

Rating Members of Insurance Groups

The dynamics within insurance groups and the relationships between affiliated companies continue to evolve. The level of support companies are willing to provide to subsidiaries or affiliates has developed substantially over the last five years. In particular, the use of support agreements, especially guarantees, continues to grow in the insurance industry.

In recognition of these trends, A.M. Best Co. has updated its policy on the level of rating consideration for both explicit support — capital infusions, guarantees, pooling arrangements and reinsurance — and implicit support — the anticipated future support likely to be available due to a subsidiary's strategic and/or financial importance within the group.

Previously, A.M. Best used the terms core, strategic and ancillary to describe the amount of rating enhancement a company can receive as a member of a larger and stronger organization. A.M. Best has moved away from the use of these terms when rating members of groups, focusing purely on the amount of rating enhancement included in the published rating opinion, rather than on determining a company's "core" status, which is the responsibility of an insurer's management. Assertions from management regarding the "core" status of a subsidiary alone are not a reason for rating enhancement.

There are many considerations that go into A.M. Best's determination of the amount of rating enhancement provided to a company's published rating. This report reviews A.M. Best's methodology for assigning ratings to companies that comprise an insurance group, including the consideration of rating drag that a weak parent can place on a subsidiary that is financially strong when viewed on a stand-alone basis.

Eligibility for Rating Enhancement

While A.M. Best recognizes that no two groups of insurers operate or are managed in

the same fashion, certain factors must be present for ratings to reflect group affiliation. In general, eligible groups are those where two or more insurers operate under common ownership (in excess of 50%) or board control and common management, common strategy or other substantial form of common corporate governance or functional area of operations (i.e., management systems and distribution). For groups with multiple operating units, A.M. Best's consideration for rating adjustment would apply to each company or group of companies serving those business segments. In some cases, it may be possible for a market or business to be core to an organization, but the subsidiary operating in that market or business may not be viewed as eligible for rating enhancement by A.M. Best after reviewing the subsidiary's market position and current operating performance relative to the group.

Rating Analyses of Groups

A.M. Best's rating approach involves comprehensive quantitative and qualitative analyses of an organization's balance sheet strength, operating performance and business profile.

Please note that for clarity within this report, the major insurance company within a group of affiliated companies or the lead company of a pooling arrangement is referred to as the "parent." While this may not always be the case, as the pooled companies could be sister affiliates, the analytics are similar to a parent-subsidiary relationship.

When assigning ratings to companies with a group affiliation, A.M. Best's approach involves an analysis of:

1. Each operating unit within the group on a stand-alone basis.

A.M. Best's rating methodology is applied on a stand-alone basis to each subsidiary or operating unit in a group in the same manner that any single company is analyzed and an internal stand-alone rating is assigned. This analysis, based on the consolidation of the company being analyzed and its own subsidiary operations, provides A.M. Best's

Questions regarding A.M. Best's methodology for rating members of insurance groups can be directed to Matthew Mosher, group vice president in the property/casualty division.



analysts with a perspective of the individual operating unit's financial strength without the benefits of implicit or prospective explicit support from an affiliate.

2. The parent organization on a consolidated basis.

The parent also is analyzed on a consolidated basis to obtain a complete picture of the risk profile of the entire organization. This consolidated view provides a perspective on the highest rating levels that are likely to be obtainable by the individual operating units in the organization.

There are situations, albeit rare, where a subsidiary might carry a financial strength rating (FSR) that is higher than its parent's rating. Although unusual, this can occur where the subsidiary's stand-alone rating is extraordinarily strong relative to the parent, and material support is not provided from, or to, the parent. Such subsidiaries can be rated up to two notches above the applicable parent rating. In general, however, it is assumed that all operating units in the group are exposed to any potential financial distress within the overall organization.¹ The degree of exposure, however, may vary depending on the regulatory regime in which a company is domiciled.

3. Each operating unit's strategic and financial importance to the group and the impact of its parent.

An assessment is made to determine if a modification to the stand-alone rating of an operating subsidiary is merited based on the level of support or drag received from the parent company. A subsidiary's rating can be negatively or positively affected depending on the parent's relative financial strength.

Monitoring

Best's Ratings reflecting parental support require ongoing surveillance by A.M. Best to ensure that there are no material changes in the degree of implicit and/or explicit parental support that would affect a company's initial classification. As with all Best's Ratings, the dynamics of each insurance group are continually re-evaluated for changes that might arise. A.M. Best's analysts maintain rating contact with company managements throughout the year and monitor each company's performance and its strategic role within the group.

¹In this context, bankruptcy remote, special purpose vehicles (SPVs) are evaluated in the context of their status and degree of operational exposure to the sponsoring organization.

Enhancement of Ratings

An individual company can receive enhancement in its rating through support from its parent or affiliated companies. This support can be explicit, such as a guarantee, new reinsurance protection, a new capital infusion, or pooling of assets and liabilities. Alternatively, it can be implicit support due to the importance of the company to the overall organization. A company or operating unit can be important in providing strategic and/or financial benefit to the organization's core operations, or it can be an integral part of the core operation itself.

In-place reinsurance protection from a parent or affiliated company and prior capital infusions are considered within the stand-alone analysis of the operating unit. However, the permanence of any capital contribution or reinsurance protection is an important aspect of any explicit support. The lack of permanence can be a significant negative factor in a subsidiary company's

A.M. Best Co.

Methodology

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The Insurance Information Source

rating despite currently strong stand-alone financial strength. The evaluation of explicit support must include a subjective review of the level of parental commitment demonstrated in the support to the company.

Modification of an operating unit's stand-alone rating can require multiple levels of evaluation. One such example would be a European parent that owns a U.S. operation, and the lead U.S. company provides reinsurance to support important U.S. subsidiaries. In this example, A.M. Best assesses the affiliated reinsurance agreement and then evaluates the overall U.S. operation for its strategic importance to its European parent and the degree of financial support provided by that parent.

Subsidiary's Status/Implicit Support

The various operating subsidiaries within a group are considered for rating enhancement ranging from no rating enhancement to full rating enhancement, in which case the company is assigned its parent's rating. These companies maintain the greatest affiliation with, or importance to, the parent and receive the parent's rating. The security offered to the policyholders of these subsidiaries is deemed to be equal to that offered to the policyholders of the parent. Those companies that receive no rating enhancement demonstrate the least strategic importance and potentially could cease operations or be sold with no material impact to the group. These companies could be assigned a rating no higher than their stand-alone rating, unless new explicit support is provided. In any situation, the published rating of a subsidiary company could be lowered from its stand-alone level, if there is a perceived drag from a weaker parent.

Rating enhancement considerations are based primarily on the level of implicit support expected from a parent or affiliate. However, the level of implicit support anticipated by A.M. Best and the level of benefit in a rating also is influenced by the amount of explicit support already provided to the operating unit. These judgments are subjective and can be decided only by a rating committee after detailed discussions with management to gain a complete understanding of the organization, its individual members and the markets in which they operate.

There is no automatic increase in the subsidiary's published rating even if rating enhancement is appropriate. The amount of

enhancement provided in the published rating, if any, is arrived at subjectively by considering factors such as:

- Subsidiary's level of importance to the parent, as perceived by A.M. Best;
- Differential between the subsidiary's stand-alone rating and the parent's rating;
- Level of the parent's rating;
- Trend in parent's rating;
- Level of the subsidiary's stand-alone rating; and
- Amount of explicit support provided to date to the subsidiary.

There are cases where a subsidiary meets the criteria to be considered for rating enhancement, but after considering the above factors its stand-alone rating and the published rating are the same (e.g. weak "A-" to a strong "A" with a stable outlook). Under the most favorable conditions, A.M. Best will raise the stand-alone FSR of a subsidiary up to two rating levels (e.g., "B++" to "A").

Subsidiaries Assigned Their Parent's Rating

Although a separate legal entity, a company is assigned its parent's rating if A.M. Best views the company to be integral to the group's primary business due to its significant financial, operational and/or strategic importance through greater market penetration or strategic diversification. A.M. Best expects that under almost any scenario, the parent would continue to support the liabilities of the subsidiary, subject to its financial ability to do so. The sale or closure of such a subsidiary would be unexpected and could imply a radical shift in the parent's strategy. As a result, these subsidiaries are assigned their parent's rating and receive a group (g) affiliation code.

In many cases the operating performance of the subsidiary and its ability to meet parental expectations are important considerations in the evaluation of rating enhancement awarded. Common characteristics of a subsidiary that is assigned its parent's rating are:

- Integral to the group's strategy and very important to its ongoing success and viability;
- Fully integrated into the group's operations;
- Carries the group name or is highly identified with the group among its distribution channels. In some cases, the subsidiary retains its own recognized brand name within its local market;
- Material part of the business profile of

- the group;
- Significant contributor to the group's earnings and capitalization; and
- Has received or is very likely to receive a form of explicit support when/if needed.

Other factors that could offset the characteristics cited above are poor historical or prospective earnings on a stand-alone basis, weak stand-alone risk-adjusted capitalization, or diminished business profile. In general, these characteristics provide guidance as to the key areas that are considered; however, the determination of the amount of rating enhancement provided is determined on a case-by-case basis. It is very unlikely that a newly started or acquired entity would be assigned its parent's rating until it had demonstrated its contribution to the group's financial strength.

Example of the Assignment of the Parent's Rating

A European parent has a Best's Rating of "A" (Excellent), which reflects the organization's strong overall profitability and position in the global marketplace. Its global presence in the U.S. market is represented by an operating subsidiary with a stand-alone Best's Rating of "A-" (Excellent), which reflects its adequate capitalization, just above required minimum levels, resulting from a higher level of underwriting leverage compared to its parent.

The subsidiary is a major participant in its U.S. market, although its principle line of business differs from the parent's non-U.S. global businesses. The U.S. subsidiary has kept its well-known brand name and operates with its own operating management team. However, members of the subsidiary's management team are board members of the parent company. Investment and underwriting guidelines are established by the management of the parent, which also provides capital to support the subsidiary via a quota share agreement.

The U.S. operations have been profitable and its earnings historically comprise the majority of the overall European parent's earnings, with gross premiums consistently making up close to half of the parent's volume.

The subsidiary is assigned its parent's Best's Rating of "A" (Excellent) with a group (g) affiliation code due to its:

- Importance to the parent's overall strategy, earnings and revenue stream, and its contribution to the parent's consolidated financial strength;

- Integrated underwriting and investment guidelines; and
- Ongoing financial support from the quota share.

Subsidiaries with Some Rating Enhancement

Those subsidiaries that receive some rating enhancement differ from those entities that receive their parent's rating in their degree of affinity. The willingness of the parent to incur the financial downside of supporting such a subsidiary, given its importance to the group, seems less absolute. The subsidiary is not integral enough to the organization that any potential sale or shut-down of the operation would imply a radical change in the overall organization's business and strategy. However, A.M. Best believes the subsidiary is important enough that the parent would incur substantially greater losses than it would be legally obligated to in order to keep the subsidiary successfully operating.

In many cases, the operating performance of the subsidiary and its ability to meet parental expectations are important considerations in the evaluation of rating enhancement awarded. Common characteristics of a subsidiary that is assigned some rating enhancement are:

- Important to the group's strategy and business profile;
- May operate on a somewhat more independent basis and is reasonably well-established in its markets;
- Integrated to some degree with one or more affiliates within the group, but might not possess the group's name or share a common identity;
- Provides diversification to the group's earnings stream;
- Meaningful contributor to the group's operating performance, financial strength or other relevant business activities of the group; and
- Has received or is likely to receive a form of explicit support when/if needed.

A subsidiary assigned some rating enhancement can achieve a Best's Rating at the same level as its parent, but within the rating analysis, it is still considered a separate operating unit with independent risk characteristics. As such, it is not assigned its parent's rating as is the case with subsidiaries assigned a group (g) affiliation code.

Example of Some Rating Enhancement

A U.S. parent company with a European

subsidiary has a Best's Rating of "A+" (Superior), reflecting its strong capitalization, profitability and position in the U.S. market. The subsidiary holds a stand-alone Best's Rating of "A-" (Excellent). It operates in the same lines of business, but under a separate brand and with its own operating management team. Investment and underwriting guidelines are established by the U.S. parent, which also provides a quota share agreement to support the capitalization of the subsidiary.

The marginally profitable European subsidiary has recently improved its profitability due to strong market conditions. However, earnings and revenue from the subsidiary make up only a modest, but growing, portion of the parent's total revenue. Financial projections indicate that earnings of the European subsidiary are expected to continue to improve over the next 12 months.

The subsidiary is assigned some rating enhancement due to its:

- Complementary business;
- Relatively small contribution to the group's financial strength, but its business profile enhances the group's global presence;
- Profitability improving and expected to meet A.M. Best/parent's expectations;
- Integrated underwriting and investment guidelines; and
- Ongoing financial support from the quota share with its parent.

As a result, the European subsidiary receives rating enhancement to the "A" (Excellent) financial strength level.

This example includes a subsidiary that writes the same lines of business as its parent and provides global diversification and market presence. A subsidiary that provides diversification across lines of business, with the appropriate expertise in those different lines of business, also could be considered for ratings enhancement due to its strategic benefit to its parent.

No Rating Enhancement

A subsidiary receiving no rating enhancement is viewed as a company that is an investment and not materially strategic to a group. In these instances, the operating unit would be assigned the rating determined by the stand-alone analysis of the operating unit itself.

Common characteristics of a subsidiary that receives no rating enhancement include its:

- Marginal or incidental status to the group's

overall strategy and can be readily sold or closed without a material impact to the group's ongoing operations;

- Separate operating platform;
- Often are independently managed or have a separate market identity from the key operations of the group; and
- Lack of significant business synergy with its parent's core operations and no meaningful diversification benefits, as it is not a significant contributor to the group's earnings and capitalization.

It is important to note that a subsidiary may represent a successful investment but still receive no rating enhancement in A.M. Best's rating analysis. The success of the subsidiary would be reflected in its stand-alone rating.

Treatment of Branches

A true branch is not a separate legal entity and is viewed as an extension of the head office. Therefore, policies are written on the paper of the legal entity of which the branch is a part. Since the rating measures the ability to meet policyholder obligations, the concern that a branch of a solvent foreign insurer may be unwilling to meet its obligations is irrelevant to the rating opinion. Therefore, the branch is assigned the rating of the head office.

The rating treatment of a branch will be modified if, from a legal and/or regulatory viewpoint, there is an acknowledged limit to the exposure the legal entity has in meeting a branch's commitments. In such cases, the branch is treated as if it were a limited liability subsidiary and rated accordingly.

Explicit Financial Support

Explicit financial support is a defined mechanism through which a group demonstrates its commitment to a subsidiary or affiliate. Explicit support comes in the form of a capital contribution or a contractual arrangement that strengthens the parent's commitment, regardless of the subsidiary's fundamental importance. Pooling, internal reinsurance, guarantees and surplus maintenance agreements are examples of explicit support. In some cases, insurance groups use this to facilitate capital management by reducing the need to capitalize each subsidiary at a level consistent with the level required of their individual net exposure prior to the contractual support.

The level of benefit afforded to the rating

of an operating unit depends on the type of explicit financial support provided. Insurers with pooled and affiliated reinsurance arrangements that meet A.M. Best's requirements are assigned the parent's Best's Rating with the appropriate affiliation code — pooled (p) or reinsured (r) — to reflect that support. Whether such arrangements meet A.M. Best's requirements depends on the disposition of the company within the organization and the likelihood that it will remain a member of that organization.

Other forms of explicit support that do not contain language specifically related to policyholder obligations or are not time-tested or approved by regulators receive consideration in the rating process, but do not warrant the assignment of the parent's rating.

Pooled Affiliations

A company whose financial results and liabilities are pooled with those of its parent or affiliates maintains, in theory, the same operating performance and balance sheet strength as other companies within the pool. All of the assets of each pool participant are available for the protection of all pool members' policyholders. Often these companies are marketed under a common brand.

Affiliated companies within a pooling arrangement are most likely to be assigned the same Best's Rating and a pooled (p) affiliation code if the following conditions are met:

- Agreement among the pooled companies is joint and several;
- Pool is pure, meaning that all premiums, losses and expenses are shared based upon the pooling percentages, with the allocation of each being consistent with the allocation of unstacked surplus among the pool members;
- After consideration of the pool, stand-alone capitalization supports the assigned rating;
- Coverage for any prior-year loss reserve development is included in the pool;
- Coverage for the run-off of all liabilities incurred on policies incepted prior to termination is included in the pool;
- Greater than 50% ownership or control of the board of directors for each of the pooled members consistent with the lead company is exhibited; and
- 12-month notification period is required before the pool can be disbanded or a company can be removed from the pool.

While meeting these expectations will

most likely result in the assignment of the parent's rating, A.M. Best reviews the amount of protection afforded to policyholders within each contract and this review is the basis for the assignment of the financial strength rating. Companies that are members of pools, which in A.M. Best's opinion do not sufficiently protect policyholders, still can benefit from their group affiliation. Depending on the strength of the pooling arrangement and any other explicit and implicit support provided, the insurer can receive the same Best's Rating (without a pooled affiliation code) as the other companies within the pool.

Reinsurance Affiliations

A company protected by an affiliate's reinsurance coverage will most likely be assigned the Best's Rating of that affiliate, along with a reinsured (r) affiliation code, if the following conditions are met:

- Quota share of 100% for all premiums, losses and expenses written by the company is maintained unless regulatory restrictions apply. In those cases, the retained percentage could be as high as the level required by regulation, up to a maximum of 20%, but those cases would be subject to additional review;
- After consideration of the affiliated reinsurance, stand-alone capitalization supports the assigned rating. For those companies with less than a 100% quota share, stand-alone operating performance also is considered in the analysis;
- No loss caps or loss corridors are included in the contract;
- A 12-month notification period is required before the reinsurance can be terminated;
- Coverage for the run-off of all liabilities incurred on policies incepted prior to termination is included in the reinsurance contract;
- Coverage for any prior-year loss reserve development is ceded through the reinsurance arrangement; and
- Assuming company must have common ultimate ownership with, or control, of the board of directors of the reinsured company.

While meeting these expectations will most likely result in the assignment of the parent's rating, A.M. Best reviews the amount of protection afforded to policyholders within each contract and this review is the basis for the assignment of the financial strength rating. Companies that are provided reinsur-

ance protection which in A.M. Best's opinion does not sufficiently protect policyholders still can benefit from their group affiliation. Depending on the strength of the reinsurance contract and any other explicit and implicit support provided, the insurer can receive the same Best's Rating (without a reinsured affiliation code) as the other companies within the pool.

Guarantees

The use of guarantees for policyholder obligations at an operating level has grown in recent years, as companies look for ways to better utilize capital. A fully enforceable guarantee could protect policyholders while not moving capital. However, there is always the concern of enforceability and who has the authority to enforce the guarantee, as well as many other uncertainties in the application of a guarantee to thousands of individual policies.

Guarantees that are not specific to individual issuances or programs (as is typically the case in the guaranteed issuance of public debt) are given consideration as explicit support to an affiliate. These guarantees, however, do not automatically merit the application of the guarantor's rating. Pooling and reinsurance contracts provide specifically defined protection for policyholders of a company. Guarantees, however, are often less specific and cover a wider array of liabilities that create additional uncertainties that must be evaluated in considering the credit provided in the rating of a company.

The rating enhancement from a guarantee depends on several factors, including:

- To what the guarantee applies;
- Enforceability of the guarantee;
- Termination provisions of the guarantee;
- Regulatory conflicts;
- Termination notification — greater than 12 months is expected;
- Public disclosure of the guarantee;
- Cut-throughs that allow the company's claimants to enforce the guarantee directly against the affiliate;
- Coverage of the run-off of liabilities incurred on policies incepted prior to termination of the guarantee; and
- Stand-alone financial strength of the company being guaranteed.

Further, when the affiliate is a sister company or a subsidiary, questions arise about the guarantee's enforceability relative to holders of the guarantor's direct liabilities. Ultimately, the scale of the guaranteed liabilities relative

to the guarantor's capacity to pay them is considered through the rating of the guarantor.

Third-party legal opinions on the enforceability of a guarantee help to eliminate some of the concern, but they must address all the regulatory and statutory issues in each domicile that could reasonably apply to the guarantee.

In addition, the mechanics and authority for triggering the guarantee must be clear. When a guarantee applies to multiple issuances, such as multiple insurance policies, A.M. Best does not believe that all of these concerns can be completely alleviated.

If the guarantee applies to a limited number of issuances, the enforceability of the guarantee to each issuance will be considered in the same context as a guarantee applying to an individual issue. Recognition of guarantees is performed in the context of the financial strength of the guarantor, as well as the protection provided to the guaranteed company, with credit for capital occurring only once.

A guarantee that is not deemed fully enforceable is considered to be a form of explicit, although weak, support from the guarantor. A guarantee, by itself, does not warrant the assignment of the parent rating, nor is a guarantee a requirement for a company to be assigned its parent's rating.

Depending on the strength of the guarantee and other factors linking the importance of the guaranteed entity to the guarantor and the overall organization, the final rating outcome will vary between the stand-alone rating of the guaranteed entity and the rating of the guarantor. The importance of the operation to the organization, the relative size of the operation to the entire organization, and the financial performance of the operation are key factors. The demonstration of past explicit support of the operation also is considered in the evaluation of the organization's willingness to support the operation in the future.

In those cases where the enforceability of a guarantee is not certain, in order to give any rating enhancement for the explicit support provided by a guarantee, A.M. Best requires a minimum stand-alone financial strength of the guaranteed company which compensates for any concerns relating to the enforceability of the guarantee. The level of minimum stand-alone financial strength required will vary depending on the following factors:

- Level of strategic importance of the subsidiary to the parent perceived by A.M. Best;

- Differential between the subsidiary's stand-alone rating and the parent's rating;
- Level of the parent's rating;
- Trend in the parent's rating; and
- Level of the subsidiary's stand-alone rating.

There are cases where a guarantee meets the criteria to warrant rating enhancement,

but the published rating of the subsidiary does not change due to the status of these factors.

Other Financial Support

Other types of financial support, such as net-worth maintenance, stop-loss reinsurance and keep-well agreements, are evaluated individually as part of the stand-alone

Best's Interactive Financial Strength Analysis

A.M. Best's interactive financial strength assessment provides an objective opinion on the ability of a specific insurance operation to meet its ongoing obligations to policyholders. That opinion is derived from the analysis of many quantitative and qualitative measures, including comparisons to peers, industry standards and Best's proprietary benchmarks, as well as an evaluation of the insurer's operating plans, philosophy and management, future profitability and liquidity.

Best's Financial Strength Rating (FSR) scale ranges from the highest, "A++" (Superior), to the lowest, "F" (In Liquidation), and is divided into two broad categories — Secure and Vulnerable. Based on Best's Insolvency Studies, Secure-rated companies have experienced a very low failure frequency; significantly lower than Vulnerable-rated companies (and companies unrated or not followed by A.M. Best). The time frame for the ability of companies to meet their current and ongoing obligations to policyholders varies. The higher a company's Secure rating, the greater its ability to withstand adverse changes in underwriting and economic conditions over longer periods. Companies with a vulnerable rating (above "Poor") have only a current claims-paying ability.

The financial strength assessment involves ongoing, in-depth reviews and incorporates a host of public and proprietary financial data and information. It takes into account an evaluation of country risks (e.g., general government economic policies, exchange risks, financial reserves and interest rates) and country-specific insurance regulations. The analytical components of Best's interactive rating process involve numerous quantitative and qualitative factors that are grouped into three evaluative categories:

Balance Sheet Strength — This is a major determinant in a company's ability to meet its current and ongoing obligations to policyholders. For an insurer to remain viable

in the marketplace, it must perpetuate a financially strong balance sheet for its policyholders.

Operating Performance — When evaluating operating performance, Best's analysis centers on the stability and sustainability of the company's sources of earnings in relation to the liabilities that are retained by the company.

Business Profile — The factors that comprise an insurer's business profile drive current and future operating performance and, in turn, can affect long-term financial strength and the company's ability to meet its obligations to policyholders.

Ratings are approved and modified through a specific committee process, including an executive committee of A.M. Best senior officers. Going forward, Best's Ratings are reviewed formally at least every 12 months. A.M. Best's analysts maintain contact with company management throughout the year to monitor each company's ongoing performance. Ratings are re-evaluated continually for interim changes that might arise during the year, or in conjunction with Best's ongoing dialogue with company management.

For an insurance organization that issues debt, the analysis includes a review of trends in financial measures and ratios in order to evaluate the issuer's ability to service its debt/preferred obligations going forward. A.M. Best uses a broad range of financial measures and ratios in its quantitative analysis of issuers. Important factors in Best's Rating analysis include the evaluation of capital structures (i.e., financial leverage, hybrid credit, coverage and cash flow) and noninsurance company subsidiaries. As these issues influence the level of the FSR rating, they become part of the determination of Best's Issuer Credit Rating and related debt ratings.

Details on each aspect of the Best's Rating process are available at www.ambest.com.

analysis. If the support mechanism is new or not yet utilized, it will be considered within the evaluation of the rating enhancement assigned to the subsidiary.

Areas considered in these types of support are:

- Loss caps or loss corridors are not included in the contract;
- 12-month notification before the agreement is terminated;
- Coverage for the run-off of all liabilities incurred on policies incepted prior to termination of the protection provided;
- Coverage for any prior-year loss reserve development is included in the protection; and
- Company providing the protection, or its ultimate parent, must have 100% ownership of the subsidiary company. Any uncertainty over the ability and willingness of minority owners to participate in the protection must be clearly addressed.

Summary

The level and type of support provided by a parent to its operating entities continues to evolve and the strategic significance of any one subsidiary within a group can change. A.M. Best's evaluation goes beyond a review of contractual support and management's view of how important the company is to the organization. A.M. Best's evaluation also includes a subjective review of the level of commitment to a company over the long term.

When assigning ratings to companies within a group, A.M. Best's approach involves an analysis of each operating unit and the internal assignment of a stand-alone rating. Each operating unit then is evaluated as to the level of implicit and explicit support it receives from the parent and for its degree of importance to the group. Based on these analyses, the stand-alone ratings of members of insurance groups may be modified as appropriate, if at all.

GUIDE TO BEST'S FINANCIAL STRENGTH RATINGS

A Best's Rating is an independent opinion, based on a comprehensive quantitative and qualitative evaluation, of a company's balance sheet strength, operating performance and business profile. Best's Ratings are not a warranty of a company's financial strength and ability to meet its obligations to policyholders.

Financial Strength Ratings

A Best's Financial Strength Rating (FSR) is an opinion of an insurer's financial strength and ability to meet ongoing obligations to policyholders.

	Rating	Descriptor	Definition
Secure	A++, A+	Superior	Assigned to companies that have, in our opinion, a superior ability to meet their ongoing obligations to policyholders.
	A, A-	Excellent	Assigned to companies that have, in our opinion, an excellent ability to meet their ongoing obligations to policyholders.
	B++, B+	Very Good	Assigned to companies that have, in our opinion, a good ability to meet their ongoing obligations to policyholders.
Vulnerable	B, B-	Fair	Assigned to companies that have, in our opinion, a fair ability to meet their current obligations to policyholders, but are financially vulnerable to adverse changes in underwriting and economic conditions.
	C++, C+	Marginal	Assigned to companies that have, in our opinion, a marginal ability to meet their current obligations to policyholders, but are financially vulnerable to adverse changes in underwriting and economic conditions.
	C, C-	Weak	Assigned to companies that have, in our opinion, a weak ability to meet their current obligations to policyholders, but are financially very vulnerable to adverse changes in underwriting and economic conditions.
	D	Poor	Assigned to companies that have, in our opinion, a poor ability to meet their current obligations to policyholders and are financially extremely vulnerable to adverse changes in underwriting and economic conditions.
	E	Under Regulatory Supervision	Assigned to companies (and possibly their subsidiaries/affiliates) that have been placed by an insurance regulatory authority under a significant form of supervision, control or restraint whereby they are no longer allowed to conduct normal ongoing insurance operations. This would include conservatorship or rehabilitation, but does not include liquidation. It may also be assigned to companies issued cease and desist orders by regulators outside their home state or country.
F	In Liquidation	Assigned to companies that have been placed under an order of liquidation by a court of law or whose owners have voluntarily agreed to liquidate the company. Note: Companies that voluntarily liquidate or dissolve their charters are generally not insolvent.	
S	Suspended	Assigned to companies that have experienced sudden and significant events affecting their balance sheet strength or operating performance whereby the rating implications cannot be evaluated due to a lack of timely or adequate information.	

Rating Modifiers and Affiliation Codes

A rating modifier can be assigned to indicate that a Best's Rating may be subject to near-term change (under review), that a company did not subscribe to Best's interactive rating process (public data) and that the rating is assigned to a syndicate operating at Lloyd's. Affiliation codes (g, p, and r) are added to Best's Ratings to identify companies whose assigned ratings are based on group, pooling or reinsurance affiliation with other insurers.

	Modifier	Descriptor	Definition				
Rating Modifiers	u	Under Review	A modifier that generally is event-driven (positive, negative or developing) and is assigned to a company whose Best's Rating opinion is under review and may be subject to change in the near-term, generally defined as six months.				
	pd	Public Data	Assigned to insurers that do not subscribe to Best's interactive rating process. Best's "pd" Ratings reflect qualitative and quantitative analyses using public data and information.				
	s	Syndicate	Assigned to syndicates operating at Lloyd's.				
Affiliation Codes		g	Group	p	Pooled	r	Reinsured

Not Rated Categories (NR)

Assigned to companies reported on by A.M. Best, but not assigned a Best's Rating. The five categories are:

NR-1: Insufficient Data.	NR-2: Insufficient Size and/or Operating Experience.	NR-3: Rating Procedure Inapplicable.
NR-4: Company Request.	NR-5: Not Formally Followed.	

Rating Outlook

Best's Ratings (A++ to D) are assigned a Rating Outlook that indicates the potential direction of a company's rating for an intermediate period, generally defined as the next 12 to 36 months. Public Data Ratings are not assigned an Outlook. Rating Outlooks, which appear in the rating rationale section of the company's *Best's Company Report*, are as follows:

Positive	Indicates a company's financial/market trends are favorable, relative to its current rating level and, if continued, the company has a good possibility of having its rating upgraded.
Negative	Indicates a company is experiencing unfavorable financial/market trends, relative to its current rating level and, if continued, the company has a good possibility of having its rating downgraded.
Stable	Indicates a company is experiencing stable financial/market trends and there is a low likelihood that its rating will change in the near term.

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GUIDE TO BEST'S CREDIT RATINGS

A Best's Rating is an independent opinion, based on a comprehensive quantitative and qualitative evaluation, of a company's balance sheet strength, operating performance and business profile. Best's Ratings are not a warranty of a company's ability to meet its financial obligations.

Long-Term Credit Ratings

A **Best's Long-Term Debt Rating** (issue credit rating) is an opinion as to the issuer's ability to meet its financial obligations to security holders when due. These ratings are assigned to debt and preferred stock issues.

	Rating	Descriptor	Definition
Investment Grade	aaa	Exceptional	Assigned to issues, where the issuer has, in our opinion, an exceptional ability to meet the terms of the obligation.
	aa	Very Strong	Assigned to issues, where the issuer has, in our opinion, a very strong ability to meet the terms of the obligation.
	a	Strong	Assigned to issues, where the issuer has, in our opinion, a strong ability to meet the terms of the obligation.
	bbb	Adequate	Assigned to issues, where the issuer has, in our opinion, an adequate ability to meet the terms of the obligation; however, is more susceptible to changes in economic or other conditions.
Non-Investment Grade	bb	Speculative	Assigned to issues, where the issuer has, in our opinion, speculative credit characteristics, generally due to a moderate margin of principal and interest payment protection and vulnerability to economic changes.
	b	Very Speculative	Assigned to issues, where the issuer has, in our opinion, very speculative credit characteristics, generally due to a modest margin of principal and interest payment protection and extreme vulnerability to economic changes.
	ccc, cc, c	Extremely Speculative	Assigned to issues, where the issuer has, in our opinion, extremely speculative credit characteristics, generally due to a minimal margin of principal and interest payment protection and/or limited ability to withstand adverse changes in economic or other conditions.
	d	In Default	In default on payment of principal, interest or other terms and conditions. The rating also is utilized when a bankruptcy petition, or similar action, has been filed.

A **Best's Long-Term Issuer Credit Rating (ICR)** is an opinion as to the ability of the rated entity to meet its senior obligations. A.M. Best also uses its Long-Term Credit Rating Scale when assigning Issuer Credit Ratings. While the above definitions apply to entities which do not issue insurance obligations, in certain markets or product lines, particularly where the credit market scale is widely recognized, A.M. Best also assigns Issuer Credit Ratings to insurance companies. The definitions applied to insurance companies that are assigned an Issuer Credit Rating are as follows: (aaa) - Exceptional; (aa) - Superior; (a) - Excellent; (bbb) - Very Good; (bb) - Fair; (b) - Marginal; (ccc-cc) - Weak; (c) - Poor.

Ratings from "aa" to "ccc" may be enhanced with a "+" (plus) or "-" (minus) to indicate whether credit quality is near the top or bottom of a category. A company's Long-Term Credit Rating also may be assigned an Under Review modifier ("u") that generally is event-driven (positive, negative or developing) and indicates that the company's Best's Rating opinion is under review and may be subject to near-term change. Ratings prefixed with an ("i") denote indicative ratings. Ratings may also be assigned a Public Data modifier ("pd") which indicates that a company does not subscribe to A. M. Best's interactive rating process.

Short-Term Credit Ratings

A **Best's Short-Term Debt Rating** is an opinion as to the issuer's ability to meet its obligations having maturities generally less than one year, such as commercial paper.

	Rating	Descriptor	Definition
Investment Grade	AMB-1+	Strongest	Assigned to issues, where the issuer has, in our opinion, the strongest ability to repay short-term debt obligations.
	AMB-1	Outstanding	Assigned to issues, where the issuer has, in our opinion, an outstanding ability to repay short-term debt obligations.
	AMB-2	Satisfactory	Assigned to issues, where the issuer has, in our opinion, a satisfactory ability to repay short-term debt obligations.
	AMB-3	Adequate	Assigned to issues, where the issuer has, in our opinion, an adequate ability to repay short-term debt obligations; however, adverse economic conditions will likely lead to a reduced capacity to meet its financial commitments on short-term debt obligations.
Non-Investment Grade			
	AMB-4	Speculative	Assigned to issues, where the issuer has, in our opinion, speculative credit characteristics and is vulnerable to economic or other external changes, which could have a marked impact on the company's ability to meet its commitments on short-term debt obligations.
	d	In Default	In default on payment of principal, interest or other terms and conditions. The rating also is utilized when a bankruptcy petition, or similar action, has been filed.

A **Best's Short-Term Issuer Credit Rating (ICR)** is an opinion as to the ability of the rated entity to meet its senior financial commitments on obligations maturing in generally less than one year. A.M. Best also uses its Short-Term Rating Scale when assigning Issuer Credit Ratings. A company's Short-Term Credit Rating also may be assigned an Under Review modifier ("u") that generally is event-driven (positive, negative or developing) and indicates that the company's Best's Rating opinion is under review and may be subject to near-term change. Ratings prefixed with an ("i") denote indicative ratings.

Rating Outlook

Best's Credit Ratings (aaa to c) are assigned a Rating Outlook that indicates the potential direction of a company's rating for an intermediate period, generally defined as the next 12 to 36 months. Public Data Ratings are not assigned an Outlook. Rating Outlooks are as follows:

Positive	Indicates a company's financial/market trends are favorable, relative to its current rating level, and if continued, the company has a good possibility of having its rating upgraded.
Negative	Indicates a company is experiencing unfavorable financial/market trends, relative to its current rating level, and if continued, the company has a good possibility of having its rating downgraded.
Stable	Indicates a company is experiencing stable financial/market trends and that there is a low likelihood that its rating will change in the near term.

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