

CO-INSURANCE CLAUSES.

Few business commonplaces are so often misunderstood as the Co-insurance or Reduced Rate Average Clause—and yet its beneficial character may be made clear by a few words of explanation.

In considering what the object of a Co-insurance or Reduced Rate Average Clause is, it is important to bear in mind two fundamental facts.

First—Insurance is a tax—a tax levied to repair fire waste. In effect each policyholder pays his premium into a fund, which the fire insurance company distributes among such of them as suffer loss by fire. The tax is laid on all to protect those who suffer.

Second—Now, as insurance is a tax, it follows that it should be equitably assessed. There should be no discrimination between individuals owning risks of equal hazard, just as there should be no discrimination by a railroad between different shippers receiving identical service.

The modern and improved method of rating risks is to endeavor to make each individual risk contribute its equitable proportion of the total sum collected for loss payments by rating them under schedules, crediting each risk in detail with its own excellencies and charging it with its own deficiencies; thereby encouraging reduction of fire hazard by reducing rates and discouraging consumption of national wealth by fire by penalizing carelessness. But property owners should understand that without the coinsurance feature any such scientific system of schedule rating is impossible.

SCIENTIFIC RATING.

For instance, a scientific rater makes, under a schedule, a rate of say 1 per cent. on a building worth \$100,000. This is upon the theory that the building will be insured for \$80,000, that it will produce a premium of \$800, and consequently be a loss-paying factor to that extent. Now, if the assured carries only \$40,000 insurance, the building will be a loss-paying factor of only \$400, and the insurance company, in providing a common fund for payment of losses to its policyholders, will, so far as this risk is concerned, be 50 per cent. out of the way in its calculation. This 50 per cent. must be made good by other policyholders if the stability of the company is to be maintained; consequently the average rate which they pay for their insurance must be proportionately increased.

If we suppose that there are twenty such buildings and that on each a different amount of insurance, from say \$25,000 up to \$80,000, is carried it will be readily seen that all calculations as to the rates become hopelessly vitiated. In other words, unless the rater knows what proportion of the value of each risk is to be insured, his rate is purely a guess—not an accurate index or measure of hazard. A rate which is perfectly fair and equitable with a certain known percentage of value insured becomes at once inequitable—too high or too low—when a different percentage is insured.

A parallel exists in the finances of a city. Let us say a city contains property with a taxable value of \$100,000,000 and its municipal expenses per annum are \$1,000,000. If it lay a tax of 1 per cent. and if all property is assessed at its taxable value, its budget of expenses will be covered. If, however, one-half of the tax payers are permitted to reduce the valuation of their property 50 per cent. the city must make a tax levy of 1.33 1-3 per cent.

INSURANCE A TAX PROPOSITION.

Insurance is a tax proposition. The taxes of the government are to cover the expense of running the government. The tax by insurance companies is for the purpose of paying the fire loss. You cannot reduce the assessable values in either case without increasing the rate. In the case of insurance the rate must not only be increased, but the inevitable result is to place an unfair burden upon those property owners who, by carrying a proper amount of insurance, have contributed most liberally to the common fund.

It is a fact that in the fire insurance business on the continent of Europe and in the marine insurance business of the whole world, coinsurance is invariably the foundation stone of the indemnity contract; furthermore, if fire insurance were to be provided by the State or National government, as it is in Germany, there can be no doubt that an assessment would be levied against all property insured in precisely the same manner as all other taxes are levied; that is, upon the full assessable value of the property to be protected. In fact, that is the way the insurance tax is collected in Germany.

One of the largest—if not the largest—property owner in the country is the United States Steel Company. That corporation, it is said, in the days when it carried fire insurance on its property, was unwilling to permit coinsurance clauses in its policies, but when later on it discontinued fire insurance and created a fund for insuring its own properties it promptly adopted the principle of coinsurance by levying an annual assessment—or premium—on each piece of property, based on its full value. That is to say the rate which each piece of property pays to the insurance fund of the United States Steel Corporation is based upon an insurance equal to its full value. The corporation was compelled to adopt this method, for there was no other way by which the cost of insurance could have been fairly distributed among the different properties.

RESULTS OF CO-INSURANCE CLAUSE.

Remember, the co-insurance clause has no effect whatever upon the amount due to the assured in the event of loss, whether such loss be large or small, provided the amount of insurance carried by him equals or exceeds the percentage of the whole value of the property insured which the coinsurance clause requires. So far as the settlement of losses is concerned, the coinsurance clause is of no effect whatever, no matter how little insurance is carried, when the insured property is totally destroyed or when the damage equals or exceeds that percentage of the total value of the property insured which is mentioned in the co-insurance clause forming a part of the policy. In all such cases the assured will be entitled to receive exactly the same amount as though his policy did not contain a co-insurance clause. The co-insurance clause, therefore, becomes a factor only when there is a partial loss, which destroys a smaller percentage of the value of the property insured than that indicated in the co-insurance clause.

That is, when the 80 per cent. coinsurance clause is used, as is commonly the case, it becomes operative in the settlement of losses only when the amount of loss is less than 80 per cent. of the value of the property insured and even then only in case the amount of insurance carried is less than 80 per cent. of the value of the property. In the case of losses which