

2010

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### Recommended Citation

Kent McKeever, *A Short History of Tontines*, 15 Fordham J. Corp. & Fin. L. 491 (2009).  
Available at: <https://ir.lawnet.fordham.edu/jcfl/vol15/iss2/5>

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## A SHORT HISTORY OF TONTINES

*Kent McKeever*<sup>1</sup>

“ . . . [T]he tontine is perhaps the most discredited financial instrument in history.”<sup>2</sup>

A tontine is an investment scheme through which shareholders derive some form of profit or benefit while they are living, but the value of each share devolves to the other participants and not the shareholder's heirs on the death of each shareholder. The tontine is usually brought to an end through a dissolution and distribution of assets to the living shareholders when the number of shareholders reaches an agreed small number.<sup>3</sup>

If people know about tontines at all, they tend to visualize the most extreme form – a joint investment whose heritable ownership ends up with the last living shareholder. The all or nothing nature of that form is memorable. The last survivor principle has been the basis for a number of dramatic works whose plots hang on the machinations of a tontine participant to murder his co-investors to insure the core property reverts to him.<sup>4</sup> In fact, tontines are far more innocuous and served as an

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1. Director, Diamond Law Library, Columbia Law School.

2. Edward Chancellor, *Live Long and Prosper*, SPECTATOR, Mar. 24, 2001, at 14.

3. The primary definition of “tontine” in the *Oxford English Dictionary* reads: “A financial scheme by which the subscribers to a loan or common fund receive each an annuity during his life, which increases as their number is diminished by death, till the last survivor enjoys the whole income; also applied to the share or right of each subscriber.” THE OXFORD ENGLISH DICTIONARY 231 (2d ed., vol. XVIII 1989). The tontine was “[i]ntroduced first in France as a method of raising government loans. Afterwards[,] tontines were formed for building houses, hotels, baths, etc.” *Id.*

4. The most widely-known, if now rarely read, tontine-based stories include Robert Louis Stevenson's novel *The Wrong Box* (1889), Henry Hawley Smart's *The Great Tontine* (1882), and Thomas Costain's *The Tontine* (1955). *The Wrong Box* was made into a movie, directed by Bryan Forbes with a screenplay by Larry Gelbart and Burt Shevelove et al., that is widely perceived to be an improvement on the novel. See THE WRONG BOX (Salamander Film Productions 1966). A more recent exploration of the idea can be found in a 1996 episode of “The Simpsons” based on a group of old soldiers, looted art work, and a tontine. *The Simpsons: Raging Abe Simpson and His Grumbling Grandson in “The Curse of the Flying Hellfish”* (FOX television broadcast

important step both in developing modern insurance plans and providing some of the earliest reliable actuarial data on which the later insurance plans could be developed.

Since tontines have been neglected for many years, this Essay is primarily concerned with providing background information. It covers the history of their development and the broad variety of uses they have served from the 17th to the early 20th centuries. It concludes with a brief exploration of the revival of the tontine as a possible addition to the range of modern financial tools.

### EARLY HISTORY

The word 'tontine' is derived from the name of Lorenzo de Tonti, an Italian political exile living in France. He proposed the original tontine to Jules Cardinal Mazarin in the early 1650's as a means for French King Louis XIV to raise revenue. The French treasury, battered by the Thirty Years War and the rebellions within France known as the 'Fronde,' needed to raise money.<sup>5</sup> The tontine scheme reputedly evolved from similar offerings in Italy, albeit on a smaller scale, to raise income from a broad spectrum of the population.<sup>6</sup>

As envisioned by de Tonti, tontine subscribers would buy a special kind of annuity at 300 *livres* a share. Investors could name a third party, often referred to as the nominee, as the life in interest for their stake in the tontine. Participation was structured in groups of equal size according to the age of the nominees: e.g. 0 to 7, 8 to 14, all the way through the age of 63.<sup>7</sup> Each beneficiary was to receive an annual payment based on the interest earned by the combined initial capital contributed of investors in the applicable age cohort. The rate of interest increased with the age of the nominee. As nominees died, the share related to that nominee became worthless and the payments based on each of other surviving nominees would increase. The subscriber

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Apr. 28, 1996); see also Season Seven, The Simpsons Archive: Episode Guide, <http://www.snpp.com/episodeguide/season7.html>.

5. ROBERT M. JENNINGS & ANDREW P. TROUT, THE TONTINE: FROM THE REIGN OF LOUIS XIV TO THE FRENCH REVOLUTIONARY ERA 4 (1982). Cardinal Mazarin seems to have been de Tonti's patron in the Neapolitan fracas and put de Tonti on a pension list in Paris afterword. *Id.* at 5.

6. *Id.* at 8-9.

7. As later tontines took off, many subscribers participated in the name and age group of their children. *Id.* at 6.

represented by the last nominee in each group would get all the interest generated by the capital within that band. On the death of the last subscriber, the capital would revert to the government.<sup>8</sup>

Neither de Tonti's original 1653 proposal nor a Danish proposal of the same year ever got off the ground.<sup>9</sup> The first operating tontine was established by the city of Kampen in Holland in October, 1670. The cities of Amsterdam and Groningen followed within the same year.<sup>10</sup> There were almost 200 local Dutch tontines offered by 1700. City-States in a still un-unified Germany followed suit.<sup>11</sup>

While de Tonti's original proposal had royal support, it was not registered by the *Parlement of Paris*, a court-like institution, which had the effect of killing the proposal.<sup>12</sup> Undeterred, de Tonti continued to press his tontine idea and various other grand schemes such as a national lottery. At some point, de Tonti offended someone in power. French Finance Minister Jean-Baptiste Colbert, the successor to Mazarin as de facto Prime Minister of France, possibly issued the 1668 royal warrant which sent de Tonti to the Bastille. He remained there until he was released in 1675.<sup>13</sup> Unfortunately, de Tonti died around 1684, five years before the first French national tontine was finally created in 1689.<sup>14</sup> An additional nine French national tontines were created at irregular intervals through 1759. The later French tontines tended to be fully

8. See *id.* at 6.

9. One author, Wagenvoort, has uncovered indirect connections between de Tonti and Klingenberg, the Danish Postmaster General who proposed the tontine in Denmark. See HERMAN WAGENVOORT, *TONTINES, AN EXAMINATION INTO THE HISTORY OF TONTINE ANNUITIES AND CONTRACTS OF SURVIVAL IN THE REPUBLIC OF THE UNITED PROVINCES* (1961).

10. *Id.* at 12-13.

11. In a delightful double gamble, the concepts of tontine and lottery were combined in Hamburg. In 1776, the city offered an annual lottery whose prizes were tontine annuities. The first and second prizes were simple life annuities, but the multiple lesser prizes, encompassing 148 other shares, took the form of small tontine groups. The prospectus for this was found in the Staatsarchiv Hamburg: K ammerei I, July 12, 1776, no. 86 (F.R.G.). See also Victor Enthoven, *Hamburg and Its Finances: Citizens, Debts and Public Credit* (2006), available at <http://www.helsinki.fi/iehc2006/papers1/Enthoven.pdf> (summary of paper given at the Fourteenth International Economic History Congress in 2006).

12. See JENNINGS & TROUT, *supra* note 6, at 8. For a short description of the nature of the Parlement de Paris, see James Beardsley, *Constitutional Review in France*, in 1975 SUPREME COURT REVIEW 189, 191 (Philip B. Kurland ed., 1976).

13. See JENNINGS & TROUT, *supra* note 6, at 9-12.

14. *Id.* at 12, 16.

subscribed.<sup>15</sup>

The British experiment with tontines, in contrast to France, was rockier. The English established seven tontines between 1693 and 1789.<sup>16</sup> One tontine offering, in 1757, was cancelled due to a lack of subscriptions.<sup>17</sup> Ultimately, only the three tontines established by the Irish parliament, in 1773, 1775, and 1777, were fully subscribed. Even the tontine initiated in 1777 was not completely 'issued' until 1781.<sup>18</sup>

The later European national tontines appealed to speculators, who formed syndicates in attempts to make the payouts last as long as possible for the participants. Geneva, in particular, was the site of ingenious schemes by investors who paid much more attention to the life-expectancies of nominees than the tontine issuing governments of France or the United Kingdom. One group of Genevan speculators formed investment 'clubs' for the 1777 Irish Tontine and sought out the guidance of a doctor who helped the investors identify a number of local families with particularly long life expectancies. The Genevan clubs invested £50,000 in the issue. The fate of the clubs' investment was tied to the life expectancies of 50 girls, ranging in age from three to seven years old, identified by the doctor. The overall tontine offering was comprised of three classes of nominees: those under twenty years old, twenty to forty, and forty and above. Forty years later, 64 percent of the youngest group of Genevan women were still alive, compared to only 42 percent of the under-twenty class for the tontine at large.<sup>19</sup>

A number of people nominated the life of King George the Third in the last English Tontine, in 1789. Although there may have been patriotic motives, the nomination of a public figure would make

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15. *Id.* at 46-47.

16. *See id.* at 33-37.

17. David R. Weir, *Tontines, Public Finance, and Revolution in France and England, 1688-1789*, 49 J. ECON. HIST. 95, 105 (1989).

18. *See* W.A. THOMAS, *THE STOCK EXCHANGES OF IRELAND 20-24* (1986) (summarizing the offering and administration of the Irish Tontines).

19. The Genevan approach to the "Irish" tontine is described in Jennings and Trout's *The Tontine*. *See* JENNINGS & TROUT, *supra* note 6, at 61-63. It involved the same strategy but a different pool of "demoiselles" from the group involved in French tontines known as the "immortals." *See* MICHAEL RAPPORT, *NATIONALITY AND CITIZENSHIP IN REVOLUTIONARY FRANCE* 123 (2000). For a short general survey including an assessment of the Swiss strategies, see Casey G. Rothschild, *Adverse Selection in Public Finance: Life-Contingent Contracts in Early Modern Europe* (M.I.T. Dep't of Econ., 2003), available at <http://stuff.mit.edu/afs/athena/course/14/14.731/papers/adverse.pdf>.

administering the tontine comparatively easy. Although he was already 51 at the issuance of the tontine, George lived until 1820 and proved to be a good investment among the oldest class of nominees.<sup>20</sup> On the other hand, Marie Antoinette's life was one of those nominated in the 1777 Irish Tontine.<sup>21</sup>

A tontine was also one of the options proposed by U.S. Treasury Secretary Alexander Hamilton as a means to reduce the national debt at the beginning of the American Republic.<sup>22</sup> Hamilton's tontine was roughly modeled on the 1789 British version and incorporated an unusual payout structure which froze investor payments to the final beneficiaries at the level reached when the survivor pool was reduced to 20 percent of the original group. These beneficiaries would still receive a dividend, but it would no longer increase as their co-beneficiaries died off. Hamilton's tontine proposal, one of several elements of a multi-pronged approach to tackling America's financial problems, was ignored by Congress.

The administration of tontines was a headache in a quill and paper environment. Documentation of identity and death was a constant problem in a world where records of such information were non-standard and scattered. Forgery of documents, intended to maintain the flow of income to the agents of a dead person, was a common problem. An abstract of an Irish parliamentary document from 1812 hints at some of the problems encountered by Irish tontine administrators:

"[T]here is evidence that many annuity owners are surprised that dividends have not advanced as expected in proportion to the general opinion of the probabilities of death of nominees. The committee finds that mismanagement has arisen. It argues that life probabilities are greater than supposed when the annuities were issued. Proposals to improve the system include finding out whether certain nominees are alive or dead, ensuring that foreign nominees complete forms correctly, and compelling forfeiture if no claim has been made for three years. Regular accounts should be kept at the tontine office."<sup>23</sup>

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20. See CHARLES COMPTON, *A TREATISE ON TONTINE* 12 (London, Effingham Wilson 1833).

21. NATHANIEL CLEMENTS, *A LIST OF THE PERSONS ON WHOSE LIVES THE SUM OF 175000£ WAS SUBSCRIBED* 10 (Published by Order of the Right Hon. Nathaniel Clements, Deputy Vice-Treasurer of Ireland, 1777).

22. See Robert M. Jennings et al., *Alexander Hamilton's Tontine Proposal*, 45 WM. & MARY Q. 107 (1988).

23. Enhanced British Parliamentary Papers on Ireland, 1801-1922, Abstract, STATE

Other aspects of tontine administration would ultimately prove successful. The information gathered to administer the tontines created some of the first truly reliable data in the development of modern mortality tables.<sup>24</sup> Unreliable actuarial tables led early tontine promoters to persistently underestimate nominees' life expectancies. The gradual increase in the average lifespan during this period may have also worked to undercut the accuracy of the tontine promoters' math.

### TONTINE DERIVATIVES

Although each share in a tontine was specifically tied to the original investor and their designated nominee, tontine shares themselves were surprisingly liquid. A tontine's annual payments flow to its current owner, so the shares dividends make the tontine intrinsically valuable. As the pool of living nominees shrank, the dividends and thus the present value of the shares would rise. This attraction was tempered by the specter of the nominee's death, an event which would instantly render a tontine share worthless. The ultimate lure, however, was the prospect of owning one of the few shares providing a payoff at the end of the designated term of a tontine with a final payout of cash or real property. These characteristics fostered the development of a secondary market for tontine derivatives.

Genevan speculators also developed means of hedging their tontine exposure. Pools would distribute the risk associated with a specific tontine across the entire pool of investors. Upon the death of a particular 'life', the pool's share owners would only lose the portion of the value

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AND MANAGEMENT OF TONTINE ANNUITIES GRANTED IN IRELAND IN 1773: SECOND REPORT AND APPENDIX FROM THE SELECT COMMITTEE, <http://web.archive.org/web/20050219111355/http://www.bopcris.ac.uk/eppi/ref12809.html> (last visited Oct. 26, 2009).

24. Sir Edmund Halley's seminal life tables project was derived solely from life cycle data from Breslau, attractive because of its stable population and good records. See Edmond Halley, *An Estimate of the Degrees of Mortality of Mankind, Drawn from Curious Tables of the Births and Funerals at the City of Breslaw*, 17 PHILOSOPHICAL TRANSACTIONS 596 (1693). However, Antoine DeParcieux's 1746 French work overtly included tontine data, as did the important English text, *Life Annuities*, by John Finlaison. See ANTOINE DEPARCIEUX, *ESSAI SUR LES PROBABILITÉS DE LA DURÉE DE LA VIE HUMAINE* (Paris, Freres Guerin 1746); JOHN FINLAISON, *LIFE ANNUITIES* (HM Stationary Office 1829).

of their shares which was dependent on the particular life.<sup>25</sup>

### TONTINES IN BRITISH CASE LAW

Reported cases reveal how the tontine investment system worked. The Irish Tontine of 1777 gave rise to an 1869 English Chancery Court decision.<sup>26</sup> At issue was the 1860's income due to investors in the tontine. An investor, Mrs. Browne, died in 1842, leaving her children four debentures based on the 1777 tontine. Browne's son inherited half of the investment, and her five daughters received ten percent each. Since the income due to Browne at the time was relatively modest, £7/10 or 150 shillings per share, Browne's stake in the tontine was not divided up, but was instead in trust. The trustees were to give each of the legatees an accounting of their investment and distribute some cash "from time to time". It is not stated in the case whose life was specified as the one on which the tontine participation was based, but he or she was still alive in 1868. The value of the tontine grew quite large. The chancery was called on to determine whether the income generated by the tontine, more than £ 1,870, was the personal property of the married daughters or was to be given to the husbands under the "settlements" executed by the parties as part of the marriage process. The case was adjudicated by Lord Romilly, Master of the Rolls. Romilly held the tontine derivative investment fell outside of the daughters' marriage covenants.

Although the key substantive law issues raised in the Browne case involve inheritance, the case reveals much about the structure of an 1860s era tontine derivative. Tonti's original proposal of a personal investment had evolved into a marketable liquid security with the potential to travel a great distance from the original tontine investor and his nominee. It is not clear whether rights of the two deceased sisters had passed on to their heirs. At a minimum, the £1,870 in question represented only 30% of the income from the four original tontine debentures. It appears the annual income of £30 (£7/10 a share x 4 shares), grew in value to more than £6,230 in the 26 years between Mrs. Browne's death and the time of the dispute. The £1,870 in dispute represents the equivalent of approximately £110,000 of purchasing

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25. See JENNINGS & TROUT, *supra* note 6, at 57.

26. *In re Browne's Will*, (1869) 7 L.R.Eq. 231.



power in 2005.<sup>27</sup>

In another case from roughly the same period, *Oldfield v. Preston*<sup>28</sup>, the consequences of a provision in a 1788-issue private tontine—the “Doncaster Universal Tontine”—was in dispute. The tontine’s dissolution was triggered when the number of shareholders fell to the point where each surviving shareholder would receive one thousand Pounds. The original group of 364 founding shareholders bought government securities (“Consols”) worth £46,000 and split the 3% interest each year. In 1860, when only forty-six of the original investors remained, the final distribution process was initiated. At issue was whether “Succession Duties” levied by a statute passed after the founding of the tontine were due on the lump sum final dividend. The state argued that the surviving shareholders were, in essence, the successors of the now deceased rest of the original group. The Chancery judges held the succession duties were not owed, reasoning the tontine created contractual obligations and not rights of succession.

Similar issues were presented by a Scottish case, *H. M. Advocate v. Findlay*.<sup>29</sup> The case illustrates tontines were mundane at their heyday. In dispute is whether the value of the property of the tontine in the estate of the final shareholder at the time of the tontine’s “falling in” should be imputed to the estates of the previous owners of the share, who died while the tontine was still active. At the time of their deaths, the value of the share was not included in the tabulation of their estates because the value of that share was too trifling to bother with. In this case, the “Hutcheson Street Tontine Society” was created in 1797 and the share originally purchased by John Orr was tied to the life of his daughter, Janet. Fractions of John Orr’s share passed through Mr. Orr’s sisters and niece until the portions were reunited in Mr. Orr’s nephew, Gilbert Kennedy, who died in 1855. The second to last “life” passed on January, 1886, almost 90 years after the creation of the tontine, and the administrator (Scots: “Factor”) of the Tontine sought a declaration as to the ownership of the tenement of houses underlying the tontine and accumulated rents and other cash. The “Factor” of Mr. Kennedy’s estate duly put in his claim. However, the tax authorities seized the opportunity to impose estate duties on the current value of the tontine property

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27. Calculated via the “Measuring Worth” Web site. See Measuring Worth, Purchasing Power of British Pounds from 1264 to Present, <http://www.measuringworth.com/ppoweruk/>.

28. *Oldfield v. Preston*, (1862) 45 Eng. Rep. 932 (Ch.).

29. *H. M. Advocate v. Findlay (Kennedy’s Factor)*, 28 S.L.R. 596 (1890).

from each of the past transmissions. The market value of the tontine shares at each stage had not been declared and would have to be declared now. Since the law at the time pegged the value of the share on the date the Factor took the oath confirming the valuation of the estate, the new, corrective oaths should have been based on the 1886 value, not the subsequent market value, when the various estates were settled. The judge felt he had to follow precedent and agree with the tax authorities, but lamented that the result “seem[ed] hard and even inequitable.”

None of these three cases prompted condemnation of the tontine itself. Rather, these cases suggest courts and investors were comfortable and familiar with tontines.

### LOCAL TONTINES

Although tontines were imperfect national tax substitutes, they developed a secondary purpose in the United Kingdom and the United States: project finance. The tontine often took the form of a private subscription, the proceeds of which were used to finance particular schemes. The Hutcheson Street Tontine discussed above, in *H. M. Advocate v. Findlay*, is an example of such a tontine. These tontines were usually founded as a tool for municipal improvement including both public and private buildings and what would now be called urban renewal or sub-divisions.

#### Limerick, Ireland

One of the best documented<sup>30</sup> is the tontine that developed six of the handsome late Georgian buildings around Pery Square, in the Newtown section of Limerick, Ireland. The tontine was proposed in 1834 and the buildings were completed in 1838. The tontine company was finally fully subscribed and created in 1840. There were 89 shares and the list of subscribers printed in 1841 was headed by Edmond Pery, the first Lord Limerick. He took 18 shares, each tied to the life of a different person, ranging in age from 2 to 27. Ten were 10 or younger. Seven were his own children. Two of the other subscribers named essentially public “lives”, the Prince Consort Albert, then aged 22, and Princess Augusta, daughter of the Duke of Cambridge, then 18. The long term payoff for this tontine was that the shareowners tied to the six

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30. JAMES MCMAHON, *THE PERY SQUARE TONTINE* (1999).

last surviving lives took full ownership of one of the six houses.

The shares were negotiable as long as the life related to that share continued. In 1882, fifty shares were still outstanding, held by 13 people. They shared the income of the company, primarily rents less expenses, which in 1882 came to roughly £ 225 (£ 15,100 in 2005 terms). The tontine was wound up in 1913, triggered by the death of the seventh-last of the named lives. Two of the six houses ended up with descendants of the original shareholders. Princess Augusta was one of the six surviving lives.<sup>31</sup>

### New York City

Another important tontine based building was the “Tontine Coffee House” in Manhattan, the first real home of what eventually became the New York Stock Exchange.<sup>32</sup> This tontine was proposed in 1790 and completed in 1792. It was slightly unusual in that the young lives nominated were also the tontine’s shareholders and would receive the rents and any other income generated by the property. There were 203 shares sold at 200 dollars each. Dissolution would be triggered when only seven nominees remained alive. The shares could be sold by the original nominees, although the status of the shares remained dependent on the lives of the original holders.

Besides serving as a home for the “Merchant’s Exchange”, the original building, on the corner of Wall Street and Water Street, was a landmark, constantly mentioned in memoirs and newspapers as the site of important public meetings. It was torn down and replaced in the middle 1850s, when only 51 shareholders remained. The triggering death occurred on November 18, 1870. After disputes delayed the final accounting the dissolution, the property was finally sold at a court ordered auction on January 11, 1881. The sale brought only \$138,550, much less than anticipated.<sup>33</sup>

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31. See also Yorkshire History, <http://www.yorkshirehistory.com/parliament/parliament.htm> (last visited Oct. 16, 2009), for a record of the various steps in the creation of Parliament Street in Hull through a tontine-based subscription process.

32. RICHARD J. TEWELES & EDWARD S. BRADLEY, *THE STOCK MARKET* 109 (7th ed. 1998).

33. *The Tontine Association*, N.Y. TIMES, Jan. 12, 1881, at 3. A large collection of the Tontine Association’s records can be found in the New York Historical Society’s Library.

Others

Additional tontine-based projects in the United Kingdom included projects in Glasgow (Coffee House),<sup>34</sup> Stourport (Inn),<sup>35</sup> Sheffield (Inn),<sup>36</sup> Peebles (Hotel),<sup>37</sup> Folkestone (Street),<sup>38</sup> and Bristol (Assembly Rooms),<sup>39</sup> among other places. The construction of the Covent-Garden Theatre in London was based on a tontine. A tontine provided more than 65% of the money to build the parish church in Wallsend in the northeast of England. The original Richmond Bridge, the second Kew Bridge over the Thames and the Birmingham Library building all owe their existence to tontine financing. In the United States the leading inn in New Haven for many years was the Tontine Hotel. There were other tontine developments in Maine; New Hampshire; Albany, NY; and several properties in Washington DC. The current evidence tends to be tontine as a name, usually for a building, sometimes a street.

In Boston, Charles Bulfinch's historically important residential buildings known as "Tontine Crescent" was originally planned to be financed through a tontine, but the State Senate voted against granting a charter to the underlying company, reportedly on the basis of the unsavory nature of a tontine. The corporate side of the project was converted by its organizers into a bank which was approved under the name of the Union Bank.<sup>40</sup>

An amusing offering in London, the 1866 "Australian Tontine Society, Ltd.," typified the shorter term of later tontines. Its term was only seven years. In order to maintain the tontine 'effect,' subscribers

34. JAMES CLELAND, *THE RISE AND PROGRESS OF THE CITY OF GLASGOW* 133 (Scotland, James Brash & Co. 1820).

35. See *Unlocking Stourport's Past*, <http://www.unlocking-stourportspast.co.uk/tontine/tontine.html> (last visited Oct. 31, 2009).

36. See Joseph Woolhouse, *A Description of the Town of Sheffield*, [http://freepages.history.rootsweb.ancestry.com/~exyl/fh\\_material/sheffield\\_circa\\_1800.txt](http://freepages.history.rootsweb.ancestry.com/~exyl/fh_material/sheffield_circa_1800.txt) (last visited Oct. 31, 2009).

37. See *Peebles Hotels*, <http://www.tontinehotel.com/> (last visited Oct. 31, 2009).

38. See *Tontine Street Folkestone Map*, [http://maps.google.com/maps?q=Tontine+street+Folkestone&oe=utf-8&rls=org.mozilla:en-US:official&client=firefox-a&um=1&ie=UTF8&hq=&hnear=Tontine+St,+Folkestone,+Kent+CT20,+UK&gl=us&ei=jsjsSpS6KcXHIAfgxOH\\_BA&sa=X&oi=geocode\\_result&ct=title&resnum=1&ved=0CAsQ8gEwAA](http://maps.google.com/maps?q=Tontine+street+Folkestone&oe=utf-8&rls=org.mozilla:en-US:official&client=firefox-a&um=1&ie=UTF8&hq=&hnear=Tontine+St,+Folkestone,+Kent+CT20,+UK&gl=us&ei=jsjsSpS6KcXHIAfgxOH_BA&sa=X&oi=geocode_result&ct=title&resnum=1&ved=0CAsQ8gEwAA) (last visited Oct. 31, 2009).

39. MARK GIROUARD, *THE ENGLISH TOWN: A HISTORY OF URBAN LIFE* 137 (1995).

40. 4 JOSEPH STANCLIFFE DAVIS, PH.D., *ESSAYS IN THE EARLIER HISTORY OF AMERICAN CORPORATIONS* 70-73 (Harvard Univ. Press 1917).

were at least seventy years old. The area proceeds of the offering were to develop Hexham, New South Wales, near Newcastle. At the end of the seven years, half of the acreage was to revert to the oldest surviving shareholder. The other parcel was to be auctioned off, the proceeds to be split among the remaining shareholders.<sup>41</sup> The project apparently never got off the ground. While the property may have been productive at the time the tontine was issued, there seems to be significant overlap between the second parcel and what is now the "Hexham Swamp Nature Reserve."

### USE OF THE TONTINE STRUCTURE FOR CLUBS

A tontine was not an uncommon way to structure some clubs.<sup>42</sup> The fact that the clubs were tontines did not make them *per se* illegal. In the 1888 New York decision excerpted below, *In re Livingston Sportsmen's Ass'n*, the judge had been asked to dissolve the club when the club's dwindling membership could not amicably respond to an internal dissolution proposal. Eventually, the judge held the tontine was not contemplated by the statute allowing court-ordered dissolution of associations. In dicta accompanying the decision, the judge explains the nature of a tontine-based club:

Prior to its incorporation the association existed under the same name, and had acquired about \$1,400 in money, which was transferred to the new organization. With this money some real estate was purchased upon the shore of Conesus Lake, where a clubhouse was erected, and other improvements were made; so that, at the time this proceeding was commenced, it appears that the association was the owner of real and personal property of the value of more than \$2,000. This property is free from encumbrances of any kind, and there are no debts existing against the club. It further appears that, at the time of its incorporation, the association consisted of 45 members, of whom 15 remain; the others having ceased to become members by reason of death, resignation, or failure to pay dues and assessments. Of the members there remaining, nine

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41. Australian Tontine Society, Ltd., Offering Agreement, available at <http://library.law.columbia.edu/mckeever/tontine.html>.

42. My personal introduction to tontines comes from sitting in the family car with my parents and siblings as we drove along the Flanders Road between Hampton Bays and Riverhead on Long Island, New York. At a certain spot my father would point to woods to the north of the road and tell us "in there is a hunting club that is based on a tontine." Then he explained what a tontine was.

are in favor of a dissolution, and six are opposed; and of those favoring the dissolution several are so situated as to be practically unable to enjoy the privileges of the association.

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[I]t appears that this association was organized upon what is termed the "tontine" principle, which confers upon the remaining members rights and privileges which it is difficult to estimate in dollars and cents. It must be assumed that the petitioners joined the association with full knowledge of the fact that those members who survived the others would enjoy such additional rights and privileges; and it is not at all improbable that the minority were induced to join, or to continue their membership down to the present time, by reason of this very attractive feature of the organization. If, therefore, this may be treated as one of the corporations contemplated by the provisions of the Code upon which this proceeding is based, what satisfactory reason can be urged for its dissolution? The organization, in some considerable degree at least, still answers the end for which it came into being; and other and stronger reasons than those assigned should be presented to the court in order to justify its interference, even at the request of a majority of its members.<sup>43</sup>

The more modern, negative, view can be found in another New York case from 1981, involving a similar club. The situation in *Quinn v. Stuart Lakes Club* involved a dispute between the heirs of the second to last to die and the presumptive sole owner of the club's land and other assets according to its tontine structure. The judge voided the tontine effect stating "This form of death gamble, bottomed on the principle that the last survivor shall fall heir to the corporation, ought not to be encouraged nor expanded beyond limits of tontine insurance which has hitherto been recognized by law."<sup>44</sup> That "ought" is telling, since the proposition has no statute or case law to support it. The short Court of Appeals decision affirming the case also fails to cite any source for the proposition that a tontine is illegal, only inherently enforceable wishful thinking.<sup>45</sup>

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43. *In re Livingston Sportsmen's Ass'n*, 2 N.Y.S. 63, 63-64 (N.Y. Sup. Ct. 1888).

44. *Quinn v. Stuart Lakes Club, Inc.*, 439 N.Y.S.2d 30, 80 A.D.2d 350, 354, 439 (N.Y. App. Div. 1981), *aff'd*, 57 N.Y.2d 1003 (1982).

45. 57 N.Y.2d 1003 (1982).

## THE TONTINE AS AN ESTATE PLANNING TOOL

Sometimes tontines were used to keep a property in a family, probably as a way to circumvent various rules against entailment. An example is found in a letter related to an 1871 English will which dictated the division of a property known as "Sandwich Farm" near Apsley, Tasmania. Two-thirds was left in trust to two brothers resident in Melbourne, Australia and the other third to the last of 22 residuary legatees, all nieces and nephews of the testator who were scattered from New Zealand to England and Belgium. The residuary legatees were to divide the total income from the farm until only one of them was left. The description of this situation is found in a letter from the estate's lawyers who were trying to rescue the estate both from the uneconomic division of too small a property and the rejection of any interest and the trust by the Melbourne legatees. The letter admits "the provisions of the will, are to say the least of them, of a very peculiar nature, and, as we informed the Testator, when we prepared the Will, of an inconvenient and unusual character, somewhat eccentric, as was also the testator himself. His desire was to keep the Farm in perpetuity in the Hooper family and in consequence of our stating to him that this could not be done according to English law, he decided to adopt the scheme contained in the will."<sup>46</sup>

Although it is not clearly stated, the letter only makes sense as a proposal to one of the residual legatees to agree to a scheme to sell the farm and split the proceeds among them according to a plan that included actuarial data to make the division equitable as possible in relation to the relative lifespans of that class of legatee under the original will. It overtly states that to do so through the Court of Chancery would be futile since that process would exhaust the value of the farm. It emphasizes the attorney's need for agreement from all the parties to the will. There is separate text at the bottom of the letter for the addressee to give his consent and it is filled in and signed by the man and his wife and witnessed by the local vicar.

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46. Letter from William Holdstock et al. to Legatees, available at <http://library.law.columbia.edu/mckeever/tontine.html>.

## TONTINES SERVING INSURANCE FUNCTIONS

France

La Tontine n'est qu'un jeu, une gageure. Ce n'est pas une opération d'assurance.<sup>47</sup>

Despite this disparaging assessment by Maurice Picard, one of the leading French scholars on insurance, companies offering tontine based annuities were one of the standard businesses within the French financial system. The tontines served as a form of social or retirement insurance.<sup>48</sup>

Cornelius Walford's charming "Cyclopedia" points out in 1876 that the French developed annuities to a far greater extent than any other country at that time. "Their annuity operations have mostly been of a tontine character. . ." He goes on to say that "[t]here appears, strange to say, hardly any annu. asso., such as we have had in the U. K., founded in France. The bus. has been almost entirely carried on by—(1) the French Gov.; (2) the tontine annu[ity] Asso[citation]; and (3) the life offices, whose dealings in life annu[ities] have been and still are, very large."<sup>49</sup>

Walford goes on<sup>50</sup> to indicate that life insurance, which was slow to get off the ground in France, became much more popular when endowment and survivorship elements were added in the early 1840's. These incorporated elements familiar to the French from tontines and are credited with giving the industry a major boost.

47. "The tontine is but a game, a wager. It is not a system of insurance." I MAURICE PICARD, *LES ASSURANCES TERRESTRES EN DROIT FRANÇAIS* § 443 (Librairie Générale de Droit et de Jurisprudence 1970). Picard's treatise proceeds to review and dismiss the tontine, once a standard form within the French insurance industry, in a single paragraph. The text remains unchanged in later editions.

48. See Roger L. Ransom & Richard Sutch, *Tontine Insurance and the Armstrong Investigation: A Case of Stifled Innovation, 1868-1905*, 47 J. ECON. HISTORY 379, 379-80 (1987) (describing tontine insurance).

49. CORNELIUS WALFORD, 4 *THE INSURANCE CYCLOPEDIA* 257, 260 (London/New York, 1871-80, unfinished in 6 volumes). The use of unorthodox abbreviations throughout the text is idiosyncratic.

50. *Id.* at 297-98.



Arthur Scratchley, a nineteenth century author on investment matters, reported smaller French offerings called “banques de prevoyance” which were short term tontines, with terms ranging from five to twenty years. He reported them as attractive to

[M]en, especially of the military profession, who had, perhaps, no relations to whom they were particularly attached, on receiving prize money for their services, placed it in a temporary Tontine. They felt indifferent to the chance of loss, should they die before the end of its term, by the fortune of war, or by the ordinary law of mortality and were willing to stake that risk against the more agreeable prospect of reaping a magnificent profit from the popular speculation.<sup>51</sup>

### British Isles

The word “tontine” survives as a name associated with burial societies, especially in Ireland. Burial societies were among the first forms of insurance, existing in Roman times. The early modern form was created among poorer populations to provide a decent and religiously correct funeral for their members and their families. In practice, these were not really tontines since their purpose was to provide a death benefit.<sup>52</sup> The narrow function of burial insurance has for the most part been absorbed into the modern practices related to general life insurance. However, burial societies still exist, especially in countries with a historical connection to the United Kingdom.<sup>53</sup> The 2005 Report of the Registrar of Friendly Societies for Ireland lists seven such associations that still have tontine in their name.<sup>54</sup>

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51. ARTHUR SCRATCHLEY, INDUSTRIAL INVESTMENT AND EMIGRATION, BEING A TREATISE ON BENEFIT BUILDING SOCIETIES AND ON THE GENERAL PRINCIPLES OF ASSOCIATIONS FOR LAND INVESTMENT AND COLONIZATION 178 (2d ed. 1851).

52. Also, in the early 1700s, a form of life insurance now known as mortuary tontines developed in England. They are succinctly described in Geoffrey Clark's *Betting on Lives* (Manchester University Press 1999) at pages 76 to 81. The use of the word tontine is misleading for these forms of insurance, since the schemes involved payouts to beneficiaries of the dead members, not a reversion of the dead participant's share to the rest of the pool.

53. However, per the current United Kingdom Financial Services Authority Registration search page (<http://www.fsa.gov.uk/Pages/register/>), there are no entities currently registered with “tontine” in its name, and only one with “burial” in its name.

54. REPORT OF THE REGISTRAR OF FRIENDLY SOCIETIES 2005, available at <http://www.entemp.ie/publications/commerce/2005/rfsannualreport.pdf>.

United States

A particular form of life insurance with a tontine element was developed in the United States during the latter part of the 19th Century. The insurance industry was evolving into a highly competitive business at that time, with the main battlers being Equitable Life and Mutual Life, with New York Life joining the pair later on. The tontine gimmick was the invention of Henry B. Hyde, who founded Equitable Life (now AXA) in 1859, after working as a clerk at Mutual Life for a number of years.

Also known as “deferred dividend” policies, tontine policies were written specifically so “no dividends, return premium, or surrender value shall be received for a term of years called the tontine period.” The death benefit would always be paid, no matter when it occurred, but only after the tontine period, ranging from five to twenty years, would the policy holder start to get dividends as well. These dividends would be based not just on the income from his premiums, but included a share of the premiums of anyone in the pool who had died during the accumulation period or whose payments had lapsed. Additionally, with some tontine schemes, the policyholder is not required to pay a premium once tontine income is sufficient to replace the premium. The tontine policies were initially drafted so the accumulation of premiums and any surplus were wholly forfeitable on a failure to keep up payments up to the expiration of the tontine period. The term “semi-tontine” was developed to describe a later, more successful version, in which only the non-premium surplus was forfeited at discontinuance of the policy.<sup>55</sup>

The tontine-related product flourished from 1868 until it was prohibited by statute in New York in 1906.<sup>56</sup> Besides developing the tontine insurance idea, Hyde is also credited with shaping the image and many practices of the modern life insurance industry, including broadening the range of products sold to suit the needs of particular individuals and being the first to give high commissions to salesmen. One later successor at Equitable described the genius of Hyde’s tontine as realizing the “risk of living too long is just as insurable and valuable as the risk of dying prematurely.”<sup>57</sup>

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55. Miles Menander Dawson, *Effects in Free Surrender and Loan Privileges in Life Insurance*, 4 PUBL’NS OF THE AM. STATISTICAL ASS’N 84-98 (No. 28/29 Dec. 1894-Mar. 1895).

56. See generally 1906 Laws of New York 763 (Chapter 326) (Apr. 27, 1906).

57. JOHN ROUSMANIERE, *THE LIFE AND TIMES OF THE EQUITABLE* 31 (Equitable

The tontine policies were not universally acclaimed, however. The tontine aspect offended those of delicate sensibilities in two ways. The basic premise was seen as directly profiting from other people's deaths and the inclusion of lapsed policy premiums in the tontine pool was seen as directly profiting from other people's economic misfortunes.

This form may be fitly characterized as the gambling form, inasmuch as the only hope of profit to a few is that the many will be robbed of their savings. Tontine insurance is profitable to the few in just proportion that misfortune shall overtake those who participate in it. No man would risk large payments with the certainty of losing all if he should fail to make one such payment in a term of years, if he were not ticked by the hope that others would be the unfortunate ones compelled by circumstances to discontinue and lose all, while he would be the exception and profit by their loss.<sup>58</sup>

Since the tontine related insurance scheme has long disappeared from modern commerce, the best descriptions are found in contemporary reports which present them as a normal business proposition. This is a fairly clear example from the Supreme Judicial Court of Massachusetts:

[The policy] was for the sum of \$10,000, payable, on the decease of the plaintiff, to him, his executors, administrators, or assigns, and was for the term of his life. It was known as a tontine policy on the savings insurance plan, and was to continue as such for the term of ten years, if the plaintiff should live so long. If the holder of the policy died during the tontine period, which expired on March 18, 1883, his estate would not receive any benefit from the dividends which ordinarily are made on life assurance policies annually or at stated periods, which dividends consist of the surplus of premiums after deducting the cost of insurance and the computed reserve, these being then held by the company for the benefit of the other policy holders, and forfeited by him. His estate would receive only the amount of his policy. If the holder of the policy also should fail during this tontine term to keep up his policy by payment of the premiums, it would be forfeited. Policies of this character are kept in classes of ten, fifteen, or twenty years, according to their tontine periods, and, while the funds of each class are not kept separate, distinct accounts are kept with each class, so as to show the amount

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Cos., Inc. 1995) (quoting Richard H. Jenrette).

58. G. A. Litchfield, *Objections to Level-Premium Life Insurance*, 4 NEW ENG. MAG. 68-77 (1886). An entertaining historical survey of some of these same issues relating to life insurance generally can be found in Clark, *supra* note 53, at 78, although tontines are only mentioned glancingly.

to which it is entitled, and by this means the amount due upon each policy at the expiration of its tontine term. At the expiration of ten years, if such be the term, or at the completion of the tontine dividend period, it is provided that "all surplus or profits derived from such policies on the tontine savings fund assurance plan as shall cease to be in force before the completion of their respective tontine dividend periods shall be apportioned equitably among such policies as shall complete their tontine dividend periods."<sup>59</sup>

The strength—and the problem—was the accumulation of "surplus" during the tontine period. With no obligation to pay dividends but only death benefits for a significant period, the insurance company could accumulate cash fairly quickly. In addition, payments made for policies that lapsed for non-payment accrued to the insurance company. In tontine policies, this accrual was added to the tontine fund. Reserves were not required to be held against tontine liabilities until the tontine period was up and there was no regular accounting of the accumulating surplus generated in relation to the policies. The companies thus had the accumulated cash to use as they wished.

The accumulated capital generated by the tontine structure is credited by some modern scholars with allowing the companies writing tontine insurance to survive the 1873 depression when many others failed.<sup>60</sup> Twenty years later, however, after a long period of deflation, the payouts on the tontines were much lower than had been projected at the point of sale.

An illustration can be found in a little pamphlet called "A Mistaken Prophecy" published by Walter Wright in 1891. He shows how the prediction of a twenty year return of \$1,135 by the Equitable Life in selling its Tontine policy actually resulted in a payout of \$751 in 1891. In the pamphlet, Mr. Wright reprints the predictive charts issued in 1871 by Equitable Life and texts supporting the math involved. He acknowledges the interest rates used in the chart were higher than actually occurred in the twenty year span, and adjusts his figures accordingly, but the payout is still lower than might have reasonably been anticipated. Wright highlights the expenses figure in the original chart and notes that it was much lower than the Equitable had ever reported during that period by using the actual expenses figures as submitted by Equitable to

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59. *Pierce v. Equitable Life Assurance Soc'y*, 145 Mass. 56, 57 (1887).

60. Roger L. Ransom & Richard Sutch, *Tontine Insurance and the Armstrong Commission: A Case of Stifled Innovation in the American Life Insurance Industry*, 47 J. ECON. HIST. 379, 382 n.10 (1987).

the Massachusetts authorities. He implies simple theft on the part of the company management. He concludes by pointing out that “. . . there is no reason to expect that the trustee will be remarkably parsimonious in determining his own compensation.”

When challenged by disappointed investors, the insurance companies were the beneficiaries of pre-consumer era courts whose judges were willing to side with the companies and state that the projections of salesmen were speculation and not an enforceable part of the overall contract. While the economic picture certainly changed, self-dealing by managers of the big insurance companies exacerbated the situation.

The first major reformist attacks on the tontine were part of progressive administration of Wisconsin led by Robert LaFollette as Governor. His Commissioner of Insurance, William Fricke, published an influential report, “The Law and Distribution of Surplus of Life Insurance Companies,” in 1902. The Wisconsin statutes at that time included an article<sup>61</sup> that the reformers contended was a ban on any policy that deferred dividends beyond five years, but the big companies interpreted the word “may” in the statute to refer to the act of providing a dividend, not to the choice of a dividend plan encompassing from one to five years, and ignored the pressure to issue regular dividends. Fricke’s pamphlet is a strong argument for a more regular return of the surplus to policy holders.

In early 1905 an internal fight for control of Equitable Life resulted in public accusations of corruption and self-dealing from competing insiders. This, combined with the growing distrust of the insurance industry generally, led to the creation of an investigatory commission supervised by the New York State Legislature. It was known as the Armstrong Commission for its chair, Sen. W. W. Armstrong, but the star of the very public process was the general counsel, one Charles Evans Hughes.<sup>62</sup> Besides the accounting flaws, the tontine aspect was again painted as an unsavory form of gambling on the lives of others. Among other reforms enacted as a result of the investigation, deferred dividend

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61. The state of the law in 1902 consisted of Wisconsin Laws of 1870, ch. 59, § 14 (as amended by Laws of 1887, ch. 309).

62. Hughes, who rode his fame from this work to the governorship of New York, Secretary of State and ultimately Chief Justice of the United States Supreme Court, later spearheaded a ban on horse racing in New York while Governor. Gambling just wasn’t in his blood. JOHN RICHARD O’HARE, M.A., VII, *THE SOCIO-ECONOMIC ASPECTS OF HORSE RACING* (1945).

insurance was forbidden by New York state legislation in 1906.<sup>63</sup> At that time, the New York State Insurance Department had authority over 95% of the US life insurance business, directly and indirectly, so the effect was felt throughout the country immediately.

Although the abolition of the deferred dividend offering is usually pointed to as the end of the overt tontine and semi-tontine policies in the U.S., they continued as part of the range of policies available much further into the century. An article inspired by proposals to specifically abolish tontine policies in 1955 written by the insurance expert Herbert Kuvin reviewed the status of tontine ideas related to insurance and found them still extant in 1955.<sup>64</sup> The contemporary assessment, found in an essay by Ransom and Sutch,<sup>65</sup> is that the tontine aspect of the standard insurance policies served as a distraction and scapegoat in coming up with remedies for the range of vices in the industry. The problem was not with the form, but with self-dealing management. Close regulation and rigorous reporting and accounting would have served to correct the problems.

#### INSURANCE RELATED TONTINE CLUBS

The national companies also facilitated an ancillary service through which standard life insurance was bought individually by members of a group with the other members of the group the ultimate beneficiaries of each other's policies. Each purchaser would buy life insurance naming himself as the beneficiary and then assign the benefit to an agent who acted as the fiduciary to re-distribute the death benefit to the surviving members of the group. In one reported case, the form to do this was actually provided by the insurance company and was labeled the "Tontine and Club Circular of the United Accident and Life Insurance Association, 44 Broadway, New York." In this particular case, the group had ten members and the heir of the first to die challenged the payment of the policy's proceeds to the agent of the "club", as, among other things, an illegal wager. The court did not interfere with the payment process nor did it recognize the arrangement as gambling.<sup>66</sup>

Of course, there is no reason why a basic tontine has to be tied to

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63. See 1906 N.Y. Laws 763.

64. Herbert A. Kuvin, *Tontine Policies and Their Use Today*, 4 INS. L.J. 345-53 (1955).

65. Ransom & Sutch, *supra* note 61, at 379-81.

66. *Hill v. United Life Ins. Ass'n*, 154 Pa. 29 (1893).

insurance models. It is actually a form of annuity.

### GUILT BY ASSOCIATION

Des Moines Concern Fails  
Iowa Tontine Investment Company Proves Short Lived  
Des Moines, Iowa, Dec 4. - The Iowa Tontine Investment Company, organized a few months ago by people from St. Louis and Sedalia, failed here today. President G. W. Stone is missing and so are the funds. Among the victims here is the president of one bank and two or three cashiers of others.

*The Daily Inter-Ocean* (Chicago), December 5, 1893, page 11, column 7

While the national insurance companies may have had messy and devious accounting, they provided essentially straightforward products and services. However, in the late 19th century local companies, often using names similar to the national companies ("Equitable Loan and Security Company" in Georgia, for example) peddled plans whose components used standard investment terms but which were basically scams. These companies sold plans that were called tontines and appeared to be similar to bonds. To make them more attractive, however, they promised to make early payment on a portion of the bond-like coupons according to a scheme that was essentially a matter of chance to the buyer, so they were condemned as lotteries and forbidden to use the mails.<sup>67</sup> In the Minnesota example below, if the instrument holder's coupon had a serial number that was low on the early redemption list maintained by the offeror, it could be subject to early redemption. The element of chance was introduced because the buyer would not know his serial number until the initial payments had been made. If it were low, the subscriber would be the beneficiary of an early redemption and receive a lump sum well beyond his initial payments. In reference to one of these schemes, an 1894 opinion by the United States Attorney General in response to a query from the Postmaster General reads in part:

[R]equesting my opinion upon the question of the right of the Tontine Savings Association of Minneapolis, Minn., to use the United States mails in the carrying on of its business.

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67. See JOHN L. THOMAS, *LAW OF LOTTERIES, FRAUDS, AND OBSCENITY IN THE MAILS* 172-91 (F.H. Thomas Law Book Co. 1903) (discussing these so-called "bond investment companies").

I concur in the conclusion reached by the Assistant Attorney-General for the Post-Office Department that the company's business is in the nature of a lottery within the meaning of sections 3894 and 4041 of the Revised Statutes of the United States, as amended by the act of September 19, 1890.<sup>68</sup>

It is not clear if any of these companies ever established themselves as real annuity providers or were all fly-by-night operations.

Another scam involved the installment purchase of a diamond based on a set number of weekly payments and deliverable at the end of the payment period. If the purchaser preferred, he could accept the equivalent in cash of roughly 150% of his payments in lieu of the diamond. The selling company could only stay in business if a substantial number of the contracts were defaulted. In one report of a dispute, "[m]embers of the company insisted that they were perfectly able to carry out the terms in their contracts and would still be making money as 80 per cent. [sic] of the policy holders would allow their policies to lapse through non-payments of assessments."<sup>69</sup> It is unclear why the term tontine was used in the name of the company, although it may be an open acknowledgement of the need for forfeitures by fellow investors in order for a purchaser to actually get his diamond or cash. A short description of one of these schemes can be found in *Barney v. Tontine Surety Co.*<sup>70</sup>

The net effect of the insurance revisions and the flim-flam men is that tontines themselves are perceived as wholly illegal in the United States.<sup>71</sup> The support for such a conclusion is tenuous. The issue is a classic one in common law: whether the prohibition developed in a

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68. 21 Op. Att'y Gen. 4 (1894).

69. *Methods of "Diamond Associations" Again Aired in Court*, WESTERN SUPP. OF THE JEWELERS' CIRC., Feb. 15, 1899, at 40.

70. 131 Mich. 192 (1902).

71. As examples of current popular thought, Goldsticker's article states boldly "[t]ontines are illegal in the United States." Ralph Goldsticker, *A Mutual Fund to Yield Annuity-like Benefits*, 63 FIN. ANALYSTS J. 63 (2007). Pechter's article starts out "[t]ontines are banned . . ." Kerry Pechter, *Possible 'Tontine' Revival Raises Worries*, ANNUITY MARKET NEWS, May 2007, at 1. To attempt to prove tontines illegal in the U.S. would be a variant of the logical torture known as attempting to prove a negative. A LexisNexis word search of "tontine" in the case law in New York (7), California (2), Massachusetts (1), and Virginia (0) from 1945 only generated ten cases and only the New York one cited at note 45, above, was relevant. Before 1945, the case law is still cluttered with tontine insurance cases. A precise answer to the question would be an article unto itself.



particular setting should be read to cover all instances, or only the instances specified by the individual cases that provoked the prohibition. There are statutory declarations relating to insurance and there is negative case law on tontine-like schemes based the regulation of wagering or lotteries. Much of that jurisprudence, however, developed before lotteries became legal in many jurisdictions.

In France, a number of spectacular financial failures were related to tontine annuity companies, most notably the Caisse LaFarge affair around the time of the revolution and the first Empire.<sup>72</sup> In modern Australasia, Ponzi schemes<sup>73</sup> appearing to be legal Rotating Savings and Credit Associations (ROSCAs, see below) are often referred to as tontines<sup>74</sup> with definite pejorative intention.

#### CURRENT STATUTES

Only Louisiana and South Carolina have actual statutes specifically outlawing tontines. Both statutes are found in the sections of their laws concerning insurance. Title 22, § 445 of the Louisiana statutes covering insurance reads “the sale by any individual, company, partnership, corporation, non-profit corporation or insurance company of tontine funds whereby any part of the principal or interest earned on individual contributions is to be used for the benefit of other contributors is hereby prohibited.”<sup>75</sup> The South Carolina text, while mentioning tontines in its title—“Tontine policies prohibited”—uses classic legislatively obscure and verbose language which has the effect of prohibiting tontines without using the word:

No life insurer, mutual aid association, or fraternal benefit

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72. GUY THUILLIER, *UNE TÉNÉBREUSE AFFAIRE : LA CAISSE LAFARGE (1787-1892)* (1999).

73. A common financial scam named for Charles Ponzi who established the first version the early 1900s. See *In re Ponzi*, 268 F. 997 (D. Mass. 1920). An entity is created through which the first investors are paid what seem to be terrific profits but which are in fact the contributions of later investors. The trick is to bail out before the spiral can no longer be sustained by new investors. The current depression has caused a number of new versions to appear, most notably underlying the Madoff scandal.

74. See *Tontine Schemes: Statement Before the Parliament of New South Wales* (2004) (statement of Paul Lynch) (transcript available at <http://www.parliament.nsw.gov.au/Prod/parliament/hansart.nsf/V3Key/LA20041112009>).

75. LA. REV. STAT. ANN. § 22:445 (2008).

association operating in this State is permitted to issue policies, certificates, or contracts to policyholders or members providing for the establishment of its policyholders or members into divisions and classes for the purpose of providing for the payment of benefits from special funds created for that purpose to the oldest member of the division and class or to the members of the division and class whose policy has been in force the longest period of time upon the death of a member in the division and class.<sup>76</sup>

Ironically, the South Carolina statutes also have another section which specifies the “[r]eserve requirements for tontine policies.”<sup>77</sup>

### MODERN VARIATIONS

#### French Real Property and Company Law

A tontine is still a form of joint ownership in France used for small businesses and real property that is based on the last survivor principle. It serves both to confine ownership to a small group and to escape liability at the point where the ownership might otherwise be subject to inheritance taxes. It can be used to make sure one half of a couple gets full ownership of property at the death of one partner. If married, the law would normally act to divide the property between the survivor and the couples’ children at the death of a spouse. When the couple owns the property in a tontine, the surviving spouse simply becomes the full owner without the children having a claim on it and without the state having an opportunity to exact an inheritance tax. It is similarly used to provide a satisfactory joint ownership tool for unmarried couples.

As a tool in company law, a tontine clause can be inserted into the articles of association of several forms of small business organizations to ensure that the survivor or survivors can continue to operate the company after the death of one of the participants. It also provides certain tax advantages that are well beyond the scope of this article.<sup>78</sup>

La Tontine is also a somewhat obsolete French card game.

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76. S.C. CODE ANN. § 38-55-90 (2006).

77. S.C. CODE ANN. § 38-55-110 (2006).

78. See generally Sébastien Moerman, *The French Tontine*, 27 INTERTAX INT’L TAX REV. 478 (1999) (discussing possible uses of the tontine under current French law).

ROSCAs in Africa and Asia

The word tontine is currently used to describe a kind of local financial association in Asia and Francophone Africa. This usage most likely the result of the widespread acceptance of a translator's approximation as the cultures first came together. However, they are not really classic tontines, but a *sui generis* micro-credit institution. For development economists, they are classed within a type of organizations known as "ROSCAs", or Rotating Savings and Credit Associations.

Rotating savings and credit associations are examples of lending groups. They are widespread in sub-Saharan Africa. Prevailing in most developing countries, rotating savings and credit associations are known under different names in sub-Saharan Africa. Names vary from tontines in French-speaking African countries such as Côte d'Ivoire, Congo, and Togo to Susu in Ghana, Esusu in Nigeria, Ekub in Ethiopia and Niangi in Cameroon. Other names are also used elsewhere. A rotating savings and credit association consists of members who know each other on a personal basis, usually as a result of social or employment, and who agree to contribute a fixed sum of money periodically to a pool that distributes the money collected by lot on agreed dates. One member receives an equal amount on the agreed date. When every member has received the money, the cycle is completed; the association can dissolve or reorganize . . . . Thus, the associations provide interest-free loans to members. These loans are short-term loans and can be used for any purpose. However, they are generally available in limited amounts.<sup>79</sup>

Local ROSCAs in Southeast Asia were called tontines as well even though the ROSCA-like entity is much older than the European tontines.

Tontines are rotating savings and credit associations (Roscas) [sic]. Roscas have a very long history. In Asia the Hui, a mutual financial association in China . . . can be traced back to the middle of the Tang dynasty ( 618-906 ) and Kou, a simplified form of group savings and loan associations, were documented in Japan in 1275 AD . . . .

Tontines are neither legal nor illegal, and are often simply outside the terms of reference and normative practices of the mainstream or

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79. NATHANAEL HISHAMUNDA & PETER MANNING, FOOD AND AGRICULTURAL ORGANIZATION OF THE UNITED NATIONS, PROMOTION OF SUSTAINABLE COMMERCIAL AQUACULTURE IN SUB-SAHARAN AFRICA: INVESTMENT AND ECONOMIC FEASIBILITY (vol. 2) 8 (FAO Fisheries Technical Paper No. 408/2, 2002), available at <http://ftp.fao.org/docrep/fao/005/Y4206E/Y4206E00.pdf>.

dominant society. Since tontines are practised [sic] within a closed socio-cultural system which is well understood by participants, Cambodians would rather use tontines than bank loans. Although tontines may seem insecure, they continue to enjoy support because they provide people from Cambodia with a comfortable and flexible means of accumulating savings and access to credit impossible through other formal means. Participants in Cambodian tontines believe that the returns from tontines are higher than those available from other saving methods. To them a tontine is a familiar financial instrument within their ethnic communities.<sup>80</sup>

The African and Asian ROSCAs tend to be somewhat extra-legal.

### CONCLUSION

The tontine has clearly had its ups and downs, but it may be due a reevaluation based on its conceptual simplicity and its potential to fill a market gap for singles and the heirless. In an era in which the range of retirement schemes is matched only by the uncertainty of the returns, the virtual guaranty of growth in a tontine is also attractive as long as the reasons for the growth are not found obnoxious.

### AFTERWORD: IS THERE A PLACE FOR THE TONTINE TODAY?

Contemporary demographics make reviving the tontine as an annuity-like instrument a realistic possibility.<sup>81</sup> The gradual increase in income to participants as they grow older is an attractive proposition, especially among a graying population for whom standard forms of life insurance are not particularly useful. Mellon Capitol, for example, has

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80. Man Hau Liev, Center for Refugee Education, School of Social Sciences, Auckland Institute of Technology, Presentation at the 12th NZASIA Conference at Massey University: Tontine: An Alternative Financial Instrument in Cambodian Communities (Nov. 26-29, 1997) (paper available at <http://www.cambodia.org.nz/Tontine.htm>).

81. After decades of neglect, a small flurry of interest has recently developed. See Gillian Tett & Joanna Chung, *Death and the Salesmen*, FT MAG., Feb. 24/25, 2007, at 27-31 (describing a somewhat furtive current English investigation into the viability of tontines). See also Chris Salih, *Investment; Is It Time for Tontines?*, MONEY MARKETING, June 28, 2007, at 36; Interview by Masashi Yamaguchi with Tadaki Nakamae, President, Nakamae International Economic Research, *Insurance Should Ease Old-Age Uncertainties*, NIKKEI WEEKLY, Mar. 12, 2007 (proposing the tontine as a useful tool for Japan's aging population). But see Kerry Pechter, *Possible Tontine Revival Raises Worries*, ANNUITY MKT. NEWS, May 1, 2007, at 1.

recently proposed a mutual fund/tontine hybrid.<sup>82</sup> A modern tontine-annuity could be an important tool to help protect against the modern problem of living too long.

To establish a fair tontine, it would be indispensable to class together none but individuals of the same age, and who were placed under nearly the same circumstances; and to enact, that the entire annuity of each class should always go to the last survivor. But it would be impossible to establish any extensive tontine upon such principles, that is, on principles that would render the chances of the subscribers equal and fully worth the sums paid for them.<sup>83</sup>

Assuming a tontine offering based on the actual lives of the participants and not some other person, the fairness that was thwarted by the limited diversity of wealth of the early 19th century might easily be achieved today. The tontine annuity could be a wholly appropriate financial instrument in the modern economic structure. Besides the simple increase of numbers of people with money to invest, the demographics of our modern urban society clearly show an increase in singles and in childless couples. A tontine is a way for singles in particular to provide for their own needs in old age when they have no social or emotional expectation of having to leave property of some sort to an heir or legatee. A tontine, in contrast to a life annuity, has the potential to grow as the participant grows older, potentially in a kind of inverse proportion to the other income of the aging participant. This may be especially useful for people who have not been able to put aside much for their retirement and come to face that issue relatively late in life.

Ben Bernanke, the Chairman of the Federal Reserve Board has recently<sup>84</sup> pointed out the nature of the demographic squeeze we face.

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82. See Ralph Goldsticker, *A Mutual Fund to Yield Annuity-like Benefits*, 63 FIN. ANALYSTS J. 63 (2007). See also Jenna Gottlieb, *Mellon Looks to Past, Finds Tools for the Future*, PENSIONS & INVS., Feb. 5, 2007, available at <http://www.pionline.com/apps/pbcs.dll/article?AID=/20070205/PRINTSUB/702050726/1031/TOC>. On the proposal by Mellon to patent the idea, see Ashlea Ebeling, *Last Retiree Standing*, FORBES, Mar. 12, 2007, at 50.

83. J.R. McCULLOCH, CONTRIBUTIONS TO THE EDINBURGH REVIEW 72 (vol. 2, 1824-31) (citing LACROIX, TRAITÉ ÉLÉMENTAIRE DES PROBABILITÉS 235 (Paris, Bachelier, 2d ed. 1822)).

84. *Long-Term Fiscal Challenges and the Economy: Testimony Before the H. Comm. on the Budget* (2007) (statement of Ben S. Bernanke, Chairman, Federal Reserve Board) (transcript available at <http://www.federalreserve.gov/boarddocs/>

“Currently, people 65 and older make up about 12 percent of the U. S. population . . . . [I]n 2030 Americans 65 and older will constitute about 19 percent of the U. S. population . . . .” At the same time, the ratio of 65 and older to the group aged 20 to 64 will rise from one to five to one to three. In addition:

Less than 25 percent of American households are married couples with children younger than 18. And more Americans are remaining single—82 million of them, to be exact. . . . In Massachusetts, Rhode Island, Louisiana, Mississippi, Nevada, New York and the District of Columbia, the majority of households now are made up of singles.<sup>85</sup>

Besides the change in demographics, the record keeping aspect of running a tontine has become much easier. The ability of plan administrators to draw on government and private databases for actuarial structuring, related financial information, and participant registration has transformed all of the insurance related industries and a tontine annuity scheme would use the same data in a slightly different framework.

The tontine is a relatively simple idea. In a society with a thousand and one proposals and schemes for investment toward provision for old age, its comparative lack of complexity is a particularly strong attraction.

#### Examples of Standard Modern Annuities

The “traditional” annuity offered by TIAA-CREF, a large pension service, currently earns 5.25 percent, with minimum contractual rate of three percent. The annuity purchaser receives an annual payment of 5.25% of the sum invested for the rest of his or her lifetime. The “stable return” annuity offered by TIAA-CREF, pays a guaranteed one to three percent a year on the principal, with the possibility of more than that each year depending on their return on the underlying investments. It currently is paying four percent. The principal can be cashed in at any time by the purchasers.

#### An Outline for Tontines as a Modern Annuity-Like Product

The principle behind the following examples is to keep the models

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testimony/2007/20070228/default.htm).

85. Dan Gabriel & Elianna Marziani, *Insight on the News*, ONE BY ONE, July 30, 2001, available at [http://findarticles.com/p/articles/mi\\_m1571/is\\_28\\_17/ai\\_76997837](http://findarticles.com/p/articles/mi_m1571/is_28_17/ai_76997837).

as simple as possible so the key features of the proposals are clear. The model has two basic versions. One would be a variation on a standard annuity and would roughly follow the plan of the original classic tontines. The second would absorb some of the notions of the deferred dividend insurance idea, and postpone initial returns to some set time in the future. Both present a host of complications which need not be discussed here.

The proposed classic tontine would be an annuity sold to groups of a particular size with an immediate regular payout of a set percent of the purchase price, but whose payouts would increase over time as fellow-purchasers die off. The provider would establish a target of certain number of subscribers and would close the offering on reaching the goal. The offer would be made to a small group defined by age and sex, perhaps as narrow as having to have been born in a specific year. The provider could offer many of these at a time, so individual groups would cover a span of, say, thirty years, from ages 30 to 60, with parallel offerings for each sex. As a particular tontine was fully subscribed, the provider could then offer another to the same age/sex group. An individual would be limited to buying one share in any appropriate offering, but could buy into as many offerings as he or she was eligible for. To reduce the gaming potential of the tontine, the shares would have to be bought in the purchaser's own name and to rely on the purchaser's own life as the measuring stick for participation. This is only a minor variation on the basic annuity. The administrative procedures might be slightly more complicated and managerial costs might be slightly higher than a standard annuity, but lure of the long-term increase for the purchaser should make it quite marketable.

The proposed deferred dividend tontine offering would also have a one-time purchase price of a set amount. The same principles underlying the structuring of the classic tontine would apply to this version as well. For the basic deferred dividend tontine, interest payments would start fifteen years after the offering was closed. While arbitrary and of course variable, fifteen years is the period needed to double capital at 5% compound interest. Using very simple figures based on the June 2006 Social Security Actuarial Life Table, a class of 50 year old males as purchasers, and assuming a dormant period accumulation at 5% a year, the annual payouts would be 11.7% of initial contribution at 65, 13.1% at 70, 15.7% at 75, and 21% at 80. In addition, different offerings could also have varied deferment periods so subscribers could select among them or buy several. For both models,

the entire capital would revert to the provider upon the death of the last participant in a particular pool.<sup>86</sup>

The tontine can also be more than a variant annuity structure. There is no reason why it couldn't also be revived as a means for aggregating capital for buildings or other civic projects. A recent essay by Andreas Lange, et al, in the NBER Working Paper series<sup>87</sup> makes this very point, comparing them to lotteries as a public project financing scheme. They "show that the optimal tontine generates contributions that are equivalent to those under a single prize lottery when agents are symmetric and risk-neutral. For symmetric risk-averse agents, contributions under the optimal tontine strictly dominate contributions raised under any lottery type."<sup>88</sup>

Another variant might involve a deferred dividend model, so there would be no need to make immediate interest payments. The organizers would face less pressure for immediate returns and would have a freer hand during the crucial initial or development period than they might in more standard financing schemes.

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86. This is a generic outline and is intended to simply suggest the possibilities. See Goldsticker, *supra* note 72 (providing sophisticated detail on the current Mellon hybrid proposal).

87. Andreas Lange, John A. List & Michael K. Price, *Using Tontines to Finance Public Goods: Back to the Future?* (NBER Working Paper No. 10958, 2004), available at <http://www.nber.org/papers/w10958>.

88. *Id.* at 20.



*Notes & Observations*