Assurances

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Résumé de l'article

Nous avons reproduit dans le numéro d'avril 1963 de la Revue un copieux extrait du document officiel soumis à la Commission Porter par le surintendant des Assurances. Nous en extrayons un autre consacré aux placements des sociétés et, en particulier, à ceux qui prennent la forme d'actions. Nous avons pensé, en effet, qu'il serait intéressant pour nos lecteurs de prendre connaissance de la politique du gouvernement fédéral dans un des domaines les plus controversés. Ils y trouveront des précisions sur des directives que la province de Québec se propose de suivre, semble-t-il, pour la politique de placement de sa Caisse de retraite.

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Le contrôle des affaires d'assurances par le gouvernement fédéral

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INVESTMENTS AND DEPOSITS OF INSURANCE COMPANIES

"Although Federal insurance legislation, either in special Acts or in the general Acts, has from the beginning limited the investment powers of Canadian insurance companies and the various classes of assets that non-Canadian companies may vest in trust for their Canadian policyholders, there has been a constant endeavour over the years to make amendments from time to time to keep the investment provisions of the Acts up to date. In general, however, classes have not been extended or new classes added until investments are seasoned by experience or are otherwise obviously sound. As time went on, new kinds of investments that were considered to be sound came to be encountered more frequently but often they differed is some technical respect from the prescribed classes, thus rendering them ineligible. Companies transacting business out of Canada were particularly prone to encounter this kind of difficulty. As a result, frequent amendments to the Acts became necessary. Also, new kinds of investments were appearing that were very difficult to describe and deal with briefly in legislation.

"Basket" Clause

"A solution was found in the enactment of the so-called "basket" clause in 1948 whereby companies were empowered to make loans or investments not complying with the prescribed classes, up to 3% of *a company's ledger assets,* virtually within the company's own direction, subject only to the retention of a few basic limitations respecting mortgage loans, the maximum proportion of shares held, bonds in default, etc. The experience with this clause proved to be quite satisfactory and the maximum limit was raised in 1961 to 5% of a company's total assets. At the end of 1961, Canadian life insurance companies as a whole had $96,298,000 invested under this clause, subdivided as follows:

		% of Total Assets
Bonds	$33,518,000	.36 of 1%
Stocks	20,041,000	.22 of 1%
Real estate	42,739,000	.47 of 1%
Total	$96,298,000	1.05%

Actually, the aggregate investments made under this clause have been substantially in excess of the above total; many investments have become eligible within the regular classes subsequent to purchase and have been transferred thereto; some others have, of course, been sold. Since the free surplus of Canadian life insurance companies amounts on the average to a little more than 6% of their total assets, the 5% limit on loans and investments that may be made under this clause covers most of a company's surplus.

"In view of the existence of this clause since 1948, and the fact that the latitude thereunder is far from being exceeded, it is rather surprising to hear criticism voiced occasionally by certain segments of the public that the investment provisions of the Insurance Acts are too stringent; that, in particular, the 7-year dividend record for common stocks prevents insurance companies from purchasing many shares alleged to be desirable investments; that the companies are prevented from investing in new enterprise, etc. The fact is that the Acts do not seriously hamper companies in any of these respects. The companies in the main are free to purchase any bonds that are not in default or any shares of stock regardless of their dividend record, up to a total of 5% of their assets; at present the total amounts to little more than 1%, so criticism of the kind referred to can only be set down as uninformed.

Investment Trends

"Sometimes, public criticism is also heard to the effect that companies have not been sufficiently responsive to the national interest, especially in reference to investments in common stocks and the retention of control of Canadian industry in Canadian hands. The following table indicates in very brief form the trends in the investments of Canadian life insurance companies during the past thirty years:

Note: The percentages for common stocks held from 1930 to 1940 were affected greatly by the very large proportion of one company's assets in common stocks during that period. For example, in 1930 the proportion for that particular company was 50.5% while for all other companies it was only 1.6%.

Assets of Canadian Life Insurance Companies as at December 31

	1930 %	1935 %	1940 %	1945 %	1950 %	1955 %	1959 %	1960 %	1961 %
Government bonds	8.0	20.8	28.6	57.0	36.5	19.0	14.5	14.8	16.0
Local authority bonds	8.0	8.5	9.7	4.6	4.7	5.3	5.3	5.3	5.5
Other bonds and debentures	12.3	11.6	17.6	14.3	25.1	29.8	28.0	26.7	24.5
Preferred stocks	3.2	1.7	1.5	1.7	2.9	1.9	1.4	1.5	1.5
Common stocks	20.6	15.9	10.6	4.2	3.1	3.3	3.6	3.7	4.0
Mortgage loans	22.4	16.0	12.5	7.7	18.1	30.4	35.4	36.2	37.0
Agreements of sale	0.9	0.8	1.1	0.7	0.2	0.1	0.1	0.1	0.1
Real estate	3.1	4.0	3.0	1.1	1.2	2.5	3.3	3.3	3.2
Policy loans	15.2	14.5	10.0	5.1	4.5	4.8	4.9	5.0	4.9
Cash	1.2	2.1	2.2	1.1	1.0	1.0	0.8	0.8	1.0
Other assets	5.1	4.1	3.2	2.5	2.7	1.9	2.7	2.6	2.3
Totals	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

"As will be seen, the proportion in government bonds rose sharply during the last war to a high point of 57% at the end of 1945; this was completely in harmony with the national interest. After the war, the companies naturally tended to shift their funds more toward municipal bonds first, yielding a higher return, then toward corporation bonds and then toward real estate mortgages. The proportion in government bonds has declined to 16.0% but the proportion in mortgages has increased from 7.7% at the end of 1945 to 37.0% at the end of 1961 and this was clearly in harmony with public demand for more mortgage money.

Common Stocks

"It is true that the proportion in common stocks has remained relatively low at about 4% for many years and various comments have been heard in regard thereto from time to time. Some comments imply that the companies have not done their duty by not investing more heavily in stocks, even to the point of acquiring enough to keep control of various industries in Canada. But funds that have been lent on real estate mortgages or otherwise invested cannot be used to purchase stocks as well. If the companies had purchased more stocks, there would have been that much less available for mortgages and other forms of investment. Moreover, it has generally been regarded as against the public interest for large financial instructions to control other industries in the country and it is difficult not to think that there would have been very serious public criticism if Canadian life insurance companies had embarked upon that course. The main purpose of the T.N.E.C. investigation in the U.S.A. some years ago was to avoid anything of this nature. Another fundamental aspect is whether stocks of the right quality and investment yield are available in Canada in sufficient quantity to make any large scale investment therein possible even if it were otherwise desirable. The yields available on Canadian stocks at prices prevailing in recent years have been very low and it would seem that U.S. stocks have had greater attraction since the present proportion of 4.0% comprises 1.3% Canadian stocks, 2.0% U.S. and .7% other (mainly U.K.) stocks. Further, many life insurance companies do not feel that common stocks are a suitable investment medium for life insurance funds and one of the very largest U.S. life companies is strongly against the investment of any life funds in that way. Certainly, if a life company does invest heavily in common stocks, it exposes itself to the wide fluctuations of the market and if it should suffer embarrassment as a consequence, the criticism of policyholders would inevitably be loud, sharp and prolonged. It is impossible to satisfy all critics and the first duty of life companies is to their policyholders. Incidentally, it might properly be suggested that those life companies that are in the process of mutualization have made a very substantial investment toward retaining Canadian control of some very important companies.

"So far as the Department is concerned, the investment provisions of the Insurance Acts seem to be generally satisfactory, being sufficiently broad not to impede the flow of capital funds for almost all legitimate purposes and at the same time to afford ample scope for different investment policies, yet circumscribed by enough safeguards to keep investments generally within safe and proper bounds.

15% Limit on Common Stocks

"There is one provision, however, that continually seems to attract attention and that is the 15% limit on common stocks; sometimes also, the requirement that stocks must be taken at their market values for annual statement purposes, comes in for some criticism by the companies. As mentioned in the brief of the Canadian Life Insurance Officers Association, at the time of the last revision of the Acts in 1961 the companies recommended that the existing limit of 15% be raised to 25% of total assets and that stocks be valued at the average of the three most recent year-end market values, but the Department did not support either of these recommendations. In this connection, sometimes suggested or implied that if it were not for the existing 15% limit and market value basis of valuation, companies might invest more of their funds in common stocks.

"Perhaps it would be interesting to mention the origin of the present 15% limit.

"Prior to 1932, there was no limit in the Insurance Act on the proportion of its assets that an insurance company might invest in common stocks. However, in this report for 1928 the then Superintendent of Insurance recommended that there be considered a statutory limitation on the proportion of the assets of any company that might be so invested. The following is an extract from that report:

> "It has been the aim of life insurance legislation in this country, on the one hand, to protect, as far as possible, the policyholders and their beneficiaries from the financial shocks

which have in the past periodically occurred through decline or disturbance of industry, and on the other hand, to permit the remunerative investment of funds in order to ensure a low cost of insurance consistent with safety, and there must, of course, be a balance between these two objectives, a middle course which will help to avoid the disadvantages of either extreme. An undue restriction in investment would undoubtedly increase the cost of insurance, and the investment of a large proportion of the funds of any company in securities subject to the fluctuation in industrial activity might at some stage cause embarrassment to the company if not loss to the insuring public. The privilege of investment in common stocks may be used to stabilize interest rates in other securities and may yield a fortuitous profit; the exercise of that privilege to an undue extent may involve a hazard not contemplated in the framing of the investment legislation."

"The concern of the Superintendent at that time arose from the fact that one life insurance company then had about 50% of its assets in common stocks, although for all the rest of the companies as a whole the proportion was less than 2%. At that time, the Superintendent did not suggest what the limitation might be.

"In his report for 1930, the Superintendent recommended an amendment that would limit the investments of any company in common stocks to 25% of the book value of the total ledger assets of the company. No action was taken on this recommendation but when the Insurance Act was re-enacted in 1932 the Bill, as introduced, contained a proposed limit of 25%. However, during the progress of the Bill through Parliament, an amendment was made on the initiative of representatives of the life insurance companies by which the limit was reduced to 15%. The Bill was enacted in this form and the limit has remained unchanged since that time. Incidentally, it might here be mentioned that there has never been any limitation on the volume of preferred shares. When this whole matter was considered in 1932, the stock market crash of 1929 was fresh in mind and the company referred to above that had such a large proportion of its assets in common stocks was seriously embarrassed. No doubt the views of all concerned were coloured by these facts.

"The present limit is expressed in terms of the book value of common stocks and the book value of the total assets of the company. The book value of stocks is usually the purchase price. Thus if there has been a substantial rise in the market value of common stocks held by an insurance company, the ratio of the market value of common stocks to the market value of all of the assets may be substantially higher than the ratio on the basis of book values. At the end of 1961, taking all Canadian life insurance companies together, the ratio of the book value of common stocks to the book value of total assets was 4.0%; and for individual companies, the ratio ranged from 0.0% to 8.3%. On the basis of market values, the ratio for all companies combined was 7.5% and the range for individual companies was from 0.0% to 14.1%.

198 "Although it may appear inconsistent that the attitude of the companies and the Department concerning the limit on common stocks has been reversed since 1932, it can be seen from the above that, taken as a whole, the companies are not nearly up to the limit now permitted by the Act. In these circumstances, there appeared to the Department to be little case for raising the 15% limit at the present time. It would seem to be time enough to give consideration to any possible change when the companies have more nearly approached the existing limit and to do so then in the light of experience with a much larger proportion than has obtained for many years. If any upward revision of the limit were made now, it could hardly be interpreted otherwise than as a direct indication of government policy that companies should place a much larger proportion of their funds in common stocks regardless of their suitability, availability, etc. This, it would seem, would be misleading, improper and unwise.

"At the time of the amendments in 1961, the strongest representations for a higher limit were made on behalf of British life insurance companies; some of them had reached the 15% limit which, in their case, is of necessity based upon the market value of their total deposits. However, the Department could see no justification for raising the limit in these cases, having regard for the fact that non-Canadian companies are not required to maintain any surplus deposits over liabilities in Canada and 15% of deposits in common stocks already exposes the total market value of deposits to substantial fluctuations. Moreover, it must be remembered that this rule applies only to the deposits of non-Canadian companies for the protection of their policyholders in Canada; there is nothing to prevent such companies from investing as much as desired in common stocks or anything else if they wish to do so as head office investments. Further still, at a time when the question of retention of Canadian control of Canadian industries has been much to the fore, it would be difficult to justify a change in rules that would have the effect of permitting, or encouraging, non-Canadian insurance companies to use more of the funds collected from Canadian policyholders or derived from other sources in Canada to purchase Canadian stocks for non-Canadian ownership.

Valuation of Stocks

"With respect to the suggestion that the current market value basis of valuation inhibits companies from investing more in common stocks, the view of the Department is that the safety of the policyholders demands that investments in common stocks be realistically valued and in our opinion the most realistic values is the market value. Any other practice results in placing an artificial value on these assets and the dangers inherent in such practice seem to far outweigh the alleged advantages of encouraging greater investment in common stocks. It seems axiomatic that investment policy as respects common stocks should be closely related to a company's surplus position; a company in a relatively weaker surplus position ought not to risk as large a proportion of its funds in common stocks as a company in a strong surplus position. It would be unfortunate if weaker companies through the use of some arbitrary values were to invest in stocks more heavily than justified by their surplus position; on the other hand, companies in strong surplus position, with strong investment reserves, are much less likely to be seriously embarrassed by earmarking those reserves to the extent required to cover any market value deficiency. It is at least doubtful whether companies would invest any more heavily in common stocks even if the valuation method were changed; many companies obviously do not regard common stocks as suitable investments for any large proportion of their funds. Also, if a change in valuation method were to encourage some companies to purchase more stocks, it is by no means clear that Canadian stocks would be chosen. *The conclusion of the Department, therefore, is that the present valuation basis for stocks should be retained.*"