BRITISH LIFE COMPANIES AND THE RATE OF INTEREST.

Considerable discussion is at present going on among British insurance officials in regard to the question of depreciation in the values of securities, and to the manner in which it shall be dealt with by the British companies. In many quarters the increase in the rate of interest realised on investments is held to justify an increase in the rate assumed in the periodical valuation of the companies' liabilities, and two of the strongest of the British life companies notify in their recently published annual reports that they have followed this course.

Even before the war, the rise in the rate of interest, and consequent depreciation of existing securities was giving the British life companies food for serious thought. A little over a year ago, before war broke out, an exhaustive paper on the subject was read by Mr. R. R. Tilt, F.I.A., before the Institute of Actuaries. A summary of this important contribution to the discussion of this question appeared in our issue of August 21, 1914. Mr. Tilt then advocated that in order to meet the present depreciation in securities the companies should write down assets rigidly at a valuation and make any adjustment that may be indicated to be justified by the new rate of yield, in the actuarial valuation.

DEPRECIATION AND FUTURE INTEREST PROFITS.

Against the proposition that depreciation (limited to that caused by an enhanced rate of interest) should be charged against future interest profits, it may be urged, said Mr. Tilt,

First—That the reserves are weakened.

Secondly—That when, in process of time, a fall in the rate of interest occurs, the offices will have difficulty in recovering their position.

To the first objection the reply seems to be that the reserves have been substantially strengthened by the increased interest margin, and that a part only of the value of the increase in yield is required for the purpose of the charge for depreciation. The balance will remain to increase future bonuses. If the depreciation is provided by the use of a higher valuation rate (or by an equivalent method), and if care is taken that nothing beyond the depreciation is released from the valuation reserves, there should be no difficulty in recovering the position when a fall in the rate occurs. On a reduction in the valuation rate following a general fall in the rate of interest, it would be legitimate to take credit for the appreciation of assets consequent on the fall in the interest rate, or, in the alternative, if the old valuation rate is retained, the large proportion of Stock Exchange securities now included in Assurance Funds would if kept at the lower prices, give stability to the rate of yield shown by the accounts.

A company is no better off, said Mr. Tilt, by keeping investments at book values and maintaining its valuation rate than by writing up investments to market values and using the increase to strengthen its reserves by a reduction in the valuation rate. The latter course may indeed be considered the better one, as new business reserves, which will gradually supplant reserves for existing business, should be taken at the lower valuation rate.

In bringing these notes to a conclusion, Mr. Tilt submitted the following propositions for consideration:

DEPRECIATION AND VALUATION RATE OF INTEREST.

(1) That at the periodical investigation a strict valuation of assets should be made, no security being taken at a price above that which, if a marketable security, it would realize according to market quotations at the date of the balance sheet; if not a marketable security the criterion of value should be taken as the price which the office would be willing to pay if the opportunity of making the investment occurred at the date of the balance sheet.

(2) That this strict valuation of assets having been made, the charge for depreciation so far as represented by a future increase in the interest surplus on the company's contracts will be treated properly by the actuary if, in his valuation, he provides for it by an increase in the valuation rate of interest or by an equivalent method, and that the balance of the depreciation (due to the increased rate of interest) may, in many cases, be similarly treated.

PROS AND CONS.

Since Mr. Tilt's paper was written, the matter has, of course, become much more urgent owing to the creation of a new interest level by the issue of the British war loan. It has been suggested that the employment of a higher valuation rate is a course that lends itself to abuse, that it is likely to be taken advantage of by weak companies, strong ones not requiring to take such a step.

A more practical objection, says the Insurance and Financial Gazette, is that the public and agents might misinterpret such a change, and that it might be made unfair use of in competition, as an indication that the reserves had been weakened. But patient instruction of policyholders, agents and the assuring public—who are rapidly becoming accustomed, in these months of stress and strain, to more startling changes than a slight increase in the rate of interest assumed in a valuation—should remove such a misgiving.

LIFE INSURANCE FOR CHARITY.

The recent notification that the estate of the late Dr. F. S. Pearson, consisting largely of Mexican investments, will be insufficient to provide for the legacies directed in the will, leads the Insurance World of Pittsburgh to point out the advantage of life insurance in this connection. It would probably have been possible for the testator in this instance to have converted a goodly portion of his estate during life time to a trust fund arrangement that would have guaranteed the carrying out of his desires. In fact, it would have been impossible to defeat his purpose once proper provision had been made. Life insurance benefits, as provided in present day contracts, may be extended to two or three generations, guaranteeing the safe handling of an estate, without any expense whatsoever to the beneficiaries. This is also true of provisions for endowing hospitals, colleges, charitable institutions, etc. The great trouble with the average estate, sagely remarks the Insurance World, is that it takes a decided slump when the builder passes away. Hence the advisability of transferring it into a safe asset during life.