Ratings Matter (Most of the Time)

Insurance company ratings are a big deal. So are the ratings you receive as an advisor. How do these two very different types of ratings intersect? It comes down to how your clients think you are looking out for them and how much attention you pay to any assets that play a role in your comprehensive planning.

Advisors have the responsibility to assure their clients that the coverage they own is real and should perform as expected. Of course, it is not the advisor's responsibility to vouch for any particular carrier, but it is a best practice to pay attention to which carriers are being relied upon and whether they remain in good financial condition.

Life insurance companies have made very long term promises to your clients. If those promises can't be met in the future due to a decline in the financial strength of the carrier, your clients can find themselves in a very difficult situation. This can be made worse by the fact that your clients will have gotten older and may have had a decline in their health. And as we have now seen with long term care products, some alternate products may no longer be available when a replacement is needed.

One of the best due diligence steps advisors can take is to periodically review carrier ratings. This can be quite simple, and AdvisorServe is here to help. With the help of Partners Financial, we maintain a list of the 35 primary carriers we encounter. On that list are key ratings: A.M. Best, Standard & Poor's, Moody's, and Fitch. In addition, we have the comparable rankings of the carriers (Comdex), and we maintain the ALIRT qualitative reports on the carriers in the group. This list is now posted on our website. Carriers on the list are quite strong, and none of them is ringing any alarm bells right now.

Since ratings can change, we are happy to update the ratings for any carrier you are addressing. We are also happy to share the qualitative ALIRT report for an individual carrier if one is available.

As much as we have said about the importance of ratings, here's an important caution: be careful that you don't overrate the ratings. Here's what I mean. The carriers on our list share these strengths:

1. Top 4 ratings classes of the 15 ratings classes at A.M.Best
2. Top 7 ratings classes of the 20 ratings classes at Standard & Poor's
3. Top 7 ratings classes of the 21 ratings classes at Moody's
4. Top 6 ratings classes of the 21 ratings at Fitch
5. All but three rank in the top 20% of all carriers as measured by Comdex, and the others are in the top 30%

As remarkable as this group might be, some agents may tell you there is a serious reason to narrow your market to only those carriers in the top 1-5%. (Of course, such claims almost always come from an agent who is the captive of one of the largest carriers). We disagree strongly. Let me share a conversation I participated in between the chairman of a major life insurance company and his top agents. We asked the chairman, why didn't his company reach for a rating of A++ with Best's, rather than staying in second position with an A+. His answer was striking. He told us that he had no intention of qualifying for an A++ rating. That's right, he didn't want it. Why? He went on to explain that the underlying bonds held by the insurance company in its general account were highly rated and generated a very attractive rate of return for the company. One of the things he would have to do to improve his rating with Best's to an A++ would be to reallocate company bond investments into lower-yielding bonds. Any good wealth manager knows that this would significantly dampen the overall investment returns for the carrier.

Our conversation with the company chairman was telling. A slight change in ratings may be of little importance more than bragging rights. Do you think that changing the oil in your car every 1,000 miles will be much better than meeting factory recommendations for the interval between oil changes? Do you think that you should never leave your house with anything less than an absolutely full tank of gas in your car? The same can be true with the selection we make in life insurance companies. There are other considerations, including who will give us better pricing based on health assessments, who actually pays higher dividend rates or at least keeps them stable, and who offers product designs that are better fits for our clients.

Just to take this one step further, it seems to me intuitively that in order to have the best ratings, some carriers will not only have poorer investment results. They might also pay out lower dividends to keep as much capital internally as possible. They might also give fewer exceptions when setting pricing for client medical conditions, and they might design products with more profit.

"Ultimately, clients might be paying too high a price for the carrier with the 100 Comdex rating, when very strong carriers are offering superior products, superior pricing, or superior performance."

We have also seen this issue appear from a very different perspective. Agents for carriers with the highest ratings may use their highest financial ratings to compete against comparable or even better products. And for the aggressive agents in this group, I should remind them that in most states it is considered unethical to misrepresent the financial condition of a competing insurer (see, for example, GA Code Section 33-6-4). So, our best advice is to put up your defenses when an agent tells you that his company's superior ratings are a reason to buy their products, when compared to the products of another very strong carrier with good ratings.

If you are an independent wealth manager, be independent. Watch those carrier ratings for your clients. Low or falling ratings should ring some alarm bells. Strong ratings (top 20% or so) are one factor that is easy to check out. Then, you need to move on to observing what was sold and determining if it continues to meet client objectives. Pricing, competitiveness, sufficiency of funding, and client health remain key factors you can and should be tracking on a regular basis. AdvisorServe is here to help you do all of this. Contact us whenever you have a client that could use a good policy review.

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