FIRE INSURANCE RATE-MAKING

(W. T. Emmet, N. Y. Superintendent of Insurance.)

When the average man talks about insurance, what he refers to in nine cases out of ten is that oldest of all forms of insurance protection, fire insurance. Multitudes of people who neither know nor care anything about any other kind of insurance rely implicity upon this one as upon a bulwark which if it were removed would leave them in desperate straits indeed. For this reason, the questions of how fire insurance rates are arrived at, and what part the State should take in protecting its citizens against the payment of excessive rates, are questions which come pretty close home to nearly everyone. During the last few years they have been asked with increasing frequency by reason of the fact that in the fire insurance business, as in most other large fields of business activity, competition between the companies in the matter of the rates they shall charge, has to some extent died out, and in its place has developed a strong tendency on the part of the old rivals to cooperate in this matter. I think I am correct in saying that at the present time this problem of rates lies at the core of all the latent dissatisfaction which exists over fire insurance conditions. The question of the solvency of the larger fire insurance companies, for instance—quite a disturbing question at one time—is not giving the public much concern any longer. Most of the orthodox legislation which can possibly be passed to ensure the solvency of these organisms has been upon our statute books for years, and the question of solvency, so far as the State is concerned, is now mainly one of supervision and administration. But the rating problem is technical, difficult, and, from a legislative standpoint, practically new. As a consequence, it is much misunderstood by the public and what little legislation we have had upon the subject has, for the most part, been either very incomplete or wholly ill-advised.

NECESSITY OF RATING COMBINATIONS.

But the time seems to have come when we should, for the sake of the men who are engaged in this business no less than of the insuring public generally, seriously try to reach some sane conclusion upon the question what the State ought to do in the matter of fire insurance rate-making, or of supervision over these rates. In approaching the problem we immediately encounter certain basic facts which must constantly be remembered if we are to get very far along the path of sanity in our treatment of this problem. One of these facts is that for the protection and safety of this business—and not, as I firmly believe, for the purpose of exploiting the public in the slightest degree—the large fire insurance interests have found it absolutely necessary to enter into combinations for the purpose of making and maintaining rates.

The fact is, a stable insurance business cannot be conducted upon a basis of open and acute competition. In this respect, the situation differs radically from that in an ordinary mercantile business. The grocer, for instance, knows the price which he has to pay for his goods, and will avoid fixing a retail price so low as to endanger his solvency. But, in the case of insurance, the indemnity is sold before the cost—that is the loss—is known, and, consequently, the seller of insurance is tempted in competition to reduce his price below what will prove to be the cost, measured by the actual loss sustained. This inevitable tendency has been thoroughly demonstrated in a sorrowful succession of rate wars, and it is now pretty generally accepted as a fact by those most conversant with the insurance business that a condition of open competition is absolutely untenable in practice, however it may be in theory, and that such a condition simply cannot be made the basis for a stable system of insurance. The companies realized this fact sometime ago, and for protection against themselves commenced to enter into mutual agreements to maintain a given minimum scale of rates. It is these agreements that have been the subject of criticism and that have been declared illegal in the anti-compact states.

ACTION IN NEW YORK STATE.

And yet in the interest of stability and solvency, somebody must fix the minimum rates and enforce their observance. The condition in anti-compact states where rates are only advisory is undeniably bad. The absence of fixed standards results in discrimination in favor of persons with influence and in the weakening of preventive work. There would seem, then, to be but two alternatives upon which to base a stable insurance system: either (1) the State must assume the duty of fixing or approving minimum rates, or else (2) the State must allow the companies to combine for the purpose of making and maintaining rates and then satisfy itself by supervision or otherwise that this power is not being abused.

The latter alternative is the one which has been followed, up to a certain point, in New York. Recognizing the need for standard minimum rates, our State has recognized the rating bureaus as having a lawful existence, and thus has given at least its tacit approval to the principle of combining to maintain rates. Nothing is more evident, however, than the fact that if the companies are to be allowed to combine, and to that extent restrain competition, the States must reserve the right to regulate such combinations sufficiently to make certain that their rates are reasonable. In New York, therefore, the rating organizations have been put under the supervision of the Insurance Department, which possesses power, under the present law, to order a rate changed when there shall appear to be discrimination between it and risks of essentially the same hazard, but which as yet has no power whatsoever to pass upon the reasonableness of a rate in relation to those charged upon dissimilar risks.

This is as far as New York has gone at present toward the control of rates, and in my judgment the progress we have made, such as it is, has been in the right direction. Our conditions here are better, I think, than those existing in parts of the country where anti-compact laws—flying in the face of that natural evolution which is taking place in our business affairs—are in effect. In recognizing, rather than in trying to break up rate-making organizations I think we are on the right track.

MR. RELTON ON THE WAY HOME.

Mr. A. J. Relton, manager, Guardian Assurance Company, London, England, who has been visiting Canada, spent a few days in New York before sailing for home on the 4th instant.