

LIFE INSURANCE COST DISCLOSURE

A Staff Report to the
Federal Trade Commission

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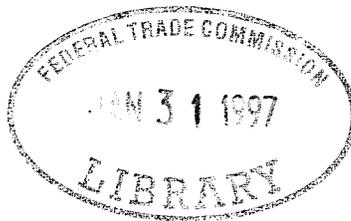
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INTRODUCTION

Recently much attention has been focused on the plight of people with relatively small amounts of savings.¹ Because of Federal regulations on the maximum interest rates that banks and savings and loan associations may pay, savers who have less than \$10,000 to invest have often had to settle for rates of 5 to 5-1/4 percent on their money, while open market rates are in the 9-1/2 to 10 percent range. Even the latter rates are barely sufficient to cover the current rate of inflation. Through a variety of exemptions and financial innovations, large savers have been able to obtain access to the open market rates from which small savers have been excluded by deposit rate ceilings. One economist has put the loss in interest earnings at over \$8 billion on passbook savings accounts at commercial banks, savings banks and S&L's in 1978 alone.² Based on similar findings, Mr. Robert Gnaizda, a public interest lawyer, petitioned Congress to require a "fair warning on every passbook, in every advertisement, and on the doors of every bank..." that "Savings may be hazardous to your wealth," if the government does not end the system of deposit rate ceilings.³

1 See Hearings on "Regulation Q" Before the Subcommittee on Commerce, Consumer and Monetary Affairs of the House Committee on Government Operations, 96th Cong., 1st Sess. (1979) [hereinafter cited as 1979 Hearings.]

2 See the testimony of Professor Edward Kane, id.

3 1979 Hearings, supra n. 1. Mr. Gnaizda puts the loss at over \$17 billion.

Virtually no attention has been paid, however, to how small savers have fared during the current inflation in the one major consumer savings medium that is not subject to deposit rate ceilings. At the end of 1977, consumer savings held by the ordinary life insurance industry amounted to approximately \$140 billion.⁴ This amount is roughly equal to the total of all passbook savings accounts held by the savings and loan industry.⁵ A major portion of this report will be devoted to an examination of consumer savings through life insurance. The life insurance industry publishes no figures on the total consumer savings which it holds. Nor does the industry publish figures on the rate of return it pays on savings, either for the industry as a whole or on individual policies. This report will examine the rates of return being paid by the life insurance industry to the 45 to 50 million households that save through life insurance. Among the important findings of this report are:

1. The average rate of return paid by the industry to all ordinary life insurance policyholders in 1977 was between one and two percent;⁶

⁴ See pages 11-12, infra.

⁵ Passbook accounts amounted to almost \$144 billion in December, 1977. 1979 Hearings, supra n. 1, at 7, Table 3 (statement by Kenneth Thygerson, Chief Economist of U.S. League of Savings Associations).

⁶ This is the average rate paid all ordinary life policy holders. Many policies currently on the market, if held for 20 years, will yield between 4 and 5 percent. See Tables II-7, II-8, infra.

2. The rate of return on new policies is, in many instances, substantially below alternatives readily available in the market place;
3. A significant number of holders of old policies are locked into a low-yield, fixed-dollar investment unsuited to cope with current inflation;
4. There are severe, but unannounced, penalties for early withdrawal of savings through life insurance policies. Unlike the withdrawal penalties mandated by Federal deposit regulations, the penalties imposed by life insurance companies do not merely reduce the return earned on the principal: they often reduce and sometimes even eliminate the principal itself. The consumer loss resulting from first-year lapse alone exceeds 200 million dollars a year. Just to break even, many policies bought in 1977 will have to be held until 1987.
5. Price competition is so ineffective in the life insurance industry that companies paying 20-year rates of return of 2 percent or less compete successfully against companies that pay 4 to 6 percent. This disparity should be contrasted with the banking industry, where differences of a quarter of a percent are considered to be competitively crucial.

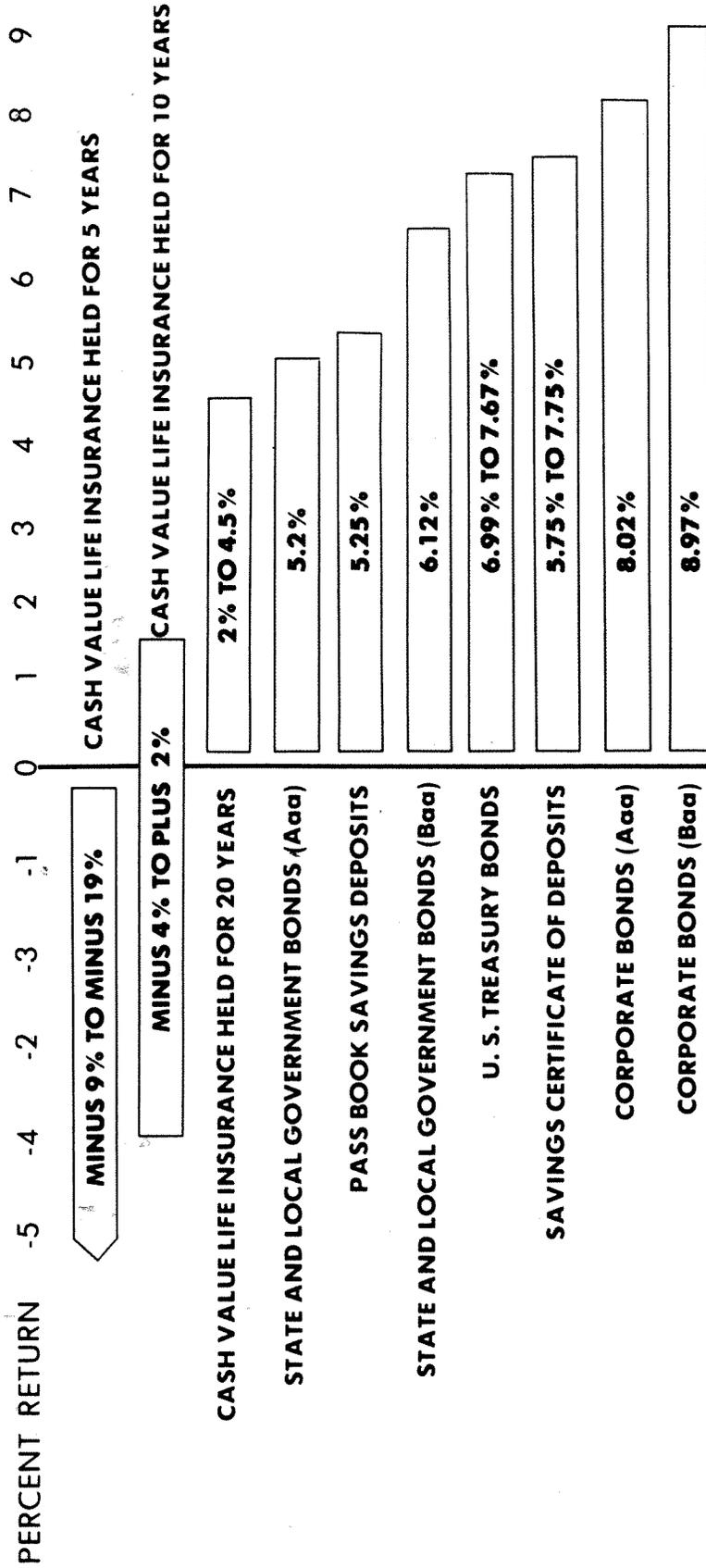
There are important differences between saving through life insurance and saving through the banking industry. In particular, the income generated through a life insurance policy

is essentially tax free; therefore, all the rates of return mentioned above should be compared to the after-tax return from other forms of savings or investments. Nevertheless the average rate of return on savings through life insurance is extraordinarily low even compared to current passbook rates offered by banks and S&L's, which are themselves kept artificially low by the deposit rate ceilings. We estimate that consumers would have had an additional \$3.7 billion in 1977 alone if the life insurance industry had paid only 4 percent on savings.⁷ Thus while deposit rate ceilings may have imposed great costs on small savers, those consumers who save through life insurance are in many instances far worse off. Indeed, life insurance savers would gain substantially if they were at least put on an equal footing with the current low deposit rate ceilings of banks and S&L's.

These problems led to this investigation of the life insurance industry. The investigation examined the magnitude of consumer injury and the extent to which life insurance cost disclosure can remedy these problems. This report is the end product of that investigation. It is divided into four parts: (1) An overview of the industry and an analysis of its role as a savings medium; (2) An analysis of consumer problems in the life insurance industry; (3) A description of some of the reasons for these problems; (4) A recommended system of life insurance cost disclosure which we believe is a prerequisite to any meaningful

⁷ See pages 18-19, infra.

RATES OF RETURN ON VARIOUS INVESTMENTS -- 1977



CAVEAT: PURCHASERS SHOULD CONSIDER TAX ADVANTAGES AND DISADVANTAGES OF ALTERNATIVE INVESTMENTS. RETURNS ON CASH VALUE INSURANCE POLICES ARE GENERALLY TAX FREE; SOME BONDS ARE TAX-EXEMPT.

SOURCE: FEDERAL TRADE COMMISSION

price competition in the life insurance industry.

I. THE LIFE INSURANCE INDUSTRY AND ITS SERVICES

A. Description of the Industry

The life insurance industry is a large and important part of our economy. The total income of domestic life insurance companies in 1977 was \$98 billion.⁸ While it is difficult to comprehend a figure this large, some comparisons may help. The \$98 billion received by life insurance companies in 1977 is approximately the same as the federal government spent for national defense in that year and more than twice as large as the total income of the entire farm population of the United States.⁹

The life insurance industry directly affects most families in this country. Seventy-two percent of the adult population of the United States and over 90 percent of all husband and wife families own some form of life insurance.¹⁰ In 1977, Americans purchased \$367 billion of additional life insurance coverage bringing the total of life insurance coverage to almost \$2.6 trillion.¹¹ Insured families paid an average of over \$500 a year in premiums and had approximately \$37,000 insurance in force.¹²

⁸ American Council of Life Insurance, Life Insurance Fact Book, at 56 (1978) [hereinafter cited as Fact Book].

⁹ Economic Report of the President, 339, 362 (1978).

¹⁰ Fact Book, supra n. 8, at 35. These figures are for 1976.

¹¹ Id. at 7.

¹² Id. at 7 and 56. This figure includes employer contributions
(Footnote Continued)

The primary focus of this report is ordinary life insurance. Ordinary life insurance policies are usually sold to individuals (as opposed to groups), and are usually sold by agents. Most ordinary life premiums are paid by mail rather than collected by an agent.¹³ In 1977 Americans paid \$24.2 billion in premiums for 140 million ordinary life insurance policies. This expenditure represented 1.9 percent of all personal income.¹⁴ In return for premiums paid, the life insurance industry performs two important services: it provides death protection and serves as a savings medium. The dual nature of the life insurance industry is reflected in the differences between the industry's two basic policies: "term" policies (which provide only insurance protection) and "cash value" policies (which provide both insurance protection and a form of savings). The following section describes these two basic types of policies.¹⁵

12 (Footnote Continued)

and is computed by dividing premium income by the number of insured families (88 percent of about 70 million families).

13 Besides ordinary life insurance, the other major products of life insurance companies are health insurance, annuities, group life, credit life and industrial life insurance. An economic profile of the whole industry is set forth in Appendix I.

14 Fact Book, supra n. 8, at 20, 58, 59.

15 All life insurance policies are either participating or non-participating. Non-participating policies do not pay dividends and are sold by stockholder owned insurance companies. Participating policies pay dividends and are primarily issued by mutual insurance companies but are also issued by stock companies. In dividend-paying policies, the premium is set at a level greater than the anticipated future cost
(Footnote Continued)

B. Basic Types of Life Insurance Policies

1. Term Insurance

Simply stated, term insurance provides solely death protection for a fixed period of time such as 1, 5, or 10 years or until the insured reaches a specific age such as 65. The face amount of the policy will be paid only if the insured dies within the time (or term) stated in the policy. Thus, a one year \$25,000 term policy, for example, obligates the insurance company to pay the beneficiary that amount should the insured die within the year. Term insurance policies are often renewable for additional terms without the insured's being required to take a medical examination. Each time the policy is renewed for another term, the premiums increase to reflect the greater likelihood of death as a person grows older.¹⁶ When the insured is young, term insurance is relatively inexpensive and provides the largest immediate death protection for the premium dollar. However, the premiums

15 (Footnote Continued)

of the policy. Dividends paid reflect the company's actual costs. See generally J. Belth, "Distribution of Surplus to Individual Life Insurance Policyholders," 45 Journal of Risk and Insurance 7 (1978).

16 Certain types of term policies provide for level premium payments. For example, "term to 65" has only one "term" and thus the premium remains at a constant level until the policy expires at the stated age. The early year premiums for this form of term insurance are significantly higher than traditional renewable term. Another level premium variant is "decreasing term", in which the face amount of the insurance decreases over time while the premiums stay the same. This type of policy is often marketed as protection for long-term decreasing debts such as mortgages.

steadily increase as the insured ages and become very high after age 65.

2. Cash Value Insurance

There are several types of cash value insurance. The most important type is "whole life" or "permanent life" insurance. Whole life insurance policies remain in force as long as the premiums are paid. They differ from term policies in three important ways. First, the premiums for a whole life policy are initially much higher than for term insurance for the same amount of insurance protection. Second, unlike the premiums for term insurance, whole life premiums do not go up with age but remain the same throughout the payment period. Third, whole life insurance policies develop cash values which increase each year.¹⁷

A whole life policy can have a premium that does not increase because during the early years of the policy the premiums are much higher than the amount needed to buy only death protection.¹⁸

¹⁷ In addition to whole life insurance, many other policies on the market combine savings and protection in various degrees. Examples include "life paid up at 65," "20-pay life," and "endowment policies." "Life paid up at 65" and "20-pay life" are policies in which the premiums are paid over a limited period instead of over the entire life of the policy. Endowments are policies in which the cash value equals the policy's face amount at the end of a limited period, usually 20 or 30 years.

¹⁸ A 35-year old man will typically pay an annual premium of \$15-20 per \$1,000 of coverage for a whole life policy, while a comparable size one-year renewable term policy would cost \$2.00 to \$6.00 per \$1,000. When the insured reaches ages 55-60, term premiums become greater than the \$15-20 level premiums of the whole life policy.

Part of these "overpayments" made in the early years of a whole life policy are invested by the company and set aside as a reserve to be used to pay part of the death benefit should the policyholder die. This reserve serves as the basis for a policy's cash values. The cash value of a whole life policy generally increases each year and is specified in the contract.¹⁹ While alive, the policyholder can either borrow against the cash value or receive it by surrendering the policy. If the insured dies, however, the insurance company pays only the face amount of the policy, not the face amount plus the cash value.

A whole life policy can be viewed as a combination of an increasing savings element (cash value) and a decreasing amount of pure life insurance protection. This is because as the cash value of the policy increases the actual amount of death protection being purchased decreases correspondingly--the sum of the cash value and the death protection always equals the face amount of the policy. The increasing cash value also explains why whole life insurance premiums stay the same throughout a person's life. Even though the chances of dying and thus the cost of pure death protection increases each year, the cash value reduces the amount of death protection that must, in effect, be purchased.

Although the description of whole life insurance as a

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The increase in cash value in any given year is due to two factors--the excess premium payments for that year and the interest credited to the cash value that has been previously accumulated. The impact of compound interest is substantial. For example, \$1.00 invested at 7.2 percent will double in ten years.

combination of death protection and savings is commonly found in insurance texts,²⁰ many people in the insurance industry assert that the separation of whole life insurance into savings and protection components is improper and that the life insurance contract must be viewed as an undifferentiated whole. They argue that the purchase of a whole life policy should be viewed as simply buying insurance protection on the level-premium "installment" plan. According to this view, under the level premium method, people "prepay" while they are young for insurance protection they will receive only many years later, while the savings element (cash value) is described as an "incidental" by-product of the level premium method of paying for insurance.²¹

It is true that the policy's savings element is a by-product of the level premium method of paying for insurance. However, it can hardly be said to be "incidental". During the initial years of a typical whole life policy the portion of the premium that goes to build up the savings element of the policy will often be 70 percent of the total premium. Over the first twenty years of a typical whole life policy issued to a male aged 25, about 40-50 percent of the premium goes into the policy's savings element.²² The fact that a major portion of the premiums for

20 See, e.g., S S. Huebner & K. Black, Life Insurance 7 (1976).

21 This argument is discussed in detail at pages 113-120, infra.

22 See J. Belth Life Insurance - A Consumer's Hand Book, 49-50, (1973).

whole life policies goes toward building up cash values makes the life insurance industry a major savings institution.

C. Life Insurance As A Savings Medium

Sales of cash value insurance policies, in conjunction with sales of annuities, make the insurance industry one of the country's major savings institutions.²³ Assets of domestic life insurance companies totaled more than \$350 billion at the end of 1977.²⁴ In recent years, life insurance companies have accounted for about 20 percent of the growth in all personal savings.²⁵ As a repository of personal savings, the life insurance industry has ranked second only to savings and loan associations among private savings institutions.²⁶

Individual savings through ordinary cash value insurance represent a significant part of the total consumer savings deposited with the life insurance industry.²⁷ Although the life insurance

²³ Although term insurance sales have been growing more rapidly in recent years than cash value sales, the latter type is still the most common form of ordinary insurance purchased and owned. Cash value policies (on adult lives and sold by ordinary agents only) accounted for about 58 percent of premiums and about 39 percent of the amount of new ordinary insurance purchased in 1975. Life Insurance Marketing And Research Association (LIMRA), 1975 Buyers Study at 19.

²⁴ Fact Book, supra n. 8, at 69.

²⁵ G. Bishop, Capital Formation Through Life Insurance, 91 (1976).

²⁶ Id. at 87.

²⁷ The remainder consists primarily of annuities and amounts held under pension plans, Fact Book, supra n. 8, at 36-38, 49-54.

industry does not publish statistics on the total consumer savings through ordinary life insurance, this number can be estimated. In 1977, it totaled approximately \$141 billion or over \$1,000 for each of the 139 million ordinary life insurance policies in force.²⁸

An indication of the relative importance of savings versus protection in ordinary life insurance can be seen by comparing it to group term insurance. In 1977, the two lines provided roughly equal amounts of death protection.²⁹ Death claims paid on ordinary life policies amounted to \$4.9 billion versus \$4.8 billion on group contracts.³⁰ Yet the public paid over \$24 billion in premiums for its ordinary life insurance coverage compared to less than \$7 billion for its group coverage.³¹ There are two major reasons for this immense difference. First, the ordinary line is dominated by cash value policies, where the savings benefits are far larger than the death protection benefits. Second, selling costs are much higher for ordinary than for group policies.³²

28 . Consumer savings consist of ordinary life cash values and accumulated dividends left with the companies at interest. For details of this calculation see Appendix II.

29 Ordinary life insurance in force amounted to \$1,289 billion, compared to \$1,115 billion for group. Fact Book, supra n. 8, at 18.

30 Id at 41.

31 Id. at 57.

32 For example in 1975, commission costs were about \$1.97 per thousand of coverage on ordinary policies versus 12 cents
(Footnote Continued)

The following tables show the relative importance of ordinary life insurance as a savings institution and as a provider of death protection. Table I-1A is a summary of the total cash flows and the increase in consumer savings in the ordinary life insurance line in 1977. Table I-1B contains the same information broken down by insured household.³³

These tables show how much money flowed from policyholders (directly and indirectly) into the industry. The money flowing into the industry consists of premiums and the investment earnings from consumer savings through ordinary cash value insurance.³⁴ The tables also show how much money flowed back from the companies to policyholders in the form of benefits. Finally, the tables show a breakdown of the money remaining with the companies broken out by the amount used to increase policyholders' savings and the amount retained for expenses and profits.

32 (Footnote Continued)

for group. Home office expenses averaged \$3.02 per thousand on ordinary versus 30 cents for group. These figures were derived from Table 2 in Appendix II.

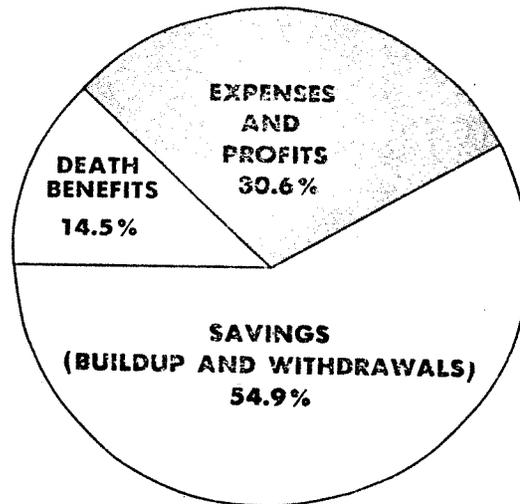
33 The numbers in Table I-1B are based on the assumption that there are 46 million households with ordinary life insurance. The derivation of the number of insured households is set forth in Appendix II.

34 These reserves are technically not owned by the policyholders. However, policyholders can surrender their policies at any time and receive their accumulated cash values and dividends. Thus, we think it is appropriate to view investment income on these reserves as funds indirectly contributed by policyholders.

The overwhelming importance of the saving element of ordinary cash value insurance is shown by the fact that, although approximately \$34 billion was contributed by policyholders to the industry, only about \$5 billion was returned in the form of death benefits. The death benefits paid are only slightly larger than the dividends paid and are much smaller than either the withdrawals from savings or the buildup of savings. From the perspective of the individual household, an average of \$525 was paid in premiums and only \$107 was received back in death benefits. This comparison excludes an additional indirect contribution of \$212 per household derived from investment income.

Table I-2 is a breakdown showing approximately how policyholder-provided income (premiums plus investment income) is used in ordinary insurance. Table I-2 shows that death benefits paid in 1977 represented only 14.5 percent of the cash flow of the industry, whereas the savings element was more than 3-1/2 times as large at 54.9 percent.

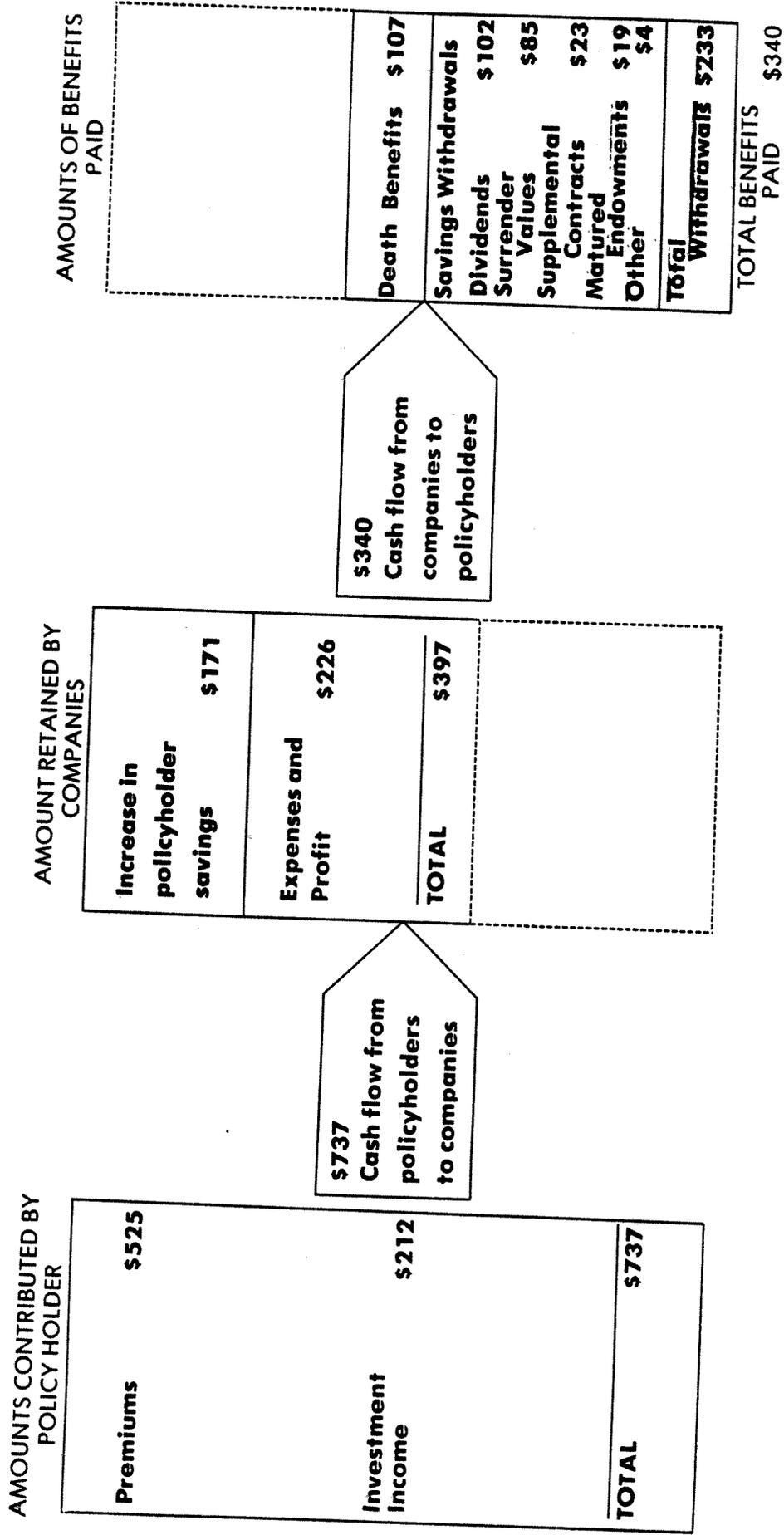
Table I-2³⁵



³⁵ Table I-2 is based upon the data contained in Table I-1A.

TABLE I - 1B
AVERAGE CASH FLOWS BETWEEN POLICY HOLDERS
AND LIFE INSURANCE COMPANIES
BY INSURED HOUSEHOLD IN 1977

(Amounts in dollars)



SOURCE: FEDERAL TRADE COMMISSION

*/ The source of the information in Table I - 1B is set forth in Appendix II.

These tables demonstrate that the life insurance industry is a major savings medium. We now turn to an examination of the average rate of return the life insurance industry pays ordinary policyholders. The life insurance industry, in return for the premiums it receives, both provides insurance protection and serves as a savings medium. By subtracting the portion of the total premium that goes to provide insurance protection it is possible to compute the average rate of return the insurance industry is paying on policyholders' savings. This rate is calculated in much the same way as the rate of return from any other savings medium such as a bank. The general formula for calculating rate of return is set forth below:

$$r = \frac{\text{savings at the end of the year}}{\text{savings at beginning of the year} + \text{deposits} - \text{withdrawals}} \quad -1$$

Using this formula, the average industrywide rate of return paid ordinary policyholders in 1977 can be calculated. Total consumer savings in ordinary life insurance were \$137.032 billion at the beginning of 1977 and \$140.910 billion at the end.³⁶ The withdrawals from savings were paid as dividends, surrender values, supplemental contracts, matured endowments and other miscellaneous benefits and totaled \$10.7 billion.³⁷ In 1977, \$24.161 billion was paid in premiums. Part of the total premiums can be allocated to the industry's cost of providing death protection and the remainder is the deposit added to existing savings.

36 See Appendix II.

37 See Table I-1A.

* / The source of the information in Table I - 1B is set forth in Appendix II.

To determine the size of the deposit it is necessary to estimate the portion of the premiums needed to provide death protection. This can be done simply by taking the cost of providing death protection (term insurance) to be some multiple of death benefits actually paid. For purposes of this calculation we used a multiplier of 1.5. That is, people pay \$1.50 in premiums to get back \$1.00 in death benefits.³⁸ Applying this 1.5 multiplier to all death benefits paid in 1977, the amount of premium dollars needed to provide death protection is \$7.364 billion:

Death benefits paid in 1977	\$4.909 billion
	<u>X 1.5</u>
Premiums needed to provide death protection	\$7.364 billion

The deposit to savings is the total premiums minus the cost of providing death protection or \$16.8 billion.

Total Premiums	\$24.161 billion
Cost of Pure Insurance	<u>7.364 billion</u>
Deposit to Savings	\$16.797 billion

Table I-3 illustrates the rate of return calculation for 1977 using the 1.5 ratio to estimate cost of providing death protection.

³⁸ A 1.5 multiplier is the same as a 66.6 percent loss ratio. This means that for each \$1.00 in premiums paid the company returns 66.6 cents in benefits. The industrywide ratio of benefits to premiums for all business in 1977 was 79 percent. Fact Book, supra, n. 8, at 62. The higher the loss ratio assumed, the lower the rate of return. The rate of return assuming different loss ratios is set forth in Table I-4, infra.

Table I-3

Rate of Return Paid by Life Insurance Companies to Ordinary
Policyholders in 1977³⁹

Savings at end of 1977	\$140.910 billion
Savings at end of 1976	\$133.032 billion
Deposit: Premiums	\$ 24.161 billion
less (1.5) X Death Benefits (4.908)	<u>7.364 billion</u>
	\$ 16.797 billion
Withdrawals: Dividends	\$ 4.671 billion
Surrender Values	3.964
Supplemental Contracts	1.059
Matured Endowments	.894
Other	<u>.163</u>
	\$ 10.751 billion
Deposit less withdrawals	\$ 6.046 billion

$$r = \frac{\text{Savings end of 1977}}{\text{Savings end of 1976 plus Deposit less Withdrawals}} - 1$$

$$= \frac{140.910}{133.032 + 6.046} - 1 = \frac{140.910}{139.078} - 1 = 1.013 - 1 \text{ or } r = 1.3 \text{ percent}$$

The industrywide rate of return depends upon the amount of the total premium dollars that are allocated to providing death protection. The dollars allocated to insurance depend upon the loss ratio assumed. Table I-4 shows the rate of return using both a 66.6 percent and other loss ratios for the years 1970, 1975 and 1977.

39. For the sources of these figures see Table I-1A, *supra* and Appendix II. The rates of return in Tables I-3 and I-4 do not take into account one of the important special features of cash value contracts, namely, the right to borrow against the cash value at a rate of interest specified in the policy. The calculations in the text are concerned with what the industry pays and treat policy loans as a separate transaction for reasons that are discussed in Appendix III. Nevertheless, the policy loan provision is of considerable value to those policyholders who can borrow funds at 5 or 6 percent, when their alternative would be at 10 or 12 percent. It is difficult to quantify this benefit since we have no information on the alternative rates of interest that the borrowers would have had to pay and because we would also have to reflect the value of the loss in insurance protection that occurs when a policy loan is made.

Table I-4

Rates of Return to Ordinary Policyholders in 1970, 1975
and 1977 Using Alternative Loss Ratios

<u>Year</u>	<u>Loss Ratios</u>		
	79% (1.2658)	66-2/3% (1.5)	60% (1.66)
1970	-1%	-0.15%	0.46%
1975	0.03%	0.86%	1.45%
1977	1.2%	1.3%	1.85%

Table I-4 shows that, depending upon the loss ratio assumed, the average rate of return paid to ordinary policyholders in 1977 ranged from 1.2 to 1.85 percent. No matter which loss ratio is assumed the rate of return is extraordinarily low, even considering that it is essentially tax-free. The extremely low industrywide rate of return reflects the consumer problems discussed in the next part of this report: low average rates of return paid on individual policies, great variability in the rates of return paid on policies, negative rates of return when early lapsation occurs, and extremely low rates of return paid to policyholders who purchased their policies many years ago when inflation and interest rates were much lower.

The industrywide rate of return can be used to estimate the total loss to consumers in 1977 from all of these problems. This is done by comparing the amount of savings that would have been available if the industry had paid a competitive tax-free rate of return on policyholder's savings rather than the approximately 1.3 percent it actually paid. A reasonable

tax-free rate of return in 1977 would have been at least 4 percent (see page 31, infra). If the life insurance industry had paid ordinary policyholders 4 percent interest, total savings would have amounted to (139.081×1.04) or \$144.644 billion instead of \$140.910, a difference of over \$3.7 billion in 1977 alone.⁴⁰

It is important to note that the available evidence does not indicate that life insurance companies are earning massive profits on the difference between their return on investments and what they pay policyholders. In 1977, life insurance companies earned an average of 6.9 percent on their investments before Federal taxes,⁴¹ while they paid approximately 1.3 percent to policyholders on funds invested with them. The large differential, however, does not necessarily result in excessive profits for the companies. The available evidence suggests that most of the differential is absorbed by high home office expenses, sales commissions to agents, and Federal and state taxes.⁴²

⁴⁰ The difference in 1977 would be substantially greater if the industry had been paying 4 percent in earlier years as well, since the total savings at the beginning of the year would have been larger and the policyholder would have earned interest on the earlier paid interest.

⁴¹ Fact Book, supra, n. 8, at 61.

⁴² A recent study of the profitability of capital stock life insurance companies found that their rates of return on net worth were higher than that of other service industries, such as banking and real estate, but lower than for manufacturing and wholesale and retail trade. Since life insurance company profits are much more stable than profits in other businesses, the authors of the study also estimated rates of return adjusted for risk. Their tentative conclusion

(Footnote Continued)

It does not really matter to consumers who purchase cash value insurance whether the low average rate of return paid ordinary policyholders is due to excess profit of companies, high expenses, or the cost of supporting an extensive agency system. What is important is that in far too many instances consumers who use cash value insurance as a way to save receive a rate of return which is substantially below what is readily available in the marketplace. The next part of this report analyzes the consumer problems in life insurance from the perspective of the individual policyholder.

42 (Footnote Continued)

was that the risk adjusted rates of return for life insurance companies are high relative to other industries but not excessively so. See S. T. Pritchett and R. Wilder, "A Comparative Study of Stock Life Insurer Profitability: Implications for Workable Competition" (Preliminary Draft), prepared for the Huebner Foundation, Wharton School, University of Pennsylvania. A further discussion of the profitability of life insurance companies is contained in Appendix I.