

Loans on Life Insurance Policies.

(Concluded.)

The year 1910 cannot be said to have been fraught with any financial unrest, for this reason; the ratio of loans to assets may be considered as perfectly normal with nearly all companies. The experience of 1910 proves conclusively that many a company is absolutely precluded from investing its assets representing its reserve in securities of the character initially contemplated by contracts which are predicated upon the predetermined and measureable law of mortality.

The amounts to be loaned from year to year have been absolutely incalculable upon any experience. A multiplicity of causes and circumstances which no one could foresee, have determined the amount which a company has loaned in any given year. These facts have required the companies, which have loaned in large amounts to policyholders, to keep large sums in liquid or negotiable assets, drawing a low rate of interest, whereas, the funds should have been invested in the most profitable as well as the most stable securities obtainable. To the extent that the loan privilege in a policy hinders a company in investing its funds as it ought, to the same degree it impedes a company in performing its primary function, that of insuring lives.

Legal Reserve Shows Large Increase.

So far the loan privilege has, possibly, not "eo ipso" jeopardized any insurance company in carrying out the purpose for which it was organized, but consider; in eight years the ratio of policy loans to assets in our legal reserve companies has increased from 5½ per cent. to nearly 11½ per cent. What can we expect in the future?

Initially, the contraction of credit manifests itself in the large commercial centres. The banks call their loans and the debtor turns to his insurance policy for relief. Ordinary stringencies in the money market have been local in their effect and the companies have met the demands made upon them by utilizing their income from the country districts, which have not been affected by panics. But with the tremendous growth of our large cities, the proportionate number of policyholders of any one company affected by a financial crisis has grown. In 1890 the inhabitants of cities in the United States, of 25,000 and over, constituted 226 per cent. of the entire population of our country. In 1900 the percentage had increased to 25.9 per cent. and in 1910, to more than 31 per cent. In addition to this vast increase of population in our cities, which have heretofore most keenly felt the effects of panics, we are now confronted with another situation. With the increased facilities of communication, by telegraph and telephone, between the smaller cities and the great money centers, and with the rural free delivery of mail leaving a daily paper at nearly every farm house, a correspondingly accentuated interest is felt in the small cities and in rural districts, in the stability of our financial institutions located in large cities. It is a matter of history that each succeeding panic has become less and less local, and more and more universal and far-reaching in its scope.

Loans on Policies and Panics.

We have observed the impetus given the policy loan practice by the panic of 1907, the effects of which, so far as insurance companies are concerned, were largely confined to the cities. Yet the panic of 1907 was felt more keenly in the smaller cities and villages than any previous panic, excepting of course, those followed by long periods of hard times. We can all recollect how, in 1907, the banks throughout the entire country refused to meet demand obligations, and how savings banks universally took advantage of the ninety days notice, to which they were entitled.

Suppose then, in the future, during some financial crisis, that the integrity of some important life insurance company were called into question. The intelligence heralded through the columns of the daily press, reaches every hamlet in the country. Grant that no days of grace are given the company within which to prepare for the demand for loans and surrender values. The wires are hot in every part of the country and a frightened public is clamoring for whatever it can get. The company must either "sit tight" or go into a breaking market and sell its securities at a loss. A company in this predicament, having the "demand clause" in its outstanding policies, would no doubt choose the former, refuse to fulfil its obligations and simply wait until it could make its loans from a normal income. Following the second course, and disposing of the company's loans, would, undoubtedly, result in the wiping out of its surplus. Every one knows what the result would be, if a dozen of our leading companies were obliged to take this action. Herein lies the

danger of containing the so-called "demand clause" in a policy.

Real panics recur in cycles of about fifteen years. With a strong popular demand for a thorough revision of the tariff and with chances a little better than an even break that we will soon have a radical National Administration, it appears safe to predict that a genuine panic, with hard times, is in store for us in the no distant future.

National Convention Condemns Practice.

Knowing the truth of the adage, "In time of peace prepare for war," the National Convention of Insurance Commissioners in 1909 saw fit to condemn the practice of loaning on demand to policyholders in the following terms: "Resolved, That in the judgment of this convention the practice of life insurance companies obligating themselves under contract to make loans to policyholders on demand is unwise, unbusinesslike, and dangerous."

In its action the convention might have proceeded a step further and gone on record with a recommendation for the passage of laws in the various States forbidding the issuance of policies containing a "demand clause," and providing that in all instances the company must provide in its policies that it may avail itself of ninety days notice. No one questions the advisability and necessity for the sixty or ninety days saving clause with which savings banks guard themselves. Experience has shown that banks can only be safely conducted where the cash reserves are equal to those funds of the institution which are subject to call on demand. An insurance company undertaking to loan on demand a sum on every policy outstanding approaching the amount of the reserve on such policy, is not only encroaching on the realm of banking, but is subordinating its true function of protecting families in order to assist speculators and indiscreet citizens, and thus steering its craft upon an uncertain sea. The time has gone by when we would think of asking for the termination of the policy loan practice, but there is no reason why this feature of a policy should be permitted to destroy the purpose of the insurance contract, or why the "tail should wag the dog."

Primary Function of Company Is to Pay Death Claims.

When loans are secured by a policyholder for the purpose of paying premiums, no one any longer questions his right or the wisdom of permitting him to do so. Public opinion demands that he be given the privilege. But the placing of a premium upon a man's investment in an insurance policy by loaning him money at a rate of interest lower than he can get in the open market, or furnishing him with cash on demand, thereby tempting him to speculate, is as pernicious as the former is meritorious.

The primary function of an insurance company is to pay death claims. Money loaning is subordinate to this function and should not be permitted to demoralize the business. Insurance men should jealously guard the dignity of their profession and see that the truest and purest purpose of their work be kept inviolate.

An insurance company should derive its strength from its ability to protect families, and should not permit itself, like an evergreen, to be cut off at the root, so that with artificial trimmings and brilliant decorations it may dazzle for a moment, only to be thrown on the scrap heap when the Christmas days are over.

However, the insurance companies are not, in the last analysis, to be blamed for such a state of affairs. In these days of keen competition, with the insurance business as highly commercialized as any, companies are frequently driven by sheer necessity to do those things which the best judgment of its managers would condemn. Without a combination with other companies which might by a court be construed to be illegally in restraint of trade, a company might find itself utterly powerless to resist or rectify the evil.

It is incumbent upon the Commissioners, whom the Legislatures so constantly advise with relative to insurance legislation, that the dangerous and pernicious practice of loaning money on demand be discontinued, by legislative act. In Minnesota a policyholder can, after his policy has been in force for a period of three years, demand whatever loan value his policy provides for. The policy may stipulate that such loan may be deferred for a period not exceeding six months; but such a clause is not obligatory, and there is no prohibition against the demand clause if desired.

Policies Should Provide Days of Grace.

A protective provision in the loan clause of the policy, to the effect that an insurance company may take thirty, sixty, or ninety days, within which to furnish money to one desiring a loan, does not mean that loans will not be made on demand. The contrary was shown in the panic of 1907.

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