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The Significance of Life Insurance

WHEN a person buys insurance of any sort he is protecting himself or his family or his business from possible catastrophe. The growth of the insurance business shows that more and more men are turning to this way of providing for contingencies.

Life insurance (the many other kinds of insurance must be left for another time) is playing an important part in our national and economic welfare as well as in individual well-being. It is preserving family life where its existence is threatened by the death of a bread-winner; it provides ready funds to meet emergencies by way of loans against the value of policies; it accumulates capital for investment in industry, community projects and defence of our country.

All of these desirable results stem from two roots: pride and responsibility. It hurts a man's pride if he or his family must fall back upon the charity of the community. It is foreign to his innate sense of responsibility not to provide for those to whom he has bound himself as a leader, provider and guardian.

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

Many sorts of policy are provided, each designed to meet a particular need, but they may be reduced to a few principal types: the life policy, which provides financial support for one's family; the annuity policy, which furnishes an income during old age; and the combination which gives protection to one's family and accumulates the principal of an old-age income.

Group insurance provides protection for tens of thousands of employees in Canada. Under the usual form of group life insurance contract the employees of a business organization are insured without medical examination. Group life insurance has great social value, since it enables some people to have life insurance protection who could not otherwise obtain it because of impaired health or other reasons.

Only psychologists can tell us how many thousands of persons worry themselves into premature graves by fear of personal or family dependence upon charity or relatives, but statistics provided by the Superintendent of Insurance tell us how many millions of persons in Canada have attained peace of mind by making provision for independence, within their means, through insurance.

Every one of us can, if he will, reduce his life's material purposes into a statement of a few words. We wish to provide enough assets to give us today's necessities and some desired luxuries; we wish to conserve enough assets to provide these necessities and luxuries when our earning power is reduced by retirement or disability; and we wish to leave enough assets to assure continuation of these necessities and luxuries to our dependents.

What insurance is

One way of contributing toward our desired purpose is by carrying insurance. This is a device people have invented for taking the sting out of risks. It is a way of distributing losses and eliminating uncertainty. It offers a plan (the policy) that enables a person (the policy-holder) to join a large group of people (the life insurance company) which undertakes to pay a sum of money to his family or others (the beneficiaries) at the time of his death, or to him if he is still living on a named date. In return, the policy-holder invests a sum of money (the premium) with the insurance company.

The whole group bears easily all the single losses which might otherwise be crushing blows to individuals. This is the very reverse of gambling, with which uninformed people sometimes compare insurance. The gambler converts a certainty into an uncertainty — the certainty that he has his money, into the uncertainty whether he will have more or less in the future. The insurer converts an uncertainty that he will be able to meet his obligations in the event of a possible misfortune into the certainty that he will.

The life insurance business is based upon a careful calculation of the degree of risk, applying the law of averages or large numbers. Winston Churchill referred to insurance as "bringing the magic of averages to the rescue of millions."

As was pointed out in our *Monthly Letter* of January, the application of this law can only be made to large numbers, never to single cases. If we say, for example, that 30 of every 100 men who reach 25 years of age will die before reaching age 65 we mean that this result will occur on the average, not that this particular result will happen to any particular 100 men, still less that any particular 30 out of any hundred will die prematurely. Likewise, your premium for a year's insurance will not cover the company's liability against your policy, but with a large number of policy-holders enrolled it is sufficient on the average.

The insurance principle

Insurance companies are formal organizations through which members insure one another. Their assets are the savings of people, left with the companies for a while to be repaid later when they are needed more. Professor John E. Leibenderfer sums up the insurance principle neatly in his book *Planning Your Financial Independence* (University of Oklahoma Press, 1954). Insurance, in its broadest sense, is the pooling of the similar risks of many individuals, uncertain insofar as each one is concerned, into a large group of risks of more certain incidence. The cost of this better-defined risk is then distributed among the participants, who make small periodic payments, known as premiums, into a fund from which the losses are paid.

Strange though it may seem to reasoning people, particularly to business men accustomed to dealing with the realities of life, there are people who find it difficult to understand that they have had their money's worth even if they have so far collected nothing by way of claim payment.

One insurance man's records tell the story of a young man who received a raise of $1,200 a year. He bought an article for his home. Within a year he died, leaving his family of three with a $5,000 estate. Had he invested that raise in life insurance that investment would have been enough to provide his widow with an annual income of $3,000 a year for at least 20 years.

How much insurance?

In planning how to spend your income the first step is quite obviously to appraise your needs. There is no unassailable formula telling how much to invest in life insurance, but there are some guides into which a man may fit his individual circumstances.

What hazards are you subject to? What may be your possible losses? What may be the effect on your family? To what extent can you or your family meet the losses incident to retirement or death without embarrassment? How can life insurance be used to fill the gap between what will be otherwise available and what you desire? What amount of premiums are you willing to pay so as to reach that objective?

Planning the future should include facing up manlike to the facts of life, analysing the risks, determining the available means for meeting them, and adopting a programme designed to meet them most effectively.

This means far more than "buying insurance." It means thinking ahead to the life of one's family when it is deprived of one's direct support. 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.

Three pertinent questions to ask at this stage of your planning are: for how long will my family need help; in what amounts; under what conditions of payment? Care has to be taken to see that the sum needed to provide this care is calculated after allowing for expenditure of the necessary clean-up amount: medical bills, taxes, and so forth.

Money value of a man

This brings up a question about the money value of a man. It isn't much, if figured materially: if the chemical elements composing the human body were isolated and sold at commercial prices they would be worth only about a dollar. But there is no way of measuring the value of a body energized by life. The only way we can reach an approximation is by calculating a man's income and projecting it for a number of years.

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, and other personal insurance 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) and 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 widows' pension, government allowances, return on investments, etc., can be provided by insurance.

The answer will not be mathematically exact, because, for example, outside help will have to be called in to do things you did around the house, and there may be greater illness expense than the year taken as a model; but the answer will be closer to fact than the nebulous ideas most people have of their life insurance needs and the state of affairs that will exist for their families after their demise.

A book has been written on this subject: *The Money Value of a Man*, by Dr. L. I. Dublin and Dr. A. J. Lotka (Ronalds Press, 1946). It gives as an example an average man whose earnings are $2,500 a year at age 30. He is worth, as a source of income, $32,300 to his family. This is the amount of the present worth (in the economic environment of 1946) of his future earnings, in excess of expenditures on his own person, discounted at 2½ per cent per annum. At age 50, if his earning capacity has increased to $9,000 a year, he has a net value to his dependents of $66,600. This is the amount his family would need to replace the share it had in his earnings during his lifetime.

A study of 500 beneficiaries reported in 1949 by the Life Insurance Agency Management Association of Hartford, Connecticut, provided some revealing figures. Family income decreased greatly in all cases following the death of the bread-winner. In the average family the drop was 63 per cent; in families that had an income of $12,000 or more the average drop was 80 per cent; in families with incomes of $4,000 or less, the average decline was 49 per cent. When asked if their families could have afforded more insurance about half of the beneficiaries answered "yes".

Insurance in business

While family protection is the chief reason for carrying life insurance, it should be said that there may also be a business reason. A man's business associates have a close interest in his welfare, whether they be his employers or subordinates. The interdependence of a man and his business is peculiarly evident in partnerships.

Life insurance may be used to furnish a self-completing sinking fund that will supply the purchase price for a man's holdings; it will protect the business against the death of personal endorsers of the firm's paper; it may be used to retire bond issues or mortgages; it may provide cash to tide the business over the disorganization that is incident to death.

The business world has yet another interest in life insurance. Much of the world's business is carried on by credit, and bank application forms for a line of credit are accompanied by a statement of affairs which requests information as to the amount of life insurance carried.

There are innumerable situations in which no collateral is required, credit being extended on personal security; then, to meet the contingency of death before repayment, the borrower may use life insurance to support his personal credit and thereby use his future earning power in the present.

Growth and strength

Canadian families took advantage of prosperous times during 1955 to increase their financial protection by adding to their life insurance holdings in record amounts. New life insurance put into force up to the end of the year reached about $3,400,000,000. Policy-holders in Canada, numbering about six and a half million, now hold about $26,600,000,000 worth of life insurance, increased from $10,000,000,000 since the end of World War II. This provides protection in excess of $6,800 per household, double that of 1945. Canadians own more life insurance in relation to national income than the people of any other country.

There are 94 life insurance companies licensed in Canada, nine of which have ceased to write new business. They compete vigorously, and operate without the benefit of any government subsidy.

Life insurance in Canada is a co-operative business. Mutual companies distribute to or hold for their policy-holders all profits arising from excess interest earnings, favourable mortality, and so forth. Companies with shareholders have written more than three-quarters of their business on participating plans, and the law requires that a minimum of 90 per cent to 97½ per cent of profits distributed on such plans must go to the holders of the policies.

Benefits paid by life insurance companies in Canada totalled $337 million in 1955, a rate of $6½ million a week. Of this sum, $244 million were paid under ordinary policies, $40 million under industrial policies, and $53 million under group contracts. In the same year these companies paid out $58 million under accident and sickness policies.

No policy-holder in a Canadian legal reserve life insurance company has ever lost a dollar through non-payment of the amount guaranteed under his policy at death or on maturity. The companies regard their assets as trust funds held against liabilities that will mature over a long period in the future.

Like the chartered banks of Canada, insurance companies come under government supervision. Their affairs are subject to careful inspection and regulation by the technical staffs of the federal and provincial departments of insurance. Detailed information on the operations of the companies is made available to the public in reports of the Superintendents of Insurance.

Life underwriters

Within themselves, the companies have set high standards and are continually striving to give improved service to the public.

There are so many good points about life insurance that one might think it should be self-selling, but this is not so. The insurance company must find a means of recruiting policy-holders so that the volume of business necessary to its successful operation may be obtained.

High-pressure salesmanship had its day, but there is no place for it in the organization of intelligent, highly-trained staffs of the present. The standard of the profession has risen, so that today's life underwriter studies to be a constructive force in providing service that will fit the policy to the policy-holder's needs.

The Life Underwriters Association of Canada commenced a course of study for its members in 1924. Upon graduating, a man 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 efficiency. Out of his store and general knowledge, his ability and his special education, it is his job to give constructive help to both policy-holder and beneficiary, and to the extent that he does so he is a successful insurance man.

Insurance in our economy

Life insurance is very important in Canada's economy, for several reasons.

A society that feels itself secure, protected from the hazards of leaving families unprovided for, is in much better position to be a stable society than one where protection is left to chance.

The homes of Canada are richer by the amount of life insurance they carry. There is no getting past the significance to our economy of the fact that life insurance per capita has grown from $595 in 1938 and $1,017 in 1948 to $1,680 in 1955. This $1,680 is a shield against adversity, a backlog of credit, and a comfort that makes minds serene.

The fact that so many thousands of bread-winners carry life insurance relieves the government, taxpayers and charitable bodies of many obligations for surviving families which they would otherwise have to assume. Life insurance does this without pauperizing families by making them wards of charity.

Life insurance helps the economy by diverting dollars from consumer spending into saving, thereby diminishing the menace of inflation.

Life insurance helps to prevent unproductive accumulation of money. Many persons with small incomes would be inclined to hoard their little savings if they had no such institution as life insurance to which to turn. By gathering up all the small sums paid in premiums and investing them in ways beneficial to society, the life insurance companies are assisting in the development of Canada.

Life insurance has an important place in our export trade. Everyone knows that Canada is at the top among nations in exports of wheat, nickel, newsprint, and other commodities, but not many realize that Canada is near the top as an exporter of life insurance. At the end of 1955 the Canadian life insurance companies employed 6,700 persons outside Canada, and 41.5 per cent of their total premium income came from other countries. This business has brought financial benefit to Canada, and is reflected to some extent in the international balance of payments.

Inside Canada, funds held by the life insurance companies to guarantee future benefits to their policy-holders provide one of the most important sources of investment capital.

It is estimated that the life insurance companies invest or reinvest a total of $600 million in Canada every year. The man who has an equity of say $10,000 in his life insurance policies has a share in thousands of different investments — government bonds, corporate securities and mortgages. It will be readily apparent that such a disposition of his funds is more secure than if his $10,000 were invested in two or three projects.

The client's interests

From these large matters of economy and investment we return, as do the insurance companies themselves, to the client.

Three developments of recent years testify to this interest in the policy-holder: the efforts made by the insurance business through its associations and individual companies to educate the public into striving for better health and longer life; the analysis given a prospective client's affairs so as to fit life insurance into its proper place in his planning; and the attention given to arranging insurance effectively and economically.

The life underwriter of today is trained to consider insurance from the client's point of view, to conduct himself in a professional way by serving both as an adviser and salesman.

A man's wants are individual, but he can find an insurance plan that will meet them substantially. Life insurance will replace personal or business income lost through premature death, thus enabling the fulfilment of one's responsibilities. It furnishes a medium through which a man may safely invest his savings to meet obligations in later life that cannot then be satisfied from current income. Protection is offered one's family, one's creditors, one's business and oneself.

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