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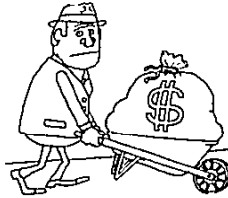
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What is Insurance?

"Each man may subject himself to a small deprivation, in order that no man may be subjected to a great loss." This graceful definition of insurance was uttered in England's House of Commons in 1825 and hasn't been improved upon since. Although the insurance business has grown greatly in size and complexity, the basic principle remains the same: a group of people contribute small sums to create a pool of money. The few contributors stricken by disaster receive payments from the money pool to compensate them, at least partly, for their loss.

The need for insurance seems to be almost instinctive in man. In pre-historic hunting tribes, the hunter who bagged a deer shared it with those who didn't. He knew that inevitably the day would come when he would return empty handed and need to share the bag of a luckier neighbor. This communal sharing of food was a way of spreading risk, and that is what insurance is all about -- transferring risk. Among the primitive hunters, the risk of going hungry was transferred from the unlucky individual to the whole tribe.

By the dawn of written history, insurance had become pretty sophisticated. The Babylonians had a system whereby a trader who organized a caravan could relieve himself of the risk of being robbed. The trader had made a loan in the first place to buy the goods for his venture. And, even as today, he would pay interest on the loan. But for an additional sum, the money-lender would agree to cancel the loan in the event that the trader lost his goods to bandits. This transferred the risk of loss from the trader to the money-lender.

The Phoenicians, Greeks, Romans and Hindus all had similar insurance systems to cover the movement of goods by both land and sea.

Indeed, the history of insurance is almost the history of civilization. As new needs were recognized, someone quickly figured out a way to cover them with insurance. The first fire insurance office was opened in London shortly after the Great Fire of 1666. No doubt fire insurance sold well then.

In 1896, there were four automobiles in the U.S. Two of them were in St. Louis, Mo. You guessed it -- the two St. Louis motorists managed to run into each other. Someone saw the handwriting on the wall and two years later the first auto insurance was issued.

The first accident policy in the United States was issued in 1863 to one James Bolton of Hartford, Conn. It covered Mr. Bolton during the two-block stroll from his home to the postoffice. The premium was 2 cents.

Today, insurance has been refined and expanded in ways that would have dazzled those traders of ancient Babylon. The money pools are created

and managed by large insurance companies which actively solicit business. And these companies intend to make a profit, both by investing the funds in the money pool and by seeing to it that their income from premiums is greater than their outgo in claims.

Today you can insure your TV tube, your jewelry, your little finger your crops against hail, your parade against rain. Several decades ago, Actress Betty Grable made headlines when she insured her then-spectacular legs for a million dollars.

Many golfers carry hole-in-one insurance against the day when the impossible happens and their tee shot finds its way into the cup on a distant green. The insurance pays for the traditional drinks-for-everybody that the lucky golfer is obliged to buy in the clubhouse after the game.

Some of those early Babylonian insurance men no doubt took a terrible financial licking. Having an entire caravan wiped out by bandits could well have wiped out the insurer too.

In Colonial America, the first mutual fire insurance company, the Friendly Society of Charleston, S.C., founded in 1735, went broke in 1740 when one of its members was the victim of a bad fire. Such was the fate of many early insurance companies.

Today, the spreading of risk by insurers is a fine art with little chance for the miscalculation that bankrupted Charleston's Friendly Society. Modern insurance companies have honed the mathematics of the business to a point that almost nothing unexpected happens.

All insurance is based on two mathematical propositions: (1) The law of probability and (2) the theory of large numbers.

Nearly everyone is acquainted with the law of probability. It says that when you flip a coin you will get heads half the time and tails half the time, or that of the cars you meet on the road, one in 10 will have a license plate ending with two identical numbers.

The theory of large numbers says that the more times you flip the coin or the more cars you look at, the more accurate the law of probability becomes. If you flip the coin 10 times, you may get seven heads and three tails, far from a 50-50 ratio. But if you flip it 10,000 times you cannot avoid coming very close to a 50-50 ratio.

So it is with insurance. Insurance actuaries know that out of 1,000 homes, a certain number will be damaged each year by fire. Furthermore, they know pretty closely the amount of damage that will be done. It may be that of the 1,000 homes in your neighborhood, none of them will be damaged by fire. But the theory of large numbers says that if enough homes are included - 10,000, 100,000 or a million - then the insurance

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