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Good morning.

Chair Warren, and members of the Congressional Oversight Panel, thank you for the opportunity to testify today. Since joining the Treasury Department (the "Treasury") in May of 2009, I have been primarily responsible for overseeing the taxpayers' significant investment in American International Group ("AIG" or the "Company"). Prior to joining the Treasury, I spent 28 years working in the private sector focused on financial restructurings.

I am here today in response to the Panel's request for an explanation of the terms of the government's investments in AIG, the evolution of those investments and the strategy for the government's exit. The Treasury is very much a reluctant shareholder, and while we leave the day-to-day management of the Company to the CEO and the Board of Directors, we actively monitor progress on the restructuring front. Our primary goals are to protect the taxpayers' investment in AIG, promote financial stability, and expedite the government's exit.

As of today, the Federal Reserve Bank of New York (the "FRBNY") and the Treasury Department have extended $132.3 billion of financial support to AIG in a variety of forms.[1]

The FRBNY has provided $83.2 billion of this support. This support is in three different forms. First, there $26.3 billion outstanding on the FRBNY loan (the "FRBNY Facility") that was first extended to AIG in September of 2008.[2] Second, the FRBNY holds $25.4 billion of preferred interests in two investment vehicles which hold, respectively, AIG's two largest international life insurance companies, AIA and ALICO (the "AIA and ALICO Preferred Interests").[3] Third, there is $31.5 billion outstanding on loans that the FRBNY made to two other investment vehicles, Maiden Lane 2 and Maiden Lane 3, which purchased certain troubled financial assets from AIG.

The Treasury has provided $49.1 billion of the total support. $41.6 billion of this support is in the form of Series E Preferred and $7.5 billion is in the form of Series F Preferred. The proceeds of the Treasury's preferred stock investments were used to reduce the Company's debt burden, to help buttress the regulatory capital of certain insurance subsidiaries, and to untangle the web of cross-ownership and intercompany funding arrangements between and among AIG and its various subsidiaries.

Finally, the AIG Credit Facility Trust (the "Series C Trust"), established for the benefit of the taxpayers in connection with the original funding of the FRBNY Facility, holds AIG's Series C Preferred, which is convertible into approximately 79.8% of AIG's common stock. The Series C Trust is governed by three independent trustees who act as fiduciaries on behalf of taxpayers.

The purpose of my testimony today is to explain how the taxpayer came to own this varied portfolio of AIG interests and the plan to extract the government from these positions, as soon as practicable.

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[1] This represents the existing outstanding amounts. Currently, there is approximately $12 billion of undrawn capacity under the FRBNY Facility, and approximately $22 billion of undrawn capacity under the Treasury Series F Preferred commitment.

[2] Amount includes accrued fees and interest.

[3] The AIA and ALICO Preferred Interests were taken in transactions that closed on December 1, 2009 in satisfaction of a portion of the debt then outstanding under the FRBNY Facility.

AIG's rescue in September 2008 sought to avoid the catastrophic consequences to our economy and to American families and businesses that would have resulted from its sudden collapse. As a result of necessary government intervention, the taxpayer became a substantial equity holder in AIG, and taxpayers' ultimate recovery on their investment in AIG depends on the strength of the Company's underlying insurance subsidiaries. Today, AIG is a "going concern" [4] with an "A-"[5] investment grade rating only because of government support. Therefore, the objective of the restructuring plan is to restructure AIG's balance sheet and business profile so that it can maintain this status on its own, thereby permitting the government to monetize the taxpayers' investment.

As a substantial equity holder in AIG, the taxpayers' ultimate recovery on its equity interests in AIG depends on the ability of AIG's management to improve the results of its core insurance businesses. Together with the trustees of the Series C Trust, the government has worked with the Company to recruit an almost entirely new Board of Directors,[6] a new CEO, a new Chief Risk Officer, a new General Counsel and a new Chief Administrative Officer. All of these executives and directors are committed to the objective of protecting the taxpayers' investment in the Company and paying back the taxpayers as promptly as practicable.

The mechanics of the restructuring plan itself are relatively straightforward in concept: sell sufficient assets at fair prices to pay off AIG's obligations to the FRBNY, streamline AIG's business portfolio, and recapitalize AIG's balance sheet to support investment grade status without the need for ongoing government support. At that point, the Company will be a simplified life, property and casualty insurer with solidly capitalized insurance subsidiaries, adequate liquidity, and a stable balance sheet. Executing this plan will enable the government to sell its equity interests in the Company as soon as market conditions permit.

The Structure of USG Assistance

On September 16, 2008 the government committed to provide unprecedented assistance to AIG. In the absence of such assistance, AIG would have then defaulted on more than $2 trillion notional of derivative obligations and on over $100 billion of debt to institutions. Those defaults would have inevitably forced AIG to commence Chapter 11 proceedings for itself, its Financial Products subsidiary (AIGFP), its aircraft leasing subsidiary, and its consumer finance subsidiary.

The initial decision to loan money to AIG fell to the Federal Reserve because, at that time, no one else could act in the same manner as the Federal Reserve. The Emergency Economic Stabilization Act (EESA) was not authorized by Congress until October 2008, and none of the agencies with supervisory authority over AIG had any tools to help directly meet the funding requirements of AIG. No one in the federal government had a mechanism, as we do for banks, to provide for the orderly unwinding, dismantling, selling, or liquidating of a global, non-bank financial institution like AIG.

[4] In accounting terminology "going concern" refers to a company's ability to continue functioning as a business entity.
[5] Throughout this testimony Standard & Poor's ratings are used as a proxy for all agencies that rate the Company's debt.
[6] The Series C Trust has elected 11 of the 13 existing board members. The two remaining directors were nominated and elected by the Treasury pursuant to rights under the documents that govern the Treasury's Series E and Series F Preferred shares.

Many observers, with the benefit of hindsight, have concluded that AIG could have been handled differently. Some have suggested that AIG should have simply been allowed to file for bankruptcy and let the losses fall where they may so as to diminish "moral hazard." Others have suggested that AIG could have negotiated a prepackaged plan of reorganization with its creditors and fixed itself without government support. Finally, there has been the suggestion that the government should have structured its rescue financing so as to protect the valuable insurance franchises without protecting the creditors who enabled and underwrote the growth in AIG's leverage.

My colleagues at the Treasury and the FRBNY have devoted thousands of hours over the past year and a half to try to maintain the Company's stability in extremely volatile markets while also de-risking and deleveraging the Company so as to protect the taxpayers' substantial investments. I am convinced today—with the benefit of hindsight and significant experience with AIG, the Treasury, and the FRBNY—that the support provided to the Company in the fall of 2008 was the only responsible and viable option on the table. I will explain why as I address certain suggested alternatives and illustrate the challenges that we still face as we attempt to exit the taxpayers' extraordinary investments in AIG.

Many observers have argued that AIG simply should have been left alone to fail and file for bankruptcy. By virtue of both the size of its balance sheet and the nature of its liabilities, an AIG bankruptcy in September of 2008 would have been catastrophic to global financial and insurance markets.

AIG was one of the largest life insurers in the United States. An uncoordinated bankruptcy filing and the consequent seizure of AIG's insurance subsidiaries could have had devastating "run" effects.[7] In rehabilitation or wind down proceedings for AIG's subsidiaries, AIG's policyholders' access to the cash and the surrender values of their life and annuity policies would have been restricted as regulators sorted out the adequacy of capital and reserves to pay all claims in full. As those restrictions became widely known, other life and annuity providers could have experienced a sharp increase in surrenders and redemptions, forcing those firms to meet the run against them with asset sales of their own. That, of course, would have put even further pressure on markets.

AIG's failure directly threatened the savings of millions of Americans. AIG had provided financial 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. Doubts about the value of AIG life insurance products could have generated doubts about similar products provided by other life insurance companies, and opened an entirely new channel of contagion.

Upon the filing of a bankruptcy petition by AIG, holders of hundreds of billions of dollars of financial assets "insured" by AIGFP would have been entitled to: (i) immediately terminate their

[7] Total weekly surrenders in AIG's Retirement Services division spiked to almost $800 million per week in the fall of 2008, before returning to a normalized level of $200 million per week after the November 2008 TARP investment.

insurance contracts with AIG,[8] (ii) apply the collateral AIG had previously posted with them to their termination claims against AIG, and (iii) offset remaining contractual claims they had against AIG against any other obligation they might owe AIG on any other qualified financial contract.

The market consequences of this rapid unwinding of AIG's credit insurance would have been severe. Having lost the benefit of AIG's insurance or "wrap" on hundreds of billions of dollars of credit instruments, AIG's counterparties would have sought to replace the insurance if it were available, or (because such insurance was largely unavailable in September of 2008) to sell the underlying credit instruments so as to mitigate future losses. The widespread sale of hundreds of billions of dollars of a concentrated class of financial assets would have created significant incremental downward selling pressure on financial assets, amplifying the selling panic that had already started following the Lehman bankruptcy. Of equal concern, the default by AIG and AIGFP on more than $100 billion of institutional indebtedness, including $15 billion of commercial paper and $85 billion of short-term repurchase obligations,[9] would have exacerbated the stresses in the money market and repo markets driven by Lehman's bankruptcy.

At that time, with the world economy under severe stress, the failure of a large, global, highly-rated financial institution that had written hundreds of billion dollars of insurance on a range of financial instruments would have dramatically amplified the crisis. Investors around the world would have pulled back from funding, out of fear that other financial institutions would fail as well. Investors would have completely lost confidence in their ability to evaluate the financial sector and distinguish between firms that were viable and those that were not. Financial firms would have been forced into even more dramatic selling of assets.

This damage would have rapidly spread beyond Wall Street. Borrowing costs for businesses would have increased dramatically, the value of pension funds would have fallen even more sharply, and job losses would have skyrocketed. While the decision to save AIG was not an easy one, it was a better choice for the American people than letting it fail.

Some have suggested that the choice between rescue and bankruptcy is a false one and that the government could have helped to arrange a prepackaged bankruptcy. As a way to shorten the Chapter 11 restructuring process, prepackaged plans only have a chance of success if there is sufficient time, before a company defaults, to organize creditors into a negotiating committee, and to negotiate and agree on a comprehensive restructuring plan which can be implemented in an expedited proceeding before the bankruptcy court.

At the end of 2008, in my private sector role as a financial advisor to companies experiencing financial distress, I negotiated just such a prepackaged plan of reorganization for Charter Communications, using the urgency of the financial crisis and Charter's imminent default to accelerate a normally cumbersome, time consuming process. However, even on that accelerated basis, it still took three months to negotiate and agree on the restructuring plan and another six

[8] Under the qualified financial contract exceptions to the automatic stay provisions of the Bankruptcy Code otherwise applicable to creditors in a Chapter 11 proceeding.
[9] Includes securities lending obligations.

months to implement it through the courts (and Charter was only a fraction of the size and complexity of AIG).

In the second week of September 2008, barely a week before AIG would have defaulted on hundreds of billions of dollars of obligations, the FRBNY, having had no previous regulatory or supervisory authority over AIG or AIGFP, simply had no time to organize AIG's thousands of creditors into an effective negotiating committee, let alone negotiate a plan of reorganization with them and implement it.

In addition, the impracticality of a prepackaged plan process for AIG was not merely about timing. Rather, there was a more fundamental problem. AIG's revenues and funding depend on its customers' and lenders' perception of its long-term viability. Unlike a manufacturing company, or a retailer, or a cable company like Charter, the stability of a financial institution like AIG depends entirely on its customers' and counterparties' confidence that it will be "good for the money." A manufacturer or a retailer or a cable company can continue to sell its products through the restructuring of its balance sheet so long as it has cars, clothes or a cable signal to sell. A financial institution like AIG cannot.

A balance sheet restructuring involving the compromise of its debt obligations, whether in or out of formal bankruptcy proceedings, is fundamentally inconsistent with the basic commitment that an insurance company gives to its customers: that it has the financial wherewithal to honor a long-term payment obligation. To seek to compromise indebtedness or to compromise counterparties' credit insurance claims is fundamentally inconsistent with what an insurance company is trying to sell to its customers – its ability to pay valid claims in full as they come due.

For illustrative purposes, assume that:

i. There existed a regulatory regime in which someone had robust supervisory authority over AIG,
ii. That regulator was vigilant and ready to prompt the Company to take actions to improve its capital position well ahead of its potential ratings downgrade,
iii. AIG's thousands of creditors could have been organized into an effective negotiating committee well in advance of its possible default, and
iv. AIG's insurance regulators in the United States and in the 130 countries in which its insurance subsidiaries operate could have been convinced to forebear from ring-fencing the subsidiaries' assets or from pushing them into protective rehabilitation proceedings while AIG negotiated with its creditors.

Even assuming all four of these held true, the highly public negotiations among creditors and regulatory uncertainties would have completely undermined the viability of AIG's insurance businesses. This is because, at the first hint of financial distress (such as any public announcement that the Company had commenced negotiations with its creditors over the potential restructuring of their debt), AIG's ability to sell new insurance policies would have evaporated. Equally, redemptions of old policies would have accelerated. Together, the loss of new sales and the increase in redemptions would have quickly created a huge drain on the insurance subsidiaries' liquidity. Similarly, short-term creditors, such as AIG's securities lending counterparties, would have refused to roll over their loans, demanding immediate payment to avoid being caught up in AIG's prepackaged plan negotiations. That "run" on AIG and its subsidiaries' liquidity would have been a regulatory trigger, forcing the hands of regulators to protect all policyholders by ring-fencing the insurers' assets or, in the extreme case, forcing the insurer into wind down proceedings.

The rating agencies would also have complicated, if not completely undermined, the possible success or utility of a prepackaged plan. Upon the announcement of a prepackaged plan, under the rating agencies' "distressed exchange" guidelines, AIG at the very least would have immediately been put on "watch negative" and, at the commencement of any plan that sought to reduce AIG's debt burden by paying AIG's creditors less than what they were owed, the rating agencies would have immediately downgraded AIG below investment grade. Further downgrades would have triggered additional collateral calls at AIGFP, putting AIG's liquidity under stress. The policyholder run on AIG's insurance subsidiaries and the counterparty run on AIGFP would have started in earnest before the prepackaged plan could be put to vote.

In my opinion, there were only two practical choices in September of 2008: (i) allow AIG to fail and put the entire financial system at risk of collapse, or (ii) fund AIG to avoid the severe financial maelstrom that would otherwise have ensued had it filed for bankruptcy.

Some have suggested that the rescue should have been structured so as to protect the valuable insurance franchises without protecting the creditors who enabled and underwrote the growth in AIG's leverage. In September 2008, there was no TARP authority nor was there any other federal government mechanism to provide for the orderly dismantling of a large, systemic, non-bank financial institution like AIG. This made it impossible to decouple the ratings of the insurance subsidiaries from the AIG parent company, and therefore impossible to extract concessions from the parent company's creditors without impairing the operating abilities of the insurance subsidiaries.

This situation could have been avoided if certain of the elements of financial reform advancing in Congress had been in place then. Despite regulators in 20 different states being responsible for the primary regulation and supervision of AIG's U.S. insurance subsidiaries, despite AIG's foreign insurance activities being regulated by more than 130 foreign governments, and despite AIG's holding company being subject to supervision by the Office of Thrift Supervision, no one was adequately aware of what was really going on at AIG. If there had there been a systemic regulator with robust oversight authority over AIG and AIGFP in the years preceding September 2008, that regulator would have been in a position to constrain AIG's risk taking. It could have imposed higher capital and liquidity requirements on AIG in the run up to the crisis, and if so AIG might never have needed government support. Both the House and Senate versions of financial reform provide such authority.

Moreover, had the resolution authority included in the regulatory reform bills been available in the fall of 2008, any support from the government that was needed would have taken an entirely different path. For example, if the systemic regulator had been required to supervise the coordination of a resolution plan involving AIG's insurance regulators, it could have pre-arranged the ownership transfer of certain insurance subsidiaries in the months leading up to

AIG's liquidity shortfall. Then, when AIG failed, the systemic regulator could have formed a "bridge bank" and transferred – with all necessary insurance regulatory approvals secured in advance – all of AIG's valuable operating businesses to it. Government financial support would have then been effectively secured by the unencumbered assets of those operating businesses, and limited to the amounts necessary to bridge the insurance subsidiaries' liquidity needs. This would have effectively decoupled the ratings of the insurance subsidiaries from the rating of the AIG parent company, and would have ensured that AIG's unsecured creditors received a recovery only after government support had been repaid.

The comprehensive financial reform legislation proposed by the Administration and advancing in Congress would remedy both deficiencies.

First, the government needs the ability to limit risk-taking for institutions that threaten the overall stability of the system and can cause extraordinary damage to the American economy. The government needs this ability not just for banks, but for institutions that operate like banks. These non-bank financial institutions existed alongside banks and yet were not subject to those constraints in the period leading up to this crisis. The government also needs to make sure that regulators have accountability and flexibility, and that they enforce sensibly-designed constraints on risk. The systemic regulatory authority that is part of financial reform addresses these needs.

Second, the government must have the ability to resolve failing major financial institutions in an orderly manner, with losses absorbed not by taxpayers but by equity holders, unsecured creditors and, if necessary, other large financial institutions. This resolution authority would allow an orderly response to a potential future crisis, protecting both the taxpayer and the overall economy. Both the Senate and House versions of financial reform generally include such tools.

The Evolution of Government Support

Forced to fund AIG's immediate liquidity needs, the government structured its rescue financing as secured debt; that is, amounts outstanding under the FRBNY Facility have priority against the value of AIG's unrestricted assets. That structure protected taxpayers in the short term if AIG had proved not to be viable in the longer term. Fortunately, AIG is proving to be viable. In addition, the FRBNY took nearly 80% of AIG's fully diluted common equity[10] to provide additional compensation to taxpayers for their assistance, and to penalize the shareholders of the Company for the fact that the Company had no alternative but to ask the government for extraordinary assistance.

The FRBNY Facility solved AIG's immediate liquidity problems, but did not alleviate the pressure on its long term credit ratings. By having drawn down a substantial amount of the FRBNY Facility to meet its cash requirements, AIG's debt to equity ratio[11] became inconsistent with its investment grade rating. A further downgrade would have brought with it the potential of significant incremental collateral calls and termination payments at AIGFP. Similarly, given the link between the parent's and insurance subsidiaries' ratings, if the parent company was

[10] In the form of the Series C Preferred Stock placed into the Series C Trust for the benefit of the taxpayer, convertible into 79.8% of the fully-diluted AIG common equity.
[11] A company's debt to equity ratio is a fundamental metric by which credit rating agencies derive corporate credit ratings.

downgraded below investment grade, it could have been the death knell to the insurance subsidiaries' abilities to write new business. A substantial and immediate reduction in the amounts outstanding under the FRBNY Facility was required to avoid another downgrade. With TARP authority having become available in early-October 2008, the Treasury injected $40 billion of preferred equity into the Company in November 2008. This allowed AIG to reduce the outstanding debt under the FRBNY Facility and increase its equity by an equal amount. This avoided downgrade and was essential for protecting the taxpayers' investment in the Company.

At the same time, to protect AIG's balance sheet against further mark-to-market losses on the RMBS portfolio it had acquired as part of its securities lending activities, and to protect AIG's liquidity position against further collateral calls arising from the deterioration in the market prices of the CDOs on which AIGFP had written credit insurance, the FRBNY created Maiden Lane 2 and Maiden Lane 3, respectively.[12]

While the actions taken in November 2008 left AIG with sufficient liquidity to weather the continuing deterioration of the credit and equity markets, its record fourth quarter losses due to deterioration in its asset portfolio (in excess of $60 billion) prompted AIG's auditors and rating agencies to require incremental equity in order to ensure that it had sufficient liquidity. Failure to obtain such a commitment would have led to a "going concern" qualification on its annual audit opinion,[13] and with that qualification, the failure of the Company. To solve this problem, the Treasury committed in April 2009 to purchase nearly $30 billion of AIG preferred stock if and when such funds were needed in the future. Since that time, AIG has requested and the Treasury has purchased $7.5 billion of the Series F Preferred. At all points since April 2009, the Company's auditors have required the Treasury to reiterate its commitment to fund the Series F Preferred – up through and including the Company's first quarter 2010 financials.[14] Without this continuing support, the auditors would issue a "qualified opinion," the rating agencies would downgrade the Company, and the taxpayers' investment would be severely impaired.

The AIG Restructuring Plan

To protect the taxpayers' now substantial investment in AIG, the restructuring plan must ultimately ensure that public confidence in AIG is restored. The Company's policyholders must be confident that AIG will be able to pay claims. The people and firms that lend money to AIG must be confident that they will be paid back. All stakeholders must be confident that AIG can independently meet all of its obligations, in full, as they come due. This is the concept upon which "investment grade status" is built, and this why the restructuring plan is centered on the maintenance of this status.

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[12] On January 27, 2010 Secretary Geithner testified before the House Committee on Oversight and Government Reform regarding the Maiden Lane investment vehicles. Please see that testimony for a more robust discussion of the formation of Maiden Lane 2 and Maiden Lane 3.

[13] The company's auditor must consider whether the use of the going concern assumption is appropriate, and whether there are material uncertainties about the entity's ability to continue to operate as a going concern that need to be disclosed in the financial statements. An auditor who concludes that substantial doubt exists with regard to the appropriateness of the going concern assumption is required to issue an opinion reflecting this – a "going concern qualification."

[14] Currently, there is approximately $12 billion of undrawn capacity under the FRBNY Facility and approximately $22 billion of undrawn capacity under the Treasury's Series F Preferred commitment.

The reason for this is simple: businesses and consumers do not buy insurance products from firms whose long-term viability is in question. Credit ratings are a short hand by which consumers and businesses alike evaluate an insurance companies' financial condition and its prospects. An investment grade rating represents a ratings agency's assessment, upon which businesses and consumers alike rely, that there is a very low probability that the entity will default on its long-term obligations. All of the Company's primary competitors in the property and casualty insurance market are rated "A-" or higher,[15] making it impossible to compete in this market without an investment grade rating.

The need to maintain an investment grade rating makes it extremely complicated, and perhaps impossible, to pursue the creditor negotiations that some have advocated should have been pursued with AIG's CDO counterparties in connection with the creation of Maiden Lane 3. The promise of full payment is the very essence of an investment grade credit rating. To act in any way inconsistent with that promise, such as by trying to coerce counterparties to give concessions on their credit insurance claims, as the agencies have made clear in their criteria governing "distressed exchanges," is a path to a downgrade.

As the last eighteen months have unfolded, the rating agencies have begun to clarify the interaction between their rating for AIG and the substantial government support it has received. Currently, as a result of the government's financial support, AIG enjoys an upward "notching" of its ratings above what it would otherwise receive on a standalone basis. Standard & Poor's has provided the most detailed public description of this relationship, specifying that the Company receives a five-notch uplift due to government financial support. In April 2010, S&P reaffirmed the Company's ratings and indicated that, absent government support, the Company would have a senior unsecured rating of BB, which is two notches below investment grade.

In order to regain a standalone "A" rating the Company needs to eliminate this gap. The elimination of that gap is a key objective of the government's resolution plan for AIG. Once AIG can maintain an investment grade rating without government support, the government can begin to sell down its equity interests in the Company. This requires substantial improvements to AIG's operations and to its leverage and capital profile. The essential elements of the resolution plan are as follows:

First, the Company will have to substantially reduce its debt. The two metrics by which this is measured are (i) "leverage," which is the amount of debt on a company relative to the amount of equity in a company, and (ii) "coverage," which is the amount of earnings or cash flow the company generates relative to the annual interest payments on its debt.

Next, the Company will have to demonstrate independent access to the capital markets and secure standby lines of credit. Policyholders, potential customers and investors must be confident that the Company has access to liquidity in times of potential stress. Finding a private market participant or facility to replace the government's support will be a key milestone.

Third, the risk profile of AIGFP will need to be reduced to the level where potential losses are inconsequential to the parent company's financial condition. More specifically, investors must

[15] Primary competitors include Ace Group, Chubb Group, Hartford, Liberty Mutual, Travelers, XL, and Zurich.

be satisfied that AIGFP does not pose a substantial threat to the Company's liquidity position, even in times of stress.

Fourth, AIG will need to divest those subsidiaries that are deemed to be non-core to its long-term strategy, and it will need to deconsolidate any businesses whose potential cash needs represent a potential drag on the AIG parent company.

Fifth, the Company will have to demonstrate that its core insurance subsidiaries are profitable, well capitalized, and have repaired the damage to the franchise caused by the financial crisis and the negative attention that the government's rescue has generated.

Finally, the Company will have to demonstrate that it has improved its risk management policies and procedures. In short, AIG will have to demonstrate that it can appropriately identify, monitor, manage and mitigate the risks inherent in its operating businesses.

Taxpayer Exit

Taxpayer exit from AIG will be in a series of steps. We expect that AIG will sell sufficient assets at fair prices to pay off obligations to the FRBNY, and the assets of Maiden Lane 2 and 3 will continue to generate cash flows sufficient to repay the loans FRBNY made to those entities. We expect that AIG will streamline its business portfolio and reduce its debt to a level that is consistent with an "A" rated company. This will enhance the value of the taxpayers' equity interests in AIG, and the Treasury will then seek to sell these interests as soon as practicable.

Asset Sales

In March 2010 the Company reached a substantial milestone, having signed separate definitive agreements to sell its two largest international life insurance subsidiaries – AIA to Prudential PLC and ALICO to MetLife. Prudential PLC is currently seeking shareholder and regulatory approvals for its $35.5 billion purchase of AIA, and MetLife is seeking regulatory approvals for its $15.5 billion purchase of ALICO. Combined with the additional financings and asset sales that the Company is currently pursuing, the proceeds from these two sales are expected to be sufficient to pay off the Company's obligations to the FRBNY in full: that is, the FRBNY Facility ($26.3 billion) and the AIA and ALICO Preferred Interests ($25.4 billion).

The consummation of the AIA and ALICO sale transactions will be a significant step on the path towards a standalone investment grade rating. First, the transactions will eliminate over $50 billion of "senior" debt, significantly reducing AIG's leverage. Second, by repaying the FRBNY Facility in full, the Company will free up assets that AIG can then use to secure new lines of credit with commercial banks — facilitating access to independent, non-governmental sources of liquidity.

AIGFP

While the Company works to close the divestitures of AIA and ALICO, it is also continuing to wind down AIGFP. The Company has reduced the notional amount of derivatives at AIGFP from $2.0 trillion in September of 2008 to $755 billion.[16] Similarly, AIGFP has reduced total number of trade positions from 44,000 to 14,300.

[16] As of March 31, 2010.

When you look specifically at credit derivatives, the notional amount of exposure has been reduced from nearly $400 billion to $136 billion. $109 billion of this remaining exposure relates to transactions with European banks, whereby AIGFP provided regulatory capital relief to these banks under the Basel I regime. Thus far, these positions have generally been eliminated at no cost to AIGFP.

With respect to AIGFP's other derivative exposures, the firm has made significant progress towards removing complex and illiquid positions – an important step because these positions would be the most challenging to manage over time. These removals ensure that the reductions in notional and trade count metrics are not achieved simply by closing out only the most "plain vanilla" derivatives exposures.

While several hundred billion dollars of notional amount of positions will remain on AIGFP's books at year-end, most will be hedged positions that do not pose a threat to the Company's rating profile or, more importantly, the financial system. Overall, the wind down of AIGFP's riskiest positions is expected to be largely completed by year-end 2010. The wind down of AIGFP has already significantly reduced the interconnectedness between the Company and other large financial institutions — reducing the risk that, in the future, AIG could pose a systemic threat.

Non-Core Asset Sales and Divestitures

The Company continues to explore opportunities to divest itself of its non-core businesses and deconsolidate subsidiaries that represent a drag on the parent company's ratings. These actions will reduce potential liquidity or capital drains from the parent company and strengthen AIG's independent credit profile. After the consummation of the AIA and ALICO sales and the divestiture of other non-core businesses and assets, the Company will be a streamlined version of the financial behemoth it once was. The largest remaining core businesses will be AIG's property and casualty insurance business (Chartis) and AIG's life and retirement services business in the United States (SunAmerica Financial). Overall, the reduction in both the number and diversity of its business units as well as the shrinking of its geographic footprint will make the Company easier to monitor and to manage.

Maiden Lane 2 and 3

The FRBNY loans to the Maiden Lane 2 and Maiden Lane 3 vehicles will be repaid over time as the assets in those vehicles generate income and are sold or otherwise retired. According to current projections, it is expected that cash inflows from those assets will significantly exceed the principal and interest due on the outstanding FRBNY loans to those entities. Even under a very adverse set of assumptions, it is expected that the loans made by the FRBNY to each of the entities will be paid in full. Currently, the fair value of the Maiden Lane 2 assets is $15.8 billion versus a FRBNY loan balance of $14.9 billion. The fair value of Maiden Lane 3 assets is $23.4 billion versus a FRBNY loan balance of $16.6 billion.

Taxpayer Recovery

Of course, the key question with respect to AIG is whether taxpayers will get all of their money back. Let me review the current prospects.

If the AIA and ALICO divestitures close as planned, proceeds of those sales are expected to be sufficient to repay the FRBNY Facility and redeem the AIA and ALICO Preferred Interests held by FRBNY almost in full. Any shortfall will be made up by other non-core asset sales that the Company is currently pursuing. It is likely that the FRBNY loans to Maiden Lane 2 and 3 will not only be fully repaid, but could also earn a profit. As a result, it seems likely that all of the credit extended by the FRBNY to AIG will be repaid in full.

At current market prices, the common stock that the Series C preferred shares represents has value.[17] Market conditions can change before the Series C Trustees have the opportunity to sell those shares and, given the number of shares that the Series C represents compared to shares currently held by the public, the sale itself may put some significant downward pressure on the trading price of AIG's common stock. That said, given today's market prices it seems that the Series C Preferred has value that will inure to the taxpayers' benefit.

That leaves the Treasury's Series E and Series F preferred equity interests (together, approximately $49 billion). The recovery on the Series E and F will largely depend on the performance of the then-remaining businesses in the AIG portfolio after it completes its asset sales and how they are valued in the stock market.

With AIA and ALICO divested, AIG's core businesses will be centered on Chartis (its global property and casualty insurance business) and SunAmerica Financial Group (its U.S. life and retirement services business). Chartis is one of the largest property and casualty insurers both in the U.S. and globally, and holds leading positions in both commercial insurance and specialty lines. SunAmerica Financial is a leading player in the U.S. life insurance and annuity sector, and a provider of comprehensive retirement services — primarily in the education and healthcare markets.

The Company has work to do in order to return these businesses to their previous levels of profitability, and it will take time to repair fully the damage to their franchises, particularly in the United States. That said the Company's progress to date is encouraging. At Chartis, first quarter 2010 operating income was $879 million (versus $710 million in the first quarter of 2009).[18] Premium retention has risen, pricing has stabilized and employee turnover has reverted to normal levels. At SunAmerica, first quarter 2010 operating income was $1.1 billion (versus a loss of $160 million in the first quarter of 2009).[19] Aggregate assets under management in the retirement services businesses have increased and premiums in the life insurance businesses have stabilized.

While it remains unclear what the Treasury's ultimate recovery on its Series E and F preferred interests will be, it is clear that the prospects for the recovery on those interests have improved, and the government remains committed to protecting the value of these taxpayer investments. The steps taken during the crisis were solely to prevent further financial contagion, and

[17] The Series C Preferred shares are convertible into 79.8% of AIG's common stock. At the closing price of $34.49 on May 25, 2010, the market capitalization of the publicly held AIG common stock, which represents 20.2% of the fully-diluted common equity (i.e., the amount not controlled by the Series C Trust), is approximately $5 billion.

[18] Before net realized capital gains and losses.

[19] Before net realized capital gains and losses.

ownership of AIG was a byproduct of these steps. As the government exits it seeks to do so in a manner that recoups as much money for the taxpayer as possible.

The timing of the Treasury's ability to monetize its investments in AIG will depend on the pace at which the other steps of the resolution plan outlined earlier in my testimony are accomplished. Whether the taxpayers ultimately recover all of their investment or make a profit will depend on the Company's operating performance and market multiples for insurance companies at the time the government seeks to monetize the taxpayers' stock interests. But AIG has made significant progress towards being able to garner standalone market confidence, without the government's continuing support. And as soon as we are confident that the stability is durable we will move to exit the taxpayers' investments as promptly as practicable.

Thank you very much for your time.