

PREMIUM RESERVES.

PART III.

(Continued from Page 92 of April issue).

After having passed in review the many plans that have from time to time been devised for raising and maintaining a "reserve fund," that shall not only be adequate to re-insure, should need be, all outstanding policies of a company at any given date, but, at the same time, enable such company to withstand the sudden shock of such great conflagrations as Chicago and Boston, exceptional in their way in modern times, without being suddenly overwhelmed and totally burned out; but just exactly how this shall be effectually accomplished none of the various plans submitted seem sufficiently developed by actual practice to warrant adoption, without additional evidence of practicability and efficiency.

"Premium Reserves,"—the laying aside of a certain proportion of the annual receipts,—is well in its way, for all reserves, of what nature so ever they may be, must in part, be composed of these receipts, but, inasmuch as losses and expenses of the business must be met by the premium receipts, it must of necessity frequently happen that there will be years when these claims will exceed receipts from this source, and there will be nothing to lay aside for a reserve. Hence, relying on premiums alone is unsafe, because uncertain and largely contingent upon circumstances beyond all control.

"Capital" is the aggregate sum of money subscribed by individuals as security for policy-holders of their companies; it thus has a dual liability, first, to the policy-holders, and, second, to the stockholders themselves. If, from a series of unfortunate years of business, the amount of chartered capital becomes impaired, the stockholders must, under the customary requirements of the law, make such impairment good out of their own individual means; capital thus becomes a debt of the company, and is so charged by all Insurance Departments; and, as it has its own specific duty to protect the policy-holder to an extent largely in excess of its own amount, it *alone* cannot be relied upon in great emergencies, as Chicago amply proved.

"Surplus," on the other hand,—the result of continuous accumulations from profits of business in prosperous seasons, and from interest and dividends upon investments fortunately placed,—while it belongs to the stockholders, is simply an interest-earning asset, that brings with it no counterbalancing liability against the company; if it be absorbed in payment of losses and expenses attendant upon the business the law exacts no compulsory reinstatement for the benefit of policyholders, as with capital, which not unfrequently has to be paid the second, if not the third time, and, in so far, is a dead loss to the stockholder as often as he may have to make good any deficiency; while, if surplus be lost once, that is the end of the stockholder's liability and loss; there is no after-clap.

Such being the only *fundamental* factors,—so to speak, which insurance offices possess, out of which to construct a reserve fund, it becomes very evident that the last-named, surplus, possesses in any degree, the sole requisite for such a purpose, and that is permanency. It may be more to-day and less to-morrow; but to some appreciable

extent it is always there; for as soon as a company ceases to have a surplus over and above its subscribed capital, with which to fight its battles for existence, just so soon must it cease business and retire to the shades of private life.

The question then arises: Surplus being changeable, now more, now less, how can it be maintained at an equilibrium that will furnish a constant and reliable reserve which can be depended upon at all times and under all circumstances?

Fortunately for ourselves, and our querists, we have a practical and living answer in what is known in the United States as the "Safety Fund Law," now in operation in the State of New York, and it is well named, because it brings real safety to those companies that have had the foresight and courage to avail themselves of its privileges, with solid security to their stockholders and policyholders as well. Inasmuch as actual facts illustrated by actual figures, will most readily explain the operation of this law to our readers, we borrow some of the more prominent forms of our contemporary, the *Insurance Age* of New York, as long since as A.D. 1881, but substitute the figures of the year 1884, as being more recent and better experience of the principle, and use American companies because we have no counterparts of them in the Dominion.

THE "SAFETY FUND LAW."

Under this law fire insurance companies are permitted to set aside yearly a certain portion of the profits of their business as a "safety fund," which shall not be liable for any loss of the company occurring after such setting apart; *provided* that an equal sum of the profits shall be set aside, called a "guaranty fund," at the same time, which shall be maintained as long, and to the same amount as the safety fund, but shall be liable for all losses and other claims upon the company; and if perchance this guaranty fund shall at any time be reduced below its normal sum, no more additions can be made to the safety fund until the guaranty fund shall be restored to its proper figure, after which all profits may again be divided, share and share alike, between the two funds, which are duly invested in interest-bearing securities and held to await contingencies, the guaranty fund by the company, and the safety fund on deposit with the Insurance Superintendent of the State, the company having the option to draw the accrued interest thereon, or leave it to increase the fund. Now, in the event of loss by fire that should wipe out the company with its guaranty fund and other assets, all of which go to pay such losses, the safety fund, together with the unearned premium reserve, then become the new capital of the company, and the security of the unburned policy holders, and the business continues just exactly as if no fire had occurred. These accumulations are to continue until the two funds shall equal the capital stock, until which time the dividends declared shall not exceed 7 per cent. upon the capital; after such accumulation the dividends are unlimited. But if at any time during such accumulation of reserve funds, the capital stock of the company shall become impaired, an amount sufficient to make such impairment good shall be taken from the safety fund, and carried to capital account.

Such are the outlines of this system, which is abundantly