Journal of Accountancy

Volume 44 | Issue 5 Article 2

11-1927

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By Walter Mucklow

"Is there anything whereof it may be said,
See, this is new?"—Ecclesiastes 1:10.

It has been generally supposed that the book of *Ecclesiastes* was written by Solomon at the close of his fervid career, when he realized acutely that although, as he says in *Proverbs*, "He who findeth a wife, findeth a good thing," there is the possibility of a surfeit, or in the language of today, "too much of a good thing." A good woman unquestionably is worth more than rubies, but an excess of jewelry indicates poor taste and in his case apparently led to a bad one, for *Ecclesiastes* was written in the spirit of the "morning after"; which leads me to the word for which I have been groping —aftermath.

Now, in the aftermath of the Florida boom we have land-value insurance, which at first sight appears to be something of an anomaly, for a boom and this insurance are diametrically opposed to each other—either one may exist, but both can not possibly live in any one place at the same time, for the two things are incompatible, mutually repelling.

It is seldom that the accountant encounters a principle or a procedure which may fairly be called "new," and when he does it is a matter of sufficient importance to warrant examination. After some thought, the writer has come to the conclusion that land-value insurance is new, and further that it may develop to such a degree that some knowledge of it will be essential to all who come in contact with transactions in which real estate is involved. Therefore, he indulges in a brief account for the benefit of his fellow practitioners.

As the business is young and has been confined to a comparatively small portion of the United States, there are relatively few who understand the methods pursued, or the principles on which they are founded. It may still be too early to predict its future with certainty, but if the child be father of the man the early days of existence may be the best time in which to commence a study of the subject.

The study falls into four parts:

1. What is land-value insurance?
2. What security does it offer and on what is this based?

3. How is it effected?
4. What effect will it have on the real-estate business?

WHAT IS LAND-VALUE INSURANCE?

While land-value insurance is applicable to single or isolated lots, or parcels, of land, at the present time it is offered only upon tracts which are intended for subdivision into lots or into farms.

If the owner of such a tract desires to obtain value insurance, he makes application to the insurance company and files with it a complete and minute description of his property, showing its area, location, improvements, etc., etc., together with a plat of the subdivision, schedules of all the proposed selling prices and proof as to his title to the property.

These statements are studied by the officers of the company, who apply to them the factors which are described later herein, and then the risk is accepted, or declined, or some modifications are suggested.

If the risk be accepted, the company and the owner enter into a contract under which the former agrees to issue, at any time within a stated period, one of its policies on each lot in the subdivision in question.

The owner then proceeds to sell his property, and each purchaser, upon making his initial payment, receives from the company an "interim certificate" stating that on his acquiring legal title to his lot, as described in the certificate, he will receive a policy insuring the value of the lot up to a stated sum.

Under this policy the company guarantees the owner that the lot specified will be worth the sum for which it is insured at the end of a stated period, usually ten years. This guaranty, or insurance, does not become effective until the expiration of the ten years (or other specified term) and always remains effective for one year only.

Therefore, the effect is that one who in 1927 purchases for $5,000, on an instalment plan, a lot which is so insured, receives an interim certificate, and upon his completing the purchase, say, on January 1, 1929, he receives a policy stating that at any time during the year 1939 the company will, on his request, pay him $5,000 for the lot upon his conveying the property to the company.

This amount is payable by the company to the assured on his request, regardless of any value or appraisal of the property in 1939.

WHAT SECURITY DOES IT OFFER AND ON WHAT IS THIS BASED?

All insurance is founded on the law of averages, and this form is no exception to the rule. The averages are determined by compiling facts from as large a number of cases as is possible and ascertaining the conditions surrounding those to whom or to which the facts relate.

These facts are usually collected and collated by actuaries who from them prepare tables which show the ratio of risks of a given class.

As has recently been well said at the eighth International Congress of Actuaries which has recently closed its sessions in London, "To the ordinary man the profession of the actuary, requiring as it does a highly specialized technique, has always remained something of a mystery. . . . The actuary has been able by his calculations to achieve the apparently impossible, to harness chance—a demon more volatile than Pegasus—and in some measure at least to clip the wings of misfortune."

Life insurance affords the closest parallel to land-value insurance and a glance at the history of the older form is interesting.

In England it was necessary to set by law the value of an estate for a single life, two lives, etc., and four hundred years ago this was arbitrarily set at seven years, fourteen years, etc., respectively. A century and a half later (A. D. 1692) the government undertook to sell annuities and lost some millions sterling in the venture.

This led the astronomer royal, Dr. Halley, to make investigations, but he had difficulty in obtaining the requisite facts. However, he did find records in Breslau, Silesia, where the data for 5 years included 6,193 births and 5,869 deaths. As no census had been taken, Dr. Halley estimated the population and in or about 1693—234 years ago—published the first crude mortality tables.

These led to further study as to collecting data and drawing proper conclusions therefrom, but little progress was made, although the first life-insurance company, the Equitable Society of London, was established in 1762.

In 1780 the Northampton table was prepared by Dr. Richard Price but in this case also no census had been taken, and subsequent experience has shown that the table contained grave errors, the average life being shown at twenty-four years, whereas the true average has been proved to be thirty years. The table is based on 4,220 births and 4,689 deaths.

The Northampton table continued to be the best available until 1815 when the famous Carlisle tables were published, on which an enormous amount of life insurance was written with safety and profit. The Carlisle tables are still recognized by the courts throughout this country. This table is based on the lives of only 7,677 people of whom 1,840 died in eight years.

In each case the observations were confined to the population of one small town, and in the two earlier instances no information was obtainable as to the census or the increase in population during the period under observation. Yet results were obtained which were sufficiently reliable to stabilize the business of life insurance, although the government for long refused to acknowledge the value of the results.

Let us compare this with the history of land-value insurance.

A few years ago, probably about 1923, there were formed the first companies to guarantee the value of real estate, and one of these, a Nevada corporation, did business in California, but it was decided that the business was practically insurance, and the company was ordered to stop operations. This brief experience had proved the value of such insurance and a company was organized as a land-value insurance company. In 1925 the California legislature passed an act controlling land-value-insurance companies, and this is now in force, the first company having been licensed on May 27, 1925. Since then, the insurance departments of other states, notably Colorado, New Mexico, Nevada, Wyoming and Florida, have passed favorably on this form of insurance and have granted permission for land-value-insurance companies to do business.

It is safe to say that similar permits will be granted by all states whose laws provide for "miscellaneous" insurance companies, and it is stated on good authority that every state in the union, except New York, does provide for such companies.

The actuaries interested in this matter naturally desired to obtain figures corresponding to those on which mortality tables are based, and for this purpose they analyzed the history of more than ten thousand subdivisions which have been made in the period 1879 to 1920, distributed throughout the United States. They also obtained and arranged all the available pertinent information, including the causes of the successes and of the failures.

This information, after the most careful analysis, shows that, based on a period of ten years, over 80 per cent. of the subdivisions have been successful and less than 20 per cent. have been unsuccessful.

This information is varied in character and includes such items as:

Increase in population
" in bank deposits and clearings
" in post-office business
" in buildings of various classes
Municipal conditions
Public utilities
Transportation
Schools
Churches
Entertainment features
Direction of civic growth
Location as regards the center of business
Type of population
Open or closed shops
Comparative prices of commodities
Proportion of available vacant property
Classes of available and vacant buildings

In the case of farm lands the character of the soil, its suitability for crops, its adaptability to irrigation and such matters are important factors.

There are in all some 87 factors which are taken into account, an appropriate "weight" being given to each factor, although these weights vary in different neighborhoods. Well established old communities present advantages and disadvantages differing from a younger and more rapidly developing neighborhood.

Before a company will consider any risks in a given territory it makes a study of the conditions, obtains the factors mentioned and applies them to the value of any tract submitted to it in such a way as to determine a value upon which the property will yield a fair return—that is, the true commercial or selling value. In determining the basic price to which the factors are applied, the companies obtain the assistance of the best appraisers or appraisal boards available.

Much stress is laid upon the proportion which the various kinds of business buildings and dwellings in any vicinity bear to each other.

The companies are not appraisal companies and do not furnish owners with valuations. They simply tell an owner whether or not they are willing to insure the owner's prices.

It is suggested that the information available for examination, coupled with the advances which have been made in actuarial science, places land-value insurance on a far broader and sounder foundation than life insurance occupied for several generations after the first company was established.

The security behind the policies is increased by the several "spreads" which apply to this kind of insurance, namely:

(1) Over a varied territory
(2) Over a variety in the character of risks
(3) Over the term of years

(1) *Territory.* No company intends to confine itself in any way. Its business will extend from its home town throughout the county and the state, and will become to a greater or less extent nationwide, thus reducing, or avoiding, danger from any local depressions in business.

(2) *Character of risks.* As at present organized, the risks may cover farming lands of varying kinds and various subdivisions, such as high-class residences, medium-priced lots and mechanics' homes, thus reducing the chance of difficulties attacking any one class of purchaser.

(3) *Term.* No policy is given until the land is fully paid for, and, in the case of lots sold on any deferred-payment plan, the policy is not delivered for several years after the date of the contract between the owner and the company, and then runs for ten years. As the owner is allowed ten years to sell the land, the policy may not become effective for twenty years in extreme cases—in all cases the risks are spread over a considerable period.

It is noteworthy that in no form of insurance is the term so definitely fixed; no other form is definitely free from liability for a specified term and in no other form is there the certainty of some salvage value, for if one of these companies suffers a loss it must acquire property of some value.

Doubtless, as years progress, these insurance companies will organize holding companies to take over properties acquired on claims. This may in itself become a profitable business, for a purchaser may be willing to sell for cash at a low price, while a holding company after keeping the property for an interval may reasonably expect to sell at an advanced price when any temporary depression has passed, especially as it will be able to give easy terms for purchase.

Reserves. It is said that the companies now organized provide under their laws that 50 per cent. of all premiums received are set aside as a sinking fund which is invested and kept inviolable. The companies also say experience shows that losses never have averaged as high as 20 per cent. of the total amount insured.

On these bases they build the following conclusions:

Premiums on insurance of $100,000 at 6%	$6,000.00
of which 50% goes into the reserve	3,000.00
Invested for, say, 12 years at 6% this will amount to	6,036.00
The losses will not be as much as 20%, or less than	20,000.00
If we assume a salvage value of 70%	14,000.00
There must be provided	$6,000.00
Which is cared for by the above sinking fund of	6,036.00

Past experience indicates that the allowance of 20 per cent. for losses included in the above estimate is adequate. The arithmetic is easily verified. The only unknown quantity is the amount of the salvage value which must, necessarily, be estimated and must depend upon the good judgment of the officers and upon local conditions surrounding each case.

In all cases the operations of the companies are subject to the direct examination, or control, of the state insurance departments. The reserve is kept apart from all other funds and may be invested only in such securities as are designated by law as legal for investment by insurance companies.

HOW IS IT EFFECTED?

After the company has made its survey of a neighborhood and is ready to consider risks therein, the procedure is as follows and includes four stages, each of which is represented by a separate document:

1. An owner desiring land-value insurance makes application on a form provided by the company which states the maximum premium to be charged, the term, or period, for which the policy is to run, a detailed description of the property and the prices proposed by the owner. This application is accompanied by a cheque for $100 for each $100,000 of insurance desired, or any

fractional part of $100,000; e. g., an application for $550,000 would be accompanied by a cheque for $600.

2. If the application is declined, the deposit is returned in full to the owner. If the application is accepted, the company gives the owner a contract which sets forth:

(a) The total amount of insurance.

(b) The premium.

(c) An agreement by the company to issue a policy to the purchaser of any lot in the tract insured for the selling price of the lot as shown on the schedule submitted with the application.

(d) The contract covers all sales made within ten years from its date and provides that policies shall be issued to purchasers when they have fully paid for the lot insured and when they receive a deed to it.

(e) The year in which the loss is payable.

Upon executing the agreement the owner makes a second payment which, together with the deposit already made, equals one-half of one per cent. of the total selling value.

Further payments of premium are made by the owner as the purchaser pays for the land, each payment bearing the same ratio to the total premium as the corresponding payment made by the purchaser bears to the total price.

The rate of premium varies with the risk, as does the term of insurance, or the period which must elapse before the insurance becomes payable. The usual term of subdivision property is ten years and the average premium is six per cent. of the total amount insured. Policies may be written for shorter periods of from five years to nine years each, but the shorter the period, the higher the rate of premium, the rates running from 3.5 per cent. to 8 per cent.

In the case of farm lands, the rate of premium runs from four per cent. to nine per cent. on a ten-year period.

The policy, when issued, follows the land and is automatically transferred to each successive owner without notice to the company.

The policy is not issued until the purchaser has paid for his lot, and does not become payable until the end of the interim period. Therefore, if a purchaser pays cash on January 1, 1926, his policy will become payable in 1936, but if he contracts to buy the property on January 1, 1926, and does not pay in full until January 1, 1931, he does not receive his policy until 1931 and it will not become payable until 1941.

3. When any purchaser of an insured lot signs a contract to buy, he receives from the company an "interim certificate" in which the company agrees to issue to him, or his successors, a policy when the purchaser has completed his payments.

4. When a purchaser has completed his payments he receives the final policy which describes the property covered, states the amount for which it is assured and the year in which claim for payment may be made.

This policy sets forth the following conditions and terms:

> That the statements made regarding the property by the owner are correct.
>
> That the policy is transferable without notice to the company.
>
> That during the year in which the policy is payable the company will pay to the assured the amount it is insured for within 60 days of receipt of claim and proof of title, and the assured will convey the property to the company.

In the event that the property has been improved and a claim is made, the assured and the company will each name an appraiser, who may name a third if necessary, and they shall appraise the property, placing separate values on the land and on the improvements. If the appraised value of the land be less than the amount of the insurance, the company may take either one of two courses:

(1) It may pay the assured the difference between the appraised value and the amount of insurance, or,

(2) The company may pay the assured the appraised depreciated value of the buildings and the insured value of the land, in return for which the assured will convey the property to the company.

The company is not responsible for loss in value due to invasion, insurrection, riot, civil war, etc., or by condemnation proceedings, unless liability therefor is assumed by endorsement on the policy.

The assured has the privilege of proving loss by selling or conveying the property.

The policy is not a lien on the property and does not vest any right in the company.

The policy may be canceled by mutual consent of the company and of the assured.

The policy is void if other similar insurance be carried, or if any misrepresentation has been made.

No suit for recovery under the policy may be brought after twelve months from the termination of the policy.

To illustrate the treatment of a claim where improvements have been made, let us suppose that a lot is insured for $1,000; that on appraisal the value of the lot is placed at $750 and the depreciated value of the improvements at $5,000.

The company has the choice of paying the assured the amount of insurance, $1,000, and the value of the improvements, $5,000, i. e., $6,000 in all, and taking the property, or it may pay the assured the loss on the land, $250, and permit the assured to retain the property.

If an assured desires to secure a larger amount of insurance on his lot, he can make application therefor and if the company approves the new valuation additional coverage can be at once obtained.

WHAT WILL BE THE EFFECT OF LAND-VALUE INSURANCE?

The real-estate business has always presented some of the most striking contrasts to be found, for while land is the most staple commodity which we have the prices for it have been subject to more frequent and violent fluctuations than have most other commodities produced directly or indirectly from it.

Anything which will stabilize these prices must be of incalculable value. The direct products of the soil—wheat, corn and other crops—are judged by a more or less fixed standard, guaranteed by some form of official certificate. Foods we eat are warranted by the manufacturers to conform to legal requirements; the necessities and luxuries we buy, whether they be motor cars or pearl necklaces, are guaranteed by the firm from which we buy them, yet land is, and always has been, bought largely on the representation of a more or less—and often less—dependable salesman whose very living depends upon the commissions he receives for making sales.

Land-value insurance will both facilitate and simplify business; it will speed up sales and will reduce or abolish the resale habit.

If the Florida boom be taken as typical, one excellent result which remains is the added care with which attorneys examine titles. In former days the country attorney frequently assumed many facts; in boom times more careful examination brought to light many a hidden defect, and the public was driven to require title insurance. It seems to the writer that similar results may come from land-value insurance. If this once is generally demanded, no boom will be possible. Suitable and legitimate developments will be encouraged and insured; land in premature and unnecessary developments will not be sold because the owners will be unable to obtain the insurance which will be demanded.

The wise developer will welcome this insurance. It not only affords him an unbiased and trained opinion as to his suggested values, but it affords him a "selling argument" which is unsurpassed.

Land-value insurance is now obtainable in a number of widely separated states and it seems probable that its use will increase and may soon become nation-wide. However, the period of operations has been too short and the area covered too wide to enable one, at this time, to make any definite statement as to the financial results obtained by the various existing companies or as to the value of the security held for the assured.

While the observations of an individual person in such a matter as this are suggestive rather than conclusive, it seems only fair to give some of the facts which have come before the writer.

The writer has made some examination of the properties which have been accepted and others which have been refused by one company operating in the southern states, and he has no doubt that in those risks which have been accepted, when the policies mature, the lots will be well worth the amount for which they are insured, for the prices have no relation to those which obtained during the so-called boom.

The valuations which have been examined all give evidence of careful investigation and are supported by facts which appear to warrant fully the figures submitted.

Probably it will be generally admitted that the supporters of the movement have proved the possibility of writing land-value insurance on a safe basis; while there can be no doubt that such insurance, if sound, would be of enormous benefit to many purchasers.

Theoretically, land-value insurance may be placed on a basis at least as firm as was that for life, fire, marine or any other form of insurance in the early years of its existence. The practical results will always depend, as they do in the case of other insurance, upon the integrity and ability of the officers directing the individual companies and on the thoroughness of the inspection of state authorities to see that wise selections have been made and that all safeguards have been used.

This means that one accepting land-value insurance should exercise the same care as he would when buying any other form of insurance, and satisfy himself as to these matters. Especially should these precautions be most carefully observed by anyone obtaining such insurance and using it as an inducement to prospective purchasers of his property.

The requirements are simple in themselves and they call for no deep knowledge of mathematics. Any careful accountant should meet with no difficulty in preparing a report stating fully the conditions of any company and showing whether or not the safety requirements have been complied with.

It is hoped that this brief account may cause accountants to watch with care the progress of a new enterprise which if properly administered presents great promise.