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The Insurance Principle and What Insurance Does

EVERY ONE OF US can, if he will, express his life's material desires in a statement of a few words.

We wish to have enough assets to give us today's necessities and some luxuries; we wish to conserve enough assets to provide these necessities and luxuries when our earning power is reduced by retirement or disability; we wish to leave enough assets to assure continuation of these necessities and luxuries to our dependents; and we wish to protect ourselves against the loss or destruction of our homes and other belongings. The surest and most easily available help toward making certain that these needs will be met is insurance.

Insurance is a device people have invented for taking the sting out of risks. It offers a plan (the policy) that enables a person (the policy-holder) to join a large group of people (through the insurance company) which undertakes to pay a sum of money to him, to his family, or to others (the beneficiaries) upon the happening of a specified event (death, fire, etc.) or upon a stated date. In return, the policy-holder invests a sum of money (the premium) with the insurance company.

All kinds of people buy insurance, in widely varying amounts and at widely varying ages. Canadians rank third in life insurance ownership in the world, and relative to national income Canadians own more life insurance than the people of any other country. The fire and casualty insurance premiums written in a year exceed $2,000 million, and the claims amount to some $1,350 million.

In an age when insecurity seems to be felt in some degree by everyone, insurance provides a method by which large numbers of people, each in some danger of a loss which he cannot prevent, or provide for single-handed, are brought together for mutual protection. When one of the group suffers a loss, it will be made good, partly or wholly, from the contributions of the entire group.

The principle

The principle of insurance is that when the similar risks of many individuals, uncertain insofar as each one is concerned, are combined into a large group of risks of more certain occurrence, the individuals can be protected.

Those who write insurance strive to be a constructive force in everyday life. They have professional rules of action and they are governed by codes of ethics.

Insurance companies have training classes for their representatives, and their associations provide advanced courses. The Life Underwriters Association of Canada established a course of study for its members in 1924. Upon graduating, a member is entitled to call himself a "Chartered Life Underwriter" and to use the designation "C.L.U.", which is accepted by the public as a hallmark of excellence. Fire and casualty underwriters and agents may qualify through a course of study for the degree of Fellow of the Insurance Institute of Canada.

Insurance services

People in the insurance business have a strong compulsion to serve their clients constructively. Some life insurance companies broadcast health talks based upon their research and study, and they distribute booklets and leaflets telling how to prevent disease.

The service idea is also found in fire and casualty insurance. These companies engage in extensive campaigns to educate people about the causes of fires, and have had much to do with the public's acceptance of standards of safety. The steam-boiler insurance companies have succeeded in forestalling by inspection every boiler explosion that could be prevented.

Education by the insurance companies can accomplish much to reverse the unhappy tendency of human beings to get into disastrous trouble. We may learn to prevent what it is possible to prevent by thoughtfulness and carefulness, and we may learn about insurance so as to protect ourselves against the perils that are beyond our control.

Today's insurance business is carried on by companies incorporated under the law of the country in which they are established. Sound insurance laws and their enforcement by experienced, competent public officials are an assurance to policy-holders regarding the standing of any company, and the fairness of the terms and conditions of policies.

Competition among life insurance companies is strong, and agents need to be men and women who are educated in their work, skilled in dealing with people, and keen in pursuit of prospective customers. In 1927 a group of 32 such people got together. They called themselves the "Million Dollar Round Table" because membership required that a man had sold at least a million dollars' worth of insurance in the year.

Although it is made up exclusively of the most successful life insurance salesmen, the group discusses not only quantity but quality. It demands high ethical standards of its members and is constantly trying to raise the level of service. Both philosophy and practice are emphasized at its annual meeting, held in Montreal in June this year.

There are more than 200 companies and fraternal benefit societies supplying Canadians with life insurance. At the end of 1970 there were more than eleven million policies in force. Federally registered, provincially registered, and other Canadian companies and societies had life insurance in force totalling $118,822 million. During the year 1970 Canadians bought $14,247 million of life insurance and drew in benefits and dividends $1,304 million.

The magic of averages

Winston Churchill once referred to insurance as "bringing the magic of averages to the rescue of millions". This magic is the outcome of voluntary economic co-operation by human beings.

The famous French mathematician, Blaise Pascal, worked out the law of averages. It tells the probability or chance that an event will or will not happen. This law of probability does not show up clearly when only a small number is involved. If you toss a coin just once you have no way of knowing whether you will get heads or tails, but if you toss it a million times you can be sure of getting very close to 500,000 of each. It is the reliability of the law of probability when large numbers are involved that makes insurance possible.

Records of births and deaths are used in figuring the premium rates based on how long people may be expected to live. The first real mortality table was prepared by the Astronomer Royal of England, Edmund Halley, the man who in 1705 predicted correctly the return of the famous comet named after him. The figures are revised from time to time in keeping with changing conditions.

Actuaries, who are skilled mathematicians, calculate the rates of mortality based on hundreds of thousands of cases, and predict with a high degree of accuracy how many people in any age group are likely to die in any particular year. From this, the insurance companies learn what the risk is. They cannot tell whether any individual customer will die within the next or some other year, but if, for example, the customer is ten years old and the mortality table shows that 32 of every 100,000 ten-year-olds die every year, the company knows the odds and the premium can be calculated accordingly.

Benjamin N. Woodson, C.L.U., a member of the Round Table, says in *The Set of the Sail*, his book of reflections on life, life insurance and life underwriting: "Life insurance says to you in effect — set aside $40 or $50 or $60 a month, and we will earmark as much as $40,000 or $50,000 or $60,000 of property for the benefit of your family in the event of your death. It is the only property which you can buy (a) in sufficient amounts, (b) on terms that you can meet, and (c) which can guarantee unconditionally to do the job you want done when there is no earned income."

Purposes of life insurance

Life insurance is concerned with two hazards that stand across the life path of every person: that of dying prematurely, leaving a dependent family, and that of living to old age without adequate means of support.

Life insurance enables the head of a family to discharge the sense of responsibility that he feels for those dependent on him. He is not satisfied to fulfil the obligations of the marriage ceremony: "till death us do part", but wishes to continue his support of those who go on living. By payment of a small premium he will create an immediate estate for his family.

Insurance fosters independence, helps to preserve the family unit, provides for the education of children, and makes it unnecessary for the individual or his dependents to rely on government aid or charity. The insured family has prepared its own independence.

For those who do not carry insurance, governments provide social insurance. The objective of social insurance is to provide the minimum standard desirable in the interest of society as a whole; private insurance seeks to make available to those who use it the maximum benefits that each individual policy-holder may aspire to attain for himself or his family.

Kinds of life insurance

An excellent description of the various types of policy is given in *The Small Business Manual*, issued by the Department of Trade and Commerce, Ottawa. An ordinary (or "straight") life policy is intended as protection for a family in case of premature death of the insured bread-winner. It requires payment of an annual premium varying in amount with the age of the insured person at the time of taking the policy. This continues until the death of the insured person, whereupon the company pays the amount of the insurance in cash to the beneficiaries. A limited payment policy is available, under which the premiums are payable until, at the end of a stated number of years, the policy is "paid up" and no further premiums are required.

A term policy provides temporary protection. It is issued, not for the whole life of the insured person, but for a limited period. If the insured dies at any time within the term covered by the policy, the principal is paid to the beneficiary. At the end of the term, if the insured person is still alive, he usually gets nothing back and the coverage ceases unless the policy is renewed at a higher rate of premium or converted into some form of straight life insurance.

Endowment insurance provides for the payment of a sum of money at the end of the endowment period. It may be made payable at the time when a child is about to enter university, or when the insured person plans to retire, or at any other date.

Group insurance covers a group of persons in the same occupation or industry, working for the same employer. It is issued in most cases without medical examination, and the employer and the employee usually share the cost, the employee's portion being deducted from wages.

Most Canadians who apply for life insurance get it. There are "extra-risk" policies, which require higher than ordinary premiums, but of the policies purchased by Canadians in 1969 only four per cent were in this class. The reasons were: 30 per cent because of heart disease, 12 per cent because of weight problems, 28 per cent because of other physical impairments, 20 per cent because of dangerous occupations, and 10 per cent for other reasons.

It is worth noting that two out of every three dollars paid out in benefit payments by Canadian life insurance companies go to living policy-holders. In the main, these are payments of matured endowments, annuities, disability benefits, cash surrender values, and policy dividends. In 1970 these payments totalled $851 million.

A life annuity provides for the payment of money in the form of an income for the remaining lifetime of the owner of the contract, thus robbing old age of the fear of destitution. If the annuitant dies within the period of a guaranteed annuity policy, the income payments are continued to a beneficiary named by the annuitant for the balance of the guaranteed period.

Planning life insurance

There are principles to be observed in investing in insurance. They involve analysis (how much will be needed) and planning (what sort of policy). How much insurance you buy is a matter of desires, needs and costs.

It is not too strong to say that programming is the vital element in good life insurance. Planning the future should include facing up to the facts of life, analysing the risks, determining the available means for meeting them, and arranging a programme designed to meet them most effectively.

This means far more than "buying insurance". It means fitting life insurance in with other secured assets so as to project one's support into the future for so long as one's family needs it. It means trying to make sure that one's desires in the way of comfort, education and a good start in life will be given one's children.

Although we have not seen it in any textbooks, the following may be a sensible way to approach a solution of the problem of how much life insurance to carry.

What were your personal expenses last year (for clothes, travelling, entertaining, lunches, magazines, books, tobacco, and all the rest)? What did you pay in life, annuity, and health insurance premiums, pension fund contributions, taxes, and investments last year? What did you spend on other things that will not be needed by your family?

Deduct the sum of these personal expenditures from your net income for the year (gross income less tax, unemployment insurance, and any other similar deductions). What is left should tell you as nearly as is important the annual amount needed to maintain your present living establishment and dependents on the same standard as last year. What is not available through widow's pension, government allowances, return on investments, etc., can be provided by insurance.

The qualified life insurance agent is competent to sit down with a man and help him to make a programme that will do with maximum benefit the things a man wants done. He will continue to give service when circumstances change in such a way as to modify needs. He will serve the beneficiaries by discussing with them arrangements for the payment of policy proceeds in the way best suited to their particular needs.

Property insurance

Property insurance differs from life insurance in its operation, though not in the principles of insurance. When a person invests in any form of life insurance he is protecting himself and others against an event that is sure to happen sooner or later. When he takes out property insurance of any kind he is investing in protection against an event that may or may not happen.

The business of fire insurance, like that of life insurance, is founded on the doctrine of averages. It cannot be known whether a particular property will be burned down, but there is reasonable probability, based upon statistical experience, that about the same proportion of all similar property exposed to fire will be burned in a year.

The first step toward setting up a fire insurance programme on business premises or on a home, is to appraise the value of your property. A home inventory should list all goods — furniture, clothing, books, musical instruments, tools, paintings, silverware, and all other personal property of those living in the house or apartment. A copy should be kept in a safety deposit box with other valuable papers.

In a typical year the most frequent known causes of fire in Canada, as reported in *Canada Year Book*, are in this order: smokers' carelessness, electrical wiring and appliances; stoves, furnaces, boilers and smoke pipes; matches; lightning; petroleum and its products; defective and over-heated chimneys and flues. Fire insurance claims in Canada run at the rate of about $180 million a year.

Explosion, riot and civil commotion, vandalism and malicious mischief make up a group of perils which can be insured against. Usually they are added to a fire insurance policy at an additional premium.

Casualty insurance is a recent development as compared with marine and fire insurance. It started with the growth of railways in England, where the first "casualty" company was formed about 1849 to provide accident insurance to those exposing themselves to the danger of travelling by steam-engine.

A long list of injuries and damage is covered by casualty insurance today: bad debts, breakage of plate glass, burglary, damage to crops by hail, and a hundred others.

Even the fixed expenses and the loss of business profit when a factory is shut down following a fire may be insured against through a "business interruption" policy. A person who travels may carry a "floater" policy, covering his movable property wherever he may take it.

Insurance is available to cover burglary, which is marked by forcible entry; robbery, which is the taking of property by violence or threat of violence; and theft, which is stealing property while it is unprotected.

Complete automobile insurance coverage includes these types of protection: liability for bodily injury and property damage, collision, fire, theft, medical payment for injuries, and miscellaneous perils such as explosion, flying objects, and malicious damage.

There are in Canada more than 300 competing companies in the fire and casualty insurance business registered with the Federal Government, and several hundred incorporated in the provinces. All of them operate subject to government supervision, and all are required to maintain reserves calculated to be sufficient to protect their policy-holders.

Business insurance

In carrying on business from day to day, insurance is of important service. The mere fact that a business concern carries life insurance on its key men is an indication to creditors that it has taken precautions to protect the business against the sudden removal of important individuals. Borrowing, too, is affected by the amount of life insurance the applicant carries, so that his insurance plays a vital part not only in the physical life of a person but in his financial affairs if he becomes a borrower.

More than almost any other kind of business, a partnership may be thrown into difficulties by the death of one partner, so partnership insurance provides funds to aid reorganization into a new partnership or a sole proprietorship.

Honest discharge of duty by employees is necessary in any kind of business. Fidelity bonds protect the business man against loss by dishonest or fraudulent acts of employees; surety bonds guarantee the performance of an obligation or a contract; forgery bonds protect against loss resulting from forgery or alteration of cheques and other securities.

Credit insurance offers protection against abnormal bad debt losses through, for example, the sudden insolvency of a large and hitherto trustworthy customer. It is available to manufacturers, wholesalers and jobbers, but not generally to retailers.

All who own property, whether business premises or a home, are responsible for it. There is a well-established principle in British law that a person is held accountable for the consequences of his acts and omissions if through failure to exercise reasonable care another person suffers damage to his person or property.

This is an obligation that should be closely attended to by business people and home owners. Even small claims may be troublesome and expensive, while damages given in serious accidents can be enormous. The contract assumed by the liability insurance company usually includes the furnishing to the insured of certain services, the payment of certain costs, and the payment of damages assessed upon the insured because of negligence.

Insurance must fit needs

What kind and amount of insurance to carry, and the value of the premium measured against other wants and needs: these are individual matters to be calculated against the possible effects of not being insured.

It can be said that when a man has adequate insurance covering his life, so as to provide for his family; insurance on his home against fire and burglary; protection against liability claims made on him; insurance according to the needs of his business; and insurance that will provide him with maintenance upon his retirement: that man can sleep well at night because he has financial peace of mind.

No one can hedge against every possibility of loss, but the growth of insurance to cover so many contingencies in one's life is one of the cheering developments of our day.

Every person must analyse his own situation, calculate his risks and the cost of covering each risk by insurance, and choose accordingly. After making sure of catastrophe protection — insurance against any occurrence that would wipe him out financially or cause a major set-back in his family's level of living — insurance against minor misfortunes can be taken purely as a matter of choice.

Arranging insurance coverage is making a programme to meet well-defined objectives, not merely the buying of a new policy from time to time. The policies, like your clothes, must fit you.