DISCUSSION BY A. C. CURRY

The inclusion of investment income in the ratemaking process for the casualty lines is a subject which is difficult to consider objectively. An individual's sentiment on the subject seems to depend upon which half of the facts he chooses to rely. Each of us has heard good arguments both pro and con. It is true, of course, that the carriers do have a source of income in addition to the premiums being charged. It is also true that the insured buys financial protection in an effort to stabilize his financial structure rather than to play the securities market.

From a review of Mr. Bailey's paper, it would appear that the dilemna which he proposes to resolve lies in the answer to two questions:

a) Why should investment income be included? and

b) What is the manner in which it should be included?

Although I can not necessarily endorse some of the figures which Mr. Bailey sets forth, his approach impresses me as being reasonable and a good compromise between both facets of the debate. I would suggest, however, that it is, in fact, a compromise because, even though I can accept his technique in general terms based upon his assumptions, I cannot endorse his assumptions.

Without getting into the question of how the industry got into this debate on investment income, I feel that it is fair to state that most proponents are seeking ultimately to reduce Mr. Public's outlay of total insurance dollars. Mr. Bailey does not propose such a reduction — neither does he propose that the allowance for profits and contingencies be increased by 2% in order to accommodate a 2% investment credit. Suffice to say that I hope we do not protect Mr. Public to the point that he can not obtain financial protection. That this can, in fact, happen has been proven in the recent past in several casualty lines.

Because Mr. Bailey does not comment upon the impact of his proposal on the overall income of the carrier, we should accept or modify his proposal for the specific reasons he gives. This is where I'm afraid he loses me. In essence, he proposes to include the investment income derived from the funds held in trust for the policyholder. This practice I would endorse wholeheartedly, but I can't find any funds held in trust for the policyholder!

Ballentine's law dictionary sets forth a lot of non-actuarial terminology with reference to trusts . . . . . plus the observation that all definitions contain the essential elements that the legal estate must be in one party and the equitable estate in another to constitute a technical trust.

Black's law dictionary also contains a few recognizable passages involving a right of property, real or personal, held by one party for the benefit of another; and any arrangement whereby property is transferred with the intention that it be administered by the trustee for another's benefit.

Crobaugh says that the trustee incurs the obligation to conserve and invest the funds for the beneficiary, and that a trustee is one in whom some estate, interest, or power in property is placed for the benefit of others.

Even in the common vernacular, a trust would have to include an obligation to preserve, not dissipate, or invest. Yet written premiums in an insurance contract represent the consideration which is necessary for the contract to be a binding one. There exists no obligation to return the premiums, conserve the premiums, or invest the premiums. Only if the contract is cancelled is there an obligation or a liability on the part of the carrier to return a portion of the premiums and this potential liability is described in the contract. The manner in which this consideration is entered on the books does not create the liability. The fact that an accounting entry is made for budgetary purposes neither produces a liability nor incurs an obligation to return the premiums paid. A budgetary reserve for the depreciation of office furniture does not create a liability to the cabinetmaker. Neither does a budgetary reserve for deferred expenses create a liability. An unearned premium reserve is merely a budgetary, fictional accounting maneuver designed to theoretically remove some of the funds from the right hand pocket and place them into the left hand pocket to remind us that the opportunity to incur liabilities has not expired. In fact, Uncle Sam, in theory at least, would accept a cash basis of accounting for tax purposes.

One could even develop a line of thinking which begins with . . . . . the annual statement is a measure of the company's condition, the rules can be set at will, etc., etc., ... and ends with the conclusion that the unearned premium reserve is an accounting requirement of the regulatory authorities in order that they may measure the company's ability to meet their future obligations. And even further, this document is neither the only measure nor necessarily the best measure particularly for any other purpose.

If I, as an individual, remove from my pocket $25 per month and put it into a credit union in order to pay my heat bill this winter, I do not in any way incur an obligation to the gas company. If we as a carrier do the same thing with some of our income, we have not incurred an obligation to the purchaser of the contract.

Loss reserves, too, would seem to be a budgetary estimate of future or potential liabilities. Reserves are necessary primarily because either the liability has not been established or the extent of liability has not been established. I would concur that if the extent of liability has been established and payment is not tendered, then some of the funds which offset these budgetary estimates do belong in theory to the *claimant* (who may or may not be the policyholder).

Through this paper, Mr. Bailey has again presented a valuable contribution to the literature of the Casualty Actuarial Society. The blueprint which he advances merits serious consideration by the members of our society. This paper represents a challenge to the rest of us to explore the attendant problems, such as:

a) The assumption of equal liquidity as respects loss reserves and capital investments.
b) Do the policyholders have an equitable estate in the "liabilities" or in the "assets"?
c) Should we act like an investment house if these assumptions are correct?
d) How can the opponents pass off investment gains as easily as the proponents pass off the market setbacks?
e) Should we subject the carriers of other lines to the fluctuations of the casualty business by combining the carriers into groups?
f) Who are we protecting if we encourage the carriers to dissipate their surplus?
g) If we intend to include IBNRs, to whom do we owe that money?

Mr. Bailey's paper in my estimation is a fine attempt to reconcile the diverse opinions available in our industry. Moreover, he has astutely directed his attention toward what will probably be one of tomorrow's facts of life. Before endorsing Mr. Bailey's general premise, however, let's be sure that we aren't about to protect Mr. Public to death by reducing his ability to obtain protection.

DISCUSSION BY RICHARD L. JOHE

Mr. Bailey states his hope that his "suggestions and data will contribute to a better understanding of the problems and possible answers regarding how much underwriting profit is realized from investments." He develops his definitions of investment income, invested assets, and "the stockholders'