PROCEEDINGS OF THE NATIONAL INSURANCE CONVENTION OF INSURANCE COMMISSIONERS OF THE UNITED STATES. TWENTY-FIRST SESSION AT CLEVELAND, OHIO, AUG. 20, 21, 1890

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TWENTY-FIRST SESSION

AT

CLEVELAND, OHIO,

AUG. 20, 21, 1890.

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PROCEEDINGS.

The Convention met according to notice at 10 o'clock A.M., on Wednesday, August 20, at the Stillman House, Cleveland, O., President Merrill in the Chair. Owing to the absence of the secretary, who was detained en route, the Convention took a recess until 2 o'clock. On reassembling, the president said: —

GENTLEMEN OF THE CONVENTION: — We may congratulate ourselves upon the pleasant auspices under which we assemble. This is practically our "freedom day," being the twenty-first session of this organization. Surely, as we turn back the pages of the record of this period, we can review the results with no little satisfaction. Twenty years ago the business of insurance, especially in the life department, while not exactly in its infancy, had experienced but a modest growth; there was little uniformity in the methods of official supervision or even as to legal requirements, and each department had a series of blanks differing from every other, necessitating the preparation by the companies of special annual reports to each one of the States requiring such a return to be made. Within this period the business of fire insurance has been enlarged, simplified and strengthened; and that of life insurance has grown to marvellous proportions, to a magnitude beyond the most extravagant dreams of its promoters in the year when this Association was formed. Our organization has not only afforded the means of a better performance of our duties, through the advantage of mutual acquaintance and the interchange of ideas, but its direct practical result in the one direction of making clear, definite and uniform the blank forms in use has been of incalculable benefit to the companies, the department and the public. To-day in this country no business over which there is official supervision or control approaches in its magnitude and importance that of insurance, and no other comes so close to the homes and hearth-stones of the people of all classes and conditions. There is no antagonism between the interests of the insurance companies and the interests of the insured. What is, in the broad and comprehensive sense, wisest for the one, is best for the other; and the duty of those at the head of the various insurance departments is alike to foster and strengthen on the one hand, and to guard and protect on the other. Believing fully in the usefulness of these gatherings, I trust the meetings of the future will find every department represented.

The roll of States was then called by Secretary Luper, the following responding: —

Colorado. — L. B. Swanbeck, auditor.

Missouri. — C. P. Ellerbe, superintendent; A. F. Harvey, actuary.

Massachusetts. — Geo. S. Merrill, commissioner.

Connecticut. — J. H. Sprague, actuary.

Nebraska. — C. B. Allan, deputy auditor.

Kansas. — James Billingslea, deputy commissioner.

Kentucky. — J. A. Coons, actuary.

Rhode Island. — E. W. Bucklin, auditor.

Ohio. — W. H. Kinder, superintendent; J. A. McEwen, deputy superintendent.

Pennsylvania. — Geo. B. Luper, deputy commissioner.

Wisconsin. — Philip Cheek, Jr., commissioner.

The President. Committees of the various insurance companies in this city, in accordance with the custom of previous years, have invited the members to accept of some little entertainment at their hands. The fire underwriters suggest that we take with them a drive about the city, and they would like to meet us at 3 o'clock to-morrow for that purpose. We also have an invitation from the life underwriters to a lunch, and they suggest 7 P.M., to-morrow.

The invitations were accepted by a unanimous vote.

On motion, the papers prepared by members were read, the first being that of Mr. Sprague of Connecticut.

VALUATION OF POLICIES BY INSURANCE DEPARTMENTS.

My purpose herein is to bring into clear view certain prevalent errors in the valuation of policies, to exhibit their magnitude, and thereby to show the need of correction.

One of the fundamental methods of valuing a policy is to ascertain the present worth of the benefit, and from it deduct the present worth of all the net premiums to be paid by or for the policy. The remainder is its value. It is obvious that the value of the benefit (which is the net single premium) is greater the shorter the interval during which payment is deferred, as in the case of any other contract for the payment of money. Again, if the premium be payable oftener than once a year, the more frequent the payments, the greater will be the probability of the insurer losing half a year's premiums in the year in which the life fails. To make up for this probable loss, the premium must be increased, and the policy-value will be increased correspondingly.

Bearing these things in mind, the fact may be perceived that, if a mortality table and a rate of interest be prescribed, the value of a policy will depend upon two things, and two only; viz., the terms of the payment of the benefit, and the terms of the payment of the premium. These two variables wholly determine the policy-value, therefore strict regard must be paid to them, if correct results are desired. Wherein due regard for one or both of these components of value is neglected, is now to be shewn.

Forty or fifty years ago, policies by their terms became due and payable at the end of the policy-years in which the assured severally died. Approximately this period would, on an average, be six months after death. Upon this basis the net premiums and the values of policies were then very properly computed, and the valuation tables made up which are in use to-day. Since that date, however, the time of payment has been changed and reduced, from six to four months after death, from four to three, from three to two, and from two to zero; the custom having become general to pay claims immediately upon receipt of proof of death. Thus, by modern practice, the insurer loses six months' interest on the reserve, which under the original practice he would have received, and, indeed, must have received, in order that the policy might be full and entire at maturity. To make up for this loss, the net premium must be increased correspondingly, and increased premium gives a larger policy-value.

Notwithstanding this reduction of six months in the time within which death-claims become payable, insurance departments and offices continue to value policies the same as if no such change in terms had occurred, and just the same as they would have done, or did, forty-five years ago. Note the effect on policy values.

At the opening of a policy, the initial value is the premium then paid. The following tabulation exhibits, in column marked (1), the annual premium customarily valued, being the premium for a policy of $10,000 payable at the end of the policy-year of death; in column (2), the true premium for the policy of practice, payable at death; in column (3), the differences between the premiums in (2) and those in (1); and in column (4), the percentage of excess of (2) over (1) at the several ages specified. The experience table of 1842 and four per cent. interest are presupposed, and net (or cost) premiums only are dealt with.

TABLE 1.

ENTRY AGE.	(1) Premium now valued.	(2) True Premium or Value.	(3) Differences of (2) and (1).	(4) Excess Per Cent. of (2) over (1).
10, ...	$104.296	$106.366	$2.070	1.98
20, ...	129.513	132.082	2.569	1.98
30, ...	169.720	173.086	3.366	1.98
40, ...	236.775	241.469	4.694	1.98
50, ...	357.757	364.857	7.100	1.98
60, ...	575.562	587.016	11.454	1.99
70, ...	982.027	1,001.698	19.671	2.00
80, ...	1,760.979	1,796.755	35.776	2.03
90, ...	3,638.884	3,715.538	76.654	2.11
95, ...	5,927.131	6,060.531	133.400	2.25
99, ...	9,615.385	9,860.819	245.434	2.55

These are the initial or starting values immediately after the first premiums are paid. From age ten to age fifty, inclusive, the true premium exceeds the premium upon which the usual valuation tables are based by 1.98 per cent., which is six months' compound interest, where the effective annual rate is four. The excess ranges from 1.98 to 2.55 per cent.

These are the initial differences. As the duration of a policy increases, the original difference in value increases. Let us see how much, by taking a policy of $10,000, issued at age thirty-five, which is about the average age of entrants, and noting the value at the end of ten, twenty, thirty, etc., years' duration. The initial difference is 1.98 per cent.

TABLE 2.

DURATION, . .	10	20	30	40	50	60	65
True values, . . .	$1,360 58	$3,073 48	$4,943 31	$6,692 44	$8,096 75	$9,280 99	$10,255 97
Values in vogue, . .	1,334 12	3,013 47	4,846 38	6,560 10	7,933 06	9,075 88	10,000 00
Difference, ...	$26 46	$60 01	$96 93	$132 34	$163 69	$205 11	$255 97
Difference per cent., .	1.98	1.99	2.00	2.02	2.06	2.26	2.56

The percentage of excess corresponds with the rate at the age attained in the preceding table.

From the foregoing it appears that, by the methods in general use, assurance policies are undervalued by about two per cent.; and this rule holds good whether the assurance be for life or for a shorter term, immediate or deferred, and whether the premium be single, limited to a fixed number of payments, annual, or more frequent.

Endowment assurances, however, are not affected to the same extent. These being a combination of temporary assurance and endowment, the endowment portion is correctly valued, and the undervaluation applies only to the temporary assurance part. These policies probably average to mature, as respects the endowment, at from age sixty to age sixty-five. Now the premiums at ages thirty, thirty-five and forty, for policies maturing respectively at sixty, sixty-three and sixty-five, is about one-half of it for the assurance and one-half for the endowment. Therefore, it is fair enough to say that endowment assurances policies are, on an average, undervalued about one per cent.