The Agency for Co-operative Housing
L'Agence des coopératives d'habitation

Q&A

Questions and Answers about Your Annual Risk Rating

What is risk rating?

Risk rating is a technique the Agency for Co-operative Housing uses to see how stable your co-operative is. It is a way to measure your financial strength that helps us assess your co-op's capacity to pay its bills and provide housing of good quality, now and in the foreseeable future. The final result of the Agency's risk-rating process is a composite risk rating for each co-op.

Important as it is, risk rating does not reveal the whole truth about your co-op. It has nothing to say about member involvement or the richness of your community life. Risk rating makes no definite statement about the quality of your management or governance or whether your co-op is complying with its CMHC agreements. This is discussed in a different report.

How does risk rating help my co-op?

Our composite risk rating gives your co-op the recognition it deserves when it is operating well. The Agency hopes that a risk rating of **Low** or **Moderate** will encourage the best-run co-ops to keep up the good work and aspire to do even better.

At the least, a risk rating of **Above Average** is a warning signal that a co-op is not as healthy as it could be. By sharing this rating with a co-op, we hope to help the co-op's board recognize a growing problem. The co-op may need to take corrective action with support from the Agency and perhaps CHF Canada or a local federation. Or it may be able to steer carefully through a weak market or a period of physical renewal.

Our risk rating can also point to danger signs that confirm the existence of more serious difficulties. A rating of **High** tells you that the co-op needs to address its problems without delay if it is continue operations over the long term.

The Agency's risk assessment also shows how a co-op's health is changing over time and what it will look like if the trend continues. This information may tell co-ops more than a snapshot taken at a particular moment.

How did the Agency come up with my co-op's Composite Risk Rating?

The Agency used several tools to build your co-op's composite risk rating:

1. **The Annual Information Report (AIR)**

   Your auditor filed your co-op's AIR over the Internet, drawing information from your latest year-end financial statements and other records. The Agency reviewed the AIR and accepted it as valid once it was complete and supported by the necessary documents.

2. **Risk Analysis**

   We put the information collected electronically through two automated tests:

   - a test of your financial strength (Liquidity Ratio)
   - a test of your current financial performance (Net-Income Ratio)

3. **Physical-Condition Rating**

   In a separate process, the condition of your co-op's property was assessed. We added the resulting Physical-Condition Rating to our information system to provide more data for the Composite Risk Rating.

4. **Further Indicators of Risk**

   These indicators are serious enough to raise the risk rating of any co-op where even one of them is found. They include being behind with mortgage payments or property taxes, not having the recommended level of insurance or getting an adverse opinion or denial of opinion from your auditor on your year-end financial statements.

5. **System-Generated Risk Rating**

   Our information system rolled together the liquidity ratio, net-income ratio, physical-condition rating and further indicators of risk into a system-generated rating of your co-op's risk level.

6. **Assigning the Composite Rating and Trend**

   Your relationship manager at the Agency looked at the system-generated rating and, using their best judgement, raised, lowered or accepted it. A rating can change because of what the Agency discovers when following up with your co-op after reviewing your AIR. Other knowledge your relationship manager has about your co-op and the marketplace around you could also explain a raised or lowered risk rating. Your relationship manager's final step is to assess whether your co-operative's situation is about the same, getting better or getting worse.

Will our rating change before next year?

If new information on your co-op's condition or operations comes to the Agency's attention or the co-op takes action on problems the risk assessment has brought to light, your composite risk rating could change during the year.

What do these ratios and ratings mean?

Liquidity Ratio

The liquidity ratio sums up your co-op's results from the time it began to the end of your last fiscal year. It measures how many months' property-tax, mortgage and average utility payments your co-op can meet at year end, after allowing for any amounts you owe on that date. If your co-op pays an annual rent for leased land, this charge is also taken into account.

The ratio is complex, so we have posted it on our website at Liquidity for those who would like to view it in more detail.

Net-Income Ratio

The net-income ratio tells us how well you did in your last reported year. Its focus is on whether the co-op earned enough to meet all its operating and debt-service costs and make a reasonable contribution to its replacement reserve. You can find the formula on our website at net income.

Physical-Condition Rating

The physical-condition rating is based on a visual inspection of your co-op, normally undertaken once every 24 months. The inspection focuses on the grounds, building exteriors, internal service and public areas, and any vacant units. Appearance, maintenance, structure and systems, and health and safety factors all contribute to your co-op's rating.

What are the possible composite ratings?

There are four possible composite risk ratings and three trends:

- High Risk and Strengthening, Stable or Weakening
- Above-Average Risk and Strengthening, Stable or Weakening
- Moderate Risk and Strengthening, Stable or Weakening
- Low Risk and Strengthening, Stable or Weakening.

The full definitions are available [on our website].

What does the Agency mean by trend?

The Agency has fine-tuned the risk assessment to show how the situation of a co-op is changing over time and where it is heading. We have started to talk about trends because the liquidity and physical-condition ratings are slow to change. Over several years a co-operative can work hard to improve its operations without much movement in either of these indicators. Even improving the net-income ratio can take several years. Yet, although the building blocks of the co-operative's risk assessment have not changed, a relationship manager knows when a co-operative's situation is Strengthening. Trend analysis allows the Agency to identify and acknowledge a co-op's improving circumstances, even if its risk profile is unchanged.

The risk trend of Stable indicates that there is little change in the co-operative's situation, which can be good or bad, depending on its risk rating. Where the risk rating is positive, so is a Stable situation, which shows that the co-operative is continuing to manage its finances effectively and take good care of its property. However, a Stable situation is not good where a co-operative has a risk rating of Above Average or High. This rating suggests either that the co-operative needs to do more to solve its problems, or that it is successfully keeping its operations from worsening while it works on solutions.

Nothing good can be said about a risk trend of Weakening. This score is a red flag for any co-operative with a positive risk rating, suggesting that it should look to the flaws in its management and governance before its problems grow. If the trend continues, the co-op's membership will lose the benefits of the good decisions and hard work in past years that earned the co-operative its positive risk rating.

A risk trend of Weakening is even more serious in a co-operative risk rated Above Average or High. This rating warns that its management may not be effective enough for its challenging situation.

Was this all the Agency looked at?

At the same time we carried out a risk assessment of your co-op, the Agency also checked that you had been doing what you said you would when you signed your operating agreement with CMHC. (We call this a compliance review). This review does not have the same focus as our risk assessment, but it could influence your composite risk rating. The results appear in a separate report.

Who gets to see all this information?

The Agency protects your co-op's composite risk rating and other data. This information is not available to the general public, although your co-op's results will be combined with those of other co-ops in our public reports about how different groups of our co-op clients are performing.

The Agency will only share your co-op's individual risk rating with

- members of the Agency's staff
- Canada Mortgage and Housing Corporation, on request,
- service organizations you belong to, such as CHF Canada, and
- professionals you deal with, provided your co-op has signed a consent to share information for its own benefit.

To find out more about our rating system and how we use the results, visit our website at www.agency.coop or contact your co-op's relationship manager at the Agency.

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