INSURANCE
SCIENCE AND ECONOMICS

A PRACTICAL DISCUSSION
OF PRESENT-DAY PROBLEMS OF
ADMINISTRATION, METHODS
AND RESULTS

For Insurance Officials, Managers, Agents, Merchants
Lawyers, Teachers, Students, and Others
Interested in The Broader Aspects of
Insurance as a Business in Its
Relation to Public Welfare
and the State

BY

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To
the Memory of
my
Father
AUGUSTUS FRANCISCUS
HOFFMANN

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PREFACE.

The modern literature of insurance in all its branches, while quite extensive and practically valuable, is largely restricted to the consideration of matters relating to the office and field administration of insurance companies. Insurance, as a branch of contract law, has a literature of its own, which, however, is quite limited in its utility to the student of insurance questions and problems of the present day. As yet, only a few really useful works have been written in English on the larger and broader aspects of insurance in its relation to public policy and the functions of government arising out of the corporate nature of insurance institutions. Obviously, the conduct of the business cannot be called entirely successful unless insurance interests are intelligently co-ordinated to an enlightened public opinion demanding economical administration on the one hand, and absolute certainty of the fulfillment of contractual obligations on the other. Insurance today is an indispensable element of social and commercial life, and it is no longer exclusively a matter of local or state concern. The marvellous growth of the business within recent years emphasizes its national, and even international, importance and the duty of government to conserve the public interests represented by it to the fullest possible extent. The questions and problems discussed in the present volume are, therefore, not only of today, but of the future, and a matter of serious concern to all who hold responsible positions with insurance companies, or who, in some capacity or another, are required to express their judgment upon public questions involving insurance considerations. The problem of a more perfect development of the abstract theory and of a better practical adjustment of insurance to the varying needs of a progressive society, are inherent in the nature of the business, but their

successful solution lies largely with men of trained minds and impartial judgment, deservedly entitled to the full confidence of all concerned. The present work is, therefore, intended for the better and more adequate study of insurance as a branch of economics, while the large number of references appended to the several chapters will facilitate research work, where limitations of space have made a more extended treatment impossible. The bibliography includes most of the principal works on insurance, from the earliest times to the present day, useful for both theoretical and practical purposes, with a due regard to the historical development of the business and the complex problems arising out of its gradual evolution from the most primitive form of individual underwriting to a corporate business of colossal national and international magnitude.

For a full quarter of a century I have been actively engaged in the business of insurance, in the office administration, as well as in the field. My own extensive experience has forced upon me the conviction that one of the most serious shortcomings of insurance at large is the lack of proper insurance education on the part of many of the men who discharge responsible functions, as managers, agents, or other field and office employees. There are few textbooks of real value accessible to students in English, although many such are conveniently available to students of insurance familiar with German or French. The tendency on the part of the International Actuarial Congress, to become more and more a gathering of men interested in insurance science, after the manner of the German national society by that name, is a further indication that the modern trend of the business gives promise of better results in the years to come. The action of numerous institutions of learning which have introduced insurance courses, foreshadows a more deliberate and practical method of insurance education than has heretofore been possible, or thought necessary. It is, therefore, to be hoped that the present volume will be an aid in this direction and that the work will

prove useful to administrative officers, teachers, managers, agents, and others in sympathy with the larger aims and ideals of a business which is second to none in the civilized world.

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INTRODUCTION.

Insurance as a science is properly considered a branch of economics, and as such it was included in the most recent authoritative classification of the sciences, adopted by the Congress of Arts and Sciences, held under the auspices of the Louisiana Purchase Exposition in 1904. At this congress two papers were read on insurance, the first on "Insurance as a Science," by myself, and the second, on "Insurance in Its General Aspects," by Prof. B. H. Meyer, now a member of the Interstate Commerce Commission.* Previous classifications of science had not included insurance, although as early as 1865 Dr. Engel, the director of the Prussian Statistical Bureau, had most ably presented the claims of insurance to scientific recognition before the International Statistical Congress held that year in Berlin. The claim of insurance to the dignity of a science, however, is not new, for certainly as early as 1747 a small tract was published in England, by Mr. Corbyn Morris, entitled, "An Essay towards illustrating the Science of Insurance. Wherein it is attempted to fix, by precise calculation, several important maxims upon this subject; to solve various problems, and cases of contest; and particularly to balance, whether it be nationally advantageous to insure the ships of our foreign enemies." John Weskett, merchant, who in 1781 published an elaborate and classical digest "Of the Theory, Laws and Practice of Insurance," particularly emphasized its scientific aspects and observed that, "There is scarcely any other occupation, or profession, though far more unimportant, and less abstruse or complicate than that of insurance, amongst

* "Proceedings of the Congress of Arts and Science," St. Louis, Mo., 1904, in 8 vols. Published by Houghton, Mifflin & Co., Boston, 1906, Vol. VII, p. 207, et. seq

the whole circle of arts and commerce exercised in this kingdom, where some method of instruction is not looked upon as requisite; and, where the persons employed in it are not pretty well versed in the grounds and theory, and the greater part of them expert in the practice of the principles on which it ought to be prosecuted:—but, one may venture to assert that, in no other class is there to be perceived so great a proportion of a numerous body of practitioners, who are so incompetently skilled in the nature of the matters about which they are occupied, and of the laws and rules, by which they ought to be governed, as amongst those who are in the actual employment of, and whose avocations and concerns are immediately connected with, affairs of insurance." What was true of this early period, when insurance was in its infancy, is equally true at the present time, that insurance education is generally neglected and upon even important matters of theory and practice there still exists much confusion and doubt, which only thoughtful consideration and painstaking analysis can set aside. The field of research is immense. The history of the business is largely unwritten and the works of classical writers are difficult of access to the student of insurance who desires to sustain his reasonings and conclusions by the same substantial foundation of knowledge as is required in every other branch of science.

Insurance as a branch of economics has also been much neglected by writers on political and social economy, but during very recent years there has been an awakening of interest in the economic theory of risk and insurance, which seems to indicate a more extended and qualified consideration of the subject in the future. It is still an open question as to which of the three general divisions of political economy—that is, production, distribution and consumption—should comprehend insurance, or whether the factor of risk assumption and distribution, through insurance, is not inherent in them all. The practical importance of such consideration is particularly apparent in the far-reaching issues involved in the question

whether insurance is commerce within the meaning of the commerce clause of the Constitution, although a number of decisions of the Supreme Court have heretofore been to the contrary. If economic theory sustains the conclusion that insurance is an element in the cost of production, and perhaps as much so in distribution, it is difficult to escape the conviction that insurance transactions fall properly within the scope of commercial undertakings, intercourse or trade, by whatsoever means or methods the same may be carried on. It requires no very extended research into the standard works on insurance theory, practice and law on the one hand, and commercial theory, practice and law on the other, to sustain the view that from the very earliest time insurance transactions have been considered, and invariably so, as being commercial transactions within the same meaning and scope as bills of lading, bills of exchange, and other negotiable instruments of various kinds. In the brief discussion of insurance as an element of early commerce only a few of the foremost authorities have been drawn upon, to avoid needless elaboration and wearisome repetition of detail. A discussion of insurance as an element of modern commerce would easily make a volume by itself, with a due regard to the numerous branches of insurance which have been developed within recent years. Their mere enumeration is sufficient to emphasize the practical commercial aspects of insurance as a necessary factor in mercantile adventure, commercial credit, and national advance. By way of illustration, reference may be made to through bills of lading, which include the assumption of risk on the part of the carrier in transportation by land, while long usage has required the assumption of the risk in navigation by the shipper and the general custom of covering such shipments by marine insurance.* Every through bill of lading, therefore, contains

* It is stated in the Compendium of the Official, Southern and Western Freight Classifications, published by the U. S. Dep't of Agriculture in 1910, that " The cost of insurance against marine risk will not be assumed by carriers unless specifically provided for in tariffs."

a special reference to the limited liability of carriers in this respect, while every invoice of a through shipment from inland points to places abroad includes a certificate of insurance for the full and necessary protection of the cargo against loss.

Reference may also be made to an important aspect of insurance in its relation to American shipping, for there is apparently much justification in the assertion of those who hold that the decline in the American merchant marine was in part the result of unfair classification by Lloyds of our ships during a critical period in the evolution of shipping, and furthermore that the American market for marine insurance is entirely insufficient for American needs.*

For the study and qualified consideration of questions and problems of this kind there is need of the accessibility of the classical writings on insurance, which are now extremely rare. Few even of those who have given much time and thought to the practical development of the business of insurance are aware of the wealth of literary material available for a history of insurance and a critical outline of the development of insurance theory and practice from the earliest times. Every student of law and legislation is familiar with the ancient maritime codes or sea-laws, of which the earliest is the Rhodian Sea-law, which during the last few years has been made accessible through the elaborate translation from original manuscripts by Mr. Walter Ashburner. All that there is contained in this fragment of law, which dates back to about 900 B. C., has its practical bearing upon modern methods of insurance, for the ancient doctrines of contributionship and average, jettison and salvage, maritime loans and other matters, are still held and applied in the courts of law of every civilized nation, including our own.

What Mr. Ashburner points out in his discussion of the Rhodian Sea-law is, unfortunately, true also of modern times,

* Hearings before the Senate Commission on Merchant Marine, Vol. I, p. 192 et. seq. Senate Report No. 2755, 58th Congress, 3d Session, Washington, D. C., 1905. See also the Report of the U. S. Commissioner of Navigation for 1890, p. 97 et. seq.

in that the ruthless destruction of commercial documents has deprived the students of law and legislation of much valuable material which is now irrevocably lost. A thorough study of insurance is out of the question until the works of the classical writers, the elaborate treatises by Magens, Molloy, Postlethwayt, Beeves, Weskett, Caines and many others are made accessible, and until even the still earlier treatises on insurance in Latin are made available in English as a necessary basis for a sound understanding of the ancient origins out of which the modern structure of insurance has developed. Early laws and ordinances dating back to the 13th and 14th centuries, are full of meaning even at the present day. Study of their provisions proves conclusively that from the very beginning of insurance as a business the insurance contract has been a matter of government supervision and control. Historical evidence is not wanting to prove that as early as 1227–1234 bottomry loans were prohibited by papal decree on the ground of their being contrary to public policy,* while as early as 1568 insurance was prohibited by the Duke of Alba as Regent of the Netherlands,† and contracts or agreements in various forms, wagering or gambling policies, etc., have been prohibited from time to time by different governments practically throughout the entire modern history of the business.

Insurance law as it is laid down in the commentaries of Blackstone and Kent, is not only an indispensable requirement in a full course of legal study, but it is equally valuable and necessary to the student of insurance in general. Kent, in his remarks upon the insurance contract and its gradual development through the course of centuries, observed, with reference to the value of insurance as an element of commerce:

"The business of uncovered navigation or trade would be spiritless and presumptuous. The contract of insurance protects, enlarges, and stimulates maritime commerce; and under its patronage, and with the stable security which it affords,

* Plass, "Geschichte der Assecuranz," Hamburg, 1902, p. 19.
† Plass, ibid, p. 32.

commerce is conducted with immense means and unparalleled enterprise, over every sea, and to the shores of every country, civilized and barbarous. Insurers are societies of capitalists, who are called by their business to study with profound sagacity, and with exactness of calculation, the geography and navigation of the globe, the laws of the elements, the ordinances of trade, the principles of international law, and the customs, products, character, and institutions of every country where tide waters roll, or to which winds can waft the flag of their nation."

A business of the magnitude of modern insurance is entitled to a literature of its own, a series of thoroughly digested text-books, a well established code of fundamental principles of law and legislation, and a national institute for promoting knowledge and developing the arts or methods by which sound theory can best be carried into practical effect. The time is slowly passing when the acquisition of new insurance through effective solicitation will constitute the chief consideration of success. Evidently it requires no argument however, to sustain the position of those who, during the formation period of the business, against almost insuperable odds, have adhered to the idea of aggressive solicitation even at considerable expense to advance the cause of insurance among every element of the population, from the poor and ignorant to the well to do and well informed. The insurance idea is subtle and difficult of clear comprehension except in actual commerce, where the necessity of insurance protection is so obvious and self-evident that it requires no argument or endorsement, as is made clear by the rapid growth of marine, fire, and other forms of property insurance, which are now quite generally made use of without the aid of much active personal solicitation. In life, accident, and many other forms of insurance, the difficulties in this respect are more serious, and the progress of insurance education is necessarily a slower one.

In the course of time, however, the insurance idea is becoming more familiar to the masses, and the sense of insurance obligations as a matter of personal or property protection

tends to become subconscious, and indifference and opposition must gradually disappear. With increasing education and the spread of general knowledge on the one hand, and the imperative need of economic security against the casualties or calamities of life, on the other, the social necessity of insurance will become more obvious and the future growth of the business will be more and more the resultant of its own momentum. In other words, insurance, from being purely a form of business enterprise or associated effort for mutual protection, tends slowly but surely to become a social and economic institution, the evidence of which is met with to an increasing extent in so-called government insurance, or compulsory insurance, or quasi forms of insurance, state security and guaranty, which imperceptibly shade off into the theory and practice of true insurance. The most interesting proof of this assertion is to be found in the elaborate consideration on the part of an English parliamentary committee of a national guaranty for the war risks of shipping, which arose out of the previous considerations of a Royal Commission on the supply of food and raw material in time of war. It is a serious but common error to seek for insurance knowledge only among the readily accessible sources of information. It is, for illustration, only known to the very few, that the very stamp act which led to the American revolution included stamp duties upon policies of insurance. It is also not generally known, if at all, that a corresponding act, imposing stamp duties upon policies of insurance, was passed by the U. S. Congress as early as 1797. The Annals of Congress, and even the Abridged Debates, by Benton, from 1789 to 1856, contain numerous and important discussions of insurance matters which are not even mentioned in the few historical works on insurance in the United States. In the Journals of the Continental Congress are contained a number of articles suggestive of proposals for annuity schemes as revenue measures to provide funds for carrying on the war of the Revolution, while the early messages of the governors of the different states contain important references to insurance of great historical and more

or less practical value today. The proceedings of commercial associations often contain important deliberations upon particular phases of insurance, and the subject, among others, was brought before the Industrial Commission and the Senate Commission on the Merchant Marine. An able discussion of marine insurance in its practical relations to freight charges and the whole problem of transportation by water is contained in the report on that subject by the Commissioner of Corporations, while numerous cases on admiralty law, particularly the case of Insurance Co. vs. Dunham, abound with suggestive judicial opinion which have a direct bearing upon the further development of sound insurance theory and the perfection of the policy contract of insurance in all its branches.*

The most urgent requirement today is for carefully prepared text-books on insurance, and the correction or re-statement of discussions of insurance practice in text-books on arithmetic, and higher mathematics. The subject of insurance in its entirety requires to be taught in our leading universities, not primarily for the purpose of training men to become insurance managers, actuaries, or specialists in particular departments, but as a branch of science in the same sense and as physics, geology, chemistry, mechanics, banking, transportation, etc., are taught. The higher form of teaching is, however, out of the question until proper text-books are provided, in which the principles and elements of insurance shall be authentically set forth so that they may safely be used as evidence in legal controversies and settlements of differences of

* Among modern works which take cognizance of insurance as an element of commerce are, "Lessons in Commerce" by Gambroro and Gault, 5th Ed., London, 1904, and "An Essay on the Early History of the Law Merchant," by W. Mitchell, Cambridge University Press, 1904. Among earlier works which should be consulted are, "Proceedings of the Commercial Convention held in Detroit, July, 1865," and "The National and Private Alabama Claims and their Final and Amicable Settlement", by Chas. C. Beaman, 1871; also, "The Report of the Commissioner of Corporations on Cotton Exchanges," Washington, 1908, and " Sea Law and Sea Power," by T. Gibson Bowles, London, 1910.

opinion concerning the proper meaning of particular terms. The general teaching of insurance as an element of commercial law as well as of contract law generally, requires also to be much improved, and the movement for uniformity in insurance legislation requires to be more actively fostered than has heretofore been the case. The pressing need of federal supervision of insurance; of expert codification, and of equitable insurance taxation, are entitled to the most serious consideration, not only on the part of those engaged in the business of insurance, but of lawyers, merchants, bankers, economists, and others whose judgment and experience would aid in the solution of pending questions which at present are largely a matter of chance opinion and of drifting public policy.

Never before was there a time when insurance in its various aspects received as much public consideration as today. Questions and problems of old-age pensions, contributory schemes or retirement funds, workmen's compensation and employers' liability, government insurance, unemployment insurance, agricultural insurance, and industrial accident insurance, aside from the question of safe and economical administration of state chartered corporations, are now subjects of general discussion, committee hearings, legislative debates, and state action, with the practical certainty that more or less serious errors of material consequence will result from imperfectly considered plans or ill-considered schemes. The necessary aid must come from those who have seriously deliberated upon these questions and who bring a ripe knowledge and large experience to bear upon conclusions and recommendations as to what is and what is not compatible with the highest grounds of public policy. In this sense I would interpret the modern conception of insurance education as a branch of science and economics, as an important department of the common and statutory law, and finally as a proper subject for historical inquiry and qualified technical research.

CHAPTER I

LIFE INSURANCE AS A SCIENCE.

The first inclusion of insurance in an authoritative classification of the sciences occurred in 1904, when the International Congress of Arts and Science, which met that year under the auspices of the Louisiana Purchase Exposition, assigned to life insurance its proper place as a branch of economics, which, broadly defined, is "the science of the relation between private property and public wealth." The honor of having been the first to assign a definite place to insurance in the science of economics appears to belong to Mr. Henry Dunning Macleod, whose conception of economics comprehends, first, material things; second, personal qualities, both in the form of labor and credit; and third, annuities. Most of the works on political economy and social science are barren of references to the third department, which, for want of a better term, Macleod defines as annuities, or "the right to receive a series of future payments." Such rights he terms "negative economic quantities," comprehending all mercantile and banking credits, checks, bills of exchange, terminable annuities, leaseholds, policies of insurance of different kinds, and many other valuable rights, amounting in value to thousands of millions of dollars, of which there is scarcely any notice in the text- books on economics. He very properly remarks that by introducing this class of incorporeal property, he has doubled the field of economics.

To establish the relation of the science of insurance to the other great divisions of accurate and systematized human knowledge is the purpose of this discussion, and the more definitely this relation is established, the more clearly we shall

comprehend the true nature, possibilities, and results of insurance as a vast and indispensable social institution of today.

Insurance, reduced to its simplest terms, means the application of the principle of association to the equalization of losses resulting from the inherent uncertainty in human affairs. This is the risk of untimely death, of fire, shipwreck, burglary, windstorms, floods, and many other contingencies outside of the control of man. The uncertainty of human life is modified by social progress, in particular by the advances in medicine and related sciences, but there must always remain the risk of premature death, which insurance alone can equalize through the principle of association. In the classic language of the first Select Committee on Friendly Societies, in 1825, it seems that "wherever there is a contingency, the cheapest way of providing against it is by uniting with others; so that each man may subject himself to a small deprivation in order that no man may be subjected to a great loss. He upon whom the contingency falls does not get his money back again, nor does he get for it any visible or tangible benefit, but he obtains security against ruin, and consequent peace of mind."

Theory of Risk and Insurance.

The theory of risk and insurance has been elaborated and set forth by Mr. Allan H. Willett in a most instructive dissertation published by Columbia University in 1901. He holds, and very properly so, that as a general rule uncertainty exercises a repellent influence in human life and that the existence of risk in an approximate static state causes an economic loss, while, on the other hand, the assumption of risk is a source of gain to society. From this point of view the business of insurance does not differ essentially from general commercial enterprises. Risk is assumed in mining and agriculture in much the same manner as risk is assumed in the business of insurance, but in life insurance, for illustration, the assumption of a risk and the equivalent premium payments required are determined by the theory of probability and the established laws of human

mortality and observed experience. In general commercial enterprise the risk assumed is, as a rule created, while in insurance the risk assumed is pre-existing. This marks the broad division between gambling, speculation and insurance. Insurance is not "in the nature of a bet," for in insurance an effort is made to eliminate an existing risk by its assumption on the part of the many, while in gambling a non-existing risk is created with resulting uncertainty and needless loss to society.

The gain resulting to society is the reduction of the uncertainty for the group as a whole, or the substitution of certain loss for uncertain loss. By this process of diminishing the degree of uncertainty, the cost of the risk to society is very largely and considerably reduced, if not entirely eliminated, and thus it follows, in the words of Willett, that "the risk an insurance company carries is far less than the sum of the risks of the insured, and that as the size of the company increases, the disproportion becomes greater"; or, to use the definition of Roscher: "The aggregate danger is less than the sum of the individual dangers, for the risk of it is more certain, and uncertainty itself is an element of danger." It is of the utmost importance that this point should be thoroughly realized by the statesman and the general public, so that from individual appreciation of insurance as a beneficent social institution may evolve the national appreciation of insurance as an institution making for the security of society and the well-being and effective protection of its members against the uncertainties of human life.

Applied Ethics.

At the outset we must consider the relation of insurance to ethics, for unless the business of insurance has the sanction of private and public morality it would be to no purpose to discuss its social and economic importance. One of the earliest objections to life insurance arose from the view that it was a form of gambling and that to insure one's life was not quite in harmony with religious duty. Even to-day a religious sect called the Dunkards object to life insurance on the ground that it has not

biblical sanction, or at least, is not specifically enjoined as a duty by biblical authority. Few things, however, it would seem, are more readily susceptible of proof than that insurance must of necessity be included in the moral forces which make for the betterment of mankind, and especially for the gradual amelioration of the condition of the poor. Life insurance in particular appeals to man's moral sentiments, making for the protection and support of others at the cost of self-sacrifice and self-denial. So well has this been realized that almost from its earliest history we hear of the *duty* of insurance, until to-day this sentiment has become subconscious and a part of the conscience of civilized man, practically the same under conditions of poverty as under conditions of material well-being.

Much injury has been done to the cause of insurance by the unfortunate and unwarranted assumption that there is a fundamental identity between insurance and gambling. There is this much truth in the assumption, that the fundamental laws of chance and probability have at times and with great skill been applied to efforts at systematic gambling, but speaking generally, without much success. Gambling, lotteries, and kindred attempts to gain by the losses of others are intrinsically immoral in their results, while life insurance is intrinsically moral as a method and means for the advancement of mankind. Insurance advances progress, while gambling retards it. This fact is well brought out by Dymond in his Essays on Morality, and is indorsed by Wayland in his Elements of Moral Science. Dymond remarks, with particular reference to the duty of insurance against fire, that "the merchant who conducts his business partly or wholly with borrowed capital is not honest if he endangers the loss of an amount of property which, if lost, would disable him from paying his debts." To guard against this possible loss he holds that it would be unjust under such circumstances not to insure, for the majority of uninsured traders, if their houses and goods were burned, would be unable to pay their creditors. The injustice, in his opinion, consists in the taking of needless or unnecessary risk. Had life insurance

in 1836, when this was written, been developed to the present extent of a universal provident institution, the Quaker moralist would, without question, have enjoined with even greater emphasis the duty of insurance protection for widows and orphans and self-protection against want in old age.

Insurance Mathematics.

The second great division of modern science is mathematics, itself the foundation stone of insurance theory and development. Without mathematics life insurance could not be thought of as a science, nor could its progress long continue without the application of mathematical checks to intricate processes, the real nature of which can only be explained by mathematical researches. It has, in fact, been common usage for many years to speak of the work of the actuary as actuarial science, and the training of the actuary and the required quality of his judgment is very largely mathematical. It is a primary necessity if he is to possess the ability to master the more subtle problems of insurance theory. It is, however, with much justice that Young and other writers hold that "every problem in life insurance administration—the scope of investments, the ratio of expenditure, and the amount of new business which will probably produce a favorable or disadvantageous effect upon profits—possesses an actuarial aspect of definite significance, and demands the application of professional knowledge and experience." But primarily the work of the actuary is concerned with the mathematical and fundamental nature of life insurance as determined by the laws of human mortality and expectancy, upon which the vast business rests with absolute certainty for the ultimate fulfillment of contract obligations. Some of the greatest names in mathematical science and astronomy are those of men who have rendered signal service to the cause of insurance. From Fermat and Pascal, Newton and Leibnitz, Bernoulli and DeMoivre, Laplace and Quetelet, we have a long list of mathematical philosophers extending to the present time, whose work has

made possible the development of the science of life contingencies. It is upon the science of mathematics that the science of insurance rests, and it is the actuary who applies abstract mathematical principles to the solution of practical problems of business administration. Hence the actuary must be more than a mathematician, and the tendency of the age is constantly to enlarge the function of this office by delegating the purely mathematical side of the work to qualified mathematicians. Much remains to be done in the field of insurance mathematics to develop the science and art of life contingencies to its highest possible degree of perfection. Great indeed as is the work of Woolhouse, Gompertz, Makeham and Young, each period presents problems of its own which demand the specialization of expert talent, never needed to such an increasing extent as in the administration of a great and successful life insurance company of to-day.

Biological Science.

Biological science, or the science of living things, rests, in a larger measure than is commonly assumed, upon a statistical foundation. Much, if not most, of what life insurance companies require to know of biology for the medical selection of risks relates to normal and abnormal man from the viewpoint of anatomy and physiology. American anthropometry, while well advanced since the army statistics by Gould were published in 1869, as a memoir of the Sanitary Commission, leaves much to be attained before we shall be in a position to deal in a strictly scientific manner with the problems of normal stature, weight, chest expansion, pulse-rate, and other elements too numerous to be here referred to. The tables published by the Association of Medical Directors and re-arranged by Dr. O. H. Rogers, are an admirable indication of the treasures which the archives of life insurance companies yield when subjected to expert tabulation and critical analysis. For the needs of accurate chest diagnosis we require more determining data than are at present available while the field of human thermometry as applied to

life insurance selection has remained almost neglected since Seguin published his work in 1876.

The larger and more involved problems of human multiplication and normal increase, the marriage rate, fecundity and sterility, consanguinity, race-mixture and intermarriage are all pending questions, toward the solution of which insurance contributes much information and expert talent. All that is summed up in the problems of heredity, both direct from parent to offspring and through collateral branches of the family, is of the utmost importance to life insurance companies, and in time the vast number of accurate family records in the possession of these companies as a part of the application for insurance, supplemented by the known results of subsequent mortality, with certified causes of death, must needs add much of value and interest to the future development and practical value of biological science. Toward the problem of reproductive selection, so admirably set forth by Karl Pearson, life insurance can contribute much valuable information, particularly on the point of the effect of the age of the parents at the time of the applicant's birth on the subsequent chances of his death.

Insurance Medicine.

If the mathematical basis of life insurance is derived from the doctrine of probabilities, the medical basis is derived from pathology, or the doctrine of diseases, their causes, mode of occurrence, etc. The position of the medical director is of equal fundamental importance in the administration of a life insurance company to the position of the actuary, in that upon the medical selection of risks proposed for insurance largely depends the subsequent mortality experience. With the immense development of life insurance in all countries has gone the advancement of insurance medicine, from the crude methods of the London Equitable Society in 1762, when a health certificate was required bearing the signatures of two witnesses, one of whom had to be a physician, to the uniform blank for medical examiners proposed a few years ago at the International Congress of Medical

Directors at Brussels. To-day there are few general practitioners who have not, at one time or another, rendered services to life insurance companies in the examination of proposed risks, and the number of physicians regularly employed by these companies is constantly increasing.

Insurance medicine has a large and valuable literature of its own, to which constant additions are being made as the result of special researches and increasing experience in a vast field with rare opportunities for the development of expert skill. The highly scientific character of this work is due, in a large measure, to the close relation of cause and effect. Errors of judgment in physical diagnosis, or the omission to note symptoms of incipient diseases, are certain to be followed by an unfavorable mortality experience. While errors of judgment on the part of the general practitioner outside of hospitals as a rule remain unknown, such errors on the part of the medical examiner are a matter of permanent record and are comparatively easy to discover.

Science of Neurology.

The neurology of the future will render even greater service to insurance science than has been possible in the past. Brain diseases, as a class, are unquestionably on the increase in this and other countries, and there is some trustworthy evidence to support the view that insanity is increasing at a perceptible rate from year to year. No extensive statistical investigation has been made into the alleged increase in insanity, which may be attributed to the complex nature of the problem, the difficulty of exact definition, the undefined borderland of sanity and insanity, and many other causes; most of all, however, to the confusing effect of the improvement in the recovery-rate and the decreasing death-rate in state and private institutions. Actuarial skill can be of great service to the medical profession in determining this question in much the same manner as in the investigation of the alleged increase in cancer by the eminent actuary, Mr. George King, cooperating with Dr. Arthur Newsholme.

Suicide.

Suicide may also properly be referred to here as one of the problems of neurology and one of great importance to life insurance companies. Suicide is on the increase in this and other countries. For illustration, in American cities the rate per 100,000 of population has changed from 12.0 during 1890 to 20.6 during 1909.* Qualified investigations into the probable causes responsible for this much-to-be-deplored increase in self-murder would be of considerable financial value to insurance companies. Of the total mortality of insured males, aged forty-five and over, 5.6 per cent. are deaths from self-destruction, and the financial loss to insurance companies is of much larger proportions than is generally assumed to be the case.†

Surgery and Gynecology.

The achievements of surgery are one of the glories of modern civilization and of both direct and indirect value to life insurance in making for an improved longevity and a resulting increase in the chances of a healthy life following a successful surgical operation. Beginning with the two principal factors—the introduction of anesthetics and the introduction of antiseptics—we have a long list of important modern discoveries in surgical methods which have done much to reduce human mortality and do away with needless suffering.

Gynecology has an important relation to insurance science. Woman as an insurance risk is one of the perplexing problems in life insurance practice. In most of the mortality tables for the general population women at nearly all ages experience a lower death-rate than men, and the tendency would seem to be toward a still greater difference in favor of women in the

* For an extended discussion of the suicide rate of American cities, with observations upon many interesting aspects of suicide in its relation to life insurance, see the annual articles by the writer in *The Spectator*, New York, 1890–1910.

† Mortality Statistics of the Mutual Life Insurance Company of New York, 1843 to 1898, page 47. New York, 1900.

future under modern conditions of life. In contrast, insured women have often proved a loss to the companies on account of certain subtle elements of adverse selection not readily comprehended or allowed for in the medical examination of women as insurance risks. As a rule, the physical examination of women, for reasons of modesty and general custom, is made with less care than in the case of men; obscure pelvic diseases and diseases of the ovaries and uterus often exist, but they are quite concealed. Many other facts brought out by extensive experience, tend to complicate the matter, and all companies, therefore, exercise great caution in the acceptance of women as insurance risks.

Science of Pediatrics.

During the past thirty years the chances of death have undergone a material modification, and in most civilized countries the general death-rate is much lower to-day than it was during the early seventies. This improvement in human longevity, however, affects almost entirely the younger ages of life and in particular children under ten years of age. The modern treatment of the diseases of children, or the science of pediatrics, combined with improved measures of public hygiene, has resulted in a great saving of infant life, which goes far to balance the general decline in the birth-rate. Industrial insurance companies in particular are affected by this improvement, and the amounts now paid at ages under fifteen for a weekly premium of five cents are at least twenty per cent. greater than they were some thirty-five years ago, when this method of family insurance was first introduced into the United States by Mr. John F. Dryden. There are, however, general benefits resulting to life insurance practice as a whole from the gradual diminution of a needless waste of infant life. A healthier type of manhood and womanhood must develop from children free from the after-effects of acute infectious diseases so extremely prevalent in the past.

Sanitary Science.

The reduction of the chances of death is primarily the result of our increasing knowledge of the causes and true nature of diseases, the conditions favoring a high or low death-rate, and the necessary means and methods for their effective control. For want of a better term we use the one of "sanitary science," which includes both *preventive medicine* and *public health* administration. As a first requirement it was necessary to perfect the official registration of deaths and the medical or legal certification of their causes. Vital statistics form the groundwork of sanitary science as it has been developed during the past fifty years in all civilized countries. The history of disease prevention, or in particular epidemic diseases. has a large literature of its own, including the modern laboratory researches which have attained to a high degree of excellence. The great work of Creighton on Epidemics in Great Britain is an illustration of what is required for our own country before medical topography and geographical pathology will have reached the high position to which they are destined in due course of time.

Medical Topography.

The American life insurance companies of the first forty years of the nineteenth century are of little more than historic interest to us at the present time. The Pennsylvania Company for Insurances on Lives and Granting Annuities, the Massachusetts Hospital, the New York Life Insurance and Trust Company, the Baltimore Life Insurance Company, the Girard Life Insurance and Trust Company, the Ohio Life and Trust Company, and others, transacted but comparatively little business, so that by 1850 it is estimated only about thirty thousand life insurance policies were in force in the United States. In 1843, however, the organization of the Mutual Life marks the beginning of a distinct period of life insurance history which extends to 1875, when industrial insurance was introduced by the Prudential. A number of valuable contributions to the literature of public medicine and medical topography had been made, and it grad-

ally became possible to obtain a more correct view of the value of human life in the different sections of the country. Bills of mortality were available for a number of important cities, and Sybert, in his Statistical Annals of the United States, published in 1808, could supplement his observations by two life-tables calculated for the use of the Pennsylvania Company for Insurances on Lives and Granting Annuities. One of these tables was derived from the records of the Episcopal Church, the other from the records of the Philadelphia Board of Health. The gradual development of public medicine is exhibited in the volumes of the Journal of Health, the first of which was issued in 1830. Ten years later a valuable report on the Sickness and Mortality of the Army of the United States, embracing a period of twenty years, was published by government authority, which contains much interesting and suggestive information relative to the health of different sections. This valuable document was followed by the classical report of Shattuck on the Vital Statistics of Boston for the period 1810-1841. In 1842 Forry brought out his treatise on the Climate of the United States and its Endemic Influences, which still retains its position as a work of great value. In 1845 Shattuck supplemented his earlier work by a Census of the City of Boston, which forms the first comprehensive statistical account of the population of an American city. Dawson and De Saussure, in 1849, published their Census of Charleston, S. C., which included observations on health, mortality and insurance. In the same year the first report of the Committee on Public Hygiene of the American Medical Association was published, which contains much valuable information on the medical topography of the most important sections of the North and South. The American edition of Tilt's Elements of Health was published in 1853 in Philadelphia, a book admirably arranged for the use of the period, with special reference to the requirements of life insurance companies. In 1854 Drake issued his medical topography on the diseases of North America, with special reference to the Diseases of the Interior Valley, unquestionably the greatest

contribution to the medical topography of our country up to that time. Following Drake, Blodget, in 1857, issued his well-known treatise on the climate of the United States, which includes a valuable chapter on medical topography. The scientific interest of American life insurance companies in the subject of human mortality is made evident by the publication, in 1857, of a Report on Vital Statistics, by James Wynne, M. D., to the Mutual Life Insurance Company, but the expenses for which were shared by seventeen other companies, including all of the more important and representative institutions of the period.

Longitude and Latitude.

The office practice of the early American life insurance companies during the fifties was, however, in a large measure determined by very fragmentary data. Most of the observations and conclusions of writers of the period on medical topography were derived from extensive travels, carried on under great difficulties and at considerable personal exposure to the ill-health-producing conditions described. The general apprehension was not so much as to the probable unfavorable experience in the country at large as in the Southern and Far Western sections. The general apprehension as to a high death-rate in the South was amply supported by the published mortality statistics of New Orleans, Mobile, and Savannah, and many able articles in the Southern medical publications. Dunglison, in his treatise on Human Health, one of the first works on hygiene published in this country, connects the science of public medicine with the science of insurance by a chapter on "Atmosphere and Locality." An Englishman by birth, he stated that when he was about to leave Great Britain to occupy a situation for which he had been selected in the University of Virginia, a life insurance company of which he was a member declined to continue the insurance unless the premium was doubled. Dunglison wrote that this requirement compelled him to sacrifice or lapse his policy. Many of the assumptions with regard to health in Southern latitudes were, however, largely exaggerated.

Dunglison's treatise did much to correct erroneous views, though on the whole a regard for truth compelled the author to admit the extensive prevalence of health-destructive conditions which it required time and an infinite amount of human labor to change for the better. Even at this early period, however, it could be said with much truth that within the last century the value of life had increased progressively and was rapidly improving, but as long as the primitive conditions of pioneer life obtained it was out of the question for life insurance companies to develop their business on a large scale, especially in the Southern and Western States. Speaking generally, the slow growth of American life insurance during the first half-century, was in a large measure, due to the high mortality, the frequency of epidemic diseases, and the fragmentary vital statistics of the period.*

The selection of risks for insurance, while primarily medical, takes also into careful consideration certain facts, most of which may be included under the general term "environment." These are locality of residence, housing, occupation, habits, and war, all of which are more or less comprehended in the department of preventive medicine and public and personal hygiene.

Psychology.

The immense development of modern life insurance, which has now become almost a universal provident institution, is primarily the result of the insurance education of the public through the solicitor or life insurance agent. Psychology alone explains the mental processes by which so abstract an idea as the theory of risk and insurance is reduced to "insurance consciousness" and made operative on conduct. It is not necessary, in fact it is not desirable, because tending to confusion of thought, that the abstract idea or even the business methods of insurance should be

* Among the important contributions to the sanitary history of this period are Fenner's Southern Medical Reports, Vols. I and II, New Orleans, La., 1849 and 1850. See also the writer's essay on Life Insurance in the South Before the War, in "The South in the Building of the Nation," Richmond, Va., 1910.

comprehended by the applicant for insurance protection, any more than we require to know the chemical analysis of foodstuffs and the processes of their manufacture to enjoy and digest our daily meal. What is required is education in the simple elements of insurance protection, emphasized by intelligent suggestion and an effective appeal to the emotions. What the prospective policy-holder needs to know is the actual expense of risk transference, the amount of insurance provided in the event of certain contingencies, and the special contract provisions of the policy, which form the legal basis of the relation of the insured to the company.

The principles of risk and insurance are of too abstract a nature to be comprehended by the average mind, even after a considerable amount of intelligent explanation. The elements of insurance practice and results, however, are readily within the mental grasp of all but a small proportion of the public, and while in consequence of the enormous development of the business there exists a vague general consciousness of the insurance idea, it is but imperfectly understood and not sufficiently operative on conduct. We are taught by psychology that "an object must be seen many times before it is *rightly* seen," and the abstract idea of insurance does not become concrete and operative on conduct until it has been emphasized and re-emphasized by the insurance instructor, who is called the agent or solicitor. The immense success of industrial insurance, with now more than sixty million policy-holders in the world, is due largely to the simplicity of the idea itself—so much to be paid each week—so much receivable in the event of death—which is readily within the mental grasp of all the people. In the more complex form of ordinary life insurance, especially when combined with investment, as in the case of endowments, the process of insurance education is much more difficult and results are secured more slowly. What is true of the progress of life at large is equally true of the progress of insurance, that "the adjustment of inner tendencies to outer persistencies must begin with the simple and advance to the complex, seeing that both within

and without complex relations, being made up of simple ones cannot be established before simple ones have been established."

The Psychology of Suggestion.

Abnormal psychology has already been briefly referred to under neurology. The psychology of suggestion in its special relation to the occurrence of mental epidemics is of considerable interest to life insurance companies. The present-day frequency of self-destruction and the unquestionable effect of suggestion in causing small epidemics of suicide of a local character is a source of considerable anxiety to the management of conservative insurance companies. What is summed up in a dissertation on The Wonders of Human Folly explains the need from time to time to recur to the experience of the past for an explanation of the experiences and occurrences of the present. Mackay's Memoirs of Popular Delusions, for illustration, throw much light upon recent experiences, and it has been said by him with much truth that while "time and progress have changed the manifestation, the spirit of ancient folly lingers still. . . . From time to time the infatuation to acquire wealth speedily by an illegitimate shifting of the cards rather than by safe and equitable methods in the employment of capital and labor, seizes the people; and thus probably it will ever be until those who possess property shall be acquainted with the principles and laws of trade and shall at the same time be desirous to restore to the commercial character generally an inviolate and inflexible spirit of single-minded honesty."

Anthropology and Anthropometry.

In the selection of risks for insurance it is necessary to take into consideration certain broad principles of anthropology, in particular the primary distinction of race, or the varieties of mankind. Even the most cursory inquiry reveals important differences between the longevity of different races and peoples which no conservative insurance company can prudently ignore. "The physical peculiarities and geographical distribution of

the human family," wrote Pickering, "form one of the most interesting problems in history"; and in the words of Darwin, "There is no doubt that the various races, when carefully compared and *measured*, differ much from each other." Unfortunately, most of the earlier anthropologists took more interest in speculations as to the unity or plurality of the human species than in determining types of mankind by careful and extensive measurements and observations of physical, psychological, and pathological characteristics.

Quetelet, to whom insurance owes much light on the theory of probability, was also the author of valuable works on normal man and anthropometry, which have done much to suggest the more recent investigations. The methods of Quetelet, as to both measurement and description, were followed to advantage in the more elaborate works of Beddoe, Roberts, Gould, Baxter, and many others. We are nearer to the truth to-day than we have been, but are yet far from having the required data for a practical anthropology or science of man applicable to the solution of pending problems of insurance.

Geographical Pathology.

Every advance in geography and the more accurate mapping of the surface of the earth contributes to the science of insurance. Medical topography and geographical pathology depend primarily upon accurate topographic surveys, and the immense advances which have been made in this direction during the past twenty years have been of great value to insurance science. The geographical distribution of disease is receiving more and more the intelligent consideration of the geographers of to-day. As an admirable illustration of what in time may develop into a distinct science, mention may be made of Haviland's work on the Geographical Distribution of Disease in Great Britain. Even the very early American geographers recognized the relation of physiographic and climatic conditions to health and mortality, and Guthrie, for example, in his geography published in 1795, refers to the subject at some length. Darby, following

Guthrie, contributed valuable observations in his various writings, particularly in his View of the United States, published in 1828, and in his Geographical Description of Louisiana, published in 1816. The ultimate tendencies of geographical science in this particular direction are best illustrated in the Appendix of Maps to the Report of Sir H. H. Johnston, as Special Commissioner on the Protectorate of Uganda. These maps illustrate with exceptional clearness the average altitude and the salubrity of each district, and it is not going too far to say that we have really more accurate information regarding this distant section of the globe than we have for many sections of our own country. The importance to insurance companies of similar investigations into our own Southern States, and in particular into our new possessions in tropical countries, cannot be overestimated. The works of Sir Henry Johnston illustrate the methods to be followed and the practical results to be attained.

Geology and Mining.

It is hardly practicable to separate a discussion of geology from the preceding discussion of geography in its relation to insurance science, since every geographical survey contributes to the development of the science of physiography by the mapping of surface geology and general topography. Areal geology often discloses important factors of soil composition, etc., which have a distinct and well-understood relation to health and mortality; as, for illustration, in the clay formations which underlie the Gulf coast of southeastern Texas, and which, in a large measure, are responsible for some perplexing sanitary problems at Houston and Beaumont. The comparatively recent development of scientific soil surveys may here be referred to, for many of the reports which have been published emphasize important points in medical topography. Of special interest, for illustration, are the reports for portions of the Yazoo Delta and the Gulf parishes of Louisiana. In addition, these reports usually contain a careful analysis of the elements of climate and other matters of interest and value to life insurance companies.

It is, however, in the field of economic geology, and the mineral industries and mining, that life insurance companies have, perhaps, the most important interest. The immense development of the mineral resources of the earth give employment to a vast army of men whose occupations are almost without exception of a dangerous or unhealthful nature. Mining accidents are still of great frequency, and the present-day tendency does not seem to be toward a substantial reduction in the rate.* The problem of miners' phthisis is attracting much attention, especially in Utah and South Africa, where exceptional conditions present unusual difficulties. The geological formation of coal areas determines in part the accident frequency from falls of roofs and gas explosions. The mineral composition of rocks has a direct relation to the frequency of industrial poisoning in the milling and smelting of copper and other metalliferous ores, while the accident liability of quarrymen depends partly upon the geologic formation of the strata to be removed.

Meteorology.

Meteorology I assume to include both climate and weather service. The field is immense, for, as has been observed by Montesquieu, "The empire of climate is the most powerful of all empires," and the progress made by meteorology has been a material gain to life insurance science. The normal climate of any given locality is a factor of great importance in determining health and longevity. The elements of temperature, barometric pressures, humidity, rainfall, prevailing winds, etc., are of considerable determining value, but as yet we have not the required standards by which accurately to measure the effects of these elements on human health under the varying conditions met with in different portions of the globe. We still speak of the "deadly climate" of the west coast of Africa or of French Guiana, with not much better knowledge of the facts

* See Bulletin No. 90, Bureau of Labor, Sept., 1910, Washington, D. C., for a full discussion, by the writer, of the frequency and causes of fatal accidents in coal mining in North America.

than when these expressions first came into use, under entirely different conditions of attempted settlement or colonization. While the climate and weather of India are the same to-day as at the time of the Great East India Company, the mortality of European troops has been reduced from seventy-six to sixteen per thousand. While it may be true, as Ripley holds, that "the English of to-day are no nearer to true acclimatization in India than they were in 1840," there can be no doubt that a more perfect knowledge of the elements of tropical climates and the resulting tropical hygiene have done much toward the ultimate solution of the white man's conquest of the tropics.*

Industrial Technology.

The applied sciences can only be discussed here in the most general way. All improvements in processes and methods of manufacture, as a rule, benefit the workmen by incidental improvements in the sanitary condition of factories and workshops. The increasing proportion of risks written by life insurance companies on the lives of persons employed in manufacturing industries points to the importance of all improvements in industrial hygiene and their resulting relation to the diseases of occupations. The improvements in the processes of manufacture imply, as a general rule, a decreasing amount of waste in the form of dust, vapor, or gases, many of which are of a health-injurious character. The utilization of waste products, on the other hand, has led to new industries, many of which are injurious to health and life. The consolidation of industries in the form of industrial combinations or trusts, primarily for the purpose of effecting economies, has done much to improve sanitary conditions by providing new and larger factories with more light and better ventilation, so that it is safe to say that since the introduction of the factory system the average workman has never been employed under healthier conditions than at

* An important contribution to the subject is "Effects of Tropical Light on White Men," by Major Charles E. Woodruff, M. D., New York, 1905.

the present time. To insurance companies the problems involved in industrial technology are, however, extremely complex and a never-ending source of anxiety. For illustration, the relatively new process of pulp manufacture is carried on by three distinct methods, the mechanical, the soda, and the sulphide, each of which represents different conditions affecting health and longevity, which require to be taken into account in the acceptance of this class of risks. In electrical engineering the truly astonishing progress which has been made during the past few years has resulted in entirely new conditions, which no prudent company can safely ignore. As an illustration, mention may be made of the introduction of electricity into mines which has been the subject of an official inquiry in England and by state mine inspectors in this country. The enormous development of electrical industries in general has resulted in entirely new conditions, which cannot be fully understood in the light of past experience. Mining engineering, perhaps most of all, requires serious consideration, and among other new factors affecting health and longevity, is the extensive introduction of coal-cutting machinery into the bituminous coal mines of our Western States. In ore-milling and smelting new processes are constantly supplanting old methods, and here again present-day practices cannot be determined by past experience. As an illustration of the benefits to health arising from the utilization of waste products reference may be made to the modern appliances in smelters by which many of the health-injurious vapors and gases are converted into profitable by-products.*

Legal Science.

The general conception of insurance law limits this term to the settlement of legal difficulties arising from the contractual relations of the company and the policy-holder. Most of the books which essay upon the subject, from Park and Marshall

* In this connection Census Bulletin No. 190, June 16, 1902, on "Utilization of Wastes and By-Products" may be consulted to advantage.

to the latest digest and dissertation, treat of insurance law in this narrow and restricted sense. We have not as yet a comprehensive work which includes the relation of the companies to the state and public policy in addition to the relations at law of the company to its policy-holders and agents. The brief consideration which I can give to this subject precludes proper treatment of so complex a relation as that of insurance to legal science, and at best I can only indicate the more important results of law, jurisprudence, and social regulations affecting insurance interests.

Under modern conditions the conduct of a life insurance business is beyond the reach of individual or private enterprise. It is to-day an accepted principle of government that "life insurance is a business of so sacred a character, and involving issues so important to the national welfare of each country, that it must be the subject of special legislation in order to safeguard the interests of the insured. . . . It is their savings in the shape of premiums and their accumulations which constitute almost the entire resources of every life insurance company, and it cannot be a subject of unconcern to any government that its citizens should have made provision for the future to so large an extent, and that the security for the eventual payment of the sums assured, as they mature, should be guaranteed by the solvency and sound investments of the companies that underwrite the contracts. " Insurance companies derive their existence from charters specially granted, but in conformity to the general corporation laws of the different states. Corporations are by law endowed with perpetual succession, or, in other words, are artificial persons having no necessary or natural term of life, and they may be regarded as an extension of individual capacity. The earlier charters of American insurance companies illustrate the crude ideas regarding the business of life insurance at a time when the term "insurance," in the words of Park, was practically equivalent to "marine insurance." Almost from the beginning of the business of insurance the importance and necessity of some form of state supervision was

recognized, and we meet with the inception of the present form of state supervision in a Massachusetts statute of 1827, which required the companies to report annually as to the condition of their business. The growth of the business and the extension of operations to other states developed the present system of state supervision, which had its origin in a law passed by the legislature of Massachusetts, establishing a separate department for the supervision of insurance interests, in 1855. To-day such departments exist in every state and territory, with more or less comprehensive powers for supervision and control. The resulting problems are of most serious concern to the companies.

State Supervision of Insurance.

The insurance laws of the different states are often widely at variance with one another. The remark of Mr. Griggs, ex-Attorney General of the United States, that while "the interpretation of the law is a science, law-making is not," applies with special force to the insurance legislation of the last thirty years. When, in 1876, Mr. C. C. Hine issued his volume on Insurance Statutes, within six years of the issue of a similar work by Wolford, he could truthfully say that "the insurance laws of five years ago are almost obsolete, and in their stead new statutes have come upon the books of almost every state and territory." The process of grinding out laws has gone on with undiminished energy, and the opinion of a learned judge that "no attorney is bound to know all the laws" may give some comfort to the law officers of insurance companies confronted by the problem of digesting the large number of special statutes passed annually or biennially by forty-nine different states and territories for the ostensible purpose of regulating the insurance business. In marked contrast, we may reflect upon English legislation affecting insurance interests, which since 1870 has practically remained the same*. Mr. Griggs, in his address on "Law-Making," properly remarks that "history of the

* The English Assurance Companies' Act of 1909 is fully discussed in Chapter VIII.

English law reveals change and growth, but growth by slow and deliberate processes." It would be an immense step in advance towards the perfection of American insurance law if a similar habit of mind prevailed in this country.

The taxation of life insurance companies need only be referred to here as an important problem of insurance company administration. If it is the duty of the state to encourage thrift or efforts on the part of the people toward economic independence and a secure position above the need of state aid, it is certainly a paradox to meet with an increasing tendency to tax life insurance policy-holders out of a relatively large share of their annual savings. In many countries other than the United States insurance is supervised and regulated by some central authority—in England by the Board of Trade, in France by the Minister of Commerce, etc. There must come a time when the burden, expense, and annoyances incident to supervision by some forty-nine different insurance commissioners of states and territories will become intolerable and some form of federal supervision must be the result.

International Law.

An increasing number of life and fire insurance companies are extending their fields of business operations to foreign countries, and in a few cases American life companies transact business in most of the civilized countries of the earth. Without wishing to underrate the ratio of progress made by life insurance companies of other countries, it is generally conceded that the American life insurance companies abroad are more aggressive, and as a rule attain more readily to a commanding position than the home companies. As a result, there is, at first, much local antagonism to foreign insurance companies, to which, in part, at least, must be attributed the burdensome regulations which have been imposed in certain countries upon American insurance companies. On the other hand, there can be no doubt that during the past quarter of a century the tendency has been politically and socially to draw states together

by the strong attraction of "common political sentiments, common aspirations and common interests of a permanent kind." Insurance may rightly claim to be one of the forces making for international harmony and good will.

Contract Law.

All insurance is in the nature of a contract between the company and the insured, who is usually referred to as the policyholder. The policy is the instrument which defines the respective rights and duties of the contracting parties, who are assumed to be aware of the fact at law that "a contract is a deliberate engagement between competent parties, upon a legal consideration, to do, or to abstain from doing, some act." Out of the contractual relation and its unavoidable disputes, misunderstandings, etc., has resulted a mass of litigation and court decisions usually comprehended under the term "insurance law." A retrospect over the many years since, in 1601, the "Court of Insurance" was established by Queen Elizabeth, and the sixty-odd cases tried during its entire history, to the present time would carry me far beyond the present purpose. Suffice it to say that the development of insurance law has gone forward with the growth of the business until this term now comprehends a variety of subjects unknown and unthought of at the time when Park and Marshall first published their works, about a century ago. Considering the enormous extent and highly complex character of the insurance business, it is a matter of surprise to find that, after all, the amount of litigation should have been so small. The tendency has been constantly towards a contract free from restrictions likely to lead to litigation, until the life insurance policy of to-day is practically a promise to pay a certain sum on the occurrence of a given event, except in the case of fraud. There has always been an unfortunate disposition on the part of the courts to construe a policy of insurance more upon the grounds of sentiment than upon the common law of contract and fraud. Mr. Davies, the eminent solicitor of the Mutual Life, has discoursed upon this matter in so able

and interesting a manner that I take the liberty of quoting to some extent from his lectures on the law of life insurance:

"A suit upon a life policy is an especially difficult one to defend for several reasons. In the first place, there exists in this country a very general prejudice against corporations, which inclines a jury to view with favor any claim by an individual against one of them. Then the plaintiff is usually a widow or some other dependent of the deceased, and the contrast is strongly drawn by the counsel *arguendo* between her poverty and the heaped-up millions of the defendant, the corresponding liabilities of the latter being carefully kept in the background. . . . And to these considerations must be added another of a much higher character, that natural human instinct which leads us all to speak well, and endeavor to think well, of the dead. The fall of the curtain upon a human life covers at the same time his faults and vices, and adds enormously to the difficulty of establishing to the satisfaction of a jury facts which are notorious, but which blacken his memory. The very neighbors, who during a man's life denounce him as a worthless sot, will, when called as witnesses in a suit upon a policy on his life, reluctantly admit that he perhaps on rare occasions drank to excess, but not to an extent to impair his usefulness or affect his health. So when a suicide takes place the associates of the deceased at once begin to think that they had previously noticed symptoms of aberration of the mind, quite sufficient to justify a strong suspicion of his sanity, although no such idea had ever occurred to them before the catastrophe."

The Law of Agency.

The life insurance agent is, as a rule, an appointed employee of the company and under contract to perform certain services in return for a stipulated compensation. The employment of agents is so universal that but few policies are obtained otherwise than through these representatives of the company. Out of this condition some very important legal questions and problems have arisen, aside from the occasional difficulties and misunderstandings between the company and its employees. The agent, as a rule, is the only personal representative known to the insured, and the agent's position is thus one of very considerable responsibility and importance. The company naturally

aims at a narrow limitation of the agent's powers as to the issue or modification of the contract between the company and the insured, and most of the policies issued contain a clause to the effect that "no condition, provision, or privilege of this policy can be waived or modified in any case, except by an indorsement signed by an executive officer of the company."

Insurance and Public Policy.

Insurance in its relation to public policy presents some very interesting problems of law and jurisprudence. A policy of insurance is issued upon the faith of the statements made in the application for insurance, and the applicant is required to warrant the truth of his statements. The effect of warranty is to insure the accuracy of the state of affairs alleged in it; and consequently the greatest care in making a declaration of them is requisite. There has been a considerable amount of litigation and resulting decisions of the courts on the question of concealment and misrepresentation, but as a rule the decisions have been in favor of the insured. It should be manifest that it is contrary to public policy to encourage fraud, concealment, and misrepresentation, by means of which insurance is obtained under conditions which would have precluded the issue of the policy had the facts been truthfully stated to the company. A common form of misrepresentation is as to the present state of health of the insured, particularly in cases where even the most advanced methods of medical diagnosis cannot establish with entire accuracy the facts at the time the application for insurance is made. Losses thus sustained by the companies are to the injury and disadvantage of the honest policyholder, and by this much the true progress of the business is retarded. A strict construction of the statute of frauds is, therefore, one of the most certain means of advancing life insurance interests.

Insurance Economics.

The economic theory of risk and insurance has only received incidental consideration by writers on economics and social

problems, with the notable exceptions of Willett and Macleod. This is unfortunate, for insurance, in one way or another, reacts upon the whole economic life of the people, and there is no hope of a rational political economy until *all* the elements of social and economic progress are taken into account. The economic value and utility of insurance are important and proper subjects of economic inquiry, and the immense progress of the business demands the impartial and critical consideration of qualified experts in economic and social science. The view of Macleod that "annuities or rights to receive a series of future payments" are negative economic quantities, under which term he comprehends all instruments of credit, shares in commercial companies, policies of insurance of different kinds, etc., does not seem to have been accepted by other writers on economic theory.

The earlier writers on the investments of the working class gave considerable attention to life insurance and its relation to the general welfare. Gregg, among others, wrote in 1851, or three years before the practical beginnings of industrial insurance in England, that "life insurance policies offer one of the most important channels of investment for the savings of all classes"; and he adds, "Of all modes of employing small savings, there is none which we should so earnestly desire to become general among workingmen; none which appears to us so deserving of the fostering care of the legislature; none which, if universal and habitual, would do so much to diminish those cases of utter and helpless destitution which press so heavily on the resources of the community in the shape of poor-rates, and which are the fruitful parents of a long progeny of calamity and crime."*

The progress of insurance since this was written challenges the admiration of the world. In the United Kingdom the

* A most interesting investigation into the subject of savings of the poor is contained in a Parliamentary Report on "Savings of the Middle and Working Classes," ordered by the House of Commons, to be printed, July 5, 1850.

industrial companies alone, excluding collecting and other friendly societies, have now some thirty million policies in force on the lives of workingmen and their families. The question raised by Prof. Falkner as to whether "the growth of insurance in recent years has been mainly among the well-to-do," can be emphatically answered in the negative. In fact, life insurance, almost from its inception, has met with greater appreciation among those who, for want of a better term, we speak of as the working class. This aspect of the business is one of economic history rather than theory, but here again we find that, with few exceptions, writers on the progress of economic and social institutions have made little of a fact which is none the less of profound economic importance and significance.

Insurance History.

The study of insurance history and the history of associations, gilds, and friendly societies, is a most instructive chapter in economics. Far back into ancient history careful students of commerce and navigation have traced at least a semblance of our present form of marine insurance. Anderson's History of Commerce contains some very suggestive illustrations of a possible connection of present-day methods to those of an earlier and almost forgotten time. Turner, in his History of the Anglo Saxons, and Eden, in his State of the Poor, throw much light on primitive methods of solving social problems in conformity to the principles of association. Walford, in his work on Gilds, and Toulmin Smith, in his great work on English Gilds, with the introduction by Brentano, are indispensable sources of information to the student who would rightly understand the foundations upon which the present massive structure of insurance rests.

But other materials of great value are readily available to the student of insurance and economic history. The great work of Walford, unhappily not completed beyond the letter H in the Insurance Cyclopaedia, published between 1871 and 1880, is a monumental work of human industry and learning. Of more

recent works on insurance history mention may be made of Martin's History of Lloyds and Marine Insurance in Great Britain, published in 1876; the century History of the Insurance Company of North America, published in 1885; the semi-centennial History of the New York Life Insurance Company, published in 1896; the quarter-century History of the National Fire Insurance Company of Hartford, published in 1897; the century History of the Norwich Union Fire Society, published in 1898; the History of the Prudential Insurance Company of America, published in 1900, and finally the half-century History of the Springfield Fire and Marine Insurance Company, published in 1901. I must also not fail to mention a reprint of Documents Relating to the Early History of the Scottish Widow's Fund and Life Assurance Society, published in 1901. The student of economic history and economic institutions will find much of value in these volumes which will aid him towards a more correct interpretation of the factors which have made for social progress during the nineteenth century.

Insurance as an Element of Commerce.

Any effort to trace the origin and growth of insurance must necessarily take into account the development of navigation and commerce during the last three hundred years. Evidence is not wanting that even among the nations of antiquity marine insurance in some form or other was not wholly unknown. Park and others have traced the beginnings of marine insurance to very early periods, but it has remained for the last three centuries to develop the system to its present state of universal utility. Even the most casual study of the history of navigation and commerce reveals the immense advantages resulting from the practice of marine and fire insurance. In the words of McCulloch: "Without the aid that it affords, comparatively few individuals would be found disposed to expose their property to the risk of long and hazardous voyages; but by its means insecurity is changed for security and the capital of the merchant whose ships are dispersed over every sea and exposed to all

the perils of the ocean is as secure as that of the agricultural risk. He can combine his measures and arrange his plans as if they could no longer be affected by accident. He has purchased an exemption from the effects of such casualties; and applies himself to the prosecution of his business with that confidence and energy which nothing but a feeling of security can inspire."

The principle of insurance in its application to commerce is, however, no longer limited to marine and fire insurance. The last fifty years have seen the practical development of the insurance idea in various other directions, of which I may mention the following: Accident, health, and employers' liability insurance; fidelity, surety, bond, mortgage, and title insurance; plate-glass, elevator, and boiler insurance; hail, windstorm, and tornado insurance; and finally, live-stock and burglary insurance. All of these have assumed the character of instruments of commerce and are in theory and fact an indispensable element of the commercial development of the present age.

Modern Tendencies.

The present-day tendency to industrial organization and the combination of capital is reflected in the status of the insurance business of the United States, which has followed the general commercial trend of the age. Of the ordinary life insurance business, six companies have fifty-six per cent, of the total insurance in force; of the industrial business, ninety-three per cent. of the policies are with three of the companies transacting this form of insurance; and of fraternal insurance, so-called, forty per cent. of the membership is in five of the principal organizations. The resulting gain has been very considerable, especially in the direction of enhancing the general security of the business and public confidence in this form of individual and family protection. This tendency has not operated injuriously to the development of a healthy spirit of competition, which may be illustrated by the fact that there are to-day about one hundred and seventy ordinary and twenty-

three* industrial insurance companies transacting business in the United States. The problem of wealth and its distribution may be summed up in the statement by Thompson that "the property of the most numerous class, that is, the poorest, is coming evermore to the front as a great problem of modern statesmanship." Life insurance is to-day one of the most important factors in the re-distribution of wealth, and perhaps of all the methods the most equitable and effective. It reaches every stratum of society and enables the poorest to provide for the future a sum of money which in every sense of the word represents capital obtained by individual efforts as the result of habitual saving and prudent self-denial. The insurance companies collect these savings in small amounts, which range as low as three cents a week, or assume considerable proportions per annum; the accumulations form the assets of the companies and as such they become available for profitable investment in productive industries and trades; they are redistributed through payments to policyholders as claims or matured endowments or annuities, in sums which range from an amount sufficient to pay for a burial to returns which represent a considerable fortune. As Walter Bagehot said some years ago, "People insure their lives who save in no other way," and the vast sums accumulated by life insurance companies, now nearly four billion dollars, represent an amount of economic security and evidence of an effective adaptation to the exigencies of modern life without a parallel in economic history.

Transportation.

The field of insurance is primarily the city and surrounding territory, but by degrees the more sparsely populated sections of the country have become available in consequence of the development of the science of transportation. From 92,000 miles in 1880, the railway system of the United States has grown to over 250,000 miles in 1909, opening immense

* Seventeen of the Industrial companies also transact ordinary insurance.

areas to settlement and leading to the subsequent development of cities and towns, which necessarily contribute towards the further extension of every form of insurance. The remarkable development of electric railways has opened large sections of the agricultural regions previously outside of the sphere of profitable business operations. Railway and navigation companies employ a large number of men exposed to a considerable accident liability, which requires special consideration. While great improvements have been made in railway transportation tending to diminish the mortality from fatal accidents, especially in connection with the coupling and uncoupling of cars, the mortality of certain classes of railway employees remains very considerably above tbe normal of men of corresponding age employed in less dangerous occupations. There has not been the reduction in the death-rate which earlier discussions and the passage of the laws relative to the prevention of accidents seemed to warrant. The problem remains one of serious concern to insurance companies transacting either a life or accident business, or both.

In still another direction are insurance companies interested in transportation science, and that is the opportunities for safe and profitable investment in railway bonds and mortgages. An incidental result of great importance has been the opening of new agricultural areas with a corresponding opportunity for profitable farm loans, which are perhaps the most advantageous and satisfactory investment of insurance companies, if made with the necessary knowledge of local conditions of soil and climate. There is, therefore, abundant evidence of the close relation of the science of transportation to the science of insurance.

Banking and Currency.

Banking, currency, and public finance are fundamental factors determining insurance progress. With more than $3,500,000,000 of assets invested in interest-bearing securities, the companies have a vital stake at issue in all questions of sound money, a stable currency, and healthful trade condi-

tions. Of the assets of the companies, nearly eighty-five per cent. are securely invested in bonds, stocks, and mortgages, including every form of approved federal, state, and municipal indebtedness, first-class railroad bonds, farm loans, etc. The necessity of earning a certain rate of interest demands the most experienced judgment in making these investments and a watchful eye on general banking and trade conditions. All of the great financial reform measures by which this country has reached its pre-eminent position in the world's money market—the National Banking Act of 1863, the resumption of specie payments in 1878, the defeat of the free silver craze in 1896 and 1900, and, finally, the passage of the Gold Standard Act—have contributed to the progress and stability of life insurance during the past forty years. In fact, such progress would have been out of the question as long as there existed "great dissimilarity in the laws governing banks in the several states, precluding uniformity, security, and safety." Hepburn points out that, in 1861, "there were then some 7,000 kinds of denominations of notes and fully 4,000 spurious or altered varieties." It is not a matter of surprise that under these conditions, between 1851 and 1861, the actual increase in life policies in force should only have been about 30,600.

But the influence of life insurance extends to every aspect of finance and trade. With its necessarily intimate relation to banks and trust companies, life insurance assumes the position of a regulating medium to which in no small degree may be attributed the more perfect control of the money market in hours of uncertainty and impending financial disaster. If crises and depressions are today a more remote element of business probability, and if this is due, in part at least, to "the greater skill and prudence exercised by bankers as the result of experience," I do not go too far when I hold that this gain is due in a measure to the fact that there are many important banks and trust companies which have on their boards of directors one or more men who are also officers of life and other insurance companies. Our financial history of the past

ten years shows conclusively the influence of conservative life insurance finance as a restraint and preventive of a recurrence of the disastrous series of panics between 1825 and 1893.

Social Science.

Sociology and social science, including all the more important divisions, is so comprehensive a term as to preclude consideration in detail. Social structure alone, as revealed by the census and other statistical investigations, bears a more or less direct relation to insurance development and progress. Census inquiries are now made with more skill and accuracy than heretofore, and every new investigation brings out new facts and tendencies of society in the process of evolution from homogeneity to heterogeneity. The mere statistics of past and present population, its distribution by rural and urban communities, its composition by sex, age, color, nativity, and occupation, are all elements of a determining nature which it is necessary to know for the more intelligent control of insurance practice. Without an accurate knowledge of the population and its distribution by age and sex, no life-tables could be worked out for the general population, and without a careful analysis of the facts of physical and social environment, no definite business policy could be established.

Most important is the relation of insurance to the family. Life insurance as a social institution primarily contemplates the certain and effective protection of widows and orphans, or, in other words, an extension of conjugal duties resulting from marriage under the existing conditions of modern life. Many of the earlier insurance companies were, in fact, called "Widows' Schemes," or "Widows' and Orphans' Assurance Societies," or, in the words of Price, "Institutions for the Benefit of Widows." The biological problems resulting from marriage and its relation to insurance are of much importance, and I may point out that among the most involved calculations of insurance practice are those of survivorship in marriage. Interesting data and calculations on this subject are to be found

among other sources in a comprehensive work on the Madras Military Fund, which includes observations on the mortality of wives, the rate of mortality and re-marriage among widows, wives, chance of widowhood, etc. Westermarck has contributed the most important investigations on the "Statistics of Marriage" derived from Danish data, while Westergaard has a discussion on the subject in his treatise on Mortality and Morbidity, which, unfortunately, has not been translated into English.

Considerations of the chances of survivorship in marriage, the well-established lower mortality of wives as compared with husbands, and the practical certainty of surviving children, point to life insurance as the most effective method yet devised to prevent suffering and dependence upon the charity of others. "A family," wrote Professor Sumner, some thirty years ago, "is a charge which is capable of indefinite development," and whatever may be its ultimate evolution, there can be no question but that life insurance acts as a conserving factor in human marriage and develops the altruistic impulse of the husband toward the wife and of the father toward the children. In the homely language of insurance parlance: "Wives often object to insurance, but widows never do," and I may add the glowing tribute of Gilbert Currie, one of the earlier writers on insurance, that "if we only could call from the dusty archives of these venerable institutions the huge piles of molding ledgers, and extract from their records, what tales would be unfolded of miseries prevented, griefs and sorrows soothed, the briny tear wiped from off the cheek, the balm of consolation imparted, the widow's heart made to rejoice with gladness, and the helpless orphan to sing for joy! This is no flight of the imagination, no picture of fancy, no figure of speech; it is sober reality, the voice of experience, and the simplicity of truth."

Life Insurance and Social Reform.

Of the problems of social wellbeing there are few of greater importance than the development of voluntary thrift and

resulting economic freedom of the masses. What Mill calls "self-regarding actions" and "actions which are not primarily or chiefly self-regarding" admirably illustrates the fundamental difference between insurance and mere saving habits. The hope of an earlier day has been realized, and life insurance at the outset of the twentieth century is a universal provident institution. The view prevails, as expressed by Marshall, that "at last we are setting ourselves seriously to inquire whether it is necessary that there should be any so-called lower class at all." Life insurance precludes the necessity of abject poverty and pauperism. Life insurance eliminates, for all but the lowest and most depraved, the possibility of a pauper burial. It has placed within the reach of the large majority at least a temporary barrier between death and dependence and the poor-house. We are still far from having realized all that is implied in the insurance idea and we still suffer much from an unsound social philosophy. We are constantly in danger of delusive schemes of social reform not based on individual effort and voluntary adaptation to existing economic conditions. The tendency, however, I believe, is in the right direction, and every year sees an advance toward a higher degree of social wellbeing. Social reform of the right kind must come from within; must be the result of individual character and individual struggle. This is the social aspect of insurance—that is, prudently to economize, to save, to invest, to insure for the financial protection of self and others in old age or at death. There is nothing in the annals of the poor more remarkable than the rise and progress of provident institutions, from burial clubs and friendly societies to the different varieties of life insurance adapted to every stratum of society. For wage-earners, or the industrial element of the population, industrial insurance may rightfully claim to meet the requirements of Currie of "its being such a system as the circumstances and conditions imperatively require, namely, the provision of means whereby they are enabled to help themselves and their families without depending upon the assistance of their neighbors or

compromising in the smallest degree their independence of character." I may also quote his conclusion, applicable to the conditions of today, that "every poor man is now called upon to fulfill his most sacred obligation, an obligation as binding upon the hard-working, honest man as upon the most opulent individual, parent, or husband in the world—to his wife and his helpless offspring." It is the mission, the aim, and the object of insurance, primarily and chiefly, to diminish dependence and increase by individual effort, frugality, and forethought the social and economic independence of the masses.

Insurance as a Career.

While insurance may rightfully claim recognition as a science, as a business pursuit it is still far from being a professional career. The general aspect of insurance as a career or business pursuit has been discussed in much detail by the Honorable John F. Dryden in a paper contributed to a series of articles on the subject to the New York Tribune.* Of late years insurance education has been introduced into colleges and universities, sometimes in connection with general instruction in commerce and banking, as, for illustration, in the Wharton School of Finance, University of Pennsylvania, and in the University of Wisconsin; or occasionally as an independent course of instruction, as, for illustration, at Yale. In a general way, however, it is yet too early to speak of insurance education as professional training. The general method of instruction in insurance is still of too elementary a character, the elements of success in office and field administration are too ill-defined, and the principles of business conduct are too far from being reduced to scientific uniformity to permit us to speak of insurance as a professional career.

But as a business pursuit it is deserving of the most serious consideration, and I may repeat the glowing tribute to the insurance agent by Elizur Wright that "among the honorable

* Reprinted in "Addresses and Papers on Life Insurance and Other Subjects," by John F. Dryden, Newark, N. J., 1910.

workers in the civilized world to whom the public as well as the insured will die indebted, we give faithful and successful life insurance agents a high place. It is hardly possible to believe that a life insurance agent can achieve any long continued success without bringing into action some of the noblest qualities of a sterling man, and no field that we know of is more inviting to an ambition that would devote the best of talents to the benefit of society at large and individuals in particular."

Insurance Libraries.

A pre-requisite for an effective university education is the need of comprehensive or approximately complete insurance libraries. All of the more important companies have libraries of more or less extent on insurance, statistics, and related sciences, but the three libraries deserving of special mention are the Walford collection of the Equitable Assurance Society, the Bibliothèque de l'Utrecht, and the library of the Prudential Insurance Company of America. The Prudential library of insurance and statistics includes over 25,000 volumes and pamphlets, supplemented by an extensive collection of data on every subject relating to insurance science. The Boston Insurance Society has a good library, of which a catalogue has been published. The Life Insurance Company of Utrecht has published a valuable catalogue, which has been re-issued in a fifth edition in 1903. No comprehensive bibliography of insurance exists, but Pocock, in 1840, published a small volume, which is now extremely rare, including a list of the more important works on insurance, the doctrine of chances, gambling, lotteries, etc., which had been printed up to that time. The list, however, is far from complete. Probably the most comprehensive collection of works on insurance and related subjects is the library of the Institute of Actuaries of Great Britain.

Religious Aspects of Life Insurance.

The relation of insurance science to religious agencies and religious influence, both individual and social, is implied in the

earlier discussion of the ethical sanction of insurance as a method of social amelioration. Professor Clark has well said that "certain modern religious problems need to be apprehended as well from the material as from the spiritual side," and of these life insurance has, almost from its inception, received the sanction and active encouragement of the Christian Church. The first name on the list of the incorporators of the Amicable Society for the Insurance of Lives, organized in 1705, is that of the Bishop of Oxford. The first comprehensive and practical work on life insurance theory was published in 1762 by the Rev. Richard Price, a Unitarian clergyman. Some of the earliest works on annuities and reversions developed out of considerations of the value of church leases and inquiries into the tenant rights of church and other foundations. Some of the first steps in the direction of improving the tables and premium rates of burial clubs and friendly societies were made by ministers of the Established Church, and I may mention the Rev. Mr. Becher, whose works are still valuable for instruction and reference. It has been for many years the practice in England to organize burial clubs and insurance societies of children of Sunday-schools, which, as far as I know, have served and continue to serve a useful purpose. The first two insurance organizations in the United States, one of which is still in existence, were the Presbyterian Ministers Fund, established in 1759, and the Society for Episcopal Clergymen, established in 1769. An insurance company for clergymen has been in existence in London since 1846, and among the efforts of the Salvation Army is an Industrial Insurance Department, which has made satisfactory progress.

These illustrations will suffice to show that the insurance idea has the sanction of the Church and religious approval generally, although some have held and still hold that "these institutions are conducted on a principle contrary to a trust in Providence." In answer it has properly been argued that "life insurance takes its rise in one of the most respected features of human nature—foresight, or a provision against contingent

evils; and having most particularly in view the succor of the widows and fatherless, it is essentially a moral and humane institution. Life insurance should not, therefore, be considered as an interference in any degree with the course of Providence, which some rashly assume it to be, but, on the contrary, the taking advantage of a means kindly offered by Providence for our benefit." This is the view which prevails at the present time and which gives religious as well as moral sanction to the development of life insurance as a universal provident institution.

Insurance as a Science.

As a comparatively new department of human inquiry and action, insurance found no place in the earlier classifications by Bacon, Comte, and Spencer, but no scientist of the future and certainly no economist can rightly ignore what, in time, will become a tremendous force making for the material wellbeing and the economic independence of the vast majority of civilized people in all portions of the earth. It is equally certain that the insurance manager of the future will give more and more consideration to the teachings of both the abstract and concrete sciences, with the aim to adjust the practical administration of insurance to sound scientific theory derived from extensive investigations into the vast range of related sciences. For the future conduct of the business the demand will be for trained minds, qualified to deal with problems more complex and involved than the problems and difficulties of the past. As it has well been pointed out by the Honorable John F. Dryden, in a paper on "Insurance as a Career:" "In a general way it may be said that the scientific temperament is most likely to lead to success in home office administration, for scientific training, as well as all higher education, distinctly qualifies a man for administrative responsibility."

Insurance is today the foremost social institution of civilized countries. The business has assumed enormous proportions, and the tendency of the "insurance idea" is toward an

ever-increasing area of general usefulness. To both the individual and the state, insurance is today an indispensable method and means for the maintenance of our standard of social security and progress. In the struggle of the masses for economic freedom and a more equitable distribution of wealth, insurance aids and sustains all other forces making for this much-to-be-desired end. Insurance in its final analysis is simply a business method to make the world a better place to live in, than which no aim or purpose could be higher or more worthy.

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CHAPTER II

INSURANCE ECONOMICS.

The place of insurance in economics has never been clearly and finally determined by recognized authorities on the subject. By far the most ambitious attempt in this field of research is the valuable monograph by Allan H. Willett, but this author considered the subject almost entirely from the theoretical point of view, with only slight regard to the actual practice of insurance in everyday life. The importance of insurance as an element of commerce and its far reaching influence on national and international commercial development would alone be sufficient to establish the necessity for a qualified inquiry to determine the place of insurance in economic science. The important relation, however, in which all forms of insurance stand to social progress at large requires that this branch of science should receive more attention from trained economists in the future than has been the case in the past. Evidently insurance is an important factor in production, for the cost of producing goods for sale must be materially diminished by insurance through the distribution of risks since the cost would necessarily be greater if the whole risk had to be assumed by the producer. It is equally evident that insurance is an important factor in distribution because the cost of transportation must be less where the risk of loss or destruction is distributed through insurance than where the whole risk has to be assumed by either the shipper or the agency engaged in transportation. It is very difficult indeed to conceive of commerce being carried on without insurance and the present high degree of security in practically all commercial transactions is, to a considerable extent, the result of the distribution of risks through insurance.

Commercial credit itself is very largely based upon insurance, without which there would be no security for full or partial recovery in the event of total or partial loss through fire, shipwreck, or other destructive agencies. Credit insurance as such has become an important branch of trade and the whole system of loans and advances on goods in storage, or in course of transportation, would be impossible were it not for the protection granted by policies of insurance.

What is true of production and distribution is also true of consumption, and the final price of every article in commerce is more or less governed by insurance even though the true incidence of the insurance premium in the price of a multitude of articles can not be traced with absolute certainty on account of the minute fraction of the cost involved. By aggregating insurance premiums, however, an enormous amount of extra commercial security is created which is nothing more nor less than the complete assumption of commercial risks in all its phases, and from every point of view, through the modern institution of insurance corporations. There is, thus, some evidence, at least available to prove that insurance is more or less a factor in the three main branches of economics—that is, production, distribution and consumption, but as yet no trained economist has concerned himself with the actual facts of insurance experience to trace this element with scientific accuracy through all the ramifications of economic science.

It is, however, a distinctly helpful sign of an awakening economic interest in this important question that so high an authority on economic subjects as Mr. J. A. Hobson should have included insurance in a separate chapter in his recently published treatise on the Industrial System, being an inquiry into earned and unearned incomes from a modern point of view and with a due regard to modern conditions of life. Equally extended and qualified consideration has been given to insurance by Prof. Irving Fisher in his treatise on The Nature of Capital and Income, published a few years previous to the work of Hobson, and both of these contributions may be said to

mark, in outline at least, the probable trend of future thought in formulating more definite conceptions of the place of insurance in economic science.

Discussion of Insurance in the Wealth of Nations.

From the time when Adam Smith published his Wealth of Nations, insurance has been referred to by economic writers and some of these references are of historic interest if not of particular value in present-day discussions of this important subject. At the outset of every discussion of insurance it is of importance to clearly realize the fundamental difference between insurance and gambling, a distinction which, unfortunately, is often lost sight of even by otherwise qualified writers on the subject. Gambling, as emphasized in the discussion on lotteries by Adam Smith, is never a complete distribution of risk, for as he observes, "There is not, however, a more certain proposition in mathematics, than that the more tickets you adventure upon, the more likely you are to be a loser," for, he continues, "Adventure upon all the tickets in the lottery, and you lose for certain; and the greater the number of your tickets, the nearer you approach to this certainty." This is the fundamental antithesis to insurance, which distributes an existing risk with a fair degree of approximation to the interests of each risk-taker, who in return for a small premium secures complete or partial compensation for loss. Smith, in his discussion of wages and profits, remarks, "That the chance of loss is frequently undervalued, and scarce ever valued more than it is worth, we may learn from the very moderate profit of insurers." This sentence brings forcibly to our attention the principle of adverse selection in insurance, whereby only those as a rule insure who feel that they have a substantial risk at stake. As in the words of Smith, "In order to make insurance, either from fire or sea-risk, a trade at all, the common premium must be sufficient to compensate the common losses, to pay the expense of management, and to afford such a profit as might have been drawn from an equal capital employed in

any common trade. The person who pays no more than this, evidently pays no more than the real value of the risk, or the lowest price at which he can reasonably expect to insure it." When this was written in 1776 the whole practice of insurance was necessarily very much more arbitrary, indefinite and uncertain than at the present time.

During the intervening long period of years an immense amount of experience has been had and really conclusive statistical data have been secured which afford a better basis for the calculation of premium rates and a more certain profit to those who undertake the assumption of risk; but in the time of Adam Smith it could very properly be said that, "though many people have made a little money by insurance, very few have made a great fortune; and, from this consideration alone, it seems evident enough that the ordinary balance of profit and loss is not more advantageous in this than in other common trades, by which so many people make fortunes." Smith was entirely correct in placing insurance, at least at this period of time, on a perfect equality with other commercial undertakings for gain, and this position insurance has practically retained in all the commercial codes of European nations of ancient and modern times. As emphasizing the strictly commercial aspects of insurance as a trade, Smith observed that, "Moderate, however, as the premium of insurance commonly is, many people despise the risk too much to care to pay it. Taking the whole kingdom at an average, nineteen houses in twenty, or rather, perhaps, ninety-nine in a hundred, are not insured from fire. Sea-risk is more alarming to the greater part of people; and the proportion of ships insured to those not insured is much greater. Many sail, however, at all seasons, and even in time of war, without any insurance."

The Problem of Self-Insurance.

Smith then considered the question of self-insurance, which of course is possible in the case of very large commercial undertakings, where the operations are on a sufficient scale

to become subject to a law of average or the law of large numbers. The conclusion advanced by Smith is favorable to the self-assumption of risk, if such it may properly be called, and in his own words, "When a great company, or even a great merchant, has twenty or thirty ships at sea, they may, as it were, insure one another. The premium saved up on them all may more than compensate such losses as they are likely to meet with in the common course of chances. The neglect of insurance upon shipping, however, in the same manner as upon houses, is, in most cases, the effect of no such nice calculation, but of mere thoughtless rashness, and presumptuous contempt of the risk." (Wealth of Nations, Book I, Ch. X.)

To the average man of business it must necessarily be next to impossible to arrive at more than an approximate estimate of the risk which he incurs without insurance. He is necessarily guided by past experience and personal observation of the disastrous consequences resulting from contempt of risk and indifference to insurance protection. With increasing average intelligence such a common contempt of commercial risk necessarily tends to disappear, and today the insurance of goods in commerce is practically universal and a duty imposed upon merchants and traders by the customs and laws of trade.

Insurance as a Branch of Commercial Enterprise.

Considering insurance by itself as a commercial institution and on an equality with commercial enterprises generally, it is suggestive to find in the Wealth of Nations a brief consideration of this point of view. Adam Smith, in discussing the rise and fall of commercial enterprises, which had or had not exclusive privileges in the nature of a monopoly ostensibly for the purpose of extending to them an extraordinary degree of security, remarks that, "The only trades which it seems possible for a joint-stock company to carry on successfully, without an exclusive privilege, are those, of which all

the operations are capable of being reduced to what is called a routine, or to such a uniformity of method as admits of little or no variation. Of this kind is, first, the banking trade; secondly, the trade of insurance from fire and from sea-risk, and capture in time of war; thirdly, the trade of making and maintaining a navigable cut or canal; and, fourthly, the similar trade of bringing water for the supply of a great city." It does not fall within the present discussion to examine into the soundness of this theory, for manifestly most other commercial enterprises carried on in the form of partnerships can safely be so carried on without the right or privilege of monopoly. The chief importance of the sentence is the sense in which the term "trade of insurance" is used in identically the same manner as the trade of banking, with the functions and purposes of which insurance has naturally much in common. Smith remarks, however, with reference to insurance undertakings, that, "The value of the risk, either from fire, or from loss by sea, or by capture, though it can not, perhaps, be calculated very exactly, admits, however, of such a gross estimation, as renders it, in some degree, reducible to strict rule and method. The trade of insurance, therefore, may be carried on successfully by a joint-stock company, without any exclusive privilege." The advantages of insurance to society and government are summarized by Adam Smith in the following suggestive sentence: "The trade of insurance gives great security to the fortunes of private people, and, by dividing among a great many that loss which would ruin an individual, makes it fall light and easy upon the whole society. In order to give this security, however, it is necessary that the insurers should have a large capital. Before the establishment of the two joint-stock companies for insurance in London (the London Assurance and the Royal Exchange Assurance), a list, it is said, was laid before the attorney-general, of 150 private insurers, who had failed in the course of a few years." (Smith's Wealth of Nations, Book V, Ch. I.)

The Early Practice of Individual Underwriting.

The last reference is to the practice of individual underwriting, which has never gained a strong foothold in this country. It was only in use to a limited extent during the colonial period. It is true, however, that through the gradual perfection of Lloyds a unique method of individual underwriting has been established in England, which for all practical purposes is probably as sound and secure as corporate underwriting, but the practice of Lloyds is limited largely to marine insurance, which in its nature differs quite essentially from insurance against fire and the contingencies of human life. The assumption of exceptional risks which are more or less in the nature of gambling ventures, by small groups of underwriters at Lloyds, does not fall within the corporate practice of Lloyds, but they are private undertakings in much the same manner as private deals may be conducted by members of an established stock exchange, including transactions which would not be recognized by the exchange itself.

Discussion of Insurance by John Stuart Mill.

From Adam Smith (1776) to John Stuart Mill (1848) insurance is only incidentally referred to by writers on political economy. The significance of insurance as an element of economics escaped the attention of writers who gave concern primarily to the purely technical aspects of economic science. Mill himself refers to insurance very briefly as one of the sources of profit, which he considers are resolved into interest, insurance, and wages of superintendence. It appears to have escaped the attention of Mill that interest itself is but a form of insurance, or at least that portion of the rate which exceeds the lowest return paid on government securities of unquestionably the highest intrinsic value. Interest, in a measure, is but another term for compensation for risk, while insurance is essentially the equivalent for risk assumption in merchant adventure

or commercial and individual enterprises of all kinds. The remuneration of capital in different undertakings at a comparatively high rate of interest is not essentially different in its nature from the assumption of risk in merchant adventure guaranteed against loss by policies of insurance. Mill observes that, "The profits, for example, of retail trade, in proportion to the capital employed, exceed those of wholesale dealers or manufacturers, for this reason among others, that there is less consideration attached to the employment. The greatest, however, of these differences, is that caused by difference of risk." He then continues, "The profits of a gunpowder manufacturer must be considerably greater than the average, to make up for the peculiar risks to which he and his property are constantly exposed. When, however, as in the case of marine adventure, the peculiar risks are capable of being, and commonly are, commuted for a fixed payment, the premium of insurance takes its regular place among the charges of production, and the compensation which the owner of the ship or cargo receives for that payment, does not appear in the estimate of his profits, but is included in the replacement of his capital." (Principles of Political Economy, 5th edition, vol. I, p. 500.)

It is evident from the foregoing that if Mill had carried his argument further he could not have failed to come to the conclusion that insurance is an element of commerce or commercial enterprise, certainly to the extent that it materially affects the cost of production, which would unquestionably be greater in many branches of industry if the undertaking had to be carried on without the protection of a policy of insurance.

Robert Ellis Thompson, who wrote a treatise on Political Economy, published in Philadelphia in 1875, and a revised edition in 1882, included insurance in a brief consideration of commercial credits, observing in part that where a seller has to grant credit he cannot afford to sell goods at as low a figure as if he were paid in cash, but that in fact prices vary according to the length of the credit, and that the difference in price is greater than the difference in the amount of loss resulting

from the discount of commercial paper. He observes that the creditor "has to insure himself against bad debts by an increase of his profits on all transactions. He must charge more to good customers in order to insure himself against bad ones." This sentence would seem to sustain the theory of Mill that insurance is an element of profit and by inference an element in the cost of production.

Viewpoint of a German Economist.

The first extended consideration of the place of insurance in political economy was brought to the attention of English readers by the translation of Roscher's Principles of Political Economy, by Mr. John J. Lalor, published in 1878. The first German edition, however, had been published in 1854. Roscher included insurance in his consideration of the elements of consumption, dividing his subject into mutual and speculative institutions, a brief discussion of the economic advantages of insur ance, and the requisites of a good system of fire insurance. It requires no extended knowledge of the subject to make it clear that this discussion was entirely inadequate and that it proceeded from a superficial appreciation of the service rendered by insurance to every important branch of trade and industry as well as its relation to the social welfare of the peoples of civilized nations. Many of his observations, made at a period when insurance was practically in its beginnings, are no longer applicable to modern conditions, as among others, his statement that, "to the poorest class of those who need insurance, private insurance will perhaps be never properly accessible." More recent experience has successfully demonstrated that for certain important ends even the poor, by small deductions from their income, can provide by insurance for what custom has sanctioned as the most necessary expenses incident to burial and funeral observances. It is true that the progress of insurance has been less successful in the case of fire insurance, but even in this direction a substantial advance has been made and with the increasing security of dwellings against fire the

absolute necessity for such protection perhaps no longer exists. Roscher, among other interesting observations, however, defined precisely the fundamental principle of all insurance in the words that, "the aggregate danger is less than the sum of individual dangers for the reason that it is more certain, and that the uncertainty, of itself, is an element of danger." While leaning strongly toward government insurance, at least in the case of fire institutions, he observes that, "the idea sometimes suggested in our day of making the system of insurance a government prerogative, arises as much from the passion for centralization as from socialistic tendencies." As partly in answer to this suggestion he quoted from Spittler's Politics the objection to insurance "that it diminishes benevolence and approximates to communism, thus hitting the dark side of all very high civilization." The German system of communal fire insurance always has been limited to houses, partly for the purpose of protecting the lender of money on mortgages against substantial loss. The function of government insurance has never extended to movable property—that is, furniture, etc.—and Roscher observes that, "the thought of making this species of insurance compulsory, or of turning it over to the State, has seldom been suggested." Aside from these considerations of insurance in its political and social, rather than in its strictly economic aspects, the observations of Roscher have no practical value to the students of economics at the present time.

Insurance as a Factor in Distribution.

Contrary to the theory of Mill, of including insurance and interest as elements of profit, Prof. Francis A. Walker considered interest as an element of distribution, distinguishing precisely between true interest, or the lowest rate of return on money lent upon absolute security, and the higher rate of interest charged on account of extra risk incurred. In the words of Walker, "A great deal that is paid under the name of interest is not interest in the true sense, but is merely a premium for the insurance of the principal sum lent. Real interest

only comprises that part of the payment made which would be paid, were the return of the principal, at the date of the maturity of the obligation, a matter of reasonable certainty. Absolute assurance can be reached in no human transaction; but where the risk is so small that it amounts to nothing in the mind of the lender, as in the case of British consols, or of a "bottom mortgage," where the sum lent is only a half or a third of the value of improved real estate, we have an instance of real interest, pure and simple." In continuation, however, he observes that, " Whatever, in the same market, at the same time, is paid above this, for the use of capital, is of the nature of insurance against the risk of losing the amount lent." And he observes further, with particular reference to extra-hazardous risks and losses in speculative undertakings, in which more than double the normal rate of interest is usually paid, that " With investments or temporary loans inside this limit, a different rule obtains. The rates of interest paid are still graded with little real appreciation of the degrees of risk taken; the sums obtained as insurance cannot be assumed to be proportioned to the hazard; yet it is generally possible for an investor or lender to say, this is more safe than that: the adverse chances here are few and small; are many and great there." Walker illustrates this principle by a concrete example of an investment by the same person on the same day, who purchases government bonds paying four per cent., railway shares paying six per cent., and loans on personal security a like amount, paying ten per cent. He remarks that the three portions of capital lent or invested exhibited no economic differences, and that the phenomenon noted—that is, the differential rate of interest paid—is due in part to the insurance of the principal sum lent. Of course, insurance in this sense is widely different from insurance in actual commercial practice, but in essence the function is the same in that the risk is distributed approximately in proportion to the degree of hazard incurred. By such distribution the hazard itself is partly eliminated and mercantile adventure is made possible; or, in

other words, risk assumption is made comparatively safe in the equalization of losses which are likely to occur with a reasonable degree of certainty in conformity to the past experience of mankind.

Insurance in Social Economics.

In social economics insurance pre-eminently signifies financial security of the family or other social relations. From the strictly utilitarian point of view insurance is a decidedly effective aid in the promotion of general happiness. Writers of the utilitarian school appear to have generally neglected insurance as a factor demanding serious consideration, and the theory of human happiness conditioned on the gratification of human wants and desires is practically independent of insurance as contributing toward this end. One of the few modern writers on utilitarianism, Mr. Michael Macmillan, has, however, given a brief consideration to the subject in his treatise on "The Promotion of General Happiness," observing that, "what remains to be done is to encourage the practice of insurance in its more readily recognized forms. Either the Nation as a whole, or individuals, must be taught to provide funds of savings for their support in times of scarcity." Life insurance, by its very nature enforces abstinence by the periodical payments required to be made, and provides more effectively than any other method of savings or investment for periods of want, scarcity and distress. The view held by Macmillan with reference to the utilitarian function of life insurance is of particular interest and in part explained as follows:

"Vegetarians and total abstainers may also be defended against the effect of misfortune by life assurance—an arrangement by which wives and children are defended against destitution, in the case of the early death of a husband and father, and by which people generally can protect themselves and their families, to a certain extent, against heavy loss from illness and accidents. It may be described in sporting phrase as a kind of hedging against extreme misfortune by an agreement between a certain number of persons, namely, those who take policies in the same office, that those who are fortunate shall

give support to those who are unfortunate. This insurance tends to equalize the lot of all insurers. Those who die young, or incur the particular misfortunes insured against, gain by insurance, while those who live long, and do not suffer from the illness or accidents, or other misfortune, against which they insured themselves, are pecuniarily losers; for, if they had invested their money in other investments, they would probably have been richer. This system has, without doubt, when applied in its natural and most common way, considerably alleviated the misery of mankind."

The Equalization and Distribution of Wealth by Insurance.

Insurance makes peculiarly for equality in the distribution of wealth, and to this extent as much as, if not more than, any other element of social and economic progress, makes for the promotion of happiness. Macmillan remarks with reference to this particular point that:

"The difference between the misery of uninsured orphans, widows, and men incapacitated for work, or attacked by sudden misfortune, and the less misery which they would suffer if protected by insurance, is greater than the loss of happiness owing to waste of wealth incurred by those who have insured against misfortune, and been long-lived and fortunate. Further, there must be taken into account the peace of mind of the man who has been prudent enough to insure himself against misfortune, as compared with the anxiety about the future in the heart of the man who has not insured himself, and those dearest to him, against sudden and overwhelming calamity. Thus, there are two great advantages secured by insurance. On the other side, it may be said, that insured persons will be less careful to avoid danger. This is true, but only to a very limited extent, and, in some occupations, it is a duty to face danger boldly, so that, in some cases, insurance helps men to do their duty well."

Social Progress and General Happiness.

The risk to life and health involved in certain occupations can, without difficulty, be conceived as a detriment to social and economic progress unless balanced by insurance protection

against extraordinary losses. Human life has a well-defined financial value, the equivalent of which is measured by the rate of insurance, which varies according to the risk incurred in the pursuit of dangerous trades. Many such trades would not be as readily followed were it not for the insurance protection secured in return for the payment of a slight additional premium. Many commercial risks would in a similar manner be avoided were it not for the security against exceptional losses secured by insurance. It is not difficult, of course, to conceive of disadvantages resulting from insurance, and among other plausible arguments against life insurance in particular, Macmillan mentions the encouragement of marriage and the resulting increase in over-population. He remarks with reference to this point, that:

"There is indeed, no doubt that young men, who would otherwise have remained single, are enabled to marry by the possibility of insuring their lives and so defending their families against destitution in the event of their early death. But this is no evil, but rather a defence against a great danger. The reckless marriages of the improvident have long threatened to drive prudence out of the world by causing a large portion of each new generation to be children inheriting improvidence from improvident parents. Whatever encourages the prudent to marry must surely have a beneficial effect on the future of the human race. So, after considering possible objections, we may come to the conclusion, that the institution of insurance has promoted the happiness of the world, and that the practice should be encouraged by utilitarians, especially among nations of vegetarians and total abstainers."

While the foregoing remarks apply to sociology, rather than to economics, they are a significant addition to the very fragmentary consideration which insurance has received from qualified writers on the subject of social economics. They confirm the consensus of opinion of the people of civilized nations, that without insurance the social and economic progress of the time could not have been achieved, and that the security resulting from the practice of insurance in every branch of trade as well as in the more delicate affairs of domestic life,

is equivalent to the attainment of a distinct and most effective form of practical humanitarianism.

Insurance as a Factor in Business.

The economic aspects of insurance as a factor in modern business enterprise, or the relation in which insurance against the risks of a business stands to the supply price of any particular commodity produced, were first considered by Marshall in his, "Principles of Economics," the first edition of which was published in 1890, written with a limited knowledge of the almost infinite possibilities of utilizing the principle of insurance in the numerous and widely varying conditions of business, Marshall held the opinion that insurance could not be effected at moderate rates against all business risks, observing that:

" The manufacturer and the trader commonly insure against injury by fire and loss at sea; and the premiums which they pay are among the general expenses, a share of which has to be added to the prime cost in order to determine the total cost of their goods. But no insurance can be effected against the great majority of business risks."

There can be no question of doubt that many of the minor risks of business can be conveniently covered by insurance, but the modern development of many branches of insurance entirely unknown in the past, proves the possibilities of further specialization, which may enable the merchant to insure against losses which are now unprovided for. Marshall remarks, with reference to this point:

" Even as regards losses by fire and sea, insurance companies have to allow for possible carelessness and fraud; and must therefore, independently of all allowances for their own expenses and profits, charge premiums considerably higher than the true equivalent of the risks run by the buildings or the ships of those who manage their affairs well. The injury done by fire or sea, however, is likely, if it occurs at all, to be so very great that it is generally worth while to pay this extra charge; partly for special trade reasons, but chiefly because the total utility of wealth increases less than in proportion to its amount. But the greater part of business risks are so inseparably con-

nected with the general management of the business that an insurance company which undertook them would really make itself responsible for the business; and in consequence every firm has to act as its own insurance office with regard to them. The charges to which it is put under this head are part of its general expenses, and a share of them has to be added to the prime cost of each of its products."

Loss Prevention and Insurance.

Many of the risks of business which Marshall must have had in mind when writing the preceding paragraph are not convertible into exact monetary equivalents, resulting, as he points out, from mismanagement, for which, of course, an insurance company can probably never assume entire responsibility. Nor would it be advisable that it should do so since such insurance might put a premium upon incapacity and negligence, which under given conditions might be decidedly detrimental to the general welfare and contrary to public policy. It is equally difficult to differentiate a theory of pure insurance against loss or uncertainty from insurance devices which really provide effective safeguards or preventive measures tending, more or less successfully, to the entire elimination of loss. This is particularly well illustrated in the case of steam boiler insurance, where most of the premium income is expended not in the payment of losses, but in expenditures for effective inspections. A similar result has followed the well known system of mutual fire insurance of Massachusetts cotton mills, which secure insurance protection at less than the ordinary rates on condition that proper sprinkling and other devices are employed, together with conformity to advanced methods of building construction. It is an open question, however, whether it is correct to consider the cost of such preventive devices as an insurance premium in the sense that it is a contribution toward the equalization of losses.

Economics of Self-Insurance.

Equally difficult of exact definition is the economic function of self-insurance—that is, where the risk of property

destruction is assumed by large owners or combinations of capital with a sufficiently large exposure of risk to secure practically the same results as would be experienced in the case of a small insurance company. Marshall refers to cases of this kind as follows:

"In some cases insurance against risk is apt to be left out of account, altogether, in others it is apt to be counted twice over. Thus a large shipowner sometimes declines to insure his ships with the underwriters; and sets aside part at least of the premiums that he might have paid to them, to build up an insurance fund of his own. But he must still, when calculating the total cost of working a ship, add to its prime cost a charge on account of insurance. And he must do the same thing, in some form or other, with regard to those risks against which he could not buy an insurance policy on reasonable terms even if he wanted to. At times, for instance, some of his ships will be idle in port, or will earn only nominal freights; and to make his business remunerative in the long run he must, in some form or other, charge his successful voyages with an insurance premium to make up for his losses on those which are unsuccessful."

Insurance Expense in Business Accounts.

In all such problems as these the insurance function is apt to be more or less obscure, and its proper apportionment as a contribution to risk assumption or loss equalization is very difficult. Marshall cautions against overlooking certain insurance expenses of this kind, more or less properly so defined and he warns against others being considered twice in mercantile accounting, observing that:

"In general, however, he does this, not making a formal entry in his accounts under a separate head, but by the simple plan of taking the average of successful and unsuccessful voyages together; and when that has once been done, insurance against these risks cannot be entered as a separate item in cost of production, without counting the same thing twice over. Having decided to run these risks himself, he is likely to spend a little more than the average of his competitors, in providing against their occurrence; and this extra expense enters in the ordinary way into his balance-sheet. It is really an insurance premium

in another form; and therefore he must not count insurance against this part of the risk separately, for then he would be counting it twice over."

The involved nature of calculations of this kind is best made evident by concrete illustrations derived from actual experience. In all such cases the insurance premium is always an element of ultimate cost to the consumer, although it serves the useful function of reducing cost by a clearly traceable reduction in risk, which would otherwise constitute a hazard requiring to be made good by an increase in price. Proper safety precautions, particularly effective methods of fire prevention, will, other things equal, result in a lower rate of insurance and to this extent lower the ultimate price of goods to the consumer; or to the extent of the saving effected increase the profits of the manufacturer or merchant. As illustrated by Marshall:

"When a manufacturer has taken the average of his sales of dress materials over a long time, and bases his future action on the results of his past experience, he has already allowed for the risk that the machinery will be depreciated by new inventions rendering it nearly obsolete, and for the risk that his goods will be depreciated by changes in fashion. If he were to allow separately for insurance against these risks, he would be counting the same thing twice over."

Insurance as an Element in the Cost of Production.

In economics insurance against risk may, in other words, be provided for by preventive measures, by increased caution, intelligence and experience, as well as by the direct payment of a premium to the insurance company assuming certain responsibility for certain well defined classes of risk. In all cases insurance is an element in the cost of production, and the cost must be diminished in proportion as uncertainty is reduced to a minimum. Trades which partake of the nature of adventure are more in need of insurance, particularly when the adventure is that of a sea voyage to distant ports, than normal commercial undertakings in the manufacture or sale of staple products, but

in each case insurance in any one or more of its various forms will prove a decided advantage and tend to establish an equilibrium in trade relations. Commercial credit itself would be a totally different matter were it not for insurance covering the value of the goods against destruction by fire, the terrors of the sea or theft, etc., as the case may be. Commercial credit without insurance would result in decidedly higher rates of interest to be paid on commercial paper, and in exact proportion the ultimate cost of goods to the consumer would be increased.

The Place of Insurance in Economic Theory.

It must be evident from the foregoing that the theory of risk and insurance requires to be elaborated more fully by qualified minds before it can be applied in its entirety to the solution of social and economic problems. Political economy itself is as yet very far from having attained to the position of a science and most of its maxims and definitions are matters of doubt, speculation, and dispute. One of the most hopeful indications of gradual perfection in economic theory is the painstaking work of Mr. Henry Dunning Macleod, who for forty years has contributed a number of very important works on the theory of credit and the elements of economics, in which he has given some consideration to insurance. No writer has more precisely defined the almost neglected field of incorporeal property, or what for want of a better term is defined by him as negative economic quantities. His definition is illustrated by the explanation that "every sum of money is equivalent not only to a certain quantity of material commodities or labor, but also to *the sum of the present values of an indefinite series of future payments, or to an Annuity.*" An annuity he defines as "the right to demand and receive a series of payments," and he remarks that "the lowest form of an annuity is the right to receive one future payment, such as a banknote or a bill of exchange." Conversely, "the highest form of an annuity is to receive a series of future payments for ever, such as an estate

in land or the funds; an annuity to receive a series of payments intermediate between these extreme terms is called a terminable annuity." Applying this theory to his definition of positive and negative signs to property, and of denoting "the right to property in things which have already come into possession as positive, and the right or property to things which will only come into possession at some future time as negative," he concludes that "many species of property are of a mixed nature; that is, the entire property in them consists partly of corporeal property and partly of incorporeal property." Holding that property in land is the highest of all forms of property, Macleod concludes that the purchase of an estate in land is simply the purchase of a perpetual annuity; and further, that every sum of money is not only equal in value to a certain quantity of material goods, or to a certain quantity of services, but also to a perpetual annuity, and that hence "an annuity, or the right to receive a series of future payments, is an economic quantity which may be bought and sold or exchanged, or whose value may be measured in money like any material chattel." It is difficult to give any clearness to this rather involved doctrine separate from the extensive discussion of the fundamental precepts and axioms which underlie the whole economic theory of Macleod; but the conclusions are of much practical significance when applied particularly to the legal doctrine that insurance is not an element of commerce, nor an instrumentality thereof. Upon the basis of Macleod's definition of an annuity he is justified in holding that such an annuity may be paid to secure a certain sum of money at a given time, or on a given contingency such as a life or fire insurance. and that the whole field of economics comprehends in its final analysis the three great departments of, first, material things; second, personal qualities both in the form of labor and credit; and third, annuities. Writers of the older school of economists have failed to realize the extreme significance of the last, although in the words of Macleod, it is indeed the most extensive branch of economics at the present day.

Negative Economic Quantities.

In other words, according to this writer, who more than any other has apparently given concern to the abstract theory of insurance and risk as elements of economics, "all annuities, or rights to receive a series of future payments, whether the right be to receive a single future payment, or a limited, or an infinite number of them, are negative economic quantities," and "these negative economic quantities comprehend all mercantile and banking credit, such as bank-notes, cheques, bills of exchange, and all instruments of credit; exchequer bills, navy bills, dividend warrants, etc.; the land, the funds, terminable annuities, shares in commercial companies, the good will of a business, a professional practice, copyrights, patents, tolls, ferries, market rights, advowsons, benefices, shootings, fisheries, leaseholds, policies of insurance of different kinds, and many other valuable rights, amounting in value to scores of thousands of millions in this country, of which there is scarcely any notice in the common text-books on economics." He very truly observed that by introducing this class of incorporeal property he has doubled the field of economics, and in all probability he has very much more than doubled it, considering the enormous extent to which commercial negotiable instruments of all kinds are utilized in the commercial activity of the present day.

Insurance as an Economic Function in Modern Life.

The science of economics in the larger sense comprehends more than a mere science of wealth or the three essential functions of production, distribution and consumption. Prof. Hadley in his treatise on Economics includes competition, speculation, investments of capital, combination of capital, money, credit, profits, co-operation, protective legislation, etc. All these are more or less affected by insurance, or they re-act, favorably or otherwise, upon the development and growth of insurance institutions. Hadley first considers insurance in an extended discussion of economic responsibility, with special reference to methods and means tending toward a deliberate reduction in

the burdens of pauperism. Commenting upon the German compulsory insurance system, which had then but a little more than a decade of actual experience, Hadley remarks:

"There are many reformers who are anxious that other countries should follow the example of Germany. But the experiment has not progressed far enough to pass judgment on its success. In many respects the gain to the public from a system of this kind is more apparent than real. The payments to the insurance funds must chiefly, if not wholly, come out of wages. Even though they be nominally levied on the employer, he is compelled by competition with other employers who are not subject to this levy to reduce in corresponding degree the wages which he pays."

Observations on Compulsory and Voluntary Insurance.

Contrasting compulsory insurance with voluntary insurance, as particularly emphasized in the friendly societies of England, Hadley remarks that these are in their nature agencies for the promotion of voluntary saving as a means of mutual insurance. He therefore concludes that, "If the government uses compulsory saving as a means to the same end, it takes away the ground for the existence of these societies and substitutes a system which secures the same material results to the workman but fails to secure the same educational and moral ones. To those who regard these educational and moral results as a chief advantage in voluntary saving, the change to a compulsory system looks like a step backward." The foregoing emphasizes once more the social aspects of economic questions. Mere political expediency may, of course, give its hearty approval to governmental schemes aiming to secure at once by compulsion what the gradual evolution of social morality would bring about in due course of time. Hadley has admirably summed up the objections to compulsory thrift in any form in the following sentences, which afford a much more concise and better explanation than could any words of mine:

"Finally, there is a danger that the apparent advantages of an insurance system of this kind may blind public opinion to the

more real advantages of better forms of insurance. A certain section of the public is so dazzled by the prospect of pensions that it overlooks the true ground on which pensions are justified. It comes to regard the pension as an end in itself rather than as a means of relieving the general funds of the government of a burden. . . . . There are certain things which society must do in justice to itself, which it cannot safely allow individuals to demand in justice to themselves. If you give every man a right to a pension when he is incapable of self-support, you tacitly approve his failure to provide for himself and his children. . . . We need measures which shall increase individual responsibility rather than diminish it; measures which shall give us more self-reliance and less reliance on society as a whole. We cannot afford to countenance a system of morals or law which justifies the individual in looking to the community rather than to himself for support in age or infirmity."

Economic Aspects of Speculation.

Aside from these considerations of insurance in its relation to economic responsibility, Hadley includes a brief reference to insurance in his discussion of the economic aspects of speculation. Distinguishing clearly at the outset insurance from gambling, and holding that the motives and effects in the two are wholly different, he points out:

"The man who wins in betting on horses secures an addition to his income which means increased luxury; the man who has insured a house that burns down prevents the distress to his family consequent upon the loss of a home. In like manner, the man who has insured his life makes small annual payments at a time when he can do so without encroaching on the comfort of his family; thereby assuring to that family, in the event of his death, a payment of money at a time when the loss of the earning power of its head might otherwise mean want and destitution. Insurance puts money where it is needed, instead of putting it where it is not needed; where it has the highest utility to the individual and to society, instead of the lowest; where the possibility of securing it, instead of being a means of demoralizing excitement, becomes a source of security and of industrial efficiency. Hence the insurance company in protecting the individual insurer against losses to himself and his family from fire, accident, or death, is rendering a public

service; and the profits of such a company, unlike those of the bookmaker or the lottery, are honestly earned by an actual contribution to the public wealth."

The economic function of insurance is admirably defined in the preceding quotation, emphasizing the high degree of utility inherent in the method as a device making for social and economic security. As concrete illustrations, Hadley refers to manufacturers' mutual insurance companies, which by seeking to reduce losses by avoiding all preventable causes of fire, have succeeded to an astonishing degree, while associations for boiler inspections have been far more successful in the exercise of their vigilance than could possibly be expected from public officials.

Insurance and Gambling Contrasted.

More recent writers on economics have given equally extended consideration to insurance, with special reference to its practical utility as an aid in the solution of economic questions. Prof. Frank A. Fetter, writing in 1904, contrasts insurance with gambling and speculative profits, calling particular attention to the element of chance inherent in all individual enterprise. He remarks:

"A general average of chances in different lines of business causes some to be called safe, others extra-hazardous. The chance is averaged and added to the profit or gain of that industry, for an extra-hazardous industry must in general afford a higher average of profit in order to induce men to engage in it. It is folly to take a risk without ascertaining its degree, so far as general experience enables one to choose. But inasmuch and in as far as the gains and losses fall unequally upon different individuals, income depends on chance." (The Principles of Economics, p. 334)

From this point of view he defines gambling as a transfer of wealth on the outcome of events absolutely unpredictable, which, of course, is the very antithesis to the practice of insurance. It is true, of course, that legitimate forms of chance in risk taking, according to Fetter, shade off into illegitimate forms of gambling, but it is an error to insist upon the gambling

aspects of insurance undertakings, since the sole object of insurance is the equalizing and eliminating of the element of chance in human affairs. Fetter observes very properly with reference to this important point, after a brief consideration of the decidedly more hazardous form of insurance underwriting in the middle ages, that:

"Gradually there came about a specialization of risk-taking by the men most able to bear it. They could tell by experience about what was the degree of uncertainty, and could lay their wagers accordingly. When several insurers were in the same business, competition forced them to insure the vessel and cargo of the ordinary trader for something near the percentage of risk involved. The insurance thus tended to become a mutual protection to the ship-owners; what had to be paid in premiums to cover risk came to be counted as part of the cost of carrying on that business."

To the foregoing he adds that modern insurance is mutual in nearly every case, and that the total premiums equal the total losses plus operating expenses, the interest on the reserve of premiums counting as part of the premium. He, therefore, concludes:

"Each one gets protection for the loss of his property in return for the payment of a sum that will cover the losses on others' property. Such an exchange is a profitable one. The premium comes from marginal income; the loss of house or property would fall upon the parts of income having higher marginal utility. The less urgent wants of the present are sacrificed in order to protect the income that gratifies the more urgent wants of the future. In insurance each party gives a smaller utility for a greater; each has a margin of advantage; while the greater certainty in business stimulates effort and rewards it. This is quite the opposite of the working of betting and gambling."

Relation of Insurance to Money, Credit, Trade and Transportation.

In 1905, Prof. Edwin R. A. Seligman published a treatise on the "Principles of Economics," with special reference to

American conditions, in which he defines among others the structure and process of economic life. In his consideration of value and exchange—that is, money, credit, international trade, and transportation—he properly includes insurance, with a brief discussion of its nature, growth, theory, and methods of public regulation. He defines insurance as a device to remove the economic consequences of uncertainty, and remarks that, "the risk with which economic activity commonly concerns itself is the degree of uncertainty rather than the degree of probability." He follows this definition with the conclusion that," The need of protection against risk grows, therefore, with the degree of uncertainty which in economic actions increases as probability increases." Uncertainty, he points out, is clearly a disadvantage, which every prudent man desires as far as possible to eliminate, and this can be accomplished in three ways—first, by avoidance; second, by prevention; and third, by assumption of risk. The entire risk, of course, may be assumed, but it is possible to reduce it by combining with others into a group and by distributing the losses to the group as a whole. In this way, according to Seligman, certainty is substituted for uncertainty, and this method of combination is called insurance. The essence of insurance, he explains, is the effort to diminish the risk of uncertainty, and considered from this point of view, " Insurance is productive, that is, it involves an increase of wealth, because it lessens the social costs of risks." He is careful to explain that we must not confuse the loss due to uncertainty with the loss due to the occurrence itself, for he remarks that:

" The occurrence is bound to happen. Death will come, fire will consume, the tornado will strike. In some cases the probability of the occurrence or the amount of the loss may indeed be somewhat lessened by preventive action. A good police force will diminish burglary, an efficient fire department and a good building code will decrease fire losses, carefully devised factory laws will lessen accidents. In all these cases, however, we have to deal with prevention, not with insurance. Insurance takes the fact itself for granted; it does nothing to eliminate the

occurrence. The loss is hence the same, whether we have insurance or not; the house is burned and there is less wealth than before."

The Compensation Required for Risk.

There is, of course, in all cases an additional loss due not to the occurrence itself, but to the uncertainty, and this, according to Seligman, can best be observed in the investment of capital. The ordinary man will not assume risk unless he is remunerated for it. When a capitalist loans funds and there is any special degree of risk connected with the transaction, it is a familiar fact that he will increase the rate of interest by a corresponding amount. This increase in the interest rate is an addition to the expenses of the borrower. To the extent, therefore, that insurance diminishes risk or uncertainty in commercial enterprise the ultimate cost of the product, or the price ultimately charged to the consumer, is correspondingly reduced, or in the words of Seligman, "if the uncertainty could be eliminated, the price of the commodity would be lower and there would be a corresponding gain to the community as a whole." Since insurance performs this function by minimizing uncertainty, it is accordingly a factor in the production of wealth.

Factors in the Cost of Production.

The practical importance of this consideration cannot easily be over-estimated. No writer previous to Seligman has so clearly defined the economic function of insurance as an element in the cost of production. In his own words,

"Like transportation, insurance falls under the head of exchange of wealth, while exchange, as we know, is itself a species of production. Improved transportation reduces the cost of having a commodity in one place become a more valuable commodity in another place; improved insurance reduces the cost of having the uncertainty of the future change into the more valuable certainty of the present. Transportation overcomes the disadvantages of space; insurance overcomes the disadvan-

tages of time. Transportation is productive because it increases space utilities; insurance is productive because it increases time utilities."

In continuation, he answers the question as to how insurance minimizes uncertainty, in the statement that:

"The answer is, through the combination of risks. This is a result of the law of probabilities. If we have accurate statistics of fires, for example, for a term of years and take the number of fires with a given number of houses during that period, we get an average. If the figures in any year correspond exactly to the average, there would be a certainty in the number of fires, and the only uncertainty would be as to which house would burn. In point of fact, however, in any particular year there will be a variation from the average. According to a well-established law, the probable variation increases only as the square root of the number of cases. If there are a hundred times as many houses, there will be only ten times as much probable variation from the average loss. Hence the larger the number of cases, the less will be the certainty as to the amount of loss which will be borne by the group as a whole. Insurance combines the risk into a group, and thus reduces the element of uncertainty. The risk of the group is less than the sum of the risks of the individuals who form the group."

Fallacies of Self-Insurance.

He also disposes of the alternative of so-called self-insurance by pointing out that only an immense corporation may practice self-insurance with a better chance of success than a corporation organized for that purpose. He concludes:

"The great benefit of an insurance company is not only that the risks are combined, but also that they are transferred to a class who can afford to make a special study of the problem, and who can thus reduce the cost of insurance by displaying their ability to estimate uncertainties. Whether the company is a stock corporation or a mutual company is of importance only as to the ultimate distribution of the profits of the enterprise; in one case, as in the other, however, the management of the business is confided to a class of experts. The more adept the insurance companies, and the more scientific their methods, the closer will be the correspondence between the

preparation for, and the fact of loss and the smaller will be the accumulation of the necessary insurance fund, the lower will be the insurance premium, and the greater will be the net gain to the community. Insurance properly conducted is the opposite of gambling. If any one takes out an insurance policy, he frees himself from an existing uncertainty and transfers the risk to some one who is more qualified and ready to assume it; if he makes a wager with another, the newly created uncertainty attaches to both. Insurance is the transfer and reduction of risk; gambling is the creation and increase of risk."

Excepting Mr. Allan H. Willett, whose dissertation on the theory of risk and insurance will be subsequently referred to, Seligman, more than any other recent writer, has measurably advanced the theoretical discussion of the subject.

Relation of Insurance to Interest and Profit.

Long previous to Seligman, Prof. Richard T. Ely had considered insurance as an element in social economics, but rather as a factor making for social efficiency and social progress than as a distinct element in economic theory. In his "Outlines of Economics," published in 1905, Ely, however, considers insurance in its relation to interest and profits, defining the elements of gross profits as replacement of capital, insurance, interest, wages of superintendence, and pure profit. The second element is necessarily the payment for risk incurred in commercial enterprise. Insurance as thus defined may not necessarily be the payment of an insurance premium to an insurance corporation, but merely the higher rate of interest paid for capital borrowed to carry on a particularly hazardous undertaking. Ely also considers insurance with reference to consumption and saving. Probably no other function in modern society serves so distinctively the purpose of increasing capital as insurance, which requires the accumulation of enormous sums as security, with the condition that such sums must be safely invested and yield a proper rate of interest. In life insurance the inducement to save periodically or systematically sums, however small, which would otherwise be wasted, or

which in any event would not be converted into capital, contributes as much, if not more than any other method of savings or investment to the increase in the national wealth. Ely refers to this relatively modern institution as one of the most valuable factors in our economic civilization, and remarks:

"It has the great merit of providing in varying proportions for both security and profit of investment. The provision for security is especially prominent in the case of fire insurance It is often said that such an insurance is simply an equalization of losses, or a distribution of a heavy sudden loss over a long period of time. In fact, it is much more than that. It is important to take the amount of loss from a business in such amounts and at such times that no vital want is left unsatisfied, and this is done by insurance. Thus perpetuity and equality of conditions is guaranteed to a business in such a way as to greatly encourage investment. The same principle applies to life insurance. The death of a business man is often a more serious shock to a business than a conflagration. The payment of a life insurance policy is often a very great relief to the financial embarrassments in which such a business is left."

While this discussion is more with reference to the social aspects of insurance, it also has a decided practical bearing upon the discussion of insurance as an element of economics. Economics, as Ely observes, is, after all, a science of man. It is continuously a question of human wants and needs, and the means and methods most productive to bring about a satisfaction of human desires at lowest cost. Without entering upon a discussion as to the distinction which requires to be made in economics between value and utility, it is self-evident that insurance is of the highest utility, because it satisfies to so large a degree, and in so effective a manner, the human wants and needs, by eliminating the inherent insecurity in business enterprise as well as in the duration of human life.

The Accumulation and Conservation of Capital.

The full significance of the economic function of insurance becomes apparent only when it is considered how enormously insurance aids in the accumulation of capital. Not only does

insurance aid in the accumulation of capital by the aggregation of the vast funds which constitute the security of the insured, but it aids further in the conservation of capital by the encouragement which it gives, and compulsion, so to speak, which it exercises in systematizing the thrift function of the people. The assets of American life insurance companies alone in 1909 amounted to $3,643,858,000, consisting chiefly of $2,700,190,000 invested in the bonds of transportation companies and in real estate mortgages; and $312,273,000 invested in other securities of this kind. A theoretical consideration of the whole question of the nature and function of capital and income would be required precisely to indicate the function which insurance performs in modern public and private finance. One of the most valuable contributions to this discussion is the treatise by Prof. Irving Fisher, on the Nature of Capital and Income, published in 1906, which properly includes a discussion of insurance in its relation to the question of risk and its assumption in the investments of capitalists. In the words of Fisher:

"Business men try not only to estimate the risks which they must encounter and to adjust their accounts accordingly, but they also endeaver to avoid such risks altogether. This follows from the existence of the factor of caution. Where the coefficient of caution is abnormal, amounting to incaution, risks are not avoided, but are expressly sought, and the phenomena of gambling and indiscriminate speculation are the result. But in the great majority of men there exists a healthy fear of risks, and in consequence a tendency to avoid or reduce them."

The Reduction of Risk by Insurance.

Fisher explains that there are five principal ways in which risk may be reduced, that is: (1) By increasing guaranties for the performance of contracts; (2) by increasing safeguards against incurring losses; (3) by increasing foresight and thereby diminishing the risks; (4) by insurance, that is, by consolidating risks; and (5) by throwing risks into the hands of a special class of speculators.

Considering the means of avoiding and shifting risks by insurance, Fisher remarks:

"Insurance involves the offsetting of one risk by another; that is, the consolidation of a large number of chances whereby relative certainty is, as it were, manufactured out of uncertainty. To illustrate this, let us suppose that 10,000 houses of the same kind are too distant from each other to be destroyed by the same fire, and let us suppose that these houses in the average would be worth $10,000 each were it not for the risk of fire; in other words, that $10,000 is the capitalized value of the services to be rendered by each house, assuming that it lives out its natural life. The value of the total number of houses would then be $100,000,000. This is the "riskless value." It is the capitalized value of the income which the 10,000 houses would bring in, were there no loss by fire. If interest is at 5 per cent., the income which is thus capitalized is $5,000,000 a year. If now we suppose that the annual risk of fire is one chance in 200, there will be about 50 houses annually burned. Reckoning the value thus destroyed at an average of $10,000 for each house, there will be $500,000 annually lost by fire. We must now deduct this from the $5,000,000, which would be the income were it not for fires. We have left $4,500,000, the capitalization of which is only $90,000,000. In other words, the total property of 10,000 houses is worth in "mathematical value" $90,000,000 instead of $100,000,000, the reduction being because of the prospect of fires. If we suppose all of these houses to be owned by one corporation, this mathematical value of $90,000,000 might also be the actual value, for such a corporation could count on about 50 houses burning annually almost as a certainty. Each house would then be worth, on an average, $9,000. But if such an individual house is owned by an individual person, this mathematical value would not be its "commercial value," on account of the element of caution. Let us say that the caution coefficient is 7–9, in which case the house would be worth $7,000. In other words, we have $10,000 as the "riskless" value of the house, $9,000 as its "mathematical" value, and $7,000 as its actual "commercial" value, assuming that there is not as yet insurance. Now if the owner of such a house could secure insurance on a purely mathematical basis of the risk, which, as we have seen, is one-half of one per cent., and, therefore, could pay only $50 per annum, in consideration of which the value of his house, if destroyed by fire, is restored

to him, it is evident that he has made a good investment; for he is now assured of a house even should a fire occur, and he has, instead of the risk of fire, merely to pay his annual premium of $50 a year, the capitalized value of which is $1,000. Consequently, his house is worth $10,000—$1,000, or $9,000.

"Such an insurance rate, however, being based on the mathematical or "pure" premiums, would not pay any profit to the companies conducting it. But even a higher insurance would leave a large margin of capital-value saved to the insured. If we suppose a "loading," so that the insurance premium is not $50, but $100, similar reasoning would show that the value of the house when insured would be to the owner $8,000 instead of $7,000. As long as the loading is not sufficient to absorb all the margin between the $7,000 and $9,000, it will be advantageous to insure."

The Protection of Income by Insurance.

Prof. Fisher emphasizes the advantages of insurance, with particular reference to conserving and equalizing the income from property, and he illustrates his views by the statement that:

"The owner of the house in question would receive, if it were not insured, a net annual income, after providing for depreciation, of five per cent. on $10,000, or $500 a year until the house was burned, after which he would receive nothing; whereas, if he insures, he receives this $500 income less his premium up to the date of the fire, and afterward the income from the indemnity paid him by the company."

What is true of fire insurance is equally true of other forms of insurance, and Fisher observes, with particular reference to life insurance, that, like the other forms, it tends to steady the income of the beneficiary. He states:

"If a wife holds insurance on her husband's life, the consequence is that, although what he gives her during his life is somewhat diminished, her income will not suddenly cease at his death. The tendency of insurance here as elsewhere is to make regularity out of irregularity, relative certainty out of relative uncertainty; and where, under the form of insurance contracts, the opposite result follows, the case is not one of true insurance, but tends to become one of gambling."

It is hardly necessary to point out that the distinction between insurance and gambling has been made so clear by those who have written upon the subject that it requires no further analysis. It is manifestly to the interest of insurance companies to discourage every form of adverse selection, or in other words, attempts to gain in an illegitimate manner by a method designed solely for the equalization of normal losses. Any attempt to pervert insurance from its legitimate function, and to afford opportunities for speculation and fraud, would divert the system into one of gambling and make it more or less contrary to public policy.

Considerations of Insurance Law.

A very interesting contribution to the economic aspects of insurance is contained in a work entitled, "On the Civic Relations," by Henry Holt, published in 1907. Mr. Holt includes insurance in his discussion of the law of personal property contracts,* observing that:

"Suretyship and warranty shade into another large class of contracts embracing all kinds of insurance. Fidelity insurance is especially like suretyship, but also fire, marine, accident, life, plate-glass and all the rest, are of course of the nature of warranty; but the warrant extends, unless otherwise agreed in the policy, not necessarily to the full amount of the policy, but only to the value of the property at the time of loss. Hence the desirability of keeping the policy small, or having it declare that the amount insured for shall, in case of loss, be taken as the value of the property. Life-insurance companies, however, are always liable for the full amount of their policies."

The Place of Insurance in the Law Merchant.

The law of insurance is very largely the law of contracts and from the earliest times it has been a part of the law merchant. The decision of the supreme court that insurance is not an element of commerce, is not sustained by the actual

* For a full discussion of the law of insurance as within the scope of personal property contracts, see Kent's "Commentaries," Vol. III.

facts of insurance history and the historical development of the insurance contract out of the earliest forms of bottomry loans. Distinguishing clearly between the principle of insurance, as such, and the application of the principle to actual practice, it requires no extended research into the history of commerce to prove that the development of the principle is practically coincident with the progress of navigation and national and international commercial intercourse. Distinguishing further between the earliest form of underwriting—that is, long before the business was conducted by corporations—insurance was in its origin as much a matter of business enterprise as any other branch of trade. In fact, one of the earlier legal definitions of insurance emphasizes this point precisely when, for illustration, John Millar, in his "Elements of the Law Relating to Insurances," published in Edinburgh in 1787 defines insurance as "a contract by which *one man*, for a consideration received, becomes liable for the loss arising to another from any specified contingency." While this form of underwriting has never been very general in this country, it prevailed quite extensively previous to the second war with England, although by that time the business of the Insurance Company of North America, and other insurance corporations had attained to considerable proportions.

The Place of Insurance in the Industrial System.

It would manifestly unduly enlarge this discussion to consider all the numerous authorities on economics who have incidentally referred to the subject. The practice of insurance is so intimately interwoven with the whole fabric of modern business life, that Mr J. A. Hobson has very properly included insurance in his elaborate outline of the industrial system, with special reference to earned and unearned incomes. According to Hobson, insurance produces four utilities: (1) reducing the pain or subjective injury of an accident, (2) producing a sense of security, (3) evoking productive energy, (4) preventing objective waste. He very properly observes that, "No de-

scription of the outlines of modern industry would be complete without reference to the business of insurance, which is so intimately associated with finance." Of particular importance, however, is the part which insurance plays in the industrial system as an instrument for producing and distributing goods and services. In answer to the question as to what insurance produces, Hobson remarks that:

"We can best formulate our answer by first putting another question, viz.. What damage would be done if there were no insurance? The life of a producer often comes to a sudden end; if no provision were made for securing to those dependent on him a continuance of at least a part of the income he earned when alive, they must sink suddenly into a lower standard of living, perhaps into penury, and both their happiness and their present or future efficiency as producers might be greatly impaired. By paying a comparatively small sum over a long term of years, which involves the habitual deprivation of what, if expended otherwise, would constitute the least useful and pleasurable part of his whole expenditure, he is enabled to avert a certain damage of a serious kind affecting the comforts, conveniences, or even the necessaries in the standard of life of his family. What insurance here produces is evidently the difference in disutility between the sum of the small losses involved in the payment of the yearly premiums and the great loss involved in the sudden total withdrawal of the whole or a large part of the family income. The substitution of the former small disutility or cost for the latter large one is in effect the production of so much utility, not merely from the standpoint of the individual but from that of the society to which he belongs. It causes, directly, no increase of concrete goods or services, but by assisting a more equitable distribution over time of the aggregate of such objective wealth, it causes more to be got out of it in satisfaction and in subjective utility In averting a damage to the productive power of industry by a sudden loss of family income insurance may also be considered as directly productive of industrial energy."

THE PROTECTION OF PROPERTY AND WEALTH BY INSURANCE.

In this important passage, in marked contrast to the often indefinite and inconclusive language of earlier writers on the

subject, Hobson, better than any other writer, emphasizes the function of insurance in the industrial economy of modern nations, and in particular the service rendered by insurance in preventing losses from falling suddenly in full force on business undertakings by distributing such losses over a large number of owners and over a long period of time. He points out that the sudden total destruction of some important part of material capital may destroy the whole efficiency of what remains and suddenly terminate the value of any given business ability. By thus conserving commercial power insurance renders one of the most useful of services to the whole national economy. In the words of Hobson:

"Without insurance the worry caused by conscious inability to provide against an increasing number of more highly-appreciated risks would become an almost intolerable strain, enhancing the subjective or human cost of production throughout the business world. As the spread of education and the stir of modern city life cause larger and larger numbers of the workers to have more feeling for the future of themselves and their families, this extensive and intensive growth of anxiety is exhibited in an immense expansion of private and public insurance. The main direct object of such insurance is the production of a sense of security."

In other words, according to the same writer, a reasonable measure of security is essential to evoke the best productive powers, for without such security man cannot, and will not, do his best. He therefore concludes that "The production of security is therefore a direct enhancement of productive energy," and this would be impossible without insurance.

The Abstract Theory of Risk and Insurance.

The foregoing considerations indicate in general outline the attention which leading writers on economics have given to the subject of insurance. It is made clear that as yet insurance has not received the full consideration, both theoretical and practical, of which it is deserving as an element of economics, commerce and social progress. The only qualified inquiry

into the whole subject is a treatise by Mr. Allan H. Willett, on "The Economic Theory of Risk and Insurance," published in 1901. This dissertation is by far the most ambitious attempt to co-ordinate the theory of risk and insurance in the light of economic teachings and with some regard to practical experience. Insurance, according to Willett, is defined as a fund accumulated to meet uncertain losses, but more precisely,

"as that social device for making accumulations to meet uncertain losses of capital which is carried out through the transfer of the risks of many individuals to one person or to a group of persons. Wherever there is accumulation for uncertain losses, or wherever there is a transfer of risk, there is one element of insurance; only where these are joined with the combination of risks in a group is the insurance complete."

Aside from the advantage resulting from the combination of risks, and the consequent reduction of uncertainty, as decided economic benefits resulting from insurance, Willett observes that there is another advantage to commercial enterprise in that,

"It is desirable for society that risks should be correctly estimated. Men differ much in their ability to judge them. The segregation of the work of estimating risks leads to a differentiation of capitalists, as a result of which those who are especially adapted to that task will be the ones who will undertake it. Moreover, their natural ability will be further developed through the experience and training of the work itself. On the other hand, there are many men capable of rendering good service to society in comparatively safe industries, who are so constituted that the necessity of running any great chance of loss seriously diminishes their efficiency. The possibility of transferring the risks of their business to others for a fixed premium frees them from the paralyzing influence of uncertainty, and enables them to make the best use of their powers in other directions. The gain to society from the transfer of risks is obtained partly through the reduction in the cost of carrying the risks when they are borne by those who have the most ability to estimate them and the most confidence in their own judgments about them, and partly through the increase in the efficiency of those who are abnormally sensitive to the influence of uncertainty."

The Economic Gain Resulting from Insurance.

The economic significance of insurance as considered from this point of view can hardly be overestimated in the case of a progressive commercial nation, in which the assumption of widely varying risks, differing in nature and degree, is a first essential in business undertakings on a large scale. To the extent that insurance encourages risk assumption it aids materially in the economic progress of the nation. Willett points out:

" How great the gain is, even under existing imperfect conditions, it is impossible to estimate, since it is difficult to conceive how the large enterprises of the present day could be carried on without the possibility of transferring to insurance companies many of the risks involved in them. It could certainly be done only on a much larger margin of safety than is now considered necessary."

Insurance as an Essential Factor in the Production of Wealth.

In brief, according to Willett the treatment of insurance naturally belongs in the division of economic theory that deals with the phenomena of the production of wealth. This view is in entire conformity to the gradually developing conviction of trained economists who have given concern to the subject as an important branch of economic inquiry. There has been, as might be expected, and as pointed out by Willett, a singular lack of unanimity among writers on economics with regard to the division of economic theory in which the treatment of insurance ought to be placed. I can not do better than conclude this inquiry (which I believe is the first summary account of the consideration of insurance by economic writers from the time of Adam Smith to the present day) by quoting the concluding paragraph of the discussion by Willett:

" Some have considered it in connection with production, others have regarded it as a phenomenon of consumption, while still others have found it inexpedient to bring it under any of the recognized divisions, and have put it at the end of their

works along with other subjects of a more or less dubious economic character. There seems to be little occasion for such uncertainty. If the old divisions of production, distribution, exchange and consumption are to be maintained, there is no doubt that the proper place for the discussion of insurance, at least so far as insurance of capital is concerned, is in the department of production. With regard to the insurance of consumption goods the case may not seem so plain at first sight, since there is not the same direct relation between such insurance and the productivity of industry. Nevertheless, it undoubtedly belongs in the division of production. It belongs there, not because it affects the productivity of other capital, but because the creation of security is in itself a form of production. If the owners of consumption goods are willing to pay a price for the sake of having them insured, it is evident that they are obtaining something in exchange which is of more value to them than the money with which they part. What they obtain is security, and whether or not it seems best to consider such security as a consumption good, or as any form of wealth, it cannot be questioned that the capital and labor engaged in creating it are serving mankind in the same way as that employed in the creation of any commodity for which consumers are willing to pay."

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CHAPTER III.

INSURANCE AS AN ELEMENT OF EARLY COMMERCE.

All commerce, ancient or modern, is more or less in the nature of a speculation, and, quite properly, the early traders were often styled "merchant adventurers," because of the substantial risk necessarily inherent in all commercial undertakings on a large scale. The most successful merchants and traders are invariably men of remarkable judgment and foresight, gifted with exceptional ability to determine in advance, with accuracy and precision, the probable chances of commercial gain. In proportion as the sphere of commercial enterprise expanded, the risk of uncertainty necessarily increased, and in no field as much as in that of maritime commerce and world-wide navigation. The perils of the sea, much more so in the ancient past than at the present time, early suggested and later made imperative, an equalization of losses among shippers and merchants by a combination of interests, equivalent to a reduction of the risk. The earliest maritime codes extant contain definite rules of contributionship as an established principle of mercantile law governing the sea trade of the period. The practice of jettison, or the "throwing overboard of part of the cargo, or anything on board the vessel, or the cutting or casting away of masts, spars, rigging, sails, or other furniture, with the object of lightening or relieving the vessel in case of emergency or necessity," is clearly defined in the Rhodian Sea Law, which dates from about 900 B.C.

The Principle of Contributionship and Average.

The principle of contributionship, as applied to marine insurance, is stated by Walford to be "that those whose goods

or interest in risk have been saved or benefited by the damage, loss or sacrifice of others, should not profit at the expense of others," and that, therefore, "those whose goods have been sacrificed or damaged, or suffered charges for the common good, advantage, or safety, ought to be indemnified," and that, therefore, "justice requires that equality should take place by contributions amongst all those interested and who have been in danger of losing all, and where some have saved what was in risk only because others have sacrificed theirs."*

But the principle of contributionship, which, by its nature, implies the joint assumption by different parties of unavoidable risk in maritime commerce, is not the only conclusive evidence of the origin of marine insurance practice in ancient maritime laws and usages. The practice of bottomry and respondentia bonds, or the lending of money at maritime interest in return for the assumption of maritime risk, was widely established even in very early times and extended references thereto occur in the Rhodian Law, the Laws of Oleron (1075–1270 A. D.), and the Laws of Wisby, promulgated in 1288 A. D. The last named laws are the first in which marine insurance is referred to as an established commercial practice of the times and by a broad interpretation of the terms used it included life insurance in a primitive form in the assumption of risk on the life and safety of the master or owner against the perils of the sea, including piracy and capture by the enemy.

The Sea Laws of Oleron and Wisby form the basis of the justly famous marine ordinance of France, enacted in 1681, which, in the words of Flanders, embodies "in systematic order the subjects of navigation, shipping, insurance and bottomry." Marshall, in his treatise on the law of insurance, the first American edition of which was published in 1808, observes that "The law of insurance is considered as a branch of marine law and was borrowed by us from the Lombards, who first introduced the use of this contract into England. It is also a branch of the law of merchant, being found in the practice

*Ins. Cyclopedia, Vol II, p. 112.

of merchants, which is nearly the same in all countries where insurance is in use; and indeed merchants themselves were, for a long time, the only expounders of it. The law of merchants not being founded in the institutions or local customs of any particular country, but consisting of certain principles which general convenience has established, to regulate the dealings of merchants with each other in all countries, may be considered as a branch of it all." The sources of the law of insurance, in the words of Marshall, are, "first, the ordinances of different commercial states; second, the treatises of learned authors on the subject of insurance; and third, the judicial decisions in this country (England) and others professing to follow the general marine law and the law of merchants.* It is thus apparent that the practice and the law of insurance have been evolved out of the principles and practice of commerce through centuries of human experience as a logical necessity or aid to the development or furtherance of commercial enterprise throughout the world.

Importance of Early Law and Custom.

A somewhat extended consideration of the early laws and usages, with particular reference to maritime commerce and legislation, is indispensable for a sound understanding of the basic principles which govern the use of insurance practice in modern life. In the course of the many intervening years, with the growth of commerce and the differentiation of human effort, many new and novel forms of insurance have come into existence, some of which touch but remotely commercial undertakings considered in the strictest sense of that term. But insurance in every form, or by every method, is based upon contractual considerations and implies the assumption of risk in return for a definite payment of money at stated intervals. The considerations which govern the insurance contract are, therefore, strictly commercial and the whole business of insurance is carried on as a species of commerce, mostly through

*Marshall on Insurance, 2d American ed., pp. 18, 19.

corporations organized and conducted in identically the same manner as commercial undertakings generally. Insurance in any one of its many and varied forms is sold the same as other merchandise, it has its price, which is governed by its cost and competition, and, as occasion may arise, by supply and demand, particularly in the case of war or impending maritime disaster. The rate in marine insurance is governed by the risks inherent in maritime commerce and inland navigation, which vary widely in their nature, according to distance, locality, and time. For all practical purposes, the principles which govern the assumption of commercial or individual risks at the present time are exactly the same as those which governed in ancient law and custom, and however remote the analogy may seem, it is nevertheless a true and connected chain of historic evidence which binds together the distant commercial period with the present, however unlike the conditions at the two extremes may appear when contrasted in the light of the marvelous changes which have taken place.

Bottomry Laws and Usury Loans.

Bottomry loans are the earliest form of maritime contracts in which are combined the elements of risk assumption in return for a special consideration. The risk assumed in bottomry loans is that the money lent is not to be returned if the vessel is lost, while the special consideration is maritime interest, or a rate in excess of the legal rate, but not in conflict with the usury laws. The leading case in which legal sanction was given to this practice in English courts of law was decided by Lord Chief Baron Hall, who held that "this (bottomry) bond is not within the statute (of usury), for this is the common way of assurance and if this were void by the statute of usury, trade would be destroyed."*

The commercial nature of this form of contract in navigation is so self-evident that it requires no legal decisions to define its position in the practice of insurance. As quoted

*The Law of Usury, by J. W. Blydenburgh, New York, 1844.

by Hall, who was the first American commentator on maritime loans (Baltimore, 1811), "There is a great resemblance between contracts of maritime loans and insurance. They frequently appear to be governed by the same rules. They are twin brothers to whom maritime commerce has given. birth; for each has a character peculiar to itself." And he continues, "It is beyond doubt that this contract, without which commerce would languish extremely, is lawful. The interest which the lender claims in case of a successful voyage is the price of hazard, and has nothing in it which resembles usury." Walford refers to bottomry loans as "very ancient—apparently coeval with the earliest development of maritime commerce," "that they were apparently devised with the view of defeating various restrictions to usury;—or, if not especially so devised, were very soon specially adapted to that end; and that, they being in themselves a species of marine insurance, are supposed to have led directly up to the present system of marine insurance." The reference to bottomry loans in the Rhodian Law is stated by Walford to be, "If masters or merchants borrow money for their voyages, the goods, freights, ship and money being free, they shall not make use of suretyship except there be some apparent danger of the sea or of pirates. And for the money so loaned the borrowers shall pay naval interest."

The Rhodian Sea Law.

Six chapters of the Sea Law deal with loans of this character, but it is conceded that the references in the original text were very obscure. Mr. Ashburner, the most learned commentator on the Rhodian Law, explains that although the terms in which loans of this kind are expressed differ, they remained substantially the same from the age of Demosthenes to the 13th Century, and that while there are differences in the wording of the documents, they do not necessarily imply corresponding differences in the legal effect of the transactions. Maritime loans under the Rhodian Law, according to this writer, "resemble ordinary loans upon a contingency, but there

is evidence that both in antiquity and the Middle Ages the forms of the maritime loans were made use of for contracts which were purely aleatory," or, in other words, in the nature of gambling ventures. The important distinction to be observed in this brief discussion is that bottomry loans were a species of contract based upon risk assumption, and while their language varies and their purpose and nature, according to the time and circumstances, the underlying object, or purpose, was in all cases the same and strictly in the nature of marine insurance. As pointed out by Mr. Ashburner, the actual commercial facts do not always correspond exactly to the language of the documents, for conveyors get into the habit of using certain forms the legal effect of which has been precisely fixed by decisions or by usage. Hence, although the commercial facts differ from those which the phrase was originally framed to express, the conveyor goes on using it, although there may be an important change in commercial conditions, even though there is no change in the language of the documents. Particularly is this the case where circumstances make it necessary to adopt expediencies such as were imperative when the Church held that maritime risk did not justify the taking of interest.

Historical Value of Commercial Documents.

To the foregoing must be added the further explanation, also set forth by Ashburner, that few commercial documents have been preserved in the original, since business men only preserve documents which enable them to enforce or resist a claim. Documents, however, which have value only for a definite period of time are usually destroyed when the limit of their practical usefulness, or value, has passed. This is as true of policies of insurance as of charter-parties, bills of lading, etc. But there is sufficient evidence in ancient maritime loans to sustain the conclusion that practically co-incident with the beginnings of an extensive commerce by sea, bottomry loans came into existence and that out of these, in course of time, developed the modern practice of marine insurance, which again gave rise

to all the other forms of insurance which have been developed and perfected at later periods.

Historical Continuity of the Doctrine of Average.

The basic doctrine in marine insurance is general average, of which, according to Duckworth, the best and most generally accepted definition is "All loss which arises in consequence of extraordinary sacrifice made, or expense incurred, for the preservation of the ship and cargo, comes within general average and must be borne proportionately by all who are interested." This doctrine of general average, according to the same authority, is admittedly "founded upon the Rhodian Law and general average loss is calculated according to the laws in force at the port of discharge." The Rhodian Law of general average was in its entirety incorporated in the Roman Civil Law and as such it became in time incorporated in the practice of the Admiralty Courts of Europe and America. According to Walford, the connecting link, so far as England is concerned, is directly obtained in the fact that William the Conqueror made, and Henry I ratified, the law concerning goods cast overboard by mariners in a storm, founded upon, or, as Molloy says, in imitation of, the ancient Rhodian Law.* Since it is not the present purpose to consider in detail the origins of insurance in all its branches, but merely the historic relation of insurance to ancient and modern commerce, it is not necessary to enlarge upon the qualifications of the term "average," nor even its main divisions into general and particular, which are, however, essential for a full understanding of the first principles of marine insurance. The doctrine of average, however, applies, in many countries, at least, also to fire insurance, the clause being most commonly introduced into mercantile policies and agricultural (hail, wind storm, etc.), insurance. Here, again, the limitations of the present inquiry preclude a more extended consideration of the details of a subject which itself is one of unusual interest and great practical importance.

*Ins. Cyclo., Vol. I, p. 225.

Early Ordinances Regulating Insurance Practices.

At the commencement of the 15th Century the practice of insurance had become quite general with European commercial nations. As early as 1435 ordinances regulating the insurance business had been adopted at Barcelona which required that underwriting should be done in the presence of a notary and policies not thus authenticated were to be considered null and void. As early as 1468, by a decree of the Grand Council of Venice, insurance cases were required to be tried before the Consular Mercantile Court, and by 1523 a complete code of insurance laws had been enacted at Florence.*

From Italy, no doubt, the practice of insurance was introduced into England through the Lombards,† for the earliest policies in existence, both marine and fire, contained the provision that "This writing or policy of assurance shall be of as much force and effect as any writing heretofore made in Lombard Street." The significance of this provision is emphasized by the fact that during Colonial times policies issued in America, certainly as early as 1746, (which is the date of the oldest American insurance policy in existence‡) contained the identical phraseology just referred to.

In 1556 Henry III., King of France, issued an edict concerning the Court and authority of the Prior in Councils of Roan, including the provision that, "As we are informed that *the trade of assurances* is of late greatly advanced by merchants of the said city of Roan (a work so honorable that it does yet beautify and greatly advance the trade and commerce of the

* For a convenient summary account of the early history of insurance, see John Beckmann's "History of Inventions, Discoveries and Origins," 4th English Ed., London, 1846, Vol. I, article on Insurance.

† Park, System of Marine Insurance, 7th Ed., London, 1817, Vol. I, p. xxxviii.

‡ An account of Early Insurance Offices in Massachusetts from 1724–1801, by E. R. Hardy, Librarian, Insurance Library, Boston, 1901. For an account of the early insurance practices in America, see the History of the Insurance Company of North America, Phila. 1885, p. 14, et seq.

said city)." It was, therefore, enacted that the merchants should choose one among them, "such an one as they should think meet, being a man trusty and expert in the knowledge of *the trade of assurances*," who should make and register the said policies of insurance. This, no doubt, was for the purpose of bringing about uniformity in insurance transactions, for it was further ordained that all judges and others concerned should thereafter give full credit to the transactions thus made a matter of record, and not "meddle in the said business of assurances or anything thereunto belonging."

The Ancient Law Merchant.

It is made evident by these references that insurance at this very early period was clearly recognized as an important element and instrumentality of commerce. Insurance laws and usages had, in fact, become as much a part of the Law Merchant as bills of exchange and other mercantile instrumentalities invented or designed for the purpose of extending and facilitating commercial relations. Vance,* in the historical introduction to his treatise on Insurance Law, refers to this period, as follows: "It is thus seen that during the fourteenth and fifteenth centuries the practice among merchants of making insurance contracts had become general throughout all the maritime states of Europe. The contracts seem to have been confined to those merchants engaged in the more extensive international commerce, and this fact *rendered necessary uniformity in the regulation* of insurance as practiced in these different countries. Thus there was impressed upon these insurance regulations, just as well *as upon other commercial rules* growing out of the custom of merchants, a certain international character, and the whole body of rules intended to govern these commercial transactions became known as the 'Law Merchant.' These rules bore a peculiar relation to the respective systems of law existing in the several countries in

*Handbook of the Law of Insurance, by Wm. R. Vance, St. Paul, Minn., 1904, p. 4, et seq.

which the Law Merchant, by virtue of the customs of merchants, prevailed."

The Beginning of Insurance Regulation in England.

By 1600 marine insurance had become firmly established in England, and in the year following, by the 43rd Elizabeth, a Court of Insurances was established in London, for the purpose of affording facilities for settling disputes arising under insurance policies. The Court included among its members eight merchants with full power and authority to see, examine, order and decree, all and every case, or cases, concerning policies of assurances in a brief and summary course, as seemed best according to their discretion and without formalities, or pleadings, or proceedings.* With the statute of 1601 begins in English law the Parliamentary *regulation of insurance*, governing chiefly as to the construction of the contract in courts of law and the manner of its making and enforcement. A similar regulation of insurance was introduced into Rotterdam in 1604 and into the French Code, known as the Guidon sur la Mer, in 1607. A Chamber of Insurance was also established at Amsterdam in 1612† and ten years later Malynes published his famous treatise Lex Mercatoria, or the Ancient Law Merchant, a third edition of which was published in 1686.‡

Insurance as a Branch of the Law Merchant.

Malynes considered the whole subject of insurance in all its branches and among other rules he enumerated twelve cardinal principles of knowledge as the foundation of complete mercan-

* Regarding the history of this unique court very little is known with accuracy. The most complete account is in Walford's Ins. Cyclo., article Chambers of Insurance, Vol. I, p. 486, et seq. See also, Park, System of Marine Ins., Vol. I, p. xi. Also, Wambaugh, Cases on Insurance, which gives in full the act establishing the Court of the Commissioners, 43rd Elizabeth, c. 12 (1601).

† Walford, Ins. Cyclo., Vol. I, p. 485.

‡ Malynes (Gerard) Consuetudo vel Lex Mercatoria, or the Ancient Law Merchant, London, 1622, (Copy in Ins. Library, Boston, Mass.).

tile instruction, of which two relate to insurances, as follows: "1st, Delivery of monies at interest or upon bottomry, or upon lives, annuities, or pensions, etc.," and 2nd, "The manner of making assurances upon goods, ships, the persons of men, or any other things adventured by sea or by land; or the customs observed between different nation or nations." In addition, however, numerous references to insurance occur throughout the work and various appendices which supplement the third edition, published in 1686. He refers to the "most laudable custom of assurances," to the end that merchants might *enlarge and augment their traffic and commerce* and not adventure all in one bottom to their loss and overthrow, but that the same might be answered for by many." He traces the origin of this custom to the ancient Sea Laws and merchant codes of maritime nations. The importance of this reference to the ancient Law of Merchants by Malynes consists in the fact that all insurances are recognized as mercantile transactions and as an aid and encouragement to commerce, including insurances on lives. To once more quote his language, perhaps rather quaint, but well adapted to the needs of the period, "For by the custom of insurances it is intended to avoid cavillations; every insurer should be bound ipso facto to the said assurance, *having a respect to the augmentation of traffic and commerce.*"

Admiralty Jurisdiction Over Insurance.

The third edition of Lex Mercatoria, published in 1686, has as an appendix a treatise on the jurisdiction of the admiralty of England by Richard Zouch. Numerous references to insurance occur therein and among others the important statement that the admiralty of England had the most ample power and jurisdiction over business relating to the sea, "to hold conusance of pleas, debts, bills of exchange, *policies of assurance*, charter parties, bills of lading, etc." These and other references to insurance prove conclusively that in the opinion of these early writers and, in fact, in daily life and by commercial custom and usage, insurance even three hundred years ago was con-

sidered an important element of the commerce of the period. While not ignoring the fact that most of the insurance contracts made by merchants at this time were of marine insurance, and probably to a not inconsiderable extent loans upon bottomry and respondentia, still the general character of the business upon the basis of the earlier definitions would seem to conclusively establish that insurance transactions as a whole were included in the Law Merchant as ordinary mercantile transactions and considered an indispensable element of everyday commercial life.

FRENCH ORDINANCES ON COMMERCE AND MARINE INSURANCE.

In 1673 an *ordinance of commerce* was enacted in France under the auspices of Colbert, as Minister of Finance to Louis XIV and this enactment in 1681 was followed by a corresponding ordinance of marine, which is justly considered the most complete code of maritime and commercial law that was ever attempted to be framed and which, considering the originality and extent of the design, in the opinion of Duer* and other writers on insurance, deserves to be ranked among the noblest works that legislative genius and learning have ever accomplished. The great importance to insurance interests, of this ordinance, or code, lies in the elaborate consideration which is given to insurance practices and the regulation of the business by government. As pointed out by Duer, "Perhaps the most valuable portion of this ordinance is that which relates to insurance, and of this no more striking proof can be given than the results from the fact that the framers of *the present commercial code* of France have adopted these chapters of the ordinance, not merely as a basis, but as the substance of their own labors on the same subject, so that the provisions (relating to insurance) in the two codes are nearly identical."†

* Duer, John, The Law and Practice of Marine Insurance, deduced from a critical examination of the adjudged cases and the general usage of *commercial* nations, Vol., 1, p. 43, N. Y., 1845.

† For a full account of the Ordinance of 1681 see Walford's Ins. Cyclo.' Vol. IV, p. 310; also Park, System of Marine Insurance, 7th ed., Vol. I, p. xxxiii, et seq.

On Contracts Depending on Chance.

Beginning with the 18th Century, the first important work giving a brief consideration to insurance in its relation to commerce, is the classic treatise on the Law of Nature and Nations by Puffendorf, Counsellor of State at one time to the King of Sweden and at another time to the King of Prussia. The first edition was printed in 1712, and the third in 1717.* The work includes a chapter on "Contracts Depending on Chance," the eighth section of which treats of insurance. There occurs therein the following significant passage: "To these contracts, that of insuring bears some affinity; when for a certain sum a man takes upon him the risk that goods are to run in transportation from place to place, usually by sea; which, if they happen to be lost, the insurer is bound to make good." The passage emphasizes the view that insurance not only was considered by this eminent author an element of commerce, but an element of commerce in course of transportation, while the fact that works of this character were translated into English, no doubt, explains, in part at least, the similarity between English and Continental customs and the incorporation into English law and usage of legal provisions which can be traced back to the commercial codes and sea laws of many other and more ancient nations.

First Discussion of Insurance in American Literature.

A few years later [1725] there was published in Philadelphia a tract of great historical value, by Francis Rawle, author, and Benjamin Franklin, printer, with the curious title "Ways and Means for the Inhabitants of Delaware to Become Rich." The tract is referred to in the History of the Insurance Company of North America,† according to which the author

* Of the Law of Nature and Nations, written in Latin by Baron Puffendorf and translated into English by Basil Kennet, D. D., 3rd Ed., London, 1717, Chap. IX on Contracts depending on Chance.

† History of the Insurance Company of North America, Phila., 1885, p. 15.

"classes insurance as a branch of trade, which, while helpful to the adventurer on risks by sea, would as well be *promotive of commerce* and agriculture." The author held the view that, "Having thus far discoursed of most of the branches of trade we are capable of, there is yet one great encouragement, to adventure in the discovery and prosecution of new markets; more safe to the industrious adventurer; namely an insurance office in one or more of these colonies; which is the interesting of divers in the loss or profit of a voyage, and is now become so much the practice of England, that insurance may be had in divers cases as well against the hazards at land, as casualities at sea, which must be acknowledged not only to be safe, but a great encouragement to adventure. ..... This will be good and safe and cannot be easily overset by a few losses; and we conceive will contribute to *keep up the value of our paper credit* by promoting of trade, navigation and building of ships, and in consequence of great advantage to this river: which we confer to the consideration of the merchant."

Early Insurance Advertisements.

This is probably the first reference to insurance practice in American literature, but mention may be made in this connection of the fact that the first advertisement of the opening of an insurance office in this country, that is, in Philadelphia in 1721, was in the American Weekly Mercury, of May 25th of that year, which commences with the significant statement that "Assurances from losses happening at sea, etc., being found to be very much for the ease and benefit of the merchants and traders in general; and whereas the merchants of this city of Philadelphia and other parts have been obliged to send to London for such assurance, which has not only been tedious and troublesome, but even very precarious," it is proposed, etc., etc.*

* History of the Insurance Company of North America, Phila., 1885, p. 15.

Encouragement of Trade by Insurance.

In 1745, John Cary, a merchant of Bristol, England, published an extremely interesting tract* with the title "A Discourse on Trade," which contains an important and extended reference to insurance. Since this tract is almost unknown, the reference to insurance is quoted in full, to explain the views of the author on the necessity of Parliamentary interference with insurance practice, to bring about much needed reforms. After discussing trade in general and the best possible means of bringing about a revival of a declining commerce with other countries, Cary observed with reference to insurance, that:

"I cannot close this discourse without speaking something of insurance. The first design whereof, was to encourage the merchants to export more of our product and manufactures, when they knew how to ease themselves in their adventures, and to bear only such a proportion thereof as they were willing and able to do; but by the irregular practices of some men, this first intention is wholly obviated; who without any interest, have put in early policies, and gotten large subscriptions on ships, only to make advantage by selling them to others; and therefore have industriously promoted false reports, and spread rumours, to the prejudice of the ships and masters, filling men's minds with doubts, whereby the fair trading merchant, when he comes to insure his interest, either can get no one to underwrite, or at such high rates, that he finds it better to buy the other policies at advance; by this means these stock-jobbers of insurance, have, as it were, turned it into a wager, to the great prejudice of trade: likewise many ill-designing men, their policies being over-valued, have (to the abhorence of honest traders, and to the scandal of trade itself) contrived the loss of their own ships. On the other side, the underwriters, when a loss is ever so fairly proved, boggle in their payments, and force the insured to be content with less than their agreements, for fear of engaging themselves in long and chargeable suits.

"Now if the parliament would please to take these things into their consideration, they may reduce insurance to its first

*A Discourse on Trade, by John Cary, a Merchant of Bristol, London, 1745, p. 93; see also Dictionary of Commerce, by Postlethwayt, 2nd Ed., pub. London, 1751, p. 142.

intention, by obliging the insured to bear such a proportionable part of his adventure, (the premio included) as to them shall seem fit, and also the insurers, when a loss is fully made out, to pay their subscriptions without abatement, which will prevent both; and if any differences should arise, to direct easy ways for adjusting them, without attending long issues at law, or being bound up to such nice rules in their proofs, as the affairs of foreign trade will not admit.

"I know, that by a clause in a statute made *prima Annae* the wilful casting away, burning, or otherwise destroying a ship, by any captain, master, mariner, or other officer belonging to it, is made felony, without benefit of clergy; but that statute is so qualified, that it is difficult to convict the offender, because the fact must be done, to the prejudice of the owner, or owners, or of any merchant or merchants that shall load goods thereon, else he doth not come within its penalty, so it doth not reach the evil I here mention, viz., the abominable contrivance of the owners to have their own ships destroyed, in order to make an advantage by their insurances; a crime so black in itself, that it cannot be mentioned without horror. These men, when they frame their dark designs, will take care, for the security of those they employ, that none besides themselves shall load goods on the ships they intend shall be thus destroyed, and it cannot be supposed that they receive prejudice thereby themselves, so the prosecution on that statute is evaded; but if the insured were bound to make out their interests, and to bear a proportionable part of the loss themselves, this would, as it were naturally prevent such scandalous practices."

The Beginning of Insurance Science.

In 1747 there was published in London a very suggestive essay on the Science of Insurance, by Corbyn Morris.* The work is practically limited to a consideration of marine insurance, but with important bearings upon the place of insurance in commercial relations. Insurance is referred to as, "that aid whereby the national commerce is supported." The work of this author confirms the view that insurance at this early period was not only considered an important element of commerce, but was in

* An essay towards illustrating the Science of Insurance by the author of "A Letter of a Bystander," (Corbyn Morris), London, 1747.

fact a distinct means or method whereby a considerable proportion of such commerce was made possible and advisable. In the words of the author, "Insurances give tranquillity and cheerfulness to the extensive trader; these only make it justifiable for him to *venture in many branches of commerce*, which are of great benefit to the nation; these enable him to lay a steady foundation of credit; to procure money upon easy terms, and to bring his goods cheap to foreign markets."* The tract contains many other and decidedly suggestive references to practices of insurance as an aid to commerce and the furtherance of commercial enterprise, at a period of time when such enterprise was particularly exposed to the perils of unknown seas and almost constant war between England and France.

Five years later, that is, in 1752, Wyndham Beawes published his Lex Mercatoria Rediviva, or, A Complete Code of Commercial Law, a second edition of which was printed in London in 1761. Insurance takes up almost sixty pages in this treatise and the references include every branch of the business, too elaborate to be reproduced here but they indicate as clearly as possible that on the part of this distinguished writer insurance was held to be an integral and indispensable element of commerce and commercial intercourse.

Trade and Commerce Defined.

In 1755 Richard Rolt published the first edition of "A New Dictionary of Trade and Commerce," including an explanation of all terms used in commerce, in which he makes extended reference to insurance. He, like many others, drew a distinction between commerce and navigation, which terms by many writers are not used interchangeably, as has since been the case in interpretations of the commerce clause of the Constitution. With reference to navigation and its relation to insurance, Rolt says that "In navigation, considered as a part of the skill of the merchant, is included, not so much the art of

* Science of Insurance, by Corbyn Morris, p. 1, et seq.

steering a ship, as the knowledge of the seacoast and of the different ports to which the cargoes are sent, the customs to be paid, the passes, permissions or certificates to be procured, the hazards of every voyage, *and the rate of insurance.*"*

Rolt gave a definition of commerce which is very broad and comprehensive, namely that "Commerce is the exchange of commodities, or the buying, selling, or trafficking of merchandise, money, *or even paper for acquisition of profit.*" He specifically refers to bills of exchange as commerce, and insurance is defined as " The security given in consideration of a sum of money paid in hand to make good ships, merchandise, and houses, to the value of that for which the premium is received and in case of loss by storm, pirates, fires, and the like." As thus defined, insurance strictly falls within his previous definition of commerce. Referring at the same time to abuses resulting from a miscarriage of effort in the development of insurance practice, he remarks that, " Though insurance was intended for the encouragement and security of trade, it has been frequently changed into a wager, to the great prejudice of commerce." That his conception of the commercial value of insurance was not limited to the marine branch is made evident by a passage which reads that " The establishment of these several offices of insurance from fire had been extremely beneficial to society; nothing was ever so well calculated for the *encouragement of trade*, nor was there ever any scheme so well adapted for the securing of private property."

* In this connection, mention may be made of a discussion of Insurance and Average, in " The Merchants and Shipmasters' Assistant," by Jos. Blunt, New York, 1832, which includes chapters on Bills of Exchange, Freight and Demurrage, Insurance and Average, Pensions, etc. There is also an extended discussion of the Law of Marine Insurance and General Average in " The American Shipmasters' Guide and Commercial Assistant," by Francis G. Clarke, Boston, 1838. But much earlier than this, the subject of Marine Insurance was dealt with at length in " The Practical Navigator," by John Hamilton Moore, 1st American Edition, printed at Newburyport, 1799.

The Foremost of Insurance Classics.

By far the most important treatise ever published on insurance, particularly at a time when a comprehensive treatment of the subject was of imperative importance to aid in the establishment of insurance upon a sound and enduring basis, was the "Essay on Insurance" by Nicholas Magens, a merchant of Hamburg, published in two volumes in 1755. The work will ever remain a classic of the highest merit in insurance literature.*

The first volume explains the nature of the various kinds of insurance practiced by the then commercial States of Europe, and showing their consistency or inconsistency with equity and the public good. The second volume is a collection of all the foreign ordinances of insurances and forms of policies translated into English, with remarks on such parts as are obsolete or defective. An English edition of this work was published in London in 1755, at which time Magens, apparently, was a resident of that city. The first volume contains a brief statement of the principles of business morality, which should not only underlie insurances, but all commercial relations: "The true scope and intention of all well-calculated commercial laws is, to unite the interest of every individual in such a manner, as that the whole community may be induced to act for the general good. If this principle be adhered to, and a due execution of those laws, and an impartial administration of justice, follow; the merchant, who should be considered as the first mover, and the great spring of action in trade, will cheerfully pursue extensive views; and by his fortune, credit, and industry, advance the public weal."

Relation of Early Commerce to Insurance.

The work is of so comprehensive a nature that it is difficult to make a selection of extracts which would do justice to this distinguished writer and his advanced views upon the importance

* An Essay on Insurance by Nicholas Magens, London, 1755, 2 Vols. (This work is in the Ins. Library, Boston, Mass.)

and dignity of insurance as a commercial institution. He discourses, among other subjects, upon the utility of insurance, in language which is full of meaning even at the present time: "*Insurances promote trade* and navigation, as thereby the risks of diligent, industrious, and inventive persons, of small capitals, are so lessened, that they may engage even in important undertakings. It is easily understood how the public are benefited thereby; and by taking such precaution, as making insurance, a greater share of confidence too is acquired among moneyed men, who seeing this wary way of proceeding of the merchant, are the more ready to assist him with their money, or to maintain his credit, by freely taking his bills of exchange. But though this be allowed, yet as the best institutions are subject to abuse, certain bounds and regulations are necessary, which, while they give such latitude as may promote and encourage trade, ought not to be so extremely wide as that ill consequences may ensue. That this consideration should be attended to in enacting all laws and ordinances relating to insurances, is not to be controverted; nor that it should also be had in view, in the explanation and application of those laws to particular cases. In our essay we shall do our utmost to point out, whatever experience has shown to deserve attention, and in what respects there seems to have been either too much, or too little, latitude given." The limitation of space makes it impossible to give additional illustrations from this remarkable work, but it contains by far the soundest reasoning up to that time on the whole question that insurance is an element of commerce by the practice and usage of the commercial nations of the world.

Insurance Essential to Commercial Security.

In 1757 Postlethwayt published the second edition of his Classical Dictionary of Commerce, in two large volumes, chiefly based upon the French Dictionary of Commerce by Savary. From this and the fourth edition of the same work, which was published in 1774, the following extracts are quoted, as illustrating that in the mind of this, one of the foremost writers of

his day, insurance formed an essential element of the commerce of the period. The work, among other subjects, in the words of the author, treats "Of the compilation of annuities on lives, leases and reversions, of insurance of shipping and merchandise, with great variety of curious cases *relating to this essential part of mercantile commerce*—with a political discussion of the point of the insuring the ship and merchandise of commerce in time of war."

The author quotes at length from a Royal Message to Parliament, in 1720, relating to the charter of the Royal Exchange and London Assurance companies, stating in part as follows: "His Majesty having received several petitions from great numbers of the most eminent merchants of the City of London, humbly praying that he would be graciously pleased to grant them letters patent for erecting corporations to assure ships and merchandise . . . . (and) His Majesty being of opinion that erecting two such corporations . . . . for assuring ships and merchandise under proper restrictions and regulations *may be of great advantage and security to the trade and commerce* of the kingdom, is willing and desirous, etc., etc."

Assurance or Insurance.

"Insurancing," he remarks in continuation, is a great *encouragement to foreign commerce*, seeing that it takes the weight of the hazard off from individuals and lays it upon numbers, yet these numbers are, upon the whole, gainers by undertaking the hazard." . . . . "*The security of our trade*, and in consequence thereof lessening our own insurancing and raising that of our enemies are of such important concernment to the nation that it may not be unacceptable to observe how, in time of war with France, a few ships of war may be employed to answer these purposes." "Assurance, or Insurance, *a term in commerce*, particularly foreign. It signifies a security, or assurance, given, in consideration of a sum of money paid, in hand, of so much per cent. to an insurer, or assurer, to indemnify the insured from such losses as shall be specified in

policy of assurance, subscribed by the insurer, or insurers, for that purpose." " This being a point of very great importance to our trading interests, is the reason of dwelling so long upon it; for which we pray rather to have the approbation than censure of our readers. In regard to the nature of insurance in foreign countries, we shall represent them in their proper places." " Bottomry, is *a marine contract in commerce*, for the borrowing of money upon the keel or bottom of a ship; that is to say, when the master of a ship binds the ship itself, that, if the money be not payed by the day appointed, the creditor shall have the said ship; and this taking up money on bottomry is commonly in nature of mortgaging a ship; and, in the instrument executed between the lender and the borrower, there is a clause which expresses, that the ship is engaged for the performance of the same."

This writer also refers to the Act of George II, 1746, relating to insurance, in which occurred the sentence, " For the encouragement of trade." [Vol. 1, p. 146] He also quotes from the famous case of Sadlers Company vs. Badcock,* decided at this time, containing the statement *"and though in cases of commerce* policies of insurance are allowed to be made, etc., etc.," all of which sufficiently confirms the view that Postlethwayt, as well as Savary, considered insurance an element of commerce, even though not perhaps a species of commerce itself.

Development of the Law of Insurance.

The accession of Lord Mansfield to the Court of Kings Bench as Chief Justice, in 1756, marked a new era in English and American insurance law, and the decisions and opinions of this distinguished jurist distinctly stamp the insurance contract as a commercial transaction subject to interpretation by the Law Merchant. No subsequent writer on insurance law has failed to refer in praise to Lord Mansfield for his transcending wisdom

* The case of Sadlers Company vs. Badcock in Chancery, Easter Term, 16 Geo. II, is given in full in Postlethwayt's Dictionary, Vol. I, p. 147.

and discriminating ability, but for the present purpose it must be sufficient to quote a brief extract from Vance,* as bearing upon the definition of insurance as an element of commerce. "This great judge, [Lord Mansfield] appreciating the peculiar circumstances that attended *the making of mercantile contracts*, and the importance of considering the usages and customs of merchants as determining their rights under such contracts, began a consistent effort to import into the common law such of the principles of the Law Merchant as would render the common law suitable for the administration of justice in regard to commercial rights. In order to determine what rules should be applied in deciding these causes, he looked to the various authorities that were in vogue on the Continent, such as have been mentioned above, and also had special juries empaneled to determine the customs of English merchants." And it is to Lord Mansfield that insurance is indebted for the dictum that "All questions of mercantile law, but more particularly of policies of insurance, are extremely important and ought to be settled." The necessity for certainty in legislation and uniformity in rulings and regulations governing insurance transactions was fully as well recognized when this was written, at the very beginning of the modern business of insurance in its various branches, as it is true of the state of the business at the present time.

Bills of Exchange and Promissory Notes.

In 1759, Mr. Thomas Cunningham, of London, published a treatise on "The Laws of Bills of Exchange, Promissory Notes, Bank Notes, and Insurances." The title itself sustains the view that the writer considered insurance as strictly a commercial transaction and by implication an essential and important element of commerce. In fact, writers on the origin and history of bills of exchange often refer to the subject in connection with insurance. Among others, the earlier laws and ordinances of Barcelona, according to Beckmann,† refer to bills of exchange

* Law of Insurance, St. Paul, Minn., 1904, p. 8, et seq.

† Dictionary of Inventions, Vol. II, p. 203.

in a general discussion of "the maritime trade and other branches of commerce." Brokers engaged in joint financial and commercial transactions, as, for illustration, in Philadelphia as early as 1792, often styled themselves "Exchange and Insurance Brokers." In all matters of this kind American commercial practice and usage has largely followed foreign methods. Thus the institution of Lloyds Coffee House, which was the centre of English individual underwriting, was copied in a similar establishment erected in Philadelphia under the title "London Coffee House," in 1762,* and at which the original lists of shipping and marine intelligence, furnished by Lloyds of London, were made available to personal underwriters in Philadelphia.

In the nature of the case, the value of insurance is in exact proportion to the risk assumed. During the last quarter of the 18th Century the most important commercial nations of the world were at war with one another and the American colonies were in successful revolt against the mother country. International commerce and navigation were most hazardous undertakings, for ships and goods were not only exposed to the perils of the sea, but even to the more uncertain and more hazardous risks of capture and destruction by the enemy. Bottomry loans in Massachusetts in 1767 brought twenty per cent., and in Salem in 1777, the rate paid for marine insurance was seventy-five per cent. Laws of shipping and insurance were rather a matter of mercantile custom and of the good faith of the underwriters than of statutory enactment. Fraud was common and the need of codification and of severe penalties was forcibly presented in the masterly treatise of Weskett,† published in 1781. No more elaborate work than this on insurance has appeared since that date. It is a remarkably clear and comprehensive exposition of the principles and practice of insurance in its particular relation to commercial enterprise.

* History of Insurance Company of North America, p. 21, et seq.

† "A Complete Digest of the Theory, Laws, and Practice of Insurance, John Weskett, merchant, London, 1781.

The First Comprehensive Dictionary of Insurance.

The work of Weskett* is practically a comprehensive dictionary of insurance, containing a concise enumeration of all the terms which were in common use at the time, with a full explanation of the practices and usages of every branch of insurance as then known and understood. In an elaborate introduction Weskett presents an outline of the whole philosophy, science and law of insurance, which has not its counterpart in any subsequent treatise upon the subject. The rightful position of insurance as an element of commerce is set forth by Weskett in the following suggestive sentence:

"The great utility of insurance, by means of which the value of property, in almost every situation, howsoever precarious, may be rendered safe against accidents, is so universally acknowledged, that there needs no attempt to prove, or explain it. Commerce is indubitably the grand source, from whence is derived all that enriches, strengthens, and adorns a State. Without an extensive and flourishing commerce, this nation could never have arisen to that superlative degree of grandeur in arts, arms, and wealth, which have made her the envy, and, till lately, the veneration of all other maritime States; and without insurance that commerce could neither have been promoted, nor carried on; nor can it ever proceed, unsupported by insurance; and, consequently, the national, as well as private advantage of well-regulated insurance is obvious and indisputable."

An Early Plea for Insurance Education.

The magnitude of the subject of insurance even at this early time suggested the necessity of qualified inquiry and study of the essential facts. Weskett suggests, therefore, that, in his opinion,

"It would seem, therefore, that little argument is necessary to show that every possible countenance and aid, both public and private, ought to be given to the attainment and culti-

*A Complete Digest of the Theory, Laws, and Practice of Insurance, John Weskett, merchant, London, 1781.

vation of the knowledge and just practice of insurance; as the primary and principal means by which the maritime and commercial interests of these Kingdoms can be maintained, cherished, and enlarged; and the property of the merchants, and, consequently, of all the other traders, manufacturers, and artisans, who depend on, or are immediately connected with them, can be rendered secure and permanent."

The need of qualified inquiry into the principles and philosophy of insurance is further brought out in a sentence which holds as true at the present time as it did at an earlier date.

"There is scarcely any other occupation, or profession, though far more unimportant, and less abstruse or complicate than that of insurance, amongst the whole circle of arts and commerce exercised in this Kingdom, where some method of instruction is not looked upon as requisite; and, where the persons employed in it are not pretty well versed in the grounds and theory, and the greater part of them expert in the practice of the principles on which it ought to be prosecuted:—but, one may venture to assert that in no other class is there to be perceived so great a proportion of a numerous body of practitioners, who are so incompetently skilled in the nature of the matters about which they are occupied, and of the laws and rules by which they ought to be governed, as amongst those who are in the actual employment of, and whose avocations and concerns are immediately connected with, affairs of insurance."

Cognizance in Law of Common Knowledge in Matters of Insurance.

The law of insurance at this time was still in a very unsatisfactory state, but as a general principle the Law Merchant was relied upon to settle controversies between the insurers and the insured. Referring to the legal aspects of insurance in matters of commerce, Weskett remarks:

"From whence is it that the most profound adepts, and sages of the law, derive their fancied superiority of skill, in the rules of justice, in matters of commerce and insurance? Hath it not, always, been from the informations and explanations of experienced and judicious merchants and insurers; from time to time given, in the several cases, which have been introduced,

discussed, and decided in courts of judicature?—and, what lamentable absurdity, and confusion of ideas, might not have been observed, in the argumentations there, upon such matters! —yet, do we not, sometimes, idly look up to, as oracles, those, whom intelligent men amongst ourselves have, in reality, instructed? Those affairs are often accompanied with such new and various circumstances and contingencies; and depend so much upon nice distinctions of special customs and usages; that the common law of England tacitly acknowledges its own imperfection, in this respect, by allowing the Lex Mercatoria, i. e., the custom of merchants,—wherein themselves, only, are properly skilled; and of which, consequently, themselves, only, can be the proper judges,—to pass as law."

Drawbacks and Duties, Smuggling and Piracy.

These and other innumerable remarks and observations by Weskett fully establish the strictly commercial origin of insurance and its great utility in the commercial development of the period. Among the particular subjects considered in much detail are the insurance aspects of drawbacks and duties on goods and freight, of robbery of goods insured, of smuggling and prohibited goods, all involving insurance considerations, some of which are now obsolete or mere matters of curiosity. Considering always the disturbed condition of the time and almost unceasing warfare between great nations, the insecurity of the sea, the widespread practice of smuggling and the arbitrary enforcement of ill-advised commercial regulations, it is but natural that the necessary degree of security against probable loss in commercial enterprises of many kinds should have been sought in the practice of insurance.

Questions of piracy, ransom, letters of marque, neutral ships, passports and hostage, all had their important insurance aspects, made evident not only by the theoretical discussions, but by the numerous cases decided in courts of law. In the case of Goss vs. Withers, Lord Mansfield said that in Spain, Venice and England the goods go to the captor of a pirate, against the owner, as there can be no condemnation to entitle the pirate; a capture by a pirate, or a capture under a commission, where

there is no war, does not change the property; yet, as between insurer and insured, they are just upon the same foot as the captures by an enemy. It was then the practice to insure against the loss of personal freedom through capture by pirates and the Ordinance of France permitted this to be done, providing that "Those who shall redeem captives may insure on them the price of their ransom, which the insurers shall pay if on their way back they should be re-taken, killed, drowned, or if they die otherwise than by a natural death."

Privateering and Rates of Insurance.

The common practice of privateering during a time of maritime war often led to disastrous results to shipping, which required the extensive use of maritime insurance to grant the necessary degree of security to commerce by sea. Privateers being private ships of war fitted out for the particular purpose of destroying the commerce of the enemy and subject only to the law of nations, more or less ill-defined, it was permitted by an English statute to make "assurance on private ships of war fitted out by His Majesty's subjects solely to cruise against his enemies, and such assurances might be made by or for the owners, interest or no interest, free of average, and without benefit of salvage to the insurer."* Endless complications ensued out of this practice, chiefly because of a disputed state of fact, always more or less difficult to determine even by the most searching inquiry. A discussion of the proper function of insurance in maritime war would require separate and extended consideration. The subject has found its most practical illustration in the so-called French Spoliation Cases, a large number of which involved considerations of insurance.†

* Statute 19, George II, chap. 37, sec. 2; see Weskett, p. 413.

† For a full and very convenient account of the French Spoliation Claims, with special reference to insurance companies, see "Statements and Papers before the Committee on Claims of the House of Representatives, on House Bill 22534, 61st Congress, 2nd Session, March 30, 1910, including statement of J. Henry Scattergood, President of the

The Liverpool Privateers.

The distinction between piracy and privateering is never very precise, at least not in many of the cases which have found their ultimate settlement in the courts. In no field has this been more clearly brought out than in the history of the privateers and the slave trade of Liverpool during the period beginning with 1744 and ending with 1812. The law of prizes makes the distinction of ships and goods taken by letters of marque, those taken from pirates or sea rovers, and those taken from professed enemies. The jurisdiction of such cases comes within the practice of the courts of admiralty which from the earliest times have taken cognizance of insurance. The Ordinances of Hamburg provided that "Any person who in time of war buys a prize, that has not yet been in any free or neutral river or port, and makes insurance on the same, is obliged to express that circumstance in the policy, for want thereof, the insurance shall be deemed to have no efficacy or value." Even the question of re-capture, that is, where a ship in her voyage happens to be taken by an enemy, and afterwards is re-taken by another ship in amity and restoration is made and she proceeds on her voyage, frequently involved considerations of insurance, as brought out in the case of Pringle vs. Hartly, decided as early as 1744.*

Insurance on Trade With the Enemy.

War in every case has the most profound and immediate effects on commerce, disturbing, as it does, the friendly relations of nations and leading to prohibition of intercourse, embargo acts, etc. What constitutes a state of war is sometimes very difficult of exact definition, never so well illustrated as in the case of our own French Spoliation cases, which occurred

Insurance Company of the State of Pennsylvania, and Bayard Henry, Attorney for Directors of the Insurance Company of North America," Washington, Government Printing Office, 1910.

* The case of Pringle vs. Hartley is discussed in Park's "System of the Law of Marine Insurance," 7th Edition, Vol. I, p. 232.

without a specific declaration of war against France. Insurance on any trade with the enemy, or insurance on prohibited goods, is contrary to public policy, and expressed in the principle that "This interdiction of commerce with enemies comprehends also the prohibition of insuring the effects which belong to them, whether they be loaded on board their own vessels, or those of friends, allies, or neutral subjects; for to insure the property of enemies, or to trade with them directly or indirectly is, in effect, the same thing." This principle, derived from the French Ordinances of commerce and marine, was not accepted by England in the war of 1756, when it was held that England "would not consider the prohibition of insurance as necessarily included in that of commerce," since they constantly insured French ships and their cargoes as in time of peace, whether they were destined for the French colonies, or any other ports of France, or those of neutral nations." This, however did not prevent the captured ships from being declared good prizes, but the result of it was, in the words of a French commentator, that, "one part of the nation restored, by the effect of insurance, what the other took away by the right of war." Naturally considerations of this kind include the whole subject of contraband goods and the principle that free goods make free ships. Within more recent times the foregoing considerations have found their application to concrete problems arising out of the War of the Rebellion, the Alabama Claims, and the results of the war between Russia and Japan. Reference may here be made to the case of Richardson vs. Maine Insurance Company, decided in 1809, in which the American doctrine of insurance in its relation to commerce in war is clearly defined. The subject itself is one of much controversy, but for the present purpose it is sufficient to have brought out the very intimate relation which has ever existed and ever will exist between the practice of insurance and the carrying on of international commerce during a time of maritime war.

The great work of Weskett, from which most of the immediately preceding observations and conclusions have been

derived, was, in 1787, followed by a treatise entitled "A Statement of the Law of Marine Insurance, with Chapters on Bottomry, etc.," by Mr. James Allan Park. This work was the first comprehensive and systematic dissertation on the law of insurance in England, and a standard authority for many years in the United States. An advertisement in the American newspapers of the period, inviting proposals to print an American edition of this work, contains the statement that it was the most complete work on the subject and that it contained all the important decisions ever made in England on insurance.*

First Systematic Treatise on Insurance Law.

John Duer, one of the foremost American authorities on the law and practice of marine insurance, writing in 1845, observed with reference to the work of Park, that it was entitled "to the praise of being the first endeavor to reduce the English law of insurance to the order of a regular science." The far-reaching influence of this work on American judicial practice is made evident by frequent references to this authority in cases decided in American courts. Written at a time when the law of insurance itself was in a much more formative state than it is now, the influence of Park was naturally very great. Available at the period when the American constitution was under consideration, and when by every authority of the day insurance was considered an element of commerce and an integral part thereof, the following remarks therefrom on the commercial aspects of insurance and its relation to the commercial transactions of the period are decidedly suggestive.

" In most of the *commercial* countries abroad, it is particularly expressed, either in their ordinances or policies, and sometimes in both, that the risk of the insurers shall commence, the moment the goods quit the shore, and shall continue till they are landed at the place of their destination. ..... "†

* "Account of the Early Insurance Offices in Massachusetts from 1728 to 1801," by E. R. Hardy, Boston, 1901, p. 90.

† Park, System of the Law of Marine Ins., 7th Ed., Vol. I, p. 28.

"It should seem, that by the common law and *usage of merchants*, any person whatever might be an insurer, however unable he might be, from poverty, to make up the losses insured against, provided the merchant was weak enough to trust to such a security. In process of time, however, there were so many who made a show of great wealth, in order to deceive the honest and unsuspicious trader out of his premiums, and who were in insolvent circumstances, that it became an object of *national concern, and parliamentary interference*. The mischiefs then existing *in this branch of trade*, and the dangerous consequences thence arising to the interests of the country, are to be collected from the preamble of the statute, which passed in the reign of George the First, to remedy these evils, and which has in some, though not in any great degree, restrained the rule of the common law as to the unlimited right any man or body of men had to become insurers."*

Insurance in Naval and Commercial Jurisprudence.

Park having, no doubt, made a careful study of the French ordinances of commerce and marine enacted during the reign of Louis XIV, under the auspices of Colbert, as minister of finance, refers to these codes and their authors, as follows: "In order to gain a proper insight into the *true effects of commerce* upon the various nations of the world, and the advantages of some particular branches of trade, he procured and employed learned and diligent men to inquire into the commercial histories of cities long since destroyed, and the nature of the climate, soil and productions of the countries then rising into notice. It was to this spirit of inquiry in this famous statesman [Colbert], that the world is indebted, as appears from the dedication, for that very masterly performance upon the commerce and navigation of the ancients, written by Huet, Bishop of Avranches and Soissons, who is justly entitled to a high rank among men of letters. Colbert having thus made use of the

* 6 George I, Chap. 18. See 7th Edition, Park, "A System of the Law of Marine Insurances," Vol. I, p. 5.

labors of others in order to gain useful information, undertook to restore the navy and commerce of France; and he completed all his services by the publication of that ancient body of sea laws known by the name of the Ordinances of Louis XIV, which comprehended everything relating to naval or commercial jurisprudence; and *of which the doctrine of insurances* forms a *considerable part.* To its merit all Europe has borne testimony; and the name of Colbert must ever be mentioned with respect, when the Ordinances of Louis XIV are the subject of conversation."*

While the work of Park became most widely known, there was published, however, during the same year an equally important treatise on the elements of law relating to insurance, by John Millar, of Edinburgh, which contains some very important observations on the relation of insurance to commerce. As observed by this author, the progress of commercial improvement has been accompanied by a corresponding extension of mercantile law, leading first to the regulation of navigation only, but at a subsequent period to the regulation of insurance and other maritime contracts. He remarks that "the utility of a contract of this nature in commercial nations is great and strong. The underwriter who promises to be responsible for the danger attending the conduct of any branch of trade receives a consideration proportionate to the risk he undertakes and, therefore, derives a reasonable profit from that employment of stock. On the other hand, the merchant, by abandoning a share of his expected gain is freed from the apprehension of a loss that might be ruinous to him. The underwriter is thus enabled to participate in the profits of every different concern. He becomes a sort of temporary partner of the most extensive trading companies." Recognizing the important relation of insurance to the general welfare, the author observes, in continuation of the preceding remarks, that "Insurance is no less advantageous to the public than to individuals by modifying and diffusing the profits of trade and by preventing

* Park, System of the Law of Marine Ins., 7th Ed., Vol. I, p. xxxiv.

incidental misfortunes from operating to the ruin of individuals or companies of merchants which might obstruct the uniform progress of commerce and endanger public credit."

Insurance in Actual Commerce.

Outside of the field of law and legal controversies arising out of differences of opinions regarding the nature and effects of the insurance contract, there is abundant evidence in the every-day commercial transactions of the period and the commentaries on commercial practice, that insurance in the minds of merchants was never separated from the subject of commerce itself. In 1788 there was published in Edinburgh an interesting "Introduction to Merchandise," by Robt. Hamilton, which includes an account of the trade of Great Britain and the laws and practice relating to sale, factorage, insurance, bills of exchange, bankruptcy, etc. Insurance is defined as "a contract whereby one party engages to pay the loss which the other may sustain for a stipulated premium or consideration. The most common sorts are insurance against the dangers of the sea, insurance against fire, insurance of debts, and insurance on lives." Bottomry bonds are defined as contracts partly in the nature of borrowing on interest and partly in the nature of insurance. Respondentia contracts are defined as being of the same kind, but secured on goods instead of the ship, the condition of re-payment being that the goods did not perish through the hazards of the sea. The observations include calculations of cases in actual practice, a brief discussion of the doctrine of chances and annuities on lives. The volume makes it evident that the commercial education of men at this early period was not considered complete without an understanding of the fundamental principles of insurance, of the theory of insurance in all its branches, and the application of established principles to everyday practice, and the law of the subject as determined by the courts.*

* For an interesting illustration of the place of insurance in actual commerce, reference may be made to "A New and Easy Method of

The Insurance Company of North America.

Marine insurance in America previous to the Revolution was exclusively a matter of individual underwriting and it was not until 1792 that the first association was formed originally with the title of the Universal Tontine, subsequently changed to that of the Insurance Company of North America. In agitating for the organization of a *corporation*, one of the promoters pointed out that his extended experience as a policy-holder entitled him to foresee the great possibilities of a large association engaging in the business of underwriting the ventures of American citizens in the growing commerce of the port of Philadelphia. Attention was directed to the frequency of defalcation on the part of individual underwriters and the superior value of a well-established corporation with a sufficient capital. Individual underwriting as it had become well-established in London at Lloyds' Coffee House, found its counterpart in America, where certainly as early as 1762 advertisements gave public notice of the opening in Philadelphia of an insurance office for insuring shipping and merchandise at the London Coffee House. As early as 1759, there was in New York an insurance office at a house adjoining the Merchants' Coffee House, where risks were advertised to be underwritten at moderate premiums. Gradually competition increased and a lowering of rates resulted in the underwriter's inability to meet his losses. That the practice of underwriting in America at this early date was quite extensive is made conclusively evident by the collection of manuscript data, including insurance books and papers, preserved by the Pennsylvania Historical Society, and covering underwriting accounts from 1768 to 1774.

The petition in 1793 to incorporate an insurance company was promptly acted upon by the General Assembly of Pennsylvania and in a report of a special committee appointed to consider the matter, occurs the important and extremely suggestive statement,

Bookkeeping; or, Instructions for a Methodical Keeping of Commercial Accounts," by Alexander Brodie, London, 1722, which gives numerous illustrations of the place of insurance in actual commerce.

that "no commerce or navigation could be beneficially conducted without insurance, nobody choosing to commit considerable property to the ocean without guarding against the numerous accidents to which it would be thereby exposed." The opposition of private underwriters prevailed to delay favorable action, but a charter was finally granted after a further report had been made by a committee of the Legislature, which, among other interesting observations, states that "As it is impossible for a merchant with safety to hazard unprotected his property on so uncertain an element as water, which is so liable to prejudice or endanger it, it becomes essential to the farmer, miller, or manufacturer, that he should insure it. Insurance is an undertaking on the part of one or more individuals, in proportions to the sums they respectively take or subscribe, to bear harmless the merchants in their export trade. *The cheaper insurance is done, the better price the farmer or manufacturer will obtain;* for this being one of the charges in transportation of the surplus it must, of necessity, be understood or reckoned in the valuation of it." No argument in favor of the contention that insurance is an element of commerce and an integral part thereof, could be framed in more concise and convincing language than this plea, written in 1794, or five years after the adoption of the Constitution.

The French Spoliation Cases.

The charter establishing the Insurance Company of North America was granted on the first of April, 1794. From that date to this the history of the company has been one of the most honorable in the annals of American commerce and insurance. From the outset the corporation became an influential factor in promoting American commercial enterprise at a time of great peril, not only arising out of the dangers of navigation, but even more so out of the almost world-wide state of war. As the result of the war between England and France, in which the United States assumed a position of neutrality, enormous depredations were committed upon American commerce by

French men-of-war and privateers, which the nation at that time was not in a position to prevent. After the close of the war in 1801 a settlement was made by offsetting joint liabilities on the part of France and the United States, in return for which the latter assumed the obligation towards its citizens to make ample restitution for the losses sustained as the result of French depredations. These claims have gone down in history as the French Spoliation Claims, with a literature of their own and innumerable Congressional considerations extending throughout the long intervening period of time.

The bearing which these claims have on the subject of insurance, which in most cases covered the ship and its cargo unlawfully seized, is partly made evident in the practical difficulties confronting the Insurance Company of North America, arising out of a state of war, which at times imperiled its very existence. The losses sustained by the company were extremely heavy and the slow communications made it impossible to estimate with accuracy the actual liabilities incurred. The company accordingly appointed a committee to confer with the Insurance Company of the State of Pennsylvania and private underwriters, to consider what steps were necessary to jointly protect their respective interests, and at a subsequent meeting it was decided to decline thereafter the underwriting of any marine risk, excepting peace risks, and upon the condition that this action be adopted by the other insurers in Philadelphia. The recommendation was not carried into effect and on October 8th, 1795, a committee was appointed to wait upon the Secretary of State, to ascertain the true state of affairs. On June 19th, 1798, it was agreed not to insure to French ports, except with a warranty against capture and seizure by the French. The total amount of the losses incurred by the company on this account were estimated at nearly two million dollars. One hundred and ten years have passed and these claims have not as yet been all disposed of. The history of the Insurance Company of North America, and the Insurance Company of the State of Pennsylvania, however, very forcibly illus-

trate the close connection existing at this early date between the carrying on of commerce by sea during a time of war and the secure protection of such commerce by insurance.

Insurance in the Diplomatic Correspondence of the Revolution.

It is not only, however, from the records of the Insurance Company of North America that evidence is available to prove the commercial aspect of insurance during the revolutionary period of the seventeen years following the peace of 1783. In the diplomatic correspondence of the Revolution are to be found various references to insurance and, among others, a letter dated August 18th, 1776, by Silas Deane, written from Paris to the Committee on Secret Correspondence, which contains the interesting statement that insurance from London to Jamaica was 20%. In a subsequent letter, dated October 29th, 1776, Deane wrote to the Committee on Secret Correspondence, also from Paris, that "The appearance of American cruisers in those seas (that is, near the coast of France) has amazed the British merchants and insurance will now be on the whole establishment. This will give the rival nations a great superiority in commerce, of which they cannot be insensible." Very much to the same effect is a statement in a letter from Arthur Lee, written from Philadelphia under date of September 9th, 1777, to the Committee of Foreign Affairs. After referring to the effect on British commerce of American cruisers, and the necessity on the part of British merchants to carry on their commerce with other nations in neutral bottoms, and the expedients to screen their merchandise in this manner, Lee remarks, "I say screen, because they cannot expect that, according to the law of nations, it will be a protection when discovered. They have been driven to this necessity by the number of successes of these (American) cruisers in and about the channel; which has raised insurance so high that their manufactures are in danger of being augmented thereby, in their price, too mnch for the European markets." Here, again, in language as con-

cise as it can be expressed, the fact of insurance as an element of commerce is clearly emphasized as a matter of practical experience in commercial affairs.

A comprehensive review of insurance as an element of early commerce would extend far beyond the present purpose. As pointed out in the comments upon the work of Weskett, insurance is more or less an element, or factor, in all that pertains to commercial development and intercourse during times of peace or war. The subject of French Spoliation alone furnishes a most fruitful source of information, warranting the conclusion that early American commerce could not have been carried on as it was carried on, nor could it have attained to the dignity of a great carrying trade if it had not been for marine insurance. This principle is clearly enunciated in international law, where insurance has often figured as an essential element in commercial disputes arising out of international conflicts or misunderstandings.

Insurance in International Arbitrations.

John Bassett Moore in his History and Digest of International Arbitrations to which the United States has been a Party, with reference to the "French Indemnity of 1831," wrote that

> "The principal cases in which claims were held to have been invalidated by the claimants themselves were those in which there was an omission to seek the relief provided by the convention of 1800, either by failure to bring the case before the proper tribunal or to produce the necessary proofs, or in which the claimant had accepted an indemnity, though an insufficient one, from France; or, most numerous of all, in which the loss was borne by insurers. In the last case the insurer was treated as having acquired *pro tanto* an interest in the fund; but if he happened to be a foreigner he was held to be excluded by alienage, and his payment for the loss operated as 'an absolute relief to the fund.'" (Vol. V, p. 4481).

The Case of the Schooner Polly.

The bearing of these considerations, which are amplified in the treatise referred to, is brought out in the numerous

cases of French Spoliations, individually considered, of which the following may serve as a typical illustration: The Schooner Polly sailed on a commercial voyage from Boston, Mass., on the 13th day of May, 1799, bound for Jamaica. While peacefully pursuing said voyage she was seized on the high seas, on or about the 10th day of June following by the French Letter of Marque Clementine of Guadaloupe and a prize crew placed on board with orders to conduct said vessel to Porto Rico. On the next day the Polly was recaptured from the French by British vessels and carried to the Island of Tortola and condemned by the court of Vice-Admiralty held in the Road Town of said island, to pay a salvage of one-sixth of the gross value of said vessel and cargo, together with costs. Thereafter in pursuance of said decree said vessel and cargo were sold, the amount realized after payment of salvage and expenses being $3,546.11. The Polly was a duly registered vessel of the United States and was built in the year 1798 and owned by citizens in the United States residing in Massachusetts. The cargo consisted of miscellaneous merchandise and the losses to the owners by reason of the seizure of vessel and cargo were estimated at $10,875.02, of which $925.00 represented the premium paid for insurance. Deducting from this sum the $3,546.11 received from the sale of the vessel after paying salvage and costs, and the insurance received from the insuring underwriters, amounting to $4,794.45, the net loss to the owners of ship and cargo was, therefore, $2,534.46. The policy of insurance was an underwriter's contract in return for a premium of 10%. The chief loss, therefore, fell upon the insurers, claim having been brought under the French Spoliation Act of 1885 by the heirs of the persons who suffered loss through the capture of the Polly and it having been specifically stated in the claim that the claimants in their respective capacity as owners of said claim disavowed any claims on account of insurance paid. The decision of the Court, filed on March 31st, 1902, was that "The Court decides as conclusions of law that it does not appear that the said seizure was illegal and

that the owners and insurers had no valid claim for indemnity therefor upon the French government prior to the ratification of the contention between the United States and the French Republic, concluded on the 30th day of September, 1800, and that the claimants are not entitled to recover from the United States."

Insurance as an Element of Ancient and Modern Commerce.

Cases like the foregoing clearly illustrate the commercial aspects of insurance, particularly in a time of war. It is absolutely certain that without insurance such commerce as is represented by cases of this kind would not have been carried on at all, in that no considerations of profit to be earned on sales to be made would be sufficiently attractive to balance the enormous risk incurred by the perils of the sea and possible capture by the enemy. In consideration of a moderate premium of only 10% this particular transaction was undertaken as a matter of commerce and the insurance consideration constitutes, therefore, an essential element of the transaction as a whole. What is true of the commerce in time of war at the end of the eighteenth century is equally true of commerce on an extensive scale throughout the whole recorded period since insurance first was introduced in the form of bottomry loans during the times of the Rhodians. What is true of insurance as an element of commerce during the revolutionary war and the depredations upon American commerce during the war between England and France, is equally true of insurance as an element of commerce throughout the whole subsequent history of commercial development. In fact, the difficulty of establishing this contention is not the paucity but rather the preponderating mass of material, consisting of commercial documents, commercial transactions, treaties, negotiations, and even considerations of values and drawbacks, fees and bills of lading, as well as commercial credit in every form as it has been perfected within modern times. When, there-

fore, Alexander Hamilton, in 1791 included policies of insurance as matters of commerce which might be regulated by the Federal government, he spoke with a perfect knowledge of the standard authorities of the day on both commerce and insurance.* That Hamilton was fully familiar with these works is made evident by the fact that in his pay-book, which he kept as Commander of the State Company of Artillery (1776), there are numerous notes concerning the books which made up his library, and among these he mentions Lex Mercatoria, Ralt's Dictionary of Trade and Commerce, Postlethwayt, and Dr. Halley's Table of Observations, including comments by himself. The modern mind, no doubt, yields itself with great reluctance to a painstaking inquiry of this kind, but it is no less a duty to establish the truth in a matter of business history and methods than in the numerous and much more conflicting and

* Hamilton's Official Opinion as Secretary of the Treasury on the Constitutionality of a United States Bank has been reprinted in full in "Legal Masterpieces," edited by vanVechten Veeder, Vol. I, St. Paul, Minn., p. 214, et seq. The qualifications of Hamilton as a lawyer familiar with the subject of insurance are concisely set forth in the following passage in Kent's "Commentaries on American Law": "Maritime law in these states became early and anxiously an object of professional research. It we take the reports of New York in chronological order, we shall find that the first five volumes occupy the period when Alexander Hamilton was a leading advocate at our bar. That accomplished lawyer (for it is in that character only that I am now permitted to refer to him) showed, by his precepts and practice, the value to be placed on the decisions of Lord Mansfield. He was well acquainted with the productions of Valin and Emerigon; and if he be not truly one of the founders of the commercial law of this state he may at least be considered as among the earliest of those jurists who recommended those authors to the notice of the profession, and rendered the study and citation of them popular and familiar. His arguments on commercial as well as on other questions were remarkable for freedom and energy; and he was eminently distinguished for completely exhausting every subject which he discussed, and leaving no argument or objection on the adverse side unnoticed and unanswered. He traced doctrines to their source, or probed them to their foundations, and at the same time paid the highest deference and respect to sound authority."

14th Ed., Vol. 3, p. 21.

far less practical matters of historical research for its own sake. For this reason, and in behalf of the truth of history, these facts have here been brought together from authentic sources of the highest rank, to establish beyond controversy the fact that in the commerce and commercial intercourse preceding the adoption of the American constitution insurance was held to be an element of commerce, an instrumentality thereof and an all-important part, without which such commerce or commercial intercourse and subsequent commercial development would not have been possible. There is nothing in the subsequent history of a hundred and twenty years of American and international commerce to disprove the contention that insurance holds to-day, as in the past, an important place in commercial enterprize and that it is, in theory and in fact, an essential element and instrumentality thereof.

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CHAPTER IV

THE ORIGIN AND GROWTH OF LAW AND LEGISLATION ON INSURANCE.

Insurance, in all its branches, is today an indispensable element of social and economic security and progress. The business, within the last half-century, has attained to such enormous proportions that its effective supervision and control has become a matter of serious government concern throughout the world. It requires no extended inquiry into the underlying principles of insurance to establish the fact that while insurance policies are, like ordinary contracts, enforcible at law, they have the essential characteristic that the subject matter, or a material part of it, "is within the peculiar knowledge of one of the parties" and that "the other party must rely to a considerable extent upon the statements made by him." * The fundamental principle which governs in modern conceptions of State supervision and control of insurance transactions was laid down by the Select Committee of the House of Commons on Assurance Associations, made to Parliament in 1853. It was said in this report that

" On the one hand, even admitting the general wisdom of the principle of non-interference on the part of the Government in matters of trade, it has been contended that the question of life insurance differs so materially in its general character from ordinary trading transactions, that it may fairly be considered as an exception to that rule. This exceptional treatment has been justified and supported, on the ground that the obligations undertaken by such associations have reference to a very remote and uncertain period; that the object which persons have in view in effecting insurances upon their lives, is generally of an

* Principles of Contract, by R. M. Benjamin, 1889, p. 72.

important and solemn character, viz., the provision for widows and orphans after the death of their natural protectors; that, unlike any other transaction of trade, a contract once entered into cannot be discharged or abandoned, if doubts of the stability of an office should arise, without a great sacrifice of premiums paid in past years, and the necessity of effecting new policies in other offices at increased rates of premium, owing to the greater age of the assured; and that in the present state of uncertainty which arises from the imperfect knowledge as to the real condition of assurance offices, persons are thus placed in the anxious and unhappy dilemma of being compelled to persevere in paying premiums from year to year, with some suspicion and doubt as to the ultimate advantage of doing so, or of incurring the serious loss which, under the most favorable circumstances, must attend the abandonment or sale of a policy. On these conditions, as a special case, it has been contended by different witnesses of great experience, that interference on the part of the Government is not only justifiable, but a matter of high duty, for the protection and information of the public."

While it may be contended to the contrary, that the business of insurance forms no exception to ordinary trading transactions, the foregoing view has prevailed, and rightly so, in the public regulation of the business by the several states in the United States and by the supreme authority of other governments throughout the world.

Exceptional Nature of Insurance Contracts.

Insurance contracts are properly held to be of a fiduciary nature and they are in law said to be *uberrimae fidei* or agreements of the most perfect good faith. In contracts or agreements of this nature it is assumed as a first consideration that nothing is concealed and particularly in insurance it is a principle of law that "the insured must preserve the most perfect good faith toward the insurer." The contractual relations of the parties in insurance involve the highest considerations of public policy and these from the earliest times have warranted or justified a more or less drastic degree of governmental supervision, interference and control. The ultimate fulfillment

of deferred pecuniary obligations of this kind demands at the outset some evidence of financial responsibility in the assumption of a risk and at least a reasonable certainty of faithful stewardship of the funds accumulated for the security of the insured. Since insurance, as the term is now understood, originated in the practice of individual underwriting, or the assumption of maritime risk on the part of financially responsible individuals, the earlier and more primitive practice led frequently to disputes at law and to the serious disappointment of the insured as the result of financial irresponsibility of the insurers. The practice of insurance, particularly in early times and especially in the marine branch of the business, also offered peculiar opportunities for fraud and even crime, which accounts for the deliberate interference of government, almost from the time of the inception of the insurance contract, in determining the contractual relations of parties, as well as the nature, function and purpose of the contract itself.*

Long before the insurance contract, as now in use, had been perfected to a degree of practical utility in the further-

* In connection with an historical inquiry into the commercial law of the ancient Hebrews, the following expression of law concerning insurance as an element of mercantile progress was discovered in the Babylonian Talmud, published about 500 A. D., by one of the contributors to the Jewish Encyclopaedia:

"Our Sages have taught: When a ship goes upon the sea and a squall strikes her, and, in order to lighten her, they throw some of the cargo overboard, they make their calculation not according to the money value, but according to the weight of the different goods, and they should not depart from the custom of skippers; *and skippers have the right to contract*, that whosoever vessel is lost, they will find him a new vessel; but if it be lost through his fault, they do not find another vessel for him, nor if he deviates into a course on which it is not customary for vessels to go."

The Babylonian Talmud is a current discussion about the Mishna, a compilation made by the Patriarch Rabbi Jehudah in North Palestine about 210 or 220 A. D., of the traditional or "Oral Law" as taught in Palestine down to his time.

The foregoing was contributed in a letter to the New York *Evening Post*, Oct. 5, 1902, by L. N. D.

ance of merchant adventures, a somewhat similar form of contract, known as bottomry loans and respondentia bonds, had been in use, from time out of mind, among the trading nations of antiquity. Bottomry bonds are in the nature of a mortgage, by which the owner of a ship, or the master as his agent, borrows money for the use of the ship, or for a specified voyage, or for a definite period, and he pledges the ship, or the keel, or bottom of the ship, as a security for its repayment, with maritime or extraordinary interest, on account of the marine risk to be borne by the lender, it being stipulated in contracts of this kind that if the ship be lost in the course of a specified voyage, or during a limited time, by any of the perils enumerated in the contract, the lender shall also lose his money. Because of the great risk incurred in contracts of this nature, absolutely essential and indispensable to the furtherance of commerce by sea in early times, the rate of interest allowed was considerably in excess of the legal rates of interest, subject later to the limitations of the usury law.

Papal Decree Prohibiting Bottomry Loans.

On this account, bottomry loans came into conflict with the usury laws of the Catholic Church and as early as 1227 A. D. there is record of a papal decree prohibiting bottomry loans, as contrary to the principles of the canon law. Since bottomry loans are strictly within the definition of insurance contracts, this decree may be accepted as the first authentic instance of government interference and regulation of insurance contracts. The view, however, which the early ecclesiastical authorities assumed in this matter was opposed to commercial practice and usage, for it was held that "bottomry is not a communication for the loan of money, but a partnership for the honest intention of seeking a livelihood by trade," and that, therefore, "no contract is usurious where the lender runs the hazard of losing all his money, both principal and interest,

as in the case of bottomry." * Bottomry bonds are of very limited utility today, but other forms of insurance contracts have become universal instrumentalities of social and commercial progress throughout the world. The principle established in prohibiting by papal decree the issuance of insurance contracts, considered contrary to public policy, is fundamentally the same which underlies all subsequent laws and legislation affecting the business of insurance. Unfortunately, the early history of insurance is shrouded in much mystery and only fragmentary accounts and records now remain. The documentary proof of early insurance contracts has only been preserved in a few isolated instances and the ancient laws and ordinances are not extant in their completeness, nor do they seem to have been subjected to a thorough critical examination by qualified experts familiar with insurance terms and usages which, naturally, during the long intervening period have undergone material and even quite radical changes.

Early Laws and Ordinances.

The history of insurance, in fact, cannot be read apart and distinct from the history of commerce and navigation, nor, in fact, from the history of the legal and economic progress of civilized nations during ancient and modern times. Laws and ordinances of the fourteenth and fifteenth centuries, for illustration, which have reference to the insurance contract and which constitute an early though primitive attempt at government regulation, are difficult of exact interpretation from modern standpoints, as to the responsibility of government in its relation to insurance interests.† The fact must never be lost sight of, that the practice of individual underwriting was not replaced by corporate underwriting until the beginning of the eighteenth century and that, therefore, early statutory requirements have reference rather to the conduct of

* Blydenburgh on Usury, p. 33. See also Blackstone's Commentaries, Book II, Chap. XXX; and Fowler's History of Insurance, p. viii, note.

† In this connection see Martin's History of Lloyds, p. 27, et seq.

individuals than to business undertakings, such as are typical of our insurance companies today. The early Florentine statute, for illustration, which has been preserved* and in which there is an attempt to regulate or define the insurance contract by law, is not necessarily the first effort in this direction, but it is suggestive that at the beginning of the fourteenth century the business of insurance had attained to sufficient proportions to attract the attention of government and lead to restrictive regulating enactments, more or less of an interference with the freedom of contract and the unrestrained development of business enterprise.

Chambers of Insurances.

As early as 1310 there was a Chamber of Insurances established by the Count of Flanders, at Bruges at the request of the merchants of that city. Chambers of insurances were more or less in the nature of societies or assemblies of merchants, traders, bankers and others, carrying on the business of insurance, acting under conditional government authority, or having the sanction of the proper authorities, for, as observed by Weskett, since undertakings of this kind "were not authorized by the King's Letters Patent, they had but little credit and their policies were neither many nor for considerable sums." †

Ordinances of Barcelona.

In the year 1367 King Ferdinand of Portugal decreed an ordinance on insurance, which takes rank as one of the very earliest efforts at government regulation, followed nearly seventy years later by the enactment of the five famous ordinances of Barcelona, passed in the year 1435. The distinctive feature of these and numerous subsequent ordinances is the underlying principle of government control over the terms and uses

* The marine policy established by the Statute of Florence, dated Jan. 28, 1523, has been re-printed in full in a Treatise on the Law of Insurance, by Geo. Richards, 3rd Ed., New York, 1909, p. 766.

† John Weskett, Theory, Laws and Practice of Insurance, London, 1781, p. 89.

of the insurance contract, which may be said to underlie all modern legislation, except, of course, that the principle of public control has been enormously extended, co-incident with the corresponding growth of the business. It is significant, however, that even at a period when the actual extent of insurance transactions must have been quite limited, public ordinances more or less regulating the issue of insurance contracts and their official registration for authentication, should have been found necessary. It is maintained by Reatz, a German writer on insurance, that the Ordinance of King Ferdinand of Portugal was really for the purpose of establishing a compulsory insurance association upon the principle of mutuality. All of these early efforts, of course, have reference only to the business of marine insurance, since life, fire, or other forms of insurance were at that time practically unknown." *

Early Records of Insurance Transactions.

The business of individual underwriting was at this time almost exclusively confined to the seaport towns, which accounts for the fact that insurance or cognate subjects are usually included within the provisions of the ancient codes of maritime commerce or the sea laws. Such inclusion, of course, arises out of the necessity of jettison and the resulting practice of contribution out of which the principles of average and marine insurance were developed in the course of time. Although the business of insurance was of comparatively limited extent, there are records to prove that as early as 1370 there were numerous insurance contracts in the nature of individual underwriting in force between the merchants of Genoa, Italy, and Bruges, in the Netherlands, while there is a record of 1399 proving that during the short period of August to September a notary of Genoa certified to not less than eighty contracts of insurance. At this early date it was the practice in marine insurance that the

* For an admirable and learned discussion of the antiquity of insurance practice, law and custom see Plass, Geschichte der Assecuranz und der hanseatischen, Seeversicherungs-Börsen Hamburg, 1902.

premium was not to be paid until the voyage was completed, which in part accounts for the not inconsiderable amount of litigation and the apparent necessity of government interference upon grounds of public policy.

The Beginning of Government Control of Insurance.

These references to the antiquity of insurance are sufficient for the present purpose, to emphasize the fact that government interest in insurance transactions has been practically co-incident with the inception of insurance and that the principle itself has been developed and perfected with the development and perfection of the insurance contract to its present form. Among other illustrations of the more or less drastic interference of government in matters of insurance, reference may be made to an edict issued by Count Philip of Burgundy, in 1458, confirming the then existing law of insurance and prohibiting the citizens of his principality to act contrary in all matters of insurance to the judgment and arbitration of the law of Flanders. Abuses in the practice of insurance were, no doubt, the chief cause of government interference, including, of course, the frequent disputes between the contracting parties under the then extensively prevailing practice of individual underwriting, which brought many cases into court for settlement or arbitration. There is record of an ordinance of Philip II of Spain, then the oppressor of the Netherlands, dated October 31st, 1563, which calls attention to the great practical value of insurance as an aid to commerce, but which also makes reference to the numerous complaints which had been made against abuses in insurance matters and which made it desirable that thereafter the Exchange of Antwerp should adopt a standard form of insurance policy, the use of which was subsequently made compulsory. A copy has been kept of the first policy form used in the city of Hamburg, which shows that the rules of Antwerp of 1563 were adopted by other European commercial nations. It is, therefore, a matter of indisputable historic

record that a standard policy form of marine insurance was enacted in the Netherlands as early as 1563.*

It was only a few years later, in 1568, when the notorious Duke of Alba, as Administrator of The Netherlands, issued an ordinance prohibiting absolutely all marine insurances and declaring all contracts of this character null and void. The great loss sustained by shipping and commerce as a result of this act brought about a material modification of the decree in 1570 and the adoption of a completely revised ordinance in 1571, which again made the practice legal and much the same as it had been theretofore. One of the unforeseen results of the prohibitory ordinance of 1568 was the transference of the seat of the chief center of individual underwriting from Bruges to Hamburg, which has maintained to the present day, its place of prëeminence in this respect among the cities of the Continent of Europe.

Insurance as a Branch of Admiralty Law.

The increasing amount of insurance litigation brought about the necessity of special consideration and in the free city of Hamburg a branch of the Admiralty was established as a Court of First Instance, to deal with cases of this kind. This inclusion of insurance contracts as within the scope of admiralty jurisdiction is an extremely interesting and suggestive fact in the historical development of insurance. In marked contrast, the English practice has, on the whole, been adverse to the recognition of insurance contracts as within the scope of admiralty jurisdiction, since they were contracts made on land, even though for the exclusive purpose of protecting property while at sea. The Supreme Court of the United States, however, in the case of Insurance Company vs. Dunham, decided in 1870, laid down the important principle that English admiralty practice regarding insurance contracts could not be accepted and that the narrow view regarding this, as well as other admiralty matters,

* See Martin's History of Lloyds, p. 27.

could not be accepted by the Court as the law of the land. It was said on that occasion, and the remarks have a broader meaning than is at first apparent on superficial reading, that, "This Court has frequently declared and decided that the admiralty and maritime jurisdiction of the United States is not limited either by the restraining statutes or the judicial prohibitions of England, but is to be interpreted by a more enlarged view of its essential nature and objects, and with reference to analogous jurisdictions in other countries constituting the maritime commercial world, as well as to that of England."* It was, therefore, decided by the Court that the contract of marine insurance was a maritime contract and within the scope of the admiralty jurisdiction of the Court, as defined in the 2d Section, 1st Clause of the 2d Article of the United States Constitution.

Colonial Admiralty Jurisdiction Over Insurance.

The importance of this case in its practical bearing upon the future interpretation of the Commerce Clause of the Constitution in its possible relation to insurance cannot easily be over-estimated. In the opinion of the Court, in the case of Insurance Company vs. Dunham, as delivered by Justice Bradley, than whom no member of the Court from its inception has had a more profound knowledge of insurance in all its branches, there is a comprehensive review of the laws and ordinances of Barcelona of 1435, of Venice of 1468, of Florence of 1523, and of Antwerp of 1537; and other ancient sea laws and mari-

* Cases on the Law of Admiralty, by Jas. Barr Ames, Cambridge, 1901, p. 47; and for a more extended discussion see "The American Admiralty, its Jurisdiction and Practice," by Erastus C. Benedict, 2nd Edition, New York, 1870, Chapter XIX, on the Admiralty and Marine Jurisdiction of the British Colonies, particularly p. 83, where policies of assurance and bottomry loans are included within the scope of the rights and privileges contained in the commission of the Vice-Admiralty Judge of the Provinces and Colonies of New York, Connecticut, and East and West Jersey, dated Oct. 15, 1762.

time codes, which do not require to be enumerated.* Upon this basis of ancient law and usage, the Court arrived at the conclusion that "in every maritime code of Europe, unless England is excepted, marine insurance constitutes one of the principal heads," and further that it is a fact that "the commissions in admiralty issued to our colonial governors and admiralty judges, prior to the Revolution, which may be fairly supposed to have been in the minds of the Convention which framed the Constitution, contained either express jurisdiction over policies of insurance or such general jurisdiction over maritime contracts as to embrace them."†

Lex Mercatoria Americana.

The marine branch of insurance is no longer the sole or most important development of the principle of insurance, but other forms of the insurance contract, particularly fire, life and accident, have assumed proportions wholly unanticipated when the law and legislation of insurance was in its infancy. Insurance, not being of English origin,‡ it has required many years to perfect both the common and the statutory law which to-day governs and controls the business. Not until the practice of individual underwriting gave place to the assumption of insurance risks by chartered corporations, did insurance attain to the dignity of a great business, entirely separate and distinct from other branches of commercial enterprise. It is only since insurance corporations, as such, have come into existence that the quasi-public character of the insurance function has become better known and understood by law-making and governing

* For extended references to the early sea laws see "A Treatise on Maritime Law," by Henry Flanders, Boston, 1852.

†Cases on the Law of Admiralty, by J. B. Ames, Cambridge, 1901, p. 47.

‡The earliest policy extant in the records of the Admiralty Court is in Italian and bears the date of 1547. The earliest policy in English bears the date 1555, and there is another policy of 1557 based on Italian forms of earlier date and simpler content than that prescribed in the Florentine Ordinance of 1523. See Gow on Marine Insurance, 4th Ed., 1909, p. 322.

bodies. While there has been this change in the public attitude toward insurance undertakings, it is nevertheless true that in most of the insurance transactions, or in the relations of the contracting parties, the Law Merchant* still governs and controls, except in so far as the common law has established certain fundamental principles and as statutory law has incorporated these principles into written provisions for the more safe and equitable conduct of the business. In England a Court of Assurances had been established as early as 1601 and it is recited in the Act of that year that policies of insurance were contracts of great value in promoting commercial adventure and, therefore, entitled to the solicitude and protection of the government. The Court of Assurances fell later into this use, but the principle of public supervision over these transactions had been clearly recognized and was never subsequently lost sight of in English law and legislation.†

* The most important American work on the Law Merchant is "An Enquiry into the Law Merchant of the U. S., or Lex Mercatoria Americana," by Geo. Caines, N. Y., 1802. (Vol. I only was printed.)

† In a letter to the Post Magazine and Insurance Monitor of London, July 25, 1908, the following letter is re-printed from the Acts of the Privy Council, 1579, according to which 22 years before the Act of 1601 was passed the Privy Council took official cognizance of insurance disputes and concerned itself with matters of investigation and adjudgment similar to the functions subsequently discharged by the Court. The letter reads in full as follows:

[EXTRACT.]

9° *Januarij*, 1579, Whitehall.

Present:—Lord Chancellor, Lord Admiral, Lord Chamberlain, Lord Hunsdon, Mr. Comptroller, Mr. Vicechamberlain, Mr. Secretary Walsingham, Mr. Secretary Wilson.

A letter to William Mericke, Richard May, Thomas Branly and the reste of the Commissioners appointed for matters of Assurances within the Cittie of London that whereby a letter from some of their Lordships of the 24th of May, 1578, they recommended unto them a complaint exhibited unto them by Hippolito Beamonti, a merchant of Luca in

Early English Insurance Law.

The earliest restrictive English legislation, on the subject of insurance except as otherwise referred to elsewhere, appears to have been 19 George II, c. 37 (1746).* which has reference to bottomry bonds, but which included a provision "that all insurances, interest or no interest, or without farther proof of insurance than the policy itself, by way of gaming or wagering, or without benefit of salvage to the insurer (all of which had the same pernicious tendency), shall be totally null and void, except upon privateers or upon ships or merchandise from the Spanish or Portuguese Dominions, for reasons sufficiently obvious," etc.†

This Act was followed in 1774 by the so-called Gambling Act, or 14 George III, c. 48, which provided that "no insurance shall be made on lives or on any other event wherein the party insured had no interest; that in all policies the name of such

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Italye, concerning a controversie betwene him and the assurers of London, which Hippolito had caused to be assured by two severall pollicies certen woade from Burdeaux to Roan and Newhaven, which woade, after the assurance made, was taken by the Vlissingers and confiscates (*sic*), whereupon the said Hippolito by means of their Lordships' said letters unto them obtayned from the said assurers the money by them assured; forasmuche as their Lordships by the peticion inclosed are geven to understand that by good proofes it is since evidentlie discovered that the said woade hathe ben againe recovered with the privitie of the said Hippolito from the Flushingers by the two merchauntes in who[se] names the same was assured, their Lordships therfore desirous to understand the veritie thereof, to th'ende that aswell restitucion maie be made unto th'assurers of the money by them without cause payed unto him, as that the lewde acte of the practiser maie not remayne unpunished, doe require them by vertue hereof to call fourthwith before them the said assurers and Hippolito, and after they shall have substancially examined the matter to certifie unto their Lordships what they finde thereof, that thereupon suche order maye be taken as shalbe aggreable with justice and equitie.

* Reprinted in full in Cases on Insurance, by Eugene Wambaugh, Cambridge, 1901, p. 6.

† Blackstone's Commentaries, Book II, Chapter XXX. (4th Ed., Vol. I, p. 796.)

interested party should be inserted, and nothing more shall be recovered thereon than the amount of the interest of the insured."

The Common Law of Insurance.

The legal principles expressed in these two Acts have remained the law of England to the present day, the first governing the marine and other property insurance contracts, while the second governs contracts involving life contingencies.* The Commentaries of Blackstone upon these Acts contain the suggestive statement that, "the learning relating to these insurances hath of late years been greatly improved by a series of judicial decisions; which have now established the law in such a variety of cases that (if well and judicially collected) they would form a very complete title in a code of *commercial* jurisprudence; but, being founded on equitable principles which chiefly result from the special circumstances of the case, it is not easy to reduce them to any general heads in mere elementary institutes. Thus much, however, may be said; that being contracts, the very essence of which consists in observing the purest good faith and integrity, they are vacated by any the least shadow of fraud or undue concealment; and, on the other hand, being much for the benefit and extension of trade by distributing the loss or gain among a number of adventurers, they are greatly encouraged and protected both by common law and Acts of Parliament."†

Smuggling and Contrabrand Trade.

Mention should be made in this connection, however, of an Act passed in 1693, when by the 4th and 5th William and Mary, it was provided that "All persons who shall undertake by way of insurance or otherwise, to deliver any goods, etc.,

* It requires to be stated in this connection that the English law relating to insurance was codified into the marine insurance Act of 1906 (6th Ed., VII, Chap. 41), but in addition thereto a new marine insurance gambling act was enacted by Parliament in 1909.

† Blackstone's Commentaries, 4th Ed., Vol. I, p. 796.

without paying the duties or customs, or any prohibited goods whatever," shall forfeit the sum of £500 and that a like sum shall be forfeited by the insured. This, so far as known, is the first prohibitory statute regulating in part insurance transactions in England, enacted, of course, before insurance corporations came into existence and when the business was exclusively carried on by individual underwriters. The object of the Act of 1693 was to place a severe penalty on all insurance of contraband trade, particularly smuggling, regarding which it has been pointed out by Millar in his treatise on The Law of Insurances (Edinburgh, 1787) that "Every person who insures contraband goods is assisting and abetting in an evasion of the law. Nay, as the insurer takes the risk of capture and seizure upon himself, it is he, properly speaking, who is to be considered as the smuggler. Every insurance upon a trade which the parties know to be illicit, must, therefore, be illegal."

First Taxes Upon Insurance Policies.

Only two years before this Act was passed the first regular office for insurance against loss by fire had been established in London by a group of individual underwriters, but as early as 1694 a high stamp duty was imposed on fire policies,* which would indicate that fire insurance at this time was not held in any particularly high regard by the government.†

Early English Fire Insurance Companies.

Fire insurance in England did not come into extended use until subsequent to the great fire of London, which occurred in 1666. Various early schemes for fire insurance institutions were inaugurated during the next thirty years subsequent to this date, but none assumed considerable proportions or attained to permanency, except in so far that earlier ideas were incor-

* Report on Fire Insurance Duties, Parl. Paper, London, 1857.

† In 1698 and during subsequent years the duties were further increased. See table of data and list of statutes with account of revenue, etc., in Report of 1857, opp. p. 9.

porated into latter day institutions. A fire office, conceived by Dr. Barbon, the first successful projector of fire insurance in England, was established in 1667 and in 1686 this concern solicited from the Lords of the Privy Council a patent for the exclusive privilege of making and registering all assurance policies and contracts on houses from fire within the bills of mortality for thirty-one years, having insured for so long a time. This desire for parliamentary sanction of what would be equivalent to a monopoly indicates also the early necessity for government protection on the part of those actively engaged in the management of institutions of this kind. In 1696, however, a society came into existence with the title "Contributors for Insuring Houses, Chambers, or Rooms from Loss by Fire, with Amicable Contributions within the Cities of London and Westminster and the Liberties Thereof and the Places Thereunto Adjoining." This title was subsequently altered to "Amicable Contributors for Insuring Loss by Fire," and subsequently to "Amicable Contributionship," and finally, in 1706, to the name of "Hand in Hand." The very title is evidence of the fact that the undertaking was a mutual agreement of joint contributors, primarily for the individual protection of the subscribers and incidentally for profit. Similar undertakings came into existence with the establishment in 1710, of the Sun Fire in 1714, the Union; and in 1717 the Westminster, but these were mere joint partnerships, and not essentially different from other trading concerns.*

* The following extremely interesting advertisement having reference to an insurance project which, in all probability, led to the granting of the charter of the Royal Exchange in 1720, was printed in the Post Magazine and Insurance Monitor of London, under date of June 4, 1910.

From "The Post Boy." Numb. 4392. From Thursday Sept. 19, to Saturday Sept 21, 1717.

The SUBSCRIPTION *at* MERCERS-HALL *in* CHEAPSIDES *for raising a* FUND *of* ONE *or* TWO MILLIONS Sterling, *in order to incorporate a* Company *for* Insurance *of* Ships, Merchandise, &c., *was open'd* the *12th of* August *last; begun by an Eminent Merchant of this City, and*

In 1711 a proposal had been made for a national insurance office, by a petition of record to the House of Commons, "For raising great sums of money all over Great Britain, for the use of the Government, to the benefit and security of all those that are anyways concerned," for the purpose of eliminating private enterprise in fire insurance, it being held that "the public good of the nation ought at all times to be preferred before the private interest of all societies."*

Royal Exchange and London Assurance.

The scheme for national insurance was not carried through, but the era of so-called "bubble companies," emphasizing the necessity of more secure and permanent insurance institutions, accounts for the passage of the Bubble Act, 6 George I c. 18, passed in June, 1720, which empowered the King to grant two charters to proposed insurance corporations, as the result of which the Royal Exchange Assurance and the London Assurance came into existence that year.† While the object of these

subscribed by several others: But being desired to be shut till some Alterations were made therein, and till several who intend to subscribe largely thereto can come to Town, to subscribe for themselves. Notice is hereby given, That pursuant to the Desire of several considerable Merchants and others, the following Alterations are made, by and with the consent of those who have already subscribed, viz. *Whereas the subscription was at first limited to such as are* Natives *or* Naturalized; *it is agreed to admit any that are His Majesty's Subjects, Men of Substance and Reputation: And instead of One* per Cent. *no Subscriber is to pay more than Half* per cent. *towards defraying the Charges of forming the* Company, *and obtaining a* Charter. N.B. *The Subscription will be open'd again on* Wednesday *next at Eight in the Morning. No Subscriber is oblig'd to pay the Half* per Cent. *nor one Penny on any Account whatever, till the Managers* &c. *are chosen; nor then, if he do not like the* Company. *Abstracts of the Articles are deliver'd* (Gratis) *to those that come or send for them to the Hall.*

* History of Fire Insurance Companies, by F. B. Relton, p. 93. See also Walford Insurance Cyclopedia, Vol. III, p. 438 *et seq.*

† For a full account of the origin, powers and privileges of the Royal Exchange and London Assurance, see Lex Mercatoria Rediviva, by Wyndham Beawes, London, 1752, p. 262 *et seq.* Also, John Weskett, Theory, Laws and Practice of Insurance, London, 1781, p. 108 *et seq.*

two institutions was primarily, and apparently exclusively, the making of marine insurances, their activity later included other branches of the business. The charters granted an exclusive monopoly, without, however, interfering with the practice of individual underwriting. The charters were revocable at the expiration of thirty-one years and it was provided that "All other corporations and all partnerships for assuring ships or merchandise at sea or for lending money upon bottomry should be restrained from underwriting any policies or making any contracts of assurance on ships or merchandise at sea," etc., but, "nevertheless any particular person shall be at liberty to underwrite policies, or may lend money by way of bottomry, so as the same be not upon the account or risk of a corporation or of persons acting in partnership."*

By an Act passed in the year 1725, "All promissory notes for assurance on ships or merchandise in either company were declared null and void." A revised set of proposals had been issued by the Royal Exchange in 1722, according to which the corporation was then authorized to assume fire risks, it being stated that "His Most Gracious Majesty, being desirous to promote and encourage such lawful and commendable undertakings as are calculated for the security of all his loving subjects, has granted to this Corporation his Royal Charter for those ends and purposes, by virtue whereof they now assure houses, buildings, goods, wares and merchandises, from loss and damage by fire, throughout the Kingdom of England, and Town of Berwick-upon-Tweed, the Kingdom of Ireland, and all other parts of His Majesty's dominions beyond the seas, upon the following easy terms," etc.†

English Insurance Law in the American Colonies.

The foregoing sentence proves clearly that the objects of the Royal Charter were to establish a national institution with

* Fowler, History of Insurance, p. 9.

† An Account of Fire Insurance companies, compiled by Francis B. Relton, London, 1893, p. 160.

power to transact business throughout the British dominions including, of course, the American colonies, but it is very curious that Scotland was not mentioned as coming within the field of the corporations' operations. Relton in this connection observes that "Respecting the undertaking insurances in all parts of His Majesty's dominions beyond the seas, it is not impossible that the projectors of the Royal Exchange Corporation, who were connected with marine insurance, were aware of the fact that Lloyds undertook such fire business (presuming that they did so), and so made it a feature in their proposals in order to compete with Lloyds in fire as well as in marine insurance." Historical evidence is not wanting to prove that a considerable amount of marine insurance was transacted in the Colonies by the mother country, for in a letter written to William Penn by a Mr. James Logan, the Secretary of the Province of London, dated January 2nd, 1706–'07, the conscientious scruples of the Quaker against insurance are answered in the statement that "I beseech thee not to be scrupulous in insuring, for if I have any right notion of the matter 'tis as just and lawful *as any other part of trade*." The considerable extent of piracy on the American coast made insurance at this time an absolute necessity and without such insurance a large part of colonial trade would, unquestionably, have come to an end.

First 'Public Insurance Office' in America.

The historical connection of what has just been related with subsequent events in America is not, of course, to be substantiated by an unbroken chain of documentary evidence. There, however, can be no doubt but that the development of the insurance business in the Colonies followed largely and in many instances almost literally the preceding development of insurance institutions in England. Co-incident therewith, of course, was the development of insurance law and the relationship of government to insurance institutions. The earliest authentic account of "a public insurance office" in America is found in an item of the American Weekly Mercury of May 25th, 1721,

in which Mr. John Copson, of High Street, offers his services as an insurance broker to the merchants of the city "and other parts." According to Fowler, the advertisement read as follows:

"Assurances from Losses happening at Sea, &c., being found to be very much for the Ease and Benefit of the Merchants and Traders in general; and whereas the Merchants of this City of Philadelphia and other Parts have been obliged to send to London for such Assurance, which has not only been tedious and troublesome, but even very precarious. For remedying of which, An Office of Publick Insurance on Vessels, Goods and Merchandizes, will, on Monday next, be Opened, and Books kept by John Copson, of this city, at his House in the High Street, where all Persons willing to be Insured may apply: And Care shall be taken by the said J. Copson That the Assurers or Under Writers be Persons of undoubted Worth and Reputation, and of considerable Interest in this City and Province."*

We have here conclusive proof that the early insurance transactions in the Colonies had been carried on in London, but that it was now proposed, since sufficient security could be furnished, to afford an opportunity for taking out insurances in the principal seaport towns of the Colonies.

A Plea for Government Insurance.

Influenced, however, in all probability, by the proposal for a national insurance office, made in 1711, the earliest of American political economists, Francis Rawle, proposed the establishment of a semi-governmental insurance institution in 1725. The proposition, in part, reads that

"Having thus far discours'd of most of the Branches of Trade we are capable of, there is yet one great Encouragement, to adventure in the Discovery and Prosecution of new Markets; more safe to the industrious Adventurer; namely an Insurance-Office in one or more of these Colonies; which is the interesting of divers in the Loss or Profit of a Voyage, and is now become so much the Practice of England, that Insurance may be had in divers Cases as well against the Hazards at Land, as Casualties at Sea, which must be acknowledged not only to be safe, but a

* Fowler, History of Insurance, p. 11.

great Encouragement to Adventure; for it may so happen that a Person may sometimes adventure his ALL, and then in case of a Loss he may be rendered uncapable of a future Trade, to the Disadvantage of the Publick, and (it may be) to the Ruin of himself; whereas could he get a part of his Interest either of Ship or Cargo insured, (tho' in Case of safe Arrival he parts with a part of his Profit, yet, in case of loss, he is secur'd of such part as he insureth, which may be sufficient Bottom to begin a new Adventure: How far this may conduce to the Trade of this River, is obvious to any Man of Thought. Now whereas there has been some Attempts made at Philadelphia, which dropt and prov'd abortive, (for what Reasons we never could learn) we humbly propose to the Legislature that an Office be erected and supported by a Fund arising out of the Interest of the Loan-Office. This will be a good and safe Bottom, and cannot be easily overset by a few losses; and we conceive will contribute to keep up the Value of our Paper-Credit by promoting of Trade, Navigation and Building of Ships, and in Consequence, of great Advantage to this River: Which we prefer to the Consideration of the Merchant." *

Aside from other reasons, this proposal could not have been carried into effect, since it would have come in conflict with the monopoly granted to the Royal Exchange and London Assurance Corporations. Rawle probably was not aware of the Statute of 6th George I, c. 18, but in any event no action was taken in the matter. The proposal, however, is a most interesting one and particularly so in view of the fact that Rawle held insurance to be a branch of trade, in full conformity to other writers on the subject of that early period.

First Mention of "America" in an English Insurance Statute.

Following the establishment of an insurance office by John Copson in 1721, the next office in Philadelphia of which there is record was established by Joseph Saunders, in 1750; followed by Thomas Wharton, in 1752; and by Walter Shee, in 1756. The small number of separate offices is not an indication, how-

*Ways and Means for the Inhabitants of Delaware to become Rich, Fowler, History of Insurance, pp. 62–63.

ever, of the amount of business transacted, since offices of this kind were merely for the purpose of facilitating intercourse between insurers and insuring merchants. The law governing these transactions in the American Colonies was, of course, the law of England, including the statute of 1746, regulating insurance on ships belonging to Great Britain and on merchandise or effects laden thereon. The preamble to this Act sets forth that,

"The making Assurances Interest or no Interest, or without further proof of Interest than the Policy, hath been productive of many pernicious Practices, whereby great Numbers of Ships, with their Cargoes, have either been fraudulently lost and destroyed, or taken by the Enemy in time of War; and such Assurances have encouraged the Exportation of Wool, and the carrying on many prohibited and clandestine Trades, which, by Means of such Assurance, have been concealed, and the Parties concerned secured from Loss, as well to the Diminution of the publick Revenue, as to the great detriment of fair Traders; and, by introducing a mischievious kind of Gaming or Wagering under the Pretence of assuring the Risque on Shipping and fair Trade, the Institution and laudable Design of making Assurances hath been perverted; and that which was intended for the Encouragement of Trade and Navigation has, in many Instances become hurtful of, and destructive to, the same: For Remedy whereof it is enacted,

That, from and after the first Day of August, 1746, no Assurance or Assurances shall be made, by any Person or Persons, Bodies Corporate or Politick, on any Ship or Ships, belonging to His Majesty or any of his Subjects, or on any Goods, Merchandise or Effects, laden or to be laden, on board of such Ship or Ships, Interest or no Interest, or without further proof of Interest than the policy, or by way of Gaming or Wagering, or without Benefit of Salvage to the Assurer, and that every such Assurance shall be null and void to all Intents and Purposes," etc.

The Act further provided that the same should "not extend to, or be in force against, any persons residing in any parts of Europe out of His Majesty's dominions, for whose account assurance shall be made before the 29th of September, 1746; nor against persons residing in any parts of Turkey, Asia, Africa, or *America*, from whom assurances shall be made before the

29th of March, 1747."* This is probably the first mention of the word 'America' in an insurance statute and by inference the reference proves that insurance transactions between the mother country and the Colonies at that time were of sufficient consequence to require special consideration.

Early Prohibitive Insurance Statutes.

Prohibitory or regulative statutes of insurance were neither new nor novel at the time when the Act of 1754 was passed. The Civic statutes of Genoa (1588), according to Fowler, prescribed penalties for securities, bonds or wagers made upon the life of the Pope, or upon the life of the Emperor, or any constituted dignitary, ecclesiastical or secular, without license of the Senate. The 24th Article of the Ordinance of Amsterdam of 1598 expressly prohibited insurance on the life of any person and even earlier than this there is record of a similar prohibition in a French maritime treatise entitled Le Guidon, according to which (Sec. 5) "Another kind of insurance is made in other nations, it is upon the lives of men; by which in case of their dying during a voyage certain sums are to be paid to their heirs or creditors. Creditors may even insure their debts if their debtors remove from one country to another; the same can be done by those having rents or pensions, so that in case of their decease there will be continued to their heirs such pension or rent. These are all forbidden as against good morals, being customs from which endless abuses and deceptions arose." † In this connection Fowler observes that "Legal regulations as following and developed by the insurance practices had shown themselves in a decree of 1369 of the Duke of Genoa in an ordinance promulgated by the magistrates of Barcelona in 1435, and in a law of Flanders of 1537." Regulations of the insurance of Antwerp and Amsterdam followed later in the 16th Century. The famous "Ordonnance de la Marine" enacted in France in

* Postlethwayt, Universal Dictionary of Trade and Commerce, London, 1751, Vol. I. p. 146:

† Fowler, History of Insurance, p. vii.

1681 provided by Art. 10, that "We forbid the making of any insurance upon the life of men," but an exception was made by Art. 11, for the insurance of persons against the risk of captivity, to provide the required amount of ransom. The prohibition of life insurance in France naturally prevented the development of this branch of insurance in that country and the practice was not introduced, according to Bunyon, until the latter part of the 18th Century. John Millar, an advocate of Edinburgh, in his treatise on the elements of the law relating to insurance, published in 1787, observes in this connection that "many of the foreign mercantile states prohibit insurance on lives, a prohibition arising from the jealousy naturally entertained in an ill-regulated government, of whatever may serve as a motive to the commission of great crimes. The same jealousy is yet more apparent in some of the Italian States, where insurance is not only prohibited on the lives of great men, but on any political occurrence, and even on marriages and the birth of children."*

Wagering Contracts in English Law.

This observation by a trained legal mind near the close of the 18th Century illustrates the viewpoint held with reference to the nature of wagering policies and the important element of insurance interest. While England was apparently the first country to prohibit insurances without interest, practices nevertheless have been permitted which have been prohibited in practically all other civilized countries. The English in this respect make a distinction, more or less clearly defined, between insurance wagers not contrary to public policy but conducive to the development of trade and insurance practices clearly contrary to the public good and incompatible with high standards of private and public morality. This explains why the immense amount of wagering transactions carried on at Lloyds upon the life of the King and a thousand and one other contingencies are permissible in England, while not permitted or condoned in other civilized countries.

* Law Relating to Insurances, by John Millar, Edinburg, 1787, p. 26.

The Doctrine of Insurable Interest.

Prohibitory or regulative statutes governing the business of insurance in England have been very few and far between. The two statutes of 1746 and 1774 have practically governed the essentials of the business even to the present day. Even these Acts were not statutory declarations of new principles of law, but rather the precise enunciation of long-established principles of the common law. The principle of insurable interest had been laid down certainly as early as 1692 in the Chancery Courts case of Goddard vs. Garrett, wherein it was stated that the Court "took it that the law is settled that if a man has no interest and insures, the insurance is void, although it is expressed in the policy 'interest or no interest'; and the reason the law goes upon is that these insurances are made *for the encouragement of trade* and not for persons unconcerned in trade nor interested in the ship to profit by it." In the famous case of Sadlers' Company vs. Badcock (1743), it was said with reference to fire insurance that "Now these insurances from fire have been introduced in later times and therefore developed from assurance on ships, because there interest or no interest is almost constantly inserted and if not inserted, you cannot recover unless you prove a property." The statutory definition of the principle of insurable interest makes, therefore, written law of what had theretofore been the unwritten or common law of England for a long period of time. The commercial character of all insurance at this early period is clearly brought out by the frequent reference to insurances as transactions in trade and the law of England, as applied to both the contractual relations of parties and the Parliamentary supervision and control over the business, has been in conformity to the principles of the Law Merchant, or, as said by Lord Mansfield, Chief Justice (1777), "A policy of insurance is in the nature of it a contract of indemnity and of great benefit to trade, but the use of it was perverted by its being drawn into a wager and to remedy this evil the statute of the 19 Geo. II, c. 37 (1746), was made."

The Evolution of Common and Statutory Law of Insurance.

The development of English statute law in conformity to previously established principles of common law is of the utmost and far-reaching importance. The trend of modern law-making, so-called, is continuously to draw away from common law principles, or to set aside long-established legal definitions which custom has sanctioned and to which immemorial usage has given a definite and generally understood meaning. Statutes, it has well been said, "are not reasons, but they are a mere command," but the common law *is* reason, or that law which derives its force and authority from the universal consent and immemorial practices of the people. The simple but effective statutes of 1746 and 1774 governed in the business of insurance in the American Colonies and they were incorporated in the law of the land, after the Declaration of Independence. The business of insurance up to that time had been practically limited to marine insurance and few cases came before the courts for final adjudication. In all such cases the law of England governed in essential matters, but particularly and without exception in the judicial construction of principles of insurable interest. In fact, the American courts adopted a far more rigid construction of the two statutes of 1746 and 1774 than had been the case in England where wagering policies were held to be valid in some cases, unless found to be distinctly contrary to public policy. The early policies issued in America were identical in phraseology with the policies issued in England, including the ancient phrase that "It is agreed by us, the assurers, that this writing or policy of assurance shall be of as much force and effect as the surest writing or policy of assurance heretofore made in Lombard Street or elsewhere in England." That phrase occurs in a policy dated Philadelphia, April 25th, 1749, the original of which has been preserved and a facsimile of which has been printed in Fowler's History of Insurance, but after the Declaration of Independence the stately phrase which had been at the head of English and Con-

tinental policies from time immemorial "In the name of God, Amen," was omitted and the phrase previously referred to was changed to read, certainly as early as 1788, "And it is agreed by us, the assurers, that this writing, or policy of insurance, shall be of as much force and effect as the surest writing, or policy of assurance heretofore made in any of the *United States* or elsewhere."

Judicial Interpretation of American Insurance Policies in Conformity to English Law and Customs of Trade.

In the judicial interpretation of insurance contracts, however, English law and usage determined the legality and as said in a case which came before the Supreme Court of Pennsylvania in January, 1795, "This case is distinguished from that of Williams vs. Craig. There was no established rule of trade between France and Philadelphia. Our trade with that country began and ended with the American war. But between England and Philadelphia a settled rule has subsisted for many years, and the usage has been generally approved of. The plaintiff's charge for insurance was contained in every account rendered to the defendant; and as he made no objection thereto, he must necessarily be supposed to have acquiesced in the custom of the English merchants." In a similar case tried before the same court, also in 1795, the testimony was accepted that "The defendant's construction of the policy was conformable to the general sense and usage of merchants and this view was adopted by the Court and Jury." * Finally, in a case decided at the March term, 1803, the Supreme Court of Pennsylvania declared that "We have adopted the policy and principle which gave rise to the British statute of 19 George II, c. 37, in courts of justice and by commercial usage, but we are not prepared to say that every particular provision or resolution under it has been engrafted into our system of law."† A few years previous the Supreme Judicial Court of Massachusetts in the case of Amory vs. Gilman (1800) reviewed the whole question

* 3 Dallas, 510.

† Fowler, History of Insurance, p. 66.

of English law as underlying American jurisprudence in matters of insurance it being stated *inter alia* that "By the common law at the time of our ancestors' emigration and for nearly a century afterward such a contract (gambling) was void. During the last century the English Courts began to sustain actions on this species of contracts, but their decisions have not been adopted here. The ancient law of England and the usage of this country must then decide this question. The forcible objections recited in the preamble to the statute 19 George II, c. 37, received additional force from our morals, manners and the spirit of our law. The question whether the statute of 19 George II has been adopted here is now before the Court on another section of it (relating to re-assurances) in which it was fully argued. But it is absurd to suppose that our courts have adopted the decisions of the English courts in the early part of the last century, involving all the mischiefs of these gaming policies, and yet have failed to adopt this statute in remedy of the evil." After an extended examination of the facts and legal principles involved in the English court decisions in plain conflict with the statute referred to, Justice Sedgwick, observed in part that "After reflecting on these observations, which every man of experience and a knowledge of the human character knows to be well founded, there can, I think, remain no doubt that it would be hostile to the welfare of society that interests which men may choose to create by such contracts should be protected by judicial authority. Much additional weight is given to the argument by the British statute, 19 George II, c. 37, prohibiting wager policies. It is the authority of a wise legislature of a nation *most deeply interested in commerce*, and best understanding its interests; and it prohibits them because they are "productive of many pernicious practices."

Insurance Contract Governed by Considerations of Public Policy.

Chief Justice Dana, observed "We must, therefore, decide this on general principles of justice and good policy. The very

forcible reasons set forth in the preamble of the statute, 19 George II, c. 37, to which I have before referred, apply equally to this and every other civilized and well-governed commercial country. Whether that statute extended to this country or not is a question not necessary now to be determined. But if it were, and we should find no precedents in our courts to overrule us, I should be prepared to say that, as wager policies are injurious to the morals of the citizens, tend to encourage an extravagant and peculiarly hazardous species of gaming, and to expose their property, which ought to be reserved *for the benefit of real commerce*, they ought not to receive the countenance of this court."

In a case quite similar, of Pritchard vs. Insurance Company of North America, Shippen, Chief Justice, in answer to a contention of counsel that the Gambling Act had not been extended to Pennsylvania by practice said, "Certainly the British Act does not bind us, *proprio vigore;* but the system of national policy which dictated the law has been adopted by our courts. We believe that policies made here, at least by the incorporated companies, do not retain the words 'interest or no interest.' " And, Yeates, Justice, for the court said: "The Chief Justice, during the argument, conveyed the sentiments of the whole court. We have adopted the policy and principles which gave rise to the act of Parliament, both in courts of justice and by *commercial* usage; but we are not prepared to say that every particular provision or resolution under it has been engrafted into our system of law. An insurance amongst us is a contract of indemnity. Its object is not to make a positive gain, but to avert a possible loss. A man can never be said to be indemnified against a loss which can never happen to him. There cannot be an indemnity without a loss, nor a loss without an interest. A policy, therefore, made without interest is a wager policy, and has nothing in common with insurance but name and form. It is not subservient to the true interests of fair trade and commerce, but is pregnant with as much mischief, both public and

private, as can proceed from any species of gaming which the legislature has hitherto found it necessary to repress. Every species of gaming contracts wherein the insured having no interest, or a colorable one merely, or having a small interest much overvalues it in a valued policy, under the cloak of insurances, are reprobated both by our law and usage."*

Limited Extent of Insurance in the American Colonies.

These illustrations from the early history of American law sufficiently prove that the fundamental principles of English law on the subject of insurance were incorporated into the system of American jurisprudence, as being in conformity to the more ancient but controlling principles of the Law Merchant, or Lex Mercatoria. The extracts quoted also prove conclusively that from the legal, as well as the general, point of view insurance was considered an element of commerce and that insurance transactions were held to be commercial transactions not separate and distinct from commercial affairs generally. It requires always to be kept in mind that insurance in the Colonies never attained to the dignity of a corporate business and that the transactions were, on the whole, of small extent and practically limited to a few seaport towns. Naturally, legislation was not required to intervene in the development of such a business and no legislative action was called for until applications were made to the different State Legislatures for charters to establish separate and distinct insurance corporations.

First Fire Insurance Association Established in South Carolina in 1735.

The first attempt to establish an insurance office in Massachusetts had been made as early as 1724 by Joseph Marion of Boston, who four years later, under date of November 18, 1728, advertised a proposal to establish the New England Sun Fire Office, which, however, did not materialize. In 1735 the Fire

* Wambaugh, Insurance Law, Cases, p. 16.

Insurance Friendly Society of Charleston, S. C., came into existence, but it was only of short duration, its career being ended by a disastrous fire in 1740, causing a loss of $1,500,000.*

The public protection against the fire risk was very crude and the first fire company for protective purposes was not established in Philadelphia until 1738. Joseph Marion, in 1748, made a second unsuccessful attempt to establish the New England Sun Fire Office, but it was not until 1752 that the first successful American fire insurance association† after the model of the London Amicable was established by deed of settlement for "not merely the mutual security of the members, but for the common security and advantage of their fellow citizens and neighbors and the promoting of a great and public good apart from all motive of private and separate gain." The name first subscribed to this deed of settlement was that of James Hamilton, the Lieutenant-Governor of the Province under the proprietors, and of this it has been said that "it was the name of a public officer; announcing the approbation and favor of the government, but indicating no special participation in originating the company." The first private name on the document was that of Benjamin Franklin, who also became one of the first Directors. Franklin has often been claimed to have been the originator of this plan, but it is practically certain that the author of the project was *John Smith*,‡ and Franklin nowhere in his writings has claimed the merit of having founded the first successful institution to transact the business of fire insurance in America.§

* For an account of "Friendly Society for the Mutual Insuring of Houses against Fire," established in Charleston, S. C., in 1735, see the South Carolina Historical and Genealogical Magazine for Jan., 1907. This was probably the very first fire insurance institution in America.

† The term "association" is used here in a general sense.

‡ "For a statement of the facts, see the account of the Centennial Meeting of the Phila. Contributionship for Insurance of Houses from Loss by Fire, Phila., 1852, p. 22 *et seq.*"

§ According to James Schouler, Franklin in 1738, however, originated in Philadelphia the First Volunteer Fire Co. for protective purposes.

The Philadelphia Contributionship.

The society was not incorporated until 1768. It was never more nor less than a mutual fire insurance society and not a trading company or partnership, engaged in the business of insurance within the meaning of the Act of 1720. It was a concern or an arrangement for the profit and loss of the members, established by public sanction through the participation of a high officer of State in its organization. The business done was very small and after ten years of effort the amount of insurance in force was less than at the end of the first. The company relied for its success upon premium charges ill-considered with reference to the true fire risk and not until a change was adopted in 1763 by which a guarantee fund was gradually accumulated as a safeguard against the conflagration hazard did the business of the society attain to considerable proportions. The society in all its essentials was modeled after the Amicable Contributionship, including the use of the sign of the clasped hands, which later gave to the London company the name of Hand in Hand. The management was remarkably able from the outset and during a whole century of active effort only one lawsuit was brought against the institution and in that the company was successful.*

First Life Insurance Institutions in America.

The Contributionship, however, was not the only insurance institution established in Philadelphia during the middle of the 18th Century. For similar reasons of mutual protection and security, the Presbyterian Ministers' Fund had been chartered in 1759 and ten years later a more ambitious charitable "corporation" of the Episcopal Church. These also were not insurance corporations as trading concerns or of general scope, but rather special efforts in the field of mutual aid, combined more or less, in the case of the last named, with charitable assistance

* Centennial Meeting of the Phila. Contributionship for Insurance of Houses from Fire, Memorial Sketch, Phil., 1851, p. 49.

from the well-to-do. It was explained in the first account of the Charitable Corporation that "The distressed circumstances in which the Episcopal Clergy in the more northern provinces of America and especially the Missionaries in the Service of the Society for the propagation of the Gospel, have too frequently been obliged to leave their families, had long been a matter of discouragement to many from entering into the Ministry of our Church, as well as of regret to pioneer and worthy members thereof." A scheme was, therefore, drawn up at Perth Amboy, N. J., May 12th, 1768, and finally adopted by the three provinces interested in the matter, a charter for Pennsylvania being obtained on the 7th of Feb., 1769. The charter began with "George the Third by the Grace of God" and included the explanation that "corporations have by charter been erected in the provinces of Pennsylvania and New Jersey for receiving moneys and dispensing of such sums of money as may be contributed *and given* as a fund towards the support and relief of the widows and children of said clergy; and for the further promotion of which laudable and *charitable* design," etc., etc.

Insurance Supervision by the Church of England.

It is thus apparent that, like the Contributionship, this was not a trading corporation or a business concern in the true sense of the word, but a semi-charitable enterprise or voluntary contributionship, established for a specific purpose and for the use and benefit of a special class. In recognition, however, of the financial and general fiduciary consideration incurred in the undertaking by the Episcopal church, it was provided in the charter, "And lastly, we do hereby, for us, our heirs, and our successors, ordain, order and appoint that the accounts and transactions of the said corporation, legally and properly vouched and authenticated shall from time to time, and as often as demanded, be laid before the Lords Archbishops of Canterbury and York and the Bishop of London, for the time being, or such persons as

they may from time to time appoint for that purpose in America, in order that the said Archbishops of Canterbury and York and the Bishop of London, for the time being, or such person or persons appointed by them, as aforesaid, may satisfy and confirm the said accounts, or subject them to such revisal, check and confirmation as may be thought just and reasonable." * In other words, the corporation was subject to the ecclesiastical authorities and the canon law with a full recognition of the principle of supervision and control over its accounts and actions. This is the first instance of public supervision and regulation of insurance in America and it is therefore historically true, that insurance, practically from its inception in all civilized and commercial countries, whether as a business or a mutual contributionship, for the purpose of gain or mutual aid, has been a matter of serious concern to government, including the ecclesiastical authorities, in the same manner that the contract has been the subject of the civil and canon law from its origin in ancient times.

The Rules and Customs of Boston.

By 1770 there were therefore only three insurance institutions in existence in Philadelphia, but none of these, as has been shown, were commercial undertakings or trading corporations, which, in fact, they could not have been without coming in conflict with the Act of 1719-'20. (6 Geo. I. c. 18) which was in full force in the Colonies. In that year, in fact, according to Schouler,† who is the best possible authority, no fire insurance company had been established in New York City at that time, nor had several attempts to organize such an institution

* " Some account of the Charitable Corporation lately erected for the Relief of Widows and Children of Clergymen in the Communion of the Church of England in America," for a copy of their charter and fundamental rules, and also a sermon preached Oct. 10, 1769, before the said Corporation on the occasion of their first meeting, by Wm. Smith, D. D., published by order for the benefit of the charity. Philadelphia, 1769, p. 11.

† Americans of 1776, by Jas. Schouler, New York, 1906, p. 69.

in Boston been successful. The Stamp Act* of 1765 included documentary duties upon all insurance policies, but this seems not to have attracted special attention or been considered a particularly obnoxious burden upon the business by those engaged therein at the time. The Revolution, naturally, was not a favorable period for the formation of chartered companies or corporations to engage in the business of insurance, but it is on record that in the first year after the peace the term "company" was used to give dignity and standing to the insurance office of some twenty associated individual underwriters of Boston. The difficulties or disputes between underwriters and the insured were, adjudicated according to the changed conditions and settled "agreeable to the Rules and Customs of Boston" and not London, just as the reference to Lombard Street and Royal Exchange and London had before this been eliminated from American policies. While the term "company" was used in the advertisement of Hurd and Jeffery of Boston,

* The paragraph in the Stamp Act referring to insurance reads, in part, as follows:

"And be it further enacted....., That every deed, instrument, note, memorandum, letter, or other minument or writing, for or relating to the payment of any sum of money, or for making any valuable consideration for or upon the loss of any ship, vessel, goods, wages, money, effects, or upon any loss by fire, or for any other loss whatsoever, or for or upon any life or lives, shall be construed, deemed, and adjudged to be policies of assurance, within the meaning of this act; and if any such deed, ...for insuring, or tending to insure, any more than one ship or vessel for more than any one voyage, or any goods..... or other matter or thing whatsoever, for more than one voyage, or in more than one ship or vessel, or being the property of, or belonging to, any more than one person, or any particular number of persons in general partnership, or any more than one body politick or corporate, or for more than one risque; then, in every such case, the money insured thereon, or the valuable consideration thereby agreed to be made, shall become the absolute property of the insured, and the insurer shall also forfeit the premium given for such insurance, together with the sum of one hundred pounds." Select Charters and other Documents illustrative of American History, 1606–1775, edited by Wm. Macdonald. New York, 1899, pp. 289–290.

there were no incorporated or chartered institutions engaged in the business of insurance in Massachusetts or New York in the first year of the Republic, except the three institutions in Philadelphia, which do not properly come within the definition of insurance companies as trading concerns.

First Massachusetts Insurance Charters.

For the apparently insignificant reason that the Philadelphia Contributionship would not accept risks upon buildings surrounded by trees, a "Mutual Assurance Company" for insuring houses from loss by fire in and near Philadelphia was organized in 1784. The *company* became known as the Green Tree Company, but in its organization differed little from the contributionships. The time, however, had come with the return of peace and prosperity for the more serious consideration of establishing insurance companies with sufficient capital to give real instead of fancied security to the insured. In 1785 a petition was presented to the Massachusetts Legislature to permit of the establishment of a fire insurance company in Boston, but according to Hardy* the petition was rejected "as not being for the advantage of the Town." Evidently the principle of insurance as a matter of corporation enterprise had made small progress even in the populous centers of trade on the Atlantic seaboard. The Massachusetts Congregational Charitable Society was established, however, in 1786, probably identical in aims and purposes with the corporation of a corresponding character established by the Episcopal Church. In all these and similar cases the object seems rather to have been to provide for a small or special class of persons than to further the principle of insurance as applicable to the masses of the people. Life insurance at this time was a matter of mere crude speculation, but as early as 1789 Wigglesworth, a Massachusetts clergyman, had calculated a life table from the more or less trustworthy vital records of a few selected counties of the

* Early Insurance Offices in Massachusetts, by E. R. Hardy, p. 57.

State. The Rev. Mr. Gordon* in a sermon preached in Boston in 1772 had argued in favor of extending life insurance to the general population, but nothing had come of it, except that some encouragement was given to promoting tontine schemes, which came perilously near to being in conflict with the provisions of the Gambling Act.

Annuity Proposals Before the Continental Congress.

Law and legislation on insurance were hardly required under conditions like these. It would have been absurd to legislate regarding a business which was of such very limited extent as insurance. Lotteries were common and absorbed most of the surplus earnings of the mass of the people. The Continental Congress had considered various annuity schemes and a committee on the subject had been appointed in Nov., 1779, but earlier than this, that is, April, 1779, it had been "Resolved that ..... million dollars be borrowed on the faith of these United States in annuities for one life at ....% and ....% for two lives, *without* distinction of age, that the annuity shall not be for less than 50 dollars on one life and 75 dollars for two lives yearly income. Strangers not naturalized, or citizens or subjects of any nation or country may acquire the said annuities, which shall not be liable to forfeiture or confiscation, even in case of war between the United States and the country of which the annuitant may be a citizen." Finally it was suggested that the Board of Treasury be authorized to take the proper measures to carry said resolution into effect. The Committee on the Treasury, under date of April 21, 1779, recommended "that twelve million dollars be borrowed on life annuities. Your Committee have reason to think that a plan of this nature would be very acceptable to the citizens

* The title of this work is "The Plan of a Society for Making Provisions for Widows by Annuities for the Remainder of Life, and for Granting Annuities to persons after Certain Ages, with the proper tables for calculating what must be paid by the several members in order to secure the said advantages," by Wm. Gordon, Boston, 1772.

of these States and meet with great encouragement." * No action was taken by the Congress in this matter, but the proposals are of much historical significance, and the first suggestions for Government Annuities in the United States. The refusal of the Continental Congress to act in the matter was, no doubt, due to the fact that the outlook for practical success, considering the poverty of the country and the novelty of the idea, was very doubtful.

Underwriters' Agreements Before the Revolution.

The insurance partnerships, or so-called "companies," in Boston had, no doubt, been established after similar enterprises in Philadelphia, dating from 1757. There also an effort to organize a company had failed (as fail it had to, because of the prohibitory Act of 1720), but a branch office was established in New York on August 21st, 1759, which illustrates the viewpoint common to the period, that in all matters of trade, including insurance, State lines were not a hindrance to the greatest possible development. Nor was there much need of apprehending a conflict with some other Provincial authority, since all insurance was transacted simply by conforming to common law principles designed to protect the public against fraud. The first combination, more or less in the nature of restraint of trade in insurance, including the "fixing" of rates, was perfected in Philadelphia as early as Feb. 12, 1762, and many similar arrangements for the protection of the underwriters were entered into from time to time, all being more or less ineffective on account of increasing competition. In 1762 it was again proposed to organize an insurance "company" in Philadelphia, but nothing came of the effort. In 1766 a very suggestive arrangement was entered into by the several industrial undertakings of Philadelphia and in 1774 a "New Lloyds Institution" was

* Journals of the Continental Congress, published by the Library of Congress, Worthington C. Ford, Editor, Washington, 1909, Vol. XIV, p. 520.

established, no doubt in opposition to, but largely on the plan of the Lloyds of London.

Effect of War Upon Premium Rates.

The first meeting of the Continental Congress (Sept. 4) this year put an end to all hopes of a peaceful settlement of the difficulties with the mother country, and insurance rates rapidly increased, particularly in the seacoast towns. The effect of war on fire insurance premiums in New York is evidenced by the statement that "We do not so much as think of shipping anything to anybody till we see affairs wear a very different aspect; indeed, all our other friends with you positively forbid us to ship a single article until further orders, and seem much surprised that they have any goods coming. Twelve Guineas per cent. premium is now given here to insure goods at New York from fire and the enemy till 1st of April next, and Twenty Guineas per cent. have been given to pay a loss, if our troops are not in possession of New York the first of this month, and we have every appearance of a French and Spanish war."* But, of course, the chief effect of the war was upon the insurance premium upon shipping, which often reached prohibitive proportions. The Government was concerned with other matters than insurance; even if the business had called for such attention, the transactions were of too limited an extent to merit much consideration as a possible source of taxation. When, therefore, the Constitutional Convention met in 1789 insurance was about the last and the least demanding inclusion in the deliberations of that body, being thought of, no doubt, as a mere incident of general trade, although at least three of the delegates to the Convention were personal underwriters.† The commerce clause, as finally adopted, in admirable terms, comprehended *all* the instrumentalities of commerce, then in use or subsequently to be developed, and while not specifically mentioned, as a needless qualification of a general

* Fowler, History of Insurance, p. 31.

† Ibid, p. 40.

principle, insurance (in view at least of what has here been written) was undoubtedly understood by the framers of that instrument to come within the meaning and scope of the commerce clause.*

INSURANCE AT THE TIME OF THE CONSTITUTIONAL CONVENTION.

The foregoing account of the origin and development of American insurance practice, law and institution, to the year of the Constitutional Convention in 1789 is a full and complete refutation of the wholly unwarranted statement in the Report of the House Committee on the Judiciary upon the Regulation of Corporations and the constitutional aspects of insurance regulation by the Federal government. In that report it is stated that "Insurance is not some new matter, developed after the Constitution was adopted, like railroads and telephones and things of that kind, but insurance was well known long before the Constitution was adopted and insurance *companies* were in active operation in this country long before the adoption of the Constitution, and ever since the adoption of the Constitution it has not been considered as an article of commerce." There were no insurance corporations in 1789, nor could there have been on account of the Act of 1720, which distinctly forbade their formation in the colonies, and it was wholly improbable that such corporations should have come into existence during the trying times of the Revolution, when men had other things to do than experiment in new fields of finance, or engage in even quasi-public enterprise of this kind. The Committee on Judiciary of the House of Representatives had, therefore, no evidence to support the statement just quoted but upon which they rest in part at least

* The fullest discussion of the whole question of insurance as an element of commerce within the meaning of the commerce clause of the Constitution, is to be found in Papers and Addresses of John F. Dryden, President of the Prudential Ins. Co. of America, Newark, N. J., 1910, Chapter XIX; see also the Argument for Federal supervision of insurance, prepared for the Senate Committee on Judiciary, by Richard V. Lindabury, of Newark, N. J.

their argument that insurance is not within the meaning of the commerce clause. The Supreme Court decisions, to which subsequent reference will be made, seem to have no conclusive bearing upon the question whether the *business* of interstate insurance, which now constitutes 82% of the existing amount of life insurance contracts in force in the United States is within the meaning of the commerce clause of the Constitution or not. The Supreme Court never considered *this* particular question, which is separate and distinct from the cases which have been decided and it would be an abject surrender of legislative authority on the part of Congress to hold that Congress cannot rightfully legislate upon the subject, leaving it of course to the Court to decide whether such legislation would be constitutional or not. The whole history of the business of insurance is, in fact, opposed to the theory that insurance is not commerce or an element of commerce by the common consent of the commercial nations of the world.

Beginning of Corporate Insurance Enterprise in America.

Insurance companies in America, properly to be so-called, as distinct from the four associations (all limited to Philadelphia) which have been referred to, did not come into existence until 1794, or five years *after* the adoption of the Constitution. A number of persons interested in or familiar with insurance principles had hoped to carry a tontine and annuity proposition into effect, and which at the time was attracting some public attention. They, therefore, organized in 1792 the Universal Tontine, and contemplated, no doubt, to transact business in all the states then constituting the Federal union. The originators of this plan included citizens of Philadelphia and Boston and the scheme was based upon the idea of the Boston Tontine Association, established in 1791, which also failed of its original intent and ultimately became a State Bank (the Union). A similar proposition in New York also came to nothing, but out of the plan of the Universal Tontine, which, as

the name implies, purposed to be national or general in its scope, developed the Insurance Company of North America, which also, as its very name *proves* beyond the peradventure of a doubt, intended to become a national institution and not a local trading concern—national and commercial and unequivocally within the meaning and the scope of the commerce clause of the Constitution, adopted but three years before.

The organization of this company (which is still in a very flourishing condition, after 117 years) was completed in the same room of Independence Hall, in which 16 years before the Declaration of Independence had been adopted and while yet a mere organization and without a charter and not even certain of obtaining one, it was proposed by the 8th Article of Association "to make such insurance upon vessels and merchandise at sea or going to sea, or upon the life or lives of any person or persons, or upon any goods, wares, merchandise, or other property gone, or going, by land or water; at such Rates of Insurance or Premium as they shall deem advisable." The first policy of insurance issued contained the phrase "and it is agreed by us the assurers that this writing or policy of insurance shall be of as much force and effect as the surest writing or policy of insurance theretofore made in any of the United States or elsewhere."

First Insurance Legislation in the United States.

The plan for the new organization was received with much public approval and steps were taken to procure a charter, and in the meantime business was commenced at once. A Bill was accordingly introduced into the Legislature of Pennsylvania, dated April 2, 1793, which is the earliest authentic date on record of legislative action in America since the adoption of the Constitution towards creating an insurance corporation as a trading concern. The act reads in part "Whereas a company has been formed in the city of Philadelphia and a competent capital thereto subscribed for the purpose of carrying on the business of insurance and application has been made

to the Legislature by the said company for an act of incorporation. In order therefore to promote an institution which by alleviating the risks and losses incident to trade and navigation must in its operations be equally beneficial to the agricultural and commercial interests of the state, etc."

In anticipation of opposition in the Legislature to the granting of a charter, which many supposed would confer monopolistic powers and privileges equal to those of the two London Companies, a carefully framed petition had been presented to the Legislature under date of Dec. 18, 1792, which in part read as follows:

"That your petitioners, attached to the public welfare, behold with the greatest satisfaction the commercial pursuits and interests of the United States becoming daily more numerous and important; but they have long regretted that, for want of sufficient number of underwriters of responsibility in the principal cities and towns of the United States, *commerce* is Burthened with the charge of commissions to European correspondents for effecting insurances, and large sums of money are consequently drained from the country."

In continuation it was said:

"That your petitioners humbly conceive that considerable benefits will result from this association as well to the citizens of this commonwealth in general, as to the mercantile part of this community in particular, by retaining in the state the money invested in their capital stock and the large sums that must otherwise be drawn from the country for premiums of insurance, by relieving *commerce* from the present tribute paid to foreign underwriters, and by securing the assured through the means of an ample capital stock from a possibility of loss, which in the manner of making insurances heretofore practiced both frequently happened through the failure of individual underwriters."

State Recognition of Insurance as an Element of Commerce.

The references to the benefits resulting to commerce from insurance are extremely suggestive, particularly when taken

into consideration with similar implications in the Bill itself. The opposition consisted chiefly of individual underwriters, whose interests, however, were briefly considered in the report upon the Bill made to the Legislature under date of March 11, 1793. In that report it is said

"That no *commerce* or navigation could be beneficially conducted without insurance, no body chusing to commit considerable property to the ocean, without guarding against the numerous accidents to which it would be thereby exposed.

That insurance cannot be so well conducted by individuals as by an incorporated company, for want of that identity that would enable such a company to be sued in case of loss, where justice could be had much more speedily than in suing every separate underwriter to a policy, a work of such immense expense and loss of time, as frequently to defeat entirely the object of insurance.

That solidity is also to be considered, which it is impossible to attain with certainty with private underwriters, whereas this Company's proposed capital of 600,000 dollars in the public funds, will be a sufficient guarantee to those who employ them.

That already the charges of insurance have been considerably abated since the establishment of this company, whereby a great saving to the mercantile body is effected, who can afford to give so much more for the produce, as they pay less for insuring it.

That the number of persons underwriting in Philadelphia, does not at present exceed about fifty, and the risques they take, being on an average only about £200, on a single bottom, of course only about £10,000 can now be insured at the different offices here on a single risque, which occasions a drain of money for insurance to Europe, or to the neighboring States, very prejudicial to the body of this one.

That it is not in the contemplation of the petitioners to exact or ask for themselves any exclusive privilege of insurance, so that those private underwriters, or any others, may still go on to insure, as heretofore, for those who will employ them; consequently that only a competition on a more enlarged scale will ensue very beneficially to the carrying on of the business in question.

That in almost all commercial countries similar incorporations exist; that in our own there are such for insuring

houses from loss by fire, it would not be easy to shew why the present Company should not be incorporated on the same or like principles."

Conformity to English Law and Precedent.

Accordingly the Committee resolved to bring in the Bill referred to. The legislative history of the measure reveals much valuable information concerning views on the commercial aspects of insurance and the reasons for its ultimate passage as an act conducive to the advancement of trade. As a compromise, however, it was finally agreed to incorporate also and at the same time "The Insurance Company of the State of Pennsylvania," practically repeating the statute of 6 George I (1720), establishing by Royal Charter two insurance exploitations at the same time, that is, the Royal Exchange and the London Assurance. The bill for the charter of the Insurance Company of North America was signed by Governor Mifflin on the 14th of April, and the bill for the chartering of the Pennsylvania company on April 18th, 1794. Thus came into existence the first two insurance *companies*, properly to be so called, in the United States of America.

No Restraint upon Interstate Trade in Insurance.

The business of the Insurance Company of North America at the outset was chiefly that of marine underwriting, which always has been and by its nature must be more or less interstate and international in scope and character. The fire business at first was limited to the city of Philadelphia, but as early as 1795 the field was enlarged to a territory of ten miles around the city, which, of course, included a part of New Jersey. It gradually became the practice to issue policies in other places and the business was systematically extended from year to year. In 1807 upon a special request that the company operate in Lexington, Ky., a committee was appointed to consider as to whether it would be to the benefit and prosperity to extend insurance against fire generally to other cities and towns

in other states, and after this agents were gradually appointed throughout the country. A London company, the Phoenix, had likewise established agents through the different states and in neither case was it assumed to be necessary to obtain special legislative permission from the several states to transact an interstate business in insurance, any more than this, under the new Constitution, was necessary for the interstate development of business generally. The Phoenix had come to the United States in 1806, but it only remained for a few years, returning to the United States, however, in 1879.

Insurance National in Scope and Operation.

A record has fortunately been preserved of an advertisement of the Insurance Company of North America, published widely throughout the country at the time, dated February 13th, 1796, in which it is stated that " The Insurance Company of North America [offer] to accommodate the publick *throughout the United States* with respect to insurance for fire, etc., etc." It, therefore, requires no further proof that the company assumed from the outset of its business operations that its field would be the whole United States and not the state of Pennsylvania, only and that its charter rights and privileges included the authority to do an interstate business. In this respect the company did not stand alone, for the next most important institution of its kind, the Massachusetts Fire and Marine, chartered under date of June 25, 1795, but operating under a charter limited to a period of twelve years, announced as early as September 23d of that year that " The company will receive proposals for insurance from any of the cities of Massachusetts, New Hampshire, Rhode Island and Connecticut." There can, therefore, be no doubt but that the position of these early companies was from the outset in favor of a national, rather than a local, and interstate rather than an intrastate business, and they had no reason to think otherwise until state jealousy and retaliation brought about a condition of law and legislation properly described as interstate chaos.

Advantages of Insurance Transacted by Corporations.

The Massachusetts Fire and Marine Insurance Company had its origin in a petition to the Massachusetts Legislature in 1795, in which, among other forcible arguments in favor of insurance by an incorporated company, it was stated that "The early establishment and continuance of similar Institutions in all parts of Europe may be produced as conclusive evidence of their beneficial effects. And Experience has taught that this species of Insurance must be performed by Companies, or corporate Bodies, having large and permanent Funds at immediate command, in order that the business may be carried to so great an Extent as to embrace any object that may offer, and still afford full Security to the Insured, without producing inevitable Ruin to the Insurers, in the greatest Losses that may probably take place." In answer to this petition a carefully framed charter was approved by the Legislature, dated June 25, 1795, in which the name of the new company was given as "The Massachusetts Fire Insurance Company."

Inception of State Supervision and Control in Massachusetts.

The charter of the company required the capital to be invested either in the funded debt of the United States, or the State of Massachusetts, or of any incorporated Bank in the State, thus early establishing the important principle of limited legislative control over the investments of insurance companies' funds. It was further provided that "no proprietor or voter shall be entitled to more than ten votes," by which the Legislature asserted its right to control the management of an insurance company in the interests of the general public. The charter was for a term of only twelve years, emphasizing the importance placed upon legislative control of institutions of this kind and the right to terminate the existence of an institution which might under certain circumstances prove contrary to the public good. The principle of charter limitation

may have been copied from the old Hamburg Marine Insurance Company ,which from 1765 operated under successive charters of ten years' duration for many years. The national character of the Massachusetts company, as previously stated, was asserted from the outset, but as a matter of permanent record, the following advertisement, published under date of November 11, 1795, is given in full: "The President and Directors of the Massachusetts Fire Insurance Company, hereby give notice, That they shall not in future, confine their Business to the four Eastern States, but will receive Proposals at their Office, in State Street, and make insurance for any citizens of the United States, on Dwelling-Houses, Stores, and all other Buildings; and on Goods, Wares and Merchandise agreeably to their Rules and Regulations, as heretofore published. By Order of the Board of Directors, Samuel Cabot, Sec'ry. N. B. The Printers *throughout the United States* are requested to publish this Advertisement. Boston, Nov. 11, 1795." The advertisement conforms to the corresponding announcements of the Insurance Company of North America and indicates that competition, aside from other reasons, would suggest a national scope of operations as legitimate and within the charter rights and privileges of the company.

The Boston Fire and Marine.

The commercial aspects of the business are also clearly indicated in an early notice, dated "Fire Office," October 7, 1797, in which occurs the statement that "The Company insures on Estates held on Mortgage, or lease for years, *and to accommodate Trade*, on Goods for one month or more." But the business was small and in three years the company had written only 1,096 policies. It is estimated that probably not over three or four hundred individuals had taken out fire insurance with the company during this period. To increase the insurance it was decided to add a marine branch and after the usual petition had been presented to the Legislature an amended charter was granted on the 13th of February, 1799, by which the name

of the company was changed to "The Massachusetts Fire and Marine Insurance Company." A similar petition having been presented the same year, praying for a charter to establish "The Boston Marine Insurance Company," both charters were granted at the same time, probably in imitation of the charter of two similar institutions in London in 1720 and in Philadelphia in 1794.

Beginnings of State Supervision and Control in 1799.

The Act under which the Massachusetts Fire and Marine Insurance Company was re-incorporated is of great historical value in connection with inquiries into the origin of insurance law and legislation in the United States of America. The new charter imposed additional requirements upon the company and among others the duty "That said Corporation previous to their issuing any Marine Policy of Insurance, shall publish in two of the Boston newspapers the amount of their actual Funds, the periods when the remainder will be paid, the greatest amount to be taken upon any one Vessel or house, and the risques they propose to insure against; and they shall keep a fair printed copy thereof in some conspicuous place in their Office, and publish the same annually. And the Real Estate which said Corporation are authorized and empowered to hold and purchase for transacting the business of said Company, may be to the value of Twenty Thousand Dollars and no more." a further qualification was the limitation of the new charter to a period of twenty years and to this limitation was added the extremely significant requirement by Sec. 8, that "the President and Directors of said Corporation shall when, and as often as required by the Legislature of this Commonwealth, lay before them such a statement of their affairs, as the said Legislature may deem it expedient to require, and submit to an examination thereon under oath."

By this important section the principle of state supervision and control over the business of an insurance corporation was established, practically at the very beginning of corporate underwritings in the United States, and I cannot do better

than quote the words of Mr. E. R. Hardy, who first called public attention to this remarkable document and who, in commenting upon this particular provision, said "The section that perhaps of all others has had the most far-reaching results is number eight. It is not found in the original charter, but in that section there was planted the seed of that mighty system of insurance supervision which dominates the business not only in Massachusetts, but throughout the land; and whenever some one asks for the beginning of insurance supervision in Massachusetts, tell him February 13, 1799."

Insurance Charters of Limited Duration.

The charter of the Boston Marine Insurance Company has not been preserved in its entirety and there is some doubt as to whether the same contained the important provision of Sec. 8 of the charter of the Massachusetts Fire and Marine. The Company's charter, however, was also limited to twenty years. An early announcement of the business to be transacted makes it evident that the term "marine insurance" was construed in a broad manner, for it is said, "The President and Directors of said Company are now ready to receive proposals (at their Office in State-street, Boston, lately occupied by the Branch Bank) and to make insurance upon Vessels, Freight, and Goods; and against captivity of persons; and on the life of any person during his absence by sea; and in cases of money lent upon bottomry, and respondentia; not exceeding thirty thousand dollars, on any one risque."

After these charters had been granted many similar corporations came into existence, but no new principles of law or legislation may be said to have been developed additional to those stated to have been expressly set forth in the early charters of the Philadelphia and Boston companies. The chartered companies soon proved their superiority over the early forms of individual underwriting, which gradually fell into disuse and finally passed away, as no longer adapted to the more complex commercial conditions of the present time.

First Act of Congress on Insurance (1797).

The earliest mention of insurance legislation by the U. S. Congress occurs in the Lex Mercatoria Americana, by George Caines, published in 1802. It is said in this work that " Neither by the acts of Congress, nor those of the different state legislatures, are there any positive regulations of the formal parts of the instrument of insurance: but custom has shown what they ought to be; and, in what appertains to trade, let it be constantly remembered, that custom alone is a law." Congress had, however, as early as 1797, passed a stamp act conforming in its essentials to the stamp duties imposed by the stamp act of 1765. In referring to this act in a discussion of the necessary formalities required for the lawful completion of the insurance contract, Caines remarks that " the proper stamp constitutes with us, the last requisite; and without it, the policy is not only void, but unless made out and duly stamped within three days after the insurance, induces a forfeiture from the insurer of $20 for every offense." The stamp duty referred to was enacted at the first session of the fifth congress (Chap. II, sec. 4) on July 6, 1797, and the act reads in part as follows:

" From and after the 31st day of December next there shall be levied, collected and paid through the United States the several stamp duties following, to wit: ..... any policy of insurance or instrument in the nature thereof, whereby any ships, vessels or goods, going from one district to another in the United States, or from the United States to any foreign port or place, shall be insured, to wit; if going from one district to another in the United States, 25 cents; if going from the United States to any foreign port or place, when the sum for which the insurance is made shall not exceed $500, 25 cents; and when the sum insured shall exceed $500, $1.00. ..... Any certificate of a share in any insurance company or any certificate of a share in the Bank of the United States, or of any State or other bank, above $20, and not exceeding $100, 10 cents; above $100, 25 cents; and for any certificate for every such share under $20 at the rate of 10 cents for $100, etc."

" Section 3 of this Act provided, "And, be it further enacted, that all deeds and writings whatsoever, or the payment of any

sum of money, upon the contingency of the loss of any ship, or goods, laden or to be laden on board of any ship, or of damage thereto, within this Act chargeable with the several rates of duty hereinafter mentioned."

Power of Congress to Supervise and Control.

There are a number of additional references to insurance, penalties, etc., in the act, but the most important of these is section 9, which, by implication at least, suggests the power of congress to supervise insurance companies and which reads:

"And, be it further enacted, that the several duties aforesaid shall be levied, collected, received and accounted for, by and under the immediate direction and management of the supervisors and inspectors of the Revenue and other officers of inspection, subject to the Superintendent's control and the direction of the Treasury Department, according to the respective authorities and duties of the officers thereof."

The act was limited to a duration of five years, but the exact date of repeal is somewhat doubtful. It is quite probable that the duties were continued in force by subsequent acts providing for a general stamp office, dated March 3, 1801 (Chap. XIX) and August 2, 1813 (Chap. LIII). No reference to the act of 1797 occurs in any of the writings on American insurance law and legislation, and the same seems to have escaped entirely the learned commentators, nor is there any reference thereto in the debates of congress leading to the enactment of the stamp duties imposed upon insurance companies during the Civil War.

Development and Growth of American Insurance Law.

Near the close of the 18th Century the business of insurance in the United States was still of very small extent and practically limited to the large seaports of the North Atlantic coast. Gradually, however, the practice of American underwriting assumed a definite character of its own and the increasing number of chartered corporations for the transaction of an insurance business naturally directed attention to the

state of the law and the required special legislation. The decisions of Lord Mansfield governed in most of the early cases and Park's classical treatise on the Law of Insurance, first published in London in 1786, had been issued in several American editions by 1810, when the great work on Insurance Law by Samuel Marshall came out in an American edition by Condy, considered by most of the writers on the subject of superior merit to the original, first published in London in 1786. The early development of American insurance law may be traced in the various American cases cited by Kent in his Commentaries, first published in 1826, but one of the most suggestive occurrences was the veto of the Council of Revision of the State of New York, under date of April 6th, 1807. A bill had been introduced entitled "An Act to restrain insurance of lottery tickets and for other purposes" and after having been referred to the Council of Revision (long since abolished) the following objection was made by Kent, Chief Justice, on the ground that the bill was inconsistent with the public good and the Constitution, because by its last section the bill declared "it to be unlawful for any company not incorporated by the laws of this State, or of the United States, or any private individual not residing within this State, to set up and keep within this State, by their agent, or otherwise, any office to insure houses or goods against fire, or vessels or merchandise against maritime losses, and that every such insurance shall be void, and every person receiving any premium therefor shall forfeit double the amount thereof." The Chief Justice argued that "This provision is inconsistent with the second section of the fourth article of the Constitution of the United States, which declares that 'the citizens of each State shall be entitled to all privileges and immunities of citizens in the several States.' This intercommunity of privilege secured to the citizens of the several States applies to their personal rights and immunities, and among others, to the free right to exercise trade and commerce."*

* The question involved in this controversy is quite fully discussed in the Special Message of Gov. Morgan Lewis, in 1807, printed in full

Freedom of Trade and Contract in Insurance.

In continuation, upon the general merits of the bill, Kent pointed out that, "The bill is repugnant to the general good, A contract of insurance, when founded on a substantial interest. and not perverted to gambling purposes, is one of the most useful species of contracts which arises in the whole course of *commercial transactions*. It ought to be left freely to be made, and not placed under the restrictions of a monopoly. If a company or an individual in another State will insure upon more reasonable terms, or possesses a sounder credit, or a more prompt disposition to adjust losses than any with us, why should a citizen of this State be denied the privilege of obtaining such insurance? And if his privilege to do so is admitted to be entire and perfect, why should a legal embarrassment be thrown in his way by prohibiting such insurances through the means of an agent here? It is a plain and most convenient rule of law, that all contracts are equally valid when made by an authorized agent as when made by his principal; and this rule ought not to be set aside, without some important object which is cogent in its reason and general in its application."

It is a remarkable fact that this extremely suggestive opinion, in favor of free intercourse between the states in matters of insurance as an element of commerce should never have been referred to by anyone who has written on the subject.

Retaliatory Legislation and Interstate Conflict.

The subsequent history of this effort is rather obscure. A similar law had been passed in Pennsylvania and in 1829 the Legislature of New York prohibited marine insurance, or lending on respondentia or bottomry, effected within the State "to all persons and companies residing in any foreign country acting by an agent here." According to Kent, "Persons and associations in other States effecting such insurance in New

in Vol. I of the " Messages from the Governors," re-published by authority of the State of New York, Albany, 1909, p. 613.

York were taxed ten per cent. on their premium" and the same check or prohibition applied to insurance against fire in New York. Thus the doctrine of prohibitory, retaliatory, or discriminating legislation on insurance, first enunciated by Count Phillip of Burgundy in 1458 is even in this country over eighty years old at the present time. Kent, however, remarked with regard to Massachusetts in this respect, that the law in that State was "more liberal and it allows, by the Act of 1816, corporate insurance companies in other States and in foreign countries to insure by their agents *upon compliance with certain conditions* intended to guard against abuse."

Legislation of this kind naturally increased with the growth of the business and new laws were called for by the separate organization of life insurance companies of which the first were the Pennsylvania Ins. Co. for the Insurance of Lives, established in 1814, and the second the Massachusetts Hospital, established in 1818. Of these two interesting institutions no full historical account has been preserved, but it may be stated as a fact that from the beginning they were the subject of special solicitude on the part of the States from which they derived their charters as moneyed corporations accumulating large funds upon long deferred contractual obligations.

Gradual Increase in State Legislation.

The principle of accountability had been laid down in the charter of the Massachusetts Fire and Marine in 1796. Charters were not easily granted and as early as 1823 a memorial was presented to the New York Legislature praying for the incorporation of an insurance company, which had evidently failed to secure a charter at a previous session of the Legislature. The business was rapidly growing and in 1825 a "Statement" was published of "all insurance companies in the State with the amount of capital stock authorized and amount actually paid in, amount of tax assessed stock, etc.," followed in the same year by a "report" upon supposed violation of their charters by certain insurance companies, and a report of the

Attorney-General on "questions affecting the right of the Legislature to alter, modify, or amend any act incorporating an insurance company." There was a further report this session of a select committee on the subject of banks and insurance companies, all of which may be considered proof that the business of insurance, at a time when by modern standards only a limited amount was actually done, was considered semi-public in character and fully within the supervising and regulating powers of the State Legislature.

Required Publicity and Statistical Returns.

In 1827 the Comptroller of the State of New York made a report on the capital employed in banking, insurance and manufacturing companies in the State and the amount of tax assessed upon the same and from 1830 onward annual returns were required of all insurance companies chartered by the State, until the year 1860 when an insurance department was established with full power of supervision and control.

Growth of the Insurance Business.

The evolution of insurance law and legislation in other states has been much the same. Out of crude beginnings a most elaborate system of supervision and control has slowly developed, until a point has been reached when a large part of the business, particularly the life branch, has practically become public in character, with a more or less implied guarantee on the part of the State for company solvency and guarantee of good faith. Most of the early chartered companies were out of existence fifty years after. A return prepared in 1861 showed that out of 336 insurance corporations chartered by that year only 114 were still in existence. Of 23 companies chartered before 1810 only one remained active in 1861. The Massachusetts Fire and Marine, established with so much difficulty in 1795 had its charter revoked in 1848. The rapid rise of the whale fishery in Nantucket accounts for the establishment of the Nantucket Ins. Co. under date of June 21, 1804, and of the

Phoenix Ins. Co. of Nantucket under date of June 12, 1818. The first named ceased to do business in 1832 and the second in 1838. How the Boston Fire and Marine, established in 1799, came to an end is not officially known. The Newburyport Fire and Marine, established in 1799 came to an end in 1832, and the Salem Marine, established in 1800, ceased business in 1839. All of these cases illustrate the difficulty of success in insurance enterprise. The rise of commerce gave birth to many of these institutions and the decline ended their career. In no case is this better illustrated than in that the two Nantucket companies, which flourished with the whale fishery and ended with the decay of that remarkable industry in one of the historically most interesting localities in America.

Massachusetts Requirements of 1807.

The first statutory requirement of Massachusetts on the subject of insurance appears to have been a Resolve of 1807 under which insurance companies were to render an account of their affairs to the next General Court. This Act called for a statement of capital paid in, the character and amount of the funds in which the same was invested and the amount of outstanding risk—in other words, all the essential facts disclosing the business transacted by the companies. A consolidated account of the returns required under this Act and made from 1816 to 1866 was published in the insurance report for that year. In 1818 an Act was passed defining "the power, duties and restrictions, of insurance companies." This was probably the first general law on the subject of insurance enacted in the State of Massachusetts, but the Act would seem to have applied only to the companies transacting a marine insurance business. The Act provided in part that "All Insurance Companies which shall hereafter be incorporated under the authority of this commonwealth shall have power and authority to make insurance on vessels, freight, money, goods and effects and against captivity of persons and on the life of any person during his absence at sea and in case of money lent upon bot-

tomry and respondentia and to fix the premium and terms of payment." *

It was further provided that "such companies shall ..... publish in two newspapers printed within this commonwealth, one of which at least shall be in the town of Boston, the amount of their stock, against what risk they desire to insure, and the largest sum they mean to take on any one risk." Other provisions of the Act required them, whenever directed by the Legislature, to submit statements of their company affairs to that body and to be examined concerning them under oath; also forbidding them to write on any one risk a sum exceeding 10% of the capital stock of their respective company. In other words, the modern theory of supervision, examination, control and publicity was fully developed in all its essentials nearly one hundred years ago and the Massachusetts Act of 1818 merely carried into effect the principle of visitorial power included in the amended charter of the Massachusetts Fire and Marine Ins. Co. of 1795.

First Law on Fire Insurance in Massachusetts.

In 1820 an act was passed in Massachusetts granting specific authority to the several insurance companies in the State to insure against fire, which was the first general law on the subject of fire insurance, such authority having, up to that time, been granted only by specific charter. The most significant phrase in the wording of this act is that authority is granted to the companies to make insurance against fire..... upon property within the *United States*." It would seem at least that State boundaries were not considered a hindrance to the widest development of the insurance business at this time

Legislation Concerning Dividends and Annual Returns.

In 1836 a report was made to the Massachusetts Legislature on the regulation of time of paying insurance dividends. In 1837 a report was made favoring annual returns of insurance

*21st Mass. Ins. Rep., p. 201.

companies with power to enforce this requirement. Insurance supervision, properly to be so called, may, therefore, be said to date from this year and between 1839 and 1866 statistical returns were made, which afforded a fairly complete view of the business of the companies during this period. That the returns were more or less objectionable to some of the companies is made evident by a petition presented to the Legislature in 1847 "against laws requiring insurance companies to make annual returns of transactions," followed in 1848 by a remonstrance signed by C. W. Cartwright against the injustice of requiring insurance companies to make annual returns. More was apparently demanded of local institutions than of the companies of other states, for in 1854 a petition was presented to the Legislature asking that foreign insurance companies should make as full returns to the State as State companies. In 1856 a protest was made to the Legislature against insufficient insurance capital in the State to meet *wants of commerce*, followed by a recommendation that the Legislature charter one or two responsible marine insurance companies with large capital to relieve requirements.

Establishment of First State Insurance Department.

An Act had been passed in 1852 under which the Secretary, the Treasurer, and the Auditor of the State, were constituted a Board of Insurance Commissioners, charged with certain limited duties, and this office was continued under the codified statute of 1854, but it was not until the year following that a regularly organized and equipped Insurance Department was established, also, however, with the title "Board of Insurance Commissioners—the Board consisting of three members, appointed by the Governor with advice of his council. The Act is quite an elaborate document of ten sections. The Act provided, *inter alia*, that "The said Commissioners, or any two of them, at least once in every two years and as much oftener as they may deem expedient shall visit every insurance company, of whatever description, which has been or may hereafter be

incorporated by authority of this commonwealth and shall have free access to their books and papers and shall thoroughly inspect and examine into *all* the affairs of said companies and make any and all such inquiries as may be necessary to ascertain the condition of said corporations and their ability to fulfill all the engagements made by them and whether they have complied with the provisions of law applicable to their transactions," etc., etc.

By this Act the modern American system of State supervision came into existence in the year 1855, and to Massachusetts in this, and in so many other legislative reforms, belongs the credit of having made the best possible beginning so that other states could safely follow. Historical accuracy requires that mention should be made of the appointment of Insurance Commissioners by the Governor of New Hampshire as early as 1850 and the publication of abstracts of returns for the two years ending with 1851, followed by the publication of annual reports from 1852 onward to date. The first annual report of the Massachusetts Department was not published until 1855, but it is to Massachusetts that the nation is indebted for the modern system of State supervision, and not to New Hampshire.

Development of the State Supervisory Function.

In some of the states, the Auditor, State Treasurer, or some other fiduciary officer has been charged with general supervisory power, previous to the establishment of regularly organized special departments. In Vermont, the Secretary of State and the State Treasurer have been Insurance Commissioners since 1852. New York established an insurance department in 1860, and Connecticut and Indiana in 1865. California followed in 1868 and Missouri in 1869. In that year the Insurance Commissioner of New York could say in his annual report that "Government supervision of insurance companies is now an established feature in State government—New York, Massachusetts, California and Missouri have separate officers and distinct

departments of their executive government organized especially for this purpose." In 1870 many more states followed and to-day every state and territory has a more or less completely organized department for the supervision and control of insurancc orporations.

Over-Legislation and Interstate Chaos.

The growth of the principle of State duty and responsidility in determining and maintaining the contractual relations of parties to the insurance contract and the safe, sound and proper administration of insurance corporations has naturally been of a most varied character in the different states, and within the last generation an immense mass of legislation on insurance has been enacted, much of which is conflicting, contrabictory and uncalled for. The amount of law and legislation no the subject of insurance has been so considerable, particularly during recent years that no summary account would do the matter justice. The simple but effective statutes of an earlier day, when the business was small and the companies few, have been replaced by drastic regulating statutes, which in some cases amount to state management and practically make the State responsible for the final outcome of much of what is called insurance companies, experience. The states to-day fix all the fundamental conditions upon which at least the life branch of the business is conducted, the rate of mortality, the rate of interest and even the expense rate. The State upon this assumption of arbitrary authority commits itself to the doctrine of state responsibility with all that is involved in that doctrine considering the magnitude and growth of the business and its probable much greater magnitude in the future. Of insurance corporations, however, it is true, as of all state chartered corporations, that what the State has created the State may destroy. As well said by Davis, in his treatise on the origin and development of modern corporations, " The great fact of the history of the old corporations is that the state has wholly or partially absorbed their powers.

To such extent as the social activity of the surviving corporations has been supplemented in response to greater public demands, it has been done almost entirely through the medium of new institutions, created, maintained and administered by the State, and not through new corporations. The absorption of the powers of a corporation by the State does not imply merely the resumption of powers previously granted by it; some of the powers may have been inoperative, when granted from lack of subject-matter on which to have effect; on the other hand, it does not follow from the absorption of corporate powers by the state that the state continues to exercise them as the corporation has previously done; they may be allowed by the state to lie dormant under the influence of political theories repugnant to their exercise," and in continuation, "As an industry becomes more public in character, it is elevated in popular estimation above the owners of it and in a sense is separated from them,—it is idealized or personified. It appears to have rights and duties in itself, distinct from those of its owners. Is that not the same movement that resulted (in a somewhat different field) in the development of the legal conception of the "ideal personality" of municipalities? The law regards the capital invested in it as "clothed with a public trust," by virtue of which its owners have only a limited control of it; its patrons are regarded as entitled by law to the benefit of its services in return for a reasonable compensation. It is the increased dependence of men on physical things, grouped in great units such as systems of railway, telegraph and water works, that has contributed in a large measure to the growth of corporations." And finally, by the same writer, "It is beginning to be recognized that more government is necessary under the developed conditions now attained by society than under the comparatively simple conditions prevalent a century ago,—and that such increased government has actually been provided, not by the state but by corporations. The plain tendency to corporate life at present, in its relations to the state, is in the direction of subjection and submission to close supervision.

In history the state has never been satisfied with the mere supervision of corporations by commissions or otherwise; it would be against the teachings of history to expect that now the state will stop short of the complete absorption of the governmental features of corporations."

Conflict of Law and Need of Uniform Legislation.

The common law of insurance in America to-day is practically what it has always been and the doctrine of insurable interest governs still with the same force as when the gambling acts were first passed in 1754 and in 1774. It has been estimated that over 30,000 American insurance decisions* have been rendered by the courts and that 12,000 of these have been fought clear through to the highest tribunal during the last twenty years alone. According to the Legislative Index over 1,200 specific laws pertaining to the business of insurance were enacted during the nine years ending with 1908 and, according to the Hon. John F. Dryden, the present statutory requirements on the subject of insurance would constitute a volume of over five thousand printed pages. Early law and legislation on insurance has been forgotten, but the principles remain the same. Early law governed in all the essentials and left sufficient contractual corporate freedom to conduct the business in harmony with the law of social and economic development or growth. Out of the common law doctrine that insurance contracts shall not be contrary to public policy and that the rights of the respective parties shall be fully protected by the courts has slowly developed the modern doctrine of state supervision and control over insurance contracts and insurance corporations. The future of the business may be viewed in the past. There will not be less regulation but more, not less visitorial power of departments but more, not less publicity of facts and experience but more, until the corporations will serve, as completely as the nature of the business permits, the higher purposes and needs of the state.

* Law of Insurance, by Geo. Richards, 3d Ed., N. Y., 1909, p. xi.

Insurance as a Branch of Legal Science.

A whole century has passed since the first American insurance corporation came into existence, and not only has there been an enormous increase in the extent of the business itself, but an immense addition has been made to the law of the subject. Willard Phillips was the first to publish a complete treatise on the law of insurance as based upon American experience, and the value of the work is indicated by the fact that a second edition was published in 1834 and a new two-volume edition in 1840. In a brief preface to the first edition Phillips assigned to insurance its proper place as a science in the remark that "No branch of law can more properly be denominated a science, than insurance; and since this contract is substantially the same in different countries, and continues to be the same now that it was formerly, the decisions of courts, whether ancient or modern, and the opinions and reasonings of writers, whether American, English, Italian, or French, are equally applicable to it."

Kent's Commentaries on Insurance as a Branch of Commercial Jurisprudence.

No one, however, did more to raise the dignity of insurance law to a separate branch of legal science than James Kent, who, in his Commentaries, first issued in 1826, gave painstaking attention to every branch of the business, with a full account of the ancient foundations of insurance contractual law. He traced, in particular, the connection between the insurance law of England and the American Colonies to the early law and practice after the peace of 1783, holding that "During the colonial government of this country, as well as for the first fifteen or twenty years after the peace of 1783, the business of insurance was almost entirely carried on by private individuals, each taking singly for himself, and not *in solido*, a risk to the amount of his subscription. But incorporated companies began to multiply and supplant private underwriters, and the business of insurance in the United States is now carried

on almost exclusively by incorporated companies." Points of divergence are carefully pointed out and emphasized by moral reflections, which may well be read to advantage even at the present day. Thus, in regard to insurance as an aid to illicit trade, Kent pointed out, "It is certainly matter of surprise and regret, that in such countries as France, England, and the United States, distinguished for a correct and enlightened administration of justice, smuggling voyages, made on purpose to elude the laws, and seduce the subjects of foreign states, should be countenanced, and even encouraged by the courts of justice. The principle does no credit to the commercial jurisprudence of the age."

Utility of Insurance to Commerce and Navigation.

This reference to insurance as an element of commerce was not accidental, for in many other parts of the Commentaries Kent re-emphasized the commercial aspect of insurance transactions. The following suggestive statement is sufficient to prove conclusively that in the mind of this, the foremost commentator on American law, the insurance contract and the insurance business were not to be considered separate and distinct from commercial law and legislation generally. "The business of uncovered navigation or trade would be spiritless or presumptuous. The contract of insurance protects, enlarges, and stimulates maritime commerce; and under its patronage, and with the stable security which it affords, commerce is conducted with immense means and unparalleled enterprise, over every sea, and to the shores of every country, civilized and barbarous. Insurers are societies of capitalists, who are called by their business to study with profound sagacity, and with exactness of calculation, the geography and navigation of the globe, the laws of the elements, the ordinances of trade, the principles of international law, and the customs, products, character, and institutions of every country where tide waters roll, or to which winds can waft the flag of their nation,"

Principles of Ancient Law in Modern Legislation.

Every writer of authority on the subject of insurance previous to the decision of Paul vs. Virginia by the United States Supreme Court, that *insurance policies are not articles of commerce* within the meaning of the commerce clause of the Constitution, has emphasized the importance of insurance as an element of commerce and maritime navigation. Some of the most important principles of ancient insurance law have been incorporated into American law, and, for illustration, a rule from Le Guidon, the early French maritime code, of which it is said by Kent, that "It is understood to be a fixed rule, that if the ship be so injured by perils as to require repairs to the extent of more than half her value at the time of the loss, the insured may abandon; for if the ship or cargo be damaged so as to diminish their value above half, they are said to be constructively lost. The rule came from the French law, and is to be found in the treatise of Le Guidon, where it is applied to the case-of goods; and in respect to both ship and cargo, the rule has been incorporated into the American jurisprudence."* No authority, on the law of insurance, has failed to lay stress upon the commercial importance of insurance and among others Duer, by far the most learned of our American writers on the law of insurance, in his treatise published in 1845, in various parts of his work fully sustains this important connection.

Considerations of Federal Supervision and Control.

The conclusion that insurance is an element of commerce or an instrumentality thereof is fundamental to all efforts to broaden the scope of insurance law and legislation by making the interstate transactions of American insurance companies subject to Federal supervision and control. In a still broader sense the business is international and for nearly a thousand years some of the most important principles of maritime law relating to the insurance contract have been the same among the trading nations of the earth. By its nature the insurance business is

* See Kent's Commentaries, Vol. III, p. 329.

national and international and to limit its development or hinder its growth as a beneficent social institution by mere arbitrary considerations resulting from conditions of political expediency is to go contrary to the whole historical development of the fundamental principles which underlie the contract and the business of insurance as now carried on by corporate enterprise throughout the world. The ultimate regulation and control of interstate insurance transactions by Federal power is, therefore the logical development of insurance law and legislation which from its origin has been practically co-incident with the insurance contract itself. It is true that the United States Supreme Court has repeatedly held that insurance *policies* are not transactions in commerce, but the cases which have come before the Court have never involved the momentous issue of declaring an Act of Congress providing for Federal regulation of insurance companies transacting an interstate business null and void. The first effort to bring about such Federal regulation appears to have been made in 1853, when it was suggested that a convention of insurance presidents and actuaries "agitate for a more proper basis of taxation and agree upon a proper memorial to the Legislatures of all the States." for it was said, "it is desirable to have uniformity in these thirty-one sovereign States."* The effort was probably suggested by the Parliamentary investigation into Assurance Associations in England in 1853 and the movement to establish effective Insurance Departments in the more important Eastern States. The suggested convention did not materialize and nothing further seems to have been done until 1866, when the first bill providing for Federal regulation and control of insurance was introduced into Congress. This bill provided for a National Bureau of Insurance in somewhat the same manner as the new National Banking Act provided for the supervision and control of national banks, in place of the more or less insecure state banks of issue. The bill did not come up for discussion and did not become a law.

* Lectures on the Science of Life Ins., by Jos. L. Knapp, Phila., 1853, p. 154.

The Case of Paul vs. Virginia.

Two years later a case was decided by the United States Supreme Court in which it was held that "issuing a policy of insurance is not a transaction in commerce" and "these contracts are not articles of commerce in any proper meaning of the word." This case of Paul vs. Virginia has become the rock foundation of the opponents of Federal supervision of insurance, as not being within the meaning of the commerce clause of the Constitution. The decision has governed in a number of cases which have followed it and of which the most important is that of Hooper vs. California, which was decided by the Supreme Court in 1895 and in which it was held "that the *business* of insurance does not *generally* appertain to such (interstate) commerce has been settled since the case of Paul vs. Virginia." From a careful reading of that first decree, however, it does not appear that the same had reference to the *business* of insurance, but rather to only a single isolated transaction incident thereto and that is the *issuing* of a policy of insurance. Surely the enormous business of insurance is more and means more than the issuing of policies! But so the Court decided and the doctrine was continued in the case of New York Life vs. Craven in 1900. The Court in that case held also that "we only repeat the business of insurance is not commerce. The contract of insurance is not an instrumentality of commerce. The *making* of such a contract is a mere incident of commercial intercourse and in this respect there is no difference whatever between insurance against fire and insurance against the perils of the sea, and we add, or against the uncertainty of man's mortality."

Constitutional Aspects of Insurance.

These decisions notwithstanding, persistent efforts have been made to bring the business of insurance within the scope and authority of Federal law. Without passing upon the soundness of the Supreme Court decisions, as determined by methods of statutory construction which do not apply to general

arguments, it may be pointed out that as far as known the briefs filed with the various cases referred to do not disclose that any of the evidence derived from an extended historical inquiry into the origin, purpose, law and legislation of insurance was taken into consideration in the disposition of the cases referred to. In due appreciation of what is common knowledge on the subject, and with a due regard to the actual facts of insurance as an element of everyday commerce and commercial life, the Supreme Court decisions are opposed to the unbroken chain of evidence from the very dawn of insurance to the present day, and the legal reasoning of all the foremost authorities on the law of the insurance contract as an indispensable aid to the commerce of the past and the present day. In justice to the integrity and intelligence of those who have made the effort for Federal supervision, it is but right and proper that they should not be charged with having wilfully disregarded the decisions of the Supreme Court as laid down in the cases referred to, but that they hold to the belief that the regulation and control of the interstate business of insurance companies now having attained to enormous proportions, is a matter totally different and distinct from the very limited transactions and very narrow considerations of law and fact involved in all the insurance cases before the Court from Paul vs. Virginia to Nutting vs. Massachusetts.

Suggestions for Federal Supervision and Control.

The various bills that have been introduced into Congress do not require to be discussed here in detail. A bill for the Federal incorporation of insurance companies had been introduced into Congress in 1868 and an effort was made in 1879, which did not materialize or cause the introduction of a specific bill. In 1892 Mr. John Patten, M. C. for Ohio (also President of the Union Central Life Ins. Co.), introduced a carefully framed bill for Federal supervision and control, followed in 1897 by a revised bill, introduced by Senator Platt of Conn., and reintroduced in 1899. A very radical bill for Federal supervision

and national control was introduced into the House by Mr. Morrell of Pa. in 1903 and two years later Senator John F. Dryden of N. J. (also President of the Prudential Ins. Co. of America) introduced a bill drawn with extreme care and modelled largely after the National Banking, Bankruptcy and other Federal Acts. The bill was re-introduced in 1906, but it never came up for public discussion. In fact, none of the bills introduced from 1866 to 1906 were ever publicly discussed by the Congress, but dropped by committees and shelved.*

Errors Concerning the Early Status and Extent of Insurance in America.

While the second Dryden bill was before the Senate the Committee on Judiciary of the House of Representatives made a report on the regulation of corporations, including insurance, from which the statement has previously been quoted that "insurance companies were in active operation in this country long before the adoption of the Constitution." (1789). The Committee held that the language of the Chief Justice in McCulloch vs. Maryland was not applicable to the doctrine involved in the constitutional aspect of Federal regulation, but they said "perhaps the language quoted would be very apt if insurance had just been developed and discovered and recognized by the commercial world as commerce and would very properly belong to commerce. No one questioned but that all would concede that it would come within this definition of commerce as mentioned in the Constitution." As a matter of fact and history and as fully brought out by this inquiry into almost neglected sources of insurance information, insurance was practically unknown and unused in the Colonies and the States previous to the adoption of the Constitution in 1789 and the first insurance *corporation* did not come into existence until 1794! By their own reasoning, therefore, the House Committee on Judi-

* The two Dryden bills have been re-printed in full, with other matter pertaining thereto in Papers and Addresses, by John F. Dryden, Newark, N. J., 1910.

ciary gave endorsement to the view that upon the facts as here disclosed, the business of insurance is within an exact and historical definition of commerce and as such within the scope of the commerce clause of the Constitution.

Argument for Federal Supervision as a Constitutional Solution.

The whole argument in favor of the power of Congress to legislate upon the subject of interstate insurance transactions (which constitute 82% of the whole business in the life branch alone) was summed up by Mr. Richard V. Lindabury, of Newark, N. J.

"Whether or not insurance is commerce is a question of fact, the answer to which depends upon the ascertainment not merely of the inherent characteristics of insurance, but also of the usages of the commercial world with respect thereto. The finding of a court, therefore, upon this question in a particular case or class of cases does not bind the public or third persons or foreclose them from insisting to the contrary of such finding in any future action where the question may arise.

The question before the court in the insurance cases was not whether a State could regulate or prohibit interstate insurance, but whether it could do this with respect to insurance effected wholly within such State.

The decisions of the Supreme Court in the interpretation of the Constitution are not to be regarded as possessing the same element of finality as are their decisions establishing rules of property. The latter cannot be departed from without danger of disturbing titles or contract rights which may have become vested thereunder. The former, however, may and should be disregarded whenever necessary to maintain the fundamental law of the Constitution or to prevent the extension of an erroneous principle.

The power of determining whether or not a particular business shall be regulated as interstate commerce, and for that purpose of determining whether or not it is capable of being so regulated, is committed by the Constitution to Congress, at least in the first instance, and it cannot be assumed that the Supreme Court, by any declaration or abjudication in advance of Congressional action, intended to prejudge the

question of the rightfulness of the exercise of this power in a given case.

It does not follow that because at one time insurance appeared to the Supreme Court to be a mere incident of commerce, it must be forever and for all purposes so regarded. Nor does it follow that Congress, in determining the public policy of the nation, may not now declare that insurance shall hereafter be regarded and treated not as a mere incident o commerce, but as an integral part of commerce or as an important aid to or instrumentality thereof."

Wilson and Hamilton on Insurance as an Element of Commerce.

To this admirable summary there is nothing to add. It is a well-reasoned opinion, in strict conformity to the facts and in harmony with the view of James Wilson, himself a member of the Federal Constitutional Convention, who, speaking of the Law Merchant, said, "This system of law has been admitted to decide controversies concerning bills of exchange, policies of insurance, and other mercantile transactions, both when citizens of different states and citizens of the same state only have been interested in the event."* Equally pertinent and conclusive is the statement of Alexander Hamilton, who, in his official opinion to Washington upon the constitutionality of a U. S. Bank, enumerated among the powers of the government to regulate commerce with foreign nations, "the regulation of policies of insurance, the regulation of pilots, and the regulation of bills of exchange." †

Advantages of Federal Supervision of Interstate Insurance Transactions.

Upon identical facts and considerations rests the whole theory and persistent agitation of the advocates of Federal supervision of insurance. The foremost of these, ex-Senator John F. Dryden of New Jersey, in an address before the Newark

*Wilson's Works, Vol. I, p. 335.

† Hamilton's Works, by H. C. Lodge, Vol. III, p. 203.

Board of Trade, on January 18, 1906, summed up the results of his own distinguished efforts in the statement that,

"A Federal insurance law will not deprive the States of any rights specifically reserved to them under the tenth amendment. The States, under the bill introduced, will retain all the rights and powers over their own corporations which constitutionally belong to them, but the bill will put an end to the multiform system of State supervision and control over insurance corporations, which has no justification in any sound theory of constitutional rights or in any common-sense conception of State duty. The bill will put an end to interstate chaos and terminate an intolerable condition of affairs jeopardizing the interests and at times the very existence of companies transacting interstate business. The bill will establish insurance companies upon a national basis and give to the business a national character. The bill will bring insurance companies engaged in interstate business within the power and control of the Federal government and provide a system of supervision, examination and control, thorough, exacting and complete. The bill will increase the value of every form of insurance, materially enhance the security of the policyholders, and broaden the field of business operations to an extent impossible under the present system of supervision and control by some fifty different States and Territories. The States will continue to supervise insurance corporations of their own creation, but they will be deprived of power to supervise corporations of other States and to legislate regarding them, chiefly for the purpose of raising revenue or of harassing the companies by vexatious statutory requirements. It is not a theory, but a condition, which confronts the companies and their policyholders, who in their aggregate capacity represent the nation and not individual States. The policyholder is primarily and chiefly interested in the security and value of his contract, in the rate of premium which he pays, and in the safe and economical administration of the company with which he insures. It is not a question with him whether the company is located in the particular State in which he lives, or in any other State. As a life insurance policyholder living to-day in one State, he may tomorrow live in another, but his contract of insurance goes with him and protects and sustains him in the event of calamity or loss. It is not a theory that this business is national in extent and character, but an incontrovertible fact readily within the com-

prehension of any one who will carefully consider the vast extent of the business operations and the true character of insurance transactions. It is upon this ground that the advocates of Federal supervision rest their arguments and anticipate a favorable ruling from the Supreme Court in the event of the constitutionality of a law to this effect being brought to a test."

Apparent Futility to Bring About Uniform Legislation.

No answer has been made to this masterly summing up of the cause of Federal supervision of insurance. No answer can be made, save in the acceptance of the principles laid down and the conclusions warranted by the facts of history and every-day business experience. The day must come when the multitude of States will no longer have the power and unequivocal privilege to impair, by more or less ill-advised legislation, an institution of such vast social and economic importance as insurance. For the time being, however, the outlook for Federal supervision of insurance is practically hopeless. The alternative lies in the direction of securing uniformity of law and legislation. Efforts in this direction have also practically been failures. At least six distinct attempts at uniform codification of the American law of insurance have been made, but no practical success has been attained. The evils of over-legislation are made evident by the statement that during the nine years ending with 1908 not less than 1,200 specific laws pertaining to the business of insurance were enacted by the different States. These laws have reference chiefly to statutory requirements, which it would be an utterly hopeless task to summarize, on account of their variety and contradictions. The state of the common law is also one of chaos, conflict and dissimilarity. As was said by ex-Senator Dryden, "What is permitted to be done in one State, is forbidden in another; and what is the law of one year, may not be the law of the next. The whole subject is enormously complicated by retaliatory laws, which have resulted in a condition properly described as interstate warfare, unworthy of the civilization of the present day."

Need of a Uniform Code on Insurance.

Previous efforts in the direction of uniform legislation have been failures, but there is hope that expert codification for the District of Columbia may produce a model law, suitable for adoption by the different States. However, as said by ex-Senator Dryden, in his address on Uniform Law and Legislation on Life Insurance at the National Conference called by the National Civic Federation, in 1910,

"The task, at best, will be an arduous one and it will be the better part of wisdom to make haste slowly. Widely conflicting views and opinions will require to be harmonized and upon some matters irreconcilable differences of opinion will make a departure from standard requirements seem advisable. I am firmly convinced that a uniform code governing the essentials both of the public and the private law on the subject of insurance can be framed and the past experience of every life insurance company transacting business in the different States makes it desirable and proper that such a code should be prepared. Failing in this, the only ultimate alternative will be the supervision and control of the interstate business of American insurance companies by the Federal government. Convinced today, as I have been for many years, that such supervision is both constitutional and a rightful exercise of Federal power, I trust that the deliberations of the convention will do away with the possible necessity of Federal supervision by the enactment of rational and uniform insurance laws throughout the different States, Territories, and possessions of the United States."

Conclusions.

Law, like insurance, is a progressive science and legislation on insurance in the long run attains the desired object of increasing the security of the contractual relations and of enhancing the economic and social value of insurance institutions to the advantage of the State. All proper insurance law has aimed towards betterment, but almost from the beginning of the recorded history of the business there is evidence that the insurance contract has been held to be one peculiarly entitled to the interest of government. The principles of equity

and public policy which underlie the earliest insurance ordinances and laws also underlie the law and legislation of today. The law laid down in the Chancery case of 1693, as to insurable interest, is the law today. The statutory enactments have given dignity and force to the legal status of insurance and the business is now the most completely supervised, controlled and regulated form of commercial enterprise in the world. The theory of insurance supervision and control is therefore not new, but as old as the business itself. The theory of State supervision did not, as often claimed, originate with the organization of the Massachusetts Department, but it had its beginning in the Gambling Acts of 1754 and 1774 and the charter provisions of the first insurance company chartered by the State of Massachusetts in 1799 and the Act of that State passed in the year 1808. The theory of State supervision of interstate business has developed out of circumstances and conditions beyond the control of the separate States. The theory of Federal supervision of insurance is the logical solution of a vast amount of conflict in law and legislation, Federal and State. Insurance corporations, chartered by the State, tend more and more to become regulated and controlled even in matters of detail, standard policies, methods of valuation, limitation of expense and limitation of business, etc., until State responsibility has almost superseded full legal and moral responsibility on the part of the companies' administrative officers. Yet it remains true, more true to-day even than when it was written by Justice Holmes on the Common Law, that "The State might conceivably make itself a mutual insurance company against accidents, and distribute the burden of its citizens' mishaps among all its members. There might be a pension for paralytics, and State aid for those who suffered in person or estate from tempest or wild beasts. As between individuals it might adopt the mutual insurance principle *pro tanto*, and divide damages when both were in fault, as in the *rusticum judicium* of the admiralty, or it might throw all loss upon the actor irrespective of fault. The State does none of these things, however, and

the prevailing view is that its cumbrous and expensive machinery ought not to be set in motion unless some clear benefit is to be derived from disturbing the *status quo*. State interference is an evil, where it cannot be shown to be a good. Universal insurance, if desired, can be better and more cheaply accomplished by private enterprise."

The following suggestive words of Herbert Spencer may also aptly be quoted in this connection: "Which is the more misleading, belief without evidence, or refusal to believe in presence of overwhelming evidence? If there is an irrational faith which persists without any facts to support it, there is an irrational lack of faith which persists spite of the accumulation of facts which should produce it; and we may doubt whether the last does not lead to worse results than the first."* The whole history of insurance law and legislation sustains the belief and conviction that government supervision, regulation and control of corporations engaged in interstate business is a Federal and not a State function and it would be going contrary to the facts of history and the growth of human intelligence and the whole theory which underlies a representative form of government, that the highest enduring considerations of public policy should be made subservient to an abuse of the doctrine of *stare decis*, or even worse, to unworthy considerations of political expediency.

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CHAPTER V.

LIFE INSURANCE SUPERVISION AND GOVERNMENT CONTROL IN GERMANY*

The adequate and effective supervision and regulation by Government of insurance corporations is one of the most important and complex problems in political science. The magnitude of the business, and its intimate relation to public welfare, precludes the idea of a let-alone policy of government on the one hand, or of a too restrictive policy of legislative interference and control on the other. The latter is practically certain in the long run to do a vast amount of permanent harm. The conflict of opinion lies between these two extremes, and as an admirable compromise the insurance legislation of Switzerland, Austria and Germany is deserving of serious and critical consideration.

Insurance Legislation in Continental Europe.

The insurance laws of Switzerland were adopted by the Federal Council in 1885 and they have remained practically unchanged during the intervening twenty-two years. The Austrian regulations were adopted in 1896, and the German code in 1901. These codes and regulations govern the business of insurance in broad outlines upon the basic principles of equity and

* Address delivered at the Annual Convention of Insurance Commissioners held in Richmond, Va., in 1906. It has not seemed necessary to bring the statistical data down to date since the practice of the Department has undergone no material change in the meantime. For much of the information contained in this address I am under personal obligations to the President of the Department, Herr Gruner, who, on several occasions kindly extended to me the courtesies of his office, to facilitate my inquiry into a rather difficult branch of German administrative law.

public policy. They confer great powers of discretion upon the supervising authorities, while providing for the necessary technical and practical qualifications in the supervising officials. The codes contain few regulations in matters of administrative detail, which is probably the chief reason why in practice they have been so generally satisfactory and effective.

The German Insurance Code of 1901.

It was originally my intention to discuss in outline the insurance legislation of the three countries named, but after further consideration I concluded that it would serve a more practical purpose to limit my observations to the insurance code of Germany. While the code has been translated into English in the consular report upon "Insurance in Foreign Countries," (1905), the translation is crude, and in matters of detail decidedly unsatisfactory. On account of material differences in institutions and methods of government, it is a somewhat difficult undertaking to present the essential facts of German insurance legislation with such brevity as would be desirable. The general literature of the subject is very extensive and upon the code itself about a dozen commentaries had appeared within less than two years after the law went into effect. The official literature is also very considerable, including, among others, five annual reports upon the business operations of the Department, supplemented by three statistical reports and some twenty-three elaborate periodical publications issued at intervals of about three months, and many special publications of the Department. Of this wealth of information and experience I have, of necessity, had to make an arbitrary selection of such matters as seemed to me to be of most practical value as a slight contribution to the high aims and purposes of this convention.

Imperial Supervision and Control of Interstate Insurance.

The German insurance code applies to the whole of Germany, but not to the German possessions in foreign countries. The

law applies specifically only to private insurance undertakings which do business in more than one German state, or in a German state and a foreign country. The separate states, however, may arrange with the Imperial Supervising Department, established by the code for the supervision of local undertakings, and some of the smaller states have already done so, while others are expected to follow. State insurance undertakings in any form are not subject to the code, but remain subject to local laws and regulations. The compulsory system of government insurance is also outside of the operations of the code, being governed separately by the Imperial Insurance Department, which must not be confused with the Imperial Supervising Department of Private Insurance Undertakings.

Insurance Companies Considered Commercial Undertakings.

The code is the logical result of more than forty years of public agitation for certainty and uniformity in insurance legislation. In its general outlines the code conforms to the commercial law, and many provisions are by specific reference adopted from the commercial code. The code considers insurance companies from practically the same legal and administrative points of view as corporations generally and while previous to its adoption mutual companies and associations did not possess the rights and privileges of corporations, this defect in the law was corrected by the code of 1901. The code does not apply to marine and inland insurance, or to re-insurance companies, upon the theory that these undertakings are so strictly commercial in character and purpose that the commercial world is fully competent to protect itself against possible mistakes. Registered Friendly Societies and Miners' Benefit Funds are also outside of the scope of the code. The code is almost free from technicalities and is readily within the understanding of anyone with a fair degree of intelligence.

Code Limited to the Administrative Law of Insurance.

The code is limited to the administrative, or public, law of insurance. For the time being the private, or contract, law of insurance remains subject to the various conflicting regulations of the different states, but a code has been framed after extended and expert consideration, which would have passed the Imperial Parliament at its last session [1906] but for its unexpected dissolution.* Similar codifications of the private law of insurance are under consideration in Austria and Switzerland. The distinction between the administrative, or public, law of insurance, and the private, or contract, law is vital, and there is practically never any confusion upon these two branches of legal science in the legislation of European countries. The Germans have a strong inclination for technical excellence in the codification of their laws, and the insurance code represents many years of careful inquiry and consideration, with a due and impartial regard to all of the interests affected by legislation of this character.

Insurance an Element of German Constitutional Law.

The code, on the whole, has worked well in practice, to the satisfaction alike of the Government, the insurance companies, and the general public. There have been no changes or amendments to the law during the five and a half years since the same went into effect. Every provision of the code was framed upon the best obtainable expert and impartial advice. Its legislative history is a credit to the German people. who, with characteristic patience and thoroughness, deliberated long but wisely before making a fundamental law to henceforth govern so vast and important a social institution as insurance. The code also

* The code governing the contract of insurance was enacted in 1908, and in its entirety the same went into effect on Jan. 1, 1910. The code, as finally adopted, was the fifth proposal, the first having been prepared by the Imperial Dep't of Justice in 1903, and changed and amended proposals having been introduced into the Federal Council in 1905 and in the Imperial Parliament in 1907 and 1908.

reflects creditably the advancement of German insurance science in its legal, administrative, and technical departments. The code is strictly constitutional legislation, since by Article 4 of the German constitution insurance is included as one of the interests subject to imperial law, following in this respect the constitution of the North German Confederacy of 1866.

Public Interest in Insurance Legislation.

I need only very briefly sketch the legislative history of the code, which, however, is decidedly instructive as illustrating the method pursued to combine a high degree of technical perfection in matters of detail with efficiency in administration. After many years of public discussion, the first draft of the code was made public on the 26th of November, 1898, and immediately attracted universal and critical attention. The code as proposed conformed in its outlines to the law as subsequently adopted, but many important changes were found necessary and made in due consideration and after extended hearings of the interests affected. Naturally, there was at first considerable opposition to some of the more restrictive provisions of the code, but an expression of expert opinion was solicited from all in a position to make practical suggestions or give useful advice. How universal the interest in the question was, and how strictly commercial the point of view, is best illustrated by the fact that in addition to the national societies of German life and fire insurance companies, the various chambers of commerce throughout the Empire submitted briefs and arguments. Among others the subject was considered in detail at various commercial congresses and by the Association of German Agricultural Interests, followed by resolutions of the German Bar Association, German re-insurance companies, English life insurance companies, German liability insurance companies, and by an elaborate brief presented by the Elders of the Association of Berlin Merchants. The facts and arguments submitted by these bodies, and many others, are evidence of the careful and impartial consideration which

had been given to every important feature of the proposed law before the same was finally adopted.

Over Two Years Allowed for Public Discussion.

Upon this basis of fact and information the Government introduced a revised bill, which was submitted to the Imperial Parliament on the 14th of November, 1900. In other words, nearly two years were allowed for public argument and discussion. Every important provision of the law was discussed at length, and with remarkable ability, in numerous articles in the technical insurance press, by lawyers of the highest standing, and by prominent economists and teachers of insurance science in German universities. The Government itself did not assume an attitude of hostility toward the companies, nor did it press for undue haste in advancing the bill through its different stages. The bill was read for the first time on November 29, 1900, and referred to a commission of twenty-one members for further consideration and report. This commission included some of the foremost experts in insurance, and during its twenty-six sittings every interest was given an opportunity to present facts and arguments for or against particular provisions of the law. A final bill, in a modified form, was submitted to the Imperial Parliament on April 20, 1901, so that there had been an intervening period of five more months for further public argument and discussion.

Code Conforms to Expert Opinion and Business Experience.

The report of the commission is a model of its kind and deserving of the most careful study and reflection by all who would like to see the conflicting statutory requirements in this country upon the subject of insurance harmonized, to the decided advantage of the insurance companies, their policyholders and the state. In the final report of the commission every section of the proposed law is fully explained, not only in its immediate bearings upon the subject under consideration,

but in its important relations to existing codes of commerce, bankruptcy, civil rights, crimes, etc. The arguments for and against particular provisions are printed in sufficient detail to afford an insight into the facts and principles governing particular provisions of the law. The code as finally revised was submitted to the Reichstag during the latter part of April, and became a law on May 12, 1901. The law became effective on January 1, 1902, except such provisions as related to the organization, etc., of the Imperial Supervising Insurance Department established by the code, which went into effect upon its passage.

Scope and Purpose of the Imperial Supervising Insurance Department.

The code is arranged in nine general sections and 125 paragraphs. Important supplementary regulations were issued by the Federal Council, and approved by the Emperor, under date of December 23, 1901, which in thirty-six sections, govern the appointments and administration of the Imperial Supervising Department established by the code. The first section is general and defines the scope and purpose of the law. The Imperial Supervising Department has complete control over everything directly or indirectly appertaining to the methods, management, or experience of the companies and associations subject to its jurisdiction. The supreme power of the Department rests primarily upon the exclusive right to grant authority for the transaction and continuance of business. The rights and duties of the companies or undertakings are, however, clearly defined by the code, and except for specific reasons the Department must issue the permission, or what, for want of a better term, may be spoken of as a license to carry on the business of insurance.

Discretionary Powers of the Department.

Insurance undertakings, to obtain authority to transact business, must submit to the Department a complete statement of facts and information to clearly establish the nature

and purpose of the business to be transacted. The Department can decline to approve the application only when there is evidence (1) that the business plan is contrary to the law; (2) that the undertaking, for one of many reasons, may not be able to carry out its intentions or meet its present or future obligations; (3) when the proposed plan or method of insurance is contrary to public policy. To make sure that these requirements are complied with in all cases, a thorough preliminary investigation is made by the Department into all the facts presented, the object being, of course, to eliminate, if possible, at the very outset, inherently weak or possibly fraudulent insurance undertakings. In this respect the Department has been eminently successful. If a similar method were followed in the United States, every application for a new insurance charter would first have to be approved by the superintendent or commissioner of insurance. The provision of the German code is decidedly effective to eliminate wildcat, speculative, and fraudulent insurance enterprises.

Safeguarding Policyholders' Rights and Privileges.

As a further condition precedent to the required authority to transact business, the code defines the principles which must govern in the articles of incorporation or association and in the policy conditions. These may briefly be defined as emphasizing the necessity for a clear and specific statement of the respective rights and duties of the insuring company on the one hand, and of the insured policyholder on the other. The object, of course, is to provide both the stockholder and the policyholder with a readily understood statement of the conditions governing their relations to the company or association. No standard forms, however are, prescribed, nor is there an attempt at uniform regulation of the details of specific policy conditions. The law permits of a deviation from the general insurance conditions, but in cases where such changes may be construed as being contrary to the interest of the insured, as, for illustration, in the earthquake clause, the same must be

clearly and fully explained for the information of the policyholder, in which event the contract may be issued. In other words, there is no interference with contractual freedom on the one hand or with the liberty of legitimate business enterprise on the other. Before a contract of insurance can go into effect a separate copy of the policy conditions must be handed to the prospective policyholder, who must give a receipt therefor in writing. This requirement, however, does not apply to open policies of insurance issued in conformity to the practice of the Stock Exchange, the rules of which are applicable to strictly commercial agreements of this character.

Special Requirements of Life Insurance Companies.

On account of the more complex nature of the life insurance business, the code provides in detail for the safeguarding of policyholders' rights, privileges, and interests. The business plan of a life insurance company or association is defined to include the premium rates and the principles of their calculation, the rate of interest, and the loading of the net premium. No specific table of mortality is required, nor a specific minimum or maximum rate of interest. The use of the preliminary-term method is permissible for the first year to the extent of $12.50 per $1,000 of insurance. The mortality table used in the calculations is required to be stated, and the same is true of tables bearing upon the probability of accident, liability, and sickness. Every division of the life insurance business, such as endowment, limited payment life, annuities, etc., must be explained in detail as to the formulas used in the calculation of premium rates and dividend apportionments, illustrated by examples in figures. If policies are issued at a higher premium, the business plan must show why, and on what principle, a special premium is to be charged.

Continuous and Complete Supervision.

The aim of the law is to provide the Supervising Department with all the necessary information to pass upon the in-

trinsic value of the proposed insurance undertaking. The Department is fully equipped with experts of the highest standing to render an impartial and trustworthy opinion upon the equity or technical soundness of proposed plans for insurance. All subsequent changes in the articles of association, or the policy conditions, or the business plan of the company, require the approval of the supervising authorities before the same can legally go into effect. As previously stated, the Department can decline to give its approval only upon the principles of equity, safety and public policy. In other words, the aim of the code clearly is to secure the highest degree of perfection in supervision as a basis of rational governmental regulation and control. There is no attempt to substitute, even in principle, State management of insurance undertakings on the one hand, or State responsibility for the fulfillment of contract obligations on the other. The Government interferes only in cases where there is evidence that the insurance undertakings are managed contrary to sound principles of equity and public policy.

Organization of the Department.

The Department has supervision over the entire business of insurance corporations and associations, and under the term, business plan, or method, is comprehended everything relating to the administration and the results of business experience. The domicile of the Department is at Berlin, where it is housed in a beautiful building especially erected for the purpose. The executive organization consists of a president, a chief director, five permanent members in the main department, four permanent members in the auxiliary department, and three *ex-officio* members who are technically qualified experts in insurance. The technical and clerical staffs of the Department consist of some thirty employees. All of the appointments are of men thoroughly conversant with either the theory or practice of the business in any one or more of its different branches, and except in the case of *ex-officio* members, the appointments are for life. The salaries paid may be considered

fairly commensurate with the very responsible duties discharged. All officers and employees are entitled to a pension in old age.

Department is an Independent Administrative-Judicial Branch of the Government.

The status of the Department is that of one of the superior courts, and its functions are both administrative and judicial. Specific rules of procedure govern the Department in practically all important details. The Insurance Department forms a subordinate, but practically independent, branch of the Department of the Interior. Persons connected in an official capacity with State insurance undertakings are not eligible to office in the Department. To facilitate the administrative functions of the Department the appointment of local commissioners is permissible, but these officials do not exercise independent functions. They are supposed to act in an advisory capacity to both the insurance companies and the Department. Thus far a very limited use has been made of this provision of the code.

Department Assisted by Advisory Council of Insurance Managers and Experts.

For the purpose of increasing the efficiency of the Department, and to secure to its decisions absolute impartiality in complicated or involved cases, the code provides for the appointment of an Advisory Council consisting of recognized experts in the theory and practice of insurance. The Council consists of not less than forty members, who, if necessity requires, may, upon the request of the Imperial Chancellor, be increased to sixty by the Federal Council. They are appointed by the Federal Council for a period of five years, subject to the approval of the Emperor. Their duties are specifically defined in the code, the main object being to secure an outside, but thoroughly qualified, expression of opinion upon complicated and difficult questions, chiefly such as require to be considered

under the provision of the code relating to the right of appeal. The members of the Council have a right to vote in specified cases, but they can be brought into the consideration of pending questions only upon the request of the president of the Imperial Supervising Department.

Organization of the Advisory Council.

The Advisory Council is divided into five groups: (1) Life and sickness insurance; (2) accident and liability insurance; (3) live-stock, hail and other forms of agricultural insurance; (4) fire insurance, including wind-storm, water-damage, and burglary insurance, and (5) all other brances of insurance or matters of a general character. The members of the Advisory Council may be appointed to more than one of the five groups. As illustrating the high character and pre-eminent qualifications of the appointees to the Advisory Council, I may mention among others, Dr. Ehrenberg, a professor of insurance in the University of Göttingen and one of the foremost authorities on insurance theory in Germany; Dr. Emminghaus, a director of the Gotha, the foremost mutual life insurance society in Germany; the late Dr. Hahn, a general director of a prominent company, president of the German Society for Insurance Science, and president of the Fifth International Actuarial Congress; also Dr. Karup, actuary and mathematician of the Gotha and one of the highest authorities in actuarial science in the world. All the other members of the Advisory Council are, in one capacity or another, identified with insurance companies or insurance interests. The members of the Council hold their positions as an honorary employment, but they are reimbursed for their expenses if required to attend meetings at the office of the Department in Berlin. At all meetings the president of the Department, or his representative, presides.

Departmental, Rulings, not Subject to Appeal.

Against the decisions of the Department, as such, or of the Department in conjunction with the Advisory Council,

there is practically no appeal, except in so far that in important cases a rehearing will be granted, at which, however, the president of the Department is again the presiding officer, but from which other executive officers of the Department are excluded if they participated in the previous decision. Upon request, in very important cases, the Advisory Council participates in such cases, sitting as a court of appeal, whose decision is final. The fundamental principle which underlies this apparently somewhat arbitrary method of procedure, is that even the general superior courts would not, as a rule, be in a better position to render justice than a special court, constituted from within the Department, and sustained by an Advisory Council derived by careful selection from among the most qualified experts in the business of insurance. On the whole, in view of some eight years of actual experience, it may be held that the results have met with general approval, and the decisions of the Department have been in strict conformity to rational principles of procedure applied to a highly complex and involved branch of business enterprise.

Effective Supervision at Minimum Cost.

The expenses of the Department are provided for by the general budget. However, upon the theory that it is equally to the interest of the companies and their policyholders, as well as of the public generally, that the business should be effectively supervised and regulated by the Government, an annual pro rata levy is made by the Department upon the companies, subject to its jurisdiction, for one-half the sum required for its maintenance during the current year.* The contributions

* During 1906 the expenses of the Department paid by the companies were assessed upon a premium income of 713,625,000 marks. The amount paid was 210,500 marks or at the rate of not quite 30c. per $1,000 of gross premium income. The previous year the rate was 0.298 (1905), 0.292 (1904, 0.277 (1903) and 0.235 (1902). During 1909 the expenses were assessed upon a premium income of 900, 838, 631 marks, and the amount paid was 271,800 marks, or 30.2 cents per $1,000 of gross premium income. In 1908 the rate was 0.289.

or fees are calculated upon the previous year's gross premium income, deducting therefrom premiums paid in advance and amounts returned to shareholders or policyholders as profits or dividends. The expenses which may be assessed upon a company, however, are limited to a maximum of one-tenth of one per cent. of the gross premium income as previously defined. There are no other fees or charges of any kind, except that in cases where needless expenses have been incurred by the Department in behalf of special efforts to secure evidence or proof in the settlement of disputes or appeals, the charges may be assessed upon the complainant.

Legal Status of Mutual Insurance Undertakings.

The organization and management of mutual insurance undertakings take up nearly one-third of the code, and for the first time these companies in Germany have secured by statute the recognition of legal corporations entitled to the same judicial rights and privileges as incorporated stock companies. Incorporated trade unions having insurance features, miners' benefit funds, and friendly societies do not come within the provisions of the code. As a general principle, the provisions of the commercial code applicable to corporations generally are extended to mutual insurance undertakings. In future, however, all such companies or associations must conform to uniform rules laid down by the code and elaborated by the Supervising Department.

Regulations Governing Mutual Insurance.

The organization of mutual undertakings, their management, election of officers, etc., are provided for by the code in a general way and without needless interference in matters of detail. All essentials, including the distribution of surplus to members and the payment of special compensation to the management, are governed by the commercial code the same as when applied to stock corporations. The regulations are admirably framed and have been universally commended and ap-

proved by insurance interests generally. In the case of new organizations the code requires a special guarantee fund for the additional protection of the members, but provision is made for its gradual elimination.

Under the provisions of the commercial code which apply to the insurance code, mutual companies or associations can be converted into stock companies by consent of the policyholders. In practice there have been a number of such changes, with the approval of the Supervising Department, while to the contrary there never has been a case of a stock company being converted into a mutual institution. Qualified critics of these provisions of the code have not failed to point out the inherent difficulties of actual participation in the management through the membership, and on the whole, official as well as private opinion in Germany seems to decidedly favor stock corporations. In actual practice there has been no participation, nor even a serious interest of policyholders, in the management of large mutual insurance undertakings, for, as has been properly pointed out, the members consider chiefly their contractual relations to the company or association as policyholders and not as members or partners in a commercial enterprise.

Legal Status of Stock Companies.

The legal status of stock life insurance companies is in part governed by the insurance code and in part by the general stock corporation law. For the adequate protection of stockholders the companies are required to gradually accumulate a reserve out of profits otherwise unassigned. This reserve is in the nature of a stock dividend required by the stock corporation law, applicable to life insurance companies. At least five per cent of the annual net profits must be set aside until the capital reserve equals ten per cent. of the amount authorized. It has been the general rule for many years, in the formation of stock life insurance companies, to pay in about twenty per cent. of the authorized capital in cash, while for the remainder the personal notes of the stockholders are required to be

deposited and made payable on demand. The intrinsic value of the notes must be periodically verified. In proportion, of course, as the capital reserve increases the individual liability of stockholders for the unpaid portion of their stock diminishes. This arrangement is covered by Section 262 of the commercial code, and a somewhat similar arrangement provides for the guaranty funds of mutual companies by Section 37 of the insurance code.

Dividends Paid by German Stock Life Insurance Companies.

The annual business report of the Department for 1906 includes some very interesting details regarding the authorized and paid-up capital, stock reserve funds, and dividends paid to shareholders by German stock life insurance companies in part as follows:

There were twenty-four stock companies, or so-called large undertakings, which had about 1,400,000 ordinary policies in force, and a total income during 1906, of 303,272,000 marks ($72,178,736).. The authorized stock capital of these companies was in round figures, 156,000,000 marks ($37,128,000), of which, as far as it is possible to judge, only 35,000,000 marks ($8,330,000) was paid in cash. For the unpaid balance of the authorized capital the shareholders are required to deposit fully secured personal notes payable on demand. For these, of course, they would become liable only in the event of failure. The commercial code requires the gradual accumulation of a stockholders' reserve equal to ten per cent. of the authorized capital out of profits not otherwise assigned, and something over 14,000,000 marks ($3,332,000) has been set aside for this purpose. Stock dividends are paid upon both the cash and the stock reserve, and in the aggregate during 1906 the twenty-four companies paid 6,060,000 marks ($1,442,280) as dividends, equal to about 17.3 per cent. of the cash paid in, and 12.4 per cent. when the stock reserve is included.

Shareholders' Participation in Profits.

I can not do better than use, for purposes of illustration, the case of a company selected at random, with an authorized capital of 9,000,000 marks ($2,142,000). Of this sum, twenty per cent. was actually paid in cash, while for the remainder the required demand notes were deposited. In the course of years the company has accumulated a capital reserve of 900,000 marks ($214,200), or the full legal limit of ten per cent. of the authorized capital stock. Combining the amount paid in cash and the capital stock reserve authorized, the total is 2,700,000 marks ($642,600), and upon this sum the company, during 1904, paid a cash dividend of ten per cent., or 270,000 marks ($64,260). The equivalent payment upon the cash actually paid in would be fifteen per cent. Another company, with an authorized capital stock of 17,142,000 marks ($4,079,796), of which only ten per cent., or 1,714,000 marks ($407,932) had been paid in cash, and which has accumulated a stock reserve of 1,714,000 marks ($407,932) more, paid during 1904 the sum of 500,000 marks ($119,000)in cash dividends to shareholders, or at the rate of 14.6 per cent. upon the aggregate present cash capital, or 29.2 per cent. upon the amount of cash actually paid in.

Companies May Pay Any Rate of Profit Actually Earned.

The companies may pay any rate of profit provided the same is actually earned. The Supervising Department considers its duty at an end if it has been furnished with conclusive evidence that the amount paid in cash dividends to shareholders is actually available and has not been derived from other funds than the balance of net profits remaining after the payment of all other obligations. The code does not restrict the companies in this respect since stock life insurance companies are considered from the same point of view as other commercial undertakings. In other words, if by reason of exceptional gain or profits resulting from executive or scientific methods of management, a balance of funds becomes available for distribution to

the shareholders, the law does not fix a maximum rate of profit which may be realized upon the investments. There is in this respect, complete freedom of trade in life insurance the same as in other business enterprises.

Stock and Mutual Companies May Transact Participating and Non-Participating Business.

The code does not prohibit life insurance companies from transacting both a participating and a non-participating business. As a rule, German companies issue both classes of policies, but the participating business predominates. In 1904, of the policies payable in the event of death, in force with German stock companies, 82.9 per cent. were on the participating plan and with mutual companies 99.4 per cent.* Mutual companies are permitted to issue non-participating policies, but the policyholders in such cases are not considered members. The non-participating rates are, as a rule, higher than the corresponding rates charged by American or English companies. Of the policies issued on the endowment plan, with stock companies, only thirty-two per cent. were on the participating plan, and with mutual companies, ninety-two per cent. As a rule, German mutual companies do not sell annuity contracts, but such as have been issued, with either stock or mutual companies, are nearly all on the non-participating plan.

Status of Foreign Insurance Companies.

Foreign insurance companies transacting business in Germany are subject to a separate division of the code, in seven sections. All such companies require permission or authority from the Department the same as domestic companies, but the final action of the Department is subject to approval by the Imperial Chancellor. This distinction, of course, rests upon

* The 29 companies transacting life insurance in the State of Massachusetts had, in the aggregate, $13,753,542,000 of insurance in force, Dec. 31, 1909. Of that amount $10,190,724,000, or 74.1 per cent, was participating and $3,562,818,000, or 25.9 per cent, was nonparticipating.

certain principles of international law and the practice of the Department of foreign affairs in its relations to the Governments of other countries. The conditions of admission, however, are practically the same as in the case of domestic companies, but the foreign company must appoint a representative with full power of attorney to act for it in an official capacity in all cases, including the signing of policy contracts and accepting service in the case of legal complications. The company must establish a chief domicile in some one state, and in all its civil relations in questions arising out of the insurance contract it becomes subject to the local law. The company is also subject to the jurisdiction of the local courts in the first instance, and it is not permitted to waive this jurisdiction even by special agreement with the local government. The premium reserve which is properly chargeable against the business of foreign life insurance companies transacting insurance in Germany must be kept and invested in Germany in such a manner that it can be disposed of only by permission or authority of the Department. The practical problems arising out of this provision of the law have not as yet been fully settled or determined.

Insurance as a Problem in International Law.

In its relation to foreign life insurance companies the Department, has, on the whole, been fairly tolerant and adjusted its requirements in the form of a reasonable compromise best adapted to meet the necessities of an exceptional situation. To leave free scope to the Government, however, in its relations to foreign powers, the Federal Council and the Imperial Chancellor are specifically authorized to act entirely according to their own discretion with respect to the granting of a concession or license to a foreign company transacting business in the German Empire. The Department, by implication, at least, would seem to have the right, and possibly the duty, of extending its supervisory powers into the domestic affairs of a foreign company, including an actual investigation into its condition at its home office. Treaty obligations between Germany and

foreign powers respecting a reciprocal arrangement regarding insurance companies are not affected by the law, and they may, therefore, be made entirely in the discretion of the Government. Insurance is therefore strictly recognized as an element of commerce and being subject to the control of the foreign office, it is governed in this respect by the principles of international law.

Adequate Fines and Penalties.

The provisions of the code are adequate with respect to the necessary penalties for non-compliance with the law or the rules and regulations of the Supervising Department. In all essentials these conform to the established rules of procedure in criminal cases arising under the general civil and penal codes. Deliberately false or misleading statements to secure a concession or permission to do business, or for the purpose of obtaining the approval of the Department in matters for which it is required, are punishable with imprisonment or a fine to the amount of about $5,000, while in addition the court can impose the loss of civil rights. Deliberately false or misleading statements regarding the funds of the company, or the character of its assets, or when, contrary to law, a division of profits to the insured or to the shareholders has taken place, or false keeping of books and accounts, or the investment and keeping of the premium reserve contrary to law, is punishable with imprisonment for not more than six months, or a fine of not more than $500, or both.

Departmental Powers Over Management.

It is only with respect to life insurance undertakings that the code contains specific regulations for the general business conduct of the companies. The most important of these relate to the reserve and the investments. To prevent speculation in real estate acquired for corporation purposes, the purchase of additional properties requires the approval of the Department except such as are necessarily acquired under foreclosure pro-

ceedings. It is also held that the object of the law is to prevent the erection of expensive buildings, chiefly for advertising purposes. Should the Department refuse its consent to the purchase, the company has not the right of appeal. Foreign companies, in this respect, are under a double disadvantage, partly for the reasons stated, and partly for additional political reasons which oppose the acquisition of real estate by aliens.

Departmental Powers Over Records and Accounts.

To place the Supervising Department in a proper position to secure all the information required in the opinion of its experts to arrive at a necessary conclusion, the code extends to it every power, judicial as well as administrative, to secure the end in view. The Department has the right to examine into all the books, papers, vouchers, etc., of a company which may bear upon its investments or upon any other question, and it can demand information from any one of the employees, including agents, with respect to any material fact of administration.

Departmental Representation at Board Meetings of Mutual Insurance Undertakings.

The code extends to the Supervising Department the right to be represented at the meetings of directors or trustees of mutual insurance undertakings by an officer of the Department and should it be necessary for special reasons, a meeting of the directors or trustees may be called by the Department, but at such meetings the Government representative presides over the proceedings. In practice the Department has not made much use of this provision of the law, and as far as I am informed, only in the case of mutual insurance companies. To carry this principle into execution in the case of many, or all of the insurance undertakings subject to its supervisory powers, would, of course, be impossible with the present organization.

Discretionary Powers in Cases of Complaint.

The Department may entertain complaints against insurance companies, but it is under no specific obligation to take action in such matters. It is admitted by the authorities, and the experience of the Department has verified this view, that such complaints are usually of an extremely trivial character or entirely without legal foundation. Most of these complaints, it is pointed out, arise in connection with the cash surrender values of life insurance policies, where the practice of the company is sometimes unintelligible to the insured. Upon inquiry it is usually found that the company has acted within its rights and according to the policy provisions, which of course, had been previously approved by the Department. Since most of such complaints arise out of the contractual relations between the insured and the company, they remain subject to adjudication by the civil courts.

Annual Statements and Reports Required to be Made.

The companies must annually make a report to the Department upon their business operations during the year, including a complete balance-sheet and revenue account. These must be prepared in accordance with the rules and regulations of the Department, issued under date of June 2, 1902, having been prepared after frequent consultation with the Advisory Council, consisting, as previously stated, of managers and experts thoroughly familiar with the subject of insurance in all its branches. The books of an insurance company must be kept in conformity to Section 39 of the general commercial code. The accounts must include a gain and loss exhibit, which, however, quite fundamentally differs from the corresponding gain and loss exhibit required by certain states of the United States. The annual report must set forth the course and development of the business during the year and conform to certain fundamental principles although the same may be amplified according to the discretion of the company. The code provides that every policyholder, upon request, shall be furnished with a copy of

the annual report. It is held that every reasonable requirement for the publicity of the essential facts of management and business experience is complied with and that any additional information would be most likely to confuse the public and furnish data more or less misleading for competitive purposes.

Rules Governing Valuations.

Special rules, based upon careful inquiry, and approved by the Advisory Council, govern the calculation and investment of the premium reserve. The reserve is properly defined as the foundation of the life insurance business. The code differentiates between the terms "Premium Reserve," and "Premium Reserve Funds." The distinction is not entirely clear. Under special conditions the law permits the use of the preliminary term, but no specific principle of mortality or rate of interest is laid down. The Department has published some very interesting contributions to the science of insurance, and particularly a monograph on the mortality tables in general use throughout Germany, and another on the various systems of distributing surplus gains to policyholders under the participating contract. Of course, if the Department is satisfied that the mortality table used is inadequate, or that the rate of interest assumed is too low or too high, it can insist upon necessary changes according to its discretion.

Actuarial Responsibility for Reserve Calculations.

The reserve is required to be calculated for every business year and separately for each branch of insurance. The reserve may be calculated for individual policies, or by groups of identical ages at entry, or according to the duration of insurance and the termination period of the contract. To provide for accuracy in the calculation the same must be certified to in the balance-sheet by at least one thoroughly competent expert mathematician or actuary, who has to certify that the premium reserve as stated in the balance-sheet has been calculated according to the formula approved by the Department. For

the accuracy of this statement the actuary or mathematician is held personally responsible, and the code provides adequate penalties in the event of a dereliction of duty. The management, however, remains also personally responsible for the accuracy of the calculations.

Rules Governing Reserve Fund Investments.

The code provides in a definite manner for the investment of the reserve, primarily in such funds as under the civil code are required for the investment of trustee funds for orphans and minors. Chiefly, of course, in mortgages and government obligations. The latter are not generally in much favor in that under the commercial code their value has to be stated on the last day of the year according to the Stock Exchange quotations on that day. Since by mere accident an exceptionally low price might prevail on that day, the true value of the investment might be materially understated. Up to ten per cent. of the reserve may be invested in collateral loans upon mortgages and securities, but in the case of the latter only to the extent of seventy-five per cent. of the par value, and if the market price is below par, to the extent of seventy-five per cent. of the same. Mortgage loans must not exceed sixty per cent. of the carefully appraised value of the property. Loans can only be made upon improved and productive properties and not upon buildings in course of construction. Investments of the reserve may also be made in policy loans, which, of course, are safest as well as, in a measure, most profitable to the company. Loans may also be made, but only to the extent of a small proportion of the aggregate, in the obligations of counties. municipalities, schools, and churches, provided they are subject to a definite method of amortization. Investments of funds of this character, however, require the approval of the Department. If no immediate investment of the reserve can be made in the required class of securities, the money may remain with the Imperial Bank, or a State Bank, or a bank specifically approved by the Department, or a public savings bank.

The Separate Accounting and Keeping of the Reserve Funds of Life Insurance Undertakings.

One of the innovations of the code is the requirement that the securities or documents representing the reserve fund, must be kept absolutely separate and distinct from any other funds of the company, and they are generally placed in a separate safe to furnish visible evidence at any given time that the reserve is actually kept intact for the ample protection of the interests of the policyholders. The separate administration of the two funds, that is, of the reserve and the remainder of the company's assets, is also required to secure to the policyholders, in the event of bankruptcy or liquidation, the rights of preferred creditors. The investments representing the reserve are required to be accounted for in a separate register. This must identify the individual securities, mortgages, or other evidences of property in such a manner that there can be no doubt as to the company's undisputed right to the property. In the case of other securities, the description must be individual and complete, including the serial number of the same, and the only exception where the facts may be stated in a lump sum is in the case of policy loans. At the end of every year the company must furnish a certified copy of the list of securities for the permanent records of the Department. It is specifically provided that no funds shall be taken from the reserve for administration expenses, the payment of dividends, etc. Of course, this regulation does not bear upon the use of the preliminary-term plan, which is permitted for the first year to the extent of $12.50 per $1,000 of insurance.

Time Allowed for Necessary Changes in Methods.

To carry the preceding rules and regulations into effect, a period of three years was allowed to the companies to provide for a separation of the premium reserve funds from the remainder of the company's assets, while a period of five years was allowed for compliance with the investment provisions of the code.

Annual Reports of Supervising Department.

The Supervising Department is required annually to publish a report of its administration, supplemented by a preliminary statement of the more important facts of the business experience of large insurance undertakings. The report for 1906, is dated May 31, 1907, and was published during the early part of August. It makes a compact volume of about 250 pages full of interesting and valuable information. In its reports and publications the Department limits itself to a statement of essential facts sufficient for public purposes. It refrains from giving publicity to information which, in all probability, would be used for improper competitive purposes to the detriment of the business and the public. While the Department requires complete information of all undertakings subject to its jurisdiction it gives publicity to only a portion of the facts collected. In the opinion of qualified experts, the distinction between information useful to the public, and information strictly for the confidential and discretionary use of the Department, has been admirably well drawn, and for this solution of a difficult question it is understood the Advisory Council of the Department was chiefly responsible.

Extent of Supervision.

On May 31, 1907, the Department had supervision over 1,219 insurance undertakings transacting the business in its various forms. Of the just mentioned total, 73 were foreign companies, the number of which has remained about the same since 1904. Evidently the effect of the code has not been to attract foreign companies to Germany as a field for the further development of their business. Of the 1,146 domestic institutions, 446 transacted interstate business. Since most of the companies have their domiciles in Prussia, which forms about two-thirds of the area of the German Empire, many undertakings by limiting their operations to that State, are, therefore, not within the jurisdiction of the Department. Since a State is permitted to arrange for the Imperial supervision of local com-

panies, various States, and the free city of Bremen, have done so, and some seven hundred insurance undertakings are supervised and controlled in this manner the same as companies engaged in interstate business. Of the 446 domestic institutions engaged in interstate business, 235 transacted life, 21 accident, 78 hail, 62 fire and 50 other forms of insurance. Of the seven hundred institutions subject to the supervising powers of the Department by the voluntary surrender of State authority, 118 were life, 513 hail, 5 fire, and 1 miscellaneous insurance undertakings. Of the 73 foreign companies, 22 were life, 5 accident, 40 fire and 6 miscellaneous undertakings.

Premium Income of Insurance Undertakings.

The total premium of the companies subject to the jurisdiction of the Department was not quite two hundred million dollars, of which a little less than ten per cent. was the income of foreign companies. Of the total premium income, fifty-five per cent. was from the life branch of the business. The overshadowing importance of life insurance is due primarily to the fact that most of the fire insurance, in some form or other is managed by the State or by local companies not subject to the jurisdiction of the Department. The aggregate assets of undertakings subject to the rules and regulations, and judicial decisions of the Department, exceed two thousand million dollars, for the accurate reserve calculations of which, and safe investment, the Department is in a large measure responsible under the law. In due recognition of this fact the Department takes its duties very seriously, and properly so, and takes no step in any direction which it might perhaps be required to retrace. Thus far its judicial decisions have stood the test, and it is significant that while the code was passed in 1901, no amendments have been made to the law during the intervening period of time.

Invested Assets.

The report for 1906 gives much space to a critical consideration of the aggregate investments of insurance companies,

seventy-one per cent. of which represent mortgage loans. The companies are required to inform the Department semi-annually in detail regarding new mortgage loans, and during 1906, eighty-seven institutions reported 3,445 mortgage loans, for the sum of 357,000,000 marks ($75,966,000). The report properly points out the intimate relation of such loans to real estate values and public credit. The report includes a table showing that most of the loans realized four per cent., interest but a fair proportion paid as much as four and one-eighth per cent. and four and one-quarter per cent., while a few were made at as low a rate as three and three-quarters per cent. and as high as four and one-half per cent. The usual rate of commission paid as part of the consideration in the making of mortgage loans was one-half per cent., with a maximum rate of three per cent.

Mortgage Loans on City Real Estate.

Most of the mortgage loans were on city real estate, and out of 3,409 mortgages, 1,169 or 34.4 per cent., were placed in the city of Berlin and suburban sections. Of the remainder, 1,153 were placed in Prussia and 225 in the Hanse towns. This concentration of real estate loans upon a comparatively small area would hardly seem to stand the test of impartial critical consideration. The local conditions, however, must be taken into account as regards loans upon landed estates or agricultural properties, which are, as a rule, either over-mortgaged or very fluctuating in value. Both the code and the rulings of the Department decidedly favor mortgage loans in the business section of large cities, but it seems that the area of such investments is not as large as would be desirable. One argument which has been advanced in favor of this practice, is that the appraisal of real estate is more accurate or more in proportion to the true value of the property in large cities than in the small communities, which is probably true.

Effective Supervision of Mortgage Loans.

The Department exercises complete and continuous supervision over the mortgage loans and keeps a card index, by cities

and streets, of all properties loaned upon. It requires to be informed of the sale price of any property mortgaged, as a check against a possible overvaluation. The report divides such sales according to the method of appraisal—that is, whether private or public, and it is shown that during the last three years, 1904–1906, of properties privately appraised, 18 per cent. realized over 100 per cent. of the appraisal; while of properties officially appraised, 68 per cent. realized more than 100 per cent. Recalling that the companies are permitted to loan only to the extent of 60 per cent. of the appraised value, it is shown that in the case of properties sold, and which had been privately appraised, about 23 per cent. brought between 60 per cent. and 80 per cent. of the appraised value, while of properties officially appraised, less than 1 per cent. came within this range of valuation. The statement is significant as illustrating the care employed to secure a really trustworthy valuation of properties loaned upon, and by means of an accurate card catalogue the Department is in full possession of all the facts at any given time to trace a possibly speculative tendency on the part of any particular insurance undertaking to loan in any particular section of a city in excess of the true value of the property.

Supervision of Reserve Funds.

On December 31, 1906, the five-year period during which the companies could perfect the necessary changes for the investment of their reserve funds in conformity to the code, expired. The provisions of the law distinguish between the separation of the reserve funds, their separate calculation according to stated principles, their separate investment, and the separate keeping of the securities. The rules governing the reserve calculations, and the keeping of the registers or accounts of the valuations, are the result of extended deliberation and joint consideration of the Supervising Department and the Advisory Council. In the first draft of the code it had been proposed to require the companies to send their reserve

registers in the original to the supervising office, but this was later modified, and only a copy, properly authenticated and sworn to, is required. The results of this practice have been entirely satisfactory. Compared with the demands upon American life insurance companies by the insurance departments of the different States, the requirements of the German Department are very moderate indeed.

Reserve Investments of Companies Transacting Business in Foreign Countries.

A difficult question confronts German companies transacting business abroad, and which, in compliance with foreign regulations, can not, as a matter of course, comply with different regulations at home. While the code apparently leaves no alternative but to insist upon the same method of investment of funds, representing the reserve in foreign business, the Department, within its power of discretion, effected a compromise, under which the companies are permitted to invest the full reserve on foreign business in conformity to foreign laws. A similar problem confronts the Department with respect to foreign companies transacting business in Germany, but here also a compromise has been reached fairly favorable to the companies. It is evident, however, from the tone of the report, as well as from the practice and rulings, that foreign life insurance companies are not desired in Germany.

Complaints.

During 1906 the Department considered 534 complaints of a varied character, most of which, however, related to the contractual relations of the companies and their policyholders, being, as such, subject to ultimate settlement in the courts. The Department, however, used its best endeavor to arbitrate differences and bring about a better understanding, and in a large number of cases it would seem this method proved effective and a preventive of needless litigation. In the case of life insurance, it is pointed out that most of the complaints had

to do with paid-up values and dividends through a misunderstanding on the part of the insured of the contract obligations contained in his policy. Of 231 complaints arising under life insurance contracts, 61 were disposed of without correspondence or a hearing of the companies interested, 118 were disposed of by a single inquiry, while 34 involved more extended consideration. The report points out that the Department had occasion to insist upon modifications of policy conditions, applications, advertising literature, etc. It also found it necessary to call the attention of the companies to a better supervision of the agency force as a most effective means to prevent misunderstandings with the insured.

Inquiries.

During the year 1906 there were 320 inquiries, including the most varied questions, many of which in their nature also involved the contractual relations of policyholders and insurance companies. Seventy of these inquiries related to the solvency of American companies, and in all of such the Department repeated its former advice that no evidence had been presented to prove that the American companies were not fully able to meet their obligations. Other inquiries related to the San Francisco earthquake, liquidations, new concessions, explanation of policy provisions, etc.

Life Insurance Problems.

Extended consideration is given in the report for 1906 to various problems of life insurance theory and practice. Among others, the question was considered as to whether a life insurance company should be permitted to calculate its premium rates upon the results of its own experience or be required to adhere to some standard table in general use. The question came up in connection with recent and very extended investigations of the Gotha and the Leipziger (Lebensversicherungs Gesellschaft auf Gegenseitigkeit, Alte Leipziger) life insurance companies, both of which are among the oldest and best

managed, insurance undertakings in the world. The Department ruled that the companies in question could safely use their own experience as being, probably, better adapted to their specific requirements than the tables of mortality in general use. The question of dividend apportionment also received extended consideration, and it was emphasized that the companies should, as far as possible, conform their preliminary estimates to the probable future results to be realized in actual experience. The dividend systems in use by German companies differ in many essentials from those in use in the United States, but practically all are on the deferred plan to this extent, that no dividends are paid during the first five years of policy duration. The dividend payments are, as a rule, on the annual plan, beginning with the sixth year. The dividend paid in the sixth year represents the gain realized upon the first year of insurance and so on. Even the preliminary-term plan in such cases admits of a dividend which has been actually earned, being paid in the sixth year of insurance. In the event of death the dividend gains or accumulations during the five preceding years are forfeited and revert to the general dividend fund.

Life Insurance of Children.

The report contains a lengthy discussion of the various methods of insuring the lives of children, with observations upon the systems in use in England, the United States, and other countries. The Department concludes, after careful investigation, that there is no necessity for entirely prohibiting the insurance of children as has been the case in France, Belgium, and Colorado, but that a maximum amount should be fixed by law, beyond which the companies should not be permitted to insure a sum payable in the event of the child's death. The Department holds that, as far as possible, the amounts should conform to the expenses of the last medical attendance, the burial and other expenses incidental to the child's death. The subject is being considered in connection with the preparation of a code governing the private or con-

tract law of insurance, and it is quite probable that a fixed table of amounts will be included the same as has been done in England, Australia, and in New York and other States of this country.*

Miscellaneous Insurance Problems.

The report considers the question of insurance without medical examination, so-called net-cost estimates, life insurance in connection with store purchases, or with savings banks, etc. The Department holds it to be unwise to combine life insurance with any other commercial elements or undertakings although it has not thought it necessary to prohibit such undertakings but has merely advised against their expediency. Among other subjects, the report considers pension funds, American life insurance investigations, accident and liability insurance, agricultural insurance, etc. In each case the more important questions are fully explained to emphasize the Department's point of view and the reasons governing decisions or rulings for or against particular practices.

Fire Insurance and the San Francisco Earthquake.

Extended consideration is given to the San Francisco earthquake and the complex problems arising out of a proper construction of the earthquake clause. The report points out that there were six German companies transacting business in California, mostly under the New York standard policy, which does not contain a clause of non-liability in the event of earthquake or destruction of buildings by dynamite, etc. In the aggregate the companies paid out 31,000,000 marks ($7,378,000) in losses. The companies, by special arrangement paid within about fifteen per cent. to twenty-five per cent. of the actual loss sustained. Three of the companies, which resisted all liability, were required by the Department to submit a full statement of the facts, and after due consideration of the

* The code here referred to was enacted in 1908 and a maximum table of amounts governing the insurance of children was incorporated therein, conforming in its essentials to the New York law.

contractual relation of the parties it was ruled that the respective rights could be determined only by the courts. The Department insisted, however, that in the future there should be more clearness and a more pointed explanation of any clause limiting the liability of a fire insurance company in cases of exceptional contingencies, so as to secure to the policyholders the largest amount of protection. With the exception of one or two, all of the companies later came to an agreement with their clients, and perhaps in no single instance was the efficiency of the Department better illustrated than in this. Some very important questions of international private law are involved in this matter, which emphasizes the importance of insurance as an international institution and the necessity, as far as possible, for uniformity and harmony in insurance legislation throughout the world.

Administrative and Judicial Functions of the Supervising Department During 1906.

During the year the Department held three general executive meetings and twenty-one open or public meetings, at which 133 decisions affecting insurance undertakings were rendered. Of the twenty-one public meetings, six affected life insurance, four accident, four agricultural, five fire, and two other insurance undertakings. During the year the Advisory Council held one general meeting, and five section meetings, for each of the divisions into which the work of the council is divided. In eighteen cases members of the Advisory Board were individually consulted for advice. The Department continued the collection of important court decisions involving insurance companies and their relations to the policyholders, and by the end of 1906 a total of 774 such decisions, by a special arrangement with the courts, had been received by the law division of the Department. Of these, 270 were published in part, with the necessary explanations for ready reference as well as for the information of insurance companies. There were nineteen applications for approval to purchase real estate

for office purposes, and of these seventeen were granted, while two were withdrawn. In eighteen cases an extension of time was granted for the separation of the reserve funds from other assets as required by the code, chiefly, as I understand it, in the case of small undertakings.

Departmental Examination of Insurance Companies.

The Department made forty-nine local examinations of insurance companies, or eighteen more than during the preceding year. Of this number forty were carried on in the offices of the companies, four at general agencies of inland undertakings, and five at general agencies of foreign companies. Of the forty-nine examinations, eighteen were of life insurance companies. Thirty-four of the examinations were considered a general business revision, while fifteen were partial or limited to the determining of special facts. While there were forty-nine examinations, these affected only forty-seven undertakings, of which fifteen were stock companies and thirty-one were mutual companies or associations. One apparently did not come within either of these two classes of corporations. The examinations took up 276 days, and including the subsequent Departmental consideration, consumed a large amount of the time of the Department during the year. As far as it is possible to judge, the examinations proceed upon somewhat different principles than those in vogue in this country, and do not enter into matters of detail to the extent as is the case over here. This, of course, in part is due to the fact that the Department is already in possession of a mass of information and data regarding the methods and experience of the companies subject to its jurisdiction. The entire expense of examinations is paid by the Department.

Procedure in the Consideration of Pending Cases.

The consideration of questions and problems arising under different provisions of the code is arranged in ten groups. Limiting the present discussion to only such undertakings as

were subject to the jurisdiction of the Department on account of being engaged in interstate business, there were in the aggregate 575 cases considered, of which 429 were disposed of, leaving 146 remaining at the close of the year. Of these, fifty-six had been disposed of by the end of May, 1907. Some of these cases had been under consideration for several years, and the procedure in many is necessarily slow. Of the 429 cases disposed of, thirty-two had to do with applications for authority to do business; 123 with the Department's approval of changes in articles of association, by-laws, etc., pertaining to the organization of insurance undertakings; eighty-eight with changes in policy conditions; forty-one with changes in premium rates; thirty-one with the introduction of new methods or branches of insurance by existing undertakings; twenty-seven with the territorial extension of business operations to other States; thirty-three with the extension of operations under other provisions of the code; seven with amalgamation; three with liquidations of mutual insurance undertakings and forty-four with the provision of the code defining small insurance enterprises.

The Duty of Publicity

The action of the Department in all important cases arising under the various provisions of the code is fully explained in an extended review forming part of the annual report. By this means an extremely valuable, continuous record of the work of the Department is preserved and made readily accessible to the companies and the public. The Department appears to recognize the fact that the duty of publicity is a mutual one, as much being required of the companies on the one hand as of the Department on the other, while at the same time there is an absence of needless publicity of facts or information likely to be used for improper competitive purposes.

The Question of Taxation.

The subject of taxation is so large and involved that it precludes adequate presentation in a discussion of this kind.

The taxation of insurance companies in Germany is left as formerly to the States or local administrative powers. Except for the difficulties arising out of a needlessly complex system of stamp taxes of which as many as three may be imposed upon one transaction, the tax problem is not a very serious one. As has been said, the cost of Imperial supervision is less than thirty cents per $1,000 of gross premium income. The total taxes paid by large insurance undertakings during 1905 amounted to 2,260,000 marks ($537,880) out of a gross premium income of 787,000,000 marks ($187,306,000). In other words, the rate of taxation was $2.87 per $1,000 of premium income. Considering life insurance companies separately, the rate was $2.33; accident and liability companies, $3.69; and of fire insurance companies $3.77. It may be said in this connection that during 1906 American life insurance companies alone paid nearly $11,000,000 in taxes, fees, etc., equivalent to 2.1 *per cent.* of the premium income. Had the rate of life insurance taxation in this country been the same in 1906 as in Germany, over $8,000,000 would have been saved to policyholders of American life insurance undertakings.*

Conclusions.

Government regulation of insurance in Germany is simple and effective. The complete supervision of the companies is obtained at a minimum of interference and expense. The code is in marked contrast to our own conflicting, costly and constantly changing system. In time, no doubt, we shall realize the futility of State legislation and State interference carried to the extreme. Some day we shall return to our earlier political ideal that "the government which governs least is the government which governs best. Efforts making for uniformity in insurance legislation will be to small purpose until existing statutory requirements are radically revised and reduced to a

* For an interesting comparison of the American and German system of life insurance taxation, see the address by Mr. John F. Dryden, republished in Addresses and Papers, Newark, N. J., 1910, pp. 165–6.

more simple, but at the same time more effective system. The essence of all law, it has very properly been said, is *necessity*, and only when law making is limited to absolutely essential needs is there a reasonable certainty that the legislation will prove effective and permanent.

The German code has not been amended or changed since it went into effect some six years ago; the Austrian regulations have not undergone a change during the past eleven years and they are practically identical with the regulations which have been in force since 1880; the Swiss laws have remained practically the same since first adopted in 1885, or over twenty years ago. In brief, these codes conform to the dictum of Mr. James Bryce that "The chief merit of a rule of law is that it should seize a feature which a large set of instances really have in common and should effectually provide for them *and for them only*,"* and of no legislation is this more important than of the statutory requirements of the business of insurance.†

During the last ten years American legal reserve life insurance companies have made a direct return to the different States of some eighty million dollars in taxes, licenses, fees, etc. For every dollar paid in taxes, etc., by American policyholders, the German policyholders have paid fourteen cents. The constant changes in statutory regulations, and the ever-increasing burdens of taxation are a serious menace to the business, but fully as much are the frequent changes in supervising officials. There is an imperative necessity for permanency in insurance law and permanency in the tenure of office of the insurance commissioner or superintendent charged with the execution of the law. In these and other matters it would seem that we may learn much from a critical and impartial study of foreign insur-

* Studies in History and Jurisprudence, by James Bryce, D. C. L. Oxford University Press, 1904.

† For an interesting account of insurance supervision in Europe, as viewed by an American Insurance Department official, see the Report by Chas. Hughes, Chief Examiner of the New York Insurance Dep't, Albany, 1910.

ance legislation, but perhaps most of all from the scientific codes of law on insurance, enacted by the German Empire in 1901 and 1908.

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CHAPTER VI

THE TAXATION OF LIFE INSURANCE INTERESTS.

The theory and practice of insurance taxation is rarely referred to in the text-books on taxation and the reports of tax commissioners, yet the taxation of insurance interests increases from year to year until a point has been reached where additional burdens are likely to imperil the future of the business. To a large extent this indifference to a scientific study of the problem of life insurance taxation is due to the fact that life insurance is a most complex business, and taxes have as a rule been imposed in ignorance of the real nature of the insurance contract. The discussions before tax commissions, in State Legislatures and Congress are proof that to the average legislator there is but one viewpoint of the matter, and that is the vast accumulation of assets held by companies for the future discharge of their liabilities. What is *seen* is the millions of dollars of funds; what is *not seen* is the corresponding liability charged against these funds; and because of the indifference to the latter, taxes are recklessly imposed and funds are diverted from their proper purpose until a point has been reached where the returns to policy-holders have diminished, where the cost of insurance has been increased, where the economical extension of the business has been made more difficult and where the future of the business is threatened unless a complete change in public opinion is brought about as to the proper scope and limits of the taxation of life insurance interests.

The taxation of life insurance involves the present and future welfare of a large and increasing proportion of our population, representing the most intelligent, industrious and

thrifty of our nation. Briefly stated, there are to-day (1909) in this country, 28,000,000 policies in force in ordinary and industrial level premium companies, which require annually in the aggregate the payment of more than $565,200,000 in premiums. Of this vast sum, representing an almost inconceivable amount of prudence and self-denial, over $12,000,000 is paid to the national government, the state or the municipality, in taxes or license fees of one form or another. In other words, out of every $100 collected in life insurance premiums, $2.15 is paid in taxes; or, if we consider the payments made to policy-holders, which now exceed $360,730,000 per annum, $3.36 is paid in taxes for every $100 paid to the beneficiaries of life insurance policy-holders!

If it is true of the general theory and practice of taxation in this and other countries that "It will be difficult to find in the whole realm of political economy a subject more generally misconceived, more disfigured by false views, more degraded by a partial study"; this is especially true of that branch of the subject which relates to the taxation of life insurance interests. It is not going too far when it is maintained by those who have given much thought to the subject, that life insurance in this country is to-day one of the most heavily taxed institutions making directly for the welfare of the people and for the diminution of public burdens which would have to be provided for by taxes upon other interests. While erroneous views on this subject are due in a large measure to the intricate nature of the life insurance business, they are more largely due to the fact that the vast accumulations of life insurance companies represent an exceptional opportunity for the raising of public revenue with a certainty of its collection.

A Tax Upon Thrift.

The utmost publicity is given by law to all the essential facts pertaining to the business; the amounts of premiums collected, the amounts of dividends paid, the amounts of assets and of surplus accumulated, are given in full in the annual

statements of the companies to the different insurance departments. Nothing unfortunately is of more common occurrence than on occasion of local need for additional revenue to demand an additional tax upon life insurance interests, and yet it requires but a brief consideration of the real interests involved and of the real nature of the business, to make it clear to those free from bias or prejudice that taxes upon life insurance are a tax upon prudence, a tax upon thrift, a tax upon a business which should be free from all burdensome restrictions to enable it to develop and to expand to the highest degree of possible usefulness.

It is one of the most common errors in the theory of life insurance taxation to assume that life insurance itself represents capital. Now, capital is realized wealth, while life insurance is merely a promise to pay a certain sum in the event of the occurrence of a contingency provided for in the policy. Life insurance is a present means of obtaining a certain advantage over an uncertain future event, and it is on this ground, though not on this ground alone, that life insurance or the premiums paid for insurance protection should not be considered a proper subject of burdensome taxation. If we inquire into the objects and nature of life insurance and the relation of life insurance to the state, we find that the primary object of this form of thrift is to provide for dependents, for widows and orphans, who, but for such provision, in many instances, would become charges or wards of the state. By just so much as this is avoided, by just so much as women and children are made independent of such assistance, the revenue of the nation or of the state, is relieved, and can, therefore, be devoted, and is devoted, to the development of other interests affecting the public welfare. Considered from this point of view, it is clear that life insurance should not be an object of taxation, but rather to the contrary, as a means of diminishing public burdens, it should in all respects receive the generous consideration of the state.

Insurance Taxation Contrary to Public Policy.

The political or economic justification for a tax on life insurance is in harmony with the theory advanced by McCulloch that "it is easily assessed and collected," but it is contrary to his conception of an equitable tax, in that it is not "at the same time conducive to public interests." More than a century ago the subject matter of life insurance taxation was carefully considered by Mr. Pitt in the framing of the English income tax bill in 1798, and it may not be out of place here to repeat the language then used, and which is as applicable to the point at issue as if it had been advanced to-day. Under the English income tax law of 1798 incomes were exempted from the payment of the tax to the extent of the premiums paid on life insurance. In defending this clause, Mr. Pitt said: "There is one case which, with a view to that class who are really willing to save for the benefit of others for whom they are bound to provide, makes some modification. It is in favor of those who have recourse to that easy, certain and advantageous mode of providing for their families by assuring their lives. In this bill, as in the assessed taxes, a deduction is allowed for what is paid on this account." This early recognition of the intimate relation between life insurance and public welfare is of more than passing significance. Life insurance in England was then in its very infancy, but even at that stage the good results likely to follow its universal extension had become manifest. It was brought out later, in the evidence submitted to a special committee on assurance associations in 1853, that largely in consequence of this exemption from taxation, life insurance in England had made material advances, a portion of which at least was directly attributed to the relief from taxation. Of one office, the Equitable (London), it was stated in the evidence that, while during the ten years preceding the passage of this act the increase in business had been but $4,500,000, the increase during the decade following the passage of the income tax law, relieving assurance associations from the payment of that tax, had been $20,000,000. The

principle laid down in 1798 has practically remained the law of England to the present time.

The principle of non-taxation of life insurance in England, as laid down by Mr. Pitt in 1798, has been frequently re-affirmed in the works of recognized authorities on economics and finance. A tax on insurance, according to Mill, as stated in his "Principles of Political Economy," "is a direct discouragement of prudence and forethought," and this view is practically accepted by McCulloch, who even more forcibly expressed himself to the point that a tax on insurance "discourages that providence and foresight, the encouragement of which ought to be an object with all prudent governments," and "seeing the vast importance of insurance, it may well be doubted whether it ought to be charged with any duty, however slight." With particular reference to taxation of insurance interests in this country, the subject was discussed in an able treatise thirty-four years ago by S. Morton Peto, according to whom "A tax on insurance is a tax not only upon industry, but upon prudence and frugality, and the American system seems to be far worse than that of which we have been so long complaining in Great Britain," and yet the conditions confronting insurance companies to-day are vastly more serious than they were under the war conditions of the early sixties.

The Practice of Life Insurance Taxation.

The method of life insurance taxation is a matter so involved and complicated by local conditions, varying with the different states, and even with the municipalities, in which the companies operate, that a critical discussion forms a subject by itself. It is the general practice of states to impose, first, the general property tax upon the real estate and personal property of the companies within reach of the tax assessor. This tax in 1909 formed about thirty per cent. of the total amount paid in taxes by a large and representative life insurance company. To this tax, provided it is properly assessed, there has never been any serious objection on

the part of life insurance companies, the burden being considered a proper one as a just contribution toward the general cost of state government.* By far the most important tax item, however, is the tax on premium income, which may vary from one to three per cent., according to the state in which a company transacts business. The tax on premiums is an unjust burden upon the business for the tax falls alike upon new premiums for risks just incurred and upon renewal premiums on risks assumed years ago. It can readily be seen that risks assumed years ago were calculated to produce a certain result on an assessment rate of mortality and interest. The imposition of taxes upon such payments must needs decrease the return to policyholders, and increase in consequence, the cost of insurance. If carried to the extreme, especially in the case of companies which issue only non-participating policies, such companies may ultimately be unable to meet in full their obligations in consequence of a policy on the part of the states which is as unwise as it is unnecessary.

Taxes on Premiums.

The practice of taxing premium receipts was ably discussed some years ago in an article in the New York Evening Post, and in part as follows:

"It is a fundamental principle of social science that the insurance contract itself ought to be free from taxation. Taxation ought to be on property, on production. Insurance contracts produce nothing.† If any tax is imposed on insurance companies or insured persons as such, it should be imposed on their property and not on their contract. The taxation of

* Probably the most important contribution to the technical consideration of the question of local taxation of life insurance companies is the brief filed by Richard V. Lindabury and Edward D. Duffield, Counsel for Plaintiff in Error, the Prudential Insurance Company of America, in the case of the Mayor and Common Council of Newark, et al., vs. The State Board of Equalization of Taxes and The Prudential Insurance Company of America, 1910.

† This question is discussed in Chapter II.

premium receipts is utterly unscientific. It has no basis of credit in the ultimate distribution of the tax. The practical effect of it is seen by a calculation of what a policy of life insurance, running thirty or forty years, will amount to at the end of the term if the premiums actually paid are accumulated at compound interest, and what it will amount to in case the premiums before accumulation are diminished by, say a three per cent. tax. Anyone making such a calculation would be startled by the result. A tax of three per cent. on a premium, when it comes to a final settlement in the payment of policies, amounts to an enormous burden on the widows and orphans of deceased policy-holders, far beyond the tax levied on any other species of property in the community."

Taxes on Surplus.

So much as regards the taxation of the premium income. The third item of importance is the tax on surplus, which forms about thirteen per cent. of the total taxes paid at the present time in the case of a large and representative company. This tax is subject to the same criticism as the tax on premiums, in that it is both unscientific and unjust, being in fact in the direction of an impairment of the contract obligations of the companies which have agreed to pay a sum certain under conditions which did not presuppose the subsequent imposition of heavy taxes. A company, by the inherent nature of the science of life contingencies, depends for the fulfillment of its obligations, first, upon a normal mortality; second, upon the realization of an expected rate of interest on its investment. The gradual decline in interest rates has made it necessary for most of the American companies to henceforth calculate their premiums on a three per cent. basis, and there has been in consequence an increase in premium rates during recent years. I doubt if this change in rates would have been necessary if the matter of state taxation had remained the comparatively unimportant item it was, even as recently as ten years ago. This point was recognized as early as 1855, when in an article entitled, "Should Life Insurance Companies be Taxed," the Insurance Monitor of New York (p. 18) said:

"The principle of insurance on lives supposes the average duration of life to be an ascertained fact, and that a given *premium* annually invested and compounded at a given rate of interest will produce the amount called for by the policy.

"Whatever, therefore, disturbs the rate of accumulation must affect the result, and a company whose engagements require $100,000 to be annually invested at six per cent will at the end of the thirty-one years (the average duration of policies) show a deficiency of $1,000,000, in case its accumulations be taxed one per cent. Taxation is therefore fatal to the business of life insurance in this state."

Stamp Taxes.

The fourth item in direct taxation is now happily a matter of history only, that is, the internal revenue tax on new insurance contracts, imposed under the war revenue act of 1898.* Under this law ordinary insurance contracts were charged a stamp tax of eighty cents per $1,000 of insurance, while industrial contracts were charged forty per cent. of the first weekly premium. This tax formed twenty-one per cent. of the total taxes paid by one large and representative company during the year 1899, and amounted to almost $100,000. A more unscientific and inequitable as well as unnecessary tax was never levied than this additional burden upon an interest already taxed beyond the point of sufferance. It was imposed upon the companies under the stress of war conditions, but even under conditions of peace the Senate submitted to its repeal only in conference committee. Those who are interested in the subject and who may wish to trace the error which underlies nearly all the insurance taxation in this country, namely, complete ignorance of the nature of the business and the effect of taxes upon vested rights and obligations, should read the debates of Congress on the reduction of the war revenue tax, February 6, 1901. (Congressional Record, Vol. 34, No. 47, p. 2194, et seq.)

* For a discussion of the first stamp taxes upon insurance imposed by the U. S. Congress, see chapter IV, p. 190.

Considering now the expenses for state supervision, licenses and fees, opinions differ as to whether these items should properly be considered taxes in the true sense of the word. The direct burden of this tax is less than the indirect burden, since in consequence of the multiform system of state supervision the general expense rate of the companies has been materially increased on account of the larger clerical expense for the compilation of data not required for office purposes and of small value or interest to the general public. Few state commissioners remain long enough in office to gain sufficient personal experience to prove of real value to the insuring public, and they seldom possess actuarial or other insurance qualifications to make their recommendations useful. Hence the cost of state supervision and the implied office expense is in itself an item of considerable magnitude imposed upon the companies in addition to the taxes already referred to.

The complications and diversities of state taxation may be further illustrated as follows: In the state of New Jersey life insurance companies pay first a tax of 0.35 per cent. on their total premium income, and in addition a tax of one per cent. on surplus. Now, in states which tax premiums collected within the state, an additional tax of from one to three per cent. may be collected, as, for instance, in the case of Kentucky, where the local state tax is two per cent. on gross premiums collected within the state. Thus the same premium income, already taxed once in New Jersey, is made subject to a second tax in the state of Kentucky, but in addition there is in force in that particular state a law under which the city of Louisville collects a further tax from life insurance companies equal to two and one-half per cent. of the premiums on new business collected in the city, imposing thus a third tax upon the same item of premium income. In Newport the same tax or two and one-half per cent. is collected, and in Covington one and one-half per cent. But this is not all, there have been paid in addition fees for state supervision, valuation, filing of certificates, etc., and license fees

for agents, all of which, of course, must come out of the premium income derived from local business, and all of which lie against the business transacted in the state of Kentucky as an expense. Even this is not all. After the various charges have been met and have been deducted from the premiums received there would be an additional tax on the remainder, if invested in local real estate, and under the war revenue act, there would have been an internal revenue tax of eighty cents per $1,000 of new insurance. Thus we have it that in this state, on a premium of say, $32.68, at age forty, for a whole life policy of $1,000, the company had to pay, first, eighty cents as the internal revenue tax; second, eleven cents as a local state tax in New Jersey; third, sixty-five cents as a local state tax in Kentucky; fourth, eighty-two cents as a local municipal tax in Louisville, Ky.: a total of $2.38, or equal to 7.3 per cent. of the premium paid!

The Burden of Life Insurance Taxation.

As has been stated, at the present time the life insurance companies of this country pay annually in excess of twelve million dollars for taxes, licenses and fees, a vast sum which, under normal conditions, would go toward a reduction in the cost of insurance or a reduction in premium rates, but which, to the contrary, have been increased in consequence of an unwise and unwarranted policy on the part of states always ready to impose additional taxes upon an interest already overtaxed. On the basis of the annual premium income of all the companies in 1909, the taxes paid were equal to 2.15 per cent. If a comparison is made with the year 1890 it appears that there has been a material increase, actual as well as relative, in the amount and proportion of taxes paid by the companies. In 1890 the companies paid $2,249,148 in taxes, equal to 1.42 per cent. of the premium income, against $12,126,470 in 1909, equal to 2.15 per cent. of the premium income. In other words, the companies in 1909 paid $4,100,000 in excess of what they would have paid had the tax rate of 1890 prevailed during the year 1909.

A still more pertinent illustration of the burden of life insurance taxation is found in a comparison of the sums paid out in taxes with the sums paid out in dividends to the policyholders. The term "dividends" in life insurance is misleading, but common usage has so adapted the term to the business that it is now difficult to invent a new one. As a rule, where the term "dividend" is used in life insurance transactions, the reference pertains to a sum of money which has originally been paid as a premium, but which subsequent experience proved not to be required. Such dividends accrue in consequence of a favorable mortality experience, of a lower expense rate than was originally assumed necessary, and occasionally in consequence of a higher rate of interest earned than the expected rate. Such dividends, then, are not profits in the ordinary sense of the word, and this fact was early recognized by Mr. Joseph J. Lewis, internal revenue commissioner in 1863, who, in his report that year to the Secretary of the Treasury, made a strong plea for the repeal of the law taxing the dividends of life insurance companies.* How far the taxes paid by life insurance companies affect the dividend paying ability of the companies is made clear by the fact that to every $100 paid in dividends in 1909 there were $19.24 paid in taxes. In other words, had there been no taxes upon life insurance interests, the returns to policyholders on participating contracts could have been materially increased in the form of larger dividends, usually applied to a reduction of the premium, or for the purchase of additional insurance.

Relation of Taxation to Cost of Insurance.

Briefly summarized, the facts pertaining to the taxation of life insurance companies may be stated as follows:

Out of every $100 received in premiums in 1909, $2.15 was paid out in taxes.

* Report of the Secretary of the Treasury, on the State of the Finances, p. 63. Washington, 1863.

To every $100 paid to policy-holders in 1909, $3.36 was paid in taxation or license fees.

To every $100 paid in death claims in 1909, $7.04 was paid in taxation or license fees.

To every $100 paid in dividends to policy-holders, largely for the purpose of reducing the cost of insurance, $19.24 was paid in taxation or license fees.

The percentage of taxation to premium income has increased from 1.42 in 1890 to 2.15 in 1909.

The ratio of taxation to dividends to policy-holders has increased from 15.5 in 1890 to 19.24 in 1909.

It is clearly indicated by these facts that the burden of taxation weighs, indeed, most heavily upon life insurance companies in the specific direction of efforts tending by economical management and careful selection to reduce the cost of insurance by dividends to policy-holders. Practically every dollar paid in taxation or license fees would naturally be returned to policy-holders as dividends, mostly used for the purpose of reducing the premiums. The increase which has taken place during the last twenty years in the ratio of taxes to premium income is still more clearly brought out in a comparison, or rather contrast, of the increase made by the companies in premium income with the increase in the total amount paid in taxation or license fees. During the period, 1890-1909, the premium income of American insurance companies increased 257.6 per cent. while the amounts paid in taxation or license fees increased at the rate of 439.2 per cent. In other words, to every one per cent. of gain in premium income or growth of the insurance business, there has been an increase of 1.7 per cent. in taxation, or burdens tending to materially hinder the greatest possible development of life insurance in this country.

But perhaps the most serious aspect of the tax question is indicated in the comparison of tax payments with the interest earnings of the companies. With companies established for many years this matter is, perhaps,not of quite so much importance as it is to companies recently organized, or which are com-

paratively new in the business of writing ordinary insurance. While the total income of all the American life insurance companies from interest and rents was $159,804,000, the taxes paid during 1909 were $12,126,470, representing 7.6 per cent. It has already become necessary for many companies to calculate their premiums on a three per cent. basis and an increase in premium rates has been made necessary because it is at present, and will probably be for many years, impossible to realize the high rates of interest obtainable in the past.

The Incidence of Life Insurance Taxation.

The incidence in general taxation has properly been called "the vexed question in finance," and, in the words of Mr. Mayo Smith, "Who really pays the tax? The person on whom it is levied or some other person upon whom the original sufferer can roll off the burden?" The answer to this question with particular reference to life insurance is that the incidence of life insurance taxation unquestionably falls upon the policy-holders, even though the company, as the representative or trustee of the policy-holders, pays the tax in the first instance. As has been said in an able article on the subject, which appeared in the Insurance Critic under date of December, 1909:

"A tax on the company is really a tax on the policy-holders who form the company, and is paid only by them. This is obvious, if it is considered that a company has no other fund than the proceeds of the premiums paid by its policy-holders, and as the tax must be paid in out of this sole fund the consequence is that the cost of the insurance to the policy-holders is correspondingly increased. This may be demonstrated as follows: The premium paid by the policy-holder is based on two things—the assumption of a rate of probable mortality, and the assumption of a probable rate of interest on that part of the premium which is the reserve, or laid aside, for the payment of future losses. To this something is added as a provision for expenses in conducting the business. These things cover the normal cost of insurance to the policy-holders. If the actual experience as to mortality, rate of interest or expense is more favorable than the assumption, whatever is left is sur-

plus and is returned to the policy-holder as an over-payment, unless insured on the non-participating plan. Any tax paid by the company comes out of that surplus, if there is any. It makes the return to the policy-holder just so much less, and, consequently, makes the cost of his insurance just so much more."

In a similar discussion the New York Evening Post of December 7, 1900, referring to the fact that the war tax on life insurance was paid by the policyholders of the company said:

"Although this tax was nominally paid by the insurance companies, it was in fact, paid by the policy-holders. This is an enormous tax on the frugal and provident men who wish to invest their savings in insurance policies for the benefit of their families when death shall deprive them of husband and father. It operates as a penalty on the prudence and thrift which alone seek this form of trust investment, and which, instead of being taxed with this oppressive burden, should be as far as possible fostered and encouraged."

The same point was also brought out in the congressional debates on the repeal of the war revenue act of 1898, when the chairman of the committee in charge of the bill said: "Then we go a step further and take the stamp tax off insurance policies. This latter tax is paid almost entirely by the man who receives the insurance. *The man who provides for the future of his family in the event of his death by securing a life insurance or in providing an indemnity for the family in case the home should burn down, was forced to pay this tax.* Hence the repeal of a law which in the first instance should never have been placed on the statute book, in plain recognition of the plea for simple justice that those who have voluntarily undergone privation and self-denial for the purpose of obtaining economic freedom for otherwise dependent survivors should not be taxed a second or a third time for the ulterior purposes of the state. A tax on life insurance, as thus paid by the policy-holders, is not a tax on their property, but on their losses, and no more justifiable than a tax on a house after it has burned to the ground. The hope for reform in life insurance taxation lies in the direction of a true appreciation and clear comprehension of the

incidence of the tax and the general recognition that this incidence cannot be and is not shifted from the policy-holder upon the shoulders of someone else more able to bear the burden.

Hence the urgent plea that this subject of life insurance taxation should receive the most serious public consideration to the end that the present tendency to increase the already heavy tax burden of the companies be checked and a gradual decrease in the present tax rate be brought about. This plea is based on the fact that the annual taxes now exceeding twelve million dollars fall with undue severity upon a class of people than whom none is more deserving of the most generous consideration on the part of the state, a class of people who in the large majority of individual cases have undergone an almost inconceivable amount of self-denial for the sole purpose that those near and dear who are to live after them may live lives free from the taint of state aid or private charity. To tax this class of people, the policy-holders of life insurance companies, is, in the words of Charles Sumner, "A tax upon a tax," and in his emphatic language, "consequently, barbarism." "Increased taxation," he said, "comes out of the thousands of policy-holders, and not from the companies' officers, as is often ignorantly assumed," and to this argument there is no answer save that the states need the money and that the life insurance companies can be conveniently made to pay it.

CHAPTER VII.

THE TAX BURDEN ON LIFE INSURANCE POLICY-HOLDERS.

Introduction.

Life insurance companies are more heavily taxed than any other commercial interest and the rate of taxation is increasing more rapidly than the growth of the business, which itself has been little short of marvelous. For many years appeals have been made to legislative bodies to refrain from a further imposition of taxes, but the arguments and pleas have, as a rule, been ignored and treated with indifference and even contempt. The earlier conviction that life insurance should not be taxed at all, and which had been favored by the foremost of English and American statesmen, from Pitt and Peel to Daniel Webster, is now no longer tenable as a proposition in public finance and the day seems to have passed when considerations of public morality and social economy had weight in the deliberations of legislative assemblies, determined to find new sources of revenue to meet the results of extravagance in public expenditures. The state having the power to tax, the power has been abused until a point has been reached where it is proper to speak with entire truth of the tax plunder of life insurance policy-holders at the present time. And the end is not yet.

The Burden of Insurance Taxes.

For it is a plunder and nothing else, when the most prudent and unselfish class of citizens are compelled, through their insurance institutions, to pay a premium income tax, and other taxes, fees and licenses of more than twelve million dollars

a year as a forced contribution to the revenues of states in which they may not reside and from the government of which they may not derive any benefit whatever. Life insurance companies or associations are not money-making institutions in the same sense as this term is used of banks, transportation companies, and mercantile undertakings generally, for while some are stock companies and others are mutual, and while still others combine both principles, it is an incontrovertible fact that they are not money-making institutions *per se* and that they have not been granted their charters for mere money-making purposes. The dividends which are declared and paid by stock life insurance companies are actually small in amount, practically uniform for a long period of years and they constitute but a relatively small item in the aggregate expenditures. The companies do not exist for the purpose of making money for stockholders, or to make profits for policy-holders, but they exist primarily and solely for the equitable distribution of losses which would otherwise fall with crushing force upon unfortunate individuals. There, however, are no objections to a tax upon stockholders' profits any more than there are valid objections to a reasonable tax upon the real and personal property of the companies, required for the conduct of their business, but there are most serious objections against a substantial tax upon the premium income, or the gross or net income, as the case may be. Life insurance by its nature involves delicate and intricate calculations arising out of the science of life contingencies and the doctrine of compound interest, and the results anticipated may not be realized if an increasing rate of taxation deprives the companies of the normal earning power of money assumed in the original premium calculations. Since the premium is the basis of the contract, the amount of which itself is the contractual consideration, an increasing rate of taxation upon the premium income may impair the contract and to that extent make the ultimate fulfillment of all contractual obligations impossible.

The Social Value of Insurance.

Without making any special claim for life insurance as a social institution of considerable value to the state or the nation, it is generally held as an incontrovertible truth, sustained by the experience of every-day life, that life insurance is the only effective method of combining the value of systematic savings with the benefits resulting from the principle of association through which adequate protection is secured against inevitable losses which would otherwise fall heavily upon the individual and the state. The insured population, as a class, represent, therefore, a much more worthy and socially effective body of citizens than the uninsured, since the former are very much less liable to require state aid in poverty and support for widows, orphans and the aged. In proportion as society advances the social duty of providing against the financial consequences of the uncertainty of life through insurance becomes more generally recognized, until the duty of insurance has become accepted as a universal principle of right conduct in the relation of the individual to society throughout the civilized world.

The Increase in Insurance Taxation.

Over forty years ago this aspect of the business was clearly recognized by the late Elizur Wright, who, in the Massachusetts Insurance Report for 1867, and at a time when the tax upon life insurance was less than one per cent. of the premium income, said, "Life insurance deserves the fostering care of wise and liberal legislation. It should be freed from all unnecessary burdens. Government should as soon tax its asylums and hospitals as to seek a gain or revenue from the deposits which foresight and affection has set apart for the protection of thousands among the most helpless of its own citizens. A tax upon life insurance is nothing more than a tax upon widows and orphans." The suggestion, unhappily, was not heeded and the tax rate has gone up year after year until it has increased from seventy cents on every $100 of premium income in 1860, to $1.23 in 1875, to $1.42 in 1890, and to $2.15 in 1909. The total

sum paid in taxes, licenses, fees and for the cost of state supervision in 1909 was $12,126,470. This sum was equivalent to 1.62 per cent. of the gross income of the companies from all sources, or equivalent to a rate far in excess of the corresponding rate of taxation imposed upon commercial interests generally. No store, no bank, no transportation company, pays taxes upon its gross income, and it must be self-evident to even the least informed or most indifferent, that the amount thus exacted bears a definite and important relation to the cost of the insurance sold. It requires no extended argument to prove that in the nature of the business and by long-established practice and usage, the money thus exacted in the form of taxes would otherwise have been returned to the policy-holders, or would have accrued to their benefit in some form or other, for the object and sole purpose of reducing the cost of insurance. It is little short of a preposterous farce for legislators to attack the companies for extravagance, or for failure to reduce expenses, when a constantly increasing tax burden is placed upon the companies, greater than any sum which could be saved by the most rigid economy in the expenses of agency or office administration.

Life Insurance Not for Profit.

It will be argued, in defence of the present system, that life insurance ought to contribute its share to state revenue, like any other industry or commercial undertaking, but life insurance is totally different from commercial enterprises generally, in its objects and aims, as well as in its fundamental, theoretical and practical assumption. It does not exist, and the companies have not been formed, for profit-making purposes, and life insurance is not for gain, but for the distribution of losses, having for its object the protection of the family or the individual against the financial consequences arising out of the uncertainties of life. By its nature, the premium (so-called) cannot be the exact equivalent of the ultimate cost, in consequence of which a re-distribution is made from time

to time, in the case of participating policies in the form of dividends, and in the case of non-participating policies in the form of voluntary concessions. This return is not a profit, but evidence of an over-charge, determined by subsequent experience and arising out of a more favorable mortality experience, or a higher rate of interest earnings, or of a lower rate of general expenses than was expected. Over-charge may be technically called surplus, but it is not surplus or profit in the commercial sense of the term, and to tax this over-charge is to take an unjust advantage of the most thrifty element of the population and to hinder materially, by increasing the cost, the largest possible progress of this form of social protection. To, therefore, tax the premium income is to tax the policyholder unjustly and every injustice in taxation reacts in time disastrously upon the progress of society itself.

The Menace of a Tax upon Reserves.

Still more of a menace to the future security of the companies is the proposal that a tax should be imposed upon reserves, so-called, which constitute the fund set aside in compliance with law for the future discharge of contractual obligations. How that fund must be accumulated, how it must be invested, how it must be conserved, is all a matter of statutory requirement and not a dollar can be improperly diverted therefrom except through the taxing power of the government. To impose a tax upon this fund of three-quarters per cent., as has been proposed by the Governor of Wisconsin, would be to imperil and to imperil with certainty the future of life insurance companies and their ability to carry out their contractual obligations with their policy-holders.

The Need of Tax Reform.

There is so much to be said upon this subject that, regardless of the fact that life insurance taxation has a literature of its own, much, if not most, of the work to bring about the necessary reforms remains to be done. Year after year earnest

and able appeals have been made by authorities on life insurance taxation, but little heed has been given to their pleas for equity and justice in behalf of the policy-holders' interests. In 1908 the whole subject was ably discussed before the Association of Life Insurance Presidents, including contributions by Prof. Zartman, of Yale, President Dryden, of The Prudential, and Samuel B. Smith, of the Volunteer State Life, and a resolution was adopted urging life insurance companies to interest their policy-holders, as far as practicable, and to enlist their co-operation in a determined opposition towards a further increase in the tax rate and efforts to bring about a reduction in the rate. President Dryden argued in behalf of a uniform rate of one per cent. of the premium income, which, if adopted throughout the country, would save the policy-holders over five million dollars per annum. He called attention to the very much lower rate in certain European countries, and in particular in Germany, where the rate is only one-eighth of what is paid by life insurance companies in America. In concluding an able and comprehensive argument, Mr. Dryden said:

Life Insurance Taxation in Germany.

"If the German Empire, with its vast burden of military, colonial and other expenditures far in excess of ours, refrains from taxing its life insurance policy-holders more than a quarter of one per cent. of the premium income, there can be no economic or political justification for imposing a tax of two per cent. (eight times as much) upon the premium income of American life insurance companies. If the great state of New York, with its numerous state and municipal expenditures of all kinds, refrains from taxing life insurance companies more than one per cent. of the gross premium income, I insist that there is no corresponding justification on the part of other states to tax life insurance companies at a higher rate."

Some Results of Public Education.

Some good, no doubt, has followed this appeal to the public and strength has been given to the movement for organized opposition towards a further increase in the rate.

As stated by Mr. Robert Lynn Cox, the General Counsel of the Association of Life Insurance Presidents,

"In seven States, therefore, it has been proposed this year (1908) to increase the tax burdens of policy-holders largely because it seemed to be an easy and effective way to raise revenue with little protest from those who pay the tax. It is pleasing to note in this connection that while bills were proposed that would have added in the aggregate by way of taxes at least $275,000 annually to the expenses of the business, and therefore to the cost of life insurance, the actual increase from the legislation of the year will amount to less than $25,000 per year. Even this increase will be offset in part by slight reduction of rates in two States. We believe that this favorable showing is largely the result of our efforts to prove to legislators that the taxes imposed upon life insurance increase the cost, thereby discouraging a business which it is the duty of the State to encourage and protect. The subject of taxation cannot, however, be dismissed from our mind when we consider the fact that at least a dozen States are facing large deficiencies in necessary revenue, and that under laws of recent enactment commissions will be required to consider the revision and readjustment of the tax laws in a dozen States within the next eighteen months. That the interests of policy-holders as a class must be represented before these commissions is manifest when we consider that they owe their existence to the needs of several States for additional revenue, and the individual who most generally does not know that he is being taxed, or, knowing, has no real opportunity to oppose, furnishes a most attractive mark for those who are seeking increased revenues."

Federal Corporation Tax on Insurance.

While some of the states have refrained from imposing further taxes, the federal government itself, through the sanction of congress, has, for the first time in its history imposed a tax upon the net income of legal reserve life insurance companies, including such companies in the same class as commercial undertakings generally, organized and carried on for profit. Stamp taxes have been imposed on two previous occasions, first, during the Civil War, and second, during the Spanish-

American War—but they were war taxes and, perhaps, as such justifiable, in view of the urgent need for additional revenue. But for the federal government to impose a tax upon the net income of life insurance companies during a time of profound peace and plenty, is but another evidence that most of what has thus far been done to oppose unjust taxation has been of no avail. If the tax imposed is really for revenue-raising purposes, the Ways and Means Committee could easily have found other sources from which to derive the necessary amount which may be required for the needs of the government. If the tax has been imposed for other purposes than revenue, it is contrary to our theory of government, which does not give to the federal government the right and the power to achieve that by indirection which it is specifically excluded from achieving by direct enactments. If the object of the taxing of life insurance companies is the same as it is alleged to be in the case of other corporations, and that is, to secure to the federal government power and control over these corporations, through the medium of taxation, then the federal government will secure the right and the power of federal insurance supervision, which has been so strenuously denied to be within the meaning of the commerce clause of the Constitution—but whatever may be the object, whether for revenue or for control, the tax is contrary to the interests of the policy-holders, a hindrance to the business, and a menace to the future, with the ever-present possibility that in addition to heavy state taxation, it may ultimately cause the companies to default in their obligations. Taxation in any form is but another word for state interference with industry, and state interference is practically equivalent to state supervision and control. If the United States Congress has *not* the power to supervise and regulate insurance companies, it would seem to be a gross abuse of the taxing power of the Constitution to use it to attain an end which is otherwise held to be unconstitutional.

Taxation Should be for Revenue Only.

There can be no more sound principle in political economy and political science than that all taxes should be for revenue only and not for a hidden or ulterior purpose. That is not honest legislation (however honest the intent) which attempts to destroy, regulate or change by taxation and thus accomplish what cannot be attained otherwise. Congress might have imposed a prohibitory tax upon lottery tickets, but Congress preferred to achieve the end sought by prohibiting the lottery companies the use of the mails. In the words of the foremost American authority on the theory, and practice of taxation, the late Mr. David A. Wells: "To seek to make taxation, which is a fit contrivance only for raising revenue an instrument for effecting some ulterior purpose, be it never so just and legitimate, to seek to use it for the attainment of any other object than the obvious one of raising money, is to lose sight of the fundamental principle of every free government and to forbid all expectation of recognizing any other basis for the exercise of this great sovereign power of the state, than expediency, which in turn will depend upon the actions, passions and prejudices of legislators who may not be the same in any two successive legislative assemblies." The same conclusion is advanced by Cooley, the foremost American authority on the law of taxation, in the statement that "A burden not laid for the purpose of producing revenue, but in order to accomplish some ulterior object, which the general government lacks the power otherwise to accomplish, comes under no definition of the word 'tax' which is recognized in public law." These objections are fundamental and they require to be brought home to every American citizen who desires the continuance of our form of government as it was established by the fathers and designed by the wisdom of true statesmen of another day.

Moral Aspects of Life Insurance Taxation.

There is another point of view from which this question may be considered and that is the morality of exacting a tax

from the contributions of the most economical, thrifty and self-sacrificing of citizens, for the furtherance of more or less ill-reasoned projects of prodigal governmental expenditures. It would be much better and more conducive to the public interest if the federal and state legislatures would concern themselves with proposals for retrenchment and economy rather than to encourage extravagance in the use of public funds. It appears to be an accepted axiom of governmental policy that the rule which applies to every citizen, not to spend more than his income, does not apply to government and that enormous burdens may be imposed upon subsequent generations in the furtherance of state or national projects, many if not most of which, involve a waste of public money rather than the achievement of any beneficial results.* Wells, quoting from Sharwood's Legal Ethics, properly observes with reference to this point, that "One grievous invasion of property—and, of course, ultimately of labor, from whose accumulations all property grows—is by government itself, in the shape of taxation for objects not necessary for the common defense and general welfare. Men have the right not only to be well governed but to be cheaply governed—as cheaply as is consistent with the due maintenance of that security for which society was formed and government instituted." And to this Wells adds the well-known words of President Cleveland in his Message of December, 1888. "To the extent that the mass of our citizens are inordinately burdened beyond any useful public purpose and for the benefit of a favored few, the government under pretext of an exercise of its taxing powers enters gratuitously into partnership with these favorites to their advantage and to the misery of a vast majority of our people."†

*I may also quote the words of Mr. G. Cassel from his treatise on the "Nature and Necessity of Interest," "that the world is not so rich that every demand can be satisfied." (p. 72).

†The Theory and Practice of Taxation, by D. A. Wells, p. 250.

Constitutional Aspects of the Tax Problem.

It is not the present purpose to discuss the question whether the Federal Corporation Tax was proposed primarily for revenue-raising purposes, or for the vastly more important object of federal government supervision and control. The constitutionality of the tax will, unquestionably, be settled by the Court of last appeal, and while the same conclusion may be advanced as in Gibbons vs. Ogden, that "Congress is not empowered to tax for those purposes which are in the exclusive province of the state," it is also well to recall that the Supreme Court has held that the judicial power cannot inquire into the intentions of Congress in imposing a tax; and that if injustice is done the only remedy is in appeal to the legislative power that has inflicted it. But it is nevertheless equally probable that the Supreme Court will take cognizance of the general state of the public mind and the public conviction, that the Corporation Tax was not enacted primarily for revenue-raising purposes, but chiefly and perhaps solely to obtain for the federal government the right and power to control and supervise state chartered corporations.

The Power to Tax Is the Power to Destroy.

The federal constitution, as interpreted by the Supreme Court, prohibits the state from taxing the agencies and instrumentalities of the federal government, and by a like inference, according to Wells, and other authorities on taxation, "The federal government cannot tax state instrumentalities or agencies," and among these there are not any more important than state chartered corporations. If the federal government can rightfully impose a tax of one per cent upon the net income of such corporations, it can impose any other tax it may deem necessary to accomplish its purposes, and among these purposes in course of time may be the desire to destroy. If the federal government can rightfully impose a ten per cent. tax upon the circulation of state banks and destroy state institutions as state banks of issue, it can in its discretion destroy, by the imposition

of a prohibitory tax, all state chartered corporations, and among these state chartered insurance companies. The principle has been laid down by the Supreme Court in the case of Weston vs. the City of Charleston, that "If the right to impose a tax exists, it is a right which in its nature acknowledges no limits."

The Inequalities of Life Insurance Taxation.

Aside from constitutional objections, there are, however, specific reasons why the federal government should not have imposed this additional tax burden upon life insurance policyholders. The total amount of revenue to be raised through the tax could have been obtained with equal facility through any one of the many stamp taxes imposed during the Spanish-American War. The tax mentioned certainly violates one of the canons of equitable taxation, as defined by Sismondi, the economist, that "Taxes should never touch what is necessary for the existence of the contributor." Life insurance, under modern conditions, is an absolute necessity for maintaining the American standard of life and social security, and in exact proportion as taxes diminish the returns to policy-holders, the cost of insurance is increased and to that extent the largest development of the business is prevented. The human mind is so constituted that even an apparently slight difference in price will affect the purchase, and every possible reduction which can be made in the cost of insurance extends the sphere of life insurance operation.

The Facts of Over-taxation.

The facts of over-taxation in life insurance are, in brief, as follows: The 189 legal reserve life insurance companies transacting business in the United States in 1909 had a total income of $748,027,892, and a premium income of $565,228,893, insuring $15,480,721,211 of family and individual protection. The companies during the same year paid $12,126,470 in taxes, licenses, fees, and the cost of state supervision, equivalent to 1.62 per cent. of the total income and 2.15 per cent. of the pre-

mium income. This enormous sum is a heavier burden of taxation than the corresponding burden placed upon any other large financial or commercial interest. In its final analysis every dollar of taxation is paid by the policy-holders and every dollar represents diminished utility of the true and ultimate value of insurance.

Taxes Paid by Policyholders and Beneficiaries.

A brief comparison of the actual facts of insurance experience will very clearly emphasize the truth and importance of the foregoing assertion. In 1909 the total amount paid in death claims to insurance policy-holders was $172,280,388. Had there been no taxes or fees of any kind, the beneficiaries could have received $7.04 more for every $100 actually received in the form of claim payments. Or, to consider the subject from another point of view, during the same year there was paid out to life insurance policy-holders $63,040,725 in dividends, so-called, including what is technically a temporary over-charge and, in fact, a return of that over-charge plus the interest accumulations for the time during which the return has been withheld. If there had been no taxes of any kind upon insurance, the policy-holders could have received $19.24 more for every $100 actually received in dividends or concessions, and by just so much the true cost of insurance would have been reduced and the utility of this method of family protection would have been correspondingly enhanced.

The Insurance Tax Ratio in Germany.

The fifty-nine German life insurance companies in 1907 received in premiums M. 498,434,000, and they paid out in taxes and fees of all kinds the sum of M. 1,222,000, or .245 per cent. of the premium income, against 2.15 per cent. paid out during 1909 by life insurance companies in the United States. Had the American companies been taxed at the same rate in proportion to their premium income, they would have saved to their policy-holders $10,741,659 during 1909 and $86,269,041

during the past ten years. The same fifty-nine German life companies had a total income during 1907 of M. 656,606,000 of which the amount paid in taxes and fees for government supervision was 0.186 per cent. In contrast, the American companies during 1909 paid 1.62 per cent. of their total income in taxes, so that if they had paid taxes in proportion to the total income by the German standard, they would have saved to their policy-holders the sum of $10,735,138 during 1909 and of $86,756,708 during the prior ten years.

The Insurance Tax Ratio in Canada.

The burden of life insurance taxation in Canada is also much less than in the United States—in fact, less than one-half the average rate in proportion to the premium income. Twelve of the principal Canadian companies, with a premium income during 1907 of $18,801,814, paid out in taxes, licenses, fees, and cost of supervision, $200,062, or at the rate of 1.06 per cent . Had the premium income of American life insurance companies during 1909 been taxed in this proportion, the total amount saved to American life insurance policy-holders would have been $6,135,044 during the year, or $47,796,987 during the last decade.

The Insurance Tax Ratio in Australia.

Mention may also be made of the fact that the insurance tax ratio in Australia is much less than in the United States. The foremost Australian company, the Mutual Provident in, 1907 had a total premuim income of £2,061,067 sterling, of which it paid £28,736 in taxes of all kinds, or at the rate of 1.394%. Had the American companies in 1909 been taxed at this rate, they would have saved to their policy-holders the sum of $4,247,179.

Income Tax Reductions on Account of Life Insurance.

In England and in some other foreign countries, deductions are permitted to be made from assessments for income tax to

the amount paid in life insurance premiums, but in England, for illustration, this amount must not exceed one-sixth of the net income liable to tax. In 1906-07 the amount of income allowed to be deducted on account of life insurance premiums amounted to £9,155,000, which at the average rate of 1s. in the pound, would have produced £457,750 of additional revenue. The amount thus freed from income tax was within two million pounds of the amount exempted in the same manner in the case of charities, hospitals, and Friendly Societies. As a further illustration of the importance of this concession to life insurance policy-holders in England, it may be stated that in the five years ending with 1908, over £100,000 was returned to the taxpayers on account of over-payments made in ignorance of this salutory provision of the law.

European Methods of Insurance Taxation.

The foregoing illustrations, derived entirely from official sources prove conclusively that other great nations have refrained from taxing life insurance as it is taxed in the United States at the present time. The Commissioner of Insurance of Texas was, therefore, in error when he made the statement that "There is no apparent reason for concluding that the average amount of taxation levied in European countries, directly or indirectly, in one form and another upon the life insurance business is less than the average tax levied in the United States." If the Commissioner had examined the revenue accounts of any single German life insurance company, he could easily have ascertained that the tax rate is very considerably less than it is in America. The total amount paid in taxes of all kinds by German life insurance companies was 0.245 per cent. compared with 2.15 per cent. of the premium income paid by American life insurance companies in 1909.* It is quite true that there are certain documentary stamp taxes required to be paid in various German states, as well

*That is to say, for every 24c paid in taxes by German Life Ins. Cos., Amer. Cos. pay $2.15.

as in other continental states and in England, but these are small in amount, they are paid directly by the policy-holder, and they are compensated for, in a large measure, by the income tax exemptions, such as are permitted to be made on account of life insurance premiums paid in England and certain other European states. It is not, however, so much a question of the method of taxation as of the tax burden itself, and no German life insurance company at the present time pays directly or indirectly in taxes what is paid by American life insurance companies. In Italy and some other countries the tax rate is high, and the progress of the business has been very slow, as a result of the heavy taxes imposed. But in the greatest of the continental states, that is, Germany, where the Imperial government is most heavily pressed for new sources of revenue, where new taxes have been imposed upon a large variety of interests and instrumentalities of commerce, including taxes on railway tickets, taxes on advertisements, taxes on gas and electricity, and increased taxes on tobacco, no additional burdens have been imposed upon life insurance, and, in fact, throughout the extended Parliamentary debates no one has proposed that the necessary revenue should be derived from the spoliation of the trust funds of life insurance policy-holders.

Gross Inequality of Life Insurance Taxes.

Granting, however, for the sake of argument, the expediency of life insurance taxation, it remains to be proven whether or not the tax on premiums is equitably assessed upon the different classes of policy-holders. It is an accepted rule in law that "While perfect equality is unattainable, only the statutes based upon false and unjust principles, or producing gross inequality will justify the interposition of the courts." It requires no extended analysis of the facts in the case to prove that a substantial tax upon premiums is productive of gross injustice in the case of one class of policy-holders as compared or contrasted with another. In the nature of life insurance, the premium is the basis of the contractual relations between the insured and the

company, and out of the premium arise all the subsequent results to the insured, favorable or unfavorable, as the case may be. If the premium is insufficient, the contract cannot be carried into effect, and it is on this ground more than on any other that legal reserve life insurance is so immeasurably superior to fraternal or so-called insurance on the assessment plan. Since the premium is conditioned by the age of the insured and the subsequent after duration of life, the premium is necessarily lowest in youth and highest in old age. That is to say, to obtain the same amount of insurance, a person of advanced years has to pay much more than a person of younger years. For illustration, a Whole Life Non-Participating $1,000 Policy costs $14.96 at age twenty and $38.83 at age fifty. Now, a premium tax of two per cent is equivalent to thirty cents per $1,000 of insurance at age twenty, and to seventy-eight cents at age fifty. If that is not gross inequality and unjustifiable discrimination in taxation, it will be difficult to establish that contention in a more satisfactory manner.

The Insurance Tax Burden on the Aged.

The importance of this consideration of equality and justice suggests a somewhat more extended consideration of this point. A policy taken out at age twenty on the Twenty Payment Life Non-Participating plan will cost annually $22.60 per $1,000, or forty-five cents in taxes, when the rate is assumed to be two per cent. In twenty years the insured will, therefore, pay $9.00 in taxes, exclusive of the compound interest accumulation on the amount paid, if available for savings or investment. The same amount of insurance on the Twenty Payment Life plan at age fifty will cost $44.99, and the average annual amount paid in taxes will be ninety cents, or $18.00 during the twenty years of policy continuance. It is, therefore, self-evident that the man at fifty pays exactly twice as much in taxes as the man at twenty, although the latter is in a much better position to pay the tax than the former. The disparity in the tax burden would naturally be still greater at higher ages.

Tax Reduction a Necessity.

It is not necessary here to consider other evidences of inequitable taxation, the conflict of state laws affecting life insurance policy-holders in different states, the evil results of retaliatory legislation, and the inequality of burdens upon different classes of policy-holders, paying the same premium but not the same tax. Evidently, uniformity is most to be desired, but next to uniformity, there should be permanency, and next to permanency there should be reduction to a maximum of not more than one per cent. This is the rate which was conceded to be fair and equitable by President Dryden in his address before the Association of Life Insurance Presidents, and this principle may be said to conform to the sentiment and views of the majority of Insurance Commissioners, who have given this subject careful and deliberate attention. At the National Convention of Insurance Commissioners, in 1909, the President of the Association, the late Mr. Benjamin F. Crouse, Insurance Commissioner of Maryland, after referring to the very exhaustive and strong report made by a Special Committee of the convention at the previous meeting, recommending conservatism in matters of taxation and a reduction in the tax rate, said, "I think that we should not fail to re-emphasize the main features of that report and thus demonstrate that we propose to stand firmly in favor of a reduction of what we believe to be excessive taxation on those who by their industry, thrift and frugality are creating a fund for old age or in the event of death to provide for those whose support is gone. The insurance business should undoubtedly bear its fair and proper share of governmental expenses, but should not be burdened with heavy and excessive taxes simply because it can be done by hiding and covering them up in the premiums paid by policy-holders or by reducing dividends which otherwise would be largely increased. I know how difficult it is to get legislatures to surrender a source of large revenue, such as the insurance business, especially when the expenses of government are greater than the income; but if the people who do the voting

are clearly convinced that those who pay insurance premiums are paying excessive taxation on their savings, some relief will undoubtedly come."

Public Interest in Life Insurance Taxation.

The time will come, undoubtedly, when policy-holders will realize and understand that they alone are paying the taxes imposed upon life insurance companies out of their premiums and that the ultimate cost of insurance is increased in practically exact proportion to the increase in the tax rate. They will understand and better appreciate the tremendously suggestive fact that since 1865 over $160,000,000 has been paid by life insurance policy-holders in taxation of every kind, including licenses, fees, and the cost of state supervision. They will protest against double taxation, they will object to the state making insurance dear, while the companies by every means in their power are determined to reduce the cost to the lowest possible basis, and having come to an understanding and a realization of the facts, the policy-holders, as voters under our representative form of government, will not fail to make themselves heard and see to it that their objections receive respectful consideration.

Life Insurance Taxation without Representation.

Every state which imposes a tax upon the total premium income of the life insurance companies, or associations transacting business therein, violates one of the first canons of equitable taxation, which is comprehended in the brief statement that "The sphere of taxation should be limited to persons, property and business exclusively within the political jurisdiction of the taxing power." As the taxes are now imposed in some of the states, the policy holders throughout the country pay their contribution prorata towards the support of state governments in which they themselves have no interest and in which they have no advantage. That is certainly taxation without representation. and, as such, contrary to the fundamental

conception of American liberty. Such taxation violates the economic axiom that "No tax should be imposed by a state or government, except by the consent of the people by whom it is to be collected, either directly or by their authorized representative in Congress, Legislature, or Parliament, assembled." And such taxes imposed under whatever circumstances, in whatever manner, or for whatever reason, or by whatever taxing authority, are contrary to our accepted principles of political justice, and they should be resisted by all proper means as a menace to the future of our political institutions.

Injustice of Insurance Franchise Taxes.

It is equally unjust and in violation of the canons of equity in matters of taxation that a state should impose a heavy so-called franchise tax, which is but another term for exacting large amounts from the companies for which no equivalent benefit is rendered. In the every-day interpretation of the term "franchise" there is implied a special concession, a special privilege, or a special advantage, such as the right of eminent domain given to transportation companies, or the right of a semi-monopoly given to public service corporations, but no such rights and privileges are given to life insurance companies in the granting of their charters. Professor E. R. A. Seligman has defined general corporation franchises as "the mere privilege to act as a corporation," that is,the right to live or to exist as a corporation, and for any state to impose in return for this right a so-called franchise tax of one per cent, or of an average of 1.62 per cent. of the gross income, is a grave abuse of the taxing power and a serious injustice to the most thrifty and unselfish portion of citizenship. While a state, no doubt, has the right to impose any condition it may see fit as a condition precedent to the granting of a life insurance charter, the state has no moral right at least to subsequently impose burdens which may make it impossible for the corporations to carry out all their contract obligations.

Ethics of Life Insurance Taxation.

But a premium income tax conflicts otherwise with the canons of equitable taxation, in view of the accepted principle in all taxation, that "The tax must above all possess the requisites of legality, of certainty, of legitimacy, or equality, and of *morality*." Granting, for the sake of argument, that the federal corporation tax upon insurance, and the state taxes upon the premium income, conform to the first four of these qualities, they certainly do not meet the last, or the requisite of morality. Every premium paid on account of life insurance is already a self-imposed form of taxation, primarily and chiefly for the benefit of others, and indirectly a contribution to the welfare of the state. Life insurance premiums are voluntary deductions from the family budget, which among the improvident, the reckless, the indifferent and the profligate are expended for drink, for tobacco, for amusement or luxuries, in disregard of every principle of economy.

A Tax Burden upon Losses and Calamities.

But if the principle of life insurance taxation is sound, why does not the state impose a direct tax upon the payments to policy-holders, which could be made to produce the same amount which is now exacted, but which in that case would be clearly apparent and readily within the understanding of the insured. Such a tax could be made progressive, so that the claims for small amounts might be exempt and the claims for large amounts be taxed in proportion to the wealth of the beneficiary. To raise the amount paid in taxes and for the cost of supervision during 1909, amounting to $12,126,470, by a direct tax on death claims would amount to 7.04% of such claims paid in 1909. If such a tax were imposed, the policyholder would know and know whom to hold responsible for a tax burden upon losses which is without a corresponding instance in the whole history of taxation. It seems appropriate to include here the sarcastic comment of the New York Sun, many years

ago, when the tax burden was very much less indeed than it is at the present time:

Early Objections to Insurance Taxation.

"Iowa and Pennsylvania make life and death alike pay tribute to Caesar, and impose a toll on the entrance to the graveyard and a transit fee upon the avenue which leads to the 'place of skulls.' They will do better to erase from their statute books a law so contrary to public policy, so hostile to prudent provision for widowhood and orphanage. It does not strike at the life insurance companies, but rebounds upon the beneficiaries and their provision. If they will persist in the collection, we will offer a hint for their Committee on Ways and Means. When the body of the departed is composed in its shroud, let the coin upon the closed eyelids escheat to the State and swell the current revenues of the treasury; and if a specific officer is created for the duty, he may be designated as the Collector of Pennies from Dead Men's Eyes."

No Objection to Rational Taxation.

No one who has ever written with authority on the subject of insurance taxation has objected to the proper taxation of the real property held by insurance companies, and in 1909 the American companies paid taxes for this purpose to the amount of $2,328,229, or 19.2 per cent. of the whole sum paid out in taxes. The remainder of the taxes, amounting to $9,798,241, was paid upon premiums, reserves, surplus, etc., or as license fees for agents and the direct cost of state supervision and examination. It is difficult to explain why so useful a person as an insurance agent should pay a license tax to carry on his trade, when a minister, a doctor, or a social worker in a settlement, is not required to pay a similar tax, to work for the amelioration of human distress in the same direction, and, broadly speaking, primarily for the same purpose of self-support. There is no more charity in the work of a doctor, or a settlement worker, than in the work of a life insurance agent, and to tax the latter and not the former is unjust and rank discrimination.

Unjust Discrimination Against Life Insurance Policy-Holders.

If the premium payments of life insurance policy-holders may be taxed to the extent of more than two per cent., why should it not be equally just and fair to impose a corresponding tax upon the receipts of hospitals, funds for foreign missions, churches, charities, settlements, etc. But, granting that these agencies fall within a narrower definition of the term "charities," there certainly is no fundamental difference in the amounts deposited in savings banks, which are exempt from taxation in most of the states, and upon the annual deposits of which no Legislature would dare to impose an annual tax of two per cent and more. To a considerable extent the savings function in life insurance performs the same purpose as in savings banks proper, being subject to the operation of the principle of compound interest, and whatever is taken from one should, with equal justice, be taken from the other.

An Abuse of State Power.

And here it may be asked, by what *right* does the state tax life insurance premiums and divert to other uses the sums contributed for a specific purpose, chiefly a purpose coinciding with the aims and ends of government itself? A state has not the right to impose inequitable and unjust taxes, although it has the power, for the abuse of state power is contrary to our theory of government, is in every respect tyrannical, and is contrary to every rational conception of political justice. The state takes policy-holders' money, but returns no proper equivalent in additional protection, and it diminishes the security to policy-holders by placing in ultimate jeopardy the funds of the companies accumulated for the faithful discharge of contractual obligations.

Life Insurance is a Semi-Public Function.

Life insurance companies are semi-public institutions and they perform a semi-public function. By the long-established

system of state supervision, the states, in a large measure, have become the responsible guardians of these companies and of the vast interests represented by them in the form of trust funds and contractual obligations. For the state and the federal governments on the one hand to insist upon the most rigid economy in administration, absolute security in the investment of funds, and sound theory in the actuarial assumptions, and on the other to tax and to tax again the premium income, or the total income, or the net income, or the reserve, or the surplus, and, in addition to these, impose fees and charges for state supervision and agents' licenses, state or municipal, presents a curious contrast in public policy and the certainty of fundamental errors in public finance. For if the states and the federal government continue to tax and to take away a part of the income at an increasing rate, as has been the case during the last twenty years, the time must come when a further increase in the tax rate must imperil the very existence of the institutions. For the possible impairment of the contractual obligation, for the failure of the companies to meet the rightful expectations of the policy-holders, the responsibility will rest with the state and the federal governments and not with the administrative officers of the companies.

Need of Expert Knowledge of Insurance.

It is perhaps but natural that the law-makers should have but little expert knowledge on the subject of insurance, and that lawyers who have given much time and thought to the practical aspects of taxation should be ignorant of, or indifferent to, the rights of insurance policy-holders and the serious menace to their interests involved in excessive taxation. This point of view was very ably emphasized in an address by the late Mr. John A. Finch, one of the few members of the legal profession thoroughly familiar with insurance law, theory and practice, who said in part, as follows:

"There is no law book on our shelves that gives the faintest suggestion of the underlying principles of insurance, nor which

shows how the insurance companies are affected by legislation. The latest work on the law of insurance is the most ambitious, containing four large volumes now in press. I have read the advance sheets and while I commend the work, I can but note its deficiency in this respect. The average lawyer, as a legislator, is as ignorant of the subject of insurance—the principles underlying the business—as is the average legislator of any other vocation.

There is no business that can so readily protect itself from the results of hostile legislation or harsh interpretation of its contract as the business of insurance. If compelled to pay a heavy tax or deprived of making a defense to an unmerited claim, the remedy is, to the fire insurance company, by an increase in the premium charges; and, to the life insurance company, *by a diminution of the dividends to its policyholders.* If the statute law is such that a life company is made the subject of imposition of any kind, against which it is helpless to defend itself, its only remedy is by lessening the dividend. *The policyholder is the sufferer.*"

The Problem Re-Stated.

I have gone far enough into the technical side of the subject of life insurance taxation to emphasize its importance as a practical question confronting the companies and their policyholders at the present time. I have shown that over twelve million dollars per annum are paid out in taxes, fees, and licenses, equivalent to more than two per cent. of the premium income and one and three-quarters per cent. of the total income. I have further shown that the tax ratio has increased from 1.42 per cent. in 1890 to 2.15 per cent. of the premium income in 1909, and it may safely be predicted as a practical certainty that taxation will materially increase in the next two years unless the appeals of the companies and their policy-holders are heeded in rightful appreciation of the justice of their case. The Federal Corporation Tax, as far as it applies to life insurance companies, should be repealed at the next session of Congress, and the state legislatures throughout the country should be impressed with the justice and the morality of the suggestion of Mr. Dryden, that the tax be

reduced to one per cent. of the premium income in all the states where a higher rate of taxation is charged at the present time.

Official Suggestion for Increased Taxation.

The danger which confronts life insurance policy-holders is far more serious than generally assumed and for the future security of the funds and the absolute guarantee of contractual obligations are menaces. This could not possibly be better and more clearly indicated than in the very recent suggestion of the Insurance Commissioner of Texas,* that the states might rightfully impose a tax upon the assets of the companies equal to the general property tax, which would yield three and a half times the amount actually paid out by them for taxes, licenses and fees of all kinds at the present time. The amount of the taxes which could thus be raised from the life insurance companies is calculated by the Insurance Commissioner of Texas at over $37,000,000, or a sum equivalent to nearly sixty per cent. of the total amount paid in dividends to insurance policyholders during 1909. If this principle were, therefore, adopted, dividends to policyholders would practically cease and the rates for new insurance would, unquestionably have to be raised. The Insurance Commissioner of Texas attempts to sustain his plea for increased taxation by specious arguments drawn from general taxation experience, but he overlooks the fact that life insurance by its nature is totally different from other business enterprises and that it is not primarily conducted for gain. He overlooks the fact that insurance enormously advances public welfare and that it aids, more perhaps than any other factor in the accumulation of capital, by the aggregation of small amounts, most of which would otherwise be wasted and perhaps dissipated in useless or even harmful personal expenditures. Life insurance accumulations, in the words of Prof. F. A. Cleveland in his treatise on "Funds and Their Uses,"† increase the financial stability and security of the government itself, and, as he further observes,

*The Weekly Underwriter, Aug. 28, 1909, p. 145. †p. 297.

Life Insurance and the Public Welfare.

"The effect of the enormous risks undertaken by the insurance companies, therefore, is not only to relieve the business world of speculative uncertainty in the numerous relations to which it is applied, but also, by the financial conservatism adopted to secure this end, the investment companies assist very materially in steadying the market and, in time of strain, relieving financial distress."

A Final Plea for Tax Reduction and Uniform Laws.

It is, therefore, unquestionably contrary to public policy and opposed to a rational system of public finance that a heavy tax burden should be placed upon the companies and that the burden should be continually changed or shifted by an increase in the rates. However much advantage there may be in the lack of uniformity in state laws, there are certain interests which require uniformity and of these there is not one more important than insurance. If uniformity of state laws in the case of negotiable instruments has been considered a public necessity, sufficiently so to secure their almost general adoption, and if it is desirable to have uniform bills of lading, then it would certainly seem equally desirable that there should also be uniformity in the method of insurance taxation, and the fundamental principle which should govern is that the rate should not exceed one per cent of the premium income.

Conclusive Evidence of Overtaxation.

As was said at the outset, no other commercial interest carries a heavy burden like this and in the evidence referred to by Wm. J. Graham, proof is to be found that if the insurance tax rate upon the gross premium income were applied to commercial enterprises, the tax would be equivalent to confiscation. An illustration is given of a retail drug store paying $91 in taxes upon the gross income and which, if taxed at the insurance rate of two per cent., would pay $1,280. The case is cited of a retail grocery paying $70 in taxes upon the gross

income and which if taxed at the insurance rate of two per cent. would pay $1,239. The case of a retail drygoods store is cited, paying $640 in taxes upon the gross income, and which, if paying at the insurance rate of two per cent., would pay $6,840.* Other illustrations could be given, but only as accumulative evidence to prove that no commercial interest could bear the tax burden if it were imposed in a similar manner upon the gross income as an index of tax-paying capacity.

Urgent Need of Cooperation of Companies, Policyholders and Others.

The time has come for an agreement upon the principles which should govern in life insurance taxation and it is a hopeful sign that the International Tax Conference has for the third time included the subject in its program as a question of the day. What has been said has been rather by way of review of previous efforts to interest the public at large and to bring about an understanding of the essential facts of the problem and its economic and legal aspects to life insurance policyholders throughout the country. An annual tax burden of more than twelve millions is paid by them and by them only, and every addition to this burden is a hindrance to the growth of the business and the deliberate aim and effort on the part of the companies to reduce the cost of insurance. In ten years the business has increased 93.7 per cent, as measured by the premium income, while the tax burden has increased 87.1 per cent. during the same period of time. The end is not in sight, unless the policy-holders throughout the country take an active interest in the subject and enlist the cooperation of all who as economists, tax reformers, and statesmen, desire to help and not to hinder those who in their own way and at their own cost, through life insurance protection, carry successfully into effect the social and economic duty of *self-help*.

* The Romance of Life Insurance, by William J. Graham.

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CHAPTER VIII.

THE ENGLISH ASSURANCE COMPANIES ACT OF 1909.

The life insurance companies of England have been under government supervision since 1870, and with slight amendments passed in 1871 and 1872 the act has remained unchanged until the close of last year, when the Assurance Companies Act of 1909 went into effect on December 3d. An interesting historical account of the first act was published soon after its passage in the October issue of The Spectator for 1870, and in this article the origin of the act is attributed to the failure of the European and Albert insurance companies. The new act is in part the result of similar causes, for in 1906, after the disclosures of the New York legislative investigation and the subsequent failure of the Mutual Reserve, which had transacted a considerable amount of business in England, a special committee of the House of Lords was appointed "to inquire and report as to what steps should be taken, by deposit of funds or otherwise, to provide adequate security for British policy-holders in life insurance companies which have their chief office outside the United Kingdom, but which carry on business in this country." The report of that committee and the hearings which were had led to a serious consideration of necessary changes in the law of 1870, and accordingly the Government brought in a bill which, after some debate in both the House of Commons and the House of Lords, was passed just before the close of the session.

The new act is in many respects a decided innovation in British insurance legislation, since for the first time the supervisory powers of the Board of Trade are extended to fire and accident insurance companies. Employers' liability insurance

companies had been brought within the scope of the act of 1870 by an act passed in 1907. The whole law is now consolidated into a single act, which also includes bond investment business, which is defined as "the business of issuing bonds or endowment certificates by which the company, in return for subscriptions payable at periodical intervals of two months or less, contracts to pay the bond holder a sum at a future date, and not being life assurance business as hereinbefore defined." The act applies to all persons or companies not registered under the acts relating to friendly societies or trades unions which carry on in the United Kingdom life assurance, fire insurance, employers' liability insurance, and bond investment business. Every assurance company is required to deposit and keep on deposit with the Paymaster-General, for and on behalf of the Supreme Court, the sum of £20,000. The Paymaster-General is required to invest this amount in such securities as are usually accepted by the court for the investment of funds placed under its administration as the company may select. The interest earnings, of course, are payable to the company making the deposits. A company conducting more than one branch of insurance is required to make a separate deposit of £20,000 for each class of business transacted.

A distinction is made for the first time in English law between insurance and assurance, the former being considered to apply to all insurance business other than the life branch, which is defined as assurance separate and distinct from every other branch of the business. In this sense it is provided that "In the case of an assurance company transacting other business besides that of assurance or transacting more than one class of assurance business, a separate account shall be kept of all receipts in respect of the assurance business or of each class of assurance business, and the receipts in respect of the assurance business, or, in the case of a company carrying on more than one class of assurance business, of each class of business, shall be carried to and form a separate assurance

fund with an appropriate name." It is provided, however, that nothing in this section shall require the investments of any such fund to be kept separate from the investments of any other fund.

The practice of permitting every assurance company to make its report according to the financial year of the date of its own selection is continued. On this account the Board of Trade returns are never an exact statement of the insurance business in the United Kingdom for any given year, although the practice of making the business year end on December 31st is extending. It would have been a decided improvement in the law if all companies had been required to make their business years end, as is required of American companies, on December 31st.

The provisions which apply to accounts and balance sheets, actuarial reports, statements of assurance business, reports to shareholders, and audits of accounts do not require particular consideration. They conform in all essentials to those of the act of 1870.

Since most of the insurance companies are also subject to some of the clauses of the earlier Companies Consolidation Act of 1845, and the act of the same title of 1908, the new Assurance Companies Act does not repeat the requirements which apply with reference to the provisions of the acts just cited. Every assurance company, however, which has not registered under the companies acts, or which has not incorporated in its deed of settlement section 10 of the Companies Clauses Consolidation Act of 1845, is required to keep a Shareholders' Address Book, in accordance with the provisions of that section, and is further required, on the application of any shareholder or policyholder of the company to furnish him a copy of such book on payment of a sum not exceeding 6 pence, for every hundred words required to be copied. Provisions referring to the deed of settlement, to the publication of authorized, subscribed and paid-up capital, to amalgamation or transfer of business, and to special provisions as

to the winding up of assurance companies, are not of particular interest nor from long established custom and precedent in English insurance or corporation legislation. An important provision, however, is section 18, which empowers the court, in the case of an assurance company which has been proved to be unable to pay its debts, to reduce the amounts of the contracts of the company upon such terms and subject to such conditions as the court may think just, in place of liquidation.

The penalties for non-compliance with the various provisions of the act are limited to a sum not exceeding £100, or in the case of continuing default, to a sum not exceeding £50 for every day during which the default continues, and every director, manager or secretary, or other officer or agent of the company, who is knowingly a party to the default, is made liable to a like penalty, which, in continuance of such default shall be a ground on which the court may order the liquidation of the company in accordance with the Companies Consolidation Act of 1908.

The act does not apply to the National Debt Commissioners, or the Postmaster-General, acting under the authorities vested in them respectively by the Government Annuities Acts of 1829-88, and the Post Office Savings Bank Acts of 1861-1908. The act also does not apply to a member of Lloyds or to any other association of underwriters approved by the Board of Trade, which carries on assurance business of any class, provided that it complies with the requirements set forth in the eighth schedule of the act, which requires that "every underwriter shall deposit and keep deposited in such manner as the Board of Trade may direct a sum of two thousand pounds. . . . The sum so deposited shall, so long as any liability under any policy issued by the underwriter remains unsatisfied, be available solely to meet claims under such policies." It is further provided with reference to this class of business, that the underwriter shall furnish every year to the Board of Trade a statement in such form as may be prescribed by the Board showing

the extent and character of the life assurance business effected by him.

Passing over the provisions which apply to special classes of business, and the Parliamentary definitions of such classes, the most important section of the whole act is the 36th, which contains various provisions as to collecting societies and industrial assurance companies. By this section a large amount and a considerable proportion of industrial business, chiefly as transacted by collecting friendly societies, is legalized and raised to the status of a legitimate insurance business. The act provides in part that:

"No policy effected before the passing of this Act with a collecting society or industrial assurance company shall be deemed to be void by reason only that the person effecting the policy had not, at the time the policy was effected, an insurable interest in the life of the person assured, or that the name of the person interested, or for whose benefit or on whose account the policy was effected, was not inserted in the policy, or that the insurance was not one authorized by the Acts relating to friendly societies, if the policy was effected by or on account of a person who had at the time a bona fide expectation that he would incur expenses in connection with the death or funeral of the assured, and if the sum assured is not unreasonable for the purpose of covering those expenses, and any such policy shall enure for the benefit of the person for whose benefit it was effected or his assigns."

Most of the Parliamentary debate which was had upon the act had reference to this particular section, upon which there was evidently a strong division of opinion. The whole discussion of the act is contained in the debates of the House of Lords for July 30 and 31, August 31, and September 14; and the House of Commons for November 4, 24 and 25. Among others, Mr. Keir Hardie, the socialist, participated in this debate on several occasions, strongly recommending the Government to appoint a Royal Commission to make an inquiry into the whole subject of industrial insurance, previous to the passage of the act. This suggestion, however, was successfully opposed as needless by Mr. Winston Churchill,

the President of the Board of Trade, in immediate charge of the bill for the Government.

The act came into operation on July 1, 1910, except section 36, referring to friendly societies and industrial insurance companies, which came into operation on its passage. The act must be considered an incomplete piece of legislation, due partly to the hurried consideration which was given to many of its essential provisions during the closing sessions of Parliament. The act fails to give a clear definition of insurable interest as applicable to Ordinary life offices, the practice of which will remain subject to the antiquated statute known as the gambling act. The new act, however, meets the most pressing needs of the business of insurance, and extends to the Board of Trade all the desired powers for adequate supervision as occasion may require. The legislation is in conformity to English ideas of a minimum degree of paternalism and the largest amount of possible confidence in the integrity and ability of corporation management. Considering the long experience which has been had with the simple but decidedly effective provisions of the act of 1870, and the remarkably clean and satisfactory history of life insurance in England during the last forty years, the new act merely gives emphasis to provisions of law which have long been in operation and amends the law in the few directions in which it was found necessary. The act is in decided contrast to the enormous amount of statutory legislation on the subject of insurance in the United States and the conflict and confusion of law on the subject of insurance in all its branches, although in proportion to population the amount of business transacted and the corresponding liability incurred is probably greater in England than in the United States.

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CHAPTER IX.

THE LAW OF AVERAGE.*

There is a great fascination about numbers, which seems to defy the understanding. Figures positively affirm or deny every conception and condition, leaving little, if any, room for speculation or uncertainty. Vast aggregations expressed in figures appeal powerfully to the human imagination and rates, or ratios, in common use aid the understanding and direct the judgment, although often erroneous or misleading. On few subjects is there so little real general knowledge as on the science of numbers and yet its utility it so enormous that the world's work could not be carried on without it. The uncritical or unreasoning use of figures, however, is in truth a very serious menace to social and individual well-being, and few educational reforms are of more pressing importance than a better understanding of the nature of numbers, their philosophy, their value, and their limitations.

Lord Bacon comprehended a vast amount of sound reasoning in the prediction that men's power over nature would be increased a thousand-fold were they to interpret her with the humility of truth-seekers, casting aside all prepossessions.

* This discussion is not intended as a scientific outline of the mathematical, or even the statistical, theory of average. The object is to emphasize the importance of general statistical results as a basis for general conduct in the everyday affairs of life. Those who are interested in the more scientific aspects of the theory and utility of averages and means, should consult the treatise on Insurance by T. E. Young, the Primer of Statistics by W. P. and E. M. Elderton, Statistical Methods by C. B. Davenport, Theory of Mental and Social Measurements by Edward L. Thorndike, Elements of Statistics and An Elementary Manual of Statistics, by Arthur L. Bowley.

Facts, in other words, require to be substituted for misconceived theories arising out of prejudice, bias, or desire, and facts in the aggregate are represented by the science of numbers, In proportion as a basis of fact replaces guesswork opinion. certainty is substituted for uncertainty, and past experience permits of at least an approximately accurate forecast of the future. The appreciation of facts, their value, sequence, and relative significance, forms the scientific temperament and the function of science. The logical sequence of a given group of facts is the *law*, in the sense in which we speak of the laws of nature in contradistinction to the laws of men. Natural laws, rightly understood, are the only trustworthy guides for the human understanding, for they permit the forecasting of future events, and such forecasts are, of necessity, a most important function in the deliberate life.

The Value of Past Experience.

For we must, of necessity, assume that the future, to a considerable degree and extent, will resemble at least the immediate past, since otherwise all human effort would be nugatory and chaos would result. It is also in the nature of things, or a natural law, that the underlying causes are, as a rule, outside of our understanding, but the larger the basis of past experience, the more likely it is that, conclusions based upon such experience will be accurate. This law of nature is otherwise expressed as the law of large numbers, which, often provides a basis for predicting with approximate accuracy the probable occurrence of future events within the normal range of human knowledge and experience. No one, without a knowledge of the facts of past experience, can forecast the future state of trade, the growth of cities, the productive activity, or any other of the thousand and one problems which confront us in our daily life.

We use the term "probability" in a general way to express that which is reasonably certain to occur, and the natural law upon which this assumption rests is the law of probability.

The underlying basis of the law of probability, is, however, the law of average, which itself depends upon the law of large numbers. An average, as such, is simply an arithmetical conception, which in every-day use is often erroneously derived from numbers too small for a correct result. The use of the term average is also applied indiscriminately in many cases as a matter of pure assumption, in contrast to the scientific method of determining the average by calculation from a large number of units assembled into an aggregate. The use of the average in this sense has a very wide application in connection with the solution of a vast number of social and individual problems, since it serves as a standard or guide in the forming of our judgment, which must needs be applied impartially, be the result what it may.

The Meaning of "Average."

In the common use of the word average, we speak of an average weight, an average crop, an average height, an average summer, and finally, of the average man or the average life. Many of these expressions are extremely vague and but imperfectly understood, and it would be extremely quite for most men to clearly define what is meant by an average in the popular sense of the word. Clearly the value of the term depends upon the nature and numerical extent of the units from which it is derived. When based upon a few cases, which may individually vary widely, the resulting average may be decidedly erroneous. The personal idea of an average summer, or an average winter, may, for illustration, rest solely upon a mere matter of personal experience, and not upon carefully collected and critically analyzed meteorological observations extending over a long period of years. The expression "average man"may rest upon complete ignorance as to the most important anthropometric proportions, or the aggregate results of a sufficient number of individual lives, carefully observed for a period of years. The term "average life time" is often assumed to mean the individual expectation, or the number of years which *a* person may expect to live subsequent to a given year which has been

attained, while in fact the expression means the equal chance of a person to live or not to live a given period of years, which is, of course, a very different matter.

More accurate is the use of the average in mechanical employments, when an engineer speaks of the average pressure per square inch, or the average work which can be done by an engine per unit, or when the railroad engineer speaks of the average speed of a train, or the average load per car. These are all measurable quantities, readily within the understanding of the man who makes use of the term. Still more clear to the human mind is the use of the term in connection with matters of business and finance, when we speak of the average rate of interest earned by investments, or the average profit realized in bargains or sales, or the average rate of loss which must be assumed as an inherent condition of every legitimate business venture.

The Proper Use of "Average."

The most erroneous use of the average is when the term is employed to forecast individual occurrences, or to verify individual predictions of individual events, which, if realized at all under such conditions, would be a mere matter of true accident, or pure chance. It is, in fact, the very opposite of the function of the average to forecast any particular event, or the occurrence of any particular contingency. The proper use of the term is limited to the forecasting of normal events, in the order of normal frequency. While, for illustration, it is not at all difficult to forecast with reasonable accuracy the population of a country as a whole for a subsequent decade, or even much longer, provided no substantial change takes place in the essential circumstances which condition its life and growth, it is quite difficult to forecast, with even approximate accuracy, the growth of any particular community with a small population, or say less than twenty thousand. When cities or towns are of very considerable size, however, such as New York or Philadelphia, a forecast may be made of the population a decade hence, which in all probability will be closely verified by the actual

enumeration. The theory, of course, is based upon the average rate of increase during a previous period of sufficient length, say a decade, or quarter century, and it rests upon the assumption that the normal conditions as then prevailing and governing the rate of increase by an excess of births over deaths, and an excess of immigration over emigration, will continue as in the past. When important changes occur, the prediction, of course, comes to naught, but in large aggregates the changes would have to be very powerful indeed, or equivalent to a catastrophe or revolution, to produce a very substantial deviation from the rate of growth in former years. Even an earthquake such as affected the city of San Francisco, may not materially change the existing numbers of the population after a sufficient period of time has elapsed for a re-assembling of the former units and a return to normal conditions of life and growth.

In trade it is practically the same, and given a knowledge such as we have, say of the total amount of foreign imports during a period of years, it is with practical certainty that we can forecast, within reasonable limitations, the approximate amount of goods to be imported during a subsequent period of years. While this is true for trade in the aggregate, it would be very hazardous, however, to forecast the probable amount of imports of any given article, since groups of the units composing the aggregate are liable to a much greater rate of fluctuation than all of the units combined. Here again it is assumed, of necessity, that conditions governing the import trade will continue uninterruptedly in the future as they have in the past, since, for illustration, a radical change in the tariff, or even a seriously threatened changein the rates of duty upon the different articles, or goods, would tend to disturb, and possibly set at naught, all predictions, however conservatively arrived at.

Forecasting the Future.

Equally imported is the use of the average in forecasting the future number of foreign immigrants, which may be estimated with reasonable accuracy upon the basis of recent returns, with a

due consideration of the fluctuations in the rate, as observed in the past. Manifestly a fundamental distinction requires to be made between averages derived from gradually increasing aggregates, resulting from an increasing population on the one hand and an increasing productive national power on the other, and aggregates which conform to the rhythm of motion as ascending and descending curves, of which the rate of immigration is a very useful illustration. It is evident that great care is required in the use of averages derived from fluctuating aggregates and that predictions are less likely to conform to subsequent experience unless there is adequate knowledge and a clear understanding of all the facts which enter into the problem. Predictions as to the future number of immigrants depend, of course, primarily upon the assumption that there will be no radical change in existing national legislation, or, in other words, that no laws will be passed under which certain nationalities are, wholly, or in part, excluded from entry at our ports. An exclusion law, however, which would only affect certain nationalities which do not contribute numerically to any considerable extent to our present immigration, would practically leave predictions unchanged.

What has been said depends, of course, upon the scientific assumption that "the same set of causes is always accompanied by the same effect," or that "the future will be like our experience of the past, which is the sole condition under which we can predict what is about to happen, and so guide our conduct." These are the words of Karl Pearson, whose Grammar of Science should be the text-book for all who desire to replace guesswork opinion by a rational, independent and impartial method of thinking. For, as Pearson has well said, "in the struggle for existence man has won his dictatorship over other forms of life by his power of foreseeing the events which flow from antecedent causes—not only by his memory of past experience, but by his power of codifying natural law, that is, by his power of generalizing experiences in scientific statements." It is in this sense that we speak of natural laws which enable us to know

how phenomena take place, but do not explain the why or wherefore. With these the man of science has no concern, since they fall within the domain of the unknowable, or what is outside the scope of the human understanding. Men's minds are great or small in proportion as they possess the power of a broad generalization, by which they are enabled to arrive at a comprehensive grasp of the facts of past experience, upon which they can forecast with approximate accuracy the occurrence of future events.

The law of the individual life is one of inherent uncertainty, which results from the nature of things. It is a truism that every man is unlike every other, and this is equally so of the success which is attained in the various directions in which men exercise their abilities. If, however, all the units are grouped, there is a degree of average success which cannot be defined in numbers, but which is fairly well comprehended without them. The struggle of the individual, however, is rarely for an average success in commerce, industry, science, or art, but rather for exceptional success, or a decided deviation from the preponderating number out of which the average is derived.

Practical Uses of "Averages."

While there is a great deal of uniformity in any large number of events, be they what they may, whether it be the annual harvest of corn or wheat, the number of railway casualties to passengers, employees, or others, the number of letters sent through the mails, or the number of telegrams sent over the wires, the variation in the units which go to make up these masses is always very great, and the degree of variation is of as much practical importance as the average which is more conveniently recalled to memory. The average price of hay per ton throughout the United States during 1906 was $10.37, but the average price for the state of Minnesota was as low as $5.50. and for the state of Rhode Island as high as $17.40. Not quite as great was the variation in the average yield of hay per acre, which was 1.35 tons for the United States, but as low as 0.78 of a ton in Missouri, and as high as 4.0 tons

in Utah. For both of these items, however, the averages would vary considerably for different years, and while, for illustration, the average yield of hay per acre in Utah was 4.0 tons in 1906, it was as low as 2.45 tons in 1901. Evidently any forecast of the future must take into consideration the fluctuation in averages for small groups, which again go to make up the averages for large aggregates. We have to consider the elements of time and place the moment we make a more narrow application of the law of average to forecast the future for a more limited range of conditions or events.

For illustration, if any one were authorized to contract for the purchase of a large number of horses, let us say ten thousand, to supply an army, or meet the needs of a large corporation, it would be reasonable to take into consideration the average price for the United States, which during 1906, was $93.50. Since, however, the variation in the average price was between $41 in Arizona and $126 in South Carolina, the local market would have to be seriously considered to make the business venture a success. In examining the data of the subject it will be found that the largest number of horses was in the states of Illinois, Iowa, Kansas, and Texas, where the respective average prices were $109, $100, $89, and $62. If, however, the place where the horses were required was in the east, let us say New York, the local market price of $111 would probably be cheaper than the more remote and lower prices, which would be increased by the cost of long transportation. Even then, however, the average derived from very large numbers, or nearly twenty million horses throughout the country, would be fairly applicable to the problem and if the mode of greatest frequency of price were considered, it would be safe to contract to supply upon the estimated basis of about $100. The data, however, would be much more determining to the government, or the corporation, than to the contractor, who would be more free to make his choice and to enter into individual bargaining not subject to the law of average, provided the number of units to be supplied was of reasonable proportion.

The Element of Chance.

The man of business, in other words, must forecast the needs of the future from day to day and year to year, even if only a moderate degree of success is to result from his efforts. There is no reliance to be placed upon luck in life, or chance, in the sense as the terms are generally used, but there are exceptional occurrences, due to causes which are outside the operation of the law of average. Good luck and ill luck, or the equivalent of exceptional success or exceptional failure, are inherent in the nature of things the moment the few are considered which form the decided variations from the average or the mode which is a more scientific and better representation of the greatest frequency of normal occurrences. Those whose conduct is influenced by exceptional occurrences, or the mere accidental fulfillment of arbitrary predictions, overlook a thousand negative results by conforming their conduct to the one accidental fulfillment of a chance prediction.

The inclination to rely upon chance is partly in conformity to the well-known principle that negative events have a far less firm and persistent hold upon the mind than positive events, which explains the still persistent belief of those who believe in weather folklore and in local weather signs, and who would connect the advent of the seasons, or their degree of severity, with animals and birds, insects and plants, the sun, the moon, and the stars. It will usually be found that popular weather interpretations, or forecasts, are easily disproved by accurate observations extending over a period of years, but all evidence of this character notwithstanding, those who will not see and will not understand persist in their course of ill-reasoning and guess-work opinion. Conduct which is made to rest upon such a basis must prove disappointing in the large majority of cases. From this point of view also all proverbial philosophy is, as a rule, misleading, and more certain to cause disaster than to bring success. It is not claimed that any amount of accumulated experience will ever enable us to forecast the future with absolute accuracy or certainty, but, other things equal,

the man who has learned to conform his conduct to the law of average, and who has amplified his knowledge by a study of the degree of normal variation and frequency, is more certain of success in business life than the one whose conduct is made to rest upon belief in luck and good fortune and whose plans change with the weather and whose purposes change with the occurrence of events. While the liability to error in judgment is enormous in the consideration of individual instances or events, the liability is reduced to a minimum when judgment is based upon the law of average, or the degree of greatest frequency, as determined by large numbers, which eliminate the fluctuations due to accidental causes.

The Law of Variation.

Recalling that the science of averages is, in fact, the science of large numbers, the resulting function must of necessity represent a large degree of variety in the individual units which compose it. In fact, the average as such, may not exactly correspond to any one of the many individual units, or groups, from which it has been derived. Thus, for illustration, the average height of a group of say, one thousand men, may be five feet, eight and one-quarter inches, but few if any one of the many may be exactly of the degree of height representing the average. A few of the men in the group may be as small as dwarfs, while a few at the other extreme may be of the height of giants, but the preponderating majority will be found to be of, or about, the height centering around the average of five feet, eight and one-quarter inches. If upon this exact average a tailor were to furnish clothing for a group of men by suits of the average dimensions, including, of course, other factors which need not here be considered, the results would conform to the needs of only a small group and be of no value whatever to a considerable proportion who would deviate too decidedly from the average.

In other words, to overlook the degree of variation is as much an error as to base judgment exclusively on exceptional

cases. To arrive at an accurate result a tailor must consider the degree of variation in different groups and must ascertain the proportion of men of different degrees of height, which would produce a result almost in exact conformity to the needs of the group under consideration. The practical application of this theory we meet with in everyday life, in any store which supplies the needs, not so much of the true average type of man as of the preponderating number grouped about the average.

The reference to dwarfs and giants, as decided variations from the height of men in the mass, will serve as an illustration of exceptional success and exceptional failure in business or private life. It is a most serious error on the part of the periodical press to over-rate the value of exceptional success and to hold out exceptional types as ideals, to which average conduct should conform. It is utterly out of the question and in contradiction to the law of probability, that more than a small group of men can attain exceptional success, riches, power, or fame, for a large group are sure to fall below and prove decided failures. It is because of this error in judgment that so large a number of men over-rate their ability and their inherent power to attain to a degree of success far above the normal which pertains to the mass of mankind, and that the proportion of complete failures is so large, the evidence of which we find in the increasing number of suicides, criminals and insane. A rational understanding of the limitations under which human life in the mass can be carried on, is one of the most certain safe-guards to a sane and rational existence. In the nature of things this must be so, and in the nature of things it can never be otherwise, all of the speculations of political and social dreamers to the contrary notwithstanding. No more will there ever come a time when all men will be of the same height, or weight, or of the same degree of physical strength, than there will ever come a time when they will be of the same degree of mental, moral and emotional development. There will always be a mass in

which the units will fairly conform to one another, though each will be more or less slightly different from any of the rest, while there always will be a small group of persons of exceptional ability at the one extreme, and a greater group of men of exceptional inability at the other.

The Law of Large Numbers.

This is the law of average, the law of large numbers, the law of nature, which governs the life of men, and things, and events, and all that there is in the world, and all that there ever will be. If we had the measurements of all the stars in the heavens we would find them to conform to the law of average, grouping in dimensions around the mode of greatest frequency, with a curve tapering down on the one side to the smallest dimensions, and on the other ascending to the largest. If we could measure every animal, every plant, every leaf, even down to the size of every grain of corn, we would find the same conformity to the law of average, and the law of greatest frequency, and the law of variation, as we find it in the life of men. But for this salutary state of things, human existence would be chaos and human life, as we understand it, would be impossible. But for the law of average, or the law of large numbers, we could not forecast the future with any reasonable degree of accuracy, and without such a forecast all our efforts would be nugatory and all our aims and aspirations would come to naught.

Futility of Gambling and Speculation.

In clear contrast to the natural law of average, or normal frequency in the occurrence of events, stands the theory of pure chance, best illustrated in gambling, betting, lotteries, and stock exchange speculations. This difference was clearly perceived among the Romans who distinguished between *Fortuna* and *Fatum*, or fortune and fate, the former being acts outside of established laws, or occurrences of mere caprice, while the latter implies predetermined events in conformity to the

science of average. It would be unwise, of course, to ignore the enormous importance of matters of pure chance in daily life, or, as it has beautifully been expressed in the words, "O, Lord, on what a slender thread hang everlasting things!" The thread of the individual life may at any moment be broken by any one of a thousand chances, which are lost in the aggregate, but emphasize the true course of nature, "How careful of the type she seems, how careless of the single life." There, however, is no premeditation, or fate, in occurrences of chance, but they result from the nature of things, which it is the object of human knowledge, as far as possible, to foresee and set aside. It is the better part of wisdom to rely upon past experience and observed events establishing the law of frequency and recurrence, than to trust to chance, or luck, as determining factors in the affairs of life. The gambler lives in opposition to this theory of a rational adaptation to things as they are, and as they ever will be, if civilization is to endure and the progress of mankind is to continue. The gambler takes his chance with a practical certainty that he will lose his all in a desperate effort to gain the all of others, and he arrives at his conclusions by an ill-reasoned hope for the most improbable occurrence of a specific event. In gambling the chance of loss amounts to practically a certainty, partly because in the nature of things, the bank, or house, relies on the science of averages, while the individual gambler relies on the theory of probability, or pure chance. This is true of stock exchange speculation, in which millions are sunk by the many in the vain endeavor to secure large gains from the few who operate in conformity to the science of average and in opposition to the principle of pure chance which governs the individual speculator or investor. In other words, certainty of results is enormously in favor of those who practically take no chance whatever, while the risk of loss is out of all proportion to the probability of gain on the part of those who rely upon an accidental occurrence which may bring them exceptional results.

Theory of Probability.

The theory of probability has its scientific explanation and use, but it has no practical value to the individual in his efforts to forecast with certainty the occurrence of a specific event. The theory of probability lies at the root of the vast business of insurance in all its branches, and being derived from the science of average it meets the conditions of this business in the most admirable manner by equalizing losses and effecting a re-distribution of results. While it is impossible to forecast the probable duration of a single life, it is not at all difficult to predict with approximate certainty the average duration of a sufficient number of lives. Accuracy in the verification of scientific prediction increases with increasing numbers, so that, other things equal, the security is greatest where the number of units is largest. The more extensive the field of operations, the more certain it is that accidental variations from the normal will balance themselves, and that the general result will conform to the expected or predicted outcome. As civilization advances, however, and with the progress of sanitary and medical science, the tendency of the human death rate will be to decline and of longevity to increase, so that an ever larger proportion of those who are born may live to the highest attainable ages, from the biblical three score and ten to a possible maximum beyond the century mark.

Law of Average Applied to Problems of Mortality.

Largely because of an increasing familiarity with the law of average, as applied to problems of human mortality, modern science has been able to determine the underlying conditions destructive to health and life, which by degrees have been removed or mitigated until very substantial fluctuations in the death rate are becoming less and less frequent. It is to-day extremely improbable that there will ever again occur cholera epidemics such as brought desolation and sorrow to tens of thousands of homes in 1849, or yellow fever epidemics such as brought ruin and disaster to the south in 1878. Occur-

rences like these raised the death rate of New York to 46.7 per thousand, and of New Orleans to 48.9 per thousand, during the years mentioned, a deviation from the normal which has not been experienced since. A knowledge of the facts in question was first necessary before remedial measures could be taken and the lessons of life insurance experience and sanitary science, more, perhaps, than any other facts of human experience, emphasize the enormous value of a scientific study of the past and the rigid enforcement of rules of social conduct based upon past experience.

American mortality experience during recent years also emphasizes the truth of this conclusion. While the average mortality from all causes in the registration area was 16.3 per thousand during the five years ending with 1907, it was 15.4 per thousand during 1908. The lowest death rate during the period of six years was 15.4 per thousand, and the highest 16.7, which conforms closely to the average during the five years ending with 1907, and also to the rate prevailing during 1904 and 1908. A similar degree of regularity is to be observed in the mortality records of other countries with conditions similar to those met with in the United States. If the death rate is somewhat higher the degree of fluctuation is somewhat greater, and the degree of variation will probably be reduced as the rate is lowered by slow degrees as the result of sanitary and social progress.

What is true of the mortality from all causes is equally true of the mortality from principal causes, except diseases of an acute or infectious character, such as smallpox, la grippe, diphtheria, measles, etc. It is possible, upon the basis of large numbers, or the science of average, to predict with approximate certainty the proportion of male births to female births, which, for Massachusetts, for illustration, is in the ratio of 105 males to every 100 of females. It is possible to predict that, other things equal, the mortality of females will be below the mortality of males at all ages, and that a larger number of women will survive to old age than of men. It is possible to predict that the proportion of deaths from con-

sumption will be approximately 9.6 per cent. of the mortality from all causes, while the proportion of deaths from diseases of the heart will be 10.5 per cent., and of diseases of the nervous system 10.2 per cent. It is possible to predict that the rate at which suicides will occur among the population of large cities will be approximately two per ten thousand of population, and that in sixty-five of our large American cities during the present year approximately 3,000 suicides will occur. It is possible to forecast the number of coal mining accidents, which amount to about 2,400 per annum and occur at the rate of 3.4 per thousand of men employed in coal mining operations. It is possible to forecast the number of railway casualties to employees, which during 1910 will probably number 4,000, or occur at the rate of 2.5 per thousand of men employed. These illustrations could be multiplied and made to include practically every condition affecting the happiness and welfare of mankind, and in proportion as the value and significance of collective phenomena is duly appreciated, and as the lessons derived from the science of average are applied to the solution of social problems, will the social progress of mankind be rapid, or the reverse.

The Inductive Method of Reasoning.

"Man," said Lord Bacon, "being the servant and interpreter of nature, can do and understand so much, and so much only as he has observed in fact, or in thought, of the course of nature: beyond this he neither knows anything, nor can do anything." Evidently the course towards a right understanding of nature is to comprehend as clearly and vividly as possible the lesson taught by collective phenomena, rather than by exceptional occurrences, or exceptional results. It is better for the average man, or more accurately, the mass of mankind, to conform their conduct to the teachings of past experience, and thus forecast with approximate accuracy the future, than to place any considerable degree of hope or reliance upon pure chance, which is practically certain to bring disappointment,

disaster and ruin. I once more may quote Lord Bacon's words that "Such is the way of all superstition, whether in astrology, dreams, omens, divine judgments, or the like; wherein men having to deal in such vanities mark the events when they are fulfilled, but where they fail, although this happens much oftener, neglect and pass them by." Instead of being led by chance occurrences, the intelligent man should dispassionately consider the facts and circumstances and realize that the probability of a recurrence of exceptional events, or luck, or good fortune, is not at all likely to take place. In other words, it is our duty to make every effort to grasp clearly and vividly the facts of human experience, and apply, as far as practicable, the lessons of such experience to our own conduct and towards the solution of such problems as we may be called upon to consider. Only that can really be called an education which leads to a discipline of the mind and real mental exertion, to bring out the best that is in us, in place of a mediocre result far below the attainable average. Our judgment requires to be made to conform to observed experience in place of guesswork opinion, with a distinct inclination towards inquiry and mature reflection, in place of hasty and arbitrary action, which is merely a matter of caprice. When this rule of conduct is observed, we shall hear less of games of chance, of manias and speculations, for the inherent absurdity of reliance upon the most improbable of events, or combination of events, will be made clear to us. We shall no longer stultify our intelligence by the notion that a mania for gambling and speculation, or a betting upon uncertainties, is a trait inherent in the nature of men, and perhaps a commendable pastime, but we shall understand that such conceptions of conduct result from ignorance of natural laws which govern human life and human actions in the mass the same as the movements of the most distant stars. In brief, we shall find it more safe to rely upon the law of average, as expressed in results of past experience, or the inherent order and degree of frequency of things and events, and by doing so increase our personal security

against disaster on the one hand, and our peace, happiness, and prosperity on the other. The more perfect our knowledge in this respect, the more certain that our course in life, though perhaps less eventful and adventurous, will be more productive of good results to ourselves and to others, while throughout social and commercial life there will be increased stability, which, other things equal, furnishes the largest degree of happiness and well-being to the largest number.

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