads act as a good early warning system that can act as a catalyst for the analytical team to initiate immediate conversations with company management. As appropriate, the rating committee would assess the current rating level and adjust it as needed.

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When an insurance company is owned by an individual(s), the analysis may require personal financial statements or other appropriate financial documents of the owners. In these cases, enhanced scrutiny of the stockholder dividend track record and the components of the expense ratio of the insurance company may take place.

In the case of a sovereign parent, A.M. Best conducts a similar analysis on the creditworthiness of the government entity, taking into account credit rating information, the sovereign's financial health (including debt and fiscal position) and market-based default probability information. In addition, the analysis incorporates an assessment of the political environment of the sovereign entity (including government stability and the degree of corruption).

The analytical team performs a detailed, relevant, independent financial analysis that could be generic enough to apply to most companies, or the team may utilize an industry-specific approach if warranted. Peer analysis of non-insurance owners also can be a valuable tool to the analytical team. Last, to the extent that a non-insurance owner has financial and nonfinancial information available in the public domain, it can be utilized by the analytical team. Information such as news reports and stock analysts' reports and recommendations can provide valuable insight. In addition to the independent financial analysis, the analytical team also may incorporate an opinion of a non-insurance owner's enterprise risk management and corporate governance policies and procedures.

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## METHODOLOGY

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**Best's Financial Strength Rating (FSR):** an independent opinion of an insurer's financial strength and ability to meet its ongoing insurance policy and contract obligations. An FSR is not assigned to specific insurance policies or contracts.

**Best's Issuer Credit Rating (ICR):** an independent opinion of an entity's ability to meet its ongoing financial obligations and can be issued on either a long- or short-term basis.

**Best's Issue Credit Rating (IR):** an independent opinion of credit quality assigned to issues that gauges the ability to meet the terms of the obligation and can be issued on a long- or short-term basis (obligations with original maturities generally less than one year).

### Rating Disclosure: Use and Limitations

A Best's Credit Rating (BCR) is a forward-looking independent and objective opinion regarding an insurer's, issuer's or financial obligation's relative creditworthiness. The opinion represents a comprehensive analysis consisting of a quantitative and qualitative evaluation of balance sheet strength, operating performance and business profile or, where appropriate, the specific nature and details of a security. Because a BCR is a forward-looking opinion as of the date it is released, it cannot be considered as a fact or guarantee of future credit quality and therefore cannot be described as accurate or inaccurate. A BCR is a relative measure of risk that implies credit quality and is assigned using a scale with a defined population of categories and notches. Entities or obligations assigned the same BCR symbol developed using the same scale, should not be viewed as completely identical in terms of credit quality. Alternatively, they are alike in category (or notches within a category), but given there is a prescribed progression of categories (and notches) used in assigning the ratings of a much larger population of entities or obligations, the categories (notches) cannot mirror the precise subtleties of risk that are inherent within similarly rated entities or obligations. While a BCR reflects the opinion of A.M. Best Rating Services Inc., (AMBRS) of relative creditworthiness, it is not an indicator or predictor of defined impairment or default probability with respect to any specific insurer, issuer or financial obligation. A BCR is not investment advice, nor should it be construed as a consulting or advisory service, as such; it is not intended to be utilized as a recommendation to purchase, hold or terminate any insurance policy, contract, security or any other financial obligation, nor does it address the suitability of any particular policy or contract for a specific purpose or purchaser. Users of a BCR should not rely on it in making any investment decision; however, if used, the BCR must be considered as only one factor. Users must make their own evaluation of each investment decision. A BCR opinion is provided on an "as is" basis without any expressed or implied warranty. In addition, a BCR may be changed, suspended or withdrawn at any time for any reason at the sole discretion of AMBRS.

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