

**Report Pursuant to Section 129 of the
Emergency Economic Stabilization Act of 2008:
Restructuring of the Government’s Financial Support to
the American International Group, Inc.
on March 2, 2009**

Overview

On March 2, 2009, the Board of Governors of the Federal Reserve System (the “Board”), based on the unanimous vote of its five members, announced its approval under section 13(3) of the Federal Reserve Act (12 U.S.C. § 343) for the Federal Reserve Bank of New York (the “Reserve Bank”) to extend credit to American International Group, Inc. (“AIG”) in connection with the securitization of the net cash flows of designated blocks of life insurance policies written by domestic life insurance subsidiaries of AIG. The proceeds of this new Reserve Bank credit will be used to repay an equivalent amount of borrowing by AIG under the revolving credit facility (the “Revolving Credit Facility”) established by the Reserve Bank in September 2008.

In connection with this authorization under section 13(3) of the Federal Reserve Act, the Board separately authorized the Reserve Bank to take certain actions to reduce and restructure the Revolving Credit Facility. Part of this restructuring will involve the exchange of a portion of the amount owed by AIG under the Revolving Credit Facility for preferred equity interests in two special purpose vehicles that will be established to hold the stock of two life insurance subsidiaries of AIG.

These new measures taken by the Department of the Treasury (the “Treasury Department”) and the Board help address the capital and liquidity needs of AIG, which continues to be systemically important, facilitate the execution of AIG’s global divestiture program in an orderly manner, promote market stability, and protect the interests of the U.S. government and taxpayers.

As Vice Chairman Kohn noted in his testimony before the Senate Committee on Banking, Housing, and Urban Affairs on March 5, 2009, the decision to provide additional assistance to AIG was both difficult and uncomfortable for the Federal Reserve. However, the Federal Reserve and the Treasury determined that the risks and potential costs to consumers, municipalities, small businesses and others who depend on AIG for insurance protection in their lives, operations, pensions, and investments, as well as the risks to the wider economy, of not providing this assistance during the current economic environment were unacceptably large. The disorderly failure of systemically important financial institutions during this period of severe economic stress would only deepen the current economic recession.

Background

AIG is a large, diversified financial services company that, as of September 30, 2008, reported consolidated total assets of slightly more than \$1 trillion.¹ AIG operates in four general business lines through a number of subsidiaries: (i) general insurance; (ii) life insurance and retirement services; (iii) financial services; and (iv) asset management. In 2007, the last year for which annual industry data is available, AIG's U.S. life and health insurance businesses ranked first in the United States in terms of net premiums written (\$51.3 billion) and third in terms of total assets at year-end (\$364 billion). For the same period, AIG's U.S. property and casualty insurance businesses ranked second in the United States in terms of net premiums written (\$35.2 billion) and third in terms of total assets at year-end (\$124.5 billion). AIG conducts insurance and finance operations in more than 130 countries and jurisdictions and has more than 74 million individual and corporate customers and 116,000 employees globally. In the United States, it has approximately 30 million customers and 50,000 employees, and provides insurance to approximately 180,000 small businesses and other corporate entities, which employ approximately 106 million people in the United States.

In addition to its on-balance-sheet positions, AIG is a major participant in a wide range of derivatives markets through its Financial Services division, and particularly through its AIG Financial Products business unit ("AIGFP"), and is a significant counterparty to a number of major national and international financial institutions. AIG also is a major provider of protection to municipalities, pension funds, and other public and private entities through guaranteed investment contracts and products that protect participants in 401(k) retirement plans. A significant portion of the guaranteed investment agreements and financial derivative transactions entered into by AIGFP include provisions that require AIGFP, upon a downgrade of AIG's long-term debt ratings, to post additional collateral or, with the consent of the counterparties, assign or repay its positions or arrange a substitute guarantee of its obligations by an obligor with higher debt ratings.

Financial markets in the United States have been experiencing significant stress for more than a year. During this period, investor confidence in U.S. financial institutions has been shaken by sharp and broad-based declines in both equity and home prices; continuing increases in mortgage delinquencies and defaults; resulting substantial drops in the values of mortgages and mortgage-backed securities; dislocations in some term funding markets; losses caused by the failure of several significant domestic financial institutions; and large losses at financial institutions in other parts of the world, among other things. The strains in financial markets and pressures on financial firms

¹ September 30, 2008, is the reporting date closest to the date on which the Federal Reserve's involvement with AIG commenced. As of December 31, 2008, the company's reported total consolidated assets were \$860 billion.

have contributed to a significant deterioration in the economic outlook for both the United States and many other countries.

In light of these and other facts, the Federal Reserve and the Treasury Department have taken a series of steps since September 2008, to address the liquidity and capital needs of AIG and thereby help stabilize the company, prevent a disorderly failure, and protect financial stability, which is a prerequisite to the resumption of economic growth. The Board previously has provided the Committees a description of, and the reasons for, the actions taken with respect to AIG in 2008 by the Federal Reserve under section 13(3) of the Federal Reserve Act and the Treasury Department under the Emergency Economic Stabilization Act (“EESA”) in the reports filed with the Committees on October 14, November 3, and November 17, 2008.²

Despite these actions, AIG continued to face strong liquidity and capital pressures in the fourth quarter of 2008. On Monday, March 2, 2009, AIG announced a loss of approximately \$62 billion for the fourth quarter of 2008, ending a year in which AIG suffered approximately \$99 billion in total net losses. As a consequence of increased economic weakness and market disruption, the insurance subsidiaries of AIG, like many other insurance companies, recorded significant losses on investments in the fourth quarter of 2008. Commercial mortgage-backed securities and commercial mortgages experienced especially severe impairment in market value, requiring a steep markdown on the companies’ books, despite a lack of significant credit losses on these assets to date.

The loss of value in the AIG’s investment portfolios, which totaled approximately \$18.6 billion pre-tax, was primarily attributable to the holdings of the company’s insurance subsidiaries. This loss was a substantial contributor to AIG’s loss in the fourth quarter of 2008. The remainder of the fourth quarter loss was significantly associated with the mark to market of certain assets transferred during the quarter to two special purpose vehicles established by the Federal Reserve to help relieve the capital and liquidity pressure on AIG from exposure to those assets, losses due to accounting on securities lending transactions that occurred during the fourth quarter, impairment of deferred tax assets and goodwill, and other market valuation losses. At the same time, general economic weakness along with a tendency of the public to pull away from a company that it viewed as having an uncertain future, hurt AIG’s ability to generate new business during the second half of 2008 and caused a noticeable increase in policy surrenders.

² These reports are available on the Board’s public website at http://www.federalreserve.gov/monetarypolicy/bst_reportsresources.htm. On February 25, 2009, the Board filed a report with the Committees that provided an update on the facilities provided AIG by the Federal Reserve. This report also is available on the Board’s public website at the address indicated.

In addition, the extreme financial and economic conditions that existed during the fourth quarter have greatly complicated and delayed AIG's plans to divest significant parts of the company in order to repay the U.S. government for its previous support. Would-be buyer themselves are experiencing financial strains and lack access to financing that would make such purchases possible. While progress has been made in reducing the risks that would be posed to the financial system by a disorderly failure of AIG, the company continues to pose systemic risks. A disorderly failure of AIG would still impose unnecessary and burdensome losses on many households and businesses, would deepen and extend market disruptions and asset price declines, further constrict the flow of credit to households and businesses in the United States, and materially worsen the recession the economy is enduring.

March 2009 Restructuring Authorizations

In the context of this backdrop, on March 2, 2009, the Treasury Department and the Board announced a restructuring of the government's assistance to AIG in order to stabilize this systemically important company in a manner that best protects the U.S. taxpayer. These actions are designed to help stabilize the company and the financial system, enhance the company's capital and liquidity, and facilitate the orderly completion of the company's global divestiture program. Importantly, these restructuring actions also will begin to separate the major non-core businesses of AIG. The long-term solution for the company, its customers, the U.S. taxpayer, and the financial system is the orderly restructuring and refocusing of the firm.

Capital Investment by the Treasury Department

A key component of the restructuring involves the provision of new preferred equity capital to AIG by the Treasury Department, and a change in the terms of the perpetual preferred shares acquired by the Treasury Department in November 2008. In particular, the Treasury Department will create a new equity capital facility for AIG pursuant to which it may obtain up to \$30 billion of capital as needed over the 5-year life of the facility in exchange for newly-issued non-cumulative preferred stock. The preferred stock issued to the Treasury Department under this facility will pay a non-cumulative dividend of 10 percent per year, and will have certain limited voting rights if AIG does not pay dividends on the preferred for four periods, whether consecutive or not. The Treasury Department also will receive warrants that will entitle the Treasury Department to purchase 1 percent of the common stock of AIG issued and outstanding on the commencement date of the capital facility, subject to customary anti-dilution adjustments.

The Treasury Department also will exchange the \$40 billion of cumulative perpetual preferred shares that it acquired in November 2008 for preferred shares with revised terms that more closely resemble common equity. The new terms will provide

for non-cumulative dividends and limit AIG's ability to redeem the preferred stock except with the proceeds from the issuance of equity capital. Additional information concerning the terms of the additional or modified preferred shares of AIG to be acquired by the Treasury Department are available on the Treasury Department's public website.³

It should be noted that, as required by the Revolving Credit Facility, AIG has issued shares of perpetual, non-redeemable convertible participating preferred stock to a trust that will hold the stock for the benefit for the Treasury Department. Under the terms of the preferred stock issuance, the preferred stock is convertible into AIG's common stock. The conversion formula provides that the Trust will receive 79.9 percent of AIG's common stock on a fully diluted basis, less the percentage of common stock that may be acquired by or for the benefit of the Treasury Department as a result of warrants or other convertible preferred stock held by the Treasury.

Board's Section 13(3) Authorization to Facilitate the Securitization of the Net Cash Flows of Domestic Life Insurance Policies

In conjunction with the Treasury Department's investment authorization, the Board authorized the Reserve Bank to extend, pursuant to section 13(3) of the Federal Reserve Act, up to approximately \$8.5 billion in credit to special purpose vehicles ("SPVs") to be established by domestic life insurance subsidiaries of AIG. The SPVs would repay the loans from the net cash flows they receive from designated blocks of existing life insurance policies held by the parent insurance companies. The total amount of principal and interest due to the Federal Reserve on this credit would represent a fixed percentage of the estimated net cash flow from the underlying policies that would flow to the borrowing SPVs. This "buffer" between the amount of the Federal Reserve's credit extension and the net cash flows from the insurance policies will provide the Federal Reserve with security and provide reasonable assurance of repayment.

The proceeds of the new credit extensions will be used by AIG to pay down an equivalent amount of the company's outstanding borrowings under the Revolving Credit Facility. The amounts lent, the percentage subtracted from the par value of the collateral taken by the Reserve Bank, and the other terms of the credit to be extended will be determined based on valuations acceptable to the Reserve Bank following due diligence to be conducted by the Reserve Bank and its advisors. In light of this required valuation process, the buffer that will exist between the estimated net cash flows from the designated blocks of life insurance policies and other expected features of the securitization structure, the Board does not expect at this time that the credit extended under this authorization will result in any losses to the Federal Reserve or the taxpayer.

³ See http://www.treasury.gov/press/releases/reports/030209_aig_term_sheet.pdf.

Other Actions Taken by the Board

In addition to this new authorization under section 13(3) of the Federal Reserve Act, the Board authorized a number of additional actions to reduce and restructure AIG's outstanding debt under the Revolving Credit Facility, which stood at \$38.2 billion as of February 25, 2009. First, the Revolving Credit Facility will be reduced by up to approximately \$26 billion in exchange for preferred interests in two SPVs created to hold all of the outstanding common stock of American Life Insurance Company ("ALICO") and American International Assurance Company Ltd. ("AIA"), two life insurance holding company subsidiaries of AIG. AIG will retain control of ALICO and AIA, though the Reserve Bank will have certain governance rights to protect its interests.

The actual value of the SPV preferred interests received by the Reserve Bank and the amount by which the outstanding obligation of AIG under the Revolving Credit Facility will be reduced as a result of the exchange will be a percentage of the fair market value of AIA and ALICO based on valuations acceptable to the Reserve Bank. The coupon rate, voting rights, and other terms of the preferred equity interests also will be determined after further consultations with AIG and the Reserve Bank. This action would be a positive step toward preparing these two subsidiaries of AIG for sale to third parties or disposition through an initial public offering, the proceeds of which would return to the Federal Reserve through its preferred equity interests in the SPVs that control these two companies.

In addition, the total amount available under the Revolving Credit Facility will be reduced from \$60 billion to \$25 billion. The interest rate payable on outstanding advances under the Revolving Credit Facility, which currently is 3-month LIBOR plus 300 basis points, will be modified by removing the existing floor (3.5 percent) on the 3-month LIBOR rate.

All other material terms of the Revolving Credit Facility will remain unchanged. For example, AIG will remain unconditionally obligated to repay the unpaid principal amount of all advances, together with accrued and unpaid interest thereon and any unpaid fees, on the maturity date. Also, all outstanding balances under the Revolving Credit Facility will continue to be secured by the pledge of a substantial portion of the assets of AIG and its primary non-regulated subsidiaries, including AIG's ownership interest in its regulated U.S. and foreign subsidiaries, as described in the reports previously submitted to the Committees.