

AN INVESTIGATION OF COSTS AND PRACTICES OF
PROPERTY INSURANCE OF KANSAS UNIFIED
PUBLIC SCHOOL DISTRICTS

by *DRU*

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PREFACE

This study developed as a result of personal interest in the subject generated during courses in school administration and business, and because of the apparent lack of similar research in the area. With the encouragement and patient direction of Dr. O. K. O'Fallon, the study proceeded to the point of collecting the necessary data from the various sources. At this point, a fact--often mentioned in the readings related to the study--became clear and immediate; namely, that adequate insurance records are often neglected. Although not true in every case, records were many times so inaccessible that they could hardly have been of effective use in the administration of the insurance program. As a result, some officials faced with questions about such records and their use in planning the insurance program, were unconcerned about the need, or defensive because of the lack.

School administration in general, and insurance in particular is an increasingly complex undertaking--one requiring analytical, unemotional study of the problems, based on complete and usable records. The efficient use of the financial support given education is always of concern in school administration; and it is hoped that the reaction to

this study will be an even greater concern for better maintenance of insurance records, and more effective use of those records in obtaining the coverage needed at the lowest possible cost-- in contrast to the reaction suggested by an anonymous author who commented, "Walter Leaf, the distinguished English banker, once declared that there are three main causes that dispose men to madness: love, ambition, and the study of currency problems. And the worst of these, he added, was the last. Mr. Leaf's use of the term "study" was probably an error. Love and ambition appear to induce madness, not because of their strain on the intellect, but because of their ability to over-excite the emotions. The same seems to be true of money; at any rate, the reaction to monetary problems has generally been more emotional than intellectual."

Any criticism implied in foregoing comments should be taken in a positive spirit, for it is not the author's intention to suggest that all the educational administrators, state officials, insurance representatives, and others who contributed to this study were neglecting their responsibility, or were uncooperative. On the contrary, without the courtesy, cooperation, and encouragement of these people, and particularly the help of Dr. O. K. O'Fallon, College of Education, Kansas State University, this study would not have been possible.

Duane R. Deyoe

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CHAPTER I

INTRODUCTION

In the United States today, as in most of the other countries of the world, rapidly increasing numbers of elementary and secondary students, and demands for a higher quality of education for them, have made the expansion and improvement of public educational systems imperative. This expansion and improvement requires great amounts of money--even now in short supply--and the future promises only rising costs for the necessary services and supplies. Education everywhere is facing a dilemma--of rising unit costs, and more students, combined with a slow-down in the rate of growth of financial resources. Education's share of national incomes and budgets has already reached a point that restricts the possibilities for adding on further increments, and yet, still more money must be made available for use if the needs of society and national development are to be satisfied. Clearly, the solution to this situation cannot be to simply continue increasing the total amount of financial resources made available for education. National budgets are of growing concern to countries around the world--and not only national budgets,

but state budgets as well. In the United States, and here in Kansas, taxpayers are rebelling against inequitable and ever-rising taxes, are refusing to approve the sale of bonds to finance educational development, and are becoming more and more critical of uses made of public funds. What, then, can be done to increase the money available for educational development, when the proportion of state and national budgets allocated to education may increase little, if any?

What can be done, and what must be done is to make more efficient use of those resources that are available. School administrators and Boards of Education must be even more concerned than before to establish priorities in budgeting--determining which budget items are essential to the operation of the school district, then working to provide those services necessary at the lowest possible cost. This may be achieved by making sure the service is purchased at the lowest prevailing price, or by cooperating with others in effecting lower prices.

One of the essential items in the on-going operation of the school, and a basic responsibility of the school district is, without question, the protection of the investment in educational facilities. Without adequate insurance protection on existing school properties, a school district risks losing thousands of dollars, in case of fire, wind, or hail damage

or loss. Few school boards care to be responsible for risking such a loss, seeking instead to transfer the risk, or to insure against the risk of loss. This has generally been accomplished by the purchase of property insurance from commercial insurance companies.

Commercial insurance represents one of the wealthiest businesses in the United States. Unnecessarily high premiums on fire and casualty insurance policies covering public school properties have, in some cases, aided in their achieving this degree of wealth.¹ School boards and their administrators, as stewards of public funds are expected to obtain a maximum of the insurance protection needed at a minimum cost. However, the establishment of the insurance rate, upon which the premium is based is a highly technical, scientifically designed procedure. The average school administrator is not an expert in the complexities of property insurance, and therefore has depended on other sources for advice and assistance. The most common source of such aid is a local agent-broker, or a local insurance board or association, who is expected to serve both the interests of the insurance companies represented, and the

¹Henry H. Linn and Schuyler C. Joyner, Insurance Practices in School Administration, (New York: Ronald Press Co., 1952), p. 73.

interests of the public schools. This situation implies a condition of conflict-of-interest, and though common, does not represent a desirable method of insurance administration. Although in many cases, insurance company representatives have served the public interest responsibly and well, there have been other cases where the pressure to take advantage of the trust and dependence placed in them has been too strong to resist, resulting in the payment of excessive amounts of public monies for school property insurance. This pressure to consider the interests of the insurer over the interests of the insured, is in many cases being exerted on the agent by the companies he represents. Insurance companies are exercising this power by cutting commission rates, dropping unprofitable agents, reversing their policy of protecting an agent who has made a mistake, and now by resisting marginal claims which earlier they might have paid to maintain the agent's favor.¹

By placing the responsibility for the insurance program in the hands of the insurance agent-broker, the school board and the administrator thereby puts both the insurance

¹Robert M. Morrison, "An Invitation to Schizophrenia," Best's Insurance News, Fire and Casualty Edition, 68:32, November, 1967.

representative and the school district in an awkward and vulnerable position. In the role of "agent", the insurance representative is expected to sell as many types of coverage with a high profit-ratio as possible, and while doing so, to avoid insuring the less desirable risks. The insurance companies judge their agents' value to them on the basis of the total volume of profitable business written, not an index of public spiritedness. In the role of "broker", on the other hand, the insurance representative is expected to secure for the school district only those types of coverage which are absolutely necessary for the adequate protection of the property, and to do so at the lowest possible cost. The insurance representative must then attempt to balance his responsibility to the insurer--his employer--and to the insured--his customer.

In far too many cases, the school district expects the insurance representative not only to buy the needed insurance protection, but also to maintain the records kept on the insurance program. If the particular agent-broker representing the school district changes, or if he becomes ill or dies, or goes on vacation, a situation could result with no continuity of record-keeping, or no access to the records kept, or records with meaning only to that agent-broker. Authorities in School Administration have encouraged better record-keeping for years,

yet a failing of many school administrations continues to be poor maintenance and use of meaningful insurance records.

Kansas public schools have a property investment in buildings and contents valued in excess of \$785 million, as shown in Table VIII. The potential loss of an investment of this magnitude requires that boards of education maintain adequate protection against the loss of these properties and make provisions for their rapid replacement in the event of loss. When planning for insurance protection, one must first consider the amount of possible loss, then the probability of loss. Although fire losses for public schools seem to be relatively low compared to other risks, Kansas educational institutions have, in the ten-year period from 1957-1966, suffered losses from fire in excess of \$1,570,000 (Table I). Losses from wind and hail damage also represent a large amount. In addition to the financial loss, one must consider the irreplaceable educational time lost to the students while financing for the replacement of facilities is being developed, and educational losses suffered from diverting educational funds to the replacement of facilities.

In carrying out the responsibility to protect the district against the risk of financial loss, the school board and administrator must also retain the responsibility

TABLE I
 FIRE LOSSES OF KANSAS EDUCATIONAL
 INSTITUTIONS, 1957-1966*
 (PUBLIC AND PRIVATE)

Year	Number of Fires	Amount of Fire Loss
1957	2	\$ 21,668
1958	13	26,074
1959	16	374,775
1960	10	51,715
1961	11	25,775
1962	28	132,489
1963	8	5,120
1964	15	332,698**
1965	22	378,840
1966	18	221,765
Total: 10 year period 143		\$1,570,899

*As reported by local Fire Chief, and compiled by Office of State Fire Marshall, State Office Building, Topeka, Kansas. (Data compiled yearly, with biennial reports published.)

**One loss, at Girard, accounted for 84% of total fire loss of all Kansas Educational Institutions in 1964.

for the insurance program. Those responsible must know what they are buying, and how much they are paying for it. The fact that this goal is not always achieved is indicated by Finchum, who states that, ". . . it is probable that expenditures for insurance premiums covering the protection of school property receive less careful attention and investigation by school authorities than any other phase of the school budget."¹ Without understanding of, and attention to the insurance program of the school district by the administrator responsible, there is always the possibility of the school district paying more, and receiving less than it should. And without complete and meaningful records of the insurance program, maintained by the school district itself, there is little chance that those whose responsibility it is, will know what coverage they have and what its cost to the district is. Furthermore, without adequate records, and attention to insurance costs for public schools on the state level, it is difficult if not impossible to determine whether current rates are justified, or to adjust them if they are not. For example, Englehart writes:

¹R. N. Finchum and N. E. Viles, School Insurance--Managing the Local Program, (U. S. Department of Health, Education, and Welfare, Government Printing Office, Washington; 1960), p. 65.

It has been my experience that the data you desire [property insurance loss-ratios for public school buildings] can be obtained only from the school districts. These have been so numerous in Missouri that we have been unable to obtain information of this type which we felt was reliable. While the loss ratio for educational buildings in this State has been rather low, it is our opinion that the ratio for public buildings [educational] has been considerably lower. It has not been possible, however, for us to gather data that would be necessary to influence insurance premium rates.¹

The Problem

There is considerable evidence that the premium-loss ratios for commercial insurance of public school properties in other states have been lower than those of similar properties, and that consequently, public schools in those states--and by inference, Kansas--have paid excessive and inequitable premiums for the insurance protection received. There are also indications that public school districts have not taken advantage of existing methods of lowering insurance costs, and that more effective practices of administering the insurance program are possible. These situations are contrary to the public interest, and should be adjusted, if they are

¹Personal Correspondence of Author, letter from George D. Englehart, Director of School Building, Missouri Department of Education, November 14, 1967.

indeed true. However, no evidence was encountered that a study of this kind had ever been made in the State of Kansas--with the result that countering arguments on both sides of the question have been based too often on emotion, rather than fact.

Purpose of the Study

The purpose of this investigation was to determine whether or not costs have been equitable and reasonable for property insurance of Kansas public schools.

Method of Research

To achieve the purpose of this investigation, the following questions were selected for specific study.

1. What is the nature and history of insurance?
2. What forces affect the operation of commercial insurance companies?
3. What has been the profit-loss experience of commercial companies?
4. What regulations affect Kansas public school districts in the purchase of property insurance?
5. What has been the experience of insurance rates affecting Kansas public school districts?
6. Have premium-loss ratios for Kansas public school property insurance been equitable--compared to ratios for all insurance business?

7. Have practices of property insurance administration by public school districts been effective in obtaining necessary insurance coverage at a reasonable cost?

An extensive survey of related literature and several interviews were conducted in order to answer the preliminary questions, and thereby gain both an orientation in the field of the problem, and an understanding of the opinions and points of view of authorities.

Included in the review of related literature were textbooks in school administration and business management, as well as periodical literature in the field. To gain a perspective of the insurance industry, textbooks pertaining to insurance administration, and insurance trade journals were surveyed. Also, insurance manuals written for school boards and administrators, and doctoral studies related to the subject were studied. In addition, a good deal of information was volunteered in correspondence by authors of certain of the above sources, and by departments of education and insurance in Kansas and states with self-insurance programs covering public schools.

Personal interviews were also helpful in gaining an orientation in the subject. These were with local and state

officials and representatives of: commercial insurance companies; the Kansas Inspection Bureau; the Kansas Association of School Boards; the Kansas Department of Insurance; the Kansas Department of Education; the Kansas State Architect; the Kansas State Fire Marshal; the Kansas Director of Revenue; and the Kansas State Auditor.

Several directly related problems and considerations affected the collection of information necessary to answer the specific questions about Kansas public school property insurance costs. A major problem was the basic reason for insurance--protection against large and uncertain, or catastrophe loss. The possibility of single losses of thousands of dollars required as large a sample of information as possible, in order to avoid the bias probable in a small sample--where one large loss could greatly affect the total results. Should the sample, then, have great breadth--with many school districts represented, or great depth--with data from several years?

In discussions with officials of the Kansas Department of Education and the Kansas Department of Insurance, it was found that no collection of the specific data desired was made by either department. Also, Englehart had suggested that "it has been my experience that the data you desire can

be obtained only from the school districts."¹ Therefore, with the advice of those experienced in the collection of such data, it was decided that the information necessary should be gathered from the school districts, by a combination of a questionnaire sent with a cover letter, followed by a scheduled personal visit and interview, when the questionnaire information could be collected and verified. The use of only a mailed questionnaire was rejected because of the type of data desired--requiring a detailed search in school records and with the probable result of either incomplete and inaccurate information, or a low percent of return of questionnaires.

In selecting the particular school districts for the study, the following factors were considered. First of all, the districts studied should be representative of all those about which inferences would be made. Second, the individual districts selected should be large enough to be reasonably sure the records desired would be available. And, third, the total sample should be large enough in size to yield representative information, yet small enough to make personal visits possible. With these considerations in mind, a random sample of thirteen unified public school districts in cities

¹Ibid.

of the First and Second Class over 2,500 population were selected for study, the geographical distribution of which is shown in Appendix B. Furthermore, it was decided that information to be collected should cover a ten-year historical review of the premiums paid and losses incurred for the representative sample, and a review of the current practices of the same districts in administering the insurance program.

The questionnaire to be used was developed through the survey of related literature, with suggestions from authorities on the problem. After development of the questionnaire, and selection of the districts in the sample, contacts were made with the administrators of the districts concerned. The questionnaire, with a cover letter by the author outlining the study, and one by the author's graduate advisor requesting the district's cooperation was sent to each of the school districts to be studied. A schedule of visits was arranged, and the author personally interviewed the appropriate people in each district who were responsible for the insurance program. In certain cases, follow-up visits and/or correspondence was necessary to obtain additional information. Despite the detailed procedure used, however, some districts were unable to supply complete information, due to lack of the appropriate records.

Delimitations and Definitions

Delimitations. Because of the possible lack of records in small districts and other factors mentioned above, this investigation was limited to Kansas unified public school districts which included cities of the First and Second Class with over 2,500 population. Data collected and compiled was limited to premium-loss ratios and selected insurance administration practices of property insurance on the above school districts.

Definitions. Terms as used in this study were defined as follows:

Agent of Record (Broker of Record) - the agent or broker named by the insured as his exclusive representative in negotiations with insurance carriers.

Deviation - the amount by which a rate differs from one published by a rating bureau.

Earned Premium - that part of an insurance premium which pays for the protection the insurance company has already given on a policy.

Experience - the loss record of an insured or of a class of coverage.

Extended Coverage - a clause in an insurance policy or of an endorsement of a policy which

provides extra or additional coverage for other hazards or risks than those provided for under the basic provision of the policy. Normally covers loss by windstorm, hail, explosion, riot, riot attending a strike, civil commotion, aircraft, vehicles, and smoke.

Hazard - a condition that creates or increases the probability of loss.

Insurance - a plan, by which the pooling technique is used to substitute an average certain loss for an uncertain actual loss. Thus, a premium, or average loss, is paid by the insured, and the insurer assumes payment of the actual losses incurred.

Loss Ratio - the relationship between premiums collected and losses paid; derived by dividing the dollar amount of losses by the premium and expressed as a percent.

Risk - the person or property insured; the chance of loss.

Unearned Premium - that portion of an insurance premium covering the unexpired term of the policy or the unexpired period of the premium.

CHAPTER II

REVIEW OF SELECTED LITERATURE

History of Insurance

The earliest and most important branch of insurance business was marine insurance, which developed from the Greeks, who may have used a form of bottomry bonds as early as the Trojan War.

English merchants seem to have practiced a form of marine insurance as early as the thirteenth century, but there is no evidence of any definitely settled regulations or methods of carrying on insurance business in London before the latter part of the 17th century. A popular meeting place for seafaring men and merchants was Lloyd's Coffee House. As early as 1688, the shippers would gather at Lloyd's and pass around a slip of paper on which was written a description of the vessel and its cargo, name of the Master and type of crew, and the voyage contemplated. Those desiring to be insurers would sign the bottom of the slip and indicate the amount for which each would be liable as an insurer. From this practice at Lloyd's is derived the term, "underwriter," as now applied to insurers. Due to the expansion and growth

of business the enterprising proprietor was forced to move several times. The corporation itself does no underwriting, but the members of Lloyd's underwrite all forms of insurance.¹

The first permanent fire insurance company in America was the Philadelphia Contributionship, a mutual, founded in 1752. It used two clasped hands as its "fire mark", an emblem that policyholders were required to attach to the outside of their buildings so that firemen would know what buildings were insured. Benjamin Franklin was one of the original directors of the Philadelphia Contributionship, and printed its early policies.

The oldest American stock fire insurance company is the Insurance Company of North America which began in 1792 in Pennsylvania. Lack of capital in the colonies prevented the formation of American stock companies prior to that time.²

Regulation and Competition Affecting Commercial Companies

From this early beginning, commercial mutual and stock insurance companies have grown to become one of the

¹C. F. Trennery, The Origin and Early History of Insurance (London: King and Son, Ltd., 1926), p. 54, as cited by George R. Robinson, State Insurance of Public School Property in Michigan (Detroit: Wayne University, 1956), p. 7.

²Ibid.

biggest industries in the United States. Because of the many companies writing insurance, the industry is affected by considerable competition; and, because of the tremendous financial power the industry holds, it is subject to varying degrees of regulation.

The regulation and supervision of insurance in Kansas are functions of the State Department of Insurance. This agency, financed by legislative appropriation, indirectly returned over \$10,000,000 in fiscal 1969 to the State from a 2% tax on premiums written in the State. The primary duties of the Department include the following six categories: 1) To determine what companies are authorized to transact business within the state and to supervise and regulate their business; 2) To supervise and record policy forms used in the state; 3) To approve and record the rate or premium charge for a given coverage--an attempt by the Legislature to protect the insured from an overloaded or discriminatory premium; 4) To supervise claims practices of insurance companies; 5) To license agents and exercise control over the methods by which the agent may solicit business; and, 6) To supervise the deposit of securities by the insurance companies with the State Treasurer.¹

¹Ninety-seventh Annual Report of the Kansas Commissioner of Insurance, (Topeka: State Printer, 1967), p. 4.

Rate Regulation. The authority of the State Insurance Commissioner includes the approval or disapproval of rates; however, the job of actually determining the rates to be submitted for approval is carried on by a central rating agency, the Kansas Inspection Bureau. The Kansas Inspection Bureau is the fire rating organization licensed under the Kansas Statutes as the rating organization for about 275 of the stock, reciprocal, and mutual fire insurance companies doing business in Kansas. Thereby, the Bureau is the legal representative of each and every member and subscriber company for various filings with the Insurance Department.¹ It should be mentioned that although the Kansas Inspection Bureau represents member companies, it is not a state, but a private organization. Also, rates set by the Bureau are only advisory, and are not binding on the member companies. Therefore, it is not unusual for companies to file "deviated" rates with the Insurance Commissioner. Insurance rates are determined by experience, from statistical loss ratios by classes--construction, occupancy, protection, and exposure to hazards ("COPE"). Several

¹Peter F. Caldwell, The Insurance Manual for Local Governments, (Topeka, Kansas: The League of Kansas Municipalities, July, 1954), p. 50.

different classes of construction, of occupancy, of protection by local fire departments, and of exposure to nearby inflammable structures exist, with various combinations of classes-- each given a rating which determines the premium to be paid.

Underwriting and Investment Income. The insurance industry is increasingly concerned about further regulation of rates, arguing that--contrary to claims by some groups-- the industry is, in fact, not making excessive profits, but is frequently losing money on underwriting. It has been stated that stock companies, collectively, have not made a satisfactory underwriting profit since 1955, and many have operated in the red (underwriting profits) more often than in the black.¹ From these statements, it would appear that insurance companies must surely fail. However, the insurance industry has been able to make a considerable profit from the investment of their reserves, which lessens the impact of complaints about underwriting losses. The property-liability industry had previously enjoyed more than 20 years of profitable underwriting, according to Best's Insurance News, and had been able to acquire a sizeable portfolio of high

¹"Review and Preview," Best's Insurance News, Fire and Casualty Edition, 68:10, January, 1968.

grade common stocks. Therefore the industry entered the period of marginal profits in good financial condition and, by participating through stock ownership in the record earnings of most other segments of the business world, was able to maintain a sound financial structure.¹ As reported in May, 1969, ". . .the investment side of the picture has been unbelievably favorable during the long period of unsatisfactory underwriting results. Net investment income showed a steady rise year after year, up 11% in 1968, and there was substantial appreciation in the market value of stocks owned in 10 of the last 15 years with only three years recording depreciation in value."²

There is, and has been for several years, a heated debate as to the size and adequacy of the profits in the industry. On the one hand, a study by the professional economists of Arthur D. Little Company showed that on the basis of ten years' experience, the insurance industry is earning inadequate remuneration on the capital invested. They arrived at the figure of 4.4% for 43 property and

¹Ibid.

²"Stock Company Operating Results," Best's Review, Property and Liability Edition, 70:14, May, 1969.

casualty insurance groups.¹ Countering that report was one which followed shortly thereafter, by other professional economists who, using a different approach, a different sample, and a fifteen year period, came to the conclusion that a "vast majority of these companies is experiencing more than satisfactory risk returns."² Continuing the debate, Balcarek cites the Little report [insurance as an industry produced the lowest return on net worth of 59 industries with which it was compared], arguing that commercial companies must maintain competitive profit levels with other industries in order to hold sufficient capital investment in the industry--that with lower profits, capital will move to other investment ventures and insurance companies will be faced without sufficient reserves, or new capital for growth.³

Reviewing operating results of stock companies in the United States from 1944-1968, shown in Table II, one can see

¹David M. Boodman and Irving H. Plotkin, "Prices and Profiles in the Property and Liability Insurance Industry," (report for A. D. Little Co.), as summarized in "Profits and Investment Income," Best's Insurance News, Fire and Casualty Edition, 68:14, March, 1968.

²R. L. Norgaard and C. J. Schick, "Profitability in the Property and Liability Insurance Industry," as cited by R. J. Balcarek, "The Capital Investment Market and the Insurance Industry," Best's Review, 69:16, April, 1969.

³Ibid.

TABLE II
 OPERATING AND UNDERWRITING RESULTS, 1944-1968
 ALL STOCK FIRE AND CASUALTY COMPANIES
 WRITING IN UNITED STATES*

Year	Premiums Written	Premiums Earned	Loss Ratio**	Expense Ratio***	Combined Ratios
1944	2,258,133	2,128,103	55.7%	38.7%	94.4%
45	2,424,651	2,256,218	57.0	38.8	95.8
46	3,063,044	2,260,202	59.6	39.2	98.8
47	3,862,123	2,286,928	58.4	37.9	96.3
48	4,403,010	3,992,930	53.9	37.3	91.2
49	4,759,920	4,424,339	50.2	37.4	87.6
50	5,137,527	4,766,434	55.5	37.5	93.0
51	5,758,796	5,378,960	60.2	36.9	97.1
52	6,410,590	5,994,398	58.4	36.0	94.4
53	7,000,347	6,661,360	57.2	35.9	93.1
54	7,143,593	6,991,598	56.9	36.7	93.6
55	7,662,138	7,341,824	58.2	36.7	94.9
56	7,991,071	7,743,974	63.4	37.1	100.5
57	8,640,093	8,325,467	66.2	36.7	102.9
58	9,076,828	8,840,841	63.7	36.3	100.0
59	9,930,697	9,526,359	62.5	35.3	97.8
60	10,527,285	10,263,741	63.6	34.8	98.4
61	10,783,344	10,707,244	64.4	35.0	99.4
62	11,599,075	11,284,633	64.5	34.5	99.0
63	11,880,747	11,594,850	66.3	34.7	101.0
64	12,647,613	12,347,164	68.0	33.9	101.9
65	13,855,059	13,378,641	69.2	32.7	101.9
66	15,196,561	14,654,787	66.2	31.9	98.1
67	16,343,457	15,853,197	67.2	31.7	98.9
68****	17,750,000	17,200,000	69.0	31.5	100.5

*"Stock Company Operating and Underwriting Results," Best's Review, Property and Liability Edition, 70:14, May, 1969. [All dollar amounts shown in thousands (last 000 omitted).]

**Losses incurred to premiums earned.

***Expenses incurred to premiums written.

****Estimated.

the trend toward higher combined loss and expense ratios, with several years showing an underwriting loss. However, Harwayne contends that it is profitable for the insurers to remain in the insurance business with combined loss and expense ratios of 104.5% in casualty and 106.3% in fire.¹ Data supporting this argument can be found in Table III comparing stock company operating results of 1967 and 1968, and in Table IV showing mutual company operating results for the same period. As shown in Table III, 154 stock companies recorded a net investment income of \$882,769,000 in 1967 and \$979,874,000 in 1968. This was an 11% increase in net investment income from 1967 to 1968, with the net investment income for each year representing nearly seven percent of the net premiums earned. Table IV shows data for 78 mutual companies who, in 1967, earned a net investment income of \$255,431,000-- 5.3% of the net premiums earned. This compared to a net investment income the following year of \$288,407,000, an annual increase of 12.9% and 5.4% of the net premiums earned. While it seems that insurance underwriting in the past few years has not always been profitable, it is also clear that

¹Frank Harwayne, "Insurance Risk, Investment and Profit," CPCU Annals, March, 1967, as cited by Balcarek (above).

TABLE III

STOCK COMPANY OPERATING RESULTS*

	1967	1968	% Change
Net Premiums Written	\$ 13,592,028,000	\$ 14,751,133,000	+8.5
Net Premiums Earned	13,161,279,000	14,272,886,000	+8.4
Loss Ratio ^a	67.5%	69.3%	
Expense Ratio ^b	31.5%	31.1%	
Combined Ratio	99.0%	100.4%	
Underwriting Profit or Loss	\$ 3,622,000	\$ -212,970,000	
Net Investment Income	882,769,000	979,874,000	+11.0
Other Investment Gains	1,127,856,000	978,942,000	

*"Stock Company Operating Results", Best's Review, Property and Liability Edition, 70:14, May, 1969. [154 stock companies representing 85% of stock company volume.]

^aLosses incurred to premiums earned.

^bExpenses incurred to premiums written.

TABLE IV

MUTUAL COMPANY OPERATING RESULTS*

	1967	1968	% Change
Net Premiums Written	\$4,958,774,000	\$5,490,094,000	+10.7
Net Premiums Earned	4,848,592,000	5,332,857,000	+10.0
Loss Ratio ^a	73.6%	75.0%	
Expense Ratio ^b	23.4%	23.3%	
Combined Loss & Expense Ratio	97.0%	98.3%	
Underwriting Profit	\$ 113,778,000	\$ 45,047,000	
Net Investment Income	255,431,000	288,407,000	+12.9
Other Investment Gains	81,226,000	159,487,000	

*"Mutual Company Operating Results," Best's Review, Property and Liability Edition, 70:15, May, 1969. [78 mutual companies representing 80% of mutual company volume.]

^aLosses incurred to premiums earned.

^bExpenses incurred to premiums written.

investment income has been sizable, offsetting low underwriting profits or losses, and negating claims that insurance companies are losing money.

A part of the debate on over-all profits of insurance companies has been the question of whether or not the investment income of insurance companies should be considered in the setting of rates. Those in the insurance industry are naturally opposed to such an idea, and base their primary argument on the A. D. Little report--supported by the American Insurance Association at a cost of \$150,000. The Association feels that the authoritative report will be very helpful in countering claims that profits are too high, or that investment income should be used in figuring rates.¹ It is Mosely's opinion that investment income from any source should not be reflected in the establishment of insurance rates. He says, "the insured pays a premium and for this premium he receives protection. . .not a share in the property of the company or its use."²

In spite of the above stated opinions, many in the insurance field feel that the industry must change by itself,

¹"Profits and Investment Income," Best's Insurance News, Fire and Casualty Edition, 68:14, March, 1968.

²Jack Mosely, "Investment Income and Ratemaking," Best's Insurance News, Fire and Casualty Edition, 68:24, July, 1967.

or it will be forced to change. "The industry should brace itself," says J. M. Muir, "for a form of rate regulation involving the states and the federal government as well." He further suggests that the time is long over-due for a code of ethics which will bring about self-regulation and self-restraint.¹ In encouraging this self-regulation, John Adam, Jr. comments, "it is time that the insurance industry realized that it exists only by public consent. Carrying on the insurance business is not an inalienable right, but rather a privilege granted the industry by the public as long as the industry remains a relatively effective means of satisfying the public's protection needs."²

There have been gradual changes in the insurance industry, changes which can be seen in the operating results of stock companies (Table II), and the operating results of 350 mutual companies (Table V). When one compares the expense ratio of stock companies to that of mutual companies, it is clear that the insured pays more for overhead with a stock

¹J. M. Muir, "Effects of Legislation and Regulation on Insurance Rates, Filings, Policies, and Underwriting," Best's Insurance News, Fire and Casualty Edition, 68:20, February, 1968.

²John Adam, Jr., "Guidelines for Tomorrow," Best's Insurance News, Fire and Casualty Edition, 68:34, March, 1968.

TABLE V
 OPERATING RESULTS, 1949-1968 FOR 350 MUTUAL
 PROPERTY AND LIABILITY COMPANIES
 WRITING IN UNITED STATES *

Year	Premiums Written	Premiums Earned	Loss Ratio**	Expense Ratio***	Combined Ratios
1949	\$1,171,260	\$1,139,003	61.0%	23.1%	84.1%
50	1,326,761	1,289,145	65.6	22.2	87.8
51	1,658,657	1,551,413	60.3	24.8	85.1
52	1,883,853	1,770,311	60.5	24.7	85.2
53	2,186,191	2,079,785	60.3	24.4	84.7
54	2,278,133	2,222,803	59.3	25.3	87.6
55	2,384,953	2,330,535	61.3	26.0	87.3
56	2,609,008	2,527,441	65.0	26.3	91.3
57	2,889,950	2,790,778	65.5	25.8	91.3
58	3,119,764	3,021,998	64.9	25.6	90.5
59	3,475,454	3,357,201	64.7	25.3	90.0
60	3,723,054	3,650,253	64.2	25.6	89.8
61	3,945,198	3,882,645	63.6	25.6	89.2
62	4,038,063	4,046,809	66.7	25.7	92.4
63	4,447,105	4,239,687	71.4	26.5	97.9
64	4,766,940	4,651,380	73.4	25.9	99.3
65	5,195,644	5,036,114	73.1	25.0	98.1
66	5,788,420	5,617,431	70.9	24.2	95.1
67	6,292,226	6,135,609	72.7	24.6	97.3
68***6	9,000,000	6,750,000	74.0	24.5	98.5

*"Mutual Company Operating Results," Best's Review, Property and Liability Edition, 70:15, May, 1969. [All dollar amounts shown in thousands (last 000 omitted).]

**Losses incurred to premiums earned.

***Expenses incurred to premiums written.

****Estimated.

company. It is also evident, however, that the stock companies, as a group, have been gradually lowering their expense ratio, whereas the mutual companies have not. Part of the reduction in expenses is a result of reducing the responsibility of the local agent-broker, and at the same time, reducing his commission. Companies are resorting to direct billing from a central office, and encouraging the selling of "package" insurance programs--with many different types of insurance in one "package." This has the advantage to the school district of combining as many of the essential coverages with one premium, and under one policy written by one agent with one insurance company and with one expiration date. Also known as "special multiperil insurance", the plan has the advantage to the company of making the school district a larger and more valuable client, with one policy to write and one agent's fee to pay, as well as a general reduction in paperwork--all of which combine to permit a reduction in the premium.¹

The multiperil policy has advantages to the company, and to the customer, but not necessarily to the agent. According to Christie, the commission paid to agents by primary

¹Robert W. Schaerer, "Package Plan Cuts Insurance Costs," Nation's Schools, 73:64, February, 1964.

companies on regular fire business usually starts at around 25% or more. On multiple peril business, however, depending on the mix of the particular policy form, the situation is such that companies have almost no minimum and some occasionally pay as little as 5%. On the whole, the going rate of commission for multiple peril business is about 7% below that which is paid for straight fire business.¹ This reinforces the predictions of Morrison, who states that the conflict of interests built into the American agency system is beginning to tear that structure apart--with the agent under greater pressure from the insurers he represents to adjust his business methods and attitudes so as to help them in their competitive battle with other insurers, and at the same time, still expected to secure for the insured a maximum of protection at a minimum cost.² This situation makes it all the more important for the school administrator to be thoroughly knowledgeable of the various policy plans available, and to have well-maintained records on the school district's insurance program, thus being better able to talk

¹ David G. Christie, "Re-insurance Rating Techniques," Best's Insurance News, Fire and Casualty Edition, 68:81, March, 1968.

² Robert M. Morrison, "An Invitation to Schizophrenia", Best's Insurance News, Fire and Casualty Edition, 68:30, November, 1967.

with insurance company representatives about the insurance needs, and at the same time, being alert to any attempts to take advantage of the school district.

Competitive Bidding. Another aspect of competition affecting commercial companies in relation to school property insurance is the use of competitive bidding in placing the school insurance business. This is also a widely debated issue concerning school insurance costs, but one which offers some potential for reducing those costs. According to authorities, competitive bidding can be of definite advantage in lowering insurance costs, while still maintaining the standards of service and reliability desired in the insurance program.¹

Competitive bidding is a common requirement for school districts in making sizeable purchases of supplies and the contracting of work to be done. Insurance has not generally been included as a purchase requiring competitive bidding, but

¹Paul B. Salmon, Fire Insurance Principles and Practices, Bulletin No. 18 (Evanston, Illinois: Association of School Business Officials, 1958), p. 26; George R. Robinson, State Insurance of Public School Property in Michigan (Detroit, Michigan: Wayne University, 1956), p. 21; Clifford H. Allen, School Insurance Administration (New York, N. Y.: The MacMillan Company, 1965), p. 4; R. N. Finchum, Fire Insurance Economies Through Plant Management, (U. S. Dept. of Health, Education, and Welfare. Washington: U. S. Government Printing Office, 1964), p. 60.

at the same time, is not limited from it either. In fact, the 1968 Kansas Legislature established a definite precedent for the use of competitive bidding in the purchase of insurance, as follows:

" . . . The school district shall purchase insurance as provided in this act [motor vehicle liability insurance and medical payment insurance] only after it has invited sealed proposals for such insurance by advertising once weekly in a newspaper having general circulation in the school district for three consecutive weeks. Such insurance shall be purchased from the lowest responsible bidder. The school district may accept or reject any or all bids. The term of any policy of insurance purchased under the provisions of this act shall not exceed three years."¹

If competitive bidding is to be used as the method of placing the insurance, a set of well-defined specifications must be established to include:

- a. The amount and type of coverage desired;
- b. The minimum eligibility for participating companies;
- c. The right of the school district to apportion the business in case of identical bids;
- d. The right of the school district to accept or reject all bids.²

¹K. S. A. 72-8404 (1968 HB 2053, Sec. 10).

²M. A. McGhehey and Lloyd P. Elliott (eds), School Insurance - A Handbook for School Boards, (Topeka, Kansas: The Kansas Association of School Boards, 1965), p. 33.

In listing specific items to be included under the above headings, Finchum suggests that both a "bid document" and a two-part "specifications document" should be prepared for the use of prospective bidders.¹

The preparation of the necessary documents, arranging the bidding procedure, and advertising the bidding obviously requires an informed school official with good records available. Also, this requires an investment in time and effort exceeding that of other methods of placing the insurance business. Yet, resulting lower insurance costs to the school district could be well worth the investment in time and effort. An increasing number of school boards are placing their property insurance by competitive bidding, a practice which is highly recommended.²

Regulation Affecting Kansas Public Schools

Public schools are accountable for ways in which the public funds entrusted to them are expended. In keeping with this principle, various regulations have been established by

¹R. N. Finchum, Fire Insurance Economies Through Plant Management, (U. S. Department of Health, Education, and Welfare. Washington: U. S. Government Printing Office, 1964), p. 60.

²Calvin Grieder, Truman M. Pierce and William E. Rosenstengel, Public School Administration. (New York: The Ronald Press Company, 1961), p. 573.

law to govern expenditures, a number of which affect Kansas public schools in the purchase of property insurance. Until March, 1968, with the passing of Senate Bill No. 327, Kansas public school districts were not specifically authorized by law to purchase any insurance coverage other than Motor Vehicle Liability.¹ Previous to the amendments contained in this Bill, school districts did, of course, buy insurance coverage on the property owned by the district, but with only the implied authority that "the board of education shall have the duty of care and repair of school property."² As required by law, the annual audit of the school records routinely reported that money had been expended for the purchase of property insurance, without the specific legal authority to do so. The County Attorneys commonly ignored the legal questions posed by the practice, as the need for fire and extended coverage insurance on school property was obvious and unchallenged. Senate Bill No. 327 amended the statutes concerning insurance for municipalities, finally making the long-established practice of purchasing property insurance by public school districts unquestionably legal.³

¹K. S. A. 12-2601, 2602 (Appendix C).

²McGhehey, op. cit., p. 7.

³Senate Bill No. 327, amending K. S. A. 12-2601 (Appendix D).

Additional regulations affecting property insurance for Kansas public schools are those having to do with construction requirements established by law. These requirements provide certain standards of fire protection, and comply with the Building Code of the National Board of Fire Underwriters, and the National Electric Code of the National Fire Protection Association. All plans must be reviewed and approved by the State Architect before contracts may be let or funds expended for the construction of school buildings.¹

¹K. S. A. 72-4604 (Appendix C).

CHAPTER III

PROPERTY INSURANCE COSTS AND PRACTICES OF KANSAS UNIFIED PUBLIC SCHOOL DISTRICTS

Introduction. As was stated earlier, the purpose of this study was to determine whether or not property insurance costs for unified public school districts in Kansas have been equitable and reasonable. As was shown, there is much evidence that on a nation-wide basis, commercial insurance companies have been making a considerably smaller profit on underwriting since the mid-1950's. The data available is on the basis of the total business of the companies reporting, however, and does not reflect the specific portion of business which school property insurance represents. Furthermore, the information presented about insurance to this point, has not been restricted to that in Kansas--the area of concern in this study. The information following was collected from the Kansas Department of Insurance, the Kansas Inspection Bureau, and the Kansas unified public school districts included in the random sample of districts which included cities of the First and Second Class. The findings presented here provide the

basis for conclusions and recommendations regarding property insurance costs and practices.

Analysis of Findings. An important consideration in the analysis of property insurance costs for Kansas public schools is the evaluation of both fire and extended coverage costs. Many previous studies of insurance costs for school properties in the United States have been concerned only with fire coverage without consideration to extended coverage--and protection against loss by two primary hazards in Kansas, windstorm and hail.

Data presented in Table VI, collected from records of the Kansas Department of Insurance, shows the loss ratios for fire and for extended coverage of companies writing insurance in Kansas from 1959-1966. As mentioned earlier, records kept by the Department of Insurance did not include separate information for public school property--the figures shown here are for the total volume of business for the coverages shown.

Comparing the loss ratios of the two coverages, year by year, it is clear that extended coverage--an important part of the total property insurance program--has generally maintained a much higher loss ratio than fire coverage. Therefore, the inclusion of figures for extended coverage tends to raise the combined loss ratio, giving a more

TABLE VI

FIRE AND EXTENDED COVERAGE INSURANCE
 PREMIUMS AND LOSSES FOR KANSAS,
 ALL COMPANIES
 1959-1966

Year	FIRE		EXTENDED COVERAGE		TOTAL FOR BOTH			Loss Ratio*
	Direct Premiums Earned	Loss Ratio*	Direct Premiums Earned	Loss Ratio*	Direct Premiums Earned	Losses Incurred	Loss Ratio*	
1959	\$21,311,128	44.0%	\$19,843,942	36.0%	\$41,155,070	\$16,520,715	40.1%	
1960	21,092,130	41.4	17,967,035	59.1	39,059,165	19,349,660	49.5	
1961	20,361,477	41.2	15,692,302	64.6	36,053,779	18,526,156	51.4	
1962	18,980,376	47.8	14,535,034	86.4	33,515,410	21,630,889	64.5	
1963	19,179,608	48.0	13,488,303	67.7	32,667,911	19,551,740	59.9	
1964	18,214,744	49.3	12,882,306	62.5	31,097,050	17,021,310	54.7	
1965	17,823,721	42.9	12,433,221	44.4	30,256,942	13,166,746	43.5	
1966	18,523,360	51.1	12,613,847	159.3	31,137,207	29,559,296	94.9	
Total for 8 year period					\$274,942,534	\$155,326,521	56.5%	

*Losses Incurred/Direct Premiums Earned.

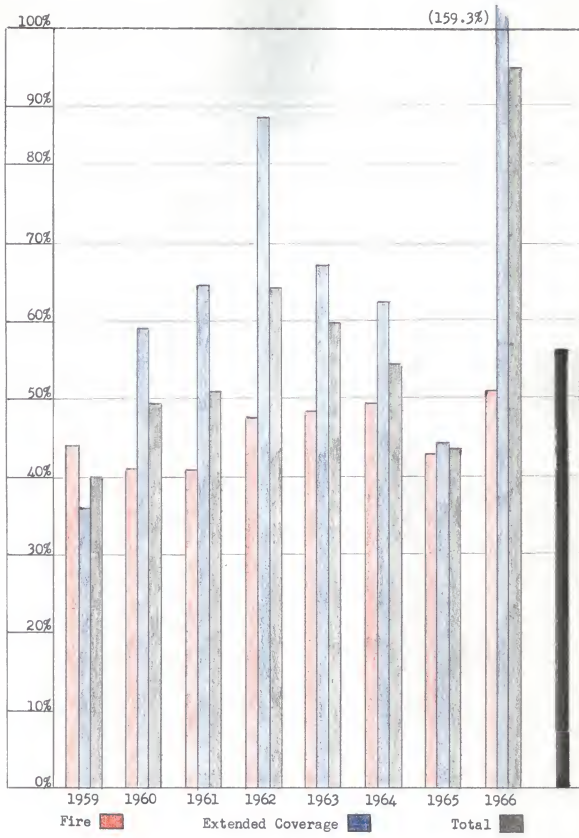


FIGURE 1

LOSS RATIOS FOR FIRE AND EXTENDED COVERAGE INSURANCE
OF ALL COMPANIES WRITING IN KANSAS, 1959-1966

realistic picture of property insurance costs than if one considered only fire insurance--as has been the case in some previous studies. Even by combining the figures for fire and extended coverage, however, the loss ratios shown for these coverages in Kansas are far lower than the nation-wide loss ratios shown for either stock companies (Table II), or for mutual companies (Table V). This would appear to indicate that either fire and extended coverage insurance cost proportionately more than other types of coverage, or that the state of Kansas paid more for insurance protection than some other parts of the United States.

Although loss ratios seem lower for Kansas than for the United States as a whole, it is interesting to note the trend shown in Table VI toward a reduction in the amount of earned premiums. Though figures on the total volume of insurance written for the years corresponding to those in Table VI are not shown, one could safely predict that the total volume increased for that period of time--at the same time as premium earnings decreased. This would indicate reductions in the insurance rates, as was indeed the case, as shown in Table VII.

The data presented in Table VII, supplied by the Kansas Inspection Bureau--the private organization which

TABLE VII

FIRE AND EXTENDED COVERAGE RATE REVISIONS FOR KANSAS, 1958-1968
PUBLIC BUILDINGS, EDUCATIONAL INSTITUTIONS AND CHURCHES

Year	Revision Date	Hazard Coverage	Risk Classification	Revision
1958	No Changes			
1959	No Changes			
1960	January 4	Fire	Frame Construction, with or without Fire Protection-Building and Contents.	15% Reduction
			Brick Construction, with Fire Protection- Building and Contents	20% Reduction
			Brick Construction, without Fire Protection- Building and Contents	15% Reduction
"	July 1*	Fire	All Classifications	25% Reduction
"	"	Extended Coverage	Buildings	40% Reduction
"	"	"	Contents	50% Reduction
1961	No Changes			
1962	December 7	Extended Coverage	Superior Wind-Resistive Construction	27% Increase
"	"	"	Ordinary Construction	23% Increase
1963	December 27**	Fire	All Classifications	15% Reduction
"	"	Extended Coverage	Buildings	30% Reduction
"	"	"	Contents	40% Reduction
			(In addition to above credits, a "package Modification Credit" was granted for all hazards covered.)	15% Reduction

(Continued)

TABLE VI (continued)

Year	Revision Date	Hazard Coverage	Risk Classification	Revision
1964	August 23	Extended Coverage	Superior Wind-Resistive Construction-Buildings	7% Increase
"	"	"	"	14% Increase
"	"	"	Ordinary Construction-Buildings	25% Increase
1965	No Changes	"	"	No Change
1966	No Changes	"	"	"
1967	October 6	Fire	Frame Construction, with or without Fire Protection-Buildings and Contents	15% Reduction
"	"	"	Brick Construction-with Fire Protection	No Change
"	"	"	"	"
"	"	"	"	"
"	"	"	Building and Contents	15% Reduction
1968	No Changes	"	Fire-Resistive Construction, with or without Fire Protection-Building and Contents	15% Reduction
1969	February 21	Extended Coverage	Superior Wind-Resistive Construction	50% Increase
"	"	"	Ordinary Construction	25% Increase

*July 1, 1960, introduction of Public and Institutional Property Plan. (Property insured to at least 90% of value; therefore, rates used for developing basic premiums were 90% co-insurance rates. From those rates, further P. I. P. credits were granted as indicated.)

**December 27, 1963, introduction of Special Institutional Program of the Special Multi-Peril Program. Rates for 90% co-insurance were used as a basis with additional credits granted as indicated.

***Personal Correspondence of Author, letter from M. E. Stubbs, Manager, Kansas Inspection Bureau, April 8, 1968; letter from C. S. Wright, Assistant Manager, May 1, 1969.

establishes advisory rates for member insurance companies in Kansas--shows the rate revisions from 1958 to May, 1969, specifically affecting public schools in Kansas. In that period of time, fire insurance rates were steadily reduced, without subsequent increases--contrary to rates for extended coverage. Notable reductions for both types of coverage occurred in July, 1960, with the introduction of the Public and Institutional Property policy. With the use of the P. I. P. plan, all classifications of fire insurance were reduced 25%, and extended coverage rates were reduced 40% for buildings and 50% for contents. Further sizable rate reductions were made possible in December, 1963, with the introduction of the Institutional Program of the Special Multiple Peril Plan. With this plan, fire insurance rates could be reduced as much as 30%, and extended coverage as much as 45% for buildings and 55% for contents. These improvements in rates for extended coverage were partially negated the following year in 1964, however, with increases of up to 25%. Heavy losses from wind and hail damage, as well as other hazards, resulted in additional increases in extended coverage rates in February, 1969, when rates were increased as much as 50%. As shown, the rates recommended for public school property by the Kansas Inspection Bureau have generally been decreasing

over the past ten years. However, with the last increase in extended coverage rates, much of the rate decrease possible with the P. I. P. plan and the Special Multiple Peril Plan was nullified.

Study of rate changes for fire and extended coverage insurance of public school property in Kansas demands consideration of three additional points. First, one must understand that a basic reason for the fluctuation in extended coverage rates--compared to fire rates--is due to the relatively greater "exposure," or potential damage area characteristic of extended coverage hazards. A fire may threaten only an adjacent building, but a wind or hail storm can damage insured properties throughout a large area of the state. Therefore, one year with numerous storms inflicting damage on properties insured with extended coverage can materially affect the rates recommended by the rating bureau.

As mentioned previously, the rates recommended by the Kansas Inspection Bureau are advisory and can be changed, or "deviated" by a company, after application to and approval by the State Insurance Commissioner. This makes it possible for a company having a better than average loss experience to obtain deviated rates, and therefore to offer substantially lower premiums for the insurance coverage in competitive bidding situ-

ations. Naturally, a company would not normally offer the deviated rates and lower premiums to a client unless it was convinced that, otherwise, the business would be placed elsewhere.

The third consideration regarding rate changes is, again, the importance of having a school official responsible for the insurance program of the school district. This official must then be aware of factors such as rate revisions which might affect insurance costs.

The data presented in Tables VIII, IX, and X was collected from records of school districts representing a random selection of four districts in cities of the First Class--a 28.5% sample; and nine districts in cities of the Second Class with populations over 2,500--a 14.5% sample.

These school districts had an attendance total of 46,933 students, in school properties insured for a total of \$70,928,766, shown in Table VIII. To gain an understanding of the magnitude of public school property insurance in Kansas, an index of the amount of insured property per student was derived. For the thirteen school districts represented, this figure ranged from \$976.00 to \$2,484.50, with an average of \$1,511 of insured property per student. Multiplying this figure by the total public school student population of

TABLE VIII

STUDENT ENROLLMENT AND INSURED PROPERTY
OF THIRTEEN KANSAS UNIFIED
PUBLIC SCHOOL DISTRICTS

Districts in Sample	Student Enrollment 1967-1968	Insured Property 1967-1968	Insured Property Per Student*
District A	8,350	\$ 9,043,865	\$ 1,203.45
District B	5,569	10,195,762	1,830.80
District C	7,961	11,670,000	1,628.80
District D	5,323	13,224,900	2,484.50
District E	1,213	1,907,905	1,572.90
District F	842	1,235,000	1,466.75
District G	2,687	4,160,691	1,548.45
District H	1,874	2,315,000	1,235.30
District I	1,515	1,592,000	1,127.85
District J	1,278	1,112,629	976.00
District K	4,226	5,542,818	1,311.60
District L	1,334	1,343,196	1,118.80
District M	4,761	7,585,000	1,770.00
TOTALS	46,933	\$70,928,766	\$ 1,511*

Total Student Population

In Kansas, 1967-1968... 520,193 X \$1,511 = \$786,011,623 Estimated Total
Insured Kansas Public School Property.

* Total insured property divided by total student enrollment.

520,193 (1967-1968) yielded an estimated total amount of insurance on Kansas public school property of \$786,011,623.

The search for reliable figures on the premiums paid for property insurance and payments received for loss claims emphasized the previously discussed lack of insurance record-keeping. In some cases, the school district apparently kept no record of the insurance program, giving up that responsibility to an agent-of-record. The agent-of-record often only had specific information for the policies which he wrote, with the remaining records scattered among the various other agents who wrote a portion of the business. Districts which did keep records, commonly listed only the agent's name, company, property covered, and amount of coverage--without figures for the premiums paid for that coverage, or loss payments returned to the district. Reporting all expenditures for insurance as a single item was also done, and in at least one case, the manner in which information was reported changed several times in the ten-year period of investigation. Sometime, "insurance" was reported as a single item, then later was itemized as: property insurance, liability insurance; and, workman's compensation.

Even where records were kept of expenditures for premiums, records of payments received for losses were often

TABLE IX

PREMIUM-LOSS RATIOS FOR THIRTEEN
KANSAS UNIFIED PUBLIC
SCHOOL DISTRICTS

Districts in Sample	Premiums Paid 1957-1967	Loss Claims 1957-1967	Loss Ratio (%)
District A	\$ 62,795	\$174,952	278.6 %
District B	96,735	4,735	4.9
District C	100,673	8,255	8.2
District D	95,253	136,396	143.2
District E	18,313	280,000	1528.0
District F	- no records available - - - - -		
District G	- no record -	50,267	- - -
District H	21,904	4,908	22.4
District I	26,560	none	0.0
District J	15,430	348	2.0
District K	43,696	41,000	83.8
District L	15,240	none	0.0
District M	94,793	52,288	55.0
TOTALS	\$591,392	\$735,149* (\$702,882)	118.8 %

*The total shown includes the loss claim of District G on one fire loss in June, 1967. For purposes of computing the loss ratio for the total, the loss claim of District G was excluded, as no records were available for the premiums paid in that district.

poorly kept or non-existent. Occasionally, the check in payment for a claim was signed over directly to a contractor, without the claim payment appearing on the financial records of the school district. Records depending on the memory of the official responsible for record-keeping were not unusual--resulting in statements such as, "I've been here for x number of years, and I don't remember any claims."

Table IX presents the best figures available for premiums paid and loss claims returned from 1957 to 1967 of the thirteen districts studied. One district had no records available for either item; another district had record of a recent loss claim, but no records of premiums paid. Totals for the two items, excluding the two districts mentioned, were \$591,392 in premiums paid and \$702,882 in loss claims. These figures show a difference of \$111,490 in favor of the school districts sampled, and a loss ratio of 118.6% for the total.

To understand the significance of these figures, one must look further than the totals shown, however. On the surface, it would appear that losses for public schools have been excessive, or that sufficient premiums have not been paid. Studying the figures for individual districts, however, one can see that losses for only three of the districts in the sample accounted for the unbalanced totals. The large

loss figure shown for District A includes two unusually large losses--\$138,000 from one hailstorm, and \$35,752 from one fire. District E recorded only one loss in 46 years, but that one was a major fire with a \$280,000 loss.

This discussion illustrates the primary difficulty in an investigation of public school property insurance--the need for nearly a 100% sample of the districts in the State to avoid the bias resulting from catastrophe losses, but with a situation where the collection of the necessary information is very difficult from even a partial sample, because of insufficient or inconsistent records.

Table X presents information regarding practices used to establish the property valuation for insurance purposes; and, those practices used to distribute the insurance business, or award the insurance contracts. The contents of buildings to be insured were commonly appraised by school employees. The buildings themselves were most commonly appraised by insurance company engineers, or in some cases by agreement between the insurance company engineer and a school official. One district used local contractors to appraise school properties. None of the administrators of the districts studied used private appraisal firms. The opinion was that the quality of the appraisal of a private firm would not be enough better

TABLE X

PRACTICES OF APPRAISING PROPERTY AND
AWARDING INSURANCE CONTRACTS
OF THIRTEEN KANSAS UNIFIED
PUBLIC SCHOOL DISTRICTS

Number of Districts	Practice
PRACTICE USED TO APPRAISE PROPERTY:	
12	Building appraisal made by an insurance company engineer, or both an insurance company engineer and the school official; contents appraised by school employees.
1	Building appraisal made by local contractors; contents appraised by school employees.
PRACTICE USED IN AWARDING INSURANCE CONTRACTS:	
4	An "Agent-of-Record" designated by school district is responsible for administering the program and distributing the business to agents in the community.
4	The insurance program is administered by a school official, who distributes the business to local agents on an informal basis using various objective and non-objective criteria.
3	Responsibility for administering the program and distributing the business is handled by a local insurance association.
1	Responsibility for administering the program and distributing the business is handled by a "school insurance committee," composed of the school business manager and representatives of a local insurance association.
1	Insurance contracts are awarded by competitive bidding against a set of specifications advertised by the school district.

than that of an insurance company engineer to justify the cost.

Practices used to determine how the insurance program would be administered, the business distributed, and the policy contracts awarded varied considerably. Ordinarily, the larger districts had better defined policies regarding the procedures to be used than did the smaller districts. Undoubtedly, the smaller number of agents desiring part of the business in the smaller districts made it possible for them to be more flexible in distributing the insurance than larger districts. At the same time, politics seemed to play a larger part in decision-making in the smaller districts, with an influential agent exerting more power, either within a local insurance association, or in relations with the school administration than might be possible in a more heavily populated district.

Four districts designated an "Agent-of-Record", either on the basis of size of agency, or service to the school district. This Agent-of-Record was responsible for distributing the insurance business to other agents in the community. The distribution of business was made on the basis of the amount of taxes paid by the particular agent, or the volume of business written in the community, or sometimes on an equal basis

to all full-time agents. In some cases, the agent-of-record wrote all the policies, and distributed his commission; in others, the volume of business was distributed, with each agent writing a policy covering a particular property. The latter practice resulted in a multitude of policies, agents, and companies--making it quite difficult to be certain that the policies were concurrent, or that all properties were adequately covered.

Four other districts administered the insurance program and distributed the business themselves, using various criteria. Most arrangements seem to have been made on a very informal basis, depending on the school administrator's opinion of the following: the agent's volume of total business in the community; the agent's reputation for service; whether or not he was a full-time insurance agent; and the reputation of the company represented. In one case, the administrator had encouraged local insurance agents to form an association, which would then be responsible for distributing the business among themselves. The response to his suggestion was that the agents were unable to reach any agreement among themselves, and that the school district should continue distributing the business as it had been doing.

In three districts, local insurance agents were successfully organized into an association which functioned as

an advisor to the school district in insurance matters, and was responsible for distributing the business. Membership in the association was sometimes only open to representatives of stock companies; whereas in others, the only requirement for membership was that the agent maintain a separate office, and consider insurance his primary occupation.

One district administered the program through an "insurance committee," consisting of the district's business manager and representatives of the local insurance association. The committee had been chaired by one of the insurance agents, who had died shortly before the time of this investigation. Consequently, the insurance program was somewhat disorganized, as many of the records had been kept by the deceased agent.

One of the thirteen districts used competitive bidding as the method for awarding the insurance contracts. However, its use was also being considered by a second district, which at the time of the study was dealing with 13 different agencies, representing 23 different companies.

The business manager of the district using competitive bidding was responsible for developing the specifications for the coverage desired, advertising the competition, and awarding the contracts to the lowest responsible bidder. The insurance

for the district had previously been handled by a local insurance association of stock company representatives, and this association appraised the property for the bid document used by the district in the bid competition.

Though comparative figures were not available, it was the judgment of the business manager that considerable money had been saved by competitive bidding, as well as effecting better records on the insurance program of the district. The successful agency agreed that their bid was "considerably less" than it would have been without competition. When asked if the lower profit would require giving less service to the school district, the agency representative answered that the service given would be the same, regardless of profit.

CHAPTER IV

SUMMARY AND CONCLUSIONS

It is important for school boards and administrators to make the most efficient use possible of the limited financial resources available for expansion and improvement of public education. This must be done by the economical purchase of those items considered most important to the educational effort.

Public schools in Kansas have a property investment of buildings and contents valued in excess of \$785 million. The potential loss of these properties represents an ever-present danger to school districts, and could severely hamper the total educational program. Protection against financial loss to the school district from damage by natural hazards is provided by insurance of the properties.

Insurance is a plan whereby an "average certain loss," or premium, is substituted for an "uncertain loss." The earliest form of insurance was marine insurance, and may have been used as early as the Trojan War by the Greeks. English merchants may have used marine insurance as early as the

thirteenth century, but evidence of regulations and methods of business dates only from the seventeenth century.

As early as 1688, seafaring men and merchants gathered at Lloyd's Coffee House, where those wanting to be insurers of ships and cargoes would sign the bottom of a paper describing the risk--from whence came the term, "underwriter," and the establishment of "Lloyd's of London."

The Philadelphia Contributionship, a mutual company founded in 1752, was the first permanent fire insurance company in America. The oldest stock company, the Insurance Company of North America, began in 1792.

From this early beginning in the United States, the insurance business has grown to become one of the biggest industries. There is considerable evidence that excessive premiums, especially on public school properties, have contributed to that success. Many of the studies presenting such evidence were made several years ago, however, and covered property insurance in states other than Kansas. Because of the lack of information on premium-loss ratios for property insurance of public school districts in Kansas, it has not been possible to determine whether or not costs for such insurance have been equitable and reasonable. The need for such information prompted this investigation, in which the following methods of research were used.

To gain an orientation in the field of the problem and an understanding of the opinions and points of view of authorities, an extensive review of literature was conducted, as well as interviews and personal correspondence with authorities.

Following the introductory study of the general subject, an investigation was conducted specifically of practices and costs of property insurance for Kansas unified public school districts. Authorities in educational research and statistical analysis were consulted, and it was decided that the validity of a statistical analysis of data would be questionable, due to the presumed lack of desired records or difficulty of obtaining them. Therefore, the plan of study was to select a random sample of Kansas unified public school districts and personally visit each one, interviewing the administrator, and if desirable, the insurance agent of record. During the interview, the information desired was to be collected and verified, with as complete an analysis of data as practical and valid.

Thirteen unified public school districts were randomly selected--four which included cities of the First Class, and nine which included cities of the Second Class with a population over 2,500. An itinerary was scheduled with administrators of these

districts, and visits were made to each. In some cases, follow-up visits or correspondence was necessary to obtain additional information.

To determine whether costs were equitable and reasonable for public school property insurance, information on competition and regulation affecting commercial insurance companies was reviewed and compared to findings of the study. Also, regulations and practices affecting public school property insurance were considered, to determine if school districts were using approved practices to effect the lowest costs possible for the necessary insurance coverage.

Commercial insurance companies are regulated and supervised by the Kansas State Department of Insurance. Advisory rates of various classes of risks are established by the Kansas Inspection Bureau, a private agency supported by member or subscriber insurance companies. The Department of Insurance must approve the rates suggested by the Kansas Inspection Bureau before they are used. It also reviews and approves or rejects applications from the companies for rate deviations. If a company has a better than average premium-loss experience, it can receive approval for "deviated rates" which will permit that company to compete for insurance business by lowering its price

The insurance industry argues that--contrary to past evidence--rates are too low and that premium income is not covering losses. Commercial insurance authorities write that, because of current underwriting losses, the industry faces financial difficulties in competing for capital investment with other segments of the economy with larger profits. There is considerable evidence, however, showing that income from investment of reserves effectively balances any underwriting losses.

Furthermore, some authorities maintain that investment income of commercial insurance companies should be considered in the establishment of rates. There are numerous arguments both for and against that proposal, with evidence presented to support both sides of the debate. In any case, it seems clear that companies can afford to compete with each other by lowering the effective price of the insurance protection.

Public school districts can lower costs by taking advantage of the competition for insurance business, and by awarding the contracts for insurance on the basis of competitive bids. Numerous manuals and textbooks offer guidelines for the specification documents necessary to advertise the competition and to receive the coverage necessary. Also, recent legislative action establishes the authority for competitive bidding on school insurance.

Public schools are affected in additional ways by legal requirements concerning property insurance. Previous to March, 1968, public schools did not have specific legal authority to purchase property insurance, and did so only with an "implied authority." Statutes requiring the audit of financial records and the reporting of expenditures not specifically authorized, required a report to County Attorneys with each audit of school records. Amendments to the Kansas Statutes now specifically permit purchase by public schools of property insurance. Other Statutes regulate school construction with regard to fire protection.

In analyzing the findings of the investigation of insurance costs and practices for Kansas public school districts, three points were clear. First of all, the premium-loss ratios for insurance companies underwriting in Kansas have been going up in recent years--to the point where annual combined expense and loss ratios have sometimes exceeded 100%, with resulting underwriting losses. These losses have generally been covered by investment income, however.

Second, rates for property insurance against fire as established by the Kansas Inspection Bureau and approved by the Kansas Department of Insurance have consistently been going down--while rates for extended coverage have fluctuated considerably, with two special policy forms lowering rates and

subsequent wind and hail losses raising them again. Generally, rates on property insurance for public schools have decreased in the past ten years.

The third, and perhaps most important point concerns the information collected from school districts themselves. Because of cases with inconsistencies in forms of record-keeping or where the data in the records could not be compared, it is questionable whether more than a general conclusion can be supported by the information collected. On the basis of the total loss ratio (118.8%), it would appear that public schools are paying far too little for the protection they are receiving. However, because of the size of sample, it was easily affected by the three districts with especially large losses. Yet, it would have been difficult to have used a larger sample in a study such as this.

On the basis of the total information presented, it seems clear that insurance costs for Kansas unified public school districts need not be unreasonable. School districts should retain responsibility for the supervision of the insurance program and for the record-keeping necessary. Records should be kept on the insurance coverage and the costs of that coverage. A standardized form with specific data to be recorded should be published and recommended by the Kansas State Department of Education. Those records should be used by the

individual districts to negotiate for the lowest rates available for the property insurance needed, or in establishing formal competitive bid procedures. On the statewide level, a standard group of data would be useful as evidence for lowering rates, if the records indicate they are too high.

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APPENDICES

APPENDIX A

THE COST OF
FIRE AND EXTENDED COVERAGE INSURANCE
FOR UNIFIED SCHOOL DISTRICTS

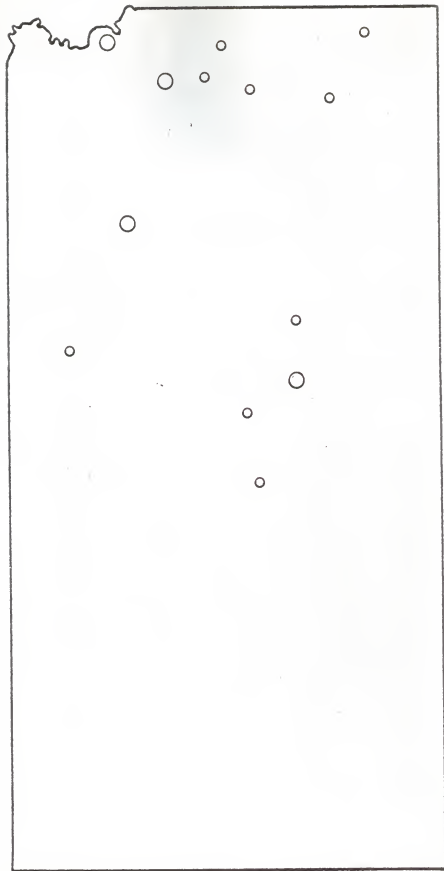
1. What is the total student population of your District? _____
2. What is the assessed valuation of the District? _____
3. Are your buildings and contents insured against fire and extended coverage on the basis of "insurable value (replacement cost less depreciation)", or "replacement value"? What is the current:
Replacement value \$ _____, or Insurable value \$ _____?
4. Are your property insurance policies written with a co-insurance clause? _____
If so, what percentage co-insurance? _____
5. What premiums have been paid for fire and extended coverage insurance between July 1, 1957 and June 30, 1967?

1957-58 \$ _____	1961-62 \$ _____	1965-66 \$ _____
1958-59 _____	1962-63 _____	1966-67 _____
1959-60 _____	1963-64 _____	
1960-61 _____	1964-65 _____	TOTAL \$ _____
6. What amounts have been received in claims for fire and extended coverage damage and loss between July 1, 1957 and June 30, 1967?

1957-58 \$ _____	1961-62 \$ _____	1965-66 \$ _____
1958-59 _____	1962-63 _____	1966-67 _____
1959-60 _____	1963-64 _____	
1960-61 _____	1964-65 _____	TOTAL \$ _____
7. Have the amounts collected in claims been equal to the amount of loss? _____
8. How is the insurance distributed? Competitive bidding? Through a local insurance association? Objective basis?
9. How are insurable values determined for the property in the District?
 _____ a commercial appraisal company?
 _____ insurance company engineers or special agents?
 _____ an employee of the district?
 _____ a local contractor?

APPENDIX B

GEOGRAPHICAL LOCATIONS OF KANSAS SCHOOL DISTRICTS IN STUDY



- Unified School Districts in Cities of the Second Class with population over 2500.
- Unified School Districts in Cities of the First Class.

APPENDIX C

SELECTED KANSAS STATUTES COVERING FIRE PREVENTION
AND PROPERTY INSURANCE REGULATIONS
FOR PUBLIC SCHOOLS

Kansas Statutes Annotated

K. S. A. 12-2601. "Municipality" and "governing body" defined. As used in this act: (a) "Municipality" shall mean county, city, township, municipal university, drainage district and any other political subdivision or taxing district of the state; (b) "governing body" shall mean the board, body, or persons in which the powers of a municipality as a body corporate, or otherwise, are vested. [L. 1955, ch. 248, Sec. 1; June 30.]

K. S. A. 12-2602. Types of insurance permitted; payment. The governing body of any municipality may purchase motor vehicle liability insurance, including medical payments insurance, for the protection and benefit of the municipality and those officers, agents and employees of the municipality responsible for the operation of vehicles owned, operated, maintained or controlled by the municipality, and of persons while riding in or upon, entering or alighting from such vehicles, and may pay for such insurance out of the general fund or other appropriate fund of the municipality for any or all motor vehicles owned, operated, maintained or controlled by such municipality. [L. 1955, ch. 248, Sec. 2; L. 1961, ch. 75, Sec. 1; June 30.]

NOTE: The above statutes are stated as written prior to the amendments enacted in Kansas Senate Bill No. 327 (Appendix D). Following are statutes as revised and amended by SB 327, and other statutes relevant to this study.

K. S. A. 12-2601. "Municipality" and "governing body" defined. (a) "Municipality" shall mean county, city, township, municipal university, drainage district and any other political subdivision or taxing district of the state except that it shall not mean or include school districts; (b) "governing body" shall mean the board, body, or persons in which the powers of a municipality as a body corporate, or otherwise, are vested. [L. 1955, ch. 248, sec. 1; June 30; L. 1968, ch. 204, sec. 1; July 1.]

K. S. A. 72-8402. Fire and extended coverage insurance; payment. The board of education or other governing body of any school district may purchase fire and extended coverage insurance upon property of the school district or under its supervision and control and pay for the same out of the general fund or other appropriate fund of the school district. [L. 1968, ch. 204, sec. 3; July 1.]

K. S. A. 72-8403. Terms of policies. The term of any policy of insurance purchased under the provisions of this act shall not exceed three (3) years. [L. 1968, ch. 204, sec. 4; July 1.]

K. S. A. 72-4604. School building construction to be accessible and usable by physically handicapped; approval of plans. The construction of all school buildings shall comply with the requirements of the 1967 edition of the uniform building code of the international conference of building officials, and all electric wiring shall conform to requirements of the 1965 issue of the national electric code of the national fire protection association. Minimum plumbing requirements shall meet the 1955 edition of the national plumbing code of the American society of mechanical engineers. The construction of school buildings shall include reasonable provision for making buildings and facilities accessible to, and usable by, the physically handicapped, as approved by the state architect. No contract shall be let for the erection of any school building, and it shall be illegal to pay out any public funds for the erection of a school building until the plans for such building shall have been submitted to the state architect and approved as to all the requirements of this act. [L. 1909, ch. 209, sec. 4; R. S. 1923, 72-4604; L. 1927, ch. 220, sec. 11; L. 1951, ch. 406, sec. 4; L. 1957, ch. 393, sec. 1; July 1; L. 1968, ch. 235, sec. 1; July 1.]

K. S. A. 75-1122. Annual audit of accounts of counties, school districts and cities of first and second class. Beginning July 1, 1967, it shall be the duty of the governing body of each county, school district and cities of the first and second class to have the accounts of such municipality (including, in case of school districts, tax and other funds including activity funds and accounts) examined and audited by a licensed municipal public accountant or accountants, or certified public accountant or accountants: Provided, That the above designated governing bodies of such municipalities shall at least once each year from the date of the first audit, provided for above, have the accounts of their respective municipalities examined and audited by a licensed municipal public accountant or accountants or certified public accountant or accountants. [L. 1967, ch. 442, sec. 1; July 1.]

I-11 Insurance Audit Procedures.

- (a) Examine insurance policies for coverage, endorsements and co-insurance clauses.
- (b) Determine that insurance policies are written in accordance with legal requirements.
- (c) Determine that insurance coverage provided is authorized by statute or ordinance.
- (d) Determine that unearned premiums on cancellations are properly accounted for.

K. S. A. 75-1126. Procedure when audit discloses law violation or grounds for ouster. When any audit under this act indicates violation of a penal statute or discloses reasonable ground for removal from office, it shall be the duty of the licensed municipal public accountant or accountants or certified public accountant or certified public accountants signing the report of such audit to file one copy of the report with the county attorney. [L. 1935, ch. 275, sec. 16; May 15.]

SENATE BILL No. 327

AN ACT concerning public schools; authorizing the purchase of insurance in certain cases; amending K. S. A. 12-2601 and repealing the existing section.

Be it enacted by the Legislature of the State of Kansas:

Section 1. K. S. A. 12-2601 is hereby amended to read as follows: 12-2601. As used in this act:

(a) "Municipality" shall mean county, city, township, municipal university, drainage district and any other political subdivision or taxing district of the state except that it shall not mean or include school districts;

(b) "governing body" shall mean the board, body, or persons in which the powers of a municipality as a body corporate, or otherwise, are vested.

Sec. 2. The board of education or other governing body of any school district owning or operating boilers may purchase boiler insurance which insurance shall include inspection of boilers, and pay for the same out of the general fund or other appropriate fund of the school district.

Sec. 3. The board of education or other governing body of any school district may purchase fire and extended coverage insurance upon property of the school district or under its supervision and control and pay for the same out of the general fund or other appropriate fund of the school district.

Sec. 4. The term of any policy of insurance purchased under the provisions of this act shall not exceed three (3) years.

Sec. 5. K. S. A. 12-2601 is hereby repealed.

Sec. 6. This act shall take effect and be in force from and after its publication in the statute book.

I hereby certify that the above BILL originated in the SENATE, and passed that body

SENATE concurred in
HOUSE amendments _____

President of the Senate.

Secretary of the Senate.

Passed the HOUSE
as amended _____

Speaker of the House.

Chief Clerk of the House.

APPROVED _____



Governor.

AN INVESTIGATION OF COSTS AND PRACTICES OF
PROPERTY INSURANCE OF KANSAS UNIFIED
PUBLIC SCHOOL DISTRICTS

by

DUANE RALPH DEYOE

B. S., Kansas State University, 1964

AN ABSTRACT OF A MASTER'S THESIS

submitted in partial fulfillment of the
requirements for the degree

MASTER OF SCIENCE

College of Education

KANSAS STATE UNIVERSITY
Manhattan, Kansas

1969

The purpose of this investigation was to determine whether or not costs for property insurance of Kansas public schools have been equitable and reasonable.

The method of research included a review of related literature, interviews and correspondence with authorities in the field, and an investigation of property insurance costs and practices of a random sample of thirteen unified public school districts in Kansas. The review of related literature and interviews with authorities included information on: the history of insurance, forces affecting insurance companies--regulation, competition, profit-loss experience, and property insurance rate changes on public school property; and, regulation of Kansas public school districts in the purchase of property insurance.

Research of property insurance costs and practices of Kansas public school districts was structured to yield the best possible data, in view of these considerations. 1) Data collected should include premium-loss experience for ten years of individual school districts, and current practices of appraising property and awarding insurance contracts which affect the cost of the insurance. 2) Data should come from as large a sample of school districts as possible, while maintaining accuracy and completeness of data reported. The nature of the data desired, and the record-keeping of that by many public schools suggested that a survey by mail would not be feasible, and that accurate and complete information

could only be collected by personal interview. Therefore, a random sample was selected of thirteen unified public school districts in cities of the First Class, and cities of the Second Class with population over 2,500. The sampled population was limited to larger unified public school districts--more likely to have complete records of data desired. The size of the sample was considered large enough to avoid biased data, yet small enough to make visits and interviews possible.

Analysis of the findings of the investigation revealed three considerations in determining whether or not property insurance costs for Kansas public school districts have been equitable and reasonable. First, premium-loss ratios for insurance companies underwriting in Kansas have been increasing in the past few years, approaching and occasionally exceeding 100%. Underwriting losses resulting when the loss ratio exceeds 100% generally have been covered by investment income, however.

Second, rates for property insurance against fire, as established by the Kansas Inspection Bureau and approved by the Kansas Department of Insurance have been going down consistently--while rates for extended coverage have fluctuated, with introduction of two special policy forms lowering rates and subsequent major wind and hail losses raising them again. Generally, insurance rates covering Kansas public schools have decreased in the past ten years.

Third, even with the precautions taken in selecting an adequately large sample of school districts likely to have complete and accurate records, the data desired was often not available, and unusually large losses in three of the districts studied caused an extremely high total loss ratio of 118.8% for the ten year period of 1957-1967. It seems likely that this figure is higher than that actually the case if it were possible to collect the necessary information from all public schools in Kansas.

On the basis of the total information presented, it seems clear that property insurance costs for Kansas unified public school districts are generally reasonable and equitable. However, it is also clear that individual school districts can do much to lower their insurance costs by employing more business-like practices in handling their insurance program. Recommended practices include: close supervision of the insurance program by school officials; more complete record-keeping by the school district; statewide collection of premium-loss data to serve as evidence in negotiating better rates for public schools and protecting related interests; and the use of negotiation or competitive bidding to place the insurance business--taking advantage of the competitive structure of the insurance industry.