

*\$100*

*Albert Washington*

AnnuitY Agreements  
of  
Charitable Organizations

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ANNUITY RATES AND INTEREST RATES

STIMULATING ANNUITY GIFTS

ACTUARIAL PROBLEMS

FAIRER ANNUITY TAXATION

•

EIGHTH CONFERENCE

WISE PUBLIC GIVING SERIES NO. 47

1946



Annuity Rates and Interest Rates  
Stimulating Annuity Gifts  
Actuarial Problems  
Fairer Annuity Taxation

PAPERS PRESENTED AT THE EIGHTH CONFERENCE ON ANNUITIES, HELD IN NEW YORK CITY, APRIL 10, 1946, UNDER THE DIRECTION OF THE COMMITTEE ON ANNUITIES



~~FEDERAL COUNCIL OF THE CHURCHES  
OF CHRIST IN AMERICA~~

~~297 Fourth Avenue :: New York 10, N.Y.~~

WISE PUBLIC GIVING SERIES NO. 47

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# REPORTS OF THE CONFERENCES ON ANNUITIES

held under the direction of the Committee on Annuities of the  
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FIRST CONFERENCE (*Wise Public Giving Series No. 18*).....April 29, 1927

- Actuarial Basis of Rates                      Legislation and Taxation
- Administrative Policy                      Finding Prospective Donors
- Securing the Gifts

SECOND CONFERENCE (*Wise Public Giving Series No. 31*).....November 9, 1928

- Legislation and Taxation
- Annuity Rates and Reserves
- Printing and Advertising
- Accounting Methods
- Investments

THIRD CONFERENCE (*Wise Public Giving Series No. 34*).....November 17, 1930

- Annuity Agreements: Cautions and Restrictions
- Uniformity of Rates, Agreements, and Terminology
- Reinsurance of Annuities
- Annuity Agreement Business: Extent and Characteristics
- Taxation and Legislation: Recent Developments
- Administration and Investment of Annuity Funds

FOURTH CONFERENCE (*Wise Public Giving Series No. 38*).....March 17, 1931

- The Trend toward Uniformity
- Legal Reserves
- Uniform Rates
- The Up-to-date Legal Situation

FIFTH CONFERENCE (*Wise Public Giving Series No. 43*).....November 20, 1934

- Investment of Funds for the Safeguarding of Annuities
- Uniform Annuity Rates
- The Mortality among Annuitant Lives
- Federal Taxation of Annuities: Law of 1934

SIXTH CONFERENCE (*Wise Public Giving Series No. 44*).....October 4-5, 1939

- How to Obtain Annuity Gifts
- Outlook for Interest Rates
- The Regulation and Supervision of the Securing Annuity Gifts
- Issuance of Annuity Agreements by a Charitable Society
- What Colleges and Universities Are Doing
- Investment Planning under Revised Insurance Law of the State of New York
- Rates for Annuity Agreements
- Taxation and Legislation Affecting Annuities

SEVENTH CONFERENCE (*Wise Public Giving Series No. 45*).....April 29, 1941

- Developments in the Regulation and Supervision of the Issuance of Annuity Agreements by Charitable Societies, and the Application of the 1941 Amendments to the New York Insurance Code
- Rates of Yield on Invested Funds under Existing Conditions, and the Probabilities as to the Future
- Rate of Mortality among the Gift-annuitant Lives
- Rates for Gift-annuity Agreements

STANDARD ANNUITY TABLE FOR COMPUTING ANNUITIES

(*Wise Public Giving Series No. 46*).....Dec. 1943

EIGHTH CONFERENCE (*Wise Public Giving Series No. 47*).....April 10, 1946

- Annuity Rates and Interest Rates
- Actuarial Problems
- Stimulating Annuity Gifts
- Fairer Annuity Taxation

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## FOREWORD

The Eighth Conference on Annuities was held on April 10, 1946 at 156 Fifth Avenue, New York City, to consider annuity rates, mortality experience, probable residua and problems of taxation.

No change has been made in the uniform annuity rates recommended by the Committee on Annuities at the Sixth Conference on Annuities on October 4-5, 1939 and adopted at the Seventh Conference on Annuities held April 29, 1941. These annuity rates were based upon the Combined Annuity Table ages set back 2 years with interest at  $3\frac{1}{2}\%$ , female lives, 70% residuum, with rates modified at ages under 55 and above 79. These rates comply with the New York State Insurance Law requiring that the annuity rates of bona fide charitable, religious, missionary, educational or philanthropic corporations or associations shall be calculated to "return to such corporation or association upon the death of the annuitant a residue at least equal to one-half the original gift or other consideration for such annuity."

Since 1941, however, most Life Insurance Companies in the United States have adopted the Standard Annuity Table with interest at  $2\frac{1}{2}\%$  at first and then at 2%. Because of adverse mortality experience, a setback of one or more years in the Standard Annuity Table has been adopted by many Life Insurance Companies during the past few years. The Treasury Department itself since 1942 requires all new annuities issued by religious, educational and charitable corporations or associations to be valued by the Standard Annuity Table ages set back 1 year, with interest at  $2\frac{1}{2}\%$ , loaded  $6\frac{1}{2}\%$ . The Insurance Department of New York State has suggested to several religious and charitable corporations licensed in New York State that they should adopt a more conservative rate of interest than  $3\frac{1}{2}\%$  in computing and segregating the legal reserves required under New York State Law. Some have already followed this suggestion, knowing that, once adopted, the more conservative standard must thereafter apply to all new annuity contracts that are issued.

No one can predict when New York State and other states may adopt more conservative valuation tables for annuity reserves based upon present interest rates and present mortality experience. As indicated above, the Standard Annuity Table at  $2\frac{1}{2}\%$  or lower is already voluntarily accepted by most of the commercial Insurance

Companies licensed in N. Y. State. Interest rates have declined substantially since 1941, when the present uniform rates were adopted. This is true of interest on real estate mortgages, as well as on bonds, and preferred and common stocks

A questionnaire sent out September 28, 1945, with the approval of the Committee on Annuities in response to inquiries received about lower annuity rates, showed as follows:—Of the replies received, 18 favored lower annuity rates; 7 were against lower annuity rates; and 7 were undecided but were willing to do what others decided was best.

The Committee on Annuities therefore had a new series of uniform annuity rates prepared by Mr. George A. Huggins and he was requested to present these proposed rates for the consideration of the Eighth Conference on Annuities on April 10, 1946.

Because the Committee was not unanimous in its judgment about lower annuity rates and residua, the rates given were not recommended but were proposed for consideration and discussion by the Eighth Conference on Annuities.

GILBERT DARLINGTON,  
*Chairman, Committee on Annuities*

# INTEREST RATES AND POSSIBLE FUTURE TRENDS

B. H. BECKHART

*Professor of Banking, Columbia University*

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To appraise the permanence or lack of permanence of the current level and pattern of interest rates, one must review the factors which resulted in present interest rate levels. Only if these factors are reviewed is one in a position to determine whether the current level and pattern of interest rates will persist or whether they may be succeeded by a different level and pattern.

At the outset one must distinguish between the level and pattern of rates. The level of rates is usually measured by the yield on long-term obligations. The yields prevailing on railroad bonds are often used for this purpose, because such bonds have been a feature of the American money market for over 100 years. Since the Civil War, yields on American railroad bonds have exhibited three major movements. The first was a decline in yields from 1868 to 1898, the second an increase, from 1898 to 1920, and the third, a decline from 1920 to 1946.

Since 1931 the decline in the level of rates has been accompanied by a change in the structure or pattern of rates. The structure of rates has to do with the relationship of short- to long-term rates. Naturally there are three possibilities. Either the short-term rate is below, equal to or above the long-term rate. Over the past fifteen years, the short-term rate has been below the long-term rate and the interest curve in consequence has been an ascending curve.

Prior to 1931 an ascending interest curve was rarely encountered. Thus in only 2 of the 31 years from 1900 to 1931 was the short-rate below the long-rate. In 10 years it was equal to the long-rate and in 19 it was above the long-rate.

At the present time the level and structure of interest rates are measured by the yield on Government obligations of different maturities. Present interest rates are abnormal in two respects. The level of rates is unprecedentedly low and the structure of rates is of the ascending type.

The decline in the average yield on long-term bonds and the greater decline in short as compared to long-rates since 1931 are the result of commercial bank purchases of the debt. Thus from the accompanying table it will be noted that commercial banks in the period from June, 1933 to December, 1941 increased their holdings of the interest-bearing debt by 14,313 million dollars, which was the largest increase occurring in any one of the different categories. In these 8½ years the rise in commercial bank holdings of the public debt came to 34.4 per cent of the increase taking place in the total interest-bearing debt.

Table 1  
Ownership of U.S. Government Securities—Direct and Fully Guaranteed  
(in millions of dollars)

End of Month	Total Interest-Bearing Debt	Ownership Distribution of the Public Debt					
		U.S. Gov't Agencies and Trust Funds	Federal Reserve Banks	Commercial Banks	Insurance Companies	Mutual Savings Banks	Other Investors
1933—June	\$22,138	\$ 689	\$1,998	\$ 7,477	\$1,000	\$ 720	\$10,300
1941—Dec	63,768	9,529	2,254	21,790	8,000	3,700	18,500

Had commercial banks not purchased Government obligations in the period covered by this table, yields would not have reflected as great a decline. Commercial banks were the most important demand factor in the market and, owing to the magnitude of their purchases, yields fell despite a sharp increase in the debt.

In their purchases of the public debt, commercial banks, on the whole, preferred the shorter obligations. This is indicated by the fact that the average maturity of the debt held by commercial banks has been less than the average maturity of the total debt. It was this preference on the part of commercial banks that caused the yield on shorter issues to decline more rapidly from 1933 to 1941 than the yield on the longer issues—in other words, that caused the emergence of the present yield curve.

It seems fairly obvious from available evidence that the decline in the yields on Government obligations which took place from 1933 to 1941 was not the result of an increase in savings but rather of an increase in credit expansion. If savings had risen *pari passu* with the

increase in the public debt, commercial bank credit would not have had to expand to absorb that amount of the debt not taken by other investors.

Shortly after Pearl Harbor the decision was made to continue with minor modifications the yield curve on Government obligations existing at that time. Inasmuch as this curve had resulted from huge credit expansion, it was recognized by students of the subject that its maintenance during a war would require credit expansion at an accelerated rate.

By the Fall of 1942 the yield curve on Government obligations assumed the form which lasted until the end of 1944— $\frac{3}{8}$  of 1% on Treasury bills,  $\frac{7}{8}$  of 1% on certificates of indebtedness, 2% on 10 year bonds and  $2\frac{1}{2}$ % on 26 year obligations.

The implication of such a curve is that interest rates will rise. In other words, its maintenance depends upon uncertainty relative to the future of long rates. If the belief becomes general that long rates will not rise, the curve will begin to change. Long-term rates will tend to fall and short-term rates to rise. In other words, the interest curve tends to become flat.

An ascending curve not only carries the implication that interest rates will rise but such a curve induces the Government to finance the deficit by increases in the floating debt which carries the lowest interest rate. Since the floating debt is held largely by commercial banks, this circumstance gives rise to further increases in the volume of credit.

The increase in bank credit during the war, from the end of 1941 to the end of 1945, was the greatest in the history of our country. Holdings of Government obligations on the part of commercial banks rose from 22 to 91 billion dollars and on the part of the Federal Reserve Banks from 2.4 to 24 billion dollars. Had the war been financed at a higher level of rates and had the interest curve been of the horizontal rather than of the ascending type, doubtless a smaller volume of bank credit would have been involved in the meeting of war costs. Higher short-term rates would have induced businesses and corporations to make greater use of their idle balances and higher long-term rates would have induced the investing public to purchase a greater volume of Government obligations.

To enable and induce commercial banks to purchase Government obligations a series of important credit and monetary actions were adopted. The Federal Reserve Banks stood ready to buy all Treasury bills offered at  $\frac{3}{8}$  of 1 per cent and, in general, to purchase other Government obligations whenever necessary to prevent yields from rising above the ceilings established. Member bank excess reserves were maintained at a level of about one billion dollars. Member bank reserve requirements were lowered in New York and Chicago. The discount rate on advances to member banks secured by Government obligations maturing or callable within one year was fixed at one-half of one per cent at all of the Federal Reserve Banks,<sup>1</sup> and at one per cent on advances secured by other Government securities. War loan accounts were exempted from reserve requirements. The reserve requirements of the Federal Reserve Banks against both notes and deposits were reduced to 25 per cent.

The exemption of the war loan account from reserve requirements meant that commercial banks increased their holdings of the public debt mainly during the loan drives. It was then that they purchased obligations sold by other investors who were reducing their portfolios in order to participate in the current drives. Later on, as the war loan account fell and private deposits rose, member banks, in order to build up their reserves to the legal minimum, shifted Government obligations to the Federal Reserve Banks.

The responsibility placed upon the Federal Reserve Banks to maintain the interest rate curve meant that they surrendered discretionary control over the amount and type of Government obligations they purchased. Control over open-market operations passed into the hands of the market. It was the market that decided the amount and type of Government securities to be shifted to the Federal Reserve Banks.

Commercial banks were not, as often alleged, simply residual buyers of the debt. They purchased the debt not at distressed prices but at rising prices. Had other policies been followed, had a larger proportion of war costs been financed from taxes, had a larger proportion of the debt been sold to buyers other than commercial

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<sup>1</sup> Eliminated April 25, 1946.

banks, had money rates not been artificially depressed, commercial banks would not have been under the same necessity to compete for the debt.

In 1945, when the belief became general that the Treasury could and would maintain interest rates, commercial banks actively purchased intermediate and long-term securities from other holders who, in turn, used the funds received to buy long-term issues currently offered in the loan drives. The competition of commercial banks for the obligations sold by non-bank investors led to an increase in their price and a sharp decline in their yield. The Treasury encouraged this tendency by not issuing 2 per cent obligations in 1945 and by refunding practically all of the maturing debt into certificates of indebtedness. This action gave commercial banks additional quantities of the short-term debt which they could shift to the Federal Reserve Banks in order to purchase the longer-term debt.

As a result of the developments outlined, the cheap-money policy developed in 1945 into a cheaper-money policy. The inflation in the Government bond market spread to other markets. Yields on corporate bonds declined. The prices of equities and real estate soared.

If inflation is to be checked, credit expansion must terminate. When credit expansion is brought to an end, interest rates will rise. Just as present interest rates are the result of huge credit expansion, so will the checking of credit expansion lead inevitably to higher interest rate levels. Short-term rates will rise faster than long-term rates and may actually exceed long-term rates.

Past experience demonstrates that a rise in prices is followed sooner or later by an increase in interest rates. The relationship existing is indicated in the following table which is based on British experience:

Table II  
LONG WAVE-LIKE FLUCTUATIONS

Wholesale Prices (England)			Long-Term Interest Rates (England)		
	<i>Periods</i>	<i>Duration</i>		<i>Periods</i>	<i>Duration</i>
Rising	1789-1814	25 years	Rising	1792-1813	21 years
Falling	1814-1849	35	Falling	1813-1844	31
Rising	1849-1873	24	Rising	1844-5-1870-4	30
Falling	1873-1896	23	Falling	1870-4-1897	27
Rising	1896-1920	24	Rising	1897-1921	24

It is to be expected that a rise in interest rates will accompany, although often lagging behind, an increase in commodity prices. Profits tend to be greater on the upward sweep of price movements. Capital issues are stimulated and borrowings for business purposes increase. The demand for capital grows more rapidly than real savings accumulate. Moreover, as the price rise gains momentum and its continuation is expected, investors are less willing to buy long-term bonds except at rising interest rates, owing to their desire to be insured against a loss of purchasing power. This factor tends to reduce the volume of funds available for long-term investment.

This brings us back again to the fundamental point—that if price inflation is to be checked, credit expansion must be checked. Credit expansion will be checked when the Federal Reserve Banks are relieved of the responsibility of underwriting an arbitrary interest rate curve on Government obligations and when in consequence they can stop buying the debt.

In the elimination by several Federal Reserve Banks on April 25, 1946 of the preferential discount rate on member bank borrowings secured by Government obligations maturing or callable within a year, the Federal Reserve System has taken the first step towards the ultimate goal of allowing the yields on Government obligations to be determined by the competitive forces of the market. Once these rates are determined by competitive forces of the market, all rates will similarly be determined. The fact that the first step towards this ultimate goal has been taken would seem to indicate that the turning point in the bond market has occurred.

## HOW TO STIMULATE GIFTS ON THE ANNUITY BASIS

WILLIAM P. SCHELL, *Executive Secretary, Board of Foreign Missions, Presbyterian Church in the U.S.A.*

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When I received the invitation to speak on this topic, the temptation was to decline it. In no sense am I an expert or an authority in raising money for annuities; many of you have had much greater success. All I can hope to do is to offer a few suggestions resulting from personal experience, all of it in the service of one organization.

First, a few words regarding the necessary *psychology* as a background or stimulus before attempting to stimulate an interest in annuities. A prime requisite is that the promoter must himself believe wholeheartedly and enthusiastically in the desirability and value of annuities. This is a job which calls for an enthusiast, one might almost say for a fanatic. The second psychological factor is the possession and manifestation of an inner confidence, based upon the financial soundness of the organization he represents. One cannot have such a confidence and assurance if the organization is compelled to pay income on annuities out of receipts from current work. The third factor is the conviction that in offering to a "prospect" an annuity investment, you are conferring a favor on that person. You are offering him three distinct advantages; namely, *safety* for his investment, a better than ordinary *income return*, and the consciousness that after his death the residue of his annuity *will be used in the Lord's work*.

About a year ago I was privileged, at his request, to have a conference with the head of the Annuities Department of one of the largest life insurance companies. He told me that his company writes a maximum of \$100,000 in annuities on one life, and then added: "People come to us because they are, in the best sense, selfish. People who come to organizations like yours are motivated to some extent by selfishness, but largely because they love the Lord. Whenever you receive 'prospects' who are just selfish, send them to us; when we talk with 'prospects' who love the Lord, we will send them to you."

Well, backed up and fortified by these psychological factors, we start out to attempt to stimulate an interest in annuities. At the outset let us avoid one mistake. That is the mistake of thinking that most of

those who will give us annuities are persons of large means. This is not true. Occasionally we shall have the good fortune to secure an annuity of \$50,000 or \$100,000; but the number of people who can take such annuities, or even annuities of \$5,000 or \$10,000, is distinctly limited—and the majority of annuities will come to us in much smaller amounts. Another mistake is to judge a person's wealth by his personal appearance. Some of the largest annuities come from people who look anything but wealthy.

Now for a few suggestions as to *methods*. Luckily a number of different methods have been tried and found productive.

### THE PERSONAL TOUCH

It is my personal conviction that nothing can take the place of the *personal* touch. One institution which has been unusually successful in stimulating an interest in annuities has six salaried men on its payroll who spend every day making calls in geographical areas assigned to them. They are required to make a specified number of calls each day and to report every night in writing to the institution's headquarters how many calls they have made and what financial results have been achieved. Manifestly, such a salaried list of workers is not possible for many organizations, but that institution is on the right track.

A year ago I was asked by our Board to spend a month or six weeks in Florida in an effort to contact personally a large number of individuals for personal contributions or annuities. That trip was undertaken with some misgivings, because of discouraging results reported by others who had engaged in similar efforts; but the results turned out to be highly encouraging, many thousands of dollars in annuities materializing. The first call I made was upon a widow who had, on several occasions, sent us gifts of \$100. The main purpose of this call was to thank her personally for those gifts. After some conversation regarding annuities and legacies, she promised an outright gift of \$1,000 for Africa and an annuity, and an assurance that the work would be remembered in her will. During the few weeks spent in Florida many new personal contacts were established and old ones renewed.

A corollary of this method of promotion is to *multiply personal*

contacts by enlisting the help of friends, missionaries and other volunteer workers. While this personal touch is of paramount importance, it cannot be employed on a nation-wide scale.

### ADVERTISING

A word now about *advertising*. Advertising is always more or less of a gamble, but, for the most part, it pays. In trying to reach Christian people with advertisements on behalf of annuities, the question is naturally asked: "What media shall be used?" Some one asks: "How about the daily papers?" That is pretty much an untried field. One organization tested it out by inserting an advertisement costing \$150 in the Sunday edition of "*The New York Times*." In response to the advertisement fifty letters were soon received, asking for further information. The first forty-nine of these letters brought no annuities. It was natural to conclude that advertising annuities in daily papers does not pay. Then the fiftieth letter came, bringing an annuity of \$1,500, or ten times the amount of the advertisement.

The organization referred to above spent the sum of \$5,000 in 1945 on advertisements. The largest number of inquiries and the largest proportionate financial returns came, not from denominational papers reaching members of the denomination with which the organization is affiliated, but from "*The Christian Herald*" and "*The Federal Council Bulletin*." This, of course, may not prove to be the final story, for the effect of many advertisements cannot be known until years afterwards—but it does give an interesting picture of one year's experiment. One organization recently received an application for an annuity based upon a leaflet issued over twenty years ago and long since out of print.

### CORRESPONDENCE

Let us now consider the method of *correspondence*. If time and stenographic help could be found to write letters to 10,000 persons, in an effort to enlist their interest in annuities, the financial returns would be many times larger than in writing to 1,000 persons. One naturally assumes that every letter of inquiry will be answered. What then? How soon, if at all, should the inquirer be followed up? My own judgment is that not more than one month should elapse before a follow-up letter is sent. If that letter brings no response, a longer

time should be allowed to pass before another follow-up is made. Names of inquirers should be kept on the active or "live" list for several years.

A few in this audience will remember the late Rev. William N. Marquis, D.D., for many years a successful pastor in Illinois and later actively engaged in promotional work and in stewardship campaigns across the country. At one of these gatherings he related the following interesting experience: In 1879 he bought a suit of clothes from a well-known clothing firm in Philadelphia. Exactly a year later he received a letter from the store, reminding him of that purchase and suggesting that he make another. As he did not follow the suggestion, they wrote him again a year later. Every year for 40 years they wrote him. In 1919 he returned to the store and bought another suit.

#### AN ANNUITY ACTUALLY A GIFT

In conclusion, may we say that everybody should be considered a potential "Prospect." May we also add that in every attempt to sign up an annuity, the promoter should remember that he is really trying to secure an outright gift, for that is exactly what an annuity becomes on the death of the annuitant. On the average an annuity of \$1,000 is actually an outright gift of at least \$500. An organization which writes \$100,000 annually in annuities has actually secured approximately \$50,000 as an outright gift, to be expended eventually in the work entrusted to it.

The future for the promotion of annuities is bright. If any or all of the methods suggested above are used in the spirit of prayer, encouraging results are bound to be forthcoming.

# PROPOSED RATES FOR GIFT ANNUITY AGREEMENTS

GEORGE A. HUGGINS

*Consulting Actuary*

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There are four basic principles involved in the financing and administration of annuities which may be summarized as follows: (1) Expense of administration; (2) Security of principal; (3) Rate of earnings on invested reserves and (4) Rate of mortality among annuitant lives.

Let us consider them in order.

## 1. *Expense of administration*

No matter how economically an annuity department may be administered by a non-profit agency, certain administrative expenses are inherent which may be classed as (a) promotion or (b) administration.

(a) *Promotion*—In this line of activity, as in nearly every other like one, it pays to advertise and the volume of gifts received as consideration for annuity agreements is generally in direct relationship to the promotional appeal. However, we do have to consider the amount that can reasonably be expended for that purpose.

(b) *Administration*—The administration expenses need not be very great but every outstanding annuity agreement carries with it some administrative expense, regardless of whether these expenses of administration are charged against the annuity department or are financed out of the general administrative expense budget of the organization. The fact remains that they are there, even though more or less under the control of the management.

In the rates proposed for consideration, we have made an allowance of 5% of the total gift for the expenses of promotion and administration. Of course, that does not necessarily mean that that money has to be expended. The lower the expense rate, the better are the results to the organization as to the available gift portion of the total contribution.

## 2. *Security of principal*

This is a very important element in our problem. However, the

principal of the reserves necessary to provide the promised annuity payments can be safeguarded by a wise investment program that is designed more with a view to the protection of the principal than to a high rate of yield. Furthermore, investment losses of principal can be made up out of profits on sales or excess earnings on the invested reserves or, as a last resort, out of the gift portion of the original contribution. This element is more or less within the control of the management.

### 3. *Rate of earnings on invested reserves*

The yield rate on invested reserves is pretty much a matter wholly out of our control. It is affected by economic and governmental influences which make us the sinned against rather than the sinners.

The basic laws of supply and demand, which should play such an important part in the yield on invested reserves; i.e., the rental value of the funds, no longer operate freely. This is due largely to governmental control and regulation of interest rates. The Federal government is confronted with the payment of interest on a funded debt that is staggering in its enormity. Therefore, from the viewpoint of the funds required annually to meet the interest on the public debt, the Treasury Department officials are directly interested in the rate of interest on the debt and aim to force down and keep down the rate of interest on U. S. Government bonds. Again, in the event of the refinancing of U. S. Government securities which cannot be met with cash, the lower the yield rate, the better the terms they can get in such refinancing.

From the standpoint of the investor another element has been injected into the situation which greatly affects the earning power of industrial corporations and consequently their ability to earn their fixed charges and to pay dividends on their stocks. This is the policy now being fostered by the Administration of encouraging demands, particularly union demands, for increased wages while holding down the market prices of the manufactured products.

During the last generation, it was quite a common practice among non-profit agencies and even insurance companies to offer annuity rates based upon 4% as the assumed rate of interest earnings on the reserves. As a matter of fact the annuity rates adopted by the First Conference on Annuities held April 29, 1927 (almost 19 years ago)

were based upon  $4\frac{1}{2}\%$  and the  $4\%$  basis was not adopted until the Fifth Conference held November 20, 1934. The assumed interest rate later had to be dropped to  $3\frac{1}{2}\%$ , then  $3\%$  and then  $2\frac{1}{2}\%$ , and today many commercial insurance company annuities are being offered on a  $2\%$  interest rate. Almost all of the non-profit agencies, however, are still using the 1941 rate based upon an assumed yield of  $3\frac{1}{2}\%$ .

When we speak of interest in this connection, we mean, of course, the interest earnings from year to year on invested reserves, but in calculating single premiums and reserves for annuities we must get the present value of future payments and so the interest element is rather a discount element. Therefore, the lower the rate of discount the larger is the principal or premium to be paid into the fund to provide a given annuity. The converse is that for a given amount of money only a lesser annuity can be provided as the interest rate is lowered. Taking all factors into consideration and in the interest of conservatism, we have used the rate of  $2\frac{1}{2}\%$  in our calculations of proposed annuity rates. This is only adopting the standard already accepted by life insurance companies for some years, but not adopting the lower current rate of  $2\%$  that is now largely in force.

#### 4. *Rate of mortality among annuitant lives*

The rate of mortality among annuitant lives affects the duration of the period of the annuity payments. While no one can foretell the future lifetime of an individual, nevertheless we can with a fair degree of accuracy ascertain the future lifetimes of members of a group. The larger the group the more normal will be the year to year experience. The smaller the group the more violent will be the year to year fluctuation and experience.

In recent years there have been material increases in the longevity of our population. For example, the Metropolitan Life Insurance Company announces that among its industrial policyholders life expectancy from birth in 1942 was 64.18 years with a slight recession later. This compares with 63.56 in 1943; 51.64 in 1919-20; 46.63 in 1911-12; and 34.00 for the period 1879-89.

According to the U. S. Census figures the expectation of life from birth among white males was 62.12 years in 1938 and 66.20 for females as compared with 59.88 for males and 63.56 for females, in

1931; while in 1901 the corresponding figures were 48.23 and 51.08. And yet one hears people sigh for the good old days.

While most of the improvement in mortality has occurred among the younger lives, nevertheless much improvement has occurred among the older lives also and here is where we come into the picture very largely in the gift annuity field.

The life insurance companies which issue annuities have had to abandon mortality table after mortality table as their experience showed lowering mortality among their annuitant lives; i.e., further lengthening of annuitant lives as a group. I have in mind the McClin- tock, the American Annuitant, the Combined Annuity Tables and now the latest table, the 1937 Standard, is already proving inadequate and has to be modified by setting back the ages one or two years.

During the period July 1, 1931 to June 30, 1936, 10 of the largest insurance companies had 5,668 deaths among annuitant lives as compared with 5,902 expected deaths on the basis of the American Annuitant Select Table, a ratio of 96%. But during the period July 1, 1936 to June 30, 1941, when measured by the same yardstick their actual deaths were 25,063 as compared with expected deaths of 30,119, a ratio of 83%; and so it goes.

To what extent these changes will go is still unknown to us. We have observed a similar experience among our gift annuitant lives, where the rate of mortality seems to be running about 80% of the Combined Annuity Table or very close to the 1937 Standard Annuity Table.

In connection with the problem of future longevity, it is of interest to note the following comparisons of years of Life Expectancy.

	(1)		(2)		(3)	(4)	(5)
	1937 Standard No set back		Combined Annuity No set back		Combined Annuity Ages set back 2 Years	1937 Standard Ages set back 1 Year	Difference in Years (3) and (4)
<i>Age</i>	<i>Male</i>	<i>Female</i>	<i>Male</i>	<i>Female</i>	<i>Female</i>	<i>Female</i>	—
60	17.55	21.02	15.79	18.49	19.91	21.75	1.84
65	14.40	17.55	12.74	15.15	16.44	18.22	1.78
70	11.60	14.40	10.06	12.17	13.32	15.01	1.69
75	9.17	11.60	7.78	9.57	10.56	12.14	1.58
80	7.11	9.17	5.88	7.37	8.20	9.63	1.43
85	5.41	7.11	4.36	5.55	6.23	7.49	1.26

When expressed in dollars the changes in the bases of the annuity rates adopted by the several conferences on annuities are as follows:

**Present value of \$1.00 of annuity payable at the end of the year**

	(1)	(2)	(3)	(4)	(5)	(6)
Mortality Table	McClintock's <i>Male</i>	American Annuitants (Select) <i>Female</i>	Combined Annuity <i>Female</i>	Combined Annuity <i>Female</i>	1937 Standard <i>Female</i>	% of Increase (1) to (5)
<i>Interest</i>	4½%	4½%	4%	3½%	2½%	
<i>Ages set back</i>	—	—	—	2 years	1 year	—
<i>Age</i>						
60	9.501	11.076	11.758	13.028	15.476	63
65	8.027	9.702	10.140	11.273	13.423	67
70	6.549	8.312	8.527	9.524	11.408	74
75	5.135	6.953	6.970	7.833	9.478	85
80	3.851	5.672	5.524	6.255	7.683	100
85	2.747	4.508	4.231	4.836	6.062	121

In studying the actual operation of a segregated gift annuity reserve fund that is conducted in accordance with the requirements of the Insurance Department of New York; viz., the Combined Annuity Table with ages set back one year and with interest at 3½% and a 10% margin for contingencies, there has been an annual deficit which approximates 1% of the reserves on hand. This is in part due to the fact that the earmarked securities do not produce the required 3½% interest and in part due to the fact that the mortality experience in the way of deaths and resulting reserves released by death is less favorable than that of the tabular basis. This experience is not a unique one and so we must face the prospect of basing our annuity rates upon a lower rate of mortality and lower rate of interest.

We can sum up the situation confronting us in considering annuity rates by saying that the administrative expenses and the security of the principal are more or less in our control but the yield on invested reserves and the rate of mortality among the annuitant lives are more or less beyond our control. We must, therefore, be very conservative in the mortality and interest basis adopted for calculating our annuity rates.

### 5. *Summary of Annuity Rates of Conferences on Annuities*

In reviewing the history of the rates adopted by our Conferences on Annuities, we find the first set of rates adopted April 29, 1927 were based upon the McClintock Table of Mortality, male life for single-life cases and male and female lives for the joint-life and survivor cases with interest at  $4\frac{1}{2}\%$  and a 70% residuum.

These rates started at 5% at age 30 and were limited to 9% at ages 76 and older.

However, we did not get many organizations to adopt these rates since they preferred to stick to their own higher ones.

The objective of this First Conference was to show rates which might be regarded as the pale, so that organizations issuing higher rates were beyond the pale and those who used these rates or lower were within the pale.

The Second Conference on Annuities held November 9, 1928 reaffirmed the rates of the April 9, 1927 Conference.

The Third Conference on Annuities was held November 17, 1930. At this Conference the question of adopting a lower set of rates and urging their adoption as uniform rates came up for consideration but no specific action was taken.

The Fourth Conference was held on March 17, 1931 and the first set of uniform rates was adopted. These were based upon the American Annuitants Table of Mortality (Select) female lives, interest at  $4\frac{1}{2}\%$ , residuum of 70%. The rate at age 30 was 4.8% with a limiting rate of 8%.

The Fifth Conference was held on November 20, 1934. At that time a lower set of uniform rates was adopted based upon the Combined Annuity Table, female lives, interest at 4% with rates starting at 3.0% and with the 8% limit at the higher ages.

At the Sixth Conference, which was held October 5, 1939, the present uniform rates were adopted. These are based upon the Combined Annuity Table, female lives, ages set back two years and interest at  $3\frac{1}{2}\%$ . The rates start at 2.5% at age 30, with a 7% limit at the higher ages.

We are now confronted with the adoption of rates on a basis of mortality and interest more nearly in line with the conditions which

now exist and which may confront us during the future lifetime of our new annuitants. This means a mortality table which would have provision for increased longevity as compared with the table of mortality now in use, and with a lower rate of interest than  $3\frac{1}{2}\%$ .

After much careful study and consideration, the Committee on Annuities proposes today a set of rates based upon interest at  $2\frac{1}{2}\%$  and the 1937 Standard Annuity Table of Mortality female lives with ages rated as one year younger.

This device of setting back the ages enables us to use a table that is standard among the life insurance companies but modified so as to make provision for greater longevity than would exist under a group whose rate of mortality exactly paralleled this table. It simply means that, for our purpose, we consider a life of 66 to have the longevity of a life of 65; a life of 71, the longevity of a life of 70, and so on down the line.

All statistical experience based upon annuitant lives has clearly demonstrated that there is greater longevity among groups of female lives than among groups of male lives, and this should be taken into account particularly where gift annuity agreements seem to predominantly involve women as the donors of these gifts subject to annuity agreements.

In the set of uniform rates approved by the Sixth Conference, which have been adopted quite universally, certainly to a very gratifying degree we have used the rates based upon a female life mortality table, even though the donor may be a male life. To what extent this has affected the volume of gifts from male lives is problematic, yet we do wish to encourage male lives to make such gifts and to remove any feeling that they are being discriminated against.

A study of the valuation reports for five different organizations shows that there were in force 244 gift annuities classed as single-life males out of a total number of 2,060, so that 11.84% of these gifts were on male lives and 1,816 were on female lives, or 88.16%.

The corresponding amounts of the original gifts were \$392,169 out of total gifts of \$3,077,241, a ratio of 12.74%.

There are several points that somewhat affect these figures, such as the fact that the surviving life of a two-life case is included in these

single life studies; nevertheless in this considerable group of annuities the proportion of annuities on male lives is quite low, approximately 12%, while the individual gifts are slightly larger, approximating 13%.

Therefore the Committee on Annuities propose for consideration that the rates for male lives be modified by allowing them the rate for a female life three years older.

For example, if this rule prevailed a male donor of 70 would receive the same annuity rate as a female of 73; viz., 5.5% as compared with 5.1%, which is the rate shown in the table for a life aged 70.

A very important consideration confronting us is to what extent the organization should be the gainer by the gift. In other words, how much of the total gift should be absorbed in the annuity payments and how much should go for the benefit and purposes of the organization. It is not our purpose to render solely annuity service to the public. That is wholly out of our province and field of activities. Our main purpose is to secure gifts to help carry on the work of our organizations. The annuity rate is incidental but, of course, must be one that would provide some income to donors at the same time that they are making a contribution to the work of the organization.

In the rates proposed, it is our thought that the organizations should share some of the losses under these adverse conditions that have developed. We are, therefore, proposing a set of rates with a 50% residuum as contrasted with the 70% residuum which has been the basis of our rates to date.

In Schedule A, herewith, there are shown three columns of rates according to the age at nearest birthday at the date the annuity agreement becomes effective.

In column (1) there are shown the present rates, in column (2) the rates that are referred to as unmodified and in column (3) those that are designated as modified, which are the rates proposed by the Committee on Annuities.

What do we mean by unmodified and modified? Unmodified rates are those that might be referred to as the tabular rates; i.e., they are calculated in accordance with the formulae and the basic table. They are the ones that are based upon age, sex, mortality, interest and residuum, as outlined in the footnotes on the sheet.

The modified rates are those that are scaled down arbitrarily at the early ages and held at 7% at the higher ages.

It will be noted that the proposed rates start at 2% up to and including age 35 and then lift by 0.1% until the unmodified rates are reached at age 50. Thereafter there is no modification until age 81, when the 7% ceiling rate becomes operative.

In Schedule B we show specimen rates where two lives are involved; that is, joint-life and survivor annuities. Here are shown the present rates and the proposed rates. The latter are calculated and modified exactly in accordance with the rules governing the calculation and modification of the single-life rates.

As a further guide to our thinking, we are submitting also Schedule C, in which we show for single-life annuities at specimen ages the commercial annuity rates generally in use today by life insurance companies, the present uniform rates, and rates calculated at various rates of interest and with various percentages of residuum. The rates in the last column in Schedule C are the ones that appear in column 2 at all ages in Schedule A.

If the proposed annuity agreement rates—single-life annuities, female—set back one year and loaded 5%—which are calculated to produce a 50% residuum (except where the modifications would produce larger results) are not used; and if the present rates are continued in use and if the actual experience as to mortality, interest and expense parallels that assumed as the basis of the proposed rates, then the percentage of residuum would be as follows:

Age Nearest Birthday	Proposed Rates	Present Rates	Present Rates Residuum %
50	3.5	4.0	32
55	3.8	4.5	27
60	4.1	4.7	35
65	4.5	5.1	39
70	5.1	5.5	44
75	5.9	6.2	47
80	6.9	7.0	49

## SCHEDULE A

## UNIFORM ANNUITY AGREEMENT RATES

(Semi-annual Annuity Payments)

*Single-Life Annuities—Female*

<i>Single-Life Annuities—Female</i>				<i>Single-Life Annuities—Female</i>					
(1)		(2)		(1)		(2)		(3)	
Age	Proposed Rates			Age	Proposed Rates				
Nearest Birthday	Present Rates	Unmodified	Modified	Nearest Birthday	Present Rates	Unmodified	Modified		
30	2.5%	2.9%	2.0%	58	4.6%	4.0%	4.0%		
31	2.5	3.0	2.0	59	4.7	4.0	4.0		
32	2.5	3.0	2.0	60	4.7	4.1	4.1		
33	2.5	3.0	2.0	61	4.8	4.2	4.2		
34	2.5	3.0	2.0	62	4.8	4.3	4.3		
35	2.5	3.0	2.0	63	4.9	4.4	4.4		
36	2.6	3.1	2.1	64	5.0	4.4	4.4		
37	2.7	3.1	2.2	65	5.1	4.5	4.5		
38	2.8	3.1	2.3	66	5.1	4.6	4.6		
39	2.9	3.1	2.4	67	5.2	4.7	4.7		
40	3.0	3.2	2.5	68	5.3	4.9	4.9		
41	3.1	3.2	2.6	69	5.4	5.0	5.0		
42	3.2	3.2	2.7	70	5.5	5.1	5.1		
43	3.3	3.3	2.8	71	5.6	5.2	5.2		
44	3.4	3.3	2.9	72	5.8	5.4	5.4		
45	3.5	3.3	3.0	73	5.9	5.5	5.5		
46	3.6	3.4	3.1	74	6.0	5.7	5.7		
47	3.7	3.4	3.2	75	6.2	5.9	5.9		
48	3.8	3.4	3.3	76	6.3	6.1	6.1		
49	3.9	3.5	3.4	77	6.5	6.3	6.3		
50	4.0	3.5	3.5	78	6.7	6.5	6.5		
51	4.1	3.6	3.6	79	6.9	6.7	6.7		
52	4.2	3.6	3.6	80	7.0	6.9	6.9		
53	4.3	3.7	3.7	81	7.0	7.2	7.0		
54	4.4	3.7	3.7	82	7.0	7.4	7.0		
55	4.5	3.8	3.8	83	7.0	7.7	7.0		
56	4.5	3.8	3.8	84	7.0	8.0	7.0		
57	4.5	3.9	3.9	85	7.0	8.4	7.0		

- BASES: (1) Combined Annuity Table of Mortality, ages rated as two years younger, female lives; interest at  $3\frac{1}{2}\%$ ; residuum of 70%; rates modified at older and younger ages.
- (2) 1937 Standard Annuity Table of Mortality, ages rated as one year younger; interest at  $2\frac{1}{2}\%$ , residuum of 50%; expense loading of 5% of total gift.
- (3) 1937 Standard Annuity Table of Mortality, ages rated as one year younger; interest at  $2\frac{1}{2}\%$ ; residuum of 50%; expense loading of 5% of total gift; rates modified at older and younger ages.

NOTE—In the case of a male life, the proposed rate applicable is the one shown in column (3) for an age three years older.

## ANNUITY AGREEMENTS

## SCHEDULE B

## UNIFORM ANNUITY AGREEMENT RATES

*Two Lives—Joint Life and Survivor—Female*  
(Semi-annual Annuity Payments)

TABLE (1) PRESENT RATES

Age Nearest Birthday	80	75	70	65	60	55	50	45	40	35	30
80	5.8%										
75	5.5	5.3%									
70	5.2	5.0	4.8%								
65	4.9	4.8	4.6	4.5%							
60	4.6	4.5	4.5	4.4	4.3%						
55	4.4	4.4	4.3	4.3	4.2	4.1%					
50	3.9	3.9	3.9	3.9	3.9	3.9	3.9%				
45	3.4	3.4	3.4	3.4	3.4	3.4	3.4	3.4%			
40	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9%		
35	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5%	
30	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5%

TABLE (2) PROPOSED RATES

Age Nearest Birthday	80	75	70	65	60	55	50	45	40	35	30
80	5.4%										
75	5.0	4.7%									
70	4.6	4.4	4.2%								
65	4.3	4.2	4.0	3.9%							
60	4.0	3.9	3.8	3.7	3.6%						
55	3.7	3.7	3.6	3.5	3.4	3.3%					
50	3.4	3.4	3.4	3.4	3.3	3.2	3.2%				
45	2.9	2.9	2.9	2.9	2.9	2.9	2.9	2.9%			
40	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4%		
35	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0%	
30	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0%

BASES: (1) Combined Annuity Table of Mortality, ages rated as two years younger, female lives; interest at  $3\frac{1}{2}\%$ ; residuum of 70%; rates modified at younger ages.

(2) 1937 Standard Annuity Table of Mortality, ages rated as one year younger; interest at  $2\frac{1}{2}\%$ ; residuum of 50%; expense loading of 5% of total gift; rates modified at younger ages.

NOTE—In the case of a male life, the proposed rate applicable is the one for an age three years older than the one shown in table (2).

## SCHEDULE C

## ILLUSTRATIONS OF ANNUITY AGREEMENT RATES

*Single-Life Annuities—Female*

Age Near- est Birth- day	Com- mer- cial Annu- ity Rates	Pres- ent Uni- form Rates	Rates with Varying Rates of Interest and Percentages of Residuum								
			70% Residuum			60% Residuum			50% Residuum		
			3½%	3%	2½%	3½%	3%	2½%	3½%	3%	2½%
30	3.5%	2.5%	3.6%	3.1%	2.7%	3.7%	3.2%	2.8%	3.8%	3.4%	2.9%
35	3.8	2.5	3.6	3.2	2.7	3.8	3.3	2.9	3.9	3.5	3.0
40	4.0	3.0	3.7	3.3	2.8	3.9	3.4	3.0	4.0	3.6	3.2
45	4.4	3.5	3.8	3.4	2.9	4.0	3.5	3.1	4.2	3.7	3.3
50	4.8	4.0	3.9	3.5	3.0	4.1	3.7	3.3	4.4	3.9	3.5
55	5.3	4.5	4.0	3.6	3.1	4.3	3.9	3.5	4.6	4.2	3.8
60	6.0	4.7	4.2	3.8	3.3	4.5	4.2	3.7	4.9	4.5	4.1
65	7.0	5.1	4.5	4.0	3.6	4.9	4.5	4.1	5.4	5.0	4.5
70	8.2	5.5	4.8	4.3	3.9	5.4	4.9	4.5	6.0	5.5	5.1
75	9.9	6.2	5.2	4.8	4.3	6.0	5.5	5.1	6.7	6.3	5.9
80	12.2	7.0	5.8	5.4	4.9	6.8	6.4	5.9	7.8	7.4	6.9
85	15.4	7.0	6.6	6.2	5.7	7.9	7.5	7.0	9.3	8.8	8.4

## BASES:

*Commercial Annuity Rates:*

1937 Standard Annuity Table of Mortality, ages rated as one year younger; interest at 2½%; expense loading of 6½% of gross; monthly annuity payments.

*Present Uniform Rates:*

Combined Annuity Table of Mortality, ages rated as two years younger, female lives; interest at 3½%; residuum of 70%; semi-annual annuity payments; rates modified at older and younger ages.

*Rates with Varying Rates of Interest and Percentages of Residuum:*

1937 Standard Annuity Table of Mortality, ages rated as one year younger; interest as indicated in table; residuum as indicated in table; expense loading of 5% of total gift; semi-annual annuity payments.

# RECENT TAXATION OF ANNUITIES

GILBERT DARLINGTON, *Chairman, Committee on Annuities*

## 1. Canadian Taxation

The Canadian Income Tax Act was amended in 1945 in respect to the taxation of annuity payments. All annuity payments are now divided into taxable and non-taxable portions. This change applies to income of 1945, and, subject to any further amendments, to income of subsequent years, and the *Life Insurance Companies in Canada* are requested to file a report with the Income Tax Division of the Dominion Government on the following form ("T-5 Annuities Supplementary") prescribed by the Minister of National Revenue, giving details of each annuity contract:

T-5 Annuities Supplementary

ANNUITIES RECEIVED UNDER A CONTRACT  
WHETHER EXEMPT OR NOT

FORM PRESCRIBED AND AUTHORIZED BY  
MINISTER OF NATIONAL REVENUE

PAYEE { Mr. Mrs. Miss		ADDRESS			
Contract Number		Date of Issue	Year of Vesting	Description of Contract	
Year of Birth	Sex	Yearly Amount of Instalments	(a) Capitalized Value	(b) Number of Yearly Instalments Expected	*Exempt Portion of Yearly Instalments
REMARKS					
NAME OF COMPANY		Date of Filing	* Formula for Exempt Portion of Yearly Instalments	=	Item (a) Divided by Item (b)

The taxpayer must make a special report under Item 32 in the 1945 Dominion of Canada Income Tax Form "T-1 General 1945." This says: "Note—All recipients of annuities must attach a statement from the issuer of the annuity on a form prescribed by the Minister or a signed statement by a qualified person showing all of the essential factors required to be considered in determining the amount in Item 32 (3). Annuity income is investment income." This makes three copies of Form "T-5 Annuities Supplementary" that should be sent, (1) to the Income Tax Division of the Dominion Government; (2) to the annuitant to forward with his 1945 Tax Return; (3) to be retained by the annuitant for use in preparing income tax returns in

future years, as the Company reports each annuity only once and not annually.

The capitalized values of Canadian Annuities are determined by the 1937 Standard Annuity Table with interest at 4% where there is no cash surrender or commuted value.

A letter from the Hon. C. F. Elliott, Deputy Minister of Taxation, Ottawa, to the American Bible Society, dated Mar. 30, 1946, does not request the Society to fill in "Form T-5 Annuities Supplementary" and to send one copy to the Income Tax Division of the Dominion Government and two copies to the annuitant:

American Bible Society,  
Bible House,  
Park Avenue & 57th Street,  
NEW YORK 22, N. Y., U. S. A.

*Attention: Mr. Gilbert Darlington*

Dear Sirs:

With reference to your letter of the 26th instant, arrangements have been made under which the taxable element in all annuities will be determined in this country. Consequently, if there are any persons receiving payments under an annuity contract issued by you, they should forward such contract to their local Inspector of Income Tax who will have the matter determined for them. In view of this it will not be necessary for you to make the determination but any person who inquires should be referred to the Inspector of Income Tax of the district in which they reside.

Yours faithfully,

C. Fraser Elliott

Deputy Minister (Taxation)

JSF/MEM

The American Bible Society is not a Life Insurance Company in Canada. It does not have offices or accept annuity gifts through agents in Canada. This letter may not apply to organizations that have offices in Canada or conduct the business of soliciting or writing annuities there.

## 2. Unfair Taxation of Annuities under the Federal Income Tax Law

The following statement is one that has been sent to the Secretary of the Treasury, the Chairman of the House Ways and Means Committee, the Chairman of the Senate Finance Committee, the Chairman of the Joint Committee on Taxation, and to others, in order to bring

out clearly the present inequitable position of annuitants under the Federal Income Tax Law.

It is assuring to know, not only that the Treasury Department and members of Congress know these facts, but also that there appears to be a willingness to remedy these injustices in the next Federal Income Tax Law.

The statement sent out by the Chairman of the Committee on Annuities on March 1, 1945 is as follows:

A great injustice is being done to annuitants by the present provisions of the Internal Revenue Code relating to the taxation of annuities. Under Section 22(b)(2) of the Internal Revenue Code annuitants are required to include in their gross income 3% of the cost of their annuities in spite of the fact that on annuities purchased in recent years life insurance companies are crediting annuitants with only 2½% or 2% interest on the diminishing amount of principal. The average rate of interest actually credited to annuitants on these annuities is therefore less than 1¼% per year over the life of the annuity. In addition the insurance companies at present add 6½% for loading to the cost of the annuities, on which no interest is, of course, ever earned.

The disparity between the amount which the Internal Revenue Code requires to be reported, in effect, as interest income and the interest actually received by the annuitant is so great that in many cases it is impossible for the annuitant ever to recover his principal tax-free. This is startlingly true with respect to younger-age annuitants, as is shown in the following few examples, which are based on the 1937 Standard Annuity Tables now in use by many insurance companies:

1. The cost of an annuity of \$100 a year for a male aged 25 is \$2,831.80; his life expectancy is 46.5 years. Under the present law he is required to report as income each year 3% of his cost, or \$84.95, excluding from income only \$15.05. He would therefore need to live 188 years from the date of the purchase of the annuity before he would receive a return of his principal tax-free.

2. For a male aged 40 the cost of a comparable annuity is \$2,291.90; and his life expectancy is 33 years. He would have to report as income each year \$68.75 and exclude \$31.25. This man would therefore have to live 73 years from the date of the purchase of the annuity, or to an age of 114 years, before he would receive a return of his principal tax-free.

3. For a male aged 60 the cost of the same annuity is \$1,435.60; his life expectancy is 17.5 years. He reports \$43.07 each year as income and excludes \$56.93. Even this man would have to live 25 years from the date of the purchase of the annuity

ity in order to recover his principal tax-free, although at that time his life expectancy is only 17 years

It is, of course, impossible to provide a simple general rule for determining for any particular annuity the exact amount of interest that will be paid to the annuitant, as we cannot predict how long the annuitant will live. It is possible, however, to provide a general rule which does reflect the *average* amount of interest for all annuities. This *average* amount of interest included in annuity payments is the excess of (1) the expected annuity payments at the time of purchase of the annuity (annual annuity payment times years of life expectancy) over (2) the cost of the annuity. In the example numbered 3 above, this is \$264 (\$1,700 less \$1,436). The interest factor divided by the number of years of life expectancy equals the average interest per year on a level straight-line basis. This figure of annual interest is as close to the actual interest credited on the annuity as actuarial science can devise.

It is respectfully suggested that the present law be amended so as to allow the interest factor in annuity payments to be determined as set forth above. Considering annuitants as a class, the Government would collect the full amount of the interest factor; annuitants who did not live out their full life expectancy would have reported less than the expected amount of interest, but this would be offset by the fact that annuitants who outlived their life expectancy would have reported a greater amount of interest. Inasmuch as annuitants who die after having received only a few annuity payments fail to recover even their principal, and actually receive no interest, the Government revenues are not injured if, in effect, those unused principal refunds are allowed to the annuitants who outlive their life expectancy.

The present law, in addition to imposing a tax on a much greater amount than is ever actually received as interest, places a difficult burden on annuitants, as they must keep exact records of the amount of principal recovered tax-free. Further, under the present system, annuitants who do live long enough to recover their principal tax-free have to pay taxes on the full amount of later annuity payments, with the result that the tax burden is greatest in the last and oldest years of life.

In view of the patent inequity of the present method of taxing annuities, I respectfully urge that the present Congress amend the law so as to provide that the total amount of interest on any annuity should be computed by subtracting the cost of the annuity from the expected annuity payments to be received, as set forth above. This total amount of interest should be computed upon the basis of the tables in use by the respective Insurance Companies at the time of the purchase of the annuity. It should further be provided that the interest income to be reported each year should be a level amount determined by dividing the total interest factor by the number of years of life expectancy at the time of the purchase of the annuity. Such an amendment would not only remove a present inequity in the

law but would also be a further and desirable step towards tax simplification, in that all annuitants would know without the necessity for an annual computation the proper portion of the annuity payment which should be reported as income.

GILBERT DARLINGTON  
Treasurer, American Bible Society  
450 Park Avenue  
New York 22, N. Y.

March 1, 1945.

GD-amg

The Canadian Income Tax Act has been amended to provide that only the interest element of annuity payments will be taxable in Canada.

It would be simpler if similar action was taken in the United States. However, as all annuities issued by religious, educational and charitable corporations after January 1, 1942 are valued by the Standard Annuity Table, it will be easy to apply this table to all future annuities and to those issued after January 1, 1942. This will mean that, as the annuity gifts are received, the annuitant can be informed of the exact amount of the annuity each year to be included in his Gross Federal Income Tax. This amount will not change as long as the annuitant lives.

However, on annuities issued prior to January 1, 1942, many of them have received back, under the Estate Tax Table, a large part of the 'market value' of their annuities. It is probably fairer, therefore, to request the Treasury Department and Congress to reduce the present 3% of the market value that must be included in gross income to 2% of the original purchase price or market value as determined by the Estate Tax Table. This 2%, however, should be made constant during the lifetime of the annuitant. Otherwise those who live beyond their life expectancy are required to include all of their annuity in their Federal Income Tax at the time when their earning power is lowest and when they are most dependent upon others because of their extreme age.

## Minutes of the Eighth Conference on Annuities, called by the Committee on Annuities of the Federal Council of the Churches of Christ in America

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The Eighth Conference on Annuities met in the Assembly Room of the Board of Foreign Missions of the Presbyterian Church, 156 Fifth Avenue, New York, N. Y. on Wednesday, April 10, 1946, at ten a. m.

Dr. Gilbert Darlington, Chairman of the Annuity Committee of the Federal Council, presided. Dr. Cavert was present and welcomed the Conference on behalf of the Federal Council of Churches.

A list of members present is in the possession of the Federal Council. See list on pages 38, 39, and 40.

After invocation by Dr. George A. Heiss (Church of the United Brethren, York, Pa.) the following addresses were presented:

### INTEREST RATES AND POSSIBLE FUTURE TRENDS.

 DR. B. H. BECKHART, *Professor of Banking, Columbia University, New York City.*

### HOW TO STIMULATE GIFTS ON THE ANNUITY BASIS.

DR. WILLIAM P. SCHELL, *Executive Secretary of the Board of Foreign Missions of the Presbyterian Church in the U. S. A. —Headquarters, New York City.*

### ACTUARIAL PROBLEMS.

Proposed rates based on the (a) Standard Annuity Table and (b) on the Combined Annuity Table. Presentation of Proposed New Annuity Rates. MR. GEORGE A. HUGGINS, *Consulting Actuary, Philadelphia, Pa.*

Before adjournment for lunch the Chairman proposed a Committee on Resolutions. He nominated the following, which Committee was approved:

DR. FRANK J. SCRIBNER, *Secretary, Annuity Fund for Congregational Ministers, New York City — Chairman.*

MR. C. N. WONACOTT, *Treasurer, Board of National Missions of the Presbyterian Church in the U. S. A., New York City.*

## ANNUITY AGREEMENTS

MR. W. H. CRAMBLET, *President, Bethany College, Bethany, West Virginia.*

MR. W. J. ELLIOTT, *Treasurer, Division of Home Missions and Church Extension—Methodist Church, Philadelphia, Pa.*

REV. THOMAS KIERNAN, *Catholic Foreign Miss. Soc. of America, Maryknoll, N. Y.*

(The Reverend Thomas Kiernan was not present.)

The Committee adjourned at twelve o'clock for lunch and reconvened at two o'clock, at which time the invocation was given by the Rev. H. Allan Scott of the **Ministers' Annuity Fund** of the Presbyterian Church in the United States, Louisville, Ky.

After a brief statement on "Taxation of Annuities" by Dr. Darlington, the Committee on Resolutions presented the following report.

## REPORT OF THE COMMITTEE ON RESOLUTIONS

I. That the Conference on Annuities—held on Wednesday, April 10, 1946 under the auspices of the Committee on Annuities of The Federal Council of the Churches of Christ in America—recommend to the various Societies, Boards, Agencies and Colleges issuing gift annuities the adoption of rates based upon the following assumptions:

- (a) An expected residuum at the termination of the annuity equivalent to 50 per cent of the original gift;
- (b) The '1937 Standard Annuity Table' of Mortality with female ages set back one year;
- (c) Expected interest at the rate of  $2\frac{1}{2}$  per cent;
- (d) An expense loading equivalent to 5 per cent of the total gift;
- (e) Rates modified in accord with the schedule attached to this recommendation as applied to ages under 50 and over 80 years.

II. That the Conference on Annuities leave to the judgment of each organization issuing gift annuities the adoption of a differential as between male and female ages.

III. That the following resolutions prepared by Dr. Gilbert Darlington be approved for substance of doctrine and be made the expression of this Conference, subject to verbal editing:

RESOLVED, that the Conference on Annuities held on April 10, 1946 in New York under the auspices of the Committee on Annuities of The Federal Council of the Churches of Christ in America and attended by representatives of 50 different Societies, Boards, Agencies, Colleges, et cetera,

APPROVES of the action of Gilbert Darlington, Chairman of the Committee on Annuities, in petitioning the Treasury Department and the Congress of the United States to change the present method of taxing annuities because it is unfair, unjust and inequitable for the following reasons:

- (1) Because the 3% rule requires earnings of almost 6% on the reserves held for each annuitant; whereas actual earnings on these reserves are very much less, and the annuitant is only credited with interest at  $2\frac{1}{2}\%$ , or 2%, on all recent annuities that are computed on the Standard Annuity Table;
- (2) Because it taxes annuitants on the refund of their principal;
- (3) Because few annuitants will live long enough to receive back tax-free all of the principal or market value paid for their annuities;
- (4) Because it places the heaviest burden of taxation on those annuitants who outlive their life expectancy and must then include the whole amount of their annuities in their gross income.

RESOLVED, that this Conference on Annuities requests the Treasury Department and the Congress of the United States to grant relief from the present unjust, inequitable taxation to all annuitants by

- (1) reducing the 3% of the original market value of their annuities that must now be included in gross income on all annuities issued before January 1, 1942 to 2% on the market value of their annuities when they were first issued, and that this 2% of the original cost or market value as determined by the present Federal Income Tax Laws remain constant during the life of the annuitant;
- (2) that on all annuities issued after January 1, 1942 the actual net interest credited to the annuitant by the tables used

by the issuing company, society or association be computed by subtracting from the sum total of the annual payments expected to be received by the annuitant or annuitants the purchase price or commuted value of the annuity. This gives the total net income credited to the annuitant or annuitants. This sum is divided by the number of years the payments are expected to run. The quotient is the average amount of income derived each year from the investment and is taxable as such.

By this method each future annuitant will know when his or her annuity is purchased, the exact amount to include in his or her gross income for the Federal Income Tax; and those who are the oldest and least able to earn their living will not be penalized in their declining years when their lack of earning power and dependence are greatest.

IV. That this Conference extend a vote of thanks to the Committee on Annuities for their services in arranging this meeting, to Mr. Huggins for his work in preparing the schedules here considered, to the Board of Foreign Missions of the Presbyterian Church, U. S. A., for the use of the room used for the meeting, and to Dr. Gilbert Darlington, Dr. B. H. Beckhart, Dr. William P. Schell, and Mr. George A. Huggins for their stimulating contributions to the program.

#### RESOLUTIONS COMMITTEE:

Dr. Frank J. Scribner—*Chairman*

Mr. C. N. Wonacott

Mr. W. H. Cramblet

Mr. W. J. Elliott

Recommendations III and IV were considered first and were passed unanimously.

Following this action there was a general discussion of Recommendation I, and especially of paragraph (a). During this discussion, in order to test the general sentiment of the Conference, it was *moved* and *seconded*: Resolved, that the Conference recommends that no change of rates be made at this time but that the whole matter of rates be referred back to the Committee on Annuities for further study.

After discussion of this motion it was *agreed* that a vote on the motion be taken as individuals and not by organizations. A standing vote was then called for and the motion to make no change of rates but to refer back to the Committee was carried by a vote of 23 in favor and 19 opposed.

The Chairman then asked the Conference to discuss further the first two recommendations of the Committee on Resolutions for its guidance in making a further study of the matter of rates, and the following actions were taken:

1. That no matter what rates were ultimately adopted the residuum should be not less than 50 per cent.
2. After a discussion of the rate of interest to be used in determining rates, it was *decided* to refer this matter to the Committee for consideration.
3. To favor a Loading of 5 per cent to cover the expense of handling and promoting annuity gifts.
4. To favor modification of rates at the older and younger ages, as proposed by the tables presented by Mr. Huggins.
5. To favor no differential between male and female lives. In this connection three alternatives were put before the Conference and the vote was as follows:
  - (a) No differential ..... 16
  - (b) Three-year differential .. 5
  - (c) Five-year differential ... 2
6. To publish the Report of this Conference, the same to sell for \$1.00. This was done on the basis that the papers presented are of value to all interested in annuities and that the printing of the proposed rates is the best way to have the proposals studied.

After the benediction, the Conference was adjourned.

GEORGE F. SUTHERLAND  
Secretary, Committee on Annuities.

## LIST OF THOSE WHO ATTENDED THE EIGHTH CONFERENCE ON ANNUITIES—APRIL 10, 1946

(\*List of those who registered but could not attend)

Organization	Represented by
American Baptist Foreign Missionary Society, New York City.	Dewey F. DeTrude H. E. Hinton *Forrest Smith
American Baptist Home Missionary Society, New York City.	S. E. Hening *H. Kummann
American Bible Society, New York City.	Gilbert Darlington Rome A. Betts William A. Plain Charles W. Baas Miss Anne M. Greene
American Board of Commissioners for Foreign Missions, Boston.	Frederick A. Gaskins Ralph R. Shrader
American Lutheran Church, Columbus, O.	H. C. Osterman
American Society for the Prevention of Cruelty to Animals, New York City.	*Sydney Coleman
American Sunday School Union, Philadelphia.	*John H. Talley
American Tract Society, New York City.	Arthur W. Cobbett Howell E. Hammer
Annuity Fund for Congregational Ministers, New York City.	Frank J. Scribner William F. Frazier Miss E. K. Robins Miss Marion Ferguson Mrs. Alma K. Quimby
Asbury Methodist Home for the Aged, Gaithersburg, Md.	Herman M. Wilson H. G. Miller W. H. Cramblett
Bethany College, Bethany, W. Va.	
Board of Conference Claimants—New England Annual Conference Methodist Church, Boston.	*George E. Heath
Board of Foreign Missions of the Presbyterian Church in the U. S. A., New York City.	William P. Schell D. M. Pattison Howard B. Vail C. A. Suite
Board of Foreign Missions—United Lutheran Church in America, New York City.	Ernest T. Proffen
Board of Ministerial Pensions and Relief of the United Presbyterian Church, Philadelphia.	*C. L. Hussey
Board of National Missions of the Presbyterian Church in the U. S. of A., New York City.	C. N. Wonacott L. H. Tribus Walter Schoggen J. A. Griff Miss M. J. Hoym Miss H. P. Wendell

Organization	Represented by
Catholic Foreign Missionary Society of America, Maryknoll, N. Y.	*Thomas Kiernan
Christian and Missionary Alliance, New York City.	W. T. Christie
Church of the Brethren—General Missionary Board, Elgin, Ill.	H. Spenser Minnich
Church Extension and Home Missions of the Church of God, Anderson, Ind.	*E. S. Adcock
Church of the United Brethren in Christ, Dayton.	Wesley O. Clark
Columbia University, New York City.	B. H. Beckhart
Division of Home Missions and Church Extension of the Board of Missions and Church Extension—Methodist Church, Philadelphia.	W. J. Elliott F. H. Parks
Division of Foreign Missions, Methodist Church, New York City.	George F. Sutherland Albert E. Beebe Kenneth MacKenzie
Drew University, Madison, N. J.	H. M. Benjamin
Evangelical and Reformed Church, Philadelphia.	William E. Lampe
Executive Comm. of Christian Education and Ministerial Relief, Presbyterian Church in the U. S., Louisville, Ky.	H. Allan Scott
Executive Comm. of Foreign Missions of the Presbyterian Church in the U. S., Nashville, Tenn.	Curry B. Hearn
Fackler & Company, New York City.	Edward B. Fackler
Federal Council of the Churches of Christ in America, New York City.	Samuel McC. Cavert
General Board—Church of the Nazarene, Kansas City, Mo.	John Stockton
General Commission on World Service and Finance of the Methodist Church, Chicago.	Thomas A. Lugg
General Conference of Seventh Day Adventists, Washington, D. C.	W. E. Nelson James F. Cummins
General Council—Presbyterian Church, U. S. A., New York City.	*D. Allan Locke
The Golden Rule Foundation, New York City.	H. G. Hillier C. V. Vickrey Alan C. Vedder
Huggins & Company (Actuaries), Philadelphia.	George A. Huggins William M. Huggins
International Committee of Y. M. C. A.'s, New York City.	W. E. Dietz
The John Price Jones Corp., New York City.	Mrs. C. Thompson
Lutheran Board of Pensions and Relief, Philadelphia.	Harry Hodges
Lutheran Church (Missouri Synod), New York City.	Louis Henze
Massachusetts Society for Prevention of Cruelty to Animals, Boston, Mass.	*Albert Pollard

Organization	Represented by
Ministerial Pension Committee—United Brethren Church, York, Pa.	George A. Heiss
Ministers and Missionaries Benefit Board of the Northern Baptist Convention, New York City.	*M. R. Cary F. L. Taylor
National Recreation Association, New York City.	J. D. Robins, Jr.
National Woman's Christian Temperance Union, Evanston, Illinois.	Mrs. M. C. Munns
New York Bible Society, New York City.	*Millard L. Robinson *Miss J. Landes
The Penn School, Brooklyn, N. Y.	*Mrs. B. C. Rush
Presbyterian Board of Christian Education, Philadelphia.	Miss Nellie W. Harbison
The Salvation Army, New York City.	*Brigadier G. B. Abrams
Save the Children Federation, New York City.	William G. Schram
Society of the United Brethren for Propagation of the Gospel among Heathens, Bethlehem, Pa.	William G. Miller
Syracuse University, Syracuse, N. Y.	George E. Van Dyke
United Church of Canada (Board of Pensions), Toronto.	W. W. Burnett
United Presbyterian Board of Foreign Missions, Philadelphia.	R. W. Caldwell
Vassar College, Poughkeepsie, N. Y.	George T. Welch
Wells College, Aurora, N. Y.	J. H. Bentley
Woman's American Baptist Foreign Missions, New York City.	Miss Annie E. Root
Woman's American Baptist Foreign Missions, South Orange, N. J.	Mrs. George W. Doane
Woman's American Baptist Home Mission Society, New York City.	Miss Edna R. Howe
Woman's Division of Christian Service of the Board of Missions and Church Extension of the Methodist Church, New York City.	Miss Henrietta Gibson Mrs. Alice Williams
Woodward, Ryan, Sharp & Davis (Actuaries). New York City.	Jonathan G. Sharp
Y. M. C. A. of the City of New York.	Clifford W. Pettit *Edward Arnoldi
Y. M. C. A. Retirement Fund, New York City.	Earl W. Brandenburg



