You Take the High Rate and I'll Take the Low Rate.....

Some aspects of fire insurance, from two viewpoints—those of insured and insurer; why there are so few arsonists in Bilibid and why you pay the rates you do for fire protection

A Manila business man with some interest in the subject told us the other day, "For some years past my company has placed its fire insurance in London, direct, and we save about 50% of the cost of insurance if placed through a local agent". When a business concern in these depression times can make a bona fide saving of 50% or anywhere near it, in an item as necessary as fire insurance, it is likely to jump at the chance.

But there is an Ethopian in the kindling some place, for one finds that similar concerns prefer to place their insurance with local agents, and figure that it is, in the end, cheaper to do so. And better business, for other reasons which will shortly appear.

If you step off of a rice paddy dike in flood time, you will find that the mud on one side is just as deep as on the other; and you may consider that the same is true of the fire insurance business in the Philippines.

As seen by the group who place their insurance abroad, direct, (let us call these Group One, for convenience), the facts line up about as follows:

1. Lloyds of London, which is practically the only group with which local businesses place foreign insurance; do not here or any other place in the world belong to tariff fixing bodies nor do they maintain deposits or legal reserves. They fix their own rates, here as elsewhere—these rates being sometimes lower, sometimes the same, and sometimes higher, than existing rates in whatever locality the risk is underwritten. It so happens that the rates charged here on some risks have been lower than local rates; maintaining no offices outside of London, and putting up no deposits, their overhead expenses are much lower, which principally accounts for the difference.

2. If such a foreign group as Lloyds is willing to underwrite a risk in the Philippines for lower rates than those charged by local agents, why should not a local business man take the saving?

That about sums up the case as seen by Group One; but, as can readily be seen, it takes no account of the problems of the local agent, and the factors which may affect rates locally quoted (if they are actually higher, which is disputed by some).

It is only fair to mention here that if any member of Group One should have a fire loss, and the foreign group with which he places his insurance should dispute his claims, no suit to recover could be brought in local courts. Such a suit would have to be filed in London, which would involve additional expense and loss of time; and also, we are informed, there is wide variation between local insurance laws and British, which might figure to the disadvantage of local concerns in such an eventuality. So far as we can learn, such a thing has not yet occurred, but remains an ever-present possibility.

Let us see what affects rates here. First factor of course is the losses due to fire, a figure which in the depression years has mounted steadily, and alarmingly. The more fires there are, the more losses the insurance companies have to pay, and the higher premiums they must charge—for, after all, there is only one place the money can come from with which to pay losses, and that is from premiums received (and, if they aren't enough, from reserves). Losses have increased greatly in the past few years. One prominent local agent says that for a large group of fire insurance companies in 1931, the loss ratio was as much as 94% (later figures not available.) For the years 1920-'30, inclusive, the loss ratio was 49.94% of total premiums received (average for all companies doing business in the P. I.) Yet during the same period, *rates* were *lowered* nearly 33%, taking into account better facilities for fire prevention, better construction of buildings, and so on. But what happened? The rate line was going downward; then suddenly the loss line started upward (depression), and the two lines met with a crash which sent many local agents reeling away, dripping red ink from many a business wound. It was terrible. But no one was killed. Why? That's another part of the story from Group Two (those who prefer to deal with local agents).

The reason why no one was killed is because the insurance laws of the P. I. are the non-shatterable glass behind which the insuranc companies ride safely through the bumps. These provide, first of all, for a deposit, on call of the insurance commissioner at all times, of a fund of ₱100,000 for each foreign insurance company represented by a local agent (excepting that an agent representing more than one foreign insurance company of the *same type*, such as more than one fire insurance company, need not in some cases put up ₱100,000 for each of them.) Figures for 1931, for instance (no material change since), showed that foreign insurance companies represented by local agents had a total of ₱1,724,000 invested here in Philippine bonds; ₱3,804,000 in local banks in cash; and ₱1,394,000 in U. S. bonds—nearly ₱7,000,000 actually invested here in the Philippines in that one item alone. This is a burden not borne by outside companies, and one reason why they may occasionally be able to quote lower rates than can local agents.

As to the justice of the laws which permit the placing of insurance outside the islands while penalizing local agents, there is perhaps a good bit to be said, and the local agents say it. But we won't go into that.

A second provision of the insurance laws, for safety, is the legal reserve. The law requires 33-1/3%; but we are informed that most companies carry 40% and some as high as 50%, of their premium income, in this item. Quite an item. Add it, too, to the cost of local agents' doing business, for it has an important bearing on the discussion.

Last, the cost of doing business in this fire insurance (sh we say "game"?—it would seem to be a word that is not c of place, as later paragraphs will show) figures out to average, they tell us, of 47% of premium income. Tha too, is a lot of many—all spent right here, of course.

So, we take our pencil and begin to add a few of the figures together—a minimum of 33-1/3% for legal reserve. plus 47% for cost of doing business; plus a certain percentage for interest on the ₱7,000,000 on deposit; plus a loss ratio of practically 50% of total premium income—and what is the total? 130-1/3%. Deduct your excess legal reserve at the end of the year, or deduct all of it—and it leaves you just about what the insurance companies which are lucky hope to make—3% of premium income. Or that is what they used to figure on, in the years 1920-'30, inclusive. Now that the loss ratio has mounted so much higher, they figure on writing their profits in red ink—on loss rather than gain.

What about the mounting fire losses? Much has been written and said on this subject, and much of it is misleading. In the first place, it is by no means a local condition but a worldwide one, and is always a characteristic symptom of depression times. Our loss rate, while high, is not the highest in the world (but comes too close to it for comfort, as we have seen). And it has apparently little to do with race, creed or color, for the losses mount in depression times among all peoples.

(Please turn to page 18)

You Take the High Rate...

(Continued from page 7)

Now, it is perfectly obvious to everyone that if losses suddenly mount when times are hard, the reason therefor is not an act of God, but incendiarism. A good fire can make a man a lot of money, and has made many a man a lot of money in these last few years, not only here, but elsewhere.

We have an excellent arson law in the Philippines. If we could only convict anyone under that law, we would certainly have them dead to rights. But convictions are next to impossible under our laws of evidence. As a recent *Bulletin* editorial puts it, unless a man announces to the whole community that he is going to commit arson on his property, and then lets the whole community see him do it, a conviction can't be had. Any insurance agent will tell you that a huge percentage of fires lately are incendiary, yet insurance companies have, except in exceedingly rare cases, had to pay such claims along with the legitimate ones; although they have often taken cases to court first.

Take two stores, each selling bicycles of the same make, imported from the same manufacturer. One, let us say, is required to pay import duties, income taxes, and what not, to run up his cost of business; the other is required to pay none of these items. Naturally the fellow who has no expenses to pay out can give you the bicycle for less money than the other one—if he will. But is it fair? The local agents say no; but on the other hand, the man who is buying insurance says, "Let me buy where I can get most value for my money." There is much to be said on both sides of the question.

On the whole, it appears that this much is true: no local agent wants to hold rates up any higher than necessary to cover the costs of doing business and leave him a small profit. If he did, he would lose out, for although there is an association which attempts to fix rates for all companies, there is actually *quite a variation in rates even among members of the association.* That constitutes one form of competition, and tends to keep down rates. It also appears that there may be some actual discrimination on which works out in favor of foreign companies unrepresented in the islands. There is a slightly higher tax rate charged on such insurance; but this apparently is not sufficient to offset the higher cost of doing business incurred by local agents, as shown elsewhere in this story.

Undoubtedly the most serious situation at present is the high loss ratio. The one sure way to normalize this figure is to find a cure for the depression; legislation alone, even if enacted, would not do it. If this figure could be flattened out to normal, it would bring a lot of insurance companies out of the red, and possibly bring down rates somewhat too; though this latter is by no means a sure thing, according to others.

It appears also that the only reason why any Philippine business man would place fire insurance direct with a foreign company is to save money; if the rates were the same, obviously the proper course would be to keep the business at home. At least, the *helpful* thing is to keep *all* business of this kind at home.

How to do it? Legislate to prevent the placing of insurance direct with foreign companies? Increase the tax penalty for doing so? Legislate to try to minimize losses through arson, thus perhaps making possible a reduction in local agent's rates? Or appeal to patriotism at the expense of the pocketbook?

It would be a fine thing for business if all insurance premiums were paid in to local companies or agents, instead of to outside companies. This can not happen until rates are equalized in all risks. Whether this will be accomplished by an upward revision of foreign rates, artificially brought about or by a downward revision of local rates, only possible by a decided change in conditions mentioned, is still a question.

It remains perfectly true, even in times of depression, that some business men are better