Key Drivers for Mutualization: Comparison between Japan and the U.S./Canada

Tatsuo Kurogi
Nagoya University of Commerce & Business

Abstract

Thirteen stock life insurers in Japan underwent mutualization consecutively in the postwar years of 1947-1948. The observed key drivers of these insurers' mutualization include dissolving Japanese conglomerates, management succession, and confrontation against labor unions. Comparative analysis between Japan and the U.S./Canada reveals that the key drivers for mutualization significantly differed by region, comprising several local- and event-driven factors, unlike those for demutualization.

1. Introduction

A mutual company is a unique corporate organization, which had been typically observed in the life insurance industry. Despite the reduced number of mutual life insurers at present, because of the global trend of demutualization [converting from a mutual life insurance to a stock life insurance company], there were many decades when they had enjoyed a very significant presence in their local life insurance markets, notably in Japan and the U.S./Canada.

Prior to the demutualization phenomenon, it was quite usual to find many mutual insurers in the top rankings of the Japanese and the U.S./Canadian life insurance markets, as seen in Table 1. In addition to the large volume of their business, they also tended to have a quite long history of operation in their domestic market. Given their markets' overwhelming presence in the world life insurance business [the combined world market share of Japan and the U.S./Canada was close to 70% in 1985 as seen in Table 2] at that time, it is reasonable to say that mutual organizations played a very important role in developing the life insurance business in the 20th century. Furthermore, it is quite noteworthy that many of these large mutual life insurers were originally established as stock life insurers at their inception, and after certain periods of operation, underwent the mutualization process to become mutual life insurers.

The purpose of this paper is to analyze the past mutualization that had once helped create an era of mutual insurers in the world's most developed life insurance markets of the 20th century, and to undertake a comparative analysis of the key drivers identified for life insurers' mutualization in Japan and the U.S./Canada.

Table 1: Life Premium Income Rankings in 1985

	U.S.A.		Premiums (US-$ mil)	Japan		Premiums (JPY mil)
1	Prudential of America	M	14,331	Nippon Life	M	3,293,144
2	Metropolitan Life	M	7,316	Dai-ichi Mutual Life	M	2,223,970
3	Travelers Ins.	S	4,270	Sumitomo Life	M	1,975,465
4	Connecticut General	S	3,922	Meiji Mutual Life	M	1,350,194
5	New York Life	M	3,830	Asahi Mutual Life	M	1,096,467
6	Atena Life	S	3,594	Mitsui Mutual Life	M	888,387
7	Bankers Life	S	3,031	Taiyo Mutual Life	M	845,674
8	TransAmerica L&A	S	2,595	Yasuda Mutual Life	M	743,100
9	Equitable Life	M	2,594	Toho Mutual Life	M	519,361
10	Massachusetts Mutual	M	2,420	Chiyoda Mutual Life	M	437,308

* M=mutual, S=stock, Japanese insurers' figures are from April 1985 to March 1986.
Source: National Underwriter (June 7, 1986), Insurance Seiho Tokeigou (1989)

Table 2: The World's Largest Countries by Life Premiums in 1985

	Country	Premiums in millions of national currency	Equivalent in millions of U.S. dollars	World share %
1	U.S.A.	114,026	114,026	39.80
2	Japan	15,646,188	78,035	27.24
3	Great Britain	15,081	21,857	7.63
4	W. Germany	44,737	18,186	6.35
5	France	71,088	9,403	3.28
6	Canada	11,096	7,926	2.77
7	South Korea	3,987,250	4,479	1.56
8	Switzerland	9,009	4,331	1.51
9	Netherlands	10,805	3,900	1.36
10	Sweden	22,658	2,973	1.04

Source: Sigma/Swiss Re 5-87, p14

2. Mutualization of Life Insurers in Japan

Mutualization of life insurers in Japan had only occurred during 1947-1948, when 13 stock life insurers converted themselves into mutual organizations, as part of the rehabilitation process from their insolvent financial status amid hyperinflation post-WWII. This resulted in 16 among the industry's total 20 domestic life insurers in postwar Japan becoming mutual, representing a substantial transformation from only three mutual players out of 20 prior to mutualization.

Mutualization of these 13 stock life insurers, however, did not follow a due process[1] [purchasing all outstanding shares from shareholders and cancelling them to become mutual] stipulated in the Insurance Business Law. Instead, they established new mutual life insurers, to which they made a

1 Kyoei Fire & Marine, a general insurer, is the only insurer ever in Japan to utilize the mutualization code of the Insurance Business Law. Kyoei was mutualized in April 1946.

comprehensive transfer of outstanding insurance policies after completing their rehabilitation process, such as a 100% capital reduction and cut-down of large insurance policies, under the Financial Institution Reconstruction Act. After the comprehensive transfer was completed, these stock life insurers liquidated themselves to leave new mutual life insurers succeeding entities. This kind of irregular approach was deployed since starting the postwar operation by newly established companies was believed to be more effective than that by previous companies who went through the rehabilitation process and suffered from damaged confidence of policyholders.

2.1. Dissolving Conglomerates

Kurogi (2014) argued that the key drivers observed for the Japanese life mutualization differ between insurers belonging to conglomerates, such as Mitsubishi, Mitsui, and Sumitomo, collectively called Zaibatsu, and others (Table 3). For seven Zaibatsu life insurers [Yasuda, Teikoku, Meiji, Nomura, Nissan, Mitsui, and Sumitomo], their mutualization was involuntary, and enforced by the GHQ/SCAP (General Headquarters, the Supreme Commander for the Allied Powers) that had a mission to dissolve Zaibatsu as part of Japan's economic democratization.

The U.S. government delegation, led by Northwestern University's anti-trust professor Corwin D. Edwards, made an intensive investigation on Japanese conglomerates during January-February 1946, and submitted a 221-page report titled "Report of the Mission on Japanese Combines"[2] in March 1946. As part of a series of measures to dissolve Japanese conglomerates or Zaibatsu groups, the Edwards report stated in Section 6 [Destroying Financial Favoritism] of Chapter VI [An Outline of Recommended Policy] that "The most practicable and expeditious manner in which to reconstitute insolvent insurance companies is to mutualize them by cutting back the face amount of outstanding policies. If this procedure were adopted, no problem of liquidating zaibatsu holdings in such companies would exist."

Table 3: Mutualized Japanese Life Insurers in the Postwar Period

Completion of Mutualization	Zaibatsu Insurers	Non-Zaibatsu Insurers
May 1947		Nippon
June 1947	Yasuda	
July 1947	Teikoku*, Meiji, Nomura*	Daido
August 1947	Nissan, Mitsui	
September 1947	Sumitomo	Daihyaku, Yamato
November 1947		Shin-Nihon*
February 1948		Taiyo

*Teikoku, Nomura and Shin-Nihon were later renamed to Asahi, Tokyo and Toho, respectively.
Source: Showa Seimeihoken Shiryo Vol. 5 [Life Insurance Association of Japan], p734-735

2 Department of State Publication 2628, Far Eastern Series 14.

The State-War-Navy Coordinating Committee [SWNCC] of the U.S. government later adopted most of the recommendations stated in the delegation report, by approving the amended SWNCC302/2 [Statement of U.S. Policy with respect to Excessive Concentrations of Economic Power in Japan] on April 29, 1947. Section 9 of the amended SWNCC302/2 states that "Zaibatsu insurance companies which are insolvent should be mutualized by cutting back the face amount of outstanding policies, where sufficient assets still exist to render this procedure practicable."

Thus, seven Zaibatsu life insurers, who were all insolvent in a substantial manner, were directed by GHQ/SCAP to undergo mutualization, by which a linkage between Zaibatsu life insurers and Zaibatsu holding companies through stock holdings was naturally lost. Apparently, mutualization was a very useful means for GHQ/SCAP to pursue its mission assigned to dissolve Zaibatsu, which is a symbol of excessive concentrations of economic power in Japan.

Unlike the aforementioned Zaibatsu life insurers, Zaibatsu general insurers, such as Tokio Marine & Fire[3] and Yasuda Fire & Marine, did not undergo mutualization at that time, since none of the Zaibatsu general insurers was insolvent.

2.2 Management Succession

Regarding six non-Zaibatsu life insurers [Nippon, Daido, Daihyaku, Yamato, Shin-Nihon and Taiyo], the key drivers for mutualization varied among the companies.

The top executives of any insurer who invested in the military-related industry during the war period were purged from public service by a GHQ/SCAP directive, which also prohibited a relative, by affinity within the third degree of the purged, to succeed and assume the same position. In case of Nippon Life, which was the largest life insurer and also the first life insurer to be mutualized, the former president Toru Naruse was purged from public service. Therefore, his younger brother Gen Hirose, who married into the family of Nippon's founder Hirose's bride, could not have succeeded to the same position of president due to the restriction mentioned earlier. GHQ/SCAP, however, considered a mutual insurer to be more democratic than a stock insurer, since the former is legally owned by its policyholders. Therefore, GHQ/SCAP exceptionally allowed a relative of the purged to assume the top management position at a mutualized insurer (Kurogi, 2015a).

On the other hand, GHQ/SCAP did not allow a major stockowner to continue in the top management of the recapitalized stock life insurer, from the perspective of promoting Japanese economic democratization. This presented the major shareholding top management with a choice of ownership or management. In case of Itaya Life, which was non-Zaibatsu and the sole life insurer to establish a new stock life insurer instead of mutual in the rehabilitation process, president Miyakichi Itaya was not allowed to continue in the top management of the new company while he maintained its ownership with less than 10% shareholding, severely reduced from over 80% shareholding in the previous company. Unlike Itaya, those who chose management embraced mutualization. Apparently,

[3] Tokio Marine & Fire and Meiji Life both belonged to Mitsubishi Zaibatsu.

mutualization was an effective solution, especially for the family-owned insurer to succeed management within the family, at the cost of losing ownership (Kurogi, 2015b).

Table 4: Management Succession at Mutualized Non-Zaibatsu Life Insurers

	Old Stock Company	New Mutual Company
Nippon Life	Suketaro Hirose (1928-1936) Toru Naruse (1937-1946)	Gen Hirose (1948-1982)
Daido Life	Keizo Hirooka (1909-1942) Masanao Hirooka (1942-1948)	Matsusaburo Hirooka (1947-1953)
Daihyaku Life	Hajime Kawasaki (1921-1929) Kineo Kawasaki (1929-1946) Shinpei Saito (1947-1948)	Yoshinari Kawai (1947-1954, chairman 1954-1963) Shinpei Saito (1954-1965) Daijiro Kawasaki (1965-1973) Minoru Kawasaki (1973-1987)
Shin-Nihon Life [renamed to Toho Life]	Seizo Ota (1909-1936) Shinkichi Ota (1936-1948)	Shinkichi Ota (1947-1961) Benjiro Ota (1961-1977) Shintaro Ota (1977-1995)
Taiyo Life	Seizaburo Nishiwaki (1911-1948)	Seizaburo Nishiwaki (chairman 1948-1962) Kyojiro Nishiwaki (1978-1990)

*Old stock companies mentioned above were liquidated upon the completion of comprehensive transfer of outstanding policies to new mutual companies in March 1948. Years in parentheses indicate a period of presidency unless otherwise mentioned. Nippon Life's president position was vacant in 1947. Yamato Life was excluded from the above list due to insufficient information.

2.3. Confrontation against Labor Unions

With the support of GHQ/SCAP's policy to promote Japanese economic democratization, labor unions were organized successively across all company levels in postwar Japan. GHQ/SCAP also demanded that additional stock issuance in the rehabilitation process of insolvent stock life insurers should be widely allocated, including their employees. For an insurer whose management and labor union were mutually hostile, additional stock issuance in lieu of GHQ/SCAP's policy presented a threat for the management to weaken or even lose its power because of an increased stock ownership by the employees or the labor union. Instead, mutualization was adopted by such a company to avoid the confrontational situation and sustain its management's safety (Kurogi, 2015a, 2015b).

Regarding a mutually hostile situation, for example, it is well known that Nippon Life's management faced the life insurance industry's first strike by its company union from April to July 1946. In addition, the company union of Daihyaku Life demanded to weaken or even eliminate the involvement of the founder Kawasaki's family in the company's rehabilitation process. The presidential appointment of Yoshinari Kawai, who did not bear the Kawasaki name but was related to the Kawasaki family, for mutualized Daihyaku Life, reflected the family's wariness of the union's repellence (Table 4).

2.4. Policyholder Interests

Out of these six non-Zaibatsu life insurers mentioned above, Daido Life had a certain possibility to be motivated by policyholder interests for the adoption of mutualization. Although Matsusaburo Hirooka from Daido's founder family succeeded to the position of president of the mutualized Daido, his tenure was as short as six years (Table 4). None of the Hirooka family members had stayed in the management since Matsusaburo's resignation. Therefore, management succession by the Hirooka family is considered an unlikely motivation for mutualization in case of Daido. In addition, there is no evidence of confrontation against its labor union.

In the prewar life insurance market of Japan, Daido was one of the few stock life insurers, which were comparable to mutual life insurers, such as Dai-ichi Mutual and Chiyoda Mutual, in terms of providing life insurance products [mainly endowment policies in those days] for policyholders at a net cost[4] as low as possible. Additionally, shareholder dividends had been kept at a very low level over decades since its inception, while almost all shares of Daido were held by the Hirooka family and related parties. In other words, Daido was a quasi-mutual life insurer in prewar Japan, in a sense that it emphasized upon policyholder interests with lowest cost of insurance products by limiting shareholder economic interests. As such, it is possible to state that Daido's adoption of mutualization in postwar Japan was a natural consequence under the circumstances of national economic democratization.

3. Comparison of Life Mutualization between Japan and the U.S./Canada

3.1. Mutualization of Life insurers in the U.S./Canada

Unlike the case of Japan as observed earlier, the number of mutual life insurers in the U.S. had historically been exceeded by that of stock life insurers (Table 5). Typical characteristics of U.S. mutual life insures include a large company size and a long history of operation.

Fletcher (1966) undertook a comprehensive analysis of the motivations underlying the mutualization of 26 life insurers in the U.S./Canada, indicating the following observed motivations.

(1) *Adverse Public Opinion*: An unfavorable public image of stock life insurers that mounted after the 1905 Armstrong Investigation of New York State prompted stock life insurers in the state to mutualize, under the revised New York State Insurance Law to accommodate the mutualization procedure.

(2) *Federal Estate Tax Problems*: Shareholders of stock life insurers that had a profile of closely held stock, successful operation, and control by the founder, were concerned about a future burden of federal estate tax upon their death. To avoid the risk of an excessive tax valuation on

4 Insurance premiums net of policyholder dividends. In prewar Japan, even stock life insurers were mainly selling participating policies since policyholder dividend was considered one of the attractive characteristics of endowment policies by prospective customers.

the unlisted stock or a low yield from the forced sale of the stock and so forth, the shareholders mutualized their companies.

(3) *Forestalling outside Control*: Mutualization was adopted to prevent the transfer of control of the company to outside interests, including foreign investors in case of Canada.

(4) *Operational Difficulties*: Stock life insurers that encountered problems of financial crisis, management-shareholder conflict, internal shareholder dissention, or change of state law relating to taxation of insurance companies, chose to mutualize.

Table 5: Number of the U. S. Life Insurers in Business at Year-End 1985

Year of Commenced Business	Stock	Mutual	Total
1875 and Prior	8	23	31
1876 – 1925	94	30	124
1926 – 1950	156	38	194
1951 – 1960	319	18	337
1961 – 1970	397	13	410
1971 – 1980	509	4	513
1981 – 1985	650	2	652
Total	2,133	128	2,261

Source: Life Insurance Fact Book Update 1987 [ACLI], p43

Gold (1975) added (5) *Slump of the Stock Prices*, to Fletcher (1966)'s observations, arguing that shareholders of stock life insurers tried to raise the stock price by utilizing mutualization.

Mayers and Smith (1986) supported Gold's view [*Slump of the Stock Prices*] by analyzing stock price variations of 30 mutualized life insurers in the U.S./Canada. On the other hand, Mayers and Smith (1986) argued against Fletcher (1966)'s first mutualization motivation (1) *Adverse Public Opinion*, pointing out that there was an eight-year gap between Metropolitan Life's announcement of mutualization in 1914, and the 1906 revision of the New York State Insurance Law to accommodate mutualization as a result of the Armstrong Investigation amid the fervent public criticism of the insurance industry. Mayers and Smith (1986) also highlighted (6) *Involuntary Mutualization*, by arguing that involvement of state insurance commissioners was detected in the case of mutualization of four life insurers among 30.

3.2 Comparison between Japan and U.S./Canada

One common fundamental motivation underlying the mutualization of stock life insurers in both Japan and the U.S./Canada is the management's fear of losing control of the company. In case of Japan, the postwar economic democratization policy of GHQ/SCAP as well as the energized labor unions presented a threat to the management, while in the U.S./Canada, the management feared losing control of the company to non-company interests, including foreign investors.

Another common factor is that involuntary mutualization existed in both Japan and the U.S./Canada. Zaibatsu stock life insurers of Japan were forced by GHQ/SCAP to mutualize for dissolving conglomerates. Mayers and Smith (1986) observed the involvement of state insurance commissioners in the mutualization of four life insurers as mentioned earlier.

In spite of the factors mentioned above, however, it is fair to say that motivations of mutualization reflected some local- and event-driven factors, such as GHQ/SCAP, the Armstrong Investigation, tax code change, and so forth. This makes it more difficult to generalize motivations than to recognize differences and variations in motivations of life insurer mutualization. As Mayers and Smith (1986) argued that the rate of mutualization has not been uniform over time, Japanese life mutualization only occurred during 1947-1948, and has never happened since then.

4. Concluding Remarks

Mutual organizations played a significant role in developing the life insurance business in both Japan and the U.S./Canada. Many of their mutual life insurers were originally established as stock life insurers at their inception, and after certain periods of operation, underwent the mutualization process to become mutual life insurers.

Unlike motivations of the recent demutualization, such as access to capital markets and reduction of agency costs (Cole et al.,1995, Carson et al.,1998), key drivers for mutualization of life insurers significantly differed by region, comprising several local factors, as observed above. It is also a noteworthy observation that policyholders' interests had very rarely been primary motivations in most cases of mutualization, although policyholders, by theory, are regarded as the sole owners of a mutual life insurer.

Finally, research on the past mutualization can add more value to the analysis of the recent demutualization trend observed in the insurance industry across the world, because several of these insurers who demutualized recently also had a history of mutualization in the past. A more in-depth analysis is expected in the future focusing on themes such as why the same life insurer underwent mutualization and then demutualization in its long history of operation.

References

Anderson, Buist M. (1973) "Policyholder Control of a Mutual Life Insurance Company", *Cleveland State Law Review*, Vo. 22, pp. 439-449

Carson, James M., Mark D. Foster and Michael J. McNamara (1998) "Changes in Ownership Structure: Theory and Evidence from Life Insurer Demutualization", *Journal of Insurance Issues*, Vol. 21(1), pp.1-22

Cole, C. Steven, Michael J. McNamara and Brenda P. Wells (1995) "Demutualization and Free Cash Flow", Journal of Insurance Issues, Vol.17 (1), pp.37-56
Dawson, Miles M. (1917) "Mutualization of Life Insurance Companies", *The Annals of the American Academy of Political and Social Science*, Vol. 70, pp.62–76
Fletcher, Linda P. (1966) "Motivations Underlying the Mutualization of Stock Life Insurance Companies", *Journal of Risk and Insurance*, Vol. 33(1), pp.19–32
Gold, Melvin L. (1975) "On the Mutualization of a Stock Life Insurance Company", *Transactions of Society of Actuaries*, Vol. 27, pp.509–518
Hansman, Henry (1985) "The Organization of Insurance Companies: Mutual versus Stock", *Journal of Law, Economics, and Organization*, Vol.1, pp.125-153
Hetherington, J.A.C. (1969) "Fact v. Fiction: Who Owns Mutual Insurance Companies", *Wisconsin Law Review*, Vol. 4, pp. 1068-1103
Kurogi, T. (2014) "Postwar Mutualization of Zaibatsu Life Insurers: Verification of the GHQ Instruction Hypothesis", *Journal of Insurance Science*, No.624, pp.103–122 (Japanese only)
Kurogi T. (2015a) "Nippon Life's Postwar Mutualization, based primarily on Oral History Analysis of Fujimoto's Dialogue", *Journal of Insurance Science*, No.628, pp. 139-157 (Japanese only)
Kurogi T. (2015b) "Separation of Ownership and Management in the Postwar Rehabilitation of Japanese Life Insurers", *NUCB Journal of Economics and Information Science*, Vol.60 (2), forthcoming (Japanese only)
MacMinn, Richard, and Yayuan Ren (2011) "Mutual versus Stock Insurers: A Synthesis of Theoretical and Empirical Research", Journal of Insurance Issues, Vol. 34(2), pp. 101-111
Mayers, David, and Clifford Smith, Jr. (1986) "Ownership Structure and Control: The Mutualization of Stock Life Insurance Company", *Journal of Financial Economics*, Vol. 16, pp.73–98