AUTOMOBILE PHYSICAL DAMAGE INSURANCE AFFILIATES
OF SALES FINANCE COMPANIES

DISSERTATION

Presented in Partial Fulfillment of the Requirements for
the Degree Doctor of Philosophy in the Graduate
School of the Ohio State University

By

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CHAPTER I

THE PURPOSES, METHODS, AND SCOPE OF THIS STUDY
OF THE SALES FINANCE COMPANY AUTOMOBILE
PHYSICAL DAMAGE INSURANCE AFFILIATES

Nature and Purpose of the Study

This research project was designed to study the automobile physical damage insurance affiliates of sales finance companies. The specific problem involved is the determination of the role played by the affiliates in the total insurance industry, with particular emphasis placed upon the outlook for this type of insurer in the future. The writer's purpose is to examine and compile information about a little-known and much-criticized class of automobile insurer, beginning with the initial entry of this type of company into the insurance industry and tracing its development to the present time. Major emphasis will be placed upon an explanation of the form of these companies, their methods of doing business and their operating results, their historical development, their relative importance to the insurance industry over the years, and the outlook for this type of insurer in the future.

Consideration will be given to the development of these insurers in terms of how and why they first developed--
their purpose of organization. What conditions existed at the time of their organization to facilitate their development?

A comparison will be drawn between past and present conditions to determine whether or not the companies are filling a current need and are now as important to the American public as they were in the past.

The author then proposes to forecast the future of these insurers by examining trends in their significance as a segment of the insurance industry offering service to the public. Conclusions will be drawn from indicia of the past and present. Specifically, the following will be examined:

1) Market penetration. What share of the physical damage automobile insurance market on financed automobiles is controlled by the affiliates?
2) Services offered to the public
3) Volatility of the market available to this type of insurer
4) Methods of distribution used
5) Rates charged the public; companies' loss experience and their cost of doing business; resultant profit or loss from underwriting
6) Competition
7) Governmental regulation
The finance affiliates have been subjected to more public scrutiny during the past five years than at any other time of their existence. An objective study of these companies is particularly timely to properly evaluate the criticism levied against this class of insurer. The information contained herein will be of value to those readers who wish to gain more of an understanding of the modus operandi of the finance affiliate and of its niche in the insurance business. In addition, the results of this study may serve as a foundation for subsequent research.

Definitions

Automobile Physical Damage Insurance

Automobile insurance falls into two major classifications: (1) casualty coverages and (2) physical damage coverages. The casualty coverages are bodily injury liability, property damage liability, and medical payments coverage. The physical damage insurance coverages are fire, theft, comprehensive, and collision.

The study is limited to a special type of insurer writing automobile physical damage coverages—forms of automobile insurance that protect the insured from loss or damage
to his automobile. Although the interest involved is primarily that of the automobile owner, others may have an incidental interest, such as that of one who has a lien against the vehicle. Thus, it will be seen later in this study that a financial institution or individual that finances the automobile may also have an insurable interest.

A party afforded physical damage insurance protection will be reimbursed for direct and accidental loss of or damage to the insured automobile caused by the perils insured against. Collision insurance covers the perils of collision with another object or by upset. Comprehensive coverage is an all-risk insurance, collision excepted. The fire and theft coverages are limited to a few named perils.

Sales Finance Companies

The term "finance company" is a designation which has in common usage included a number of financial institutions—small loan companies, industrial loan companies, accounts receivable financing companies, and sales finance companies.

The sales finance companies engage primarily in buying from dealers consumer instalment contracts and in providing financing for these dealers. They perform two different basic activities: (1) the purchase from retail merchants of retail
paper (the promissory notes signed by consumer buyers) and the collection of the instalment payments due thereon, and (2) the provision of floor planning for retail dealers (the financing of wholesale purchases by dealers from manufacturers).

Some sales finance companies do a significant volume of small loan business, making direct loans to consumers who can then pay cash for merchandise purchased from dealers. Some institutions which are characterized as being small loan companies do a large volume of sales finance business.

This study is primarily concerned with the insurance operation which attends the sales finance activities. With this in mind, the writer takes the liberty of including in the category of "sales finance companies" not only those companies engaged primarily in buying consumer instalment contracts, but also several companies, which, although engaged primarily in making small loans, do a significant amount of business characterized as sales finance business.

An example of this type of company is the Seaboard Finance Company. Although engaged primarily in the small loan business, it does a substantial amount of sales finance business. It is in connection with this latter aspect of the company's operation that this study pertains. Thus, a sales
finance company, as defined herein, shall include a company primarily engaged or substantially engaged in the sales finance business.

Affiliates

The word "affiliates" is subject to either broad or narrow definition. It is sometimes used to designate the affiliation of a subsidiary company with its parent organization. The parent exercises direct control over the subsidiary's operations.

The definition has been expanded to include the relationship existing between the subsidiaries of a parent company. Although the connection is not direct, the business cooperation between the two subsidiaries is no less effective than that of a parent company and its subsidiary.

Another type of affiliation is that existing between two or more companies, which, although no affiliated company owns stock of another, nevertheless, share the same quarters, facilities, and personnel. Sometimes the board members are identical. Here, too, the relationship is of such a nature as to effect the same business cooperation that is accomplished in the other types of affiliations which have been discussed. This cooperation is the business arrangement between a sales
finance company and an insurance company whereby the former uses the latter exclusively, or almost exclusively, to insure its collateral, the financed automobile.

The definition of affiliates as contemplated in this study shall mean all three types of relationships where there is obvious or apparent business cooperation and dependence existing between the companies, irrespective of stock ownership or direct legal connection.

Examples of types of affiliates. An example of direct affiliation through stock ownership of a subsidiary by the parent company is afforded by the Emmco Insurance Company. All of the stock of this company, except directors' qualifying shares, is owned by the Associates Investment Company, a sales finance company incorporated under the laws of the State of Indiana.

The second type of affiliation, that of affiliation of two subsidiaries of the same parent, is exemplified by the relationship existing between Service Fire Insurance Company of New York and Universal CIT, an automobile sales finance company. The common parent, CIT Financial Corporation, is a commercial banking enterprise. The business of Service Fire Insurance Company of New York is directly related to the business
financed by Universal CIT, the sales finance company. All of the business volume of the insurance company is insurance written on automobiles financed by the affiliated sales finance company. Of the automobiles financed by the sales finance company, Service Fire Insurance Company insures 60 per cent of the new automobiles and 50 per cent of the used automobiles. There is no relationship between the business of the parent organization and the insurance subsidiary.

The third type of affiliation is illustrated by the Government Employees Insurance Company of Washington, D. C. Financial control of this company was in the Graham-Newman Corporation of New York until 1949. In July of that year the company distributed its holdings of the insurance company stock to the stockholders of Graham-Newman Corporation. The Government Employees Corporation was incorporated concurrently. Engaged in the automobile finance business, Government Employees Corporation shares the same quarters, facilities, and personnel with the Government Employees Insurance Company. Neither of the affiliated companies owns stock of the other. Board members, however, are identical. Whereas the typical affiliate was organized to provide insurance service to its affiliated sales finance company, the Government Employees Corporation was organized to provide automobile finance facilities for the policyholders of Government Employees
Insurance Company. Approximately 90 per cent of the borrowers of the finance company carry their automobile coverages with the insurance company, and 83 per cent of the borrowers are already policyholders of the Government Employees Insurance Company.

Methodology

Research Method

The research method employed both primary and secondary sources of information. The writer interviewed executives of seven of the finance affiliates. Semi-directed interviews were used by the author with top and intermediate management executives of companies situated in Baltimore, New York, South Bend, Indiana, and Columbus, Ohio. The interviews ranged in length from five and one-half to seven hours with each company, and from thirty minutes to six hours per executive interviewed. Published statistical data, informational brochures, and other similarly-prepared data were furnished by the companies.

Material was gathered from state regulatory authorities, insurance rating bureaus, and from insurance associations. The National Association of Better Business Bureaus furnished information. Use was made of the proceedings of five days of
hearings before the United States Senate Subcommittee of
the Committee on Interstate and Foreign Commerce dealing
with the practice of some insurance companies, including
several finance affiliates, in the misclassification of
insureds in the writing of automobile physical damage insur-
ance.

Extensive use was made of library material, with par-

ticular reliance on insurance reporting services, financial
reports, and periodicals.

Material obtained from the foregoing sources was
further augmented by a large amount of personal correspondence with the various primary sources of information cited.

The Sample

The sample includes the majority of the finance affiliates, both in respect to numbers and to volume of insurance written. Since the definition of affiliates used in this study includes both formal and informal affiliations, the author does not purport to have included all companies in his study which might fit into the affiliate category. The sample selected, however, encompasses most of the companies which can properly be included under this definition, and the com-
panies which have been included are highly representative,
since, of the forty companies selected, eight of them write 80 per cent of the volume of this class of insurer.

The Approach

Recognizing that the subject of this study has in the past been highly controversial, the author has attempted to present an exposition of the subject and an expression of his opinions and conclusions from an unbiased viewpoint, presenting the tenets advanced by both the proponents and the antagonists of this class of insurer, and then concluding with the author's opinion. No attempt shall be made to justify or to censurate the existence of the finance affiliate except in light of the facts presented.

The finance affiliate has been presented as a distinct class of insurer, which in some cases is more academic than real, doing business within one segment of insurance buyers, namely, those purchasing automobile physical damage insurance. The analysis undertaken by the writer presents a comparison of the finance affiliate with other classes of insurers writing the same type of insurance business. This comparison embraces operating principles, practices, procedures, and results.

Approaching the analysis from the viewpoint of the insurance consumer, the writer judges the relative efficiency,
cost, and services of the finance affiliates and competing insurers. He then arrives at his conclusions regarding the justification for the existence of this type of insurer in terms of service rendered to the public.

The Limitations of the Study

The subject of the automobile physical damage insurance affiliates of sales finance companies is extremely broad and full of complex ramifications. It was necessary to delimit the problem so that the report would be of practical benefit to those reviewing it. Because of wide variances existing between companies, the individual differences have been noted briefly; however, the analysis and conclusions have been largely based upon analyses of the few large companies which do the vast bulk of the business written. To this extent, therefore, the study is oriented to the large companies.

A further limitation of the study is that it presents a broad, cross-section analysis of the finance affiliate as a class of insurer without attempting to present a detailed analysis of the companies presented. There are many individual differences present among the companies.

The data used have been limited to that available in accurate detail and sufficient quantity for a reasonable and
practical amount of comparative analysis. In most cases analysis and comparison is based upon 1957 data because of the lack of more recent statistical material available from the classes of insurers used for comparison but which are not the specific subject of this study. The writer believes, however, that this is not a defect, since the relative position of the finance affiliate in the automobile physical damage insurance industry has not changed appreciably in the past year.

Notwithstanding the foregoing discussion, the limitations confronted by the study have not been too serious because of the willing and complete cooperation given the writer by the companies visited.
CHAPTER II

A HISTORICAL BACKGROUND

The end of the nineteenth century ushered in a new invention which would in a few years create the nation's number one industry. This invention was the automobile. Its early development came during an era of engineering miracles in the United States. The country had during the preceding decades launched its industrial revolution. This revolution would bring about sweeping economic and sociological changes and would give this nation the world's highest standard of living. The automobile was to play an important role in effecting these changes.

The automobile, a complicated mechanical contrivance, presented a myriad of business problems. Manufacturing difficulties were many. Its production necessitated the expenditure of a great amount of time and money. This, in turn, brought about the necessity for methods of financing the new product. Where financing facilities were lacking, new institutions sprang up to provide the required services.

As public awareness of the new product grew, channels of distribution were established, and finance facilities were extended to the consumer as well as to the manufacturer.
Soon it became apparent that here was a form of personal property which was subject to a number of perils because of its value, mobility, and destructibility. New insurance coverages evolved.

This chapter briefly introduces the early history of the automobile and shows the economic conditions which created the sales finance companies and the automobile physical damage insurance affiliates of the sales finance companies.

The Automobile

Invention and Early History

The automobile is popularly regarded as a comparatively recent invention, usually associated with the turn of the twentieth century. To many people, the word automobile has come to be synonymous with the era of Henry Ford. The automobile, however, dates back much further than this.

Early in the eighteenth century reference is made by both French and English writers to various attempts to construct a road vehicle propelled by steam generated in a boiler carried within the vehicle. Credit for the first "road wagon" propelled by its own engine is generally given to a Frenchman, Nicholas
Joseph Cugnot, who in 1769 completed and successfully operated a self-propelled steam wagon.¹

During the latter half of the eighteenth century a few other attempts were made to build steam carriages, many of which were incapable of operating under their own power. The next century, however, saw a number of steam vehicles put to practical use in transporting passengers, particularly in England.

The success of these early vehicles, however, was short-lived. About 1831 the English parliament enacted laws which practically eliminated the steam coaches from the roads. An example was the Red Flag law which required that a man precede the horseless carriage, carrying a red flag by day and a red lantern by night. In addition, the toll roads and bridges raised the charges for the steam carriages until they could no longer operate at a profit. They were extremely heavy, cumbersome vehicles, occupying a large portion of the roadway, blocking it en-

tirely whenever they attempted to turn around, and no doubt made a great deal of noise.²

Thus, it was public prejudice rather than a want of engineering skill which caused the slow development of the automobile, in England at least.

Meanwhile, in Germany and France interest turned toward the internal-combustion engine to replace the cumbersome power plant of the early steam vehicles. As early as 1875 Siegfried Marcus of Austria had built a four-wheeled vehicle powered by an internal-combustion engine. Karl Benz of Germany produced a tricycle with an internal-combustion engine in 1885. The general credit for revolutionizing automobile transportation, however, goes to Gottlieb Daimler of Germany, who in 1886 patented his high-speed internal-combustion engine. With the creation of the internal combustion gas engine, new interest was aroused and automobile development started up with considerable activity, particularly in France where the earlier stages of its development took place.

The motor car is not the product of a single inventor, nor of men of one country, nor even of men within a single century. Many countries had a hand in its development, and the

contribution of the United States, although generally at a later date than that of other countries, was monumental.

The Automobile in the United States

Automobile construction was not successfully undertaken in this country until about 1891 or 1892 when Charles E. and J. Frank Duryea, American bicycle makers, began construction of a four-wheeled vehicle. This vehicle was completed in 1893, and besides being practical, embodied many of the principles now retained in the construction of gasoline-driven automobiles. Several other men brought out their initial efforts at approximately the same time. In the next six years automobile construction was undertaken by automobile manufacturing pioneers, Maxwell, Dodge, Ford, Nash, and Studebaker. All over the nation operators of machine shops, bicycle makers, and carriage manufacturers attempted to perfect some sort of self-propelling vehicle.³

A risky business. By 1899 there were 57 establishments reported as manufacturing automobiles, bodies, and parts. A new industry was born. It was an industry characterized by high risk.

The difficulties confronted by the early automobile manufacturers were tremendous. The automobile was an untried product; it was a new and radical invention. It was characterized by a comparatively high original cost and a high cost of maintenance. Automobiles were always breaking down; they were unreliable, uncomfortable, and costly to operate. Repairs were expensive and difficult to make. Popular opinion in the early years of manufacturing of automobiles characterized the automobile as an expensive passing fad; it was associated with sporting rather than as a means of transportation.

By 1904 the number of manufacturing establishments had increased to 178 with 103 proprietors and firm members and a total of

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tal of 13,333 persons employed in the automobile industry. By 1909 there were 743 establishments with 405 proprietors and firm members and a total of 85,359 persons employed in the industry. Value of product increased from $4,748 in 1899 to $249,202 in 1909.\footnote{Department of Commerce, \textit{loc. cit.}}

The first years of this industry saw many failures. Of the companies which survived, many owe their survival to the fact that they did not depend upon automobile manufacturing for income. More than half of the several hundred firms manufacturing automobiles in the United States in 1912 conducted this enterprise in connection with, or in addition to, some other line of manufacturing.\footnote{Dunlop, \textit{loc. cit.}} Between forty and fifty new makes of automobiles appeared each year during the early years of the century. Of the 181 automobile producers studied by one writer during the period, 1903-1926, a total of 137 had retired from the field by 1926. The average (median) length of life for all 181 companies was seven years.\footnote{Ralph C. Epstein, \textit{The Automobile Industry} (Chicago: A. W. Shaw, 1928), pp. 162-164.}
**Financing the Automobile**

As the automobile manufacturing industry assumed greater proportions, more and more money was needed to finance the expanding industry. Manufacturers sought after sources of funds. As public awareness of the new product grew, channels of distribution were established. Dealers were set up. They desired financing. The great American institution of credit buying was in its infancy. Consumers wanted automobiles, and instalment purchasing required consumer credit.

Thus, there were three groups which were concerned with the financing of automobiles—the automobile manufacturers themselves, the dealers, and the American public. The sales finance companies and their insurance affiliates were a natural outgrowth of the demand generated by these three groups.

**Financing the Automobile Manufacturer**

Commercial banks and investment bankers constituted the only important source of funds for the possible financing of the new industry. Neither of these sources was interested in furnishing the early automobile manufacturing companies with the necessary capital, and it was not easy to find many independent
capitalists or financiers who were willing to provide the required funds.10

There were many reasons why the commercial banks did not wish to finance the manufacture of automobiles. The industry was still in its infancy. The product was still in the experimental stage. The commercial bank, historically conservative, did not wish to enter such a highly speculative area of financing.11

In the first quarter of the present century banks did not have to look for new areas of financing. There was adequate employment of their funds available in orthodox lending to enterprisers engaged in agriculture, established forms of manufacturing, and commerce.

Financing the Automobile Dealers

The automobile manufacturers were not in a position to finance dealers, and the retailers were unable to finance the


increasing number of consumers who wished to purchase automobiles on long credit terms. Unlike other consumer goods, such as food or other lines of nondurable goods, the retailer needed large financial resources to sell on credit. Most prospective consumers could not pay cash or could not pay in thirty days or so, yet prospective automobile consumers wanted the new product, and they wanted credit terms. The dealer in the vast majority of cases lacked the resources to do the necessary financing.12

Most of the men available for "franchises" were small merchants—bicycle dealers or repair men, hardware dealers, locksmiths, or electricians. They were the logical persons to handle motor cars in their communities, for few others could arrange readily to give the mechanical service the consumer required. Thus with few exceptions the retailer of automobiles was possessed of few assets.13

Unable to obtain financing from the manufacturer, the dealers approached the banks but found that conservative commercial banks did not wish to finance this type of credit risk.

12Ibid.
13Epstein, op. cit., p. 140.
Financing the Automobile Consumer

Since the manufacturer and the dealer were unable to provide financing facilities for the consumer, he paid strictly in cash.\(^{14}\) The purchase of an automobile by the consumer required a considerable outlay of cash; therefore, during the first part of the century the automobile was a rich man's toy. In 1900 the average wholesale value of a passenger automobile was $1,225; in 1910 it was $1,190; and in 1920 it was $950.\(^{15}\) In 1909, it required three years' average factory pay (at $512.00 per year) to buy a medium-priced automobile.\(^{16}\) It is apparent that the average American could not provide the cash to purchase an automobile.

Before 1930, the commercial banks looked askance at the business of lending to individuals for consumption expenditures.\(^{17}\)

\(^{14}\)Kent, op. cit., p. 653.


For years bank loans that were not for "productive" or "commercial" purposes were frowned upon, and it was not considered wise for commercial banks to loan to consumers for household or luxury purposes.

In the mid-twenties, the attitude of the National Association of Credit Men was reported to be in general that "instalment sales are clearly justified in the case of producers' goods but are indefensible when applied to consumers' goods."18

In the pre-World War I period, lending to consumers was almost entirely handled by pawnbrokers and unlicensed lenders or loan sharks. No self-respecting banker wanted to be associated in the public mind with those who lent to consumers and whose operations he regarded as a petty lending business transacted at usurious rates which sometimes approximated 120 to 240 per cent or more per annum.

There was a strong prejudice against the use of credit by consumers, especially instalment credit, and particularly for the purchase of what were regarded as luxuries, like automobiles. The use of credit, and particularly consumer instalment credit, was characterized by the commercial bankers as

tending to break down credit morale. It was attacked as
tending to "weaken the moral fiber of the Nation," and as
dangerous to the economy of the United States.

There were other reasons why commercial banks did not
wish to finance automobile consumers. The new financing service
called for retailing credit in small amounts in contrast to the
profitable business of wholesaling large amounts of credit. It
necessitated the making of long-term advances of as much as a
year in contrast to making loans for 30, 60, or 90 days. Banks
did not care to set up special credit and collection departments
to check losses, make repossessions, and in general, do the exten-
sive and systematic work necessary to enforce instalment terms.

In addition, the paper represented by the instalment notes of the

19 James E. Moffat, "Is Instalment Selling a Boon or a
Menace?" Bankers Magazine (February, 1926), pp. 224-225.

20 Dunbar, loc. cit.

21 Knauth, loc. cit.

22 Ellis E. Inskeep, "Financing Automobile Sales," Credit
consumers "was essentially lacking in the element of liquidity which the banks were accustomed to demand."\textsuperscript{23}

\section*{The Demand for Automobile Financing}

As long as automobiles were purchased only by the wealthy, as long as production was devoted to satisfying only the needs and the desires of the few, no real financial problem was involved. The wealthy consumer paid cash to the automobile retailer who was thereby enabled to pay cash to the automobile manufacturer. The results were apparent. The practice of selling only for cash resulted in restricted production for the few, high prices of automobiles, and because of restricted production, limited employment in the automobile industry. These results did not come about. In 1952 one out of every seven workers in this country was employed in the highway transport industries, which embrace the manufacture of motor vehicles, parts, tires, petroleum refining, automobile sales and service, road construction, and truck and bus operation. One out of every six sales and service firms in the na-\textsuperscript{23}E. R. A. Seligman, \textit{The Economics of Instalment Selling} (New York: Harper and Brothers, 1927), vol. I, p. 31.
tion were automotive, and one out of every five retail sales dollars was spent for automotive sales and service.24

The masses were to be served. From all parties to the automobile sales transaction--manufacturers, dealers, and consumers--there came a demand for machinery which would render possible a greater volume of transactions by providing the necessary financing. The solution was found in the creation of the sales finance companies.25

The Sales Finance Companies

Development of the Sales Finance Company Concept

The earliest of the automobile sales finance companies were not organized for the purpose of transacting that business. Most of the early companies were concerned with buying accounts receivable. These were not retail accounts, but the accounts


25 Seligman, op. cit., p. 33.
owing to manufacturers and wholesalers by a wide variety of retail merchants. 26

The first of these companies can be traced to Chicago. In 1904 Arthur R. Jones and John L. Little saw the need for organizing a financing institution which would provide additional working capital to businesses by purchasing their accounts receivable. The following year they incorporated the Mercantile Credit Company.

The Bankers Commercial Corporation, originally named the Fidelity Contract Corporation, was also organized in 1904. Its purpose was to discount retail piano paper.

In 1908 Henry Ittleson formed the Commercial Credit and Investment Company to finance manufacturers and jobbers by buying their open accounts on the non-notification plan and purchasing their drafts and notes receivable. 27 This company later became the C.I.T. Financial Corporation. The National Trust and Credit Company, organized by John L. Little and Melville N. Rothschild, was also formed in 1908. Reorgan-


ized in 1914 as the National Bond and Investment Company, it became an important factor in financing automobile paper.

Commercial Credit Company was incorporated in 1912, followed by the Associates Investment Company in 1918 and the General Motors Acceptance Corporation in 1919.

Although the early companies originally were organized to finance accounts receivable, they were soon induced by automobile dealers to buy a few retail instalment contracts. Annual production of automobiles had grown from 4,192 passenger vehicles in 1900 to 181,000 in 1910. By 1914 annual production had increased to 548,139 passenger vehicles. The accounts receivable finance companies continued to buy more and more automobile paper from dealers as automobile production volume soared, and some of these companies found themselves almost exclusively in the retail automobile financing business. The transition was so gradual that the companies themselves do not know exactly when they came to be engaged mainly in the business of what is now called a sales finance


company instead of in the business of purchasing accounts receivable.\textsuperscript{30}

By 1917, perhaps forty concerns were in operation as sales finance companies.\textsuperscript{31} The years immediately following marked a fantastic increase in the number of companies, and the years from 1921 to 1925 may be called the boom period in the organization and expansion of sales finance companies. The number of finance companies dealing with automobile paper had reached about 1,000 in 1922. The number increased to 1,600 or 1,700 by 1925.\textsuperscript{32} Total volume of sales finance business in 1926 amounted to approximately 3.9 billion dollars. Automobile paper accounted for 69 per cent of the total.\textsuperscript{33}

\textsuperscript{30} Ayres, loc. cit.

\textsuperscript{31} "Instalment Finance," The Index (April 1, 1937), p. 39.

\textsuperscript{32} Seligman, op. cit., vol. I, pp. 48-49.

Until approximately the year 1933, the sales finance companies purchased almost all the paper arising from installment sales other than that financed directly by retail merchants.

Development of Competition

By the mid-thirties the commercial banks as well as the industrial banks began to show great interest in the direct purchase of installment paper. As indicated in the last section, some financing was also done by the retailers, automobile dealers.

The commercial banks. When the Great Depression struck the country, the commercial banks discovered that the orthodox banking business which had historically provided safety and liquidity was the hardest hit. The inadequate demand for their regular commercial loans, the unexpectedly low rate of losses on installment paper and the excellent record of earnings of the sales finance companies caused the commercial banks to begin offering services of financing installment dealers, buying installment notes of consumers, and making in-
stalment loans to consumers.\textsuperscript{34} Even during this period, however, banks were selective and cautious in entering this field of financing.

Today, as in the past, the commercial bank still operates under a more conservative policy of financing than that of the sales finance companies. Whereas the finance company is more free in its policy of lending, because its funds are its own, the banks' philosophy is expressed as follows:

\begin{quote}
It is well to remember that as bankers we have more depositors than borrowers, and that the depositor should be protected . . . Ninety-two per cent of the funds we administer are not our funds, which makes it all the more important to administer them wisely and conservatively.\textsuperscript{35}
\end{quote}

In 1958 total instalment credit in the United States amounted to $33,865,000,000. Of this amount, automobile paper represented a total of $14,131,000,000. The sales finance company held $6,404,000,000 of this latter figure, which represents the largest segment of total automobile paper held by any instalment credit holder. The second largest holders of automobile paper in 1958 were the commercial banks, with purchased


\textsuperscript{35}Chester A. Rude, "News for Instalment Credit Men," \textit{Banking} (April, 1953), p. 93.
automobile paper holdings of $2,191,000,000, making a total of automobile paper holdings of $6,129,000,000. Table 1 indicates the automobile paper instalment credit by holder from 1939 to and including 1958.36

**TABLE 1**

**AUTOMOBILE PAPER INSTALMENT CREDIT BY HOLDER** (in millions of dollars)

<table>
<thead>
<tr>
<th>End of Year</th>
<th>Total Automobile Paper</th>
<th>Sales Finance Companies</th>
<th>Automobile Dealers</th>
<th>Commercial Banks</th>
<th>Other Financial Institutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1939</td>
<td>1,497</td>
<td>878</td>
<td>123</td>
<td>415</td>
<td>81</td>
</tr>
<tr>
<td>1941</td>
<td>2,458</td>
<td>1,363</td>
<td>188</td>
<td>785</td>
<td>122</td>
</tr>
<tr>
<td>1945</td>
<td>455</td>
<td>164</td>
<td>28</td>
<td>209</td>
<td>54</td>
</tr>
<tr>
<td>1951</td>
<td>5,972</td>
<td>2,863</td>
<td>290</td>
<td>2,446</td>
<td>373</td>
</tr>
<tr>
<td>1952</td>
<td>7,733</td>
<td>3,630</td>
<td>389</td>
<td>3,262</td>
<td>452</td>
</tr>
<tr>
<td>1953</td>
<td>9,835</td>
<td>4,668</td>
<td>527</td>
<td>4,082</td>
<td>538</td>
</tr>
<tr>
<td>1954</td>
<td>9,809</td>
<td>4,870</td>
<td>463</td>
<td>3,937</td>
<td>539</td>
</tr>
<tr>
<td>1955</td>
<td>13,472</td>
<td>6,919</td>
<td>487</td>
<td>5,305</td>
<td>761</td>
</tr>
<tr>
<td>1956</td>
<td>14,459</td>
<td>7,283</td>
<td>502</td>
<td>5,726</td>
<td>948</td>
</tr>
<tr>
<td>1957</td>
<td>15,409</td>
<td>7,470</td>
<td>478</td>
<td>6,555</td>
<td>1,106</td>
</tr>
<tr>
<td>1958</td>
<td>14,131</td>
<td>6,404</td>
<td>425</td>
<td>6,129</td>
<td>1,173</td>
</tr>
</tbody>
</table>

---

In examining the figures contained in Table 1, it is observed that of total automobile paper held by all holders in 1939, the sales finance companies held approximately 58 per cent of the total. By 1958 these companies held approximately 45 per cent of the total.

The commercial banks in 1939 held approximately 28 per cent of total holdings. By 1958 their participation in total business had increased to approximately 45 per cent. Thus the comparative importance of the commercial bank in the automobile finance business has increased, while that of the sales finance companies has declined.

The dominant role played by the sales finance companies in automobile financing is not entirely indicated by these figures, however. It was estimated in 1948 that possibly as much as 90 per cent of all retail paper was sold originally to sales finance companies, and that "the percentage of purchased paper in the hands of banks, originating with sales finance companies, equals about two-thirds of the total purchased paper held by banks."^37

The automobile dealer. The automobile dealer plays an important part in the financing of automobiles. Automobile dealers account for about half of the total instalment sales volume. About 90 per cent of the paper covering the instalment sales of automobiles is sold to financial institutions by the car dealers. Couple with this the fact that dealers hold in excess of three per cent of the total automobile paper (1958 figures), and the significance of the automobile dealer to the automobile sales transaction is readily apparent.

Sales Finance Companies Today

Despite the serious inroads of competition into what was once almost exclusively sales finance company business, today's sales finance companies are growing. This is particularly true of the largest of the companies. Four companies acquire most of the automobile paper being purchased by sales finance companies today, and all four have shown significant increases in business volume and profits for the period from 1951 through 1957. These four organizations, sometimes char-

acterized as the "Big Four" in the automobile finance field, are, in order of size, the General Motors Acceptance Corporation, C. I. T., Commercial Credit Company, and Associates Investment Company.

All four have large affiliated automobile physical damage insurers. Much of their success can be attributed to the fact that they have maintained these insurance affiliates. This is because of the fact that the basis for the entire finance transaction is the automobile itself and the availability of that automobile to serve as collateral for the finance transaction.

The protection of the billions of dollars invested in automobiles as finance collateral is vital to the success of the finance business. This is where insurance enters into the picture. The development of physical damage insurance was a logical and highly essential adjunct to the entire automobile finance business.

Why the sales finance companies chose to acquire or to organize their own insurance affiliates rather than to utilize existing insurance facilities is considered in the following chapter.
CHAPTER III

RISE OF THE INSURANCE AFFILIATES

The Need for Physical Damage Insurance

As the automobile sales finance companies developed, it became apparent that the collateral which secured the finance transaction was subject to considerable risk. Even as early as the first two decades of the present century it was increasingly obvious that the risks attendant to the operation and maintenance of a motor vehicle were formidable.

Protection for Collateral

The basis for the finance transaction was the availability of the automobile itself to act as security. Consequently, the protection of the millions of dollars invested in automobiles was vital to the success of this form of financing. Here is where insurance was needed to provide security to a collateral which was subject to the ever-increasing hazards of storage and operation. The sales finance companies
began to insist that financed automobiles be protected by insurance coverage during the period in which the installment indebtedness was being liquidated.

**Lack of Insurance Facilities**

In the beginning, attempts were made to obtain insurance protection from existing automobile insurers. There were perhaps twenty five companies engaged in writing automobile insurance by the end of 1908. Of this number, only eleven wrote some type of collision coverage, ten companies insured against fire (two of these excluded self-ignition), and only nine insured against theft.¹

By 1912 there were engaged in the automobile insurance business in this country about eighteen regular marine companies and some fifteen fire companies whose charters permitted the assumption of the automobile risk. There were also a number of mutual companies located in the country which offered automobile contracts of one form or another, although as a rule, they were not as liberal in their provisions as those of the stock companies. In addition to these companies, there were

about twenty-five casualty companies engaged in insuring against the hazards incident to the operation of automobiles.\textsuperscript{2}

Irrespective of the existence of these companies, it was difficult to obtain insurance on financed automobiles. The insurance which was provided was available only on the more select automobile risks. Insurance was not provided for all automobiles financed by the sales finance companies.

Moreover, when losses occurred or information was received by the insurance company that an insured was an undesirable risk, the company was quick to cancel coverage.

As a consequence, whichever party was doing the financing, whether it be a dealer or a finance company, was confronted by an undesirable situation. It was impossible to obtain insurance protection on some automobiles because some automobile purchasers were considered undesirable risks. Even when insurance was available on a given automobile, there was no assurance that the coverage would continue until the finance account was paid. There still remained the very real possibility that the insurance company would cancel the policy if it should decide that the risk was no longer desirable.

The reluctance to insure financed automobiles came about from two reasons. First of all, people who purchased automobiles on time were in the lower income group and were generally considered to be poorer insurance risks than people who could pay cash for automobiles. Early experience corroborated this fact.

Secondly, a difficulty arose between the insurance companies and their agents. Insurance coverage was provided on financed automobiles without using regular agents as intermediaries. The agents put pressure on the companies to discontinue this service whenever the agent was by-passed. Although financed automobiles as a class were not desirable risks, some automobile instalment purchasers were considered good risks, and the agents resented the competition which their companies had created for them.

Formation of the Affiliates

Faced with the prospect of having a great deal of unsecured credit on their hands and realizing that they could not rely on the existing insurers to protect their collateral, the sales finance companies found it necessary to make other arrangements. One after another, the leading sales finance companies either purchased existing insurance companies or
organized subsidiaries in order to provide insurance protection for themselves, their dealers, and their installment buyers.

Besides the lack of complete insurance facilities, there was another reason which prompted the formation of the sales finance company insurance affiliates. The finance companies were not satisfied with the quality of claims adjusting being performed by the insurers which originally handled the insurance on financed automobiles.

One dissatisfaction arose out of the failure of the insurer to protect the finance companies' equity in automobiles when a total or sizable loss occurred. When such a loss occurs, there are two parties who have a pecuniary interest in the settlement. The automobile purchaser has an interest in his equity, but first, the unpaid balance on the finance contract must be protected. Since the automobile has been pledged as security, and the automobile no longer exists in the case of a total loss, the finance company is entitled to the amount of its interest out of the insurance settlement. The automobile purchaser is entitled to the balance.

Current adjusting practice dictates that in the event there is a lien on the automobile and a loss occurs, the insurance company draws the check to the order of both the finance company and the insured. Before the check can be cashed, the lienholder
can make certain that it recovers its interest in the automobile.

The early insurance companies often failed to place the name of the finance company on the settlement check. Then if the insured cashed the check and failed to pay the balance on the finance contract, the finance company often did not collect the balance of the amount owing. This led to hard feelings between the finance company and the insurer.

The sales finance company further complained of slow claims service. Companies sometimes took weeks or even months to conclude a simple physical damage insurance claim. In the opinion of the sales finance companies, a delay in claims adjustment by the insurance companies resulted in the dissatisfaction of dealers and policyholders.

Thus, the finance company insurance affiliates were established to form a highly essential adjunct to the operations of the sales finance companies. These companies did not wish to enter the insurance business but were compelled to do so to protect the collateral which other insurance companies would not protect and to provide the service which was not furnished by the then-existing insurance companies.
The Need Today

As the automobile industry has grown tremendously during the past four decades, the volume of automobile finance business handled by the sales finance companies has likewise grown. Most of the automobile insurers, not affiliated with sales finance companies, still do not wish to insure financed automobiles as a class, although some insurers attempt to select the better risks within the class.

Today’s automobile purchaser who finances through the sales finance company has the option of applying for automobile insurance from another company or from the finance company insurance affiliate.

If he applies for insurance with another company, one of several things may occur. In the first place, he may be rejected by the other company, because the company refuses to insure the financed automobile class or because he is considered an undesirable risk for other reasons. If the company decides to insure him, he may subsequently fail to pay the premium, since in most cases it is either an annual or semi-annual premium and requires a considerable outlay of cash by the insured. If he fails to pay the premium, the policy is cancelled.

If he is accepted by the other company, he may subsequently be cancelled by the company as an undesirable risk, in
the event that further underwriting information or subsequent losses reveal that he is not a select risk.

Many automobile purchasers who exercise their option to purchase automobile physical damage insurance from non-finance insurers end up with no insurance because of the foregoing reasons. As a result, both the public and the finance companies have suffered. One of the large sales finance companies with automobile physical damage insurance affiliates suffers an annual loss of $200,000 on uninsured automobiles which have been pledged as security to finance transactions. This is the case even though the automobile purchaser is required to obtain insurance when the automobile is first financed.

If the automobile purchaser obtains his insurance from the sales finance company insurance affiliate, he is not faced with an immediate cash outlay on the insurance premium. The premium, like the automobile, is paid for in monthly installments. He cannot allow his policy to lapse for non-payment of premiums without also defaulting on his finance contract. He will not be rejected as an insured because he falls within a "prohibited list" occupation or age class. Once he is insured, there is only a very small possibility that he will subsequently be cancelled by the sales finance company insurance affiliate.
These points will be explained and discussed in more detail in later chapters.

The advocates of the sales finance company insurance affiliates believe that the original reason still remains for the existence of the insurance affiliates. The collateral must still be protected. Without the insurance affiliates, the finance companies believe that they would be faced with tremendous losses because of the destruction of uninsured collateral of the finance transaction.
CHAPTER IV
THE COMPANIES

Characteristics

The nature of the finance affiliates can be better understood if some of their distinguishing characteristics are examined. This chapter will accomplish that examination.

Company Numbers and Insurance Volume

There are in the United States today over forty companies which can properly be called automobile physical damage insurance affiliates of sales finance companies. A listing of forty companies is provided in the appendix.\(^1\) Combined direct writings of physical damage insurance of these affiliates for the year 1957 totalled approximately $320 million. This compares with total stock industry direct premium writings of $1,302 million and total mutual industry direct writings of $447 million. Thus, the finance affiliates accounted for 25 per cent of total stock industry volume and 20 per cent of com-

\(^1\)Appendix A.
bined stock and mutual industry volume. Total stock industry direct writings are made up of totals of 539 companies writing automobile collision coverage and of 537 companies writing automobile fire, theft, and comprehensive coverages. Mutual industry figures represent 225 companies and 233 companies, respectively, in the two categories of physical damage insurance.  

Writing one-fourth of total physical damage insurance volume of all stock companies and almost one-fifth of total industry writings, the relatively few finance affiliates represent an important segment of the automobile insurance industry.

Probably more significant, of the total number of finance affiliates, eight companies affiliated with the "Big Four" automobile sales finance companies, wrote approximately 80 percent of total business written by the finance affiliates in 1957. Two of these insurers, Motors Insurance Corporation and General Exchange Insurance Corporation, writing insurance induced by the financing operations of the General Motors Acceptance Corporation, accounted for direct writings in excess of $160 million, or one-half of total finance affiliate business.

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In terms of size, age, area of distribution, method of distribution, insurance lines handled, underwriting policy and other features, many differences exist among the finance affiliates.

**Company Size**

In the matter of company size, companies range from the huge General Motors' affiliates, representing admitted assets of $242 million and direct writings of $160 million in 1957, to small operations such as the Standard Fire Insurance Company of Alabama, with admitted assets of $358,000 and direct writings of $112,000 in 1957.

The second largest finance company, C. I. T., has two automobile physical damage insurance affiliates. These are Service Fire Insurance Company of New York and the Service Casualty Company of New York. Combined admitted assets of the two companies in 1957 totalled $106 million. Total direct written premiums amounted to over $45 million.

The Commercial Credit Company has two automobile physical damage insurance affiliates, Calvert Fire Insurance Company and the Cavalier Insurance Corporation. With admitted
assets of $68 million in 1957, the two companies wrote automobile physical damage insurance totalling over $24 million.

The fourth member of the "Big Four", Associates Investment Company of South Bend, Indiana, has two affiliates writing automobile physical damage insurance. These are Emmco Insurance Company and Excel Insurance Company. The two insurers had admitted assets of somewhat over $46 million in 1957, with direct premium writings of automobile physical damage insurance of $24.5 million for the same year.

Two additional companies wrote in excess of five million dollars in premiums in 1957. Government Employees Insurance Company wrote $12.5 million in direct writings. Stuyvesant Insurance Company, subsidiary of General Acceptance Corporation, wrote approximately $6 million in premium direct writings.

The fifth largest company in the automotive sales financing field, Pacific Finance Corporation, has two affiliates, Marathon Insurance Company and Olympic Insurance Company. The 1957 direct writings of the two companies in physical damage insurance totalled $7.5 million.

Of the remaining finance affiliates studied, ten companies wrote between one million dollars to nearly five million in direct writings; eight companies wrote a volume between one-half million to under one million; and ten wrote under one-half million.
Age of the Companies

The years following World War II can be characterized as "The Age of the Finance Affiliates," for it has been since World War II that the large majority of the companies have been organized. Although most of the companies are of fairly recent origin, the largest of the companies pre-date World War II. This is true in the case of the eight companies affiliated with the "Big Four" finance companies, with the exception of the Service Casualty Company, an affiliate of C. I. T. Service Casualty, which began business in 1945, derives most of its premium volume through a 20 per cent reinsurance participation in the commitments of the Service Fire Insurance Company. It also serves as a means by which the automobile physical damage coverages can be solicited through agency channels.

The oldest of the companies is the Stuyvesant Insurance Company, which dates back to 1851. Originally a fire company, it did not become affiliated with a finance company until 1945, when the General Acceptance Corporation of Allentown, Pennsylvania, acquired the company. The oldest actual finance affiliate is the Frontier Insurance Company. The company was organized in 1923 as a finance affiliate. Its parent is the Securities Credit Corporation.
General Exchange Insurance Corporation and Calvert Fire followed soon afterward in 1925. In 1929 the third member of the "Big Four" entered the picture with the organization of the Service Fire Insurance Company of New York. The affiliates of Associates Investment Company were not organized until 1936 and 1939. The largest of the finance affiliates, Motors Insurance Corporation, also dates back to 1939.

It is natural that there has been increased activity in organizing and creating the finance affiliates since the World War II days. Insurance affiliates' business, for the most part, has been tied directly to the automobile financing activities of the parent companies. During the war years, the production of motor vehicles for other than military purposes was almost nil. It was not until the war was over that civilian passenger motor vehicle production was resumed. Production then soared. Whereas passenger automobile sales had fallen to 70,000 in 1945, by 1950 they had skyrocketed to 6,666,000.3

A few companies seemingly planned their entry into the field somewhat untimely. For example, the Southeastern Fire Insurance Company of North Carolina, organized in 1940, found it necessary to broaden its underwriting facilities in 1942 to

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to supplement its income by writing fire and allied lines. Mid-States Insurance Company, affiliate of General Finance Corporation, writes only automobile physical damage coverages, and it was incorporated February 24, 1941, about nine months before Pearl Harbor.

With business directly tied up to automobile sales, most of the already-established companies felt the impact of the war years. The president of one of the large affiliates stated:

Our experience during the war was terrible. Only old cars were insured, because there were no new cars. It was a period of inflation, and there were no increases in rates.

The secretary and attorney for another of the large affiliates remarked that his company had cut down to almost a skeleton crew and at one time during the war years lost $150,000 per month.

The finance affiliates, lacking the versatility accompanying underwriting diversity, were faced with a volatile business situation during the war. The dozen or so companies in existence drastically restricted operations or broadened out into other lines until the resumption of automobile production following the war. Upon the latter happening, there was a resurgence of this type of insurer.
Area of Distribution

It is in the area of distribution that there is considerable difference existing between the finance affiliates. As can be expected, the large companies have a wide physical dispersion. General Exchange and Motors Insurance Corporation do business in all states, the District of Columbia and all provinces in Canada. Service Fire and Service Casualty, the C. I. T. affiliates, and Calvert Fire, Commercial Credit Company's affiliate, do business in all states and the District of Columbia. Emmco, affiliate of Associates Investment, however, does business in only three-fourths of the states. Notwithstanding its smaller area of distribution, it had more volume of business in 1957 than did Calvert Fire.

Stuyvesant Insurance Company does business in all states except Massachusetts and Mississippi. Government Insurance Company is licensed in 80 per cent of the states.

Generally speaking, companies that did $2,000,000 or more in direct writings in 1957 were operating in twelve or more states. Exceptions to this are Commercial Insurance Company and Southeastern Fire Insurance Company. Commercial, a subsidiary of Southwestern Investment Company, is licensed in five western states and writes a small volume of inland marine business as well as automobile physical damage insurance. Southeastern Fire, affiliate of Auto Finance Company, writes primarily
automobile physical damage insurance but also writes a large amount of fire and extended coverage, accident and health, automobile liability coverage, and miscellaneous lines.

As a general statement, it can be said that of those companies which write physical damage insurance only, volume of writings is tied directly to the size of the area of distribution. The two exceptions noted generate more volume in a smaller area of distribution because they employ agents and offer additional lines.

The smaller affiliates usually restrict their operations to one section of the country or to one state. Chesapeake Insurance Company, affiliate of Maryland Credit Finance Corporation, and Mt. Beacon Insurance Company, affiliate of Bankers Commercial Corporation, are examples of companies which operate in from three to five states in the east. Companies which distribute in only one state are organizations such as Permanent Insurance Company of Ohio, an affiliate of the Aid Investment and Discount, Inc.; Arrowhead Insurance Company of California, affiliated with Seaboard Finance Company; and Gateway Insurance Company of Pennsylvania, whose parent is the Continental Commercial Corporation, a company which has been engaged in the automobile finance field since 1916.
Of the forty companies studied, 60 per cent distribute in less than twelve states; 50 per cent do business in less than six states. Most of the finance affiliates are small companies.

Method of Distribution

One of the most distinguishing features of the automobile physical damage insurance affiliates of sales finance companies is their method of distribution. It has the following characteristics: (1) no advertising is used in the usual sense, and the solicitation of business is limited, and (2) most of the business written by the affiliated insurers originates through the automobile financing activities of the sales finance companies. The automobile dealer, at the time of the finance transaction, acts as the intermediary in the insurance transaction.

There are some differences existing among the finance affiliates in their methods of distribution, and these will be noted.

Absence of advertising and limited business solicitation. No advertising, in the usual sense, is employed by the typical affiliate. Of particular interest is the example
afforded by the Service Fire Insurance Company of New York. In checking for this company's telephone number in the New York City telephone directory, it was discovered that this company, which wrote $40 million worth of insurance in 1957, is not even listed in the yellow pages. The company has only a small, ordinary-sized listing, identical to that used by an individual with a four-party line.

Direct solicitation of business is limited to providing insurance facilities and drawing the attention of the automobile purchaser to the fact that these facilities exist. The purchaser who finances through the sales finance company is told that the facilities are there so that he might insure the financed automobile through the insurance affiliate if he elects to do so. For example, Associates' Investment Company has a purchaser's statement which reads as follows:

Fire, Theft, and Collision Insurance is Required:
1. Is the dealer to include this insurance? Yes ____
   No ____. If No, answer question No. 2.
2. Name of Agent______________ Telephone No. or
   Address______________Name of Company _________
   Address _________Name of Company _________
   Kind of Coverage _________Date Expires________

If the customer does not have an agent and elects to have the dealer include insurance in the transaction, Emmco Insurance Company writes the coverage.

Some solicitation for renewals is practiced. Emmco Insurance Company does nothing to solicit business after the
finance account has been paid and the finance company no longer has an insurable interest. Service Fire and Calvert Fire send invitations to policyholders to renew their policies which are about to expire in coverage. Unlike the average automobile insurance company which may renew 60 per cent or more of its business, Service Fire, for example, renews about four per cent, which is an indication of the extent that the affiliates actively solicit business.

Business generated through affiliated sales finance company. Most of the business written by the affiliates originates through the automobile financing activities of the affiliated sales finance company. The automobile purchaser buys an automobile from the dealer. It is financed, perhaps jointly by the dealer and by the finance company, or it may be financed completely by one or the other. Dealers financed three per cent of total automobile paper in 1958. Whether it is the dealer or the finance company that finances the automobile, collateral is required. That collateral is the automobile. Since automobiles

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are subject to a multitude of perils, no one wishes to advance money on such collateral without the protection of insurance.

Before the deal is financed, insurance is required on the automobile. The purchaser has the option of obtaining coverage through his regular agent, if he has one. If he does not, the automobile will be insured by the insurance affiliate of the finance company, if the customer so elects.

In any event, the finance company or the dealer have the right to insist that their equity be insured. Therefore, for example, if the dealer is financing the deal, he has the right to purchase insurance to protect his equity. He is an insurance purchaser under the "Time Price Doctrine."

A question sometimes arises as to the status of the automobile dealer when he acts as an intermediary in the insurance transaction when he has no equity remaining in the finance transaction. Is he an insurance agent? Most of the states have agency qualification laws requiring the licensing of individuals performing acts pertaining to the solicitation or securing of insurance, the issuance of binders, or the collection of premiums.

The automobile dealer is not an insurance agent because he acts as intermediary. When the financing arrangements are transacted, the purchaser agrees to furnish the necessary insurance, and, failing to do so, he authorizes the dealer from
whom he purchased the car or the dealer's assignee (the finance company) to purchase insurance on his behalf and for his protection as well as the protection of the dealer and the finance company. Under this theory the finance companies purchased insurance under the authority of the purchaser of the automobile, providing protection for the parties who had an equitable interest in the automobile. This theory is still ruling in most jurisdictions; however, a number of states have required the licensing of dealers. The affiliates' members of management doubt the authority of the states to require licenses, but they have no special objection to the requirement. In addition, they see no wisdom in contesting the states' authority in a court action, since the states would probably accomplish the same licensing requirement by specific legislation.

By virtue of the automobile purchaser's direct request or by his delegation of the purchase of insurance to the dealer or the finance company, the insurance business is referred to the affiliated insurer. The general conclusion can be reached that the larger the insurer, the more likely is it that its business is developed through the financing activities of its affiliated sales finance company. The large insurance affiliates procure their business almost exclusively through the finance activities of the sales finance companies.
In the case of Motors Insurance Corporation, affiliate of GMAC, business is procured by agents. This is explainable by the fact that GMAC requires all of its dealers to be insurance agents. Other finance companies would find it difficult to dictate this requirement to their dealers, since they have no control over the dealers' source of automobiles.

Other than what has been said about the large affiliates, no correlation can be drawn between the size of a finance affiliate and its method of distribution. A number of variations in method of distribution will be mentioned.

Variations in distribution methods. Among the medium-sized and smaller affiliates, some companies' business is closely allied with the finance activities of the sales finance company. Other companies generate business through banks and other finance companies. Still others use the American agency system.

Stuyvesant Insurance Company, one of the large medium-sized companies, generates only 15 per cent of its business through the activities of its affiliated sales finance company. The company is represented by approximately 350 agents. Other insurance lines are written besides automobile physical damage, and standard commissions are paid on this business. Automobile physical damage insurance is largely procured through agency
commission contracts which are on a sliding scale or are on a retrospective basis.

The Service Casualty Company of New York, a smaller affiliate of C. I. T., solicits business through some regular insurance agents and through dealer-agents. This company provides insurance facilities for purchasers of automobile physical damage insurance who finance through a bank or a dealer or who purchase for cash.

Calvert Fire Insurance Company has already been mentioned as securing most of its business through the activities of Commercial Credit Company. The affiliate is also experimenting on a small scale with selling through agents.

Two of the smaller affiliates, although they have comparable volumes of direct writings for 1957, use entirely different distribution systems. Balboa Insurance Company develops business through 1,400 agents, banks, independent finance and loan companies, as well as from automobile dealers and merchants financing their own sales. Less than 20 per cent of premium production represents writings originating through the financing activities of the parent finance company. Balboa's automobile physical damage insurance volume for 1957 totaled almost $3 million.

By contrast, the Industrial Insurance Company, with a comparable volume of business, writes insurance exclusively in
behalf of the affiliated finance company, Financial General Corporation, a holding company whose subsidiaries and affiliates are sales finance companies.

**Insurance Lines Handled**

If there is one single aspect of the finance affiliate that bears out the fact that this type of company is an adjunct to the business of the affiliated finance company, it is in the insurance lines handled. A total of 26 of the 40 companies studied write automobile physical damage insurance only. The primary concern of these 26 companies, is to insure the credit collateral which secures the finance transaction.

Of the remaining 14 companies, only two write a fairly broad variety of coverages. The broadest coverage of the two is written by the Olympic Insurance Company of Los Angeles, affiliate of the Pacific Finance Company. Most of Olympic's business is automobile physical damage insurance, but the company also writes fire and allied lines, inland marine, accident and health, workmen's compensation, miscellaneous bodily injury and property damage liability, automobile liability, glass, and burglary and theft.

Fire and Casualty Insurance Corporation of America, the other company which offers a variety of coverages, writes auto-
mobile physical damage, fire and allied lines, hail on growing crops, inland marine, accident and health, livestock, medical payments, and glass insurance coverages. Its parent company, Thorp Finance Corporation, was established in 1925. Besides its automobile financing function, it specializes in small loans; finances purchases of auctioned goods; and manages auctions of livestock and farm equipment.

The remaining twelve companies confine their underwriting to two or three lines in addition to automobile physical damage insurance. The most common coverage, other than automobile physical damage, is inland marine, handled by nine companies. Fire and allied lines are written by eight companies; automobile bodily injury and property damage liability insurance is handled by six companies; and five companies write accident and health. The type of insurance coverage written and the number of companies writing the insurance are indicated in Table 2. The most surprising fact that confronts the reader is that in today's era of multiple-line underwriting for an insurance-buying public that has been educated to buy the combination automobile policy, that of 40 affiliates offering automobile physical damage insurance coverage, only six companies also offer other automobile insurance coverages, the casualty coverages.
### Table 2

**Insurance Lines Handled by the Finance Affiliates**

<table>
<thead>
<tr>
<th>The Type of Insurance</th>
<th>No. of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Automobile Physical Damage*</td>
<td>40</td>
</tr>
<tr>
<td>Inland Marine</td>
<td>9</td>
</tr>
<tr>
<td>Fire and Allied Lines</td>
<td>8</td>
</tr>
<tr>
<td>Automobile Liability (BI and PD)</td>
<td>6</td>
</tr>
<tr>
<td>Accident and Health</td>
<td>5</td>
</tr>
<tr>
<td>Glass</td>
<td>2</td>
</tr>
</tbody>
</table>

One Company Writes Each of the Following:

- Ocean marine, hail on growing crops, livestock, medical payments, comprehensive personal liability, credit, miscellaneous liability, workmen's compensation, burglary and theft

* 26 Companies write Automobile PHD exclusively

---

Underwriting Policy

It is an axiomatic principle in the insurance business that good underwriting practice is indispensable to the conduct of the business and the welfare of the insurance company concerned. The underwriter is primarily responsible for the underwriting results experienced by his insurer. These results depend upon the creation and maintenance of a sound portfolio or book of business. To accept every risk, with the usual precautions taken in sound underwriting, would be disastrous, according to modern underwriting theory.

Nevertheless, the typical finance affiliate presents the enigma of a company which apparently does not underwrite its risks. For example, Emmco Insurance Company wrote a total of 212,500 policies in 1958, accommodating the finance business of its sponsors. Of this number, the company subsequently canceled 5,000 policies, or 2.5 per cent. A company officer stated:

The only risks we won't write are those no one would write. We write what would ordinarily be substandard business for other companies at standard rates. And it must be remembered that the majority of companies will not write substandard business--what is usually referred to as "marginal risks."

Service Fire Insurance Company accommodates Universal C. I. T. "as long as it does not jeopardize our financial interest."
We generally do not impose control on underwriting offices until the loss ratio makes the business unprofitable.

Business has not been unprofitable for Service Fire. During the eight years, 1951-1958, the company's combined loss and expense ratio averaged approximately 72 per cent, and underwriting profits exceeded $85 million.

An officer of Calvert Fire Insurance Company stated that his company does not employ underwriters. Calvert Fire Insurance Company will write everything that the Commercial Credit Company will finance. Another officer remarked:

We agree to insure where Commercial Credit Company agrees to finance . . . 100 per cent accommodation, and then we cancel about one per cent.

Finance affiliates that develop business through agents, banks, independent finance and loan companies (other than the parent or affiliate) do not write business ordinarily on an accommodation basis. Business is typically written on a select basis. However, those finance affiliates whose insurance activities are closely connected with the finance activities of the parent or affiliate exist primarily for the purpose of facilitating the finance transaction, and, therefore, accommodate the finance company to the necessary extent, limited by the reservation that the finance affiliate shall impose underwriting restrictions if underwriting experience runs bad.
In a sense, therefore, these finance affiliates take the automobile physical damage insurance business mine-run without any underwriting restrictions. This is not so extreme as it might appear, however, for some of the "bad apples" who are refused credit by the finance company are precluded from obtaining insurance from the affiliate. Thus, some initial screening is done by the finance company. Although this is true in many cases, a man may be a good credit risk and be a poor insurance risk. Credit is advanced if a man has collateral, capacity to earn, and character to pay back the loan. It is possible for an insured to possess these characteristics and still be a poor insurance risk. Thus, a man who is wealthy and has an excellent earning capacity besides the reputation for promptly paying bills may be a poor insurance risk. He may be a reckless driver and constantly involved in serious automobile accidents.

As a consequence, the finance company accepts contracts on people who are poor insurance risks but good credit risks. The protection afforded the insurance company is the right to cancel the coverage of the poor risk after writing it if it becomes apparent that the risk is not good.

It is apparent from the foregoing considerations that the affiliate accepts risks of all classes and has no "prohibited list" within those classifications. Insureds are class-
ified according to their desirability or lack of desirability as a risk. Class 2 risks are the least desirable class. The classifications will be discussed in more detail in a later chapter.

The finance affiliate writes Class 2 risks, but most other companies look askance at this classification. An example is afforded by the following instructions to agents published by one large, well-known insurance company:

**Automobile Risks Not to be Bound--5.** Any risk where the automobile is owned by or primarily operated by any student enrolled in any college, school, or university.

In addition, companies specify certain occupations that fall within the prohibited list. Another company includes the following on its prohibited list: bartenders or employees in beer parlors or taverns, professional entertainers and musicians, road house proprietors or employees, pool room owners or employees, professional sportsmen, students using car at school, and illegal occupations—bookmakers, gamblers, and persons employed in slot machine activities. Also excluded is any person with any physical disability (eyes, ears, limbs, or otherwise).

Another company is even more particular. In addition to the foregoing, the company excludes servicemen, traveling salesmen, used car dealers, taxi drivers, unemployed, liquor salesmen, persons of poor moral repute, persons of bad repute
because of criminal record, illegal or disreputable business or excessive use of alcohol, and a number of other risks deemed not acceptable. The company lists in excess of three dozen models of sports cars which are on its prohibited list.

Producers are advised:

1- We consider sports cars unacceptable because the operators are frequently interested in the speed capabilities of such vehicles. It is beyond the scope of this company's low cost underwriting procedures to attempt to differentiate between the acceptable and unacceptable sports cars owners.

It is apparent that the finance affiliate is unique in its underwriting policy. Where other insurance companies are continually attempting to upgrade their risks by becoming more selective, specifying prohibited risks, and canceling out insureds with adverse experience, the affiliate is writing everything that the finance company finances. It then cancels a very small percentage of its business. One of the large finance affiliates subscribes to this policy:

We will underwrite almost anything that does not have a real bad record. Other companies have a prohibited list, but we underwrite on the basis of the individual and not on the basis of the class in which the man falls. If a man is good in the class, we take him.

Surprising as the finance affiliates' underwriting, or rather, lack of underwriting, is, it is even more surprising to note that these companies write at standard rates promulgated by the national rate-making bureau for automobile physical damage insurance, the National Automobile Underwriters
Association. With the loss ratio on finance business running 20 per cent or more higher than the business of other automobile insurers, it is a wonder that these companies are able to make money, particularly in light of industry experience on automobile physical damage insurance. For example, in 1957, stock companies suffered an underwriting loss of $4,645,000 on automobile collision insurance and a loss of $33,003,000 on automobile fire, theft, and comprehensive.\(^5\)

The affiliates' operating record will be discussed in the following chapters when the operating results and particulars of the finance affiliates are presented. It will then be seen how the affiliates have fared in light of their high loss experience and in light of industry-wide adverse experience.

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CHAPTER V
OPERATING ANALYSIS - LOSS EXPERIENCE

Introduction

In this chapter and the next the operations of the finance affiliates are examined. This chapter presents the loss experience of the affiliates and the various components of that experience. The following chapter presents the underwriting experience and profits or losses.

To make the discussion more meaningful, the operating figures of the affiliates are compared with the figures of the industry and of selected company experience. These select companies are chosen on the basis of the criteria explained below.

At the conclusion of the chapter the operating figures are evaluated in terms of their significance.

The Approach

In order to understand the approach used in presenting operating data within this chapter and the following chapter,
it is necessary to know the nature and the limitations of the data.

The data. Some of the data were obtained by the writer from the companies visited. These companies constituted most of the largest of the finance affiliates. They are highly representative of this class of insurer because of the nature of their operations and because of the large volume of business transacted.

The most complete operational data available for analysis is that published by an insurance reporting service. These data are adequate for this study, and significant conclusions may be drawn from the analysis. Much of the information obtained from the companies is repetitious of data which are published by the insurance reporting service. The same service also publishes data of other companies, not the subject of this study, and in addition, it publishes industry figures.

1 Alfred H. Best Company, Inc., publishers of a statistical history of the fire and casualty business, reporting on more than thirteen hundred insurance companies and associations operating in the United States and Canada.
Since the finance affiliates are compared with other companies and with the industry, the data classifications used will be those which are available from the other companies and from the industry so that the same basis of comparison is used.

By-line operating figures are presented by the reporting service in two categories: (1) collision and (2) fire, theft, and comprehensive. Within these two categories, loss experience is broken into three sets of ratios for individual companies and for the stock industry. The three ratios are: (1) losses incurred as a ratio to premiums earned; (2) the ratio of adjusting expenses incurred to premiums earned; and (3) a combination of the first two, the ratio of losses and adjusting expenses incurred to premiums earned. The by-line breakdown and the three ratios are used in this analysis.

**Companies Selected for Comparison**

In addition to comparing operating figures of the affiliates with those of the stock company industry, the operating figures of selected companies are also compared with the operating figures of the affiliates. To use industry data exclusively is subject to some error. Published industry figures include the operating results of the finance affiliates. No
attempt has been made to isolate the operating data of all of the affiliates from industry figures, for some of the necessary data are not available. This does not constitute a serious defect for comparison purposes, for individual differences existing between the finance affiliates and other segments of the industry are so marked that small errors are inconsequential to this study.

Select companies are used to show some of the general patterns of losses and expenses existing among individual insurance companies not affiliated with sales finance companies. The criteria for selection of these individual companies are given in the following section.

Criteria for selection. Five criteria are selected for the purpose of choosing companies with which to compare the finance affiliates:

1) The line of business written. In Chapter IV it was observed that twenty-six of the forty finance affiliates which were studied write automobile physical damage insurance exclusively. Almost all of the remaining companies primarily write automobile physical damage coverage. Consequently, the companies selected for comparison will be limited to those
which write the same coverage, automobile physical damage, and will be limited to that coverage.

2) Rating procedure. The vast majority of finance affiliate business is written at standard rates. The companies selected for comparison, therefore, are standard rate companies.

3) Type of legal organization. The finance affiliates are stock companies. Consequently, the companies used for comparison are also stock companies.

4) Method of distribution. The typical finance affiliate does not use agents for distribution. On the other hand, the typical insurance company not affiliated with a sales finance company does use agents. The agents' associations have been the most active antagonists of the sales finance company insurance affiliates. Companies using agents to distribute coverage are selected for comparison with the affiliates.

5) Volume of coverage written. Since there are some advantages to large-scale production, and since the business methods of two companies doing comparable volumes of business are often similar, companies are selected because of similarity in the volume of insurance (automobile physical damage) written. This criterion is subject to criticism. If an affiliate writing one million dollars volume is compared with an insurer writing the same volume of physical damage insurance, it is possi-
ble that an erroneous picture will be presented. Although 
the one million dollar volume of the affiliate may repre-
sent its total business volume, the other insurer may write 
many other lines and have a total insurance volume of one 
hundred million dollars. As a result, it may be able to use 
large scale business methods (such as employing expensive 
electronic computers) which would not be available to the 
smaller company, the finance affiliate.

A further limitation in the selection of companies 
for comparison is the fact that there is a lack of other 
insurers to compare with certain of the affiliates, particular-
ly the largest of the affiliates. This is understandable when 
it is remembered that eight of the finance affiliates write 
25 per cent of all automobile physical damage insurance writ-
ten by the stock company industry, while 555 other companies 
write the remaining 75 per cent.

There is a larger selection of other insurers to com-
pare with the small affiliates, and in these classifications 
companies are selected at random, provided that they qualify 
under the selection criteria.
Affiliates Compared

The automobile physical damage insurance affiliates of the "Big Four" automobile sales finance companies write the vast majority of the business transacted by this class of insurer. Accordingly, these companies are typical of the finance affiliate and almost all are selected for comparison where it is possible to find other stock companies of comparable volume with which the affiliates can be compared. Smaller affiliates of varying sizes are selected at random to show some of the individual differences existing among this class of insurer.

There is not complete correlation between the volume of collision insurance written and the volume of fire, theft, and comprehensive insurance written. As stated earlier in this chapter, these two categories of automobile physical damage insurance are presented separately by the insurance reporting service. Since the volume classifications of each category are different, they will also be presented separately in this paper. Evaluation of the data and presentation of conclusions and implications of the material of the two categories of automobile physical damage insurance are presented together, since the same principles apply to both. As a consequence, the evaluation is withheld until the data of both categories of coverage are presented.
Collision Insurance

Volume Classifications

The volume classifications of net premiums written and net premiums earned are stated in approximate figures. These classifications, together with finance affiliates falling within these classifications, are as follows: $35 million, the Service Group (Service Fire Insurance Company of New York and Service Casualty Company of New York); $18 million to $20 million, Calvert Fire Insurance Company and Emmco Insurance Company; $4 million to $6 million, Stuyvesant Insurance Company; and $1.5 million to $2.5 million, Balboa Insurance Company, Commercial Insurance Company of Texas, Marathon Insurance Company, and Olympic Insurance Company. Table 3 presents the finance affiliates and other stock insurers having comparable premium volume.

Collision Loss Experience

An examination of Table 4 reveals that the finance affiliates have reported loss ratios (losses incurred to premiums earned) ranging from 63.1 to 73.9. The worst loss experience among the affiliates was experienced by Calvert Fire.
### TABLE 3

**Finance Affiliates* and Other Stock Insurance Companies With Comparable Volume of Collision Writings**

1957

<table>
<thead>
<tr>
<th>Companies and Classes</th>
<th>Net Premiums Written</th>
<th>Net Premiums Earned</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$35 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Travelers Indemnity</td>
<td>37,627</td>
<td>34,853</td>
</tr>
<tr>
<td><em>Service Group</em></td>
<td>34,072</td>
<td>37,228</td>
</tr>
<tr>
<td><strong>$18-220 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aetna Casualty &amp; Surety</td>
<td>20,796</td>
<td>18,314</td>
</tr>
<tr>
<td>America Fore Group</td>
<td>20,013</td>
<td>18,911</td>
</tr>
<tr>
<td>U.S. Fidelity &amp; Guaranty</td>
<td>18,843</td>
<td>17,626</td>
</tr>
<tr>
<td><em>Calvert Fire Insurance</em></td>
<td>16,828</td>
<td>18,981</td>
</tr>
<tr>
<td><em>Emco Insurance Company</em></td>
<td>17,908</td>
<td>19,314</td>
</tr>
<tr>
<td><strong>$4-$6 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Bankers</td>
<td>4,054</td>
<td>3,355</td>
</tr>
<tr>
<td>Continental Casualty</td>
<td>6,637</td>
<td>5,397</td>
</tr>
<tr>
<td>Glens Falls Insurance</td>
<td>5,894</td>
<td>5,595</td>
</tr>
<tr>
<td>National Fire Group</td>
<td>3,178</td>
<td>5,219</td>
</tr>
<tr>
<td><em>Stuyvesant Insurance</em></td>
<td>3,879</td>
<td>5,368</td>
</tr>
<tr>
<td><strong>$1.5-$2.5 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers'</td>
<td>2,178</td>
<td>2,026</td>
</tr>
<tr>
<td>American Home Assurance</td>
<td>1,761</td>
<td>1,481</td>
</tr>
<tr>
<td>Gulf Insurance</td>
<td>2,083</td>
<td>2,038</td>
</tr>
<tr>
<td>Indiana Insurance</td>
<td>1,913</td>
<td>1,926</td>
</tr>
<tr>
<td>Merchants Group</td>
<td>2,336</td>
<td>2,129</td>
</tr>
<tr>
<td>Westchester Fire</td>
<td>1,577</td>
<td>1,559</td>
</tr>
<tr>
<td>*Balboa Insurance</td>
<td>1,625</td>
<td>1,431</td>
</tr>
<tr>
<td><em>Commercial Insurance</em></td>
<td>2,198</td>
<td>2,052</td>
</tr>
<tr>
<td>*Marathon Insurance</td>
<td>1,601</td>
<td>1,565</td>
</tr>
<tr>
<td>*Olympic Insurance</td>
<td>2,852</td>
<td>2,309</td>
</tr>
</tbody>
</table>

The loss ratio of the stock industry (563 companies) amounted to 57.9 in 1957. Thus, the loss ratio of the typical finance affiliate runs appreciably higher than that of the industry.

Adjusting expense ratios of the finance affiliates vary between 7.1 (Commercial Insurance Company of Texas) and 15.8 (Olympic Insurance). There is a wide variance among the affiliates. However, as a group they show a larger adjusting expense ratio than do other stock insurers. It is particularly noticeable among the large finance company insurance affiliates. Emmco Insurance Company, the Service Group, and Calvert Fire Insurance Company show ratios of 11.8, 12.8, and 15.3, respectively. This is compared to the industry average adjusting expense ratio of 8.3.

Table 4 also reveals that high loss ratios of the finance affiliates are generally accompanied by high adjusting expense ratios, so that the ratio of combined losses and adjusting expenses of the finance affiliates runs between 4.8 (Stuyvesant Insurance Company) and 23.0 (Calvert Fire Insurance Company) above the stock company industry average of 66.2, or a range of 71.0 to 89.2.
TABLE 4
COMPARISON OF COLLISION LOSS EXPERIENCE, 1957

<table>
<thead>
<tr>
<th>Companies and Classes</th>
<th>Losses Incurred</th>
<th>Adjusting Expenses Incurred</th>
<th>Losses &amp; Adjusting Expenses Incurred</th>
</tr>
</thead>
<tbody>
<tr>
<td>(*Affiliates)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>$35 Million Class</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Travelers Indemnity</td>
<td>57.8</td>
<td>5.1</td>
<td>62.9</td>
</tr>
<tr>
<td>*Service Group</td>
<td>63.1</td>
<td>12.8</td>
<td>75.9</td>
</tr>
<tr>
<td>$10-$20 Million Class</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aetna Casualty &amp; Surety</td>
<td>55.8</td>
<td>6.1</td>
<td>61.9</td>
</tr>
<tr>
<td>America Fore Group</td>
<td>57.6</td>
<td>11.0</td>
<td>68.6</td>
</tr>
<tr>
<td>U.S. Fidelity &amp; Guaranty</td>
<td>55.1</td>
<td>6.9</td>
<td>62.0</td>
</tr>
<tr>
<td>*Calvert Fire</td>
<td>73.9</td>
<td>15.3</td>
<td>89.2</td>
</tr>
<tr>
<td>*Emmco Insurance</td>
<td>71.8</td>
<td>11.8</td>
<td>83.6</td>
</tr>
<tr>
<td>$4-$6 Million Class</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Bankers</td>
<td>62.9</td>
<td>5.9</td>
<td>68.8</td>
</tr>
<tr>
<td>Continental Casualty</td>
<td>75.0</td>
<td>6.0</td>
<td>81.0</td>
</tr>
<tr>
<td>Glens Falls Insurance</td>
<td>59.4</td>
<td>10.3</td>
<td>69.7</td>
</tr>
<tr>
<td>National Fire Group</td>
<td>61.6</td>
<td>7.9</td>
<td>69.5</td>
</tr>
<tr>
<td>*Stuyvesant Insurance</td>
<td>63.5</td>
<td>7.5</td>
<td>71.0</td>
</tr>
<tr>
<td>$1.5-$2.5 Million Class</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers'</td>
<td>52.7</td>
<td>6.6</td>
<td>59.3</td>
</tr>
<tr>
<td>American Home Assurance</td>
<td>65.4</td>
<td>9.4</td>
<td>74.8</td>
</tr>
<tr>
<td>Gulf Insurance</td>
<td>51.1</td>
<td>4.6</td>
<td>55.7</td>
</tr>
<tr>
<td>Indiana Insurance</td>
<td>53.3</td>
<td>8.0</td>
<td>61.3</td>
</tr>
<tr>
<td>Merchants Group</td>
<td>56.9</td>
<td>6.8</td>
<td>63.7</td>
</tr>
<tr>
<td>Westchester Fire</td>
<td>56.2</td>
<td>6.6</td>
<td>62.8</td>
</tr>
<tr>
<td>*Balboa Insurance</td>
<td>70.8</td>
<td>9.0</td>
<td>79.8</td>
</tr>
<tr>
<td>*Commercial Insurance</td>
<td>65.8</td>
<td>7.1</td>
<td>72.9</td>
</tr>
<tr>
<td>*Marathon Insurance</td>
<td>66.7</td>
<td>11.7</td>
<td>78.4</td>
</tr>
<tr>
<td>*Olympic Insurance</td>
<td>65.6</td>
<td>15.8</td>
<td>81.4</td>
</tr>
<tr>
<td>Stock Industry (218 Cos. with writings over one million dollars)</td>
<td>57.7</td>
<td>8.2</td>
<td>65.9</td>
</tr>
<tr>
<td>Total Stock Industry (563 Companies)</td>
<td>57.9</td>
<td>8.3</td>
<td>66.2</td>
</tr>
</tbody>
</table>

Source: Ibid.
Fire, Theft, and Comprehensive Insurance

Volume Classifications

The same finance affiliates are selected for comparison as were used in the discussion of automobile collision insurance. A similar classification system is used, based upon the volume of net premiums written and net premiums earned. Since a smaller volume of business is written than in collision coverage and since there is no correlation between the volume of the two categories of physical damage insurance written by the individual companies, the reader will notice that the relative volume ranking of some of the selected companies has changed. In addition, because of the lack of similarity in amount of volume between the affiliates and the other stock companies used in the previous comparison, some additional companies have been substituted for comparison purposes.

The volume classifications which will be used for this section are $11.3 million to $12.5 million, into which classification the Service Group falls; $4 million to $6 million, including Calvert Fire Insurance Company and Emmco Insurance Company; and $1 million to $1.5 million, which includes Balboa Insurance Company, Commercial Insurance Company of Texas, Marathon Insurance Company, Olympic Insurance Company, and the
Stuyvesant Insurance Company. Table 5 indicates these volume classifications in terms of net premiums written and of net premiums earned.

The same ratios examined for collision insurance are also used with fire, theft, and comprehensive insurance.

Loss Experience

Table 6 gives the loss experience of the selected companies for 1957. The total stock industry of 574 companies had an average loss ratio of 60.2. By way of comparison, the large affiliates, Service Group, Calvert Fire, and Emmco Insurance, run above the industry average with ratios ranging from 63.3 to 67.5. The smaller affiliates report ratios under the industry average; and Balboa, Marathon, and Olympic are well below the average, reporting ratios of 40.6, 47.0, and 46.4, respectively. The large affiliates, however, report comparable ratios to the experience on automobile collision insurance. There are two exceptions. Calvert Fire's loss ratio is 10½ per cent lower, and Emmco Insurance Company's ratio is four per cent lower in the case of fire, theft, and comprehensive insurance.

The adjusting expense ratio, as in the case of collision experience, again shows the large affiliates with ratios in excess of the industry average of 9.6 per cent. The smaller
### TABLE 5

**FINANCE AFFILIATES* AND OTHER STOCK COMPANIES WITH COMPARABLE VOLUME OF WRITINGS**

**FIRE, THEFT, AND COMPREHENSIVE INSURANCE, 1957**

<table>
<thead>
<tr>
<th>Companies and Classes</th>
<th>Net Premiums Written (000 omitted)</th>
<th>Net Premiums Earned (000 omitted)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$11.3-$12.5 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hartford Group</td>
<td>12,654</td>
<td>11,859</td>
</tr>
<tr>
<td>*Service Group</td>
<td>11,302</td>
<td>11,345</td>
</tr>
<tr>
<td><strong>$4-$6 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Acceptance Group</td>
<td>4,415</td>
<td>4,005</td>
</tr>
<tr>
<td>Home Insurance (N.Y.)</td>
<td>5,821</td>
<td>5,936</td>
</tr>
<tr>
<td>Loyalty Group</td>
<td>6,283</td>
<td>5,915</td>
</tr>
<tr>
<td>*Calvert Fire</td>
<td>6,084</td>
<td>5,954</td>
</tr>
<tr>
<td>*Ememco Insurance</td>
<td>4,846</td>
<td>4,726</td>
</tr>
<tr>
<td><strong>$1-$1.5 Million Class</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers¹</td>
<td>1,166</td>
<td>1,044</td>
</tr>
<tr>
<td>Hanover Group</td>
<td>1,524</td>
<td>1,480</td>
</tr>
<tr>
<td>Sun Group</td>
<td>1,470</td>
<td>1,158</td>
</tr>
<tr>
<td>*Balboa Insurance</td>
<td>1,279</td>
<td>1,126</td>
</tr>
<tr>
<td>*Commercial Insurance</td>
<td>1,198</td>
<td>1,119</td>
</tr>
<tr>
<td>*Marathon Insurance</td>
<td>1,171</td>
<td>930</td>
</tr>
<tr>
<td>*Olympic Insurance</td>
<td>1,647</td>
<td>1,266</td>
</tr>
<tr>
<td>*Stuyvesant Insurance</td>
<td>1,337</td>
<td>1,587</td>
</tr>
</tbody>
</table>

TABLE 6

COMPARISON OF LOSS EXPERIENCE, 1957
FIRE, THEFT, AND COMPREHENSIVE

<table>
<thead>
<tr>
<th>Companies and Classes</th>
<th>Ratios to Premiums Earned</th>
<th>Losses Incurred</th>
<th>Adjusting Expenses Incurred</th>
<th>Losses &amp; Adjusting Expenses Incurred</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$11.3-12.5 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hartford Group</td>
<td>58.5</td>
<td>7.5</td>
<td>66.0</td>
<td></td>
</tr>
<tr>
<td>*Service Group</td>
<td>65.0</td>
<td>13.2</td>
<td>78.2</td>
<td></td>
</tr>
<tr>
<td><strong>$4-6 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Acceptance</td>
<td>57.5</td>
<td>6.7</td>
<td>64.2</td>
<td></td>
</tr>
<tr>
<td>Home Insurance</td>
<td>60.2</td>
<td>10.5</td>
<td>70.7</td>
<td></td>
</tr>
<tr>
<td>Loyalty Group</td>
<td>62.1</td>
<td>11.5</td>
<td>73.6</td>
<td></td>
</tr>
<tr>
<td>*Calvert Fire</td>
<td>63.3</td>
<td>13.1</td>
<td>76.4</td>
<td></td>
</tr>
<tr>
<td>*Emmco Insurance</td>
<td>67.5</td>
<td>11.1</td>
<td>78.6</td>
<td></td>
</tr>
<tr>
<td><strong>$1-1.5 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers’</td>
<td>60.3</td>
<td>7.4</td>
<td>67.7</td>
<td></td>
</tr>
<tr>
<td>Hanover Group</td>
<td>60.7</td>
<td>5.3</td>
<td>66.0</td>
<td></td>
</tr>
<tr>
<td>Sun Group</td>
<td>58.4</td>
<td>6.9</td>
<td>65.3</td>
<td></td>
</tr>
<tr>
<td>*Balboa</td>
<td>40.6</td>
<td>5.4</td>
<td>46.0</td>
<td></td>
</tr>
<tr>
<td>*Commercial</td>
<td>60.4</td>
<td>6.6</td>
<td>67.0</td>
<td></td>
</tr>
<tr>
<td>*Marathon</td>
<td>47.0</td>
<td>8.1</td>
<td>55.1</td>
<td></td>
</tr>
<tr>
<td>*Olympic</td>
<td>46.4</td>
<td>10.8</td>
<td>57.2</td>
<td></td>
</tr>
<tr>
<td>*Stuyvesant</td>
<td>60.1</td>
<td>6.7</td>
<td>66.8</td>
<td></td>
</tr>
<tr>
<td>Stock Industry (163 Cos. Writing volume of $1 million or more each)</td>
<td>61.1</td>
<td>10.1</td>
<td>71.2</td>
<td></td>
</tr>
<tr>
<td>Total Stock Industry (574 Companies)</td>
<td>60.2</td>
<td>9.6</td>
<td>69.8</td>
<td></td>
</tr>
</tbody>
</table>

Source: Ibid.
affiliates generally show improved ratios on this type of business in comparison to their collision experience. As a result, the combination ratio of losses and adjusting expenses incurred to premiums earned shows the large finance affiliates with figures well over the industry average of 69.8. The smaller affiliates, unlike the experience reported on collision insurance, reported ratios lower than the stock industry average.

**Evaluation**

**Loss Experience of the Finance Affiliates**

In the discussion of finance affiliates' loss experience as indicated in Table 4, it was pointed out that the typical affiliate experiences a much higher loss ratio than that of other stock companies writing automobile physical damage insurance. Is this an indication that the affiliate is less economical in disposing of a physical damage claim; or is it a reflection of a higher claim frequency because of the class of insured; or do the affiliates pay more liberally on their claims than do other companies; or is it a combination of all three?
The finance affiliates actually settle claims for a smaller average amount per claim than the other stock insurers. Some insight can be gained by comparing the average cost per claim of the finance affiliates with that of the General Adjustment Bureau. The General Adjustment Bureau, Inc., is a national loss and claim adjusting organization owned by nearly 300 capital stock fire and casualty insurance companies and their subsidiaries. The average collision payment made by the Bureau in 1958 was $317.66. By comparison, Calvert Fire Insurance Company paid an average of $287.00 per claim; Motors Insurance Corporation paid an average of $285.00; and Service Fire Insurance Company of New York paid an average of $266.00.

The lower average cost per claim can be explained. The typical stock insurance company handles all lines of insurance, or at least, all lines of automobile insurance. A claims adjuster selected by the company is expected to be able to settle both physical damage and liability claims. Some companies do have specialists; however, the typical adjuster for a multiple line company is a general practitioner.

Although individual practices differ relative to the adjuster's required qualifications, companies ordinarily believe that a legal education is helpful in adjusting claims because of the questions of liability which arise in the administration of liability claims. Thus, most of the emphasis is
placed on preparation to handle liability matters. Automobile physical damage claims are often relegated to the position of "routine" in the claims procedure. The insured is requested to obtain two or three competitive estimates. The adjuster then checks the damaged automobile with the estimates, and after he has been an adjuster for a reasonable period of time, he can do a fair job of determining whether or not the estimates are out of line. In absence of special training, the typical adjuster relies in large part upon competition to do his job for him. The philosophy behind this thinking is that repair shops will compete for the business and that this competition will keep the estimates down to a reasonable figure since each shop knows that other shops will bid on the same job. In the event that there is something which is particularly out of line on an estimate, the adjuster's experience will enable him to catch the irregularity.

Unfortunately, the adjuster knows that there are insureds who will obtain more than three estimates and submit the three highest. Settlement is made on the basis of the lowest of the three. The insured has his automobile repaired by the shop which submitted the lowest of the other bids he obtained and pockets the difference. The adjuster also knows that some insureds will obtain a competitive estimate of damages and will show that estimate to the repair shop of their
choice to make certain that its estimate will fall just under the amount of the first bid.

The questionable practices of some insureds and of some repair shops, together with the adjuster's often-times inaccurate judgment of the reasonableness of an estimate, are not apparent in the finance affiliates' adjusting operations. Since the finance affiliate typically writes only automobile physical damage insurance, there is no need to have an attorney or law-trained man to handle claims. The finance affiliates' adjusters are required to know automobiles and to be able to recognize the extent of the damage. They are required to itemize cost in terms of the labor and parts which are needed to repair the vehicle.

Adjusters of the finance affiliates are hired on the basis of body and mechanical experience. The companies prefer to hire body shop foremen, inspectors, and estimators who have an intimate knowledge of an automobile body and its mechanical make-up.

The men selected are frequently given additional training by the company. Such training consists of an indoctrination into the company's practices and methods. In addition, adjusters are furnished with factory manuals, up-to-date labor charges, and the most recent parts-price listings of automobiles. An example of the extra training given finance affil-
iates' claim adjusters is the four-week school in Yonkers conducted by the Service Fire Insurance Company of New York for its adjusters.

The key to the practice and procedure of claims adjusting by the finance affiliates is the fact that the affiliates' adjusters make their own estimates. This is highly important in the control of claims costs. No chicanery can exist between an insured and a repair shop, because the finance affiliates send their own qualified estimators to determine the amount of physical damages to the automobile.

Originally, some of the repair shops were not receptive to the idea of having an insurance adjuster come into their shops and tell them how much a repair job was worth. The repair shops have now generally accepted the practice. The affiliates represent a large number of automobile owners. The repair shops want the business; they must cooperate with the affiliates. By so doing, the result is a savings in time of the estimators employed by the commercial shops. By estimating with a high degree of accuracy how much money should be spent to repair a damaged automobile, the affiliates are able to provide a savings in average cost per claim.
The high loss ratios of the affiliates. The high loss ratios of the finance affiliates are caused by a high claim frequency per number of insureds. Like other insurance companies, the finance affiliates obtain a share of the better risks. However, financed automobile insurance business contains many of the so-called marginal risks, which other insurance companies do not wish to write. The information obtained from the finance affiliates reveals that the under-age drivers, the transients, the in-service risks, and other categories of marginal risks are typically the people who buy their automobiles on time. This does not mean that the better risks do not avail themselves of the financing facilities of the sales finance companies. The insurance affiliates typically are confronted by a larger share of the poor risks. This is a reflection of the fact that many people who cannot qualify for other types of financing turn to the sales finance companies.

The typical insurance company will reject the undesirable risks through careful underwriting. As explained in an earlier chapter, the finance affiliate does not underwrite its business. The whole purpose of its existence is to accommodate the sales finance company by providing protection for the collateral which secures the finance transaction. The typical affiliate is unique in the insurance business. Where other
insurance companies are continually attempting to grade up their risks by becoming more selective, specifying prohibited risks, and by quickly cancelling out insureds with adverse experience, the finance affiliate is writing everything that the finance company finances. It then cancels a small percentage of its business, which is generally so poor that no company would write it. This is borne out by the fact that the prohibited list of many insurance companies includes the financed automobile. A typical exclusion reads, "Automobile Risks Not to be Bound—7. The following types of risks: (n) finance accounts." \(^2\) Insurance companies in general do not want this class of business.

One writer states:

You must realize that today insurance carriers are not seeking finance company business. If you have been a student of insurance facts for the last decade—or even longer—you must have discovered that finance company's insurance has never been profitable to the insurance companies.\(^3\)


The same writer also suggests that the large sales finance companies consider the insurance feature of financing as an integral part of the entire financing transaction. They are therefore prepared to accept a loss in their wholly-owned insurance company as long as such loss brings forth a net profit in their entire operation.  

Adjusting Expenses

The finance affiliates show a higher adjusting expense ratio as a group than that of other stock insurers, and it is particularly noticeable among the large finance company insurance affiliates.

The claims superintendents of the affiliates attribute this higher cost to claims service superior to that of other companies. The author believes that the higher adjusting expense ratio of the finance affiliates can be attributed primarily to three factors.

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4Ibid., p. 19.

5The author was claims attorney for a large, multiple-line stock insurer for a period of five and one-half years.
First, the affiliates typically handle only automobile physical damage insurance. All claims which arise are for the one line of insurance. All adjusting expenses incurred are attributable to automobile physical damage losses. Other stock companies handle complete automobile insurance. Thus, if one of the adjusters of one of the latter companies adjusts a claim involving the theft of an automobile, all of the adjusting expense is attributable to the automobile physical damage loss. If, however, the same adjustor receives notice of an automobile accident involving the insured's vehicle and two other automobiles, he may spend time investigating and settling bodily injury liability claims and property damage liability claims, as well as handling the collision claim of the insured.

When the adjuster has concluded the settlement of all claims, part of the time and expense devoted to the accident will be allocated to the liability lines and part will be allocated to automobile physical damage. The reason for this is that the adjuster can perform adjusting functions on both claims simultaneously, thus some logical allocation of expense is made. An example would be the allocation of the adjuster's automobile expense to and from an accident where adjusting functions were performed on the liability claims and on automobile physical damage on the same trip.
The point illustrated is that one adjuster handling the liability claims and the physical damage claim somewhat simultaneously will spend less time and money concluding the claims than will two adjusters, one handling the liability and the other handling the physical damage. When the company which has concluded the claims under a combination policy allocates adjusting expense to the automobile physical damage portion of the case, the amount so allocated will be less than the amount expended by the adjuster settling only one type of claim, the automobile physical damage claim.

The second factor accounting for the higher adjusting expense ratio is the fact that the affiliate adjuster makes his own estimates. The typical adjuster for other insurers has the insured submit two or three bids. Sometimes the adjuster will accommodate the insured by calling repair shops and arranging to have estimates made. If the automobile cannot be driven, the adjuster leaves the office and inspects the automobile in the place to which it has been towed. If it can be driven, the insured usually drives it to a designated place, and the adjuster checks the damages with the estimates. The adjuster for the affiliate does the same thing, with the exception that he makes his own estimate. This will require more of the adjuster's time.
Possibly a third factor contributing to the finance affiliates' high adjusting expense ratio is the character of the affiliates' branch offices. The branch offices of other stock insurers typically perform a number of functions—production, underwriting, accounting, and claims. Some companies do have specialized claims offices. The branch office of the finance affiliate is primarily a claims office. An example is afforded by Motors Insurance Corporation. The branch manager is in charge of production. Subordinate to the branch manager is the following organization: the claims manager, the claims examiner, claim supervisors, and adjusters. The claims manager runs the branch, for the most part, although the branch manager is his superior. Since the branch is primarily devoted to claims functions, it is possible that the adjusting expense ratio is influenced.

**Conclusions**

The combined losses and adjusting expenses ratio of the finance affiliates runs appreciably higher than the industry average. With this combined loss ratio approximating 30 per cent to 90 per cent of total premiums earned, it would
appear that there is very little left to take care of underwriting expenses and still leave an underwriting profit for the companies.

The following chapter examines the underwriting expenses and profit and loss results of the affiliates. It will therefore be possible to determine whether these companies are competing effectively from the standpoint of business efficiency.
CHAPTER VI
OPERATING ANALYSIS
UNDERWRITING EXPERIENCE AND PROFIT OR LOSS

Introduction

Any insurance company which intends to remain in business for any length of time must make a profit. Whether or not an underwriting profit is forthcoming depends upon the volume of premium income compared to outgo, which is represented by the sum of loss experience and underwriting experience. The preceding chapter presented the loss experience of the finance affiliates. It was observed that it is bad as compared with the stock industry average.

This chapter examines the underwriting experience of the finance affiliates in the writing of automobile physical damage insurance. The loss experience of the preceding chapter is combined with the underwriting experience of the finance affiliates in order to show profit and loss figures.

At the conclusion of this chapter the underwriting experience of the affiliates is evaluated in terms of its significance.
The Approach

The approach used in this chapter is similar to that used in the examination of loss experience. Data utilized is from the same source. By-line operating figures are presented in two categories: (1) collision and (2) fire, theft, and comprehensive.

Within these two categories underwriting expenses are broken down into four ratios: (1) commissions and brokerage fees incurred to premiums written; (2) other acquisition expenses incurred to premiums written; (3) general expenses incurred to premiums written; and (4) taxes incurred to premiums written.

The total of the four ratios represents total underwriting expenses. This total together with the combined loss and adjusting expense ratio is the combined loss and expense ratio. The latter ratio gives the reader some insight into the question of whether or not an individual company has made an underwriting profit or has sustained an underwriting loss.

The foregoing data and the ratios mentioned above form the basis for the examination and analysis presented in this chapter.
Companiees Selected for Comparison

The companies selected for comparison, both the finance affiliates and the other stock insurers, are the same as were compared in the preceding chapter. The same business volume classifications are utilized. Criteria for selection of the companies are likewise identical.

Collision Insurance

Underwriting Experience

Table 7 presents the underwriting experience of the selected companies in the writing of collision insurance.

In the case of commissions and brokerage fees incurred there is a wide difference existing between the finance affiliates and the other stock insurers. Of the affiliates represented on Table 7, only Stuyvesant Insurance Company and Balboa Insurance Company have ratios approximating those of other companies writing collision coverage. Stuyvesant has a ratio of 28.0, and Balboa shows a ratio of 24.4. The remaining affiliates have ratios which range from 1.5 (Marathon Insurance Company) to 13.8 (Olympic Insurance Company). The largest of the affiliates represented, Service Group, Calvert Fire, and Emmco Insurance, report ratios of
## TABLE 7

**UNDERWRITING EXPENSES INCURRED**

**COLLISION, 1957**

| Companies and Classes (*Affiliates) | Ratios to Premiums Written |  |
|---|---|---|---|---|---|---|---|---|
| $35 Million Class |  |
| Travelers Indemnity | 25.3 | 4.3 | 3.0 | 2.6 | 35.2 |
| *Service Group | 2.4 | 2.3 | 4.0 | 3.1 | 11.8 |
| $18-$20 Million Class |  |
| Aetna Cas. & Surety | 26.2 | 3.7 | 7.4 | 2.2 | 39.5 |
| America Fore Group | 25.1 | 5.5 | 7.5 | 2.8 | 40.9 |
| U.S. Fidelity & Guar. | 26.9 | 3.4 | 3.9 | 2.8 | 37.0 |
| *Calvert Fire | 2.4 | 4.0 | 0.3 | 3.3 | 10.0 |
| *Emisco Insurance | 2.5 | 1.1 | 2.5 |  |
| $5-$6 Million Class |  |
| American Bankers | 22.9 | 1.8 | 2.4 | 2.5 | 29.6 |
| Continental Casualty | 26.0 | 3.0 | 3.9 | 1.8 | 34.7 |
| Glens Falls | 27.4 | 5.5 | 6.0 | 2.9 | 41.8 |
| National Fire Group | 28.9 | 9.2 | 8.8 | 2.9 | 49.8 |
| *Stuyvesant Insurance | 28.0 | 3.3 | 4.6 | 2.7 | 38.6 |
| $1.5-$2.5 Million Class |  |
| American Employers' | 28.2 | 3.3 | 6.6 | 2.5 | 40.6 |
| American Home Assurance | 33.3 | 3.3 | 8.8 | 2.5 | 49.9 |
| Gulf Insurance | 26.8 | 3.5 | 3.9 | 2.0 | 36.2 |
| Indiana Insurance | 28.7 | 1.9 | 4.4 | 0.6 | 35.6 |
| Merchants Group | 27.9 | 2.8 | 3.2 | 2.5 | 36.4 |
| Westchester Fire | 25.2 | 5.6 | 9.6 | 2.8 | 43.2 |
| *Balboa Insurance | 24.4 | 2.3 | 4.3 | 2.9 | 33.9 |
| *Commercial (Texas) | 5.7 | 2.6 | 4.4 | 1.8 | 14.5 |
| *Marathon | 1.5 | 6.0 | 5.5 | 2.2 | 15.2 |
| *Olympic | 13.8 | 10.7 | 4.1 | 2.4 | 31.0 |
| Stock Industry (218 Cos. writing $1 Million or over) | 20.9 | 5.4 | 4.6 | 2.6 | 33.5 |
| Total Stock Industry (563 Companies) | 21.1 | 5.4 | 4.8 | 2.6 | 33.9 |

Source: Ibid.
only 2.4, 2.4, and 2.5, respectively. This is compared to the industry average of commissions and brokerage fees paid by stock companies. The industry average is 21.1.

Thus, most of the selected finance affiliates have ratios which are well under the industry average, and it is apparent that a wide difference exists between this aspect of acquisition costs of the affiliates and of other stock insurers. This point will be discussed at length at the conclusion of the chapter.

The second component of total underwriting expenses incurred is that of other acquisition expenses, including such things as advertising, surveys and underwriting reports, and amounts paid to boards, bureaus, and associations.

Examinations of the ratios of the companies included on Table 7 reveals some wide differences existing among companies irrespective of whether or not they are finance affiliates. Ratios vary from 1.1 in the case of Emmco Insurance Company to 10.7 in the case of Olympic, so that there are finance affiliates at both extremes. Stock industry average stands at 5.4. Six of the affiliates show other acquisition expense ratios under the stock industry average, while the remaining two affiliates fall over the ratio of 5.4.

General expenses incurred is the third component of underwriting expenses and includes such items as insurance,
rent, and equipment. The industry average is 4.6, while the
range existing between the affiliates included in Table 7 re-
veals a spread of 0.3 (Calvert Fire) to 5.5 (Marathon Insurance).
The eight affiliates fall either on the industry average or be-
low, with the exception of Marathon.

The fourth ratio is that of taxes incurred to premiums
written. There is no appreciable difference between compan-
ies.

The final comparison is that of the total underwrit-
ing expenses incurred by companies. Table 7 reveals that
ratios vary among the affiliates from 8.6 (Emmco Insurance)
to 38.6 (Stuyvesant Insurance). The stock industry average
ratio is 33.9. Five of the affiliates have ratios varying be-
tween 8.6 and 15.2; the sixth is under the industry average
with 31.0; and the two remaining, Balboa Insurance and Stuy-
vesant have ratios equal to or exceeding the industry average,
viz., 33.9 and 38.6, respectively.

It is apparent that although the affiliates as a class
experience high loss ratios and high adjusting expense ratios,
they nevertheless have low operating costs, as evidenced by
their low total underwriting expense ratios. The next sec-
tion will determine whether the savings in operating expenses
offset the high combined loss ratio so as to enable the affili-
ates to show a profit on automobile collision insurance.
Operating Results

The reader will recall that losses incurred and adjusting expenses incurred were expressed as a ratio to net premiums earned. The various components of underwriting expenses were expressed as ratios to premiums written. This is the manner in which the industry reports its operating results. As a consequence, there will be some variation existing between the combined loss and expense ratio and its relationship to 100 per cent of net premiums earned. One of the ratios is based upon net premiums earned; the other is based upon net premiums written. The difference between the figures is not sizable, but it will affect the interpretation of the combined ratio and its relationship to underwriting profits or loss. For example, in examining Table 8, the reader will notice some companies with combined loss and expense ratios which are under 100 per cent, but nevertheless, the company shows an underwriting loss. The variance between the net premiums written and the net premiums earned accounts for this difference. This variance amounts to $8.6 million on total stock industry business of 563 companies. Total net premiums written amounts to $896,164,000 for the
### TABLE 8
COMPARISON OF OPERATING RESULTS
COLLISION, 1957

<table>
<thead>
<tr>
<th>Companies and Classes (*Affiliates)</th>
<th>Combined Loss &amp; Expense Ratio</th>
<th>Underwriting Profit or Loss (in thousands of dollars)</th>
<th>Ratio to Premiums Earned</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$35 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Travelers Indemnity</td>
<td>98.1</td>
<td>-343</td>
<td>-1.0</td>
</tr>
<tr>
<td>*Service Group</td>
<td>87.7</td>
<td>4,948</td>
<td>13.3</td>
</tr>
<tr>
<td><strong>$18-220 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aetna Cas. &amp; Surety</td>
<td>101.4</td>
<td>-861</td>
<td>-4.4</td>
</tr>
<tr>
<td>America Fore Group</td>
<td>109.5</td>
<td>-2,241</td>
<td>-11.9</td>
</tr>
<tr>
<td>U.S. Fidelity &amp; Guar.</td>
<td>99.0</td>
<td>-282</td>
<td>-1.6</td>
</tr>
<tr>
<td>*Calvert Fire</td>
<td>99.2</td>
<td>362</td>
<td>1.9</td>
</tr>
<tr>
<td>*Emisco Insurance</td>
<td>92.2</td>
<td>1,625</td>
<td>8.4</td>
</tr>
<tr>
<td><strong>$4-36 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Bankers</td>
<td>98.4</td>
<td>-154</td>
<td>-4.6</td>
</tr>
<tr>
<td>Continental Casualty</td>
<td>115.7</td>
<td>-1,278</td>
<td>-23.7</td>
</tr>
<tr>
<td>Glens Falls</td>
<td>111.5</td>
<td>-768</td>
<td>-13.7</td>
</tr>
<tr>
<td>National Fire Group</td>
<td>119.3</td>
<td>6</td>
<td>0.1</td>
</tr>
<tr>
<td>*Stuyvesant Insurance</td>
<td>109.6</td>
<td>60</td>
<td>1.1</td>
</tr>
<tr>
<td><strong>$1.5-$2.5 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers'</td>
<td>99.9</td>
<td>-60</td>
<td>-3.0</td>
</tr>
<tr>
<td>American Home Assurance</td>
<td>124.7</td>
<td>-506</td>
<td>-34.2</td>
</tr>
<tr>
<td>Gulf Insurance</td>
<td>91.9</td>
<td>148</td>
<td>7.3</td>
</tr>
<tr>
<td>Indiana Insurance</td>
<td>96.9</td>
<td>64</td>
<td>3.3</td>
</tr>
<tr>
<td>Merchants Group</td>
<td>100.1</td>
<td>-77</td>
<td>-3.6</td>
</tr>
<tr>
<td>Westchester Fire</td>
<td>106.0</td>
<td>-110</td>
<td>-7.1</td>
</tr>
<tr>
<td>*Balboa</td>
<td>113.7</td>
<td>-262</td>
<td>-18.3</td>
</tr>
<tr>
<td>*Commercial</td>
<td>87.4</td>
<td>237</td>
<td>11.6</td>
</tr>
<tr>
<td>*Marathon</td>
<td>93.6</td>
<td>95</td>
<td>6.1</td>
</tr>
<tr>
<td>*Olympic</td>
<td>112.4</td>
<td>-455</td>
<td>-19.7</td>
</tr>
<tr>
<td><strong>Stock Industry (218 Cos. $1 Million or more)</strong></td>
<td><strong>99.4</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Stock Industry</strong></td>
<td><strong>100.1</strong></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Ibid.
year of 1957, while total net premiums earned for the same period totals $887,552,000.¹

When Table 8 is examined, it can be seen that the affiliates, generally, in spite of their adverse loss and adjusting expense ratios, show favorable combined loss and expense ratios and have realized an underwriting profit in 1957. The two exceptions are Balboa Insurance Company, with a combined ratio of 113.7 and an underwriting loss of $262,000, and Olympic Insurance Company, with a combined ratio of 112.4 and an underwriting loss of $455,000. Although Stuyvesant Insurance Company has a combined ratio of 109.6, it shows an underwriting profit of $60,000, which can be accounted for by the wide spread between its net premiums written ($3,879,000) and net premiums earned ($5,368,000).

It is apparent that the heavy loss experience of the finance affiliates is compensated for by significant savings in underwriting expenses, so that operating results for 1957 have been favorable. The most striking example is afforded by the Service Group with a combined ratio of 87.7 and an underwriting profit of almost $5 million.

Most of the affiliates made money while the large majority of stock insurers of other types lost money. The combined average ratio for the stock industry was 100.1 for 1957, and this figure includes the favorable experience of the affiliates.

Fire, Theft, and Comprehensive Insurance

Underwriting Experience

The experience of the selected companies in writing fire, theft, and comprehensive insurance is presented in Table 9.

In the case of the ratio of commissions and brokerage fees incurred, the experience reported by the affiliates is almost identical to that reported on collision underwriting. Again, the affiliates, with the exception of Balboa and Stuyvesant, show ratios well under the industry average ratio of 22.5. Service Group, Calvert Fire, and Emmco Insurance have particularly low ratios.

Ratios of other acquisition expenses incurred by the affiliates are almost identical with the figures reported on collision insurance. The same is true in the general expenses incurred. The only substantial variance is that of Emmco In-
### TABLE 9

**COMPARISON OF UNDERWRITING EXPENSES INCURRED**  
**FIRE, THEFT, & COMPREHENSIVE, 1957**

<table>
<thead>
<tr>
<th>Companies and Classes (Affiliates*)</th>
<th>Ratios to Premiums Written</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>$11.3-31.5 Million Class</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hartford Group</td>
<td>26.8</td>
<td>7.1</td>
</tr>
<tr>
<td>*Service Group</td>
<td>2.4</td>
<td>2.3</td>
</tr>
<tr>
<td>$4-36 Million Class</td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Acceptance Group</td>
<td>26.9</td>
<td>3.1</td>
</tr>
<tr>
<td>Home Insurance (New York)</td>
<td>26.2</td>
<td>7.9</td>
</tr>
<tr>
<td>Loyalty Group</td>
<td>24.7</td>
<td>5.9</td>
</tr>
<tr>
<td>*Calvert Fire</td>
<td>2.4</td>
<td>4.0</td>
</tr>
<tr>
<td>*Emaco Insurance</td>
<td>2.5</td>
<td>1.1</td>
</tr>
<tr>
<td>$1-31.5 Million Class</td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers'</td>
<td>28.9</td>
<td>3.3</td>
</tr>
<tr>
<td>Hanover Group</td>
<td>30.5</td>
<td>5.4</td>
</tr>
<tr>
<td>Sun Group</td>
<td>27.8</td>
<td>4.2</td>
</tr>
<tr>
<td>*Balboa</td>
<td>24.3</td>
<td>2.5</td>
</tr>
<tr>
<td>*Commercial</td>
<td>5.7</td>
<td>2.6</td>
</tr>
<tr>
<td>*Marathon</td>
<td>1.7</td>
<td>5.6</td>
</tr>
<tr>
<td>*Olympic</td>
<td>13.8</td>
<td>10.6</td>
</tr>
<tr>
<td>*Stuyvesant</td>
<td>32.9</td>
<td>2.8</td>
</tr>
<tr>
<td>Stock Industry (163 Cos. Writing $1 Million)</td>
<td>21.8</td>
<td>5.8</td>
</tr>
<tr>
<td>Total Stock Industry (574 Companies)</td>
<td>22.5</td>
<td>5.8</td>
</tr>
</tbody>
</table>

Source: Ibid., pp. 129-130.
surance Company, which shows a 9.1 ratio on fire, theft, and comprehensive, compared with a 2.5 ratio on collision insurance.

Again there is no significant difference in individual ratios of companies, finance affiliate or other stock insurers, respecting taxes incurred.

As in the case of collision insurance, total underwriting expenses incurred expressed as a ratio to premiums written indicate extremely low expense experience of the affiliates relative to the volume of net premiums written. The three exceptions are Balboa Insurance Company, with a 33.4 ratio; Olympic Insurance Company, with 30.8; and Stuyvesant Insurance Company, with 43.3. The stock industry average is 36.6.

Operating Results

Operating results of the finance affiliates during 1957 were generally very successful as compared with the stock industry on fire, theft, and comprehensive insurance for automobiles. The exception was Stuyvesant Insurance Company. Table 10 indicates that Stuyvesant experienced a combined ratio of 110.1, and an underwriting loss of $52,000. The combined loss and expense ratio for 163 companies writing over $1 mil-
# TABLE 10

## COMPARISON OF OPERATING RESULTS

**FIRE, THEFT, & COMPREHENSIVE, 1957**

<table>
<thead>
<tr>
<th>Companies and Classes (*Affiliates)</th>
<th>Combined Loss and Expense Ratio</th>
<th>Underwriting Profit or Loss (in thousands of dollars)</th>
<th>Ratio to Premiums Earned</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>$11.5-31.5 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hartford Group</td>
<td>108.4</td>
<td>-1,349</td>
<td>-11.3</td>
</tr>
<tr>
<td><em>Service Group</em></td>
<td>89.9</td>
<td>1,144</td>
<td>10.2</td>
</tr>
<tr>
<td><strong>$4-96 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>General Acceptance Group</td>
<td>101.6</td>
<td>-221</td>
<td>-5.5</td>
</tr>
<tr>
<td>Home Insurance (N.Y.)</td>
<td>114.8</td>
<td>-831</td>
<td>-14.0</td>
</tr>
<tr>
<td>Loyalty Group</td>
<td>112.9</td>
<td>-904</td>
<td>-15.3</td>
</tr>
<tr>
<td><em>Calvert Fire</em></td>
<td>86.4</td>
<td>797</td>
<td>13.4</td>
</tr>
<tr>
<td><em>Emmco Insurance</em></td>
<td>94.0</td>
<td>262</td>
<td>5.6</td>
</tr>
<tr>
<td><strong>$1-31.5 Million Class</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Employers'</td>
<td>109.5</td>
<td>-150</td>
<td>-14.3</td>
</tr>
<tr>
<td>Hanover Group</td>
<td>110.0</td>
<td>-167</td>
<td>-11.3</td>
</tr>
<tr>
<td>Sun Group</td>
<td>107.6</td>
<td>-220</td>
<td>-19.0</td>
</tr>
<tr>
<td><em>Balboa</em></td>
<td>79.4</td>
<td>181</td>
<td>16.1</td>
</tr>
<tr>
<td><em>Commercial</em></td>
<td>81.5</td>
<td>196</td>
<td>17.5</td>
</tr>
<tr>
<td><em>Marathon</em></td>
<td>69.7</td>
<td>246</td>
<td>26.4</td>
</tr>
<tr>
<td><em>Olympic</em></td>
<td>88.0</td>
<td>34</td>
<td>2.7</td>
</tr>
<tr>
<td><em>Stuyvesant</em></td>
<td>110.1</td>
<td>-52</td>
<td>-5.3</td>
</tr>
<tr>
<td>Stock Industry (163 Cos. Writing $1 Million)</td>
<td>107.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Stock Industry (574 Companies)</td>
<td>106.4</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Ibid.
lion in insurance volume each was 107.0 in 1957, whereas the combined ratio for the total stock industry of 574 companies was 106.4.

**Evaluation**

**Underwriting Expenses of the Finance Affiliates**

It has been observed that the typical finance affiliate operates at a much lower expense ratio than the other stock insurers. This fact is borne out by an examination of Tables 7 and 9.

In the preceding discussion of commissions and brokerage fees incurred, it was pointed out that there is a wide difference existing between the finance affiliates and the other stock insurers. This is readily understood when one remembers that the finance affiliates typically do not use agents as intermediaries, while other companies use agents and pay commissions which usually amount to 20 per cent or 25 per cent.

The finance affiliates, in spite of the fact that they do not use agents as intermediaries, are required to pay resident agents a countersignature commission in the states where the company operates. This varies from 1½ to 3 per cent.
Some of the finance affiliates, such as Stuyvesant Insurance Company (with a 28 per cent ratio on commissions and brokerage) and Balboa Insurance Company (with a 24.4 per cent ratio) develop business through agents and pay regular commissions on their business. This accounts for their higher ratios.

Thus, the difference existing between the typically low ratio of the affiliates, 2.4 or 2.5 per cent, compared to the ratio of the stock industry average (in excess of 20 per cent) is attributable to the fact that agents are not used by the affiliates and are used by other companies. This is the situation existing in all but nine states which require that automobile dealers be licensed.² Even in the states where a dealer must be licensed, the finance affiliates do not pay a commission, except in California and Kentucky where dealer-agent's commissions are required.

It has been stated that the "typical" finance affiliate does not pay agents' commissions. Motors Insurance Corporation, the largest of the affiliates, does pay agents' com-

²An automobile dealer must obtain an insurance agent's license in Alabama, Arizona, California, Kansas, Kentucky, Nevada, North Carolina, Oklahoma, and West Virginia.
missions. The company has a closely controlled dealer-finance company-automobile manufacturer relationship which has made it possible to require that all of its dealers obtain agents' licenses in those states which allow dealer licensing. In states not permitting dealer licensing—Ohio, Michigan, New York, and Massachusetts—Motors Insurance Corporation's sister insurer, the General Exchange Insurance Corporation, operates at deviated rates of 25 per cent. In many respects these two insurers are highly typical of the finance affiliates. In other respects it is difficult to categorize them along with Calvert Fire, Service Fire, and Emmco. In the case of the latter three companies, they exist as an accommodation to their sales finance company affiliates to protect the security pledged in finance transactions. In the case of the two General Motors' companies, they exist to accommodate the business of General Motors Acceptance Corporation, but in addition, and perhaps more important, the primary business consideration is to sell automobiles and other products manufactured by General Motors.

Neither of the General Motors affiliates is a typical affiliate nor a typical stock insurer. Although Motors Insurance Corporation writes a huge volume of physical damage insurance ($131,974,000 in direct writings in 1957), it reinsures 80 per cent of it with its sister insurer.
Relating expenses incurred in obtaining direct writings to net premiums in the case of the two General Motors affiliates, plus the fact that adequate operating data are not available on the two companies, would result in distorted comparisons. For the foregoing reasons, Calvert Fire, Service Fire, and Emisco have been characterized as typical affiliates, while the General Motors affiliates have been excluded.

Other underwriting expenses. Earlier in this chapter it was indicated that there appeared to be no significant pattern existing to differentiate the affiliates from other companies in the matter of other acquisition expenses incurred. The same is not true in the case of general expenses, however. Particularly in the case of the largest affiliates, general expense ratios fell appreciably below the industry average. Even the smaller affiliates fell either below the average or fairly close to the industry average, which also includes the favorable experience of the larger affiliates.

In breaking down the expense items, several important factors are noticed. The first is the absence of advertising on the part of the affiliates. These companies ordinarily do not advertise. They may solicit renewals, but they have typically restricted their business to insuring the automobiles
which have been financed by their sales finance company, and they do not solicit business from any other segment of the insurance market.

A second factor which can be noted is that the ratio of expenses of payments made to boards, bureaus, and associations generally runs about 60 per cent or less than that paid by other standard rate companies.

Third, the relative incidental costs of underwriting, such as underwriting reports and surveys is considerably lower in the case of the affiliates than that of the industry. Again this may be attributed to the lack of the function of underwriting, in the usual sense of the word.

An examination of the general expenses of the large finance affiliates, Calvert Fire, Service Group, and Emmco, shows lower general expense items throughout. This is attributable to mass production, standardization (since only one line is written), and the streamlining of operations, particularly noticeable in the ultra-modern offices of Service Fire Insurance Company in New York City and the offices of Calvert Fire Insurance Company in Baltimore.

It would not be expected that the ratio of taxes to premiums written would vary appreciably from company to company. The tax rate of the majority of the states is identical, and the balance of the states vary only one per cent
either way. Differentials in the tax ratio can be accounted for by differences between companies in their area of distribution (states in which they operate) and the volume of insurance business written in each jurisdiction.

Conclusions

It is apparent that the finance affiliate is unique in the insurance industry. Here is a class of insurer which experiences an unusually high loss ratio of a magnitude which would quickly run other insurers out of business. However, because of peculiar advantages in its method of operation and because of highly successful efforts to obtain efficiency and economy in its business operations, the finance affiliate has been able to show an underwriting profit. Its continued success in the insurance world will depend upon its ability to preserve the competitive advantages that it enjoys.
CHAPTER VII
THE MISCLASSIFICATION FUROR

Introduction

In 1954 a scandal was disclosed which shocked the insurance industry and which caused substantial embarrassment and bad publicity for the companies involved. It was discovered that some companies had misclassified insureds for rating purposes with respect to automobile physical damage insurance. The matter has been aired by federal and state governmental authorities, the press, and the insurance industry through June of 1959.

The Problem

The misclassification situation is discussed in this study because of its particular pertinence. A number of the insurance affiliates of sales finance companies were involved in the scandal. Finance affiliates were attacked by various insurance associations, the National Association of Better Business Bureaus, Inc., and by regulatory officials. The United States Senate through an investigating committee conducted two
hearings on the subject. The subcommittee was highly critical of the finance affiliates. Criticism came at a time when the entire field of automobile marketing practices was under surveillance. Legislation was proposed to correct some of the abuses which had been charged to the finance affiliates. Organizations such as the National Association of Casualty and Surety Agents recommended a severance of connections between sales finance companies and affiliated insurance companies.¹

The chapters dealing with the misclassifications are not written to vindicate the affiliates. Rather, their purpose is to present a comprehensive picture of many of the aspects of the misclassification scandal, presenting both sides of the situation. This is important, for most of the writings on the subject are characterized by a one-sidedness which does little to provide the reader with a complete understanding of the subject.

The Classification System

To fully understand the situation the reader should have some knowledge of the automobile physical damage insurance

classification system. Certain classifications have been established by the National Automobile Underwriters Association to provide a means by which insureds can be classified for rating purposes. The system attempts to establish criteria whereby insureds can be rated as more or less desirable insurance risks.

Most of the states now place insureds under one of three classifications and a variety of sub-classifications. Originally, all insureds were charged the same premium rate. Class 1 and Class 2 rates became effective in most states in the latter part of 1950, and the majority of states adopted the Class 3 classification in 1953 or in 1954.

The system utilizing all three classifications established a 35 per cent rate spread between the highest and the lowest premium rates. Class 3 was charged the original flat rate; Class 2 was surcharged 15 per cent over flat rate; and Class 1 was discounted 20 per cent from flat rate. By the adoption of such a system it was made possible to penalize bad risks and to provide coverage to the so-called good risks at lower rates.

An example of a typical private passenger automobile classification plan is afforded by the State of Ohio:
Collision - Class 1

Class 1 means (Individual Owners Only):

a) The use of the automobile is not required by or customarily involved in the occupational duties of any person except in going to and from the principal place of occupation; and

b) There is no male operator of the automobile under 25 years of age resident in the Named Insured's household or employed as a chauffeur of the automobile.

Class 1F means (Individual Owners only):

a) The automobile is owned by an individual or by husband and wife living in the same household, and principally garaged on a farm or ranch and such automobile is not customarily used in going to or from work other than farming and is not used in any occupation other than farming; and

b) There is no male operator of the automobile under 25 years of age resident in the same household as the Named Insured or employed as a chauffeur of the automobile.

Collision - Class 2

Class 2A means (Individual Owners only):

There is a male operator under 25 years of age resident in the Named Insured's household or employed as a chauffeur regardless of whether or not the automobile is used in the occupation, profession or business of the Named Insured or of any other person customarily operating the automobile; and

a) The male operator under 25 years of age is not the owner or principal operator of the automobile, or

b) The male owner or operator under 25 years of age is married.

Class 2C means (Individual Owners only):

There is a male operator under 25 years of age resident in the Named Insured's household or employed as a chauffeur regardless of whether or not the automobile is used in the occupation, profession or business of the Named Insured or of any other person customarily operating the automobile, and the male operator under 25 years of age is the owner or principal operator and is not married.
Class 2AF means (Individual Owners only):

There is a male operator of the automobile under 25 years of age. The automobile is principally garaged on a farm or ranch and is not used in any occupation other than farming; and

a) The male operator under 25 years of age is not the owner or principal operator of the automobile, or

b) The male owner or operator under 25 years of age is married.

Class 2CF means (Individual Owners only):

There is a male operator of the automobile under 25 years of age. The automobile is principally garaged on a farm or ranch and is not used in any occupation other than farming, and the male operator under 25 years of age is the owner or principal operator and is not married.

Collision - Class 3

Class 3 means (Individual Owners only):

a) The use of the automobile is required in the occupation, profession or business of the Named Insured or any other person customarily operating the automobile; and

b) There is no male operator of the automobile under 25 years of age resident in the Named Insured's household or employed as a chauffeur of the automobile.

Misclassification

If an insured does not use his automobile in connection with his occupational duties, and if there are no underage drivers using the automobile, he is entitled to Class 1 rates. He will pay 35 per cent less in premiums than will the Class 2 risk.
If an insured entitled to Class 1 rates is arbitrarily placed in Class 2, he will be required to pay a substantially larger premium than is justified. If an insured were improperly classified in 1953, he would pay a 33 per cent extra charge, amounting to as much as $125 on a three-year policy. The amount would depend upon the territory involved and upon the particular sub-classification.

Insurance companies normally require as routine procedure in writing each individual policy that certain underwriting information be obtained from the insured. Such information includes a description of the vehicle (make, age, motor and serial numbers), date of purchase of the vehicle, cost, whether or not there is a lienholder, and the use to which the automobile will be put. Usually the first thing asked of the insured is whether or not he has an underage driver who will be operating the vehicle.

By use of such information it is possible to select the proper premium rate for each insured. The misclassification furore arose when it became apparent that there existed a serious discrepancy in the manner in which many insureds were being classified.
Disclosures in Texas

The first activity on the misclassification subject started in the summer of 1954 when the Texas Board of Insurance Commissioners received information that a number of insureds of the Service Fire Insurance Company were misclassified. A preliminary investigation revealed that approximately 85 per cent of this company's insureds in Texas had been placed in Class 2.

This figure was extremely high as compared with nationwide averages. The National Association of Insurance Commissioners at that time reported that only 13 per cent of all insureds in all companies were in Class 2. Eighty per cent of insureds were entitled to the less expensive Class 1 rates, while seven per cent fell into other classifications.

Informed of the situation by the Texas Board, the company sent a letter to policyholders which it had placed in Class 2. Insureds were advised that they might have been misclassified and that they would be given refunds upon proof of misclassification. A total of 42 per cent of the policyholders responded to the letter, of which 85 per cent reported having been misclassified. The company promptly refunded $89,000 to these policyholders.
The Texas Board of Insurance Commissioners conducted investigations to determine whether other insurance companies were complying with Texas requirements concerning classification of automobile risks. Five additional companies were found to have made similar misclassifications. An additional $100,000 was refunded to policyholders of these companies: Calvert Insurance Company, Cavalier Insurance Corporation, Marathon Insurance Company, Consolidated Lloyds, and the Home Service Casualty Company. No publicity was given to the Texas development originally, according to the Texas Casualty Commissioner, because the department wanted to "correct the situation rather than penalize an insurer." An investigation by the Texas Insurance Board in 1955 indicated that the companies previously at fault were properly classifying their risks.

It became evident that practices leading to misclassification were not confined to Texas but existed on a national scale. In April of 1955 the National Association of Insurance

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Commissioners conducted an examination of the Service Fire Insurance Company at its home office in New York. A check of all policies written by this company during April of 1955 showed that 26.33 per cent were in Class 1, 46.04 per cent in Class 2, and 27.83 per cent in all other classes. Here again the Class 2 figures varied from the reported national average of 13 per cent, and the conclusion was reached that many insureds were misclassified. According to a Texas examiner who participated in the examination, Service Fire misclassification went back as far as 1951 and:

... the further back we went the worse it was. In St. Louis in 1951 I found as high as 90 per cent in Class 2 that should have been in Class 1... The majority should have been in Class 1.4

Other states began to look into possible misclassifications within their jurisdictions. The Zone 5 commissioners5 met in the middle of September, 1955, for a hearing on the misclassification problem.6 At the hearing the Texas insurance examiner mentioned above testified that he and other examiners

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4 Collision Insurance Overcharges, loc. cit.

5 Zone 5 is made up of the following states: Arkansas, Kansas, Nebraska, Oklahoma, Texas, and Wyoming.

had estimated that the total overcharges involved might exceed $25 million.7

The NAIC Resolution

As the nationwide aspects of the overcharging became more apparent, the National Association of Insurance Commissioners appointed a special committee to study the problem. This led to the adoption of the following resolution in December, 1955:

Whereas it has come to the attention of this committee that some insurers engaging in the business of automobile physical damage insurance covering financed cars, due to possible misclassification of some insureds, had charged premiums in excess of the applicable rates; and

Whereas this matter has been receiving the serious consideration of this committee, not only from the standpoint of fashioning measures to prevent any misclassification but also with a view toward effecting the return of the overcharges, if any; and

Whereas there exists a grave question of law in most states as to who may be entitled to the return of any such overpayment; and

Whereas it appears that at least one of the insurers which may have misclassified assureds has, effective as of July 1, 1955, installed new rating procedures on a nationwide basis which were designed to an in all likelihood will prevent future errors in the classification of assureds; and

Whereas there has now been proposed a settlement pursuant to which the aforesaid insurer will undertake to recheck its rating data in respect of all policies previously written which were in force on June 30, 1955, and on the basis thereof and without resolving the question of law involved, refunds of proven overpayments will be made to the assureds; and

Whereas under the proposed settlement an assured will be entitled to a refund of over-payment by furnishing rating information on a prescribed form properly verified showing that there was an error in his classification; and

Whereas the offer of settlement is made without prejudice to the legal rights or contentions of any parties concerned: Now, therefore, be it

Resolved, that it is the sense of this committee that such offer is fair and reasonable; and be it further

Resolved, that this committee recommend favorable consideration of such offer by the several states to which it may be made, unless the laws thereof otherwise provide; and be it further

Resolved, that this committee recommend to the several states that such offer be the pattern for the disposition of all similar situations.8

8Ibid., p. 28.
The NAIC resolution was not binding on or acceptable to all state insurance departments. The resolution proposed a settlement which provided that the insurance company referred to (Service Fire) would recheck policies which were in force on June 30, 1955. Since the three classifications were used by most states prior to this date, compliance with the agreement would obviously not produce complete refunds. Supporters of the resolution presented two reasons for its adoption. First, the June 30, 1955, cut-off date would pick up most policies. The average policy of Service Fire ran for a period of 18 to 22 months; thus policies written as early as January, 1954, would still be in force on June 30, 1955. Prior to 1954 rate differentials within the classes involved were not great. Secondly, the date limit was also dictated largely because of the fact that records going back more than two years were not available.9

These arguments were unsatisfactory to some of the insurance departments in the United States. Connecticut, Massachusetts, Kentucky, New Jersey, and Pennsylvania announced that they would seek to have all excessive charges returned to policyholders regardless of the date of policy issuance.

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9Ibid., p. 29.
The National Association of Better Business Bureaus, Inc.

The National Association of Better Business Bureaus, Inc., was probably the principal agitator of the misclassification publicity. The Association, located in New York City, is a non-profit federation of 108 local Better Business Bureaus, supported by 75,000 business firms. It was established by American business in 1912 to protect itself and the public from business practices which are fraudulent, misleading, or unfair, where such practices exist on a national or regional scale. Expressing the will of legitimate business to deal fairly with its customers, the Association thereby seeks to build and maintain public confidence in business.

The Association issued a statement to the effect that the NAIC resolution was a whitewashing of the misclassification practices.\textsuperscript{10} It was the contention of the Association that the refund policy decided upon was inadequate. Contrary to the arguments supporting the resolution, the Association argued that the formula provided for no restitution in the case of:

1) Policies written for less than 18 months prior to January 1, 1954, although classification (and the opportunity for misclassi-

\textsuperscript{10}Ibid., p. 8.
ification) has existed in the same states since as early as
the year 1950.

2) Policies written for less than 18 months after January 1,
1954, on which payment was completed prior to June 30, 1955;
and policies written for more than 18 months after January 1,
1954, but canceled before June 30, 1955.

The Association was also critical of the resolution's
reference to the existence of a "grave question of law" as to
who was entitled to the return of overpayments.

Because of dissatisfaction with the manner in which the
misclassification matter was being handled by the NAIC, the
National Association of Better Business Bureaus sent question­
naires, dated February 24, 1956, to the insurance commissioners
The questions were designed to elicit explanations for the pro­
visions of the resolution, as well as to reveal the names of
companies involved and the total amounts in refunds forthcoming
from each state. No answers were received from a majority of the
states, and the Association concluded that most of the state in­
surance officials were unwilling to disclose all of the facts.11

11 Ibid.
The Association believed that the misclassification scandal was "the most important case ever to come to Better Business Bureau attention," and despite the nationwide implications and the huge sum involved, it appeared to the Association that little was being done to tell the public about it. As a consequence, it was decided to issue a direct warning to the public.

The 1956 BBB bulletin. In September of 1956 the Association distributed nationally a bulletin denouncing certain sales finance companies' automobile insurance affiliates. The bulletin stated:

Insurance companies known to be involved and their automobile finance company affiliates are:

- Cavalier Insurance Company (Commercial Credit Company)
- Calvert Fire Insurance Company (Commercial Credit Company)
- Emnco Insurance Company (Associates Discount Corporation)
- Industrial Insurance Company (American Instalment Credit Corporation)
- Marathon Insurance Company (Pacific Finance Corporation)
- Service Fire Insurance Company (Universal CIT Credit Corporation)

12 Ibid., p. 173.
The bulletin pointed out that the insurance industry as a whole had not been involved, nor had all finance company insurance affiliates been implicated.

So far as is known, the comparatively few insurance companies at fault are affiliates of automobile finance companies, but it would be wrong to conclude that all such companies have made such overcharges. Some insurance companies and their finance affiliates have been scrupulous in their insistence on adequate information from which the proper rate could be determined and have charged accordingly.14

The Senate Subcommittee Hearing--March, 1957

It was largely through the efforts of the National Association of Better Business Bureaus, Inc., that the United States Senate decided to look into the situation. Senator A. S. Mike Monroney (Democrat, Oklahoma), Chairman of the Subcommittee on Automobile Marketing Practices of the Committee on Interstate and Foreign Commerce, announced that hearings would be opened early in 1957 to look into charges made by the NABBB of misclassification of automobile collision rates by finance company insurance affiliates.15

14 Collision Insurance Overcharges, loc. cit.

15 "Senate Group to Probe Automobile Misclassifications," The Eastern Underwriter (January 25, 1957), volume 58, p. 16.
On March 18, 1957, the Subcommittee met to look into automobile marketing practices, and specifically those pertaining to finance and insurance. In four days of hearings testimony was taken of several officers of the national and regional better business bureaus, of commissioners and examiners representing state insurance departments, and of officers of several of the insurance affiliates of sales finance companies.

Subsequent Developments

In May of 1957 the National Association of Insurance Commissioners held a hearing in New York to consider the correction of mispractices in connection with insurance sold on installment sales of automobiles and other products. At the hearing the National Association of Mutual Insurance Agents attacked the finance affiliates and declared that there should be a separation of the business of lending money from that of selling insurance by the same institution. 16 Less drastic proposals were made which suggested that the situation could be handled by requiring full disclosure and notification procedure between automobile

16 "NAIC Hearing Held on Automobile Misclassification," The Eastern Underwriter (May 17, 1957), volume 58, p. 29.
dealers and insureds and requiring that necessary information be obtained from the insured to indicate his proper classification. ¹⁷

By June of 1957 the National Association of Insurance Commissioners reported that the necessary reforms had been effected, indicating the elimination of misclassification, and that it was "unnecessary to take further action at this time." ¹⁸

By February of 1958 the National Association of Better Business Bureaus, Inc., was still dissatisfied with the progress made on the misclassification scandal. In a press release the Association charged that if the insurers involved had done a good job of seeking out the persons over-charged, the refunds would total approximately $25 million instead of the $6 million which had been paid to that date. ¹⁹

On August 7, 1958, the United States Senate subcommittee headed by Senator Monroney again met to consider the overcharge-


ing in the field of collision insurance. The Senator began the hearings with a review of findings of the subcommittee arising from the previous hearings of March, 1957. The subcommittee loosed a verbal barrage against certain affiliates of finance companies and against the insurance departments of most states.²⁰

Developments since August of 1956 have not been particularly significant, although refunds are still being reported. Interest has diminished and some of the charges made against the finance affiliates have been all but forgotten.

Charges Against the Affiliates

In the course of the investigations conducted of the misclassification situation, a number of serious charges were levied against the affiliates. The major abuse cited, of course, was that of the practice of misclassifying insureds so

that excessive premiums were charged them. Most of the other abuses were in some way related to misclassification, while others were not.

The Abuses

Besides the practice of misclassification, the following abuses were uncovered in the course of the investigations:

1) In many cases policies of insurance were not issued to the purchaser of the financed motor vehicle.

2) In cases where master policies were issued to the automobile dealer, the insured did not receive any insurance certificate.

3) Policies and certificates had been signed in blank before issuance.

4) Rate charts were used improperly.

5) Unlicensed persons were acting in the negotiation of insurance policies.

6) There was coercion in connection with the placing of insurance on financed motor vehicles.

7) Insureds were forced to take "package deals"--other types of insurance as well as the automobile physical damage insurance.
8) Unearned premiums were not returned to the insured on cancelation.

9) Insureds were charged premiums for $50 deductible coverage but received a deductible policy of $100 at the $50 deductible rate.

10) There were territorial misclassifications resulting in higher than normal premiums.

11) Full cost of insurance was not stated to the purchaser.

12) Purchaser of motor vehicle on finance plan received no statement setting forth his insurance coverage.

**Blaming the Affiliates**

Throughout the history of the misclassification scandal the finance affiliates were blamed almost exclusively for the abuses which had been uncovered. As already mentioned, the misclassification matter was first discovered in connection with one of the large finance affiliates, the Service Fire Insurance Company of New York. As state after state reported its results of investigation, the finance affiliates figured prominently, almost to the exclusion of other companies.

A typical report was that of the Massachusetts insurance department:
With the exception of the American Fidelity & Casualty Company, located in Richmond, Virginia, the four companies who were found to have misclassified policyholders are so closely affiliated with large finance companies as to be generally referred to as "captive companies" or specialty writing companies.21

Some of the companies involved, however, were not finance affiliates. When requested to do so by members of the Senate subcommittee, the Massachusetts insurance commissioner presented a list of companies which had made refunds up to the time of the March, 1957, hearings. Among the companies listed were large, well-known insurers which were not finance affiliates. Included were Travelers Insurance Company, Insurance Company of North America, Phoenix of Hartford, The America Fore Group, Continental Company, Niagara Fire Insurance Company, National Fire Insurance Company of Hartford, and others.

Expressing concern that the press might not understand the role played by these companies in the misclassifications, the commissioner took particular care to point out:

I want to forcibly underline that point, that we still feel that these companies have the highest of reputations. It is unfortunate that they became involved, and they were involved on an agency level.22 I am convinced . . . that the companies themselves and their

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21 The United States Senate, Hearings, March, 1957, op. cit., p. 139.

22 Ibid., p. 156.
top officers have no knowledge of this.\textsuperscript{23} those cases are not the ones that we are talking about of widespread nationwide violations.\textsuperscript{24}

Several states reported that they had found companies which were guilty of misclassification. Only a few states would reveal the names of those companies. Information was obtained concerning some of the large finance affiliates, however, and their nationwide involvement was well known even though some states did not publish the names of implicated companies.

While the finance affiliates were being blamed for the misclassifications, frequent opinion was expressed that the misclassifications were deliberate.

\textbf{Mistake or deliberate act?} Throughout the Senate subcommittee hearings charges were made that the misclassifications could not have been accidental. The principal insurance examiner of the state of Massachusetts testified:

These misclassifications by the so-called specialty insurance companies are by no means accidental, or can they be attributed to human error. Insurance depart-

\textsuperscript{23}Ibid., p. 156.

\textsuperscript{24}Ibid., p. 157.
ment examiners, while examining dailies in the home offices of these companies noted Hooper-Holmes and retail credit reports attached to the dailies, stating that no drivers under 25 resided or drove the particular cars in question. The dailies themselves would be rated class 2 and such credit reports were attached to the dailies.

This investigation unit . . . also has in its possession at the present time automobile collision insurance charts which have been placed in the hands of various automobile dealers by a national financing company to be used for time-payment plans on new and used cars. These charts were originally calculated from finance charts which include class 2 collision premiums. In other words, if an automobile times sales buyer actually rates class 1, or class 3, he is still charged the highest rate, class 2. The instructions to the automobile dealer further states that if the customers feel that they are being overcharged, or are eligible for preferential collision rating in class 1 and class 3, the so-called adjustment charts for these classes are to be employed.

The Massachusetts insurance commissioner charged:

There are those who contend that the widespread misclassification practices uncovered are merely mistakes which had remained undetected by all concerned. I will readily concede that this practice could well have commenced by mistake. However, I believe that those finance companies, the insurance companies, and captive insurance companies who benefited most by it soon had full knowledge, not only of what they were doing but also that they were wrong in doing it. The underwriting of automobile physical damage insurance, even under the best of conditions, demands supervision by skilled persons, and there is no doubt insurance facilities as a pawn to increase profits, rather than

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25 Ibid., p. 33.
to render service to the public, and the subsequent mishandling of their insurance companies has resulted in their getting burned fingers.26

The New Jersey insurance commissioner reportedly informed the National Association of Better Business Bureaus, Inc., on March 25, 1956:

In the early part of this investigation we formed the opinion that the omission of complete classification data was deliberate because in many cases, the underwriting information was retained in the office of the finance company or bank, where the business originated, and was not forwarded to the home office of the company for proper classification by the company underwriters.27

The New York Times for January 30, 1957, quoted the commissioner as explaining that "in most instances" the overcharges "appeared to have been deliberate," but that no case of "outright fraud" had been uncovered.

Agents' associations attributed the abuses to the finance affiliates' method of distribution--the use of automobile dealers. The New York State Mutual Agents Association contended that the automobile dealer is not an insurance man and as long as he is allowed to sell insurance there will continue to be misclassifications, misunderstandings, coercion, and many other consumer

26 Ibid., p. 139.

27 Ibid.
abuses. The New York State Association of Insurance Agents charged that the dealers "victimize" insurance buyers whom licensed agents try to serve.

Not only were there charges made that the misclassifications were deliberate, but the Senate subcommittee went further to say that once the misclassifications were discovered, the companies deliberately failed to take all of the necessary steps to rectify the situation. Note the following:

The committee found in its hearings that the attempt of the companies to return these refunds was half-hearted and intentionally confusing to the ordinary car buyer. A combination of deliberate factors gives rise to this conclusion. The failure of the companies to clearly state in the letters (sent to policyholders that had been classified Class 2) that they were being sent to determine if refunds were due caused many of them to be thrown away. Many people simply did not realize that they might be entitled to refunds if they filled out the complicated questionnaire. Furthermore, notarization was required in most cases. This was a difficult burden for the average person to bear, especially since he could not clearly know that he would be eligible for a return of his money. The burden should have been on the companies' shoulders to affirmatively find out whether or not the policyholder had been overcharged.

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30 The United States Senate, Hearing, August, 1958, op. cit., p. 443.
misclassification Evidence

Some of the companies admitted that they had misclassified and immediately began to make refunds when the situation came to light. There was other strong evidence that misclassification overcharging had occurred. The discrepancy existing in underwriting information (such as in the case of the Hooper-Holmes and retail credit reports) has already been mentioned. Probably the most significant point raised by the investigators was that of the high percentage of finance affiliates' insureds which had been placed in class 2.

Class 2 Distribution

The early figure of national average of Class 2 business, quoted by the NABBB as originating from the NAIC, was 13 per cent. During the 1958 hearing the NAUA introduced nationwide figures, with the exception of a few states, of collision distribution of cars by classification. These figures were broken down into distribution for $50, $75, $100, and $150 deductibles on collision coverage. Figures given in Table
show a variation of distribution in Class 2 risks of 26.1 per cent in 1952 to 12.7 per cent in 1956.\textsuperscript{31}

TABLE 11
PRIVATE PASSENGER AUTOMOBILES
COLLISION DISTRIBUTION BY CLASSIFICATION

<table>
<thead>
<tr>
<th>Calendar Year</th>
<th>1952</th>
<th>1953</th>
<th>1954</th>
<th>1955</th>
<th>1956</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exposure - Total No. of Car Years (in thousands)</td>
<td>9,265</td>
<td>9,821</td>
<td>9,651</td>
<td>11,349</td>
<td>11,246</td>
</tr>
<tr>
<td>Class 1</td>
<td>47.9</td>
<td>52.0</td>
<td>63.9</td>
<td>69.6</td>
<td>79.2</td>
</tr>
<tr>
<td>Class 2</td>
<td>28.1</td>
<td>28.7</td>
<td>27.9</td>
<td>22.5</td>
<td>12.7</td>
</tr>
<tr>
<td>Class 3</td>
<td>24.0</td>
<td>19.3</td>
<td>8.3</td>
<td>7.9</td>
<td>8.1</td>
</tr>
</tbody>
</table>

These figures, of course, represent all coverages, whether they be $50 deductible collision or $150 deductible collision. However, the figures for all coverages closely approximate those figures of $50 deductible collision coverage, for the $50 deductible represents the large majority of total collision coverage written (varying from 85 per cent of total collision coverage written in 1952 to 70 per cent in

\textsuperscript{31}\textit{Ibid.}, p. 468.
1956). The $100 deductible collision coverage represents the second largest volume of coverage (approximately 29 per cent of total in 1956). Most affiliate business is, likewise, $50 deductible collision coverage.

In the early hearings the Senate subcommittee had attempted to ascertain from the involved companies the percentage of their business which had been placed in Class 2. Comparing these figures with the national average of collision business in Class 2, the subcommittee had hoped to come up with a reliable figure of the actual amount of misclassification which took place by company.

The companies had never kept a breakdown of business placed in Class 2, according to testimony of company officers. They stated that there was no business purpose to be served by keeping such figures; and that if such figures existed, they would be in the possession of the NAUA, the official rate-making organization which handled the affiliates' statistical information.

The NAUA reported that the 1954-55 data were no longer available. Since such material is voluminous, the organization destroys records after a suitable period of time in order to avoid burdensome warehouse problems. The NAUA did furnish such information earlier to the states of New York, New Mexico, and Oklahoma on certain companies specified by the insurance depart-
ments. Other than that, no figures were available. Class 2 collision distribution of some of the finance affiliates are given in Tables 12, 13, and 14 for the three states.\textsuperscript{32}

\begin{table}[h]
\centering
\caption{Oklahoma Percentage Distribution Collision - 3rd Quarter, 1954}
\begin{tabular}{lccc}
\hline
Company Name & Class & Percent & Exposure (Car-Months) \\
\hline
Service Fire & 1 & 1.5 & 505 \\
 & 2 & 98.3 & 32,143 \\
Marathon & 1 & 1.6 & 324 \\
 & 2 & 98.2 & 17,221 \\
Calvert & 1 & 7.2 & 604 \\
 & 2 & 92.8 & 7,833 \\
Cavalier & 1 & 40.0 & 12 \\
 & 2 & 60.0 & 18 \\
\hline
\end{tabular}
\end{table}

\textsuperscript{32}The United States Senate, \textit{Hearings}, \textit{op. cit.}, March, 1957, pp. 16-18.
### TABLE 13

**NEW MEXICO PERCENTAGE DISTRIBUTION**

**COLLISION - 3d QUARTER, 1954, & DECEMBER, 1955**

<table>
<thead>
<tr>
<th>Company Name</th>
<th>Class</th>
<th>Percent</th>
<th>Exposure (Car-Years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Motors Insurance</td>
<td>1</td>
<td>67.9</td>
<td>2800</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>30.0</td>
<td></td>
</tr>
<tr>
<td>Service Fire</td>
<td>1</td>
<td>10.1</td>
<td>490</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>86.8</td>
<td></td>
</tr>
<tr>
<td>Calvert Fire</td>
<td>1</td>
<td>30.2</td>
<td>352</td>
</tr>
<tr>
<td></td>
<td>2</td>
<td>67.6</td>
<td></td>
</tr>
</tbody>
</table>

### TABLE 14

**NEW YORK PERCENTAGE DISTRIBUTION**

**COLLISION - 3d QUARTER, 1954**

<table>
<thead>
<tr>
<th>Company Name</th>
<th>Class 1</th>
<th>Class 2</th>
<th>Exposure (Car-Months)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Calvert Fire</td>
<td>28.0</td>
<td>70.5</td>
<td>64,450</td>
</tr>
<tr>
<td>Cavalier</td>
<td>39.7</td>
<td>58.5</td>
<td>61,845</td>
</tr>
<tr>
<td>Emmco</td>
<td>75.5</td>
<td>19.7</td>
<td>500,557</td>
</tr>
<tr>
<td>General Exchange</td>
<td>17.6</td>
<td>80.0</td>
<td>32,900</td>
</tr>
<tr>
<td>Motors Insurance</td>
<td>5.9</td>
<td>14.7</td>
<td>5,597</td>
</tr>
<tr>
<td>Industrial</td>
<td>27.7</td>
<td>71.9</td>
<td>12,770</td>
</tr>
<tr>
<td>Interstate</td>
<td>10.3</td>
<td>89.0</td>
<td>125,959</td>
</tr>
<tr>
<td>Mount Beacon</td>
<td>15.4</td>
<td>74.6</td>
<td>19,398</td>
</tr>
<tr>
<td>Service Casualty</td>
<td>22.2</td>
<td>72.7</td>
<td>25,003</td>
</tr>
<tr>
<td>Service Fire</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stuyvesant</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>American Fidelity Fire</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
The General Motors' affiliates, General Exchange and Motors Corporation, were not implicated in the misclassifications. The Senate subcommittee and the NABBB reported that there was no evidence that these companies had overcharged. Table 14 indicates a 1954 class distribution for the General Motors affiliates in New York of 75.5 per cent in Class 1 and 19.7 per cent in Class 2. An NAUA officer expressed the opinion that New York would be representative of the nation as a whole. Said he:

It is a large and important state, representing a tremendous volume of business, and if you had to choose a single state, I would say New York would be an excellent sample.33

Since the General Motors' affiliates experienced comparable distribution figures (77.3 per cent in class 1 and 16 per cent in class 2) nationwide during the last of 1957 and the first two months of 1958, the implication developed by the subcommittee was that the 1954 figures of the other affiliates in New York could be compared with the same companies' 1957-58 experience nationwide to determine percentage-wise the extent to which these companies misclassified. This appears to be a valid approximation of affiliate misclassification.

33 The United States Senate, Hearing, op. cit., August, 1958, p. 476.
A number of representatives of the finance affiliates testified at the Senate subcommittee hearings. Present were officers from Service Fire Insurance Company, Industrial Insurance Company, Emmco Insurance Company, Calvert Fire Insurance Company, and Cavalier Insurance Corporation.

Testimony of Company Officers

J. Page Risque, vice president of the Service Fire Insurance Company of New York, testified during the 1957 hearings. Characterizing certain accusations as being inaccurate statements, he dealt with them in the following order:

1) The $25 million "guesstimate"—he pointed out that the figure was attributable to the Texas insurance examiner who mentioned this amount when the matter first arose in Texas. According to Mr. Risque, that same examiner, after a prolonged examination of Service Fire, signed a report of examination.
stating that a reserve of $1,585,000 was an ample reserve to cover the total liability of the company. By March of 1957 the company had made refunds exceeding $1,400,000.

2) The assertion of wilfulness in misclassification--Mr. Risque stated that the company had always abided by NAUA rules. When the rules were shown to be inadequate, the company voluntarily adopted remedial procedures which were later embodied in the revised rules of the NAUA.

3) Knowledge of excessive writing of Class 2 risks--Mr. Risque stated that no company made a practice of keeping such figures and that no business purpose could be served by such a practice.

4) Contrary to accusations made, Service Fire had cooperated fully and in good faith to carry out its refund program.

5) He was very critical that only the affiliates had been singled out to bear the fault. The evidence clearly implicated many insurers not affiliated with sales finance companies.

During the hearings, Senator Monroney mentioned the large number of letters mailed and the publicity given misclassifications in Massachusetts and Connecticut, resulting in higher percentages of return as compared with other states. Refunds made over letters sent in Connecticut were 65.1 per cent and in Massachusetts were 46.7 per cent as compared to an average for
all states of 22.8 per cent, with the figures of the two states included. The senator asked Mr. Risque why a larger percentage of refunds were made in these two states. Mr. Risque replied in essence that if one dangles a worm in front of a fish long enough, it will bite.

I think it may well have resulted in the inclusion of many people who would unfairly have claimed refunds.\textsuperscript{1} He further stated:

\ldots and I do think there is reason that if you just put a letter out that said you will probably get a refund or you may be entitled to a refund, sign here, that you would get lots of people signing that form.\textsuperscript{2}

In support of his theory Mr. Risque cited a spot check made by his company in the state of Texas. Of 425 people who wrote in for refunds, 25 per cent were found to have misrepresented and were not actually entitled to refunds. In a spot check conducted in another state of 250 to 500 insureds, 28 per cent of the returns were misstated as to the right to obtain a refund.

\begin{footnotesize}
\\footnote{\textsuperscript{1}The United States Senate, \textit{Hearings, op. cit.}, March, 1957, p. 268.}
\\footnote{\textsuperscript{2}Ibid., p. 267.}
\end{footnotesize}
Mr. Risque commented further:

When you send out a form that simply asks the question, if you sign here you may be entitled to a refund, I would sign it. Most people would. Insurance companies are fair game today.3

Mr. Henry L. Van Horn, present Chairman of the Board of Calvert Fire Insurance Company and the Cavalier Insurance Company, likewise denied that there was any knowledge on the part of his companies that misclassification existed. He pointed out that his companies did not underwrite risks—every risk submitted is insured. Therefore, there is no need for the usual skilled underwriting personnel with a responsible position in the management of the company, and as a matter of fact, the company does not employ underwriters. Therefore, an unusual number of class 2 risks would not be significant to the companies' personnel, mostly girls, who compute premiums on the policies.

Regarding a previous witness's mention of a discrepancy existing between insurance dailies and Hooper-Holmes reports, Mr. Van Horn said of his own companies' participation in such discrepancies:

Needless to say, the element of human error cannot be avoided entirely. We do not deny that in some few instances, which to our best recollection were less

3Ibid., p. 269.
than a dozen out of several thousand policies, Hooper-Kolmes reports were secured and through clerical inadvertence were filed with the underwriting file without the classification being changed as was indicated by the report.

I was very much surprised that any emphasis was put upon that, because the examiner who made the examination recalled these few items, and I think in his own mind knew they were merely clerical errors, ... and to attach any significance to it, in my opinion, is wrong.4

Emmco Insurance Company representatives attacked the allegation that the company's personnel had any knowledge of the misclassification prior to the general disclosure of the situation or that there was any deliberate intention to overcharge. Reference was made to the conference examination of the company by the NAIC for the period ending 1954. The report stated:

For a 12-month period ending September 30, 1955, a tabulation of 279,504 policies issued by the company shows 58.6 per cent of the risks were given class 1 rating, 37.7 per cent class 2 rating, and 3.8 per cent class 3 rating. A test check of these percentages proved them to be substantially accurate.5

The company further stated that as early as August of 1954, it was observed that the NAUA classification plan was re-

4Ibid., p. 379.

5The United States Senate, Hearing, op. cit., August, 1958, p. 481.
resulting in some misclassifications. Emeco, on its own initiative, the first company to do so, devised and put into effect its own form which left room for no assumptions but required the insured to answer "yes" or "no" to a group of questions so that the fact would affirmatively appear for its classification in the case.\(^6\)

The company presented a state by state breakdown of action taken on misclassifications and reported that as of June 30, 1958, it had refunded a total of $660,276 to policyholders. This was an increase of over $400,000 since the March, 1957, hearings.

### Extent of Refunds

The Senate subcommittee staff reported at the time of the March, 1957, hearings that the total amount of refunds for all 48 states was somewhere in the neighborhood of $5,200,000. By April 30, 1958, total refunds had increased to the amount of $8,339,754, an increase of $3,150,000 over the early 1957 figures.

\(^6\)See purchaser's statement, supra, p. 57.
As previously indicated, a Texas insurance examiner had estimated the total amount of overcharges in excess of $25 million. Commenting upon the April 30, 1958, refunds figure, Senator Monroney at the 1958 hearing stated:

Our staff studies—and again it is my opinion—is that $25 million is a low figure... and if the $25 million would be assumed to be a reasonable figure, if they returned roughly $8.5 million, there would still be $16 million that has not been returned under this sort of a self-willingness program by the grace of the companies to reimburse the overcharges.7

It is pure conjecture to speculate how accurate the Senator's supposition might be without knowing the basis of facts upon which it is founded. It does not seem possible, however, that his estimate can be too far from wrong. Many letters to overcharged insureds were possibly ignored or never reached their addressees. The number of replies received to letters mailed was far from complete. Then, too, there is surely no assurance that all companies guilty of misclassification were detected. On the contrary, the evidence supports the opposite view.

The latest refund total available is that of April 30, 1959, as submitted by insurers to the National Association of

7The United States Senate, Hearing, op. cit., August, 1958, p. 456.
Insurance Commissioners. The total is $10,272,730. The breakdown by state is given in Appendix E.

Criticism of State Insurance Departments

The Senate subcommittee and the National Association of Better Business Bureaus, Inc., were highly critical of the manner in which most of the insurance departments in the United States had handled the misclassification situation.

Senator Konroney made the following statement at the beginning of the 1958 hearing:

"... most states left the refund program up to the companies themselves, and made little or no effort to determine whether or not the letters circulated were clear and definite as to purpose, or were addressed to all of the class 2 policyholders. They made little or no effort to check on replies, or to recontact those who had not replied. Nor did they determine that they were refunding the full amount of the overcharge. Also, they failed to give sufficient publicity through the press of these widespread misclassifications."

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8 The National Association of Insurance Commissioners, Subcommittee Reports—Insurance Problems in Connection with Instalment Sales and Loans, June 8, 1959, meeting.

9 The United States Senate, Hearing, op. cit., August, 1958, p. 443.
He went on to state that much of the failure to diligently and effectively follow up the disclosures of the overcharges undoubtedly was due to lack of staff aides and clerical assistance. He also believed that state insurance commissioners had failed to require adequate statistical controls of the insurance companies involved.

An officer of the NABBB asserted that the extent to which refunds are or will be made to those who are entitled to receive them appears to depend largely upon the diligence which the insurance departments devote to the task. He drew a contrast between the Connecticut and Tennessee departments.

Connecticut insurance examiners visited the home offices of all insurers writing automobile physical damage insurance in the state and obtained lists of all Connecticut policyholders. Tabulating runs produced the names of 58,000 insureds which were charged the class 2 rate.

All of the companies were directed to send questionnaires to these policyholders. If these failed to get a response, followup letters were sent out by the department itself. These elicited a high percentage of replies. In addition, his department issued press releases to news media publicizing the misclassifications and urging the public to reply to the questionnaires being mailed.
By December 2, 1956, refunds of more than $450,000 had been made by the fifteen companies involved. Reporting these results, the Bridgeport Herald for December 2, 1956, stated:

Commissioner Spellacy's campaign has been in marked contrast to the look-the-other-way approach of most other insurance commissioners.

In contrast to the activities in Connecticut, the NABBB cited the activities of the Tennessee insurance department. After the NABBB bulletin was released, the commissioner was interviewed by the Memphis BBB which was reportedly informed that the insurance department had ordered Service Fire to review every policy which had been sold since June 30, 1955. The company reportedly had refunded some $22,000 in premium overcharges. The commissioner stated that Cavalier Insurance Corporation, Calvert Fire Insurance Company, and Emmco Insurance Company had been investigated, and that there was no evidence of misclassification. Commenting on the report, an NABBB official remarked:

I am not suggesting that conditions in Connecticut and in Tennessee, which has one and one-half times the population of the New England state, were identical. However, no profound exercise of either the intellect or the imagination is required to discern the difference in the corrective and protective measures taken by the insurance departments of the respective states and the results obtained.10

10 The United States Senate, Hearings, op. cit., March, 1957, p. 35.
It is also significant to note that Calvert Insurance Company subsequently made refunds in Tennessee exceeding $41,000.\textsuperscript{11}

The California insurance department wrote to the Long Beach Better Business Bureau on March 2, 1956, and stated:

> It is probably an overworked statement to say that California is different from other states ... vigorous enforcement of the regulations by this department has been of proven value in keeping such inimical practices to a minimum in this state. Those complaints we have received have been occasional individual matters rather than an indication of a widespread, concerted practice.\textsuperscript{12}

As of December 31, 1956, Calvert Fire Insurance Company had refunded a total of $44,995.30 in the state of California.\textsuperscript{13}

The Oregon insurance commissioner made a similar assertion:

> We are not aware of any overcharges made in the state of Oregon, and we attribute this to the fact that the business is highly competitive, and the buyer or borrower must be completely informed as to his insurance policy.\textsuperscript{14}

\textsuperscript{11}Ibid., p. 167.

\textsuperscript{12}Ibid., p. 46.

\textsuperscript{13}Ibid., p. 410.

\textsuperscript{14}Ibid., p. 72.
In Oregon, Calvert Fire Insurance Company made refunds in the amount of $9,503.86 total. 15

The foregoing, according to the NABBB, were only a few isolated examples of the activities of the state insurance departments, but were representative of the majority of the states. In concluding, the NABBB official remarked:

Generally speaking, we have found that where the insurance department has publicized this thing vigorously there has been a higher percentage of refunds, a proportionately higher percentage of refunds, than where it has been kept secret. 16

As support for this statement, the states of Connecticut, Massachusetts, Kentucky and others were cited as instances where aggressive action had been taken by state insurance departments to publicize the matter and work to obtain refunds where misclassifications were evident. In these states there was a correspondingly greater percentage of refunds made to the number of letters mailed. 17

15 Ibid., p. 411.
16 Ibid., p. 80.
17 Ibid., pp. 164-167.
Evaluation

During the period that the misclassification matter was being aired, serious accusations were made against one segment of the insurance industry, the insurance affiliates of sales finance companies. The major companies, with the exception of the General Motors' affiliates, were charged with a deliberate overcharging of the American public.

Publicity given to the matter by a few insurance departments and the efforts of the National Association of Better Business Bureaus caused the situation to reach national prominence and ultimately resulted in two United States Senate hearings.

A lack of data and information was evident immediately and was continually commented upon by Senate investigators. The companies reported that they did not have the statistical information desired and could not procure it without considerable cost and delay. Little information was available from state insurance departments, most of which did not have the information or appeared reluctant to disclose it.

Although the whole matter was marked by incomplete information, avoidance of the subject by some quarters, and by inconsistencies in the testimony given, conclusions can be drawn from the information and material which developed out of the misclassification scandal.
Misclassification of policyholders did occur, and the number was obviously of huge proportions. Some companies took it upon themselves to immediately look into the matter to determine whether or not and to what extent they themselves might be overcharging their customers. Some company officials readily admitted that their companies were guilty of overcharging.

What has been in issue has been how much money was involved.

How Much Money Involved?

From the amount of money which has already been refunded, it is apparent that overcharges totalled millions of dollars. How many millions were involved is a matter of opinion. A total of $10,273,000 had been refunded as of April 30, 1959.

The evidence bears out the fact that many people to whom letters were mailed failed to receive the letters because they had moved and could not be located. Others failed to respond to the letters. Percentages of response in some states were low.

The complaint was made that some states did little to uncover misclassifications. It is not inconceivable that large sums are still owing in these jurisdictions.
It is impossible to arrive at a definite conclusion regarding the amount of overcharges which are still outstanding, but it could well be staggering.

Who Was Responsible?

It is a foregone fact that misclassifications took place. It is also readily apparent that certain of the insurance affiliates of sales finance companies were extensively implicated. It was charged that the affiliates were aware that they were overcharging, for it must have been apparent to them that they were writing too many class 2 risks. It was further charged that the refund program was deliberately impeded by the framing of ambiguous questionnaires and the requirement of notarization.

Over-distribution of class 2 risks could only be ascertained if current distributions could be compared to a standard. When the scandal was first disclosed, it was reported by the NABBB that the NAIC had indicated that the nationwide average class 2 distribution was 13 per cent of insureds. Better Business Bureau testimony in the 1957 hearings stated that this percentage should be not more than 20 per cent.18 On January 28,

18Ibid., p. 5.
1957, F. Roger Downey, administrative assistant to the New York superintendent of insurance, stated that, normally, 30 per cent of policies on automobile finance accounts should be class 2.19

Many opinions were expressed on the subject of what would be a normal class 2 percentage of distribution, but no one seemed to know. The situation was summed up by Mr. Risque of Service Fire:

In the outset of these (classification) plans no percentage was ever promulgated by the NAIA, or other groups, to say that all members should have this percentage. The percentages have been in doubt. . . we did not receive percentages showing that this is what you should have, and thereby be aware that we should have that kind of classification.20

There was an honest belief on the part of affiliate members of management that the affiliates would normally write a high percentage of class 2 risks because of their underwriting policy, or rather, lack of underwriting policy. Since these companies handle all risks, they would surely accept a large number of under-age drivers, in-service risks, and others which would be class 2. When class distribution figures were finally developed by these companies in 1957 and 1958, the writer is convinced that the low percentage of class 2 risks came as a genuine surprise to the companies.

19 Ibid., p. 27.
20 Ibid., p. 243.
The writer believes that some of the early questionnaires were subject to criticism. Obviously, if a policyholder receives a form in the mail that merely asks questions without telling why, and perhaps even leads the addressee to suspect that his premiums might be raised, this would surely discourage a response. Then, too, if the policyholder found it necessary to pay a notary fee and to go to the inconvenience of having a form notarized, this would discourage returns.

Service Fire's early questionnaire read as follows:

We are making an audit to determine the accuracy of premiums charged on collision insurance. As you may be entitled to a lower cost on your policy described above, it is important that the following form be completed and returned as promptly as possible. 21 (This was accompanied by a notary form)

Industrial Insurance Company's form read:

To help us determine the accuracy of the rate, will you please answer all of the questions. . . . If an error in classification is found, an adjustment will be made by us, but in no event will there be an increase in premium.22

Calvert's first general circularization read as follows:

To assist us in checking the premium to be charged for the insurance on your car, please give us the follow-

21Ibid., p. 197.

22Ibid., p. 328.
ing information . . . In the event we do not hear from you within 30 days we will assume that the premiums shown in the policy are correct.23

Calvert's second general circularization had the following wording:

If an error in classification is found with reference to your policy, a proper adjustment will be made. In no event will there be any increase in the insurance charge on your policy.24

The requirement of notarization and the early wording of the questionnaires were probably objectionable. Several insurance departments required recircularization and a re-wording of the forms. The companies that used the original wording and the notary form defended on the grounds that it would cut down on the number of people who claimed refunds who were not entitled to them.

Other companies involved. There is concrete evidence that companies other than the finance affiliates were involved. This was brought out particularly in the 1958 hearing. Connecticut reported that eight of the fifteen companies in that state were not affiliates. Oklahoma, New Jersey, Kansas, Florida, and

23 Ibid., p. 405.

24 Ibid.
Maine all mentioned companies which were not finance-owned.
The company which reportedly refunded the largest amount in
Washington, D.C., up to the time of the 1958 Senate hearing
was not a finance affiliate. 25

Reference has been made earlier to the class 2 distribution percentages in New York for 1954. 26 Referring again
to the same source, New York revealed a large number of companies other than finance affiliates that had high percentage
distributions of class 2 risks. These distributions are set forth in Table 15. The Senate subcommittee did not mention
these companies. This is surprising in view of the fact that
the NAUA had indicated that insurance activities in New York
would be highly representative of insurance activities in the
nation as a whole.

Besides the companies included in Table 15 there were
an additional 12 companies in New York with a class 2 distribution of 40 per cent or more. Another 20 companies had a class
2 distribution of 30 per cent or more.

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26 Table 14, supra, p. 148.
<table>
<thead>
<tr>
<th>Company Name</th>
<th>Exposure (Car-Months)</th>
<th>Class 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quaker City Fire &amp; Marine</td>
<td>125</td>
<td>76.8</td>
</tr>
<tr>
<td>American Home Assurance Group</td>
<td>13,001</td>
<td>66.9</td>
</tr>
<tr>
<td>South Carolina Insurance</td>
<td>5,842</td>
<td>80.7</td>
</tr>
<tr>
<td>Pacific Fire</td>
<td>16,709</td>
<td>77.3</td>
</tr>
<tr>
<td>Jersey Insurance</td>
<td>26,060</td>
<td>88.5</td>
</tr>
<tr>
<td>Millers National Group</td>
<td>1,707</td>
<td>90.7</td>
</tr>
<tr>
<td>Albany</td>
<td>2,732</td>
<td>61.1</td>
</tr>
<tr>
<td>Continental Insurance</td>
<td>26,146</td>
<td>56.0</td>
</tr>
<tr>
<td>Phoenix Insurance Group</td>
<td>93,127</td>
<td>60.1</td>
</tr>
<tr>
<td>Kansas City Fire &amp; Marine</td>
<td>3,636</td>
<td>62.4</td>
</tr>
<tr>
<td>Bankers &amp; Shippers</td>
<td>27,197</td>
<td>58.8</td>
</tr>
<tr>
<td>Fireman's Fund (Boston)</td>
<td>17,546</td>
<td>55.1</td>
</tr>
<tr>
<td>Fireman's Fund Group</td>
<td>52</td>
<td>57.7</td>
</tr>
<tr>
<td>Granite State Fire</td>
<td>3,809</td>
<td>59.0</td>
</tr>
<tr>
<td>Great Eastern Fire</td>
<td>10,866</td>
<td>50.7</td>
</tr>
</tbody>
</table>

Wilfulness in misclassifications? Earlier in this study there were noted a number of accusations made by the NABBB and insurance departments that these misclassifications were "by no means accidental, nor can they be attributed to human error." They were further characterized as being "unconscionable practices," and they "appeared to have been deliberate."

The Massachusetts insurance commissioner testified in the 1957 hearings:

I will readily concede that this practice could well have commenced by mistake. However, I believe that those finance companies, the insurance companies who benefited most by it soon had full knowledge, not only of what they were doing but also that they were wrong in doing it. The underwriting of automobile physical damage insurance, even under the best of conditions, demands supervision of skilled persons.27

He went on to say that the other companies that had been found to be misclassifying were companies of "the highest of reputations."

It is unfortunate that they became involved, and they were involved on an agency level . . . I am convinced . . . that the companies themselves and their top officers have no knowledge of this.28

He discounted the misclassifications of companies other than finance affiliates as innocent and the fault of "unscrupulous

27Ibid., p. 139.

28Ibid., pp. 156-157.
agents." On the other hand, throughout the hearings it was contended that the finance affiliates should have known and in fact did know that misclassifications were occurring because of the high percentage of their business which was written in class 2.

It is not entirely clear to this writer, that if the finance affiliates should have known, why shouldn't other companies have also known that they were writing too many policies in class 2, particularly when such other companies have underwriting policy which normally rejects most class 2 business and would accordingly write a smaller percentage of class 2 risks? Then, too, some companies refuse to write class 2 risks at all because of very select underwriting policy. The finance affiliate does not underwrite.

Further, how can a company sit back and issue the statement, "It was the fault of unscrupulous agents?" Surely any company can examine the writings of a certain agency and determine that the percentage of class 2 risks written are out of proportion to the so-called national average. How could there possibly be any reason for agency companies to misclassify when such companies employ agents who are experts in writing automobile coverage and who presumably know the importance of obtaining complete underwriting information?
The high percentage and amounts of misclassification on the part of the finance affiliates can possibly be attributed to several reasons. First, the large affiliates operate nationally. From a total dollar standpoint they would be more involved, all other things being equal, in misclassifications than would most other companies because of comparatively higher volume of business.

Secondly, and more important, is the manner of distribution. These companies do not select risks. Moreover, they procure business through automobile dealers, and underwriting information is obtained (or not obtained) by these dealers. Control over the dealers by the finance company was not present in any marked degree, for the dealer could turn to another finance company if he did not like the restrictions imposed upon him by the first company. The dealer, whose principal concern was that of selling automobiles, was obviously not concerned with good underwriting procedure. Then, too, because of the so-called "repossession reserve" paid the dealer by the finance company on total volume, there may have also been some incentive for him to fail to obtain underwriting information, with the realization that an insured would be placed in the more expensive class 2.

The affiliates admit that they should have checked their underwriting practices, but in retrospect, they state that it
was not done, perhaps because of the nature of those underwriting practices. As pointed out by an officer of Calvert Fire:

"We don't underwrite. I think it would be safe to say that we don't have an underwriter in the company. We write all of the business the finance company accepts. We have ten girls who write policies. They could have put 100 per cent in class 2 and never have suspected that anything was wrong."

Emeco Insurance Company attributed the misclassifications to the complexity and the newness of the classification system.

"We know that our company has some class 2 risks in class 1 and class 3, because we find them while we are investigating collision claims made by such insured. This fact refutes the loose charges made by some that the classifications are a giant racket for defrauding the insuring public, and discloses that misclassification is a result of human error arising in the struggle of a large industry to adapt itself to a difficult process."

It is difficult to understand why a company would deliberately risk its reputation and its right to do business by engaging in illegal practices. The insurance departments have the right to revoke the license of any company that violates the law. The legal officers of each state surely have the right to bring criminal prosecution against parties found guilty of criminal practices.

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29 The United States Senate, Hearing, op. cit., August, 1958, p. 481.
In Conclusion

It is the opinion of this writer, without making any attempt to justify the activities of the finance affiliates, that the latter were singled out to bear the brunt of fault and of the publicity attendant to the investigations, particularly in the earlier stages of the scandal disclosure. Service Fire first drew attention to this segment of the industry. The activities of the NABBB and its distribution of the September, 1956, bulletin, naming the finance affiliates and no other companies, tended to further the emphasis and attention placed on the finance affiliates.

The evidence brought out in the hearings would tend to indicate that some jurisdictions seemingly confined their investigations solely to companies which had been named in the NABBB bulletin. Other states, having declared conclusively that misclassifications did not exist within their confines, would never have known otherwise had it not been for the action of the finance affiliates in making refunds in those states.

The charges of the NABBB and of some of the state insurance departments cannot be dismissed lightly. There was no doubt some evidence which would indicate that there were some deliberate, illegal practices existing.
The evidence points to the fact that certain of the finance companies were guilty of misclassifications on a large scale, and undoubtedly on a larger scale than any other segment of the industry. This is attributable to their method of distribution and to nationwide coverage and their large volume of physical damage business.

In states where investigations were more complete, many companies were uncovered. In the balance of the states, the limelight seems to have been placed so completely on the companies charged in the NABBB bulletin, that they were generally picked as the scapegoats, rightfully so, but not to the exclusion of mentioning other companies involved. The general quality of investigations conducted by many states can attest to no other conclusion. Some states were greatly handicapped by lack of funds and personnel, and their comparative lack of action can perhaps be understood.

In the final analysis it would seem apparent that of all the people in the United States who were wrongfully overcharged for their automobile insurance coverage because of misclassification, many have not received refunds. Because of the lateness of the day, it is further apparent that many will never receive refunds. Part of this is due to the fact that some people cannot be located, and a large part is due to the inherent difficulties of media of communication. It is safe to say
that some companies and some agents which practiced misclassification were never discovered, and it is not unreasonable to assume that some companies that have contacted their policyholders have probably done an incomplete job in circularization of inquiry letters and refunding of overcharges.

The large finance affiliates themselves are surely not proud of the misclassification scandal and hope that they have corrected their practices so that there can be no future repetitions.

About all that can be said about the whole affair is that although the refunds are probably not complete, the attention focused on the entire matter has resulted in rating and underwriting reforms and has produced a more vigilant attitude on the part of insurance departments and insurance companies alike, with the realization that federal regulation is hovering near if the states and the companies fail to protect the general public.
CHAPTER IX

AFFILIATE GROWTH AND DECLINE

Introduction

It is apparent from the preceding chapters that the finance affiliates enjoy a peculiar competitive advantage arising out of their ability to keep down operating costs. The most significant of these operating costs is that of acquisition expenses. By avoiding the insurance agent in the insurance transaction, the affiliates are able to save approximately 25 per cent of net premiums written, which would otherwise be paid out in commissions and brokerage fees.

This ability to by-pass the insurance agent in the distribution of insurance is essential to the affiliates' entire method of operation. By automatically acquiring insurance business from the affiliated sales finance companies, the affiliate will most likely continue to prosper, provided that the sales finance company itself continues to acquire automobile sales finance business. If the source of that insurance volume should fail, wholly or in significant part, to provide the business, the
affiliate cannot help but fail unless it drastically modifies its methods of operation.

This chapter examines the business volume growth or decline of the large affiliate groups and compares them to the business volume growth or decline of 31 other stock company insurance groups.

In addition, the business volume relationship of the affiliates and their sales finance companies are explored. Specifically, of all of the automobiles which are financed by the sales finance company, what per cent are now being insured by the affiliate? Even more important, is this business penetration percentage of the sales finance company insurance potential increasing, or is it decreasing? Only by examining the business volume picture of the affiliates together with their operating figures is it possible for the reader to gain insight into the complete competitive situation of the affiliates.

Physical Damage Insurance Volume

Volume Growth—The Stock Industry

Table 16 shows the automobile physical damage insurance net premium volume for stock companies on a group
basis for the years 1955 through and including 1957.
Total net premiums written by the thirty five insurance
groups which are represented increased from the 1955 figure
of 857,120,000 to a record high of 1,352,583,000 in 1956;
fell to 1,203,556,000 in 1957; and gathered strength in 1957
to end the year with a total volume of 1,506,684,000. The
1957 volume figure represents a 30 per cent increase over
the 1956 figure.

Individual group gains in premium volume were
significant. For example, eight groups show premium volume
increases of 50 per cent or more from 1956 to 1957 inclusive.
These are Aetna Life, with 60 per cent increase, repre­
senting an added premium volume of $12 million over the
1956 figure; Employers, with 70 per cent and 64.3 million
increase; Travelers, 75 per cent and 633.6 million; General
Accident, 87 per cent and 6.5; General America, 107 per
cent and 99.4 million increase; and United States Fidelity
and Guaranty Company, showing an increase of 192.2 million
and an impressive 211 per cent.

The most phenomenal increase in volume, however, was
that recorded by Allstate. With a net premium volume of
$211.2 million in 1956, volume skyrocketed to 334.7 million
in 1957, representing an increase of 964 million for a
percentage increase of 908 per cent over 1956 figures.
TABLE 16

AUTOMOBILE PHYSICAL DAMAGE
NET TURBULUM VOLUME, 1950-1957
STOCK COMPANY GROUP BASIS

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Aetna Insurance</td>
<td>10,238</td>
<td>11,167</td>
<td>11,659</td>
<td>15,169</td>
<td>12,105</td>
<td>11,905</td>
<td>11,404</td>
<td>11,668</td>
</tr>
<tr>
<td>Aetna Life</td>
<td>19,169</td>
<td>20,713</td>
<td>23,268</td>
<td>25,473</td>
<td>24,266</td>
<td>25,625</td>
<td>26,343</td>
<td>31,030</td>
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<tr>
<td>Allstate</td>
<td>21,222</td>
<td>25,969</td>
<td>30,230</td>
<td>51,198</td>
<td>56,638</td>
<td>72,631</td>
<td>75,909</td>
<td>84,734</td>
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<tr>
<td>America Fore</td>
<td>30,379</td>
<td>32,698</td>
<td>31,003</td>
<td>23,650</td>
<td>27,421</td>
<td>27,854</td>
<td>25,196</td>
<td>29,457</td>
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<td>American of Newark</td>
<td>10,340</td>
<td>10,842</td>
<td>11,049</td>
<td>10,914</td>
<td>10,143</td>
<td>23,180</td>
<td>26,668</td>
<td>27,133</td>
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<td>American Associated</td>
<td>14,684</td>
<td>14,746</td>
<td>14,514</td>
<td>15,117</td>
<td>15,526</td>
<td>12,024</td>
<td>11,605</td>
<td>12,159</td>
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<tr>
<td>Chubb &amp; Son</td>
<td>10,611</td>
<td>10,790</td>
<td>13,551</td>
<td>14,374</td>
<td>11,022</td>
<td>12,024</td>
<td>11,605</td>
<td>12,159</td>
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<tr>
<td>*Commercial Credit</td>
<td>32,295</td>
<td>34,757</td>
<td>46,042</td>
<td>42,535</td>
<td>24,085</td>
<td>30,088</td>
<td>23,662</td>
<td>24,613</td>
</tr>
<tr>
<td>*Commercial Inv. Trust</td>
<td>57,904</td>
<td>57,456</td>
<td>74,054</td>
<td>67,819</td>
<td>22,778</td>
<td>60,925</td>
<td>47,565</td>
<td>45,574</td>
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<tr>
<td>Crum &amp; Forster</td>
<td>6,321</td>
<td>5,142</td>
<td>6,775</td>
<td>8,170</td>
<td>7,764</td>
<td>6,831</td>
<td>7,312</td>
<td>9,432</td>
</tr>
<tr>
<td>*Eunoico</td>
<td>19,054</td>
<td>21,237</td>
<td>30,749</td>
<td>25,962</td>
<td>25,691</td>
<td>31,340</td>
<td>29,907</td>
<td>25,203</td>
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<tr>
<td>Employers</td>
<td>6,618</td>
<td>7,541</td>
<td>7,721</td>
<td>7,997</td>
<td>7,668</td>
<td>8,632</td>
<td>9,513</td>
<td>11,253</td>
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<td>The Fund</td>
<td>17,591</td>
<td>19,161</td>
<td>23,705</td>
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<td>18,639</td>
<td>19,315</td>
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<td>General Accident</td>
<td>7,126</td>
<td>8,171</td>
<td>9,050</td>
<td>10,572</td>
<td>10,886</td>
<td>10,822</td>
<td>10,909</td>
<td>15,376</td>
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<td>General America</td>
<td>9,541</td>
<td>10,565</td>
<td>12,445</td>
<td>13,175</td>
<td>13,663</td>
<td>19,610</td>
<td>18,700</td>
<td>18,697</td>
</tr>
<tr>
<td>*General Motors</td>
<td>127,763</td>
<td>112,038</td>
<td>147,442</td>
<td>166,138</td>
<td>168,930</td>
<td>200,289</td>
<td>181,528</td>
<td>180,581</td>
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<tr>
<td>Glens Falls</td>
<td>7,081</td>
<td>6,404</td>
<td>10,000</td>
<td>10,504</td>
<td>6,344</td>
<td>7,922</td>
<td>7,273</td>
<td>8,761</td>
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<tr>
<td>Great American</td>
<td>11,256</td>
<td>12,459</td>
<td>13,366</td>
<td>17,521</td>
<td>12,705</td>
<td>12,733</td>
<td>12,108</td>
<td>13,605</td>
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<tr>
<td>Hartford</td>
<td>21,360</td>
<td>24,351</td>
<td>37,694</td>
<td>40,707</td>
<td>36,932</td>
<td>35,646</td>
<td>34,544</td>
<td>36,356</td>
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<td>Home (N.Y.)</td>
<td>19,962</td>
<td>21,940</td>
<td>21,241</td>
<td>21,645</td>
<td>18,430</td>
<td>20,139</td>
<td>15,705</td>
<td>19,091</td>
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<tr>
<td>Insurance of N.A.</td>
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<td>14,002</td>
<td>16,193</td>
<td>16,205</td>
<td>16,099</td>
<td>15,296</td>
<td>15,471</td>
<td>16,931</td>
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TABLE 16
(Continued)

<table>
<thead>
<tr>
<th></th>
<th></th>
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<th></th>
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<tbody>
<tr>
<td>Loyalty</td>
<td>14,036</td>
<td>14,823</td>
<td>18,624</td>
<td>15,915</td>
<td>16,509</td>
<td>17,617</td>
<td>17,356</td>
<td>18,923</td>
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<td>Maryland Casualty</td>
<td>8,893</td>
<td>9,497</td>
<td>10,845</td>
<td>12,272</td>
<td>11,928</td>
<td>18,062</td>
<td>18,295</td>
<td>15,124</td>
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<td>5,702</td>
<td>5,935</td>
<td>6,488</td>
<td>7,152</td>
<td>7,046</td>
<td>7,199</td>
<td>7,937</td>
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<td>9,991</td>
<td>12,126</td>
<td>14,074</td>
<td>12,713</td>
<td>12,573</td>
<td>14,484</td>
<td>14,055</td>
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<td>Pacific (N.Y.)</td>
<td>8,172</td>
<td>8,099</td>
<td>9,474</td>
<td>10,611</td>
<td>9,461</td>
<td>9,397</td>
<td>8,372</td>
<td>9,069</td>
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<td>Pacific Indemnity</td>
<td>5,804</td>
<td>5,591</td>
<td>5,061</td>
<td>4,583</td>
<td>4,855</td>
<td>4,465</td>
<td>4,606</td>
<td>5,546</td>
</tr>
<tr>
<td>Phoenix of Hartford</td>
<td>13,418</td>
<td>14,014</td>
<td>20,169</td>
<td>16,346</td>
<td>12,411</td>
<td>11,901</td>
<td>11,179</td>
<td></td>
</tr>
<tr>
<td>Resolute</td>
<td>14,083</td>
<td>17,590</td>
<td>20,473</td>
<td>13,724</td>
<td>16,113</td>
<td>15,610</td>
<td>16,228</td>
<td></td>
</tr>
<tr>
<td>St. Paul</td>
<td>15,937</td>
<td>14,466</td>
<td>15,455</td>
<td>15,665</td>
<td>14,742</td>
<td>12,350</td>
<td>15,318</td>
<td>17,298</td>
</tr>
<tr>
<td>Springfield</td>
<td>6,108</td>
<td>5,810</td>
<td>6,757</td>
<td>6,976</td>
<td>5,610</td>
<td>5,737</td>
<td>4,490</td>
<td>4,331</td>
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<tr>
<td>Transamerica</td>
<td>13,297</td>
<td>11,199</td>
<td>16,000</td>
<td>15,708</td>
<td>15,178</td>
<td>11,455</td>
<td>8,996</td>
<td>8,112</td>
</tr>
<tr>
<td>Travelers</td>
<td>31,044</td>
<td>36,221</td>
<td>42,033</td>
<td>46,999</td>
<td>43,189</td>
<td>40,217</td>
<td>43,583</td>
<td>55,555</td>
</tr>
<tr>
<td>U.S. Fidelity &amp; Guar.</td>
<td>2,054</td>
<td>14,594</td>
<td>22,721</td>
<td>24,605</td>
<td>23,725</td>
<td>24,405</td>
<td>24,245</td>
<td>28,528</td>
</tr>
<tr>
<td><strong>TOTALS</strong></td>
<td>657,190</td>
<td>671,914</td>
<td>820,063</td>
<td>833,334</td>
<td>791,850</td>
<td>890,559</td>
<td>807,856</td>
<td>856,624</td>
</tr>
</tbody>
</table>

Individual group volume increase or decrease since 1950 is indicated in Table 17.

The Finance Affiliates

Meanwhile, the four finance affiliate groups represented in Table 10 showed no consistency in growth pattern, except that they all fell below the industry average volume increase of 30 per cent. The General Motors' affiliates showed up very well with an impressive increase of $32.6 million in volume, but since they were already writing $127.7 million in 1950, this represented a percentage increase of only 20 per cent. Banko showed an increase of $4.2 million, or 22 per cent over 1950 figures. The other two affiliates, however, showed drastic reductions in volume while the stock group industry volume was advancing. Commercial Credit Company's affiliates, Calvert Fire Insurance Company and Cavalier Insurance Company, dropped $3.1 million, representing a decrease of 25 per cent in volume. The CIT affiliates, Service Fire Insurance Company of New York and Service Casualty Insurance Company of New York, fell $12.5 million in volume, or a decrease of 22 per cent from 1950 volume.

Since two of the affiliates have shown an appreciable growth in business volume during the past seven years,
### TABLE 17

**AUTOMOBILE PHYSICAL DAMAGE**

**NET PREMIUM VOLUME, GROWTH & DECLINE, 1950-57**

**STOCK COMPANY GROUP BASIS**

<table>
<thead>
<tr>
<th>Groups</th>
<th>Volume Increase or Decrease Since 1950</th>
<th>In Billions</th>
<th>Percentage of Dollars</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Aetna Insurance</strong></td>
<td></td>
<td>1.5</td>
<td>14</td>
</tr>
<tr>
<td><strong>Aetna Life</strong></td>
<td></td>
<td>12.0</td>
<td>60</td>
</tr>
<tr>
<td><strong>Allstate</strong></td>
<td></td>
<td>84.0</td>
<td>300</td>
</tr>
<tr>
<td><strong>America Fore</strong></td>
<td></td>
<td>-7.0</td>
<td>-19</td>
</tr>
<tr>
<td><strong>American of Newark-Assoc.</strong></td>
<td></td>
<td>1.9</td>
<td>6</td>
</tr>
<tr>
<td><strong>Chubb &amp; Son</strong></td>
<td></td>
<td>1.4</td>
<td>15</td>
</tr>
<tr>
<td><strong>Commercial Credit</strong></td>
<td></td>
<td>-8.1</td>
<td>-22</td>
</tr>
<tr>
<td><strong>Commercial Inv. Trust</strong></td>
<td></td>
<td>-12.5</td>
<td>-22</td>
</tr>
<tr>
<td><strong>Crinn &amp; Forster</strong></td>
<td></td>
<td>2.5</td>
<td>36</td>
</tr>
<tr>
<td><strong>Elmico</strong></td>
<td></td>
<td>3.2</td>
<td>22</td>
</tr>
<tr>
<td><strong>Employers</strong></td>
<td></td>
<td>4.6</td>
<td>70</td>
</tr>
<tr>
<td><strong>The Fund</strong></td>
<td></td>
<td>2.2</td>
<td>12</td>
</tr>
<tr>
<td><strong>General Accident</strong></td>
<td></td>
<td>9.3</td>
<td>17</td>
</tr>
<tr>
<td><strong>General America</strong></td>
<td></td>
<td>9.5</td>
<td>107</td>
</tr>
<tr>
<td><strong>General Motors</strong></td>
<td></td>
<td>32.6</td>
<td>26</td>
</tr>
<tr>
<td><strong>Glens Falls</strong></td>
<td></td>
<td>1.7</td>
<td>24</td>
</tr>
<tr>
<td><strong>Great American</strong></td>
<td></td>
<td>2.5</td>
<td>22</td>
</tr>
<tr>
<td><strong>Hartford</strong></td>
<td></td>
<td>7.2</td>
<td>23</td>
</tr>
<tr>
<td><strong>Home (I.A.)</strong></td>
<td></td>
<td>-1.9</td>
<td>-4</td>
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<tr>
<td><strong>Insurance of N.A.</strong></td>
<td></td>
<td>5.0</td>
<td>22</td>
</tr>
<tr>
<td><strong>Loyalty</strong></td>
<td></td>
<td>4.9</td>
<td>35</td>
</tr>
<tr>
<td><strong>National of Hartford</strong></td>
<td></td>
<td>6.2</td>
<td>70</td>
</tr>
<tr>
<td><strong>Northern (I.A.)</strong></td>
<td></td>
<td>2.3</td>
<td>31</td>
</tr>
<tr>
<td><strong>Ohio Casualty</strong></td>
<td></td>
<td>4.9</td>
<td>53</td>
</tr>
<tr>
<td><strong>Pacific (I.A.)</strong></td>
<td></td>
<td>4.9</td>
<td>11</td>
</tr>
<tr>
<td><strong>Pacific Indemnity</strong></td>
<td></td>
<td>-1.9</td>
<td>-5</td>
</tr>
<tr>
<td><strong>Phoenix of Hartford</strong></td>
<td></td>
<td>3.4</td>
<td>41</td>
</tr>
<tr>
<td><strong>Resolute</strong></td>
<td></td>
<td>-5.2</td>
<td>-32</td>
</tr>
<tr>
<td><strong>Royal-Globe</strong></td>
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<td>5.2</td>
<td>21</td>
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<tr>
<td><strong>St. Paul</strong></td>
<td></td>
<td>5.4</td>
<td>24</td>
</tr>
<tr>
<td><strong>Springfield</strong></td>
<td></td>
<td>-1.2</td>
<td>-20</td>
</tr>
<tr>
<td><strong>Transamerica</strong></td>
<td></td>
<td>-5.7</td>
<td>-41</td>
</tr>
<tr>
<td><strong>Travelers</strong></td>
<td></td>
<td>23.8</td>
<td>75</td>
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<tr>
<td><strong>U.S. Fidelity &amp; Guaranty</strong></td>
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<td>19.2</td>
<td>211</td>
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</tbody>
</table>

*Source: Figures from Table 16.*
while the other two have experienced a considerable volume decline, there is a divergence of opinion among executives of the affiliates relative to the competitive position of the affiliates in the insurance industry.

One school of thought believes that the sales finance company insurance affiliate is holding up very well against competition. Although the individual company is not commanding the same proportional share of the market as it had in the past, volume has nevertheless increased, and this is all that can be expected.

The other school views with increasing alarm what is characterized as a deterioration in the affiliates' competitive position. Since the affiliates' share of the market is decreasing, these companies are looking for means by which the situation can be improved. They believe that the affiliates' insurance market is volatile and that serious problems must be solved by this type of insurer.

Affiliate Dependence Upon the Automobile Industry

One of the aspects of volatility is the nature of the insured property itself, the automobile. Since the automobile sales finance companies rely upon the financing of automobiles for their income, their volume of business
is directly tied up with the volume of automobiles sold and financed each year. The insurance affiliates in turn depend upon the volume of business of the sales finance company. There are, however, a number of variables which enter into these relationships.

The most important variables are the percentage penetration of a given sales finance company into the total financed automobile business and the percentage penetration of the affiliate into the business financed by the finance company. In other words, it is possible to establish a correlation between the business of the sales finance company and the total automobile sales finance business done in a given year, provided that the company's share of the market does not change.

It was observed in an earlier chapter that with the entry of the commercial banks into the automobile finance business, that the percentage participation of the sales finance companies in financed automobile business has decreased.

Likewise, the insurance business volume of the insurance affiliate can be correlated with an increase or decrease in sales volume of the automobile business, provided that the volume of the affiliated automobile sales finance company remains constant, and provided that the insurance affiliate's share of the business of the finance
company remains constant. It has been seen that the first supposition does not exist in fact, nor does it exist in the second case.

It would be logical to suppose that the insurance affiliate would write a large percentage of the automobile insurance on the automobiles financed by the affiliated finance company. As a matter of fact, this is one of the complaints made by the various agents associations—that the finance affiliates have captive customers who are forced to obtain their insurance from the affiliates of the sales finance company. Charges of coercion have frequently been lodged against the finance affiliates.

A decreasing share of business. When the insurance affiliates were first organized, they wrote most of the insurance on the automobiles financed by the sales finance companies with which they were affiliated. This was to be expected, since no other insurance companies wished to touch this class of insured. Through the years, however, there has been an increasing realization by other insurers that not all of the financed automobile insurance business is bad. Thus, there have been ever-increasing efforts exerted on the part of the other insurers to take over some of the
better financed automobile risks hitherto written exclusively by the affiliates.

For example, one of the large finance affiliates wrote in excess of 70 per cent of all of the automobiles financed by its affiliated finance company a decade ago. This penetration has fallen to 60 per cent on new automobiles and 50 per cent on used automobiles.

This reduction of penetration has been even more marked in the case of other large affiliates. One company wrote in excess of 60 per cent of the automobiles financed by the sales finance company a few years ago. The percentage of penetration has continually decreased through the years. In 1954 it was 86 per cent; 1955, 64 per cent; 1956, 54 per cent; 1957, 30 per cent; and in 1958, it fell to 50 per cent.

Another affiliate had a penetration of 79 per cent ten years ago. This penetration has decreased through the years as follows:

<table>
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<tr>
<th>Year</th>
<th>Penetration</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950</td>
<td>71.9</td>
</tr>
<tr>
<td>1951</td>
<td>73.3</td>
</tr>
<tr>
<td>1952</td>
<td>73.5</td>
</tr>
<tr>
<td>1953</td>
<td>69.3</td>
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<tr>
<td>1954</td>
<td>67.7</td>
</tr>
<tr>
<td>1955</td>
<td>67.0</td>
</tr>
<tr>
<td>1956</td>
<td>65.8</td>
</tr>
<tr>
<td>1957</td>
<td>61.0</td>
</tr>
<tr>
<td>1958</td>
<td>54.0</td>
</tr>
</tbody>
</table>

Today, the finance affiliates are writing only half of the business which is financed by their affiliated finance companies. The percentage of penetration is continually
decreasing. Accompanying this decreased penetration has been a drop in business volume experienced by some of the finance affiliates.

The concluding chapter of this study examines some of the significant reasons for this decreased business penetration. In addition, comments are made of some of the things which are being done and which should be done by the managements of the insurance affiliates to attempt to remedy what appears to be a market deterioration.
Certain affiliate business practices are unique and worthy of mention. These practices and related problems are discussed in this chapter.

**Distribution Methods**

The affiliates have been criticized for their method of insurance distribution. Organizations such as the National Association of Casualty and Surety Agents have worked hard to force a severance of connections between finance companies and insurance companies or agencies.

**Agents' Resentment**

Agents resent the fact that the affiliates do not use regular insurance agents, but rather, contact the insured through automobile dealers.

The dealers, the finance companies, and the affiliates do not consider the dealer as a seller of insurance.
The dealer is a purchaser under the "True Price Doctrine." Under this doctrine, the dealer, the finance company, and the insured all have an insurable interest in the automobile. The purchaser either authorizes the purchase of insurance by the dealer or by the dealer's assignee, or the purchaser may obtain the insurance himself. If the premium is included in the finance deal, the dealer has the right to buy the insurance. If he assigns the note to a finance company, the latter then has the right. Since the dealer and the finance company are insurance buyers, not sellers, there is no agency relationship.

Automobile Dealer Licensing

The question of the propriety of licensing automobile dealers as insurance agents has been in controversy for a number of years. Motors Insurance Corporation has appointed dealers as insurance agents since 1939 to act on behalf of the company. This has concerned the National Association of Insurance Agents who see in such a relationship a serious infringement of the traditional business province of the American agency system. Agents believe that a "captive" relationship exists and that coercive tactics, however subtle, are used by dealer-agents to induce the
automobile purchaser to obtain his insurance from the affiliated insurer.

All of the concern of the insurance agents is not in fear of automobile dealer competition. Agents are concerned that dealer licensing marks a dangerous precedent, marking a trend toward licensing all parties who finance automobiles or who sell appliances and other financed personal property.

Agents' associations have initiated litigation attempting to stop the practice of automobile dealer licensing.

The Ohio case. A case in point arose in Ohio in 1950 involving the Motors Insurance Corporation. The specific point in issue was whether or not the Ohio superintendent of insurance had authority to refuse to renew existing agents licenses to automobile dealers representing this insurer. The case turned upon the wording of an Ohio statute providing that a license was not to be used primarily to effect insurance on property for which the licensee is vendor. The automobile dealer was precluded from obtaining a license.

This law is peculiar to the state of Ohio. Three other states have statutes which prohibit automobile dealers from obtaining an agent's license.1

1Michigan, New York, and Massachusetts.
It is apparent that Motors Insurance Corporation, with its system of dealer-agents, enjoys a favorable competitive position. Some will argue that the company enjoys a monopoly. This is not the case, for Motors Insurance Corporation does not write all of the insurance on the automobiles financed by its affiliated finance company.

It was observed in the preceding chapter that the General Motors' affiliates had since 1950 increased their net premium volume some $32.6 million, representing a 26 per cent increase over the 1950 volume. Surely these insurers have no more of a captive business or better opportunity to market their product than does Allstate Insurance Company, with its booths set up strategically by doorways and escalators of the Sears retail stores. During the same period of time, Allstate showed a volume increase of $54 million, representing 300 per cent volume increase over the 1950 figures.

Should the Affiliates Pay an Agent?

Under their present method of doing business, the affiliates could not pay agents' commissions without
experiencing difficulties. It was observed that the affiliates have abnormally high loss and adjusting expenses. These are offset by unusually low underwriting expenses which are attributable to the fact that the usual agent's commission is not paid. If it were paid, such an increment to underwriting expenses would result in an untenable combined loss and expense ratio. The companies could not continue long with ratios approximating 110 per cent to 11.5 per cent of premiums. They would be faced with one of two alternatives: (1) drastic revisions would have to be made in underwriting policy to eliminate the poorer risks, or (2) the insurer would have to operate at a loss.

It has been noted that the finance business, too, is highly competitive. It is unlikely that the finance company could long afford to absorb the loss of its insurance affiliate. Consequently, a select underwriting program would have to be instituted by the insurer. This would necessitate dropping many of the so-called marginal risks from the company's portfolio.

Members of management of the finance affiliates estimate that 50 per cent of their business is undesirable from the ordinary underwriting viewpoint. If 50 per cent of the affiliates' business risks were dropped, who then would protect this uninsured collateral?
Substandard Companies

The substandard companies will write almost anything. They generally surcharge from 150 per cent to 200 per cent; some will run as high as 300 per cent. A marginal risk can obtain his insurance from the affiliate at standard rates. If he attempts to obtain his insurance from another company, other than an affiliate or a substandard company, he is rejected as undesirable. If he should apply for insurance at a substandard company, he would probably be accepted but would be surcharged as much as 500 per cent over standard rates. Thus, if the standard rate for physical damage insurance on his 1965 Ford automobile amounted to \$75, he would be charged \$280 by the substandard company. What effect might this have on his decision to purchase the automobile in the first place? Would he insure? If he did insure, would he cancel shortly after he had satisfied the requirements of the finance company?^2

The finance affiliates were organized originally to provide insurance protection on a collateral that no other company would insure. That purpose still exists in large part. Despite the existence of their insurance

^2An officer of at least one finance affiliate believes that the higher rates paid to substandard companies do not influence automobile purchasers in their decision to purchase a car. This view is not shared by the majority of members of management interviewed by the writer.
affiliates, sales finance companies are still losing hundreds of thousands of dollars per year on uninsured collateral. Finance accounts not insured by the affiliates are cancelled by other insurers as bad risks, or else the insured has allowed his policy to lapse or to be cancelled for non-payment of premiums.

If the affiliates did not exist, what effect would this have on the financing policy of the sales finance companies? It is not unreasonable to assume that greater restrictions would be placed on the financing of automobiles. The finance company, unable to obtain insurance protection, would refuse to sell on time to a large class of people who are undesirable insurance risks. What would happen to new and used car sales, with the resultant effect on the automobile manufacturing industry and on all related industries if this should happen? If the affiliates discontinued business, these questions would require answers.

Affiliate Services to the Public

General Services

The affiliates provide on-the-spot insurance protection. Affiliate proponents point out that it is characteristic of the automobile purchase transaction
to be consummated quickly. The automobile dealer does not know until the last minute that the sale has been made. When the customer decides to buy, the dealer must prepare the finance papers and see that there is insurance on the collateral. The customer wants his automobile right away. Although he may spend days in shopping for the right buy, once he has selected the automobile and made his decision to purchase, he wants to drive the automobile away. The insurance facilities are immediately available through the affiliate.

The purchaser is not inconvenienced with calling up an agent and with the necessity of paying the insurance premium. The premium is merely added to the contract amount and is paid on a monthly basis with the usual monthly automobile payment.

As an additional service, the finance company will often finance the cost of liability insurance. The purchaser may obtain this coverage from a liability insurer and the premium is added to the finance contract.

When an automobile purchaser negotiates for insurance from a non-finance insurer, a delay often occurs. Some institutions making instalment loans to consumers . . . have become acutely conscious of the time-consuming effort involved in handling the insurance phase of automobile lending . . . We distinctly recall an instance in which we found it necessary to engage in
five telephone conversations with a local agent in order to arrive at a complete understanding regarding insurance which a borrower wished to place with him.  

When there is such a delay, insureds will turn to the convenient facilities of the affiliate.

Regular agents can, and in many cases do, provide such excellent service that they need not fear affiliate competition. Where the agent is poorly serving his insureds, he will lose business to the affiliate. Affiliate insurance men cite instances where the affiliate has been accused of coercive practices, but where investigation revealed that the insured turned from his regular agent because the agent was not providing service.

Affiliate members of management do not fear competition afforded by the American agency system. Agents' criticism prompted one large affiliate to make a study in one state during World War II. When this company's insureds had discontinued their coverage with the affiliate after paying their finance account, insurance agents picked up only 15 per cent of this business.

The affiliates offer an advantage in another aspect of their operations. There is little danger that a policy

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will be cancelled by the affiliate. If the insured does not obtain his insurance from an affiliate, he may be unable to pay another company's annual premium. He either lapses or is cancelled for non-payment of premiums. With the premium included in his monthly payment on the automobile, he is more likely to keep up his payments. He needn't pay a large annual premium at a given time. Then, too, if he obtains his insurance from the affiliate, there is only a one per cent to three per cent chance that he may be cancelled for any reason. Affiliates' members of management point out that the rate of cancellation of other insurers is ordinarily higher.

Claim Services

Claim services rendered by the affiliates are generally superior to those afforded by other insurers.

Prompt adjustments. The affiliates attempt to settle claims with no delay. Emco Insurance Company, for example, gives 24-hour service in the vast majority of claims handled. Service Fire and Calvert Fire report

4 However, it is to be noted that several groups of non-finance insurers are also offering a monthly payment plan.
similar results. Specialized nationwide staff adjusting offices are maintained to give rapid local adjusting service.

Insurance companies vary considerably in promptness with which adjustments are made. Insurers relying on independent adjusters sometimes find that small losses involving automobile physical damage matters are relegated to secondary attention. Independent adjusters are inclined to give larger losses (e.g., residential or business fires) or liability matters precedence in settlement. The nationwide adjusting service of the affiliate should logically provide faster service. Some other insurers compare favorably since they likewise maintain nationwide staff adjusting offices.

Satisfactory repair work. The finance affiliates want the insured to be happy with the repair job on his automobile. A dissatisfied insured may discontinue paying on his finance contract. Consequently, the insured is allowed to take his damaged automobile to his own dealer where the parts for his automobile are readily available. The adjuster makes the estimate, and the automobile is repaired. If the job is not satisfactory, the claim is re-opened until the job is done properly.
To determine if the adjustment has been satisfactory, Service Fire Insurance Company of New York has adopted a routine control procedure. Spot check surveys are made. The home office sends out questionnaires to insureds after their claims have been settled, soliciting comments regarding the quality of the claim service rendered to them. Branch offices have no knowledge of what extent their claims are reviewed. Company officers report that complaints received run two per cent or less on claims handled. Most of these do not involve poor service on the part of an adjuster but are related to some aspect of the repair work. Complaints are quickly investigated and adjustments made where necessary.

In the opinion of the writer the routine solicitation of insureds' opinions relating to the quality of service rendered to them is unique in the automobile insurance industry as a whole.

Emergency financing. There is an area of claim service allied with the finance function of the sales finance companies which is unique to the finance affiliates. An insured is afforded emergency financing at the time of an accident. It can be illustrated in the following example:
We have a very bad physical damage claim, and the insured calls the company. Our man gets to him promptly. The adjuster immediately makes the estimate and pays on the coverage in excess of the insured's deductible. The insured is perhaps on his way on a vacation or on a business trip, and he has just enough money with which to cover his needs. To pay the deductible amount owing on his car repairs is going to leave him short. Consequently, the adjuster arranges with the company's nearest office to add the deductible to this man's account. The adjuster pays the deductible to the repair shop, and the insured is on his way.

The close relationship existing between the insurer and the sales finance company gives the insured a service not available from another insurer.

Automobile replacement. A service which is overlooked by some insurers is that of substitution of automobiles when a total loss occurs. Briefly, here is what happens: an accident destroys the insured's automobile. The insurer determines market value, relying upon National Automobile Dealers Association "blue book" values, sometimes revised up according to local situations, and adjusted for salvage value. The insurer will usually issue a draft to the insured with which he may presumably purchase another automobile.

Unfortunately, the insured will sometimes discover that he has no equity left in his automobile. Where the insured has recently purchased the automobile, most of his
initial payment has gone to insurance charges and to
initial loading. When the insurer settles the loss, it
designates the insured and the mortgagee as co-payees on
the draft. The loss payee, the mortgagee, takes most of
the proceeds and cancels the finance contract, leaving
the insured hurt and disillusioned.

The affiliates attempt to avoid this harsh result.
Service fire, for example, in most cases replaces the
destroyed automobile rather than making a cash settlement.
Although replacement is not mandatory for the insured, it
is highly recommended, and over 90 per cent of Service
fire's insureds have their automobiles replaced when there
has been a total loss. When the automobile is replaced,
the finance company merely substitutes the new automobile
for the old on the same finance contract.

Replacement is advantageous to the insured. He
needn't shop for another automobile, finance it, and pay
the initial charges over again. Furthermore, there is
assurance that he will be satisfied with the replacement
automobile. The finance company that finances the dealer
wishes to make certain that the security is sound and that
the insured is satisfied so that he will pay his finance
account. Under the circumstances, the dealer is usually
anxious to satisfy the insured.
Competition of the Affiliate

The finance affiliates now face the most difficult competitive situation in their history. The typical affiliate has limited its market to automobiles financed by the affiliated sales finance company. Year after year, the affiliate has obtained a decreasing percentage of the volume of business financed by the finance company. Many years ago, the affiliate could expect to write policies from 70 per cent to 80 per cent of all the contracts financed by the sales finance company. In the past decade the penetration has receded to a point where in some instances it is below 50 per cent. This situation has resulted from a number of significant factors.

Price and Advertising Competition

The affiliates did much to generate public awareness to the automobile physical damage coverages. This trend of itself has generated business for these insurers. It has also attracted other companies to write automobile physical damage coverages. Other insurers have prospered by aggressive advertising and by offering the same coverages at less cost to the public. This has cut serious inroads into business historically belonging to the affiliates. Insurers such
as Allstate, State Farm Mutual, and Nationwide have expended millions of dollars per year in fantastic advertising campaigns. The public has come to identify automobile insurance with the names of these companies.

**The Commercial Banks**

Commercial banks have steered business away from the finance affiliates. Whereas the sales finance companies originally handled almost all of the automobile paper, the commercial banks now handle an almost identical share. Business which does not go to the sales finance company does not go to the insurance affiliate. Had the commercial banks remained out of this field of financing, the affiliates would undoubtedly be writing a larger volume of insurance.

**Popularization of the Automobile Liability Coverages**

Perhaps the worst development from the affiliates' viewpoint has been the widespread generation of public awareness and the popularization of the automobile liability coverages. With the advent of laws requiring liability insurance, the liability companies have prospered. This alone would not bother the affiliates if automobile liability
insurance policies were sold alone. However, the public has been educated to buy all of its automobile insurance needs in a combination policy. Why purchase automobile insurance from two companies, with resultant confusion and inconveniences, when it is possible to obtain both automobile physical damage and liability coverages in a single policy administered by a single company? This type of thinking has been deleterious to the affiliates, for they offer only automobile physical damage insurance.

In Conclusion

The insurance industry, now more than it has for several decades, is undergoing a metamorphosis. In a business characterized by rapid changes in recent years, the insurance affiliates of sales finance companies are confronted by problems which require solutions in the years to come. How they respond to the challenge presented will determine their future in the insurance industry and in the eyes of the American public.
The invention of the automobile introduced a new industry to the American scene. With it came the need for financing. Commercial banks and investment bankers were the only potential source of funds to finance the automobile manufacturer, dealer, and consumer. The conservative banks did not wish to enter the highly speculative area of automobile financing. The sales finance companies came into being to provide the much-needed service.

Sales finance companies sought insurance protection for their finance collateral, the automobile. Existing insurers would provide coverage only on the more select risks, and when losses occurred, they were quick to cancel.

The sales finance companies were faced with the prospect of having much unsecured credit on their hands. Unable to rely on existing insurers, they made other arrangements. They either purchased existing insurance companies or organized insurance subsidiaries to provide the necessary protection.
The insurance affiliates of sales finance companies constitute a unique segment of the insurance industry. Consisting of approximately 40 insurers, they write 25 per cent of the automobile physical damage insurance written by all stock companies (539 companies) and 20 per cent of all such coverage written by the industry (including an additional 215 mutual companies).

The bulk of the affiliates' business is written by a few companies. Eight insurers write 50 per cent of the total volume while two of those companies write one-half of total affiliate business.

An affiliate's size and the extent of its area of distribution is generally related to its age. The large firms typically write in all or almost all states and were organized before World War II. The smaller firms were generally organized since the war and typically do business in less than twelve states.

The majority of the affiliates limit their business to the writing of automobile physical damage insurance only, which bears out the fact that the affiliate is an adjunct to the business of the sales finance company. The typical finance affiliate presents the enigma of an insurance company which apparently does not underwrite its risk. This is
because its primary concern is to accommodate the sales finance company by insuring the credit collateral which secures the finance transaction. Where other insurance companies are continually attempting to upgrade their risks by becoming more selective, specifying prohibited risks, and cancelling out insureds with adverse experience, the affiliate writes everything that the finance company finances. It cancels a very small percentage of its business.

Affiliate Operating Experience

The claims losses of the typical finance affiliate run appreciably higher than those of the industry. This is caused by a higher claim frequency per number of insureds. The affiliates insure a large portion of poor risks which are not acceptable to other insurers. Under the present method of operation, this situation is inevitable, for the affiliates insure the business financed by their affiliated sales finance companies. The adverse loss experience is a matter of concern, and the insurers are seeking solutions to remedy the situation. This is discussed later in this chapter.
Affiliates' adjusting expenses run higher than the industry averages. This is due to three factors: First, the affiliates handle only automobile physical damage insurance. Part of the claims expense cannot be apportioned to other automobile lines which are adjusted concurrently with the physical damage lines. Secondly, the adjuster spends more time on claims when he makes his own estimate. Thirdly, affiliates' branch offices are typically claims offices, and their overhead will unduly influence adjusting expense figures.

Adjusting expense figures of the affiliates attributable to automobile physical damage insurance can be reduced by handling all automobile lines. The additional time spent by the adjuster in making his own estimates cannot be avoided; however, this activity results in a savings in claims losses and is offset. Affiliate branch offices are devoted almost exclusively to the performance of claims functions because sales and underwriting activities are relatively insignificant to the affiliate.

Underwriting expenses of the typical affiliate are low. The most significant reason is that the usual agents' commissions are not paid. The insurer obtains business from automobile dealers. When an automobile purchaser desires financing, he is required to obtain physical damage insurance to protect the automobile. He may obtain his
insurance from any company. If he has no preference, the insurance affiliate of the stock finance company writes the coverage. The only commission which must be paid by the affiliate is a counter-signature commission to a resident agent.

The typical finance affiliate made money during 1957. adverse loss experience and high adjusting expenses were offset by low underwriting expenses, and underwriting profits resulted. The majority of other stock insurers lost money. Although other insurers have better loss experience and lower adjusting expenses, higher underwriting expenses caused them to sustain an underwriting loss. Automobile premium rates have been inadequate in the past two or three years. With the recent rate increases the stock industry as a whole should experience underwriting profits, and the profits of the affiliates should be correspondingly higher.

The Misclassification Furore

Two United States Senate subcommittee hearings resulted from a scandal which shocked the insurance industry and caused bad publicity for insurers involved. It was discovered in 1954 that some companies had misclassified
insureds on automobile physical damage insurance. Insurance examiners estimated that total overcharges might exceed $25 million. A number of the affiliates were involved, and they bore the brunt of accusations made by state and federal regulatory authorities and by various insurance and business associations.

The investigations which ensued were marked by incomplete information, avoidance of the subject by some quarters, and by inconsistencies in the testimony given. However, certain conclusions can be drawn.

Missclassifications did occur, and the amount of overcharges involved was of huge proportions. As of April 30, 1959, refunds were made to policyholders totaling over $10 million.

Certain of the sales finance company insurance affiliates were extensively implicated. They have readily admitted that they did overcharge.

The writer believes that the investigations conducted by most of the state insurance departments were far from adequate. Some states seem to have limited their investigations to the finance affiliates. The latter were picked as scapegoats and rightfully so; however, there is definite evidence that companies other than the finance affiliates were involved. They, too, should have been implicated.
Remedial activity has not been entirely satisfactory. Refunds are probably far from complete. However, the attention focused on the scandal has resulted in rating and underwriting reforms. It has also resulted in a more vigilant attitude on the part of insurance departments and insurance companies alike, with the realization that federal regulation is imminent if the states and the companies fail to protect the general public.

**Affiliate Practices**

Certain business practices of the affiliates are unique and are worthy of mention. The affiliates' claim service and their distribution method are discussed.

**Claim Service**

The affiliates render a claim service which is generally superior to that afforded by other companies. Claims are settled for a smaller average amount than is true for other stock insurers. This is largely due to the fact that the affiliate's adjuster is experienced and trained in estimating automobile damages, and he makes his own estimate of the insured's damages. This adjusting
practice is unique in the insurance industry. By knowing the extent of the damage, the adjuster can arrive at a more proper figure than if he leaves it up to the insured to obtain two or more estimates of damage from repair shops. This claim procedure is also intrinsically speedier than that of other insurers. Since he makes his own estimate, the affiliate's adjuster can get the automobile repair job started faster. Other companies usually allow more time to elapse while they are waiting for two or more estimates to be made.

**Distribution Method**

The finance affiliates have been criticized for their marketing methods. The typical affiliate either does not use insurance agents at all or it procures business through automobile dealer-insurance agents. In either case, the American agency system insurance agent is by-passed. The agent is concerned because he would like the opportunity to insure the better risks among financed automobile insureds. The agent believes that the finance affiliates have created a monopoly for themselves. They believe that coercive tactics, however subtle, are used by automobile dealers to induce the automobile purchaser to obtain insurance from the affiliated insurance company.
Undoubtedly, some coercion does take place. However the affiliates do not possess a monopoly on the insurance written on automobiles financed by their affiliated sales finance companies. When they were first organized, they wrote most of the insurance on the automobiles financed by these firms. Today, they write only half of this business, and the percentage of penetration is continually decreasing.

The Affiliates and the Future

The affiliates are concerned with the deterioration of business. This is marked by: (1) a decrease in percentage penetration of business in the total automobiles being financed by the affiliated sales finance companies and (2) a poorer quality of insured risk. There is a move on to obtain more business and to obtain a better quality of business.

More Business

Competition faced by the affiliate has never been more intense than it is today. It has resulted from a number of significant factors. Companies writing at lower premiums accompanied by ambitious advertising campaigns
have taken business from the affiliates. Although commercial banks originally would not finance automobile paper, they now handle as much as do the sales finance companies. This affects the affiliates, for business which does not go to its sales finance company, does not go to the insurance affiliate. Public awareness of the automobile liability coverages has been generated largely by the advent of laws requiring liability coverage. The public has been educated to buy a combination policy which includes the physical damage and liability coverages. Since the affiliates offer only physical damage coverage, their business has been hurt as customers seek to deal with only one insurer.

The most obvious development among the finance affiliates to hedge against the future has been the move toward multiple-line underwriting. With some companies this was a stop-gap measure used to tide the companies over the lean war years. Automobiles were not being produced. There was little business and what business was available was bad.

There is now serious consideration being given to re-entering these fields. Some of the affiliates have relatively inactive sister insurers available should the members of management decide to enter multiple-line underwriting. Other companies have been working energetically
toward multiple-line underwriting by attempting to be licensed for multiple-line business wherever possible. If the decision is made to diversify, the framework and machinery will be available when and where needed.

Some affiliates have begun to diversify. Finance affiliate tie-ups make it possible for the automobile purchaser to obtain automobile physical damage insurance, credit life insurance, and accident and health insurance.

With the increasing popularity and public acceptance of the combination automobile policy, there has been considerable speculation among the affiliates regarding the desirability of writing the automobile liability coverages. Such a step would pose two problems: (1) the need to establish liability claim facilities; and (2) the problem of undesirable risks.

Affiliate members of management believe that liability claim facilities could be established if necessary by adding liability adjusters to the present claim organization. The problem of undesirable risks poses a more serious question.

**Better Insureds**

If automobile liability lines are to be written, a better class of insured is desirable. It is to be remembered
that affiliate business includes a large segment of marginal risks. With these risks the claim potential can be estimated with some degree of accuracy with the physical damage coverages. Claim frequency and monetary exposure are known. The liability coverages present a frightening unknown when marginal risks are insured. Nevertheless, as public acceptance of the combination policy grows, the affiliates will probably be forced to write the liability coverages.

Some affiliates are working with agents. What agency business is available is favored. Affiliate men believe that agents perform more selective underwriting. Unfortunately, little automobile physical damage insurance business is available through agents at the present time. Agents want to sell combination policies, and the affiliates do not offer combination policies.

The affiliates are interested in automobile merit rating. It is believed that the philosophy behind merit rating is good. The basic idea of giving the insured a premium discount for safe driving and surcharging the unsafe driver is sound. If it can be worked out, the increased premium on the marginal risk would be favorable. Because of increased premiums and the finance affiliates' low expense ratio, the affiliates could compete well.
Some finance affiliates favor a strict underwriting policy—the adoption of prohibited lists of undesirable classes of drivers and types of automobiles as well as the establishment of more strict personal qualifications with respect to applicants. Since there is a need to accommodate the finance business of the affiliated sales finance company, the poor risks would be required to obtain their insurance from companies which write substandard business. Some companies have reported unsuccessful results with this suggestion. The management of at least one affiliate believes that it has worked so well that the company is considering forming a companion insurer to write substandard business.

In Perspective

In the opinion of this writer the typical finance affiliate is doing a commendable job in providing a highly essential service to the American public. The affiliate is providing insurance protection and a high quality of service at a premium which is competitive with rates of many companies now offering the same type of insurance.

The affiliates are continuing to make money although other automobile insurers are losing money. With major
revisions of automobile insurance rates taking effect in many states, the situation could well improve for the affiliates.

These insurers will ultimately have to diversify to a considerable extent in order to obtain more stability in business volume. This will require the consideration of new types of distribution and more selective underwriting policies. It is becoming more and more apparent to forward-thinking insurance men today that the public is becoming attuned to the idea of a "one-sto, insurance shopping center." As the trend develops toward the package policy concept, the finance affiliates will have to adjust.

In the opinion of this writer these insurers have the resources and talent available to produce imaginative answers to the problems which are developing now and which will arise in the future.
Listing of the Finance Affiliates

Arrowhead Insurance Company
Audubon Insurance Company
Balboa Insurance Company
Calvert Fire Insurance Company
Cavalier Insurance Corporation
Chesapeake Insurance Company
Commercial Insurance Company
Emerald Fire and Casualty Insurance Company
Excel Insurance Company

Fire and Casualty Insurance Corporation of America
Frontier Insurance Company
Gateway Insurance Company
General Exchange Insurance Corporation
Government Employees Insurance Company
Industrial Insurance Company
Interstate Insurance Company
Manchester Insurance Corporation
Marathon Insurance Company
Midland Empire Insurance Company, Inc.

Mid-States Insurance Company
Motors Insurance Corporation
Mt. Vernon Insurance Company
Olympic Insurance Company
Permanent Insurance Company
Service Casualty Company of New York
Service Fire Insurance Company of New York
Southeastern Fire Insurance Company
Southern Insurance Company
South State Insurance Company

Southwest Insurance Company
Southwest Underwriters Insurance Company
Standard Casualty Company
Standard Fire Insurance Company of Alabama
Stuyvesant Insurance Company
Superior Automobile Insurance Company
Transnational Insurance Company
Twin States Insurance Company
United Public Insurance Company
Universal Security Insurance Company
## APPENDIX B

**TOTAL REFUNDS BY STATE AS OF April 30, 1950**

<table>
<thead>
<tr>
<th>State</th>
<th>Number of Companies Reporting</th>
<th>Number of Lettersailed</th>
<th>Number of Refunds Made</th>
<th>Amount of Refunds</th>
<th>Average Amount of Refund</th>
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<tr>
<td>Alabama</td>
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<td>24,447</td>
<td>4,612</td>
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<td>4,993</td>
<td>22,093</td>
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<td>State</td>
<td>Number of Companies Reporting</td>
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<td>Number of Refunds Made</td>
<td>Amount of Refunds</td>
<td>Average Amount of Refund</td>
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<td>------------------------</td>
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</tr>
<tr>
<td>Vermont</td>
<td>6</td>
<td>5,121</td>
<td>2,454</td>
<td>50,950</td>
<td>23.27</td>
</tr>
<tr>
<td>Virginia</td>
<td>6</td>
<td>3,765</td>
<td>1,097</td>
<td>23,313</td>
<td>13.87</td>
</tr>
<tr>
<td>Washington</td>
<td>6</td>
<td>5,127</td>
<td>1,004</td>
<td>17,857</td>
<td>17.86</td>
</tr>
<tr>
<td>State</td>
<td>Number of Companies Reporting</td>
<td>Number of Letters Failed</td>
<td>Number of Refunds Made</td>
<td>Amount of Refunds</td>
<td>Average Amount of Refund</td>
</tr>
<tr>
<td>--------------</td>
<td>-------------------------------</td>
<td>--------------------------</td>
<td>------------------------</td>
<td>-------------------</td>
<td>--------------------------</td>
</tr>
<tr>
<td>West Virginia</td>
<td>8</td>
<td>12,703</td>
<td>5,722</td>
<td>145,205</td>
<td>25.05</td>
</tr>
<tr>
<td>Wisconsin</td>
<td>9</td>
<td>11,788</td>
<td>2,551</td>
<td>50,319</td>
<td>19.56</td>
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<tr>
<td>Wyoming</td>
<td>5</td>
<td>5,063</td>
<td>1,150</td>
<td>40,590</td>
<td>27.26</td>
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<tr>
<td><strong>Total - All States</strong></td>
<td><strong>1,262,631</strong></td>
<td><strong>451,178</strong></td>
<td><strong>18,272,730</strong></td>
<td><strong>222.77</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: The National Association of Insurance Commissioners, Subcommittee Reports—Insurance Problems in Connection with Installment Sales and Loans (June 8, 1959, meeting).
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I, Willis Park Rokes, was born in Salt Lake City, Utah, December 25, 1926. I received my secondary school education in the public schools of Salt Lake City and my undergraduate training at the University of Utah, which granted me the Bachelor of Science degree in banking and finance in 1948. In 1951 I received the Bachelor of Laws degree from the same institution. I was admitted to the Utah State Bar and the federal bar in 1952 and engaged in private legal practice and was claims attorney for a general insurance agency until 1957. In 1957 I returned to the University of Utah and received the Master of Science degree in management the same year. During the academic years of 1957-58 and 1958-59 I held the teaching positions of assistant and assistant instructor at the Ohio State University while engaged in doctoral studies in the academic fields of insurance, real estate, management, economic theory, and economic history. I was appointed Assistant Professor at the Montana State University for the 1959-60 academic year and there completed the requirements for the degree Doctor of Philosophy.