What Makes the Rates of Fire Insurance So High.

Rates and Cost in the United States Compared with European Countries— What Enters Into Rates Everywhere

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Rates and Cost of Fire Insurance.

Introductory.

I DO NOT know how many of you actually appreciate the magnitude of the fire insurance problem, as it affects your state, your nation and the civilized world. Perhaps few of you know that the United States, by reason of its wealth, enterprise and the prodigality of its growth, pays more fire insurance premiums than all the rest of the world combined. It has also more fire losses than all the rest of the world combined. It is the great world arena of activity and competition for all branches of insurance. In 1912 it paid general fire premiums alone of $309,000,000. Of this vast sum the fifty greatest companies of foreign countries operating here collected about $90,000,000, which was 40 per cent of all their premiums collected in all the countries of the world combined, including the United States. The total premiums of these foreign companies, therefore, were about $225,000,000, of which only about $135,000,000 came from the rest of the world as against the aggregate $309,000,000 of the United States.

This association of manufacturers is organized, as I understand it, and as your program indicates, for almost the sole purpose of investigating and securing correction of erroneous methods and inequalities of state taxation of your business interests, and to obtain relief in competition with rival manufacturers of other states. Your rate of state taxation is 50 cents per $100 of assessable value. Now, your rate of taxation for insurance—not the less imperative to be paid because it is purely voluntary—is about $1.38, or more than two-and-a-half times the state rate of taxation. You have given years of patient attention and spent large sums of money investigating state taxation, comparing its rate and methods with those of other states and countries. Meanwhile you have absolutely ignored the much greater and more serious problems of insurance rates—their nature; what makes them; their application and their justice by comparison. Yet it is $1.38 rate against 50 cents and the values upon which you pay the insurance rate are very much higher than the assessable values on the same property.

I wonder if you have considered this fact: That while you have labored patiently to understand and adjust the smaller tax, you have abandoned the much greater and more personal one to be the football of political agitation and temporary excitement. It ought not to be so. You ought to investigate and know exactly the cause of your insurance rates and insist that this great burden be handled as a business economy and not as a subject of campaign agitation and political prejudice.

What Determines Its Cost.

I SHALL talk about fire insurance from the standpoint of rates and cost because at present there are all sorts of reasons given for rates being so high and all sorts of experiments being made to force them down. Fire insurance seems to be a full fledged member of the High-Cost-of-Living family and it ought to be brought into the limelight and fully discussed without any sort of concealment. I hope we shall all be able to get together at the start on one proposition. **There is nothing in the world that does not cost too much**—when we come to paying for it. The other fellow's bill is invariably too high; though it always seems to me that my bill to him is perfectly reasonable. I suppose it strikes most of us about the same way.

Fire insurance seems to cost more in the United States than anything. That is so because it is the smallest number of us who ever get anything back for our insurance premiums. I have been paying fire and life and accident premiums for the past thirty-five years and never yet got a cent back. Of course I've had peace of mind, a sense of being protected and good sound sleep that I might not have had otherwise—but never a cent of money. And I have always felt the rate was entirely too high. I have no doubt many of you feel the same way about it, and for similar reasons. But I have for a quarter of a century been in a position to know that **the rates were not too high for the facts.** Rates have been stable and subject to few fluctuations. Some years, therefore, they were apparently too high; other years they were apparently too low; and thus in the long run they worked out practically fair, and just about adequate to the risks I had. Not adequate to my own pecuniary benefit, but to the benefit of others who had the losses.

Those of us who have had no losses—when we look at our bills paid for old insurance policies long dead and buried—wish we had our money back; but only for the past. We are very willing to pay it out for present and future peace of mind in protection.

For your knowledge and the delight of your souls I want to tell you just how high insurance rates are in this country as compared with those of other countries. It is needless to discuss Kentucky rates apart; they are exactly as just or unjust as those of other states —no less, no more. I shall therefore merge them into those of the United States as the political entity.

In the United States the rate has averaged about $1.11 per $100 of insured value in the last ten or fifteen years.

What it Costs Abroad.

THERE is no close approximate information about England, because insurance is free trading there, just as commercial business is here; but it is estimated roughly at about 25 or 30 cents per $100. For France there are no figures, for reasons you will later appreciate; but the nominal rate there is quite as low as and probably much lower than in England. Italy and Spain probably have the lowest rate of all.

In Norway it is 45 cents.
In Sweden it is 40 cents.
In Austria-Hungary 30 cents.
In Germany 22½ cents.

Now here is what makes the rates in all the countries named: Loss paid on each $100 insured—

In the United States	was	64	cents
In Norway	"	24	"
In Sweden	"	21	"
In Austria-Hungary	"	16	"
In Germany	"	12	"

In other words we have burned nearly three times as much property per $100 of value as Norway and we have paid about 2½ times as much rate. We have had more than five times the losses of Germany and have paid a little less than five times the rate. Varying proportions hold as towards the other countries. The Greeks said 3,000 years ago that every man got only what he was willing to pay the price for. So we can continue to have the 64 cents loss on every $100 worth of property insured as long as we will pay for the glorious privilege of holding business bonfires at a cost of $650,000 a day!

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Uncle Sam Highest; Germany Lowest.

YOU will observe that the United States and Germany are at the extreme ends of the rate list—we with the highest, Germany with the lowest. The causes of this enormous difference between 22½cents per $100 and $1.11 per $100 are curious as well as vital. You know that none of you pay insurance bills for the charitable purpose of supporting insurance agents and providing profit for the companies. You pay solely for being repaid your loss by fire, if you have any; the expenses and profits are merely incidental to getting the protection you are paying for.

As a matter of fact it may be said that if you are buying anything when you buy insurance, you are buying distributed losses. The loss per $100 to be distributed being 64 cents here and 12 cents in Germany you are buying five and three-tenths times as much loss distribution here as must be purchased in Germany. And you actually buy it in bulk that way at a cheaper rate here than in Germany. For, taking the German rate of 22½ cents, if you purchase 64 cents worth of loss over there it will cost you 5.3 times 22½ cents, which is $1.20 as against $1.11 in the United States. Here is the balance sheet on the two transactions:

Property Owner's Account.

	Germany	U. S.
To cost of 64 cents loss	1.20	1.11
Credit by cash loss paid	.64	.64
Excess paid	.56	.47

Company's Account.

Received for 64 cents loss		1.20		1.11
Paid on cash loss	.64		.64	
Paid expense 34.7% Germany	.41			
38.5% U. S.			.42	
		1.05		1.06
Profit and loss		.15		.05

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The Plain Moral of it.

THE moral plainly is that if you want to buy 64 cents loss distribution the United States is the cheapest country to buy it in, although the expense is higher. The profit rate for the German companies would seem to be 200 per cent greater than for American companies; yet as the German companies operate on a very small scale at home the volume of their profits is of course much smaller. The private incorporated companies of Germany take in at home aggregate premiums of about $30,000,000 a year, whereas New York state alone here pays about $45,000,000 premiums a year and the total premiums of the United States in 1912, paid to 181 private companies, were $309,-000,000. The leading German companies all compete here for business.

> **If you can believe that the leading companies of all the world and the United States are engaged in a riot of extravagance, wastefulness, arson and conspiracy when such enormous sums are concerned on the narrow expected basis of 3½ per cent profit on the turnover, it seems to me you must have a queer idea of other people's business. There is no watered stock in insurance, either; it has to be paid up in cash by blood and sweat or the company is closed up.**

You are all business men and understand the principles of your own business. The principle is the same in all businesses; it is only the things produced and handled and sold that vary. The only difference between any business here and in other countries lies in the obstacles or assistances which governments and custom create in hindering or facilitating business exchange. In everything else your business adapts itself to the natural demands upon it. So it is with fire insurance the world over.

Here, as in Europe, **the steady normal rate of loss** per $100 of value insured, plus the expense of doing business and allowance for a fair profit, **fixes the rate.** Whatever the rates may be, high or low, more than two hundred years of experience in the civilized countries of the globe have served to demonstrate that every one dollar of premium taken in is distributed so that from 50 to 60 per cent of it goes to pay losses, about 34 to 40 per cent to pay expenses. If anything remains it goes for profits and accumulations against the conflagration that always comes—it may be in Boston, Baltimore, Chicago, San Francisco, Jacksonville, Chelsea, to-day, to-morrow or next week; but it always comes. In the past twenty years in the United States, of every premium dollar received 58 cents have been paid back in losses, and 38½ cents have been paid out in expense—making 96½ per cent of it paid back immediately into the channels from which it came, leaving about 3½ per cent to provide for all profits, failures and accumulations for the next conflagration.

That is about the business experience of fire insurance the world over. It applies alike to Germany's 22½ cents of premium and to the United States' $1.11 of premium. It applies in New Zealand to the fire insurance business conducted there by the government itself; it applies in Germany where some cities carry on municipal fire insurance; it applies in the United States where the government has nothing to do with insurance except to put heavy taxes on it and increase the cost. In New Zealand losses are even higher all around than in the United States. It is a newer country.

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Why Expense is High.

THE rate of expense in the United States is higher by about 4 or 5 points than anywhere else **because the taxes and cost of operation under multiple state governments are so high.** English companies can do business at home for 34 per cent; here they are lucky to get off now under 38 or 40 per cent. Insurance is outrageously taxed in the United States. About 6 per cent of your premiums goes for government taxation. Your state governments demand an average of 3 per cent and require the companies to collect it. The cost of collection by this farming-out process doubles the tax. Insurance companies pay about twelve million dollars of this tax every year and it costs the premium payer over twenty millions. Of that vast amount less than a million and a half is used by the states for paying the cost of insurance supervision. The rest goes to the general fund to be paid out for those economical purposes that state governments in so many ways nourish with "easy money."

You may think there is room for improvement in the business in spite of its 200 years of experience. There is; but at the same time there has been as much progress and improvement in insurance and in all its influences as there has been in any other business in the world. Younger than many other necessary businesses, it has developed on scientific lines of great strength, and does its work with marvelous efficiency and no more waste than the best of other businesses.

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How Rates May be Reduced.

THERE are only three directions in which rates may be reduced:

1. **By reducing the profits.**
2. **By reducing the expenses.**
3. **By reducing the losses.**

They are stated in this order for convenience in handling only. As to the first it may be said that if profits are reduced there will be no corporation insurance. Capital does not readily seek such a hazardous business. Few of you, I suspect, own any fire insurance stock. The best managed and oldest companies make fair and steady profits, as the result of long experience and wide distribution of risks. But profits are exceedingly difficult for small and for new companies, howsoever much capital may be provided for the latter. Out of 1,400 or 1,500 companies organized in fifty years there have been more than 1,200 failures and retirements for lack of profit. Less than 200 companies remaining write more than 90 per cent of all the general fire insurance business of the United States. It is very difficult to establish successfully a new company, on account of the hazardous nature of the business united to the oppressive burdens which state laws impose upon their operations. No large general fire insurance company has been organized and successfully conducted in the United States with one exception in forty-one years. If there were enormous profits there would be more companies organized to get them.

As to the second direction, that of reducing rates by reducing expenses—I can leave that to you as business men to consider almost without comment. You know how much you can reduce the prices of what you have to sell by reducing the expense of your methods of selling them. If you are in a competitive business you know that competition makes the cost of selling. If you have a monopoly you know equally well that without compulsion you keep the expense as low as possible in order that you may increase your profits. Exactly the same influences obtain in fire insurance. **Competition and the natural value of the service rendered have regulated the expenses of fire insurance the world over. They are about the same all over Europe, South America, Asia, Australia, the United States and Canada.** Managers in all lands cannot all be in conspiracy to waste funds in expenses. American companies practically do not write in any foreign countries with the exception of a few in Cuba, Canada and Mexico. Foreign companies from all over the world operate in the United States. If they could reduce expenses some of them might be relied upon to do so, in order to add to their profits; but none has succeeded in doing so. If there is any expert promoter of business who can operate a fire insurance company on a two or three point reduction of its expenses he can reap a splendid fortune by applying to me with the proper guarantee. I do not own any company, but I know many companies anxiously seeking him and can usher him into his opportunity.

There remains, then, only one unquestioned way to reduce the rates. That one way will also automatically reduce the volume of expenses and profits. The moment we reduce the fire loss in this country to the European standard, that moment we will get the European rate standard. When we have cut down our 64 cents loss on every $100 of property insured to the German figure of 12 cents we will get the German rate

of 22½ cents. Not before, because it is a plain mathematical process—not a financial juggle. You all know that the higher the price of an article the more it costs to handle and sell it. In that exact proportion it costs more to handle and sell 64 cents of loss on American property than 12 cents loss on German property.

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Reduce Loss: Lower Rate.

TO SHOW you that this process of reduction works out inevitably in the United States and Germany alike, you have only to look at some of your own manufacturing risks. Old cotton and woolen mill managers and stockholders easily remember the time when those risks cost from 1.25 to 3.50 per cent to insure, and cotton and woolen mill fires were numerous. So, manufacturers got together, formed a select mutual association, made it a peremptory requisite to build safely, to remove all the hazards possible and protect those that could not be removed, and provide fire preventive and extinguishing apparatus. In twenty-fives years under those conditions the rates on first class cotton mills have come down from 1.25 and 3.50 per cent to 15 cents and 25 cents per $100 insured. It is seldom you hear of cotton or woolen mills burning down now. You have approximated the German basis by adopting German care. The same thing has been accomplished in other manufacturing lines. I know of manufacturing risks that get a net rate of 5 or 7 cents per $100 per annum—lower than Germany even. It has cost money on the original expenditure to provide fireproof or slow burning construction, segregated hazards, sprinkler systems, etc., but that expenditure practically has to be made but once, whereas the savings not only on the insurance rate, but on the actual business losses—against which no insurance can protect—go on forever. **You can never get the low German rate without equaling German safety.**

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Influence of Laws on Cost.

NOW let me describe the difference between American and German laws and insurance practice. Say I own a store or a factory and because of my lax methods of management, or the rush of business, or for some other reason of carelessness or neglect, rubbish accumulates, a heat conductor gets out of order, or the electric wires are neglected. The insurance inspector or a municipal official notifies me of it, or does not. At any rate I am too busy to attend to it, or I neglect it because of natural indolence. The fire starts from one of these causes. It may result in a ten dollar loss or it may burn down the city, as in Chicago or Baltimore. The insurance companies pay the losses as far as their liability goes. Perhaps there are enormous losses uninsured and unpaid. Well, it is "tough luck"; but there is no investigation or punishment; it is apparently nobody's fault; I am a "good fellow"—everybody is sorry for my loss—unless I am fully "insured" and in that case they congratulate me. And we continue to pay high insurance rates because of such losses. If we want to live that way we must pay the price.

> **Suppose the same thing occurs in Germany. The police take charge of the premises while the fire is burning and investigate the cause of the fire. If it originated in the carelessness or the neglect of the occupant the fact is declared. He must prove it did not. He cannot receive any insurance payments unless he does prove it. If it is a false alarm or a small damage he must pay the expense of the fire department run, ranging from $12.50 to $100 as the case may be. He must pay all the expense of the investigation, and the loss caused by his negligence and failure. It does not pay to be careless about fire in Germany, as it sometimes does here. And if you think carefully over the German penalty laws, I think you will concede that perhaps our insurance rates are as low as the German cost.**

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Under The Code Napoleon.

THUS far I have dealt with Germany alone. Now I want to give you an idea of fire insurance and fires in the European states where the Code Napoleon is in force. That is, in France, Spain, Italy, Holland, Belgium and the Rhenish Provinces. Under the Code Napoleon, you know, every man is personally liable for the damage he may cause to others in the proportion of his carelessness, neglect or intention. He cannot escape paying for the glass if he breaks the window.

In France, for instance, in order to protect yourself by insurance you must also protect others. In French cities, particularly, three separate sets of policies are habitually carried by everybody at comparatively low rates, but of course at very much higher proportionate rates for the loss incurred than we pay in the United States. If you occupy leased premises there, you pay for insurance against loss to your landlord, against loss to your neighbor, and against loss to yourself. The landlord pays for insurance against loss to you, as his tenant, that may occur through any defect in building; the builder is liable to the landlord if he fails to build properly and gives rise to a fire. **Whosoever is responsible for the fire is held for it** and does not get a cent of insurance until the claims of all others have first been paid.

They don't monkey with the fire fiend in France, as we do here. The annual fire loss in Paris, with 3,000,000 population is often no greater than here in Louisville with 240,000.

Business insurance under the Code Napoleon is a marvel of complex distribution. The landlord and every tenant (even in a flat building) is compelled for self protection to insure against loss—from his carelessness or negligence—to the building and to the property of all tenants, and in addition, against possible damages, that may accrue to the buildings on either side, as well as in the rear, and damages to all the tenants of those buildings. Every merchant who stores goods in a public warehouse must insure not only his own goods, but the warehouse and its entire contents against loss by fire that may originate in his goods stored there. It will astonish you to know that even the **janitors, housekeepers and house porters must pay for insurance on property under their care** against any loss by fire that may be caused by their negligence. The rates on each set of policies are low, of course; but when they are added up and the commissions and expense and the infinite detail and annoyance are considered, you may decide for yourself whether Europe gets off cheaper than we do. I say it does, in one important sense; because they do not have the fires there that destroy here not only hundreds of millions yearly but ruin many businesses by consequential losses.

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In The Good Old U. S. A.

THERE is no law in the United States that prohibits a man from having a destructive fire on his premises, except the law against arson. If I deliberately set fire to my house I can be sent to prison; only you have to prove it on me first. But I can set fire to it in a hundred ways by **carelessness, neglect and stupidity and you and**

all of you must pay for it in your own rates, the while you sympathize with me for my misfortune. I couldn't do that in Europe. There I should lose heavily by it.

It has occurred to no legislature in the United States to make a penalty for the fire that originates from any but an unpreventable cause on anybody's premises and causes damage to others. THAT IS WHY OUR RATES ARE SO HIGH. It may perhaps be better suited to the nature of our democratic institutions to let every man protect himself, not only against his own carelessness but against his neighbor's, by taking out insurance at a lump rate and letting everybody else look out for himself in the same way. It seems to me that a failure to enact penalty laws is instinctive among us and represents our democratic idea of liberty. If that is so, then **eternal insurance at infernally high rates will continue to be the price of that liberty.**

The amount of the loss incurred per $100 burned will always be the basic cost of solvent insurance. No legislative juggling with laws will affect that natural fact any more than it will make the Ohio River run up-stream in times of flood.

Here in Kentucky, as in several other states, the legislature is trying an experiment sixteen hundred years old. In about A. D. 300 the Emperor Diocletian concluded that everybody in the Roman Empire could be made happy and prosperous if a just scale of prices were fixed for all commodities and all work performed. So he decreed a law fixing prices for everything, with heavy penalties for its violation. The result was that pretty much everything in the Roman Empire came to a stand-still except poverty and charity. Both of these flourished until the charity was all used up, and then poverty had a complete monopoly. Of course nobody would sell anything at state prices if the natural prices were higher. And nobody would buy at state prices if the natural prices were lower.

As business men you all know that **exactly the same would happen in Kentucky if the state should fix prices for your goods and your labor.** The commodity which fire insurance sells is indemnity to you against loss by fire. The commodity is generally A1, as good as government bonds. The service rendered by agents and companies requires careful, almost professional, training, untiring zeal and energy and a high order of natural skill, because upon its successful exercise great sums of capital are hazarded.

In the year 1906 the insurance companies were called on unexpectedly to pay out an amount equal to half the annual receipts of the United States Government, as a result of the San Francisco earthquake and conflagration. They did it patiently and successfully, but it wiped out the profits of many years

and compelled them to put more than 75 millions of new capital into the business to meet their liabilities.

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State-Made Prices.

NOW, you may decide for yourselves, whether the legislature of Kentucky can fix the price of indemnity and service in insurance any more than it can for your manufactured products and the wages you pay. One thing you may be sure of. If the state fixes the rate high enough to cover the risk you can continue buying the insurance; otherwise you cannot. It is not because the insurance companies resent the state's interference. **You know perfectly well that no business man cares what laws may be put on the books if he can operate under them at a fair profit. And no matter how much a business man may admire any theory of state laws he must cease operating if he cannot make a fair profit under them.** It is not a question of intellectual favor or opinion; it is a cold, naked matter of fact—of life and death to the capital involved on both sides.

The first thing done under the new Kentucky rate law was to reduce rates 20 per cent on farm insurance. Two weeks after the reduction was made forty counties in the state were not able to buy any farm insurance. In the other eighty counties indemnity was limited and only the safest farm risks could find part protection only. THE RATE WAS MADE TOO LOW.

The insurance business is exactly like yours in respect to price and cost. Insurance companies are largely selling their credit to property owners needing the protection. If the prices are not high enough they cannot extend the credit any more than you can. And you must remember that disorganized rates and uncertainty of insurance have a very bad effect on all the business of the state, rendering capital very chary of investment and credit very hard to command.