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GAO

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Highlights

Highlights of GAO-09-975, a report to congressional committees

TROUBLED ASSET RELIEF PROGRAM

Status of Government Assistance Provided to AIG

Why GAO Did This Study

GAO's seventh report on the Troubled Asset Relief Program (TARP) focuses on the initial assistance the government provided to American International Group, Inc. (AIG)—an organization with over 200 companies operating in over 130 countries and jurisdictions and $830 billion in assets—in September 2008 and the restructuring of that assistance in November 2008 and March 2009. The unfolding crisis threatened the stability of the U.S. banking system and the solvency of a number of financial institutions, including AIG. In September 2008, downgrades of AIG's credit rating prompted collateral calls by counterparties and raised concerns that a rapid and disorderly failure of AIG would further destabilize the markets. As a result, the Board of Governors of the Federal Reserve System (Federal Reserve) authorized the Federal Reserve Bank of New York (FRBNY), in consultation with the Department of the Treasury (Treasury), to provide assistance to AIG. This report describes (1) the basis for the federal assistance, (2) the nature and type of assistance and steps intended to protect the government's interest, and (3) selected GAO-developed indicators of the status of federal assistance and AIG's financial condition.

To do this, GAO reviewed signed agreements and other relevant documentation from the Federal Reserve, FRBNY, Treasury, and AIG and interviewed their officials, among others. To develop the indicators, GAO reviewed rating agencies' reports, identified critical activities, and discussed them with the above named agencies and AIG.

Treasury had no substantive comments on the report. It provided technical comments along with the Federal Reserve, FRBNY, and AIG.

View GAO-09-975 or key components.
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What GAO Found

The Federal Reserve and Treasury provided assistance to AIG to limit further disruption to financial markets. These agencies determined that market events could have caused AIG to fail, which would have posed systemic risk to the financial system. According to the Federal Reserve, a disorderly failure of AIG would have contributed to higher borrowing costs and additional failures, further destabilizing fragile financial markets. The Federal Reserve and Treasury determined that an AIG default would place considerable pressure on AIG's counterparties and trigger serious disruptions to an already distressed commercial paper market. They concluded that because AIG was a large seller of credit default swaps—protection against losses from defaults—on collateralized debt obligations (CDO), had AIG failed, its counterparties would have been exposed to large losses if the values of the CDOs had continued to decline and AIG defaulted on its contracts. The Federal Reserve intended the initial September 2008 assistance to enable AIG to meet these added obligations with its counterparties and begin the process of selling business lines to raise monies to repay the government and resolve other liabilities. Subsequent assistance in November 2008 and March 2009 was intended to augment these goals, support liquidity needs, and repay FRBNY while mitigating disruptions in the broader financial markets.

To address systemic risk that could result if AIG were to fail, the Federal Reserve and Treasury made over $182 billion available to assist AIG between September 2008 and April 2009. As of September 2, 2009, AIG's outstanding balance of assistance was $120.7 billion. Some federal assistance was designated for specific purposes, such as a special purpose vehicle to provide liquidity for purchasing assets such as CDOs. Other assistance, such as that available through the Treasury's Equity Facility, is available to meet the general financial needs of the parent company and its subsidiaries. The table on the next page provides an overview of the total federal assistance to AIG and its related entities. Repayment of the $120.7 billion outstanding government exposure is expected to come from various sources. As of September 2, 2009, $6.8 billion was paid toward principal on the Maiden Lane facilities created by FRBNY to purchase certain AIG assets and provide AIG with liquidity. In providing the assistance, the Federal Reserve and Treasury have taken several steps intended to protect the government's interest. These include making loans that are secured with collateral, instituting certain controls over management, and obtaining compensation for risks such as charging interest, requiring dividend payments, and obtaining warrants. Moreover, Federal Reserve and Treasury staff routinely monitor AIG's operations and receive reports on AIG's condition and restructuring. While these efforts are being made, the government remains exposed to risks, including credit risk and investment risk, which could result in the Federal Reserve and Treasury not being repaid in full.

While federal assistance has helped stabilize AIG's financial condition, GAO-developed indicators suggest that AIG's ability to restructure its business and repay the government is unclear at this time. Indicators of AIG's financial risk suggest that since AIG reported significant losses in late 2008, AIG's operations, with federal assistance, have begun to show signs of stabilizing in mid 2009. Similarly, after a declining trend through 2008 and early 2009, indicators of AIG insurance companies' financial risk suggest improved financial conditions that were largely results of federal assistance. Indicators of AIG's repayment of federal

Overview of Federal Assistance Provided to AIG as of September 2, 2009

Dollar in millions

	Description of the federal assistance	Amount of assistance authorized: Debt	Amount of assistance authorized: Equity	Outstanding balance	Sources to repay the government
Implemented					
Federal Reserve	FRBNY created a Revolving Credit Facility to provide AIG a revolving loan that AIG and its subsidiaries could use to enhance their liquidity. In exchange for the facility, for $0.5 million, a Treasury trust received Series C preferred stock for the benefit of the Treasury, which gave Treasury a 77.9 percent voting interest in AIG.	$60,000[a]		$38,792.5	Proceeds from dispositions of AIG businesses, internal cash flows, and restructuring part of the Revolving Credit Facility from debt into equity. The initial fee paid by AIG was reduced by $0.5 million to pay for the Series C shares and will not be repaid.
	FRBNY created SPV—Maiden Lane II—to provide AIG liquidity by purchasing residential mortgage-backed securities from AIG life insurance companies. FRBNY provided a loan to the SPV for the purchases. It also terminated a previously established securities lending program with AIG.	22,500		16,899	Proceeds from the assets in Maiden Lane II will be used to repay the FRBNY loan to Maiden Lane II.
	FRBNY created a SPV called Maiden Lane III to provide AIG liquidity by purchasing CDOs from AIG Financial Products' counterparties in connection with termination of credit default swaps. FRBNY again provided a loan to the SPV for the purchases.	30,000		20,196	Proceeds from the assets in Maiden Lane III will be used to repay the FRBNY loan.
Treasury	Treasury purchased Series D cumulative preferred stock from AIG. AIG used the proceeds to pay down the Revolving Credit Facility. These shares were later exchanged for Series E noncumulative preferred shares. Unpaid dividends on the series D shares were added to the Treasury's equity in the Series E shares.		40,000	41,605	Proceeds from dispositions of AIG businesses and internal cash flows of AIG.
	Treasury purchased Series F noncumulative preferred shares of AIG and is allowing AIG to draw up to $29,835 million through an equity facility to meet its liquidity and capital needs. Amounts drawn by AIG represent the cost of the federal equity interest in these shares.		29,835	3,206[b]	Proceeds from dispositions of AIG businesses and internal cash flows of AIG.
	Subtotals	**$112,500**	**$69,835**		
	Total authorized and outstanding assistance[c]		**$182,335**	**$120,698.5**	
Pending	AIG created two SPVs to hold the shares of two of its foreign life insurance businesses to enhance AIG's capital and liquidity, and to facilitate an orderly restructuring of AIG. The Revolving Credit Facility will be reduced by the amount of preferred equity interest in the SPVs to be received by FRBNY.	0	(25,000[d])	0	Proceeds from the public sale of the SPVs' common stock could be used to buy out the federal preferred equity and pay down part of the Revolving Credit Facility.
	AIG will create SPVs that will issue up to $8,500 million in notes to FRBNY, which will be funded with a loan from FRBNY. AIG will use the proceeds to pay down part of the Revolving Credit Facility.	(8,500[d])		0	FRBNY's loan to the SPVs will be repaid from net cash flows of the life insurance policies.

Source: AIG SEC filings, Federal Reserve, and Treasury data.

[a]The facility was initially $85 billion but was reduced to $60 billion in November 2008.
[b]Amount as of September 8, 2009.
[c]Does not include AIG's participation in the Federal Reserve's Commercial Paper Funding Facility.
[d]These transactions have not been completed and are not included in the total assistance provided to AIG. The amount of the Revolving Credit Facility will be decreased by an equal amount upon completion.

assistance show some progress in AIG's ability to repay the federal assistance; however, improvement in the stability of AIG's business depends on the long-term health of the company, market conditions, and continued government support. Therefore, the ultimate success of AIG's restructuring and repayment efforts remains uncertain. GAO plans to continue to review the Federal Reserve's and Treasury's monitoring efforts and report on these indicators to determine the likelihood of AIG repaying the government's assistance in full and the government recouping its investment.