



## ALL EYES ON AIG

November 4, 2008

It is common knowledge that the AIG Group is in financial distress due to its heavy involvement with Credit Default Swaps (CDS). CDS are used by insurers to reinsure/guarantee institutions that deal with subprime mortgages. AIG subsidiaries appear to have been huge participants in both.

AIG Group's liability in this area has not yet been made public; but AIG has issued an estimated \$440 billion in CDS. For the record, AIG's Financial Products Division was the primary unit heavily involved in these high risk deals and not the traditional AIG insurers.

The intent of this article is not to articulate the events that caused the high default rate; but to advise the viability of using select AIG Insurers. Therefore, we shall discontinue the subprime mortgage discussion and focus on the viability of AIG Insurers.

Although the AIG Group as a whole is in serious financial crisis, this is one time that care should be taken to segment "AIG Insurers" vs. "AIG all other." Below is a brief overview of the reasons why certain categories of AIG Insurers with reasonable caution are still viable.

**Bottom line**, as long as the AIG company is State regulated and its financials are strong, it is our opinion that it is reasonable to use these AIG insurers. This needs to be examined ongoing and certainly prior to any renewal for the reasons cited below.

Reasons are as follows:

- The AIG Property and Casualty insurers that are regulated by the States appear financially strong. Care should be taken to review the individual carrier's financial strength.
- Federal Bankruptcy laws do not pre-empt State Insurance laws.
- Debtors in possession of AIG cannot seize assets or funds without regulatory approval.
- The parent company can take no more than 10% as an upstream dividend per year.



# ALL EYES ON AIG CONTINUED

The only concern that we see at this time is if the group rating goes down to less than A-. Then a move to a stronger rated insurer is recommended since AIG would look unattractive to reinsurers; and underwriters would be reluctant to go excess of a policy that did not carry an A.M. Best rating of at least A-. We have been advised that AIG is endeavoring to convince the rating Bureaus to provide individual ratings by insurer.

Finally, as an added concern, the terms of the Federal loan are pretty difficult to respond to by AIG and still get healthy – 14% interest on monies AIG draws and 8.5% on the funds it does not use. It has already drawn about \$70 billion plus. And the subprime issue may not be easily quantifiable and can indeed bode disaster for the parent. They may conduct a fire sale, but there does not appear to be anything that can be done by them to hurt the insured within a policy period.

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