HOLDING COMPANY REPORT OF EXAMINATION

June 11, 2007

American International Group, Inc.
70 Pine Street
New York, NY
Docket Number: H2984
Structure Number: S2262

OTS Region	Complex and International Organizations
Type of Examination:	Holding Company Regular
Examination Date	06/11/2007

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Holding Company Structure

Name and Address of Holding Companies	Type of HC	H Number
American International Group, Inc.(AIG)	Diversified-Unitary	H-2984
The Starr Foundation (Starr Foundation)	Diversified-Unitary	H-3574
CV Starr & Co., Trust (Starr Trust)	Diversified-Unitary	H-3575
CV Starr & Co., Inc. (Starr Inc)	Diversified-Unitary	H-3576
Starr International Company, Inc. (SICO)	Diversified-Unitary	H-3577

Thrift Subsidiaries (Name, City, State)	Region	Docket No.
AIG Federal Savings Bank, Wilmington, DE	Northeast	14939

Other Affiliates
21st Century Insurance Group (21st Century)*
AGC Life Insurance Company (AGCL)*
AIG Annuity Insurance Company (AIGA)*
AIG Consumer Finance Group, Inc. (CFG)
AIG Europe SA (AIGE)*
AIG Financial Products Corporation (AIGFP)
AIG Global Investment Corporation (AIGGIC)
AIG Private Bank, Ltd. (AIGPB)*
AIG UK Holdings, PLC (AIGUK)*
American General Corporation (AGC)
American General Finance, Inc. (AGF)
American General Insurance Company (AGIC)*
American Home Assurance Company (AHAC)*
American International Assurance Company, Ltd. (AIA)*
American International Insurance Company (AIIC)*
American International Reinsurance Company, Ltd. (AIRCO)*
American International Underwriters Overseas, Ltd. (AIUO)*
American Life Insurance Company (ALICO)*
International Lease Finance Corporation (ILFC)

Other Affiliates
Lexington Insurance Company (LIC)*
New Hampshire Insurance Company (NHIC)*
National Union Fire Insurance Company of Pittsburgh, PA (NUFI)*
SunAmerica Life Insurance Company (SunAmerica)*
The Hartford Steam Boiler Inspection and Insurance Company (HSB)*
Transatlantic Reinsurance Company (TRC)*
Variable Annuity Life Insurance Company (VALIC)*
United Guaranty Insurance Company (UGIC)*
* Denotes a functionally regulated company reviewed through applicable examination reports and filings.

Office of Thrift Supervision
Department of the Treasury *Complex and International Organizations*

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Washington, DC 20552

October xx, 2007
Mr. Stephen L. Hammerman, Chairman of the Regulatory, Compliance and Legal Committee
American International Group, Inc.
70 Pine Street
New York, NY 10270

Members of Committee:

Pursuant to Section 10 of the Home Owners' Loan Act, we performed a risk-focused examination of American International Group, Inc.

The comments that follow summarize conditions, policies, practices, and trends that affect the risk level of the consolidated enterprise. All matters of criticism, violations of laws and regulations, and other matters of concern identified within this Report of Examination require the Board of Directors and management's timely corrective action.

Information, comments and conclusions contained in this report are based on filings made with the Office of Thrift Supervision or other functional regulators, and the books and records of the holding company and its subsidiaries. We prepared this report for supervisory purposes, and you should not consider it an audit report.

Please review the report in its entirety at your next meeting and note your review in the minutes of that meeting.

If you have any questions, please call me at (202) 906-6035. If I am unavailable, please call Bradley Waring, Director, Conglomerate Operations at (202) 906-6177.

Sincerely,

C.K. Lee
Managing Director,
Complex & International Organizations

Signatures of Directors

We, the undersigned directors of American International Group, Inc. or their representatives, have personally reviewed the contents of this report of examination.

Signature	Date
Robert B. Willumstad, Chairman	
Edmund S.W. Tse, Vice Chairman	
Marshall A. Cohen	
Martin S. Feldstein	
Ellen V. Futter	
Stephen L. Hammerman	
Richard C. Holbrooke	
Fred H. Langhammer	
George L. Miles, Jr.	
Morris W. Offit	
James F. Orr, III	
Virginia M. Rometty	
Martin J. Sullivan	

Signatures of Directors (continued)

Michael H. Sutton

Frank G. Zarb

Note: This form may remain attached to the report of examination and be retained in the holding company's file for review during subsequent examinations or may be sent to the OTS Regional Office.

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Examination Conclusions and Comments

	Current Examination 06/11/2007	Previous Examinations 06/05/2006	05/31/2005
Holding Company Rating	2[a]	S	S

	Current Category	Prior Category
Holding Company Risk/Complexity Category	III	III

We assign American International Group, Inc. (AIG, the company, or the conglomerate) a "2" composite rating. The company has strong capital and earnings, ample organic cash flow, and continued access to the capital markets. The company provides effective strategic, managerial, and capital support to all of its subsidiaries. While the organizational and risk management structures are improved since the previous examination, they require significant further development, prioritization on remediation and modernization projects, and improved communication to the Board to strengthen and ensure a sustainable control structure.

We note and management acknowledges sizeable organizational structure deficiencies in controls, human resources, processes, and systems conglomerate-wide, which impede AIG's efforts to improve risk management, compliance, and governance responsibilities. The deficiencies reflect the magnitude of AIG's previous underinvestment in infrastructure and inefficient organizational design but not its management quality, dedicated employee base, or strong efforts toward remediation. Structural and resource deficiencies persist with business line controls over financial reporting and disclosure, which require significant attention at the corporate level to submitted financial information and a burdensome level of compensating controls. In addition, AIG has not fully deployed its compliance and operational risk functions and consequently has not fully assessed its global regulatory, reputation, and operational risk exposures. AIG must also finalize its full-spectrum catastrophic risk management program with clear reporting to and involvement of the Finance Committee in establishing the firm's risk appetite.

AIG is making progress, although the additional volume and complexity of remedial actions and risk management improvements will take time to fully implement. Appropriately, management and the Board have placed priority on conglomerate-wide financial modernization and organizational simplification efforts to improve controls and financial reporting. We noted substantial progress in several areas of the remediation plan, and AIG implemented most of the recommendations from the prior Office of Thrift Supervision (OTS) Report of Examination (ROE). While management and the board need to address the company's weaknesses, its organizational diversity and financial strength affords the company with time and resources to address the weaknesses in the normal course of business and to withstand adverse business conditions.

[a] OTS published a proposed new rating system for holding companies in the Federal Register on April 9, 2007. Under the proposed new system, OTS rates companies on a scale of 1 through 5. The last page of this report contains definitions of the new ratings scale.

Examination Conclusions and Comments (continued)

This report documents the results of OTS's continuous supervision and examination program for AIG during the period since the previous examination (the review period). OTS categorizes AIG as a complex, diversified, unitary thrift holding company through its ownership of AIG Federal Savings Bank (AIG FSB), an OTS-chartered savings association. The company is subject to consolidated supervision by OTS pursuant to Section 10 of the Home Owners' Loan Act. In addition, OTS is the company's consolidated supervisor[b] under the European Union's (EU) Financial Conglomerates Directive (FCD).

Our continuous supervision and examination program is top-down and risk-focused. It follows the revised CORE assessment framework described in the April 9, 2007 Federal Register notice. This approach includes evaluations of AIG's overall financial condition and capital adequacy, the primary risks facing the firm, and the adequacy of policies, procedures, and risk management controls to measure, monitor, and mitigate significant risk exposures. The approach also assesses the company's organizational structure and risk management including reviews of intra-group transactions, risk concentrations, internal control structure, corporate governance practices, and strategic business initiatives. We base our conclusions on reviews of internally and externally prepared documents and reports; targeted reviews of business lines, subsidiaries, and control activities; and discussions with business unit management, risk managers, functional supervisors, and the company's internal and external audit staff. We also reviewed functional supervisors' reports, filings with the Securities and Exchange Commission (SEC), and rating agency and investment analyst reports.

In our role as the holding company supervisor, we coordinate with domestic and foreign supervisors in areas where AIG is sizably invested or is building its presence. In compliance with the Gramm-Leach-Bliley Act, we also coordinate with functional supervisors responsible for the direct supervision of entities within the holding company structure. Lastly, we coordinate and consolidate conclusions and corrective actions that affect multiple regulated entities, when appropriate. Over the past year, we exchanged information with the French banking and insurance supervisors, Commission Bancaire (CB) and Autorité de Contrôle des Assurances et des Mutuelles (ACAM). OTS also contacted or worked with the Financial Services Agency of the United Kingdom (UK) and Japan, multiple state insurance supervisors in the United States of America (U.S.), and supervisors from Hong Kong, Poland, Taiwan, Singapore, Switzerland, China, and Brazil. Through this interaction, we enhanced our understanding of processes and issues regarding the supervision of AIG's subsidiaries in those jurisdictions.

[b] Because of its operations in the EU, the FCD requires AIG to have a consolidated home country supervisor. For a non-EU based regulator to serve as a consolidated supervisor, an EU coordinating supervisor must make a special designation. AIG's EU coordinating supervisor is Commission Bancaire (CB), who in turn designated OTS as the consolidated supervisor. CB granted OTS equivalency on January 17, 2007.

Examination Conclusions and Comments (continued)

/s/ Thomas J. O'Rourke, F.T.R
Examiner-in-Charge
OTS Complex and International Organizations Division

Matters Requiring Board Attention

The following items require the ongoing attention of the Board to ensure appropriate follow up and ultimate remediation. The Board should:

- Monitor remediation efforts with respect to the income tax accounting material control weakness and the significant control deficiencies relating to the financial close process and Domestic Brokerage Group (DBG) reinsurance. Progress in the latter two efforts has not been consistent.
- Ensure implementation of a long-term approach to solving organizational weaknesses and increasing resources dedicated to solving identified deficiencies. Management should give the highest priority to the financial close remediation and the related long-term solution to financial reporting weaknesses (project FIRE).
- Monitor the continued improvement of corporate control groups ability to identify and monitor risk. Management should complete the holding company level risk assessment, risk metrics, and reporting initiatives and fully develop risk reporting.
- Increase involvement in the oversight of the firm's overall risk appetite and profile and be fully informed as to AIG Catastrophic Risk exposures, on a full-spectrum (credit, market, insurance, and operational) basis.
- Ensure the prompt, thorough, and accountable development of the Global Compliance program, a critical risk control function where organizational structure impediments have delayed program enhancements.

The Board should also review the summary of OTS Targeted Reviews and other recommendations contained throughout this report, which we communicated to respective senior managers of these functions and entities.

Examiner Findings

Major Areas of Review

CAPITAL

Component Rating

We assign AIG a "1" Capital component rating.

Conclusion

AIG's capital position is strong. The consolidated capital level supports the volume and risk characteristics of the conglomerate and its business lines and products; provides a significant cushion to absorb unanticipated losses; and fully supports AIG's level and composition of borrowing and its business plans and strategies. AIG is able to enter capital markets to raise additional capital as necessary. AIG's capital allocation and planning process is adequate and improving. While capital is subject to potential losses from weaknesses in AIG's organizational structure, significant, systemic loss exposure is remote. We make several recommendations for continued development of capital related activities and capital management processes at the end of this section.

Comments and Supporting Analysis

Scope of Review

The examination team assessed the adequacy of AIG's capital using the standards in OTS's Holding Company Handbook. The review considered the amount, quality, and management of AIG's capital resources relative to the conglomerate's overall risk profile and in relation to functional regulatory requirements. Our evaluation relied on information from internal and external sources including AIG's annual and quarterly financial and statistical supplements to its Form 10-Q and 10-K SEC filings as well as filings and reports of rating agencies, financial analysts, and other regulators. We also interviewed AIG personnel, including senior management from enterprise risk management (ERM), internal audit division (IAD), and the Treasury Group. The holding company assigns responsibility for capital and liquidity management to the Treasury Group. The examination team identified and assessed capital management and risk management strategies and controls.

Capital Adequacy

The consolidated capital level, the ratio of capital to assets, and the capital level in excess of aggregate risk-based requirements all increased during the review period due to strong earnings retention, especially in the domestic general insurance and foreign life insurance segments. AIG maintains a strong capital position in relation to risk-based regulatory requirements for subsidiaries and its preliminary Economic Capital Model (ECM) results. Capital is also sufficient in relation to

Examiner Findings (continued)

catastrophic exposures as measured by a combination of aggregate limits, modeling, monitoring, and reinsurance protections. In relation to earnings and capital levels, AIG maintains conservative balance sheet growth targets, debt levels, and intangible asset levels. Both the share repurchase program and dividend policy are modest and are not expected to have a material impact on capital levels or ratios. Rating agencies have affirmed financial strength and issuer credit ratings at an "AA" level.

Leverage Impact from Capital Activities

AIG demonstrated ample access to capital markets in the review period with both routine funding programs and hybrid debt issuances. AIG completed planned issuances of four hybrid securities (Euro, Sterling, USD, and USD retail) totaling $4.5 billion to replace higher cost equity (AIG stock share repurchases). As part of AIG's organizational structure simplification project, the conglomerate may use hybrids in 2008 to fund acquisitions or expand its network of regional holding companies. AIG also accesses capital markets by issuing multi-currency denominated debentures as part of a matched investment program.

Catastrophic Exposures

OTS performed a targeted review of risk mitigation for management and reporting of catastrophic insurance risk (specifically the potential threat to shareholder's equity posed by major disasters such as earthquakes, hurricanes/typhoons, and terrorist actions). Overall management of catastrophic insurance risk exposure in both the life and property and casualty business lines is effective based on the risk mitigation of the Global Reinsurance Division, prudent exposure limits in relation to shareholder's equity, and the historical ability of AIG to withstand major catastrophic events with manageable losses in relation to shareholder's equity.

Capital Management

The Treasury Group's plans, procedures, controls, and systems (capital management processes) assure that the conglomerate has sufficient capital resources to meet all reasonably foreseeable demands. The formation of the AIG Capital Committee has increased formalization and transparency in capital management. The creation of this committee satisfies a recommendation OTS made in its previous examination report. This committee provides a venue for management to review and document capital related activities to ensure that it recognizes and mitigates potential risks. The committee also reviews and presents significant issues to the Board or Finance Committee when necessary. We recommend the Capital Committee develop the methodology, metrics, and benchmarks for capital adequacy and deployment of excess capital as measured by SCAR, rating agency requirements, and ECM.

Holding Company Capital Analysis and Reporting

Examiner Findings (continued)

Many capital management processes are manual. AIG underinvested in automation in prior years. Management has begun long-term corrective action with a series of initiatives to automate and enhance processes including improved reporting capabilities and controls. These actions include the Economic Capital Modeling (ECM) and Financial Reporting Environment (FIRE) transformation, which pose a moderate amount of integration and operational risk. In the interim, collecting and analyzing data is challenged by legacy system constraints and requires significant AIG resources.

We noted procedural improvements in monitoring and allocating capital over prior years. AIG aggregates conglomerate-wide, risk-based capital requirements through Supplementary Capital Adequacy Requirement (SCAR) analysis and reporting. Through this process, OTS evaluates holding company capital adequacy and AIG's compliance with the European Union Financial Conglomerates Directive. The company has made substantial progress developing adequate and transparent holding company level risk reporting and controls, although it has not fully developed the processes have yet to be fully developed. During the review period, system limitations and complexities contributed to delayed or incomplete SCAR reports and related analysis. AIG also faces limitations and complexities relating to the current internal financial reporting system, the implementation of the new automated clarity system for SCAR data gathering, and the ECM reporting format.

We support the Treasury Group's efforts to coordinate data collection, analysis, and dissemination to ensure comprehensive, consistent, and timely information flow throughout the conglomerate. IAD has scheduled a review of these processes in 2008. We will assess the IAD review upon its completion as well as any additional changes management makes to improve timely and comprehensive analysis and reporting.

Economic Capital Model Implementation

ECM integration with capital management presents challenges in developing model consistency, organizational communication, and data requirements/assumptions. AIG's business lines have diverse risk profiles, which make developing consistent model methodologies difficult. AIG is expanding efforts to gather available data and develop assumptions and parameters to support model simulations. AIG is also devoting considerable resources to communicating ECM terminology, purpose, approach, and results throughout the organization.

Management is working with consultants, rating agencies, and regulators to ensure that ECM methodologies are sound before implementation of model validation requirements and disclosure of key assumptions (such as diversity benefits across business lines, geographic regions, and risk categories). Management's goal is to use ECM to evaluate capital decisions, including deployment of excess capital, dividend policy, equity share repurchase, and potential acquisitions and

Examiner Findings (continued)

divestitures. Management intends to extend ECM applications to risk retention reinsurance and hedging strategies; benchmark asset allocation and optimization; and the budget process.

We view ECM results as preliminary. AIG has not received an independent model validation. Management recently engaged independent resources to perform model validation reviews. Management has briefed rating agencies and regulators regarding its ECM methodology foundation; however, it has not fully disclosed its assumptions for estimating unexpected losses and diversity benefits. A targeted review will focus on these efforts beginning in the fourth quarter of 2007. This coincides with the anticipated completion of initial model validation procedures.

Capital Model Validations
AIG has not finalized comprehensive validation procedures for the internal capital models (ICMs) that it uses in the SCAR calculation. Management projects that independent model validation will commence for the ECM project in the fourth quarter of 2007. The ECM modules for ILFC and AGF are similar to the ICMs the company uses in the SCAR calculation. As a result, their validations may suffice for SCAR purposes, assuming the independent review documents and employs comprehensive, in-depth, and independent standards.

AIGFP ICM Model Accuracy
AIGFP ICM results are reasonable and conservative in measuring proxy capital requirements; however, the capital model, which Standard & Poor's (S&P) developed for financial products subsidiaries of insurance companies, does not comprehensively capture financial market risk exposures to commodities or foreign exchange positions. It also does not precisely capture the risk for off-balance sheet super senior credit derivatives because the capital requirement is rules based and not statistically driven. Although the model lacks sophistication and precision in estimating the capital charges for these risks, management provides alternative data indicating that the capital charges are conservative. Management has not determined whether it will replace the model with a more dynamic ICM as part of the ECM project or with an upgrade from S&P.

Recommendations and Ongoing Remediation

- *Holding Company Capital Analysis and Reporting* – Continue to improve the transparency, consistency, and comprehensiveness of capital planning and analysis as outlined in Capital Committee meeting notes of April and June 2007.
- *Holding Company Capital Analysis and Reporting* – Continue to develop the methodology, metrics, and benchmarks for capital adequacy.
- *Holding Company Capital Analysis and Reporting* – Complete the analysis and reporting of excess capital in a timely manner.
- *ECM Implementation* –
    - Fully develop and implement capital management, monitoring processes, and controls before significantly deploying excess capital identified by the model.
    - Establish benchmarks in defining and deploying excess capital.

Examiner Findings (continued)

- *Capital Model Validation* – Complete an in depth and timely capital model validation. Management responded to recommendations regarding model validation in the prior examination and engaged independent third parties to complete the process.
- *AIGFP Model Accuracy* -- Develop or adopt a more robust ICM to estimate AIGFP capital charges for all risks precisely and comprehensively.

Examiner Findings (continued)

Capital Analysis

Consolidated Capital Summary ($ millions)				
	03/31/2007	12/31/2006	12/31/2005	12/31/2004
Consolidated GAAP Capital	$103,055	$101,725	$86,317	$79,673
Total Available Capital[c]	$74,722	$70,985	$62,632	$59,782
Total Required Capital	$29,166	$29,102	$28,979	$27,994
Total Excess Capital	$45,555	$41,882	$33,653	$31,788
Total Mobile Capital[d]	$10,139	$10,519	$10,289	$7,475
Leverage Ratio	12.9%	13.8%	10.9%	10.7%

- AIG GAAP capital is diverse among operating subsidiaries (52.2 percent Life & Retirement Services; 37.4 percent General Insurance; 12.8 percent Financial Services; and 7.3 percent Asset Management). GAAP capital increased mainly due to retention of earnings in each of these subsidiaries.
- Excess capital resides mainly in the insurance sector (AIRCO $5.7 billion; AGC Life $5.3 billion; ALICO $5.1 billion; SALIC $4.1 billion; Star $2.4 billion; and UGC $1.3 billion) and financial sector (ILFC $1.8 billion and AGF $1.4 billion). Growth in excess capital resulted mainly from strong profitability of insurance companies, particularly DBG companies and AIUO. AIRCO updated statutory filings to 2005 from 2003 (delayed because of statutory restatements), resulting in $1.4 billion increase to excess capital.
- The leverage ratio (debt + preferred equity/total capital) is manageable at 12.9 percent. Total capital ($14.3 billion insurance debt; $1.5 billion preferred equity; hybrid equity $3.8 billion; common equity $103.1 billion = $122.7B) includes $3.8 billion in hybrid capital, which represents 3.1 percent of total capital. Modest net increases in leverage were the result of the hybrid issuances in 2007.

[c] Regulatory capital as defined by each company's primary regulator or proxy equivalent for unregulated companies. For insurance companies, this represents capital adjusted for intangible assets and non-admitted assets such as deferred acquisition costs. For other regulated financial services companies and unregulated companies, available capital represents a risk-based capital concept or equity capital adjusted for intangibles and illiquid assets with additions for allowable loss reserves and subordinated debt.

[d] Represents the total of excess capital at the corporate entity level, which AIG may withdraw from the entity without advance regulatory approval or any other restrictions.

Examiner Findings (continued)

ORGANIZATIONAL STRUCTURE

Component Rating

We assign AIG a "3" Organizational Structure component rating.

Conclusion

The organizational structure exhibits weaknesses that range from moderate to severe. We noted and management acknowledges sizeable deficiencies in staffing levels, skill levels, processes, and systems conglomerate-wide. Financial reporting and certain risk mitigation processes are not developed to the level required by the enterprise's size, complexity, and operating profile, which raises supervisory concern. Management has devoted substantial resources to implement corrective actions, and the Board has demonstrated support for those actions. However, sustainable and comprehensive solutions to the identified weaknesses will require long or uncertain implementation timeframes during which the company will continue to have heightened risk exposure. While the company needs to address these weaknesses, its organizational diversity and financial strength affords it with time and resources to address the weaknesses in the normal course of business and to withstand adverse business conditions.

AIG identified most of the organizational structure weaknesses through its conglomerate-wide remediation process and the work of its independent auditors. The weaknesses resulted from several years of underinvestment in human capital (staffing levels and qualified personnel), processes (complexities of managing the decentralized holding company structure), and systems (automation and integration of financial systems and controls).

Comments and Supporting Analysis

Scope of Review
The review of the organizational structure component assesses the operations and inherent risks in the holding company enterprise. OTS evaluates organizational structure through reviews of business and product lines, including affiliate relationships, concentrations, exposures, and the inherent risks in the structure. The examination team monitors and analyzes the risk assessments of the corporate control groups, decisions of AIG's committees, and the findings of the independent auditor PriceWaterhouseCoopers (PwC) in its assessment of the organizational structure.

OTS evaluates management's ability to identify and monitor issues and risks through the nine holding company level corporate control groups, divisions, and functions: Comptroller, Treasury, Global Compliance, ERM (which houses the credit, market, and operational risk functions), IAD, Global Reinsurance, and Casualty Actuary. We also evaluate AIG's committee structure, which

Examiner Findings (continued)

includes operating, governance, and special committees that serve as conduits to report and rectify organizational issues and risks. We also follow the work of the independent auditors. PwC contributes to the transparency goal of the conglomerate, especially regarding the accuracy of the external financial statements and the SEC-required annual independent assessment of AIG management's control environment over financial information.

Key Businesses and Relationships

Summary of Business

AIG is a diversified, worldwide insurance and financial services conglomerate with operations in more than 130 countries and jurisdictions. AIG companies serve commercial, institutional, and individual customers through extensive property-casualty and life insurance networks. In addition, AIG companies provide retirement services, financial services, and asset management. Based on revenues, domestic general insurance (30.7 percent) and foreign life insurance and retirement services (31.2 percent) are the largest operating segments of the company. The other segments of the conglomerate include domestic life and retirement services (14.3 percent), foreign general (10.8 percent), financial services (8.0 percent), and asset management (5.0 percent).

There is functional regulation for AIG's insurers both domestically and abroad. AIG owns three large unregulated financial services companies: International Lease Finance Corporation (ILFC), American General Finance (AGF), and AIG Financial Products (AIGFP). ILFC is a significant provider of aircraft operating leases. AGF is a major provider of consumer finance products in the United States. AIGFP is a significant participant in the global capital markets (including commodities, credit, energy, equities, and foreign exchange and rates) and offers a range of derivatives and structured products.

Summary of Inherent Risks in the Organizational Structure

AIG is subject to insurance risks through its underwriting, investment, and reinsurance activities. With respect to general insurance operations, elevated risk occurs when significant catastrophic events take place in a relatively short period, if pricing and underwriting does not reflect assumed risks, or when competitive market influences persist. AIG's investment strategies are based on preservation of capital and growth of surplus. It typically invests in fixed income and equities of highly rated companies (lower risk profiles). Reinsurance receivables are subject to risk from changes in the value of underlying collateral or the strength of reinsurance companies participating in the underwriting and risk of catastrophic events. With respect to life and retirement insurers, risk is elevated when paid losses accelerate or policy surrenders increase. These operations are also subject to risk of national or regional economic collapse, nationalism, terrorism, or pandemic events. Financial services operations are subject to inherent credit risks of lending (pricing and underwriting) and increases to costs of funding (capital markets).

Examiner Findings (continued)

In the annual review of the major business lines, we noted innovative product development; sound underwriting discipline, pricing strategies, and market share strategies; and minimal known exposure from systemic, compliance, legal, and regulatory issues. Risk monitoring of these exposures remains a work in progress. The review noted the following business unit challenges that increase risk exposure:

Business Unit	Potential Sources of Risk Exposure
Property and Casualty	Directors & officers, excess casualty, and workers' compensation coverages have increased pricing and market share competition.
Personal Lines	AIG aggressively pursues market share. Pricing competition remains heavy.
Mortgage Guaranty	AIG reports sizable operating losses resulting from weakness in the U.S. housing market.
Domestic Retirement Services	The unit has negative individual fixed annuity net flows (although there are incremental improvements in 2007). Surrender rates increased due to a large number of policies coming out of their surrender charge periods and competition from bank and other short-term fixed rate products.
Foreign Life Insurance & Retirement Services	Declining sales and increased expenses related to the termination of certain tax-related products and provisions related to the continuing industry-wide regulatory review of claims continue to affect 2007 Japan results.
Domestic Consumer Finance Group	2007 operating income was significantly lower due to charges taken for the estimated cost of implementing the financial remediation plan, pursuant to the terms of the Supervisory Agreement reached by AIG's domestic consumer finance operations with OTS. AGF recorded a $50 million charge in the quarter ended June 30, 2007 in addition to the $128 million charge in the first quarter of 2007. Lower real estate production volumes and margin compression are also affecting AGF. While charge-off and delinquency ratios increased primarily due to seasoning of the portfolio, they remain stable and near historic lows.
Overseas Consumer Finance Group	The Taiwan credit card market crisis, sluggish results in Asia, and higher expansion related expenses are affecting CFG overseas operating results.

<u>Other Potential Systemic Risks within the Organizational Structure</u>

Existing strategic planning, legal, and reputation issues pose modest risks. Management has established reasonable strategic planning in AIG's business lines that addresses these risks through decentralized business line strategies and accountability. The ECM project will improve strategic planning commensurate with the complexity of the conglomerate. Management will use the ECM to centralize holding company level strategic planning initially. AIG then plans to implement the ECM in its business lines over the next several years. Processes exist to monitor profitability results and capital levels in the interim. AIG holding company level monitoring is adequate in terms of demonstrated ability to administer liquidity functions and capital needs.

OTS reviews significant inter-company relationships and concentrations through its continuous supervision and examination program. Intra-group transactions and risk concentration risk reporting adequately identifies and monitors activities and risk relationships between entities. However, many of the processes and reports are labor intensive to create and maintain. These processes will benefit from strategic initiatives to upgrade financial and risk reporting systems. We recommend completion of the organizational simplification process, which will result in more transparency of inter-company

Examiner Findings (continued)

relationships, including complex pooling arrangements and reinsurance treaties that distribute risk and profits/expenses among many AIG subsidiaries.

Global compliance and the conglomerate's susceptibility to reputation damage is a high-risk area particularly during AIG's reorganization and simplification. The company must ensure that it develops a comprehensive process to identify and document all significant business level compliance risks throughout the organization. AIG is rebuilding the compliance corporate control group. Given the diverse risks that arise from global operations, the challenge of automating and integrating an adequate risk reporting system is substantial. OTS will continue to monitor progress in this area. Through targeted reviews and the continuous supervision program, the examiners did not identify systemic or large compliance exceptions with a significant financial impact to AIG.

Subprime Exposures

AIG has exposure to subprime mortgages via several of its business segments and products. AGF extends first and second-lien mortgages to borrowers, including subprime mortgages. United Guaranty provides mortgage guaranty insurance for first and second-lien mortgages, including subprime mortgages, which protect lenders against credit losses. AIG insurance companies and AIGFP invest in Mortgage Backed Securities (MBS) and Collateralized Debt Obligations (CDOs), in which the underlying collateral includes pools of subprime mortgages. AIGFP also provides default protection through credit default swaps on the "Super Senior (AAA+)" tranche of CDOs, in which the underlying collateral includes pools of subprime mortgages.

AIG provided significant public disclosure of its subprime mortgage exposure with its second quarter 2007 earnings release. Management is comfortable with the size of the exposures and the quality of the respective investment portfolios and operations. Credit deterioration has materially affected current results in United Guaranty Corp. (UGC), AIG's mortgage guaranty insurance business. The remaining subprime exposures are performing as expected. The portfolios consist of highly-rated securities with substantial collateral subordination, which management subjects to ongoing monitoring, modeling, and analysis. AIG's disclosure is consistent with the results of OTS's review of subprime exposures. AIG is adequately tracking its consolidated exposures in this area. OTS will continue to monitor the effects of AIG's subprime mortgage market exposure, and the management of that exposure, as part of its continuous supervision program.

Financial Modernization

AIG's long-term approach to solving organizational weaknesses is appropriate. AIG has defined critical projects for the enterprise to achieve long term, sustainable solutions to control weaknesses, improve financial reporting and risk management, develop infrastructure for future growth, and enhance governance. Management is prioritizing and dedicating resources to complete the critical projects. AIG should give the highest priority to the financial close remediation and the related long-

Examiner Findings (continued)

term solution to financial reporting weaknesses (project FIRE) in light of the potential risk consequences of systemic breakdowns. The present accumulation of projects is vast in relation to human capital and management resources; therefore, AIG should move more quickly to prioritize critical projects.

Organizational Simplification

AIG is simplifying its organizational structure to improve operational efficiencies and meet regulatory requests for increased transparency. The company assembled a steering committee comprising key business unit Chief Financial Officers and representatives from the Treasury Group, the Legal Department, the Tax Department, and the Operations/System Group. The purpose of the committee is to vet specific country and cross border tax, capital, earnings allocation, underwriting, and reinsurance issues. The major initiatives of the project include Domestic and Foreign General Insurance and Domestic Personal Lines reorganization. The process includes simplifying legal ownership, improving company valuation transparency, assessing rating agency implications, evaluating marketplace impact, and assessing/restructuring guarantees and agreements between entities.

AIG has identified 4,500 entities within the conglomerate inclusive of operating entities, branches, and special purpose entities. It will dissolve or consolidate approximately 330 companies as part of organizational simplification, which will result in 7.5 percent fewer entities. Management plans to complete 154 simplification projects in 2007 and the remaining projects by 2009, although it has not set a date for 105 projects. There are many integration challenges and operational risks of such a project. Solvency II and other EU directives are evolving and may result in cross-border ownership implications. Internal conflict also exists between business lines (control and transparency objectives) and corporate groups (tax and capital ramifications). The steering committee exists to crystallize these issues so that senior management can comprehensively evaluate key decision drivers (tax, capital, policies, and reinsurance). Most importantly, however, management views organizational simplification as complementary to the financial close remediation and financial modernization initiative (and not a conflict or competition for limited accounting resources). Many of the projects will reduce delays in the close process or otherwise simplify the quarterly roll-up of financial reporting. OTS supports these initiatives and will continue to monitor the status of the project and evaluate the integration and operational risks.

Other Material Changes in or Impacts on the Organizational Structure

<u>Corporate Control Groups</u>

AIG maintains corporate control groups to identify and monitor risks throughout the conglomerate. Consistency and adequacy of risk assessments are improving. Management is also developing risk metrics to improve monitoring.

Examiner Findings (continued)

Independent Auditor Findings - Control Environment

AIG has complicated issues within the control environment and the organizational structure that are difficult to remediate. These weaknesses subject AIG to systemic and operational risks. PwC identified several significant internal control deficiencies in its review of income taxes, the financial close process, reconciliations, investment accounting, DBG reinsurance, access controls, and model/spreadsheet validation and control. The deficiencies include heightened risk of financial losses, dependency on manual processes, gaps in internal controls, and gaps or turnover in qualified personnel. AIG has instituted compensating controls, which mitigate loss exposure; however, it cannot assure the sustainability of full remediation under the current operating environment and structure, thus highlighting the need for financial reporting modernization.

Corporate Governance

AIG has a sound network of operating, governance, and special committees. In addition to reviewing the work of the board of directors, OTS focused on audit committee materials to evaluate issues and risks facing the organization. The Board, audit committee, and other key committees adequately vet issues and risks. Board minutes reflect that directors receive committee reports at each regularly scheduled Board meeting. These reports consist of oral presentations, and the Board does not maintain written documentation in its records. The Board reviews and ratifies all committee meeting minutes, which provide detailed documentation of committee activities. Given the change being driven through the organization, the committee structure is critical to identifying organizational weaknesses and implementing remediation.

The Board and all committees (with the exception of the recently formalized Finance Committee) performed written self-evaluations in 2007. The Chairman also conducted individual director assessments. There was a minor change in Board composition with the retirement of one outside director and the election of another to fill the vacancy. Two current directors will be ineligible to stand for re-election in 2008 due to AIG's imposed age limitation. The Nominating and Corporate Governance Committee has established criteria for suitable director candidates and engaged a search firm to provide candidates to fill these upcoming vacancies.

However, the Board needs more information from management to perform necessary oversight of full-spectrum catastrophic risk management. In addition, the Board should be more involved in the process of determining AIG's overall risk appetite.

Examiner Findings (continued)

RISK MANAGEMENT

Component Rating

We assign AIG a "2" rating for the Risk Management component.

Conclusion

AIG's overall risk management has improved, but considerable work remains in several key areas. Board and senior management oversight, policies and limits, risk monitoring procedures, reports, and management information systems are effective. The management of risk is largely effective. The company has a long-standing culture of strong and independent insurance, credit, and market risk control; however, operating complexity, geographic dispersion, and diverse regulatory requirements require a more robust and expansive risk management structure. Risk mitigation practices and infrastructure in these key areas are satisfactory and generally adjusted appropriately in response to changing industry practices and current regulatory guidance.

The ERM group is the overarching risk management layer and demonstrates a responsiveness and ability to cope successfully with existing and emerging risks that may arise in carrying out business plans. While AIG has significant remediation work and risk infrastructure in various stages of completion, these problems are recognized and in the process of being resolved. ERM staff experience, expertise, and depth are generally appropriate to manage the assumed risks. Due to the depth and breadth of remediation projects, AIG is integrating additional resources into the risk management process. Remediation reflects internal control weaknesses and deficiencies, including diversion of ERM resources from core risk management tasks. Audit and Regulatory, Compliance and Legal committee attention is significant and it has developed plans to take appropriate corrective actions with respect to remediation and implement required compliance recommendations.

Comments and Supporting Analysis

Scope of Review

We assess Risk Management by evaluating the directors' and senior management's ability to identify, understand, and control the risks within the holding company enterprise. The evaluation considers the adequacy of policies, procedures, and limits given the risks inherent in the activities of the consolidated enterprise. OTS also evaluates AIG's stated goals and objectives; the adequacy of the enterprise's accounting and risk disclosure policies and procedures; the adequacy of risk measurement and monitoring; and the adequacy of the holding company's management reports and information systems. The evaluation underscores the importance of the control environment, considering the complexity of the enterprise and the risk inherent in its activities, as well as risks from new products, new markets, and changing market conditions.

Examiner Findings (continued)

AIG's operations provide it with a diversified and powerful platform for scalable operating leverage. The conglomerate also faces significant challenges managing the risks of highly regulated, widely dispersed, and complex operations. The Audit Committee is the Board's representative in most Risk Management activities; however, the newly formed Finance Committee will oversee certain risk management functions.

AIG's risk management performance is satisfactory, but it requires continued close monitoring and review. There are several risk management areas that AIG should develop and improve, including reporting to the Board. Our review of risk management encompasses the following: AIG's control of credit, market, operational, and catastrophic risk (Enterprise Risk) combined with the economic capital initiative; remediation of identified internal control deficiencies; financial reporting integrity; internal audit coverage; compliance-regulatory-reputation management; reinsurance transfer; insurance reserving; and the Complex Structured Financial Transactions review process at both the corporate and business unit level.

Enterprise Risk Management (ERM)
The ERM program is the focal point for risk management and reporting activities. The program's operational risk management (ORM) and full-spectrum catastrophic risk management components are in development. In addition, AIG is experiencing complications in the remediation of the high error rate associated with business unit reporting in the financial close process. Notwithstanding these challenges, ERM is satisfactory based on AIG's strong and tested credit and market risk management programs, intensive efforts to address identified weaknesses and the favorable operating results in various business cycles. Risk management is also effective in the credit, insurance, and market risk areas where AIG has demonstrated positive results in the identification, monitoring, and control of risk. The risk management processes in these areas include well-defined policies, procedures, controls, and limits; regular monitoring against risk tolerance guidelines; and programs to provide technical assistance to the business units. Adequate risk management information systems, while manually intensive in some cases, further support risk management.

ORM, catastrophic event risk management, and the remediation of the financial close process are in development. These processes have not achieved the level of effectiveness that AIG needs to ensure comprehensive risk management. AIG should continue to develop effective controls embedded into its decentralized business units and to implement accurate financial reporting without reliance on time-consuming manual controls.

Economic Capital Initiative
ERM and AIG's Treasury Group are working to develop and deploy the ECM, which will become the standard for decision making for capital deployment, utilization, structure, and target levels. AIG expects to finalize an operational version of its model in late 2007. Management acknowledges challenges with integrating ECM into capital management relating to model consistency,

Examiner Findings (continued)

organizational communication, and data requirements/assumptions. AIG has not conducted model validation, but management has engaged independent resources to perform model validation reviews.

AIG is in the latter stages of the development and testing phase in the economic capital process. One of the challenges facing AIG in developing a consolidated ECM is the company's geographic and product line diversity. Management has briefed rating agencies and functional regulators with respect to its ECM methodology foundation; however, it has not fully disclosed details including the extent and consistency of data gathering and automation efforts and assumptions in estimating unexpected losses and diversity benefits. ERM plays a critical role by fostering consistent data and risk reporting throughout the conglomerate and monitoring execution risk associated with the ECM project. The financial reporting modernization and remediation is also critical for automation and consistency of data gathering across the unique business segments. Financial modernization is a project that will likely take several years to implement.

Remediation of Control Deficiencies

During a series of regular meetings, ERM and PwC advised OTS on the status of AIG's remediation efforts for the remaining material control weakness (income tax accounting) and the eight significant control deficiencies. OTS has particular concern with the financial close process and DBG reinsurance operations. These two significant control deficiencies represent critical control functions that should ensure the prompt and accurate presentation of financial statements and the accurate and timely reporting of reinsurance placement, both of which are key risk mitigation tools. Both of these deficiencies present a higher risk of out of period adjustment, potential restatement, late filing, and large post-closing entry risk that can cause the financial statements to contain material errors. ERM closely monitors the progress on all remediation items and reports its assessment to the Audit Committee. Management must show more progress on these two significant control deficiencies. It must also sustain progress on the remaining material weakness and six other significant deficiencies while ensuring that it maintains compensating controls to mitigate the risk of a large misstatement of AIG's public financial information.

Enterprise-wide Initiatives – Prioritization and Execution

Management has identified 113 critical projects for the conglomerate. AIG is prioritizing these projects, initially identifying project FIRE, control remediation, legal entity simplification, FAS 157/159, economic capital, and others as enterprise-wide priorities and creating governance structures to ensure quality, timely, cost effective, and coordinated project execution. We support management's efforts to prioritize and execute projects, many of which are critical to building sustainable improvements to the organizational structure and internal controls. AIG is only in the initial stages of prioritization, but is already implementing changes to enhance controls, improve financial reporting, better manage risk, build infrastructure, and enhance governance. Execution risk is high given the limited resources and systems with which AIG has to implement the complex and,

Examiner Findings (continued)

in some instances, interdependent projects. We recommend that management place top priority on the financial close remediation and the related long-term solution to financial reporting weaknesses, project FIRE, given the potential consequences of identified weaknesses.

Comptroller's Role in Control Environment

The noted control deficiencies require the Comptroller's unit to manually oversee those risk areas, requiring significant resource allocation for reviewing financial information submitted from numerous reporting units and over 500 general ledger systems. This manually intensive review and quality control process extends the time AIG requires to produce its quarterly financial statements. OTS meetings with the Comptroller's group indicate AIG's commitment to provide required staffing for key Comptroller functions; however, the staffing augmentation will take time due to high demand for qualified accounting resources. The Comptroller's unit also is responsible for AIG's accounting policy, which establishes global accounting requirements for the firm and provides GAAP implementation guidance. AIG's Office of Accounting Policy has been active in disseminating US GAAP guidance to AIG's global business units and has hiring plans for key overseas locations requiring detailed US GAAP knowledge, such as Hong Kong. The Comptroller maintains a reliable financial reporting system, despite the requirement for significant manual review, elongated reporting timeframes, and a high level of accounting adjustments during the financial close process. Consequently, AIG's financial reporting process is not sustainable, and the company must place priority on remedial efforts.

Internal Audit Division, External Audit, and Audit Committee

The Internal Audit Division (IAD) is becoming a reliable and key control function that serves the Audit Committee in its oversight of the firm's business units. IAD Director Roemer has increased the amount and quality of audit staff, revamped the audit program, and reformed the audit grading system. The Audit Committee provides appropriate oversight of IAD. This committee monitors IAD's progress in completing its annual audit plan, staffing adequacy, internal audit issues, and the IAD budget. In addition, the Audit Committee is monitoring the remediation of control deficiencies from reports provided by ERM. PwC also reports regularly to the audit committee and cited one material control weakness relating to controls in the opinion to the December 31, 2006, audit report. The area cited was control over income tax accounting, an area also noted in the 2005 audit as a material weakness. As of the exam date, management believes that remediation of this item is possible, but not certain for 2007. In addition, PwC reports regularly to the audit committee on the status of the eight control deficiencies. Overall, the Audit Committee has conducted its required functions in an acceptable manner and IAD has achieved sufficient conglomerate-wide coverage based on the 2007 audit plan.

Global Compliance Program and Anti Money-Laundering

Examiner Findings (continued)

This function underwent a management change during the review period and is implementing a model that integrates the corporate compliance discipline into business operations. AIG hired VP and Chief Compliance Officer (CCO) Kathleen Chagnon in April 2007. CCO Chagnon is driving significant changes and enhancements to make the Global Compliance Program (GCP) more effective and accountable. Examples include clarifying the performance expectations of business unit compliance officers and hiring new senior compliance officers to provide top down oversight of key areas such as anti-money laundering (AML), Office of Foreign Asset Control, Foreign Corrupt Practices Act, the PATRIOT Act, anti-fraud measures, and internal investigations. AIG is also undergoing an independent consultant's review of the GCP, which will result in recommendations to the Regulatory, Compliance, and Legal Committee.

Effective July of 2007, the company combined the ORM and Corporate Compliance Group (CCG) top-down risk assessment processes. Management indicated that by combining the two assessments, it would eliminate any redundancies that may have existed by having two separate assessments. This should further strengthen the partnership approach of ORM, CCG, and IAD to create a more efficient and effective risk identification and assessment process. Finally, management developed a more robust risk and control self-assessment (RCSA) that will expand on the top-down risk assessment process already in place. The 2008 annual budget and planning process will include the revised RCSA process.

AIG's AML program remains largely unchanged from the prior review. The company adopted a revised "Global AML and Anti-Terrorist Funding Policy" in November 2006 that contains the essential elements provided in the regulatory guidance and more specifically addresses the FinCEN insurance company rules. However, implementation of the policy has been delayed pending review and approval by the independent consultant who must review AIG's policies, procedures, and the effectiveness of its compliance function as required by the 2006 regulatory settlement with the SEC et al. This has delayed AIG's plan to update and bring more uniformity to individual AIG company AML programs. IAD continues its program of AML audits of the companies and business lines, and the CCG now participates in the annual internal audit plan process to ensure AML issues receive appropriate attention and to monitor disposition of outstanding AML audit deficiencies. The CCG also performs its own selected AML reviews. Each functional business line performed a Compliance Risk Self-Assessment in 2006 with risk ratings ranging from "low risk" to "low to medium risk".

CCO Chagnon is modifying and enhancing the conglomerate-wide, compliance and AML reporting process, and existing compliance reports indicate there are no systemic compliance issues. Nonetheless, the timeline for having a fully functional and centrally controlled GCP is extended and by consequence increases global compliance reporting risk. The present situation requires additional effort to ensure that the company identifies, communicates, and resolves all compliance issues with CCO concurrence. Through continuous supervision and examination, which includes monthly

Examiner Findings (continued)

meetings with the CCO, OTS will monitor the development of the enhanced compliance program, including oversight and management of global compliance issues.

Global Reinsurance Division (GRD)

Reinsurance is a key risk mitigation tool for AIG's domestic property and casualty business. The reinsurance program allows the company to broaden its reserve capacity to meet customer coverage demands in a competitive market. The GRD is at the center of AIG's reinsurance management operations and it provides reinsurance analysis and monitoring, tracking, oversight, and placement of certain quota share and facultative coverage agreements as well as the catastrophic coverage programs. Internal control deficiencies exist in reinsurance operations (particularly in the Domestic Brokerage Group) due to the lack of a unified system for tracking reinsurance placements, recoveries, and reporting to regulatory authorities. Notwithstanding this significant control shortfall, GRD has historically provided effective risk management services, as demonstrated by its management of catastrophic insurance risk. AIG needs to extend the catastrophic risk management function to the credit, market, and operational risk areas and provide the results of this reporting to the Finance Committee of the Board.

AGF, WFI, and AIG FSB Supervisory Agreement with OTS

This agreement addressed significant control deficiencies in the oversight of subprime lending programs conducted through AGF subsidiaries and the FSB. The provisions of the agreement are detailed in the "Enforcement Actions" section of this report and will require AIG oversight to ensure that compliance is achieved on a sustained basis. Managing the provisions of this agreement will expose the company to potential reputation risk and additional financial risk; however, the financial risk is manageable for the consolidated entity.

Reserve Adequacy – Chief Casualty Actuary

AIG's maintenance of sufficient reserves for insured losses is fundamental and consequently makes the work of the team led by the Chief Casualty Actuary crucial to the viability of the company. AIG's Chief Casualty Actuary provides proper oversight of the loss development analysis and the resulting carried reserves. In connection with the 2005 regulatory settlement, AIG decided to obtain an outside review of its reserve adequacy. Milliman, Inc., a nationally recognized insurance actuary, conducted this review. The Milliman analysis resulted in AIG's augmentation of reserve levels in several ongoing long tail casualty lines of business and in its discontinued asbestos and environmental lines, which has experienced some adverse loss development in the first half of 2007. AIG's overall loss experience for 2006 and the first quarter of 2007 continues to be in line with actuarial estimates with more recent accident years (post 2003) showing more favorable loss development than previous years. AIG is committed to having an outside firm evaluate its overall casualty reserves periodically.

Examiner Findings (continued)

Complex Structured Financial Transactions Committee (CSFTC)

The CSFTC program, under the guidance of ERM, is becoming a key risk control through standardization of the process used to submit, evaluate, and up-channel transactions meeting the criteria for consideration and approval. AIG established the CSFTC in 2004 and revised the CSFTC policies and procedures in July 2006. The policies and procedures provide guidance and minimum standards that business unit level Transaction Review Committees (TRC) must follow. For example, under the polices and procedures requirements, AIG-FP's business line personnel submitted fourteen transactions for consideration and approval by AIG-FP's TRC during the review period, accompanied with approval request forms, executive summaries, and other supporting documents to comply with the CSFTC policies and procedures. AIG-FP's TRC documented its decisions and the rationale in minutes and submitted two transactions to the CSFTC for its consideration and approval. The minutes covering CSFTC activity during the review period indicate substantive rigor in vetting the submitted transactions and, in many cases, deferral of final decisions pending better information. OTS will continue to review the evolution and maintenance of the CSFTC process at both the corporate level and selected business unit levels to ensure that it remains a key component of the firm's risk management architecture.

Examiner Findings (continued)

EARNINGS/LIQUIDITY

Component Rating

We assign AIG a "1" Earnings component rating.

Conclusion

AIG's overall financial performance is strong. The quantity and quality of earnings from the conglomerate's major business lines and subsidiaries, and on a consolidated basis, are sufficient to make full provisions for the absorption of losses and the accretion of consolidated capital in light of risk exposure and business plan objectives. Earnings reflect consistent product, service, and geographic growth, breadth, and diversification. The diversification and breadth of earnings sources provide stability and mitigate earnings volatility. The enterprise maintains strong liquidity levels along with well-developed and tested funds management practices. The parent company and its subsidiaries have reliable and sufficient access to sources of funds on favorable terms to meet present and anticipated liquidity needs.

Comments and Supporting Analysis

Scope of Review
We assess earnings by evaluating the adequacy of the enterprise's overall financial performance, including the quantity and quality of earnings and liquidity. Our review considers the level, trend, and sources of earnings on a consolidated level, as well as for material legal entities and business lines. Our review also considers the ability of earnings to augment capital and provide ongoing support for the enterprise's activities. In addition, we consider the enterprise's ability to attract and maintain the sources of funds necessary to achieve financial efficiency, support operations, and meet obligations. We evaluate the funding conditions for each material legal entity in the holding company structure to determine if any weaknesses exist that could affect the funding profile of the consolidated enterprise.

Earnings Trends
AIG's revenues, net operating income, and net income improved. Trends are positive for three of the enterprise's four business segments. The Financial Services segment had negative earnings trends due to changes in accounting rules rather than core fundamentals. The continued improvements reflect business, product, and market growth within the enterprise's General Insurance and Life Insurance & Retirement Services business segments. There were also no significant catastrophic losses during the review period.

Examiner Findings (continued)

Total revenues increased due to growth in premiums earned and net investment income, along with an interest rate environment that resulted in a higher level of net investment income. Developing new markets, expanding distribution channels, and providing a wider range of products all contributed to the revenue increase. In addition, product innovations, such as offering more investment-linked products and providing riders to its products that fit more closely with the current demand, increased market share in competitive markets. Revenue growth is strong outside of the United States, notably in the European and Asian markets.

The Financial Services business segment's revenues declined 24 percent from 2005 to 2006, as a result of hedging activities at AIG-FP that did not qualify for hedge accounting treatment under FAS 133. Absent the accounting impact, the Financial Services segment's revenues would have increased. AIG-FP reinstituted hedge accounting in 2007, resulting in more stable revenues. ILFC accounted for nearly half of the Financial Services segment revenues in 2006. It is experiencing strong financial performance due to a favorable environment for aircraft lessors.

Product, service, and geographic breadth and diversification are fundamental to AIG's business model. These fundamentals provide AIG earnings growth, consistency, and stability to endure financial setbacks within its business lines. For example, total revenues, net operating income, and net income, increased despite the Financial Services business segment's decline in revenues from 2004 to 2005, a $128 million charge in the domestic consumer finance operation as a result of the OTS review of its subprime lending activities, and $2.1 billion in after tax catastrophe losses experienced in 2005.

Earnings Management and Projections

AIG approaches earnings management strategically and provides effective tools for decision-making and financial control. AIG prepares and vets comprehensive, annual planning scorecards that identify one year and three year strategic and financial, customer, and talent management objectives. The scorecards also track external environment considerations, competition, distribution issues, market outlook, operational risks, major initiatives, cost containment, and remediation issues. AIG also prepares annual budgets for each major operating unit and monitors performance using detailed variance analysis.

AIG projects 19 percent growth in consolidated net income to $16.7 billion for 2007. This amount is achievable based on AIG's strong first and second quarter results, its ability to create products to fit current demand, and, as of the conclusion of this examination, the absence of any catastrophe-related losses. If the company fails to complete its financial remediation and modernization plan or incurs charges related to remediation of material income tax and investment accounting weaknesses, it could unfavorably affect earnings. Other events that might negatively influence earnings include regional economic downturns (i.e. subprime mortgage and related credit crises), changes in foreign currency

Examiner Findings (continued)

exchange rates, political upheaval, or nationalization and other restrictive government actions. In the domestic market, earnings could decline due to significant competition from other insurers. However, current strategies and existing fundamentals should help AIG achieve projected growth.

Liquidity

Dividends from the company's insurance and financial services subsidiaries are the principal source of funding for its top tier operations. Dividends are a sound funding source because the subsidiaries have proven earnings and cash flow records. In addition, AIG issues commercial paper to fund short-term cash needs, medium term notes to fund its matched investment program (MIP), and long-term debt securities to capitalize subsidiaries and repurchase common stock. It has established back-up credit facilities with financial institutions to support its liquidity needs should it lose access to the commercial paper facility. AIG also has access to a $2 billion inter-company line of credit with its insurance subsidiaries. These sources of funding are readily available at reasonable cost with sufficient capacity to meet unforeseen cash needs. While debt rating downgrades could result in higher funding costs and increases in future collateral requirements, the rating downgrades in 2005 had minimal impact on AIG's ability to raise reasonably priced funds. Similarly, the disruption in debt markets that began in August 2007 is having no discernible impact on AIG's ability to raise reasonably priced funds.

AIG uses funds mainly to service debt obligations, pay dividends to shareholders, allocate capital to subsidiaries, and repurchase outstanding common stock. It relies very little upon liquid assets or net proceeds from the sale of assets to fund operations. The bulk of assets consist of investment in subsidiaries and in the matched investment program. Although reliance on debt issuances for funding has increased in recent years, much of the new debt issuances have been hybrid instruments with certain equity like characteristics. AIG's directly issued and guaranteed borrowings represented 61 percent of consolidated borrowings of $157.2 billion at March 31, 2007. Most of the guarantees related to notes, bonds, and Guaranteed Investment Agreement obligations of AIGFP ($68.6 billion) and commercial paper issued by AIG Funding, Inc. ($4.2 billion). These subsidiaries are generating the necessary cash flow to service, repay, and renew their own debt.

AIG Treasury, which develops policy and funds management practices at the parent level, is developing benchmark ratios for liquidity measurement and control. We will continue to closely monitor these initiatives as part of our continuous supervision of the AIG conglomerate.

Compliance With Enforcement Actions

On June 7, 2007, the following AIG subsidiaries executed a Supervisory Agreement with the OTS relating to improper control over lending practices in the sub prime product group:

- AIG Federal Savings Bank
- Wilmington Finance, Inc.
- American General Finance, Inc.

Provisions of the agreement included the following:

- Plan for Financial Remediation – AIG will submit a plan to OTS that specifies outreach efforts to include an offer of a new loan and/or refund of fees to certain borrowers facing a high risk of foreclosure due to placement in an unsuitable loan.
- Consumer Complaint Processing and Resolution – AIG subsidiaries will consent to third party review of complaint processing procedures to ensure that the remediation plan addresses any abusive lending practices.
- Financial Remediation Plan Monitoring – AIG subsidiaries will engage a consulting firm (with the prior non-objection from OTS) to evaluate ongoing compliance with the Remediation Plan and to provide quarterly reports to the respective Boards of the three subsidiaries.
- Financial Literacy Education and Credit Counseling – AIG subsidiaries will fund $15 million to several designated non-profit entities for this purpose.

This enforcement action will remain in effect until OTS communicates, in writing, the termination or suspension of all or parts of the agreement. OTS Northeast Region personnel will have primary responsibility for assessing compliance with the agreement and the OTS Complex and International Organizations division will closely monitor for impact on conglomerate supervision.

Statements of Financial Condition

Statement of Financial Condition Fully Consolidated (in millions)	Period Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
Assets			
Investments, financial services, and cash:			
Bonds available for sale, at fair value	$390,141	$387,391	$359,516
Bonds held to maturity, at amortized cost	21,414	21,437	21,528
Bond trading securities, at fair value	8,845	9,037	4,636
Equity securities, common stocks, at fair value	30,213	27,683	21,186
Equity securities, preferred stocks, at fair value	2,703	2,539	2,402
Mortgage loans on real estate, net of allowance	18,228	17,067	14,300
Policy loans	7,521	7,501	7,039
Collateral and guaranteed loans, net of allowance	4,840	3,850	3,570
Financial services assets:			
Flight equipment primarily under operating leases, net	41,345	39,875	36,245
Securities available for sale, fair value	47,643	47,205	37,511
Trading securities, at fair value	5,369	5,031	6,499
Spot commodities	73	220	92
Unrealized gains on swaps, options, forwards	16,547	19,252	18,695
Trading assets	3,883	2,468	1,204
Securities purchased under agreements to resell	31,775	33,702	14,547
Finance receivables, net of allowance	29,508	29,573	27,995
Securities lending collateral, at fair value	74,827	69,306	59,471
Other invested assets	44,167	42,114	31,072
Short term investments, at cost	25,866	25,249	15,342
Total investments and financial services assets	804,908	790,500	682,850
Cash	1,702	1,590	1,897
Investment income due and accrued	6,170	6,077	5,727
Premiums and insurance balances receivable, net of allowance	19,731	17,789	15,333
Reinsurance assets, net of allowance	23,130	23,355	24,978
Deferred policy acquisition costs	37,691	37,235	32,154
Investments in partially owned companies	1,179	1,101	1,158
Real estate and other fixed assets, net	4,898	4,381	3,641
Separate and variable accounts	73,971	72,655	63,797
Goodwill	8,687	8,628	8,093
Other assets	17,680	16,103	13,423
Total assets	$999,747	$979,414	$853,051

Statements of Financial Condition (continued)

Statement of Financial Condition Fully Consolidated (in millions)	Period Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
Liabilities			
Reserve for losses and loss expense	$81,135	$79,999	$77,169
Unearned premiums	27,135	26,271	24,243
Future policy benefits for life, accident, and health	123,806	122,230	108,807
Policyholders' contract benefits	246,301	244,658	227,027
Other policyholders' funds	8,476	10,238	10,870
Commissions, expenses, and taxes payable	6,053	5,305	4,769
Insurance balances payable	4,537	3,789	3,564
Funds held by companies under reinsurance treaties	2,446	2,602	4,174
Income taxes payable	10,992	9,546	6,288
Financial services liabilities:			
Borrowings under obligations of GIAs	19,771	20,664	20,811
Securities sold under agreements to repurchase	17,581	22,710	11,047
Trading liabilities	7,546	3,141	2,546
Hybrid financial instruments liabilities, at fair value	8,459	8,856	
Securities and spot commodities sold	4,056	4,076	5,975
Unrealized loss on swaps, options, and forwards	9,679	11,401	12,740
Trust deposits, deposits due to banks and others	4,245	5,249	4,877
Commercial paper	9,228	8,208	6,514
Notes, bonds, loans and mortgages payable	91,186	87,602	71,313
Commercial paper	4,149	4,821	2,694
Notes, bonds, loans and mortgages payable	19,185	17,088	7,126
Junior subordinated debt	3,793	-	-
Liabilities connected to trust preferred stock	1,440	1,440	1,391
Separate and variable accounts	73,971	72,655	63,797
Securities lending payable	75,913	70,198	60,409
Minority interest	8,166	7,778	5,124
Other liabilities	27,343	27,021	23,273
Total liabilities	$896,592	$877,546	$766,548
Preferred shareholders' equity in subsidiary companies	100	191	186
Shareholders' equity			
Common stock	6,878	6,878	6,878
Additional paid in capital	2,674	2,590	2,339
Payments advance to purchase shares	(2,851)	-	-
Retained earnings	88,493	84,996	72,330
Accumulated other comprehensive income	9,854	9,110	6,967
Treasury stock, at cost	(1,993)	(1,897)	(2,197)
Total shareholders' equity	103,055	$101,667	$86,317
Total liabilities and shareholders' equity	$999,747	$979,414	$853,051

Statements of Financial Condition (continued)

Statement of Financial Condition Fully Consolidated (in millions)	Period Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005

Statements of Operations

Comparative Statement of Operations Fully Consolidated (in millions)	Quarter Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
Revenues:			
Premiums and other considerations	$19,642	$74,083	$70,209
Net investment income	7,124	25,292	22,165
Realized capital gains (losses)	(70)	106	341
Other revenues	3,949	13,713	16,190
Total revenues	30,645	113,194	108,905
Benefits and expenses:			
Incurred policy losses and benefits	16,146	59,706	63,711
Insurance acquisition and other operating expenses	8,327	31,801	29,981
Total benefits and expenses	24,473	91,507	93,692
Income before taxes, minority interest, and accounting change	6,172	21,687	15,213
Income taxes	1,726	6,537	4,258
Income before minority interest and accounting change	4,446	15,150	10,955
Minority interest	(316)	(1,136)	(478)
Income before cumulative effect of accounting change	4,130	14,014	10,477
Cumulative effect of accounting changes, net of tax	-	34	-
Net Income	$4,130	$14,048	$10,477
Supplementary Information:			
Earnings per common share, basic	$1.58	$5.39	$4.03
Earnings per common share, diluted	$1.58	$5.36	$3.99

Reconcilement of Consolidated Net Worth

Net Worth Reconciliation Fully Consolidated (in millions)	Quarter Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
Common stock:			
Balance at beginning of period	$6,878	$6,878	$6,878
Issued under stock plans	-	-	-
Balance at end of period	$6,878	$6,878	$6,878
Additional paid in capital:			
Balance at beginning of period	$2,590	$2,339	$2,094
Excess of cost over proceeds of stock issued under stock plans	(16)	(128)	(91)
Other	100	379	336
Balance at end of period	$2,674	$2,590	$2,339
Payments advanced to purchase shares	$(2,851)	-	-
Retained Earnings			
Balance at beginning of period	$84,996	$72,330	$63,468
Cumulative effect of accounting changes, net of tax	(203)	308	-
Adjusted balance at beginning of period	84,793	72,638	63,468
Net income	4,130	14,048	10,477
Cash dividends to common shareholders	(430)	(1,690)	(1,615)
Balance at end of period	$88,493	$84,996	$72,330
Accumulated other comprehensive income (loss):			
Balance at beginning of period	$10,083	$8,348	$10,326
Unrealized appreciation (depreciation) of investments, net of taxes	879	1,735	(1,978)
Balance at end of period	10,962	10,083	8,348
Foreign currency translation adjustments, net of taxes	(442)	(305)	(1,241)
Net derivative gains (losses) from cash flow hedging, net of taxes	(27)	(27)	(25)
Retirement plan liabilities, net of taxes	(639)	(641)	(115)
Balance at end of period	$9,854	$9,110	$6,967
Treasury stock, at cost:			
Balance at beginning of period	$(1,897)	$(2,197)	$(2,211)
Cost of shares acquired during the period	(167)	(20)	(176)
Issued under stock option plans	70	291	173
Other	1	29	17
Balance at end of period	($1,993)	$(1,897)	$(2,197)
Total shareholders' equity at end of year	$103,055	$101,677	$86,317

Cash Analysis

Cash Analysis	Period Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
Cash Flows from Operating Activities:			
Net income	$4,130	$14,048	$10,477
Noncash revenues, expenses, gains, and losses included in income:			
Net gains on AFS securities	(250)	(763)	(1,218)
Foreign exchange translation (gains)	305	1,795	(3,330)
Net unrealized (gains) on non-FP derivatives	61	(713)	878
Equity in income of partially owned companies	(1,329)	(3,990)	(1,421)
Amortization of DAC	2,921	11,578	10,693
Amortization of premium/discount of securities	38	699	207
Depreciation	646	2,374	2,200
Provision for finance receivable losses	87	495	435
Impairment Losses	467	944	598
Changes in operating assets and liabilities:			
General and life insurance reserves	4,190	13,173	27,299
Premiums and insurance balances receivable and payable	(1,192)	(1,214)	192
Reinsurance assets	223	1,665	(5,365)
Capitalization of DAC	(3,750)	(15,363)	(14,454)
Investment income due and accrued	(109)	(235)	(171)
Funds held under reinsurance treaties	(158)	(1,612)	770
Other policyholders' funds	223	(953)	518
Income taxes payable	1,076	2,003	1,543
Commissions, expenses, and taxes payable	661	408	140
Other assets and liabilities – net	774	331	2,966
Bonds, common and preferred stocks trading - FV	(1,260)	(7,851)	(5,448)
Trading assets and liabilities – net	1,805	(668)	2,272
Trading securities	(337)	1,339	(3,753)
Spot commodities	147	(128)	442
Net unrealized (gain) on swaps, options, forwards	962	(1,482)	934
Securities purchased under agreement to resell	78	(19,154)	11,725
Securities sold under agreements to repurchase	(2,100)	11,645	(12,534)
Securities sold but not yet purchased – MV	(20)	(1,899)	571
Finance receivables held for sale - originations/purchases	(2,433)	(10,786)	(13,070)
Sales of finance receivables – HFS	2,573	10,602	12,821
Other, net	204	541	(1,535)
Total adjustments	4,503	(7,219)	14,905
Net cash provided by operating activities	$8,633	$6,829	$25,382

Cash Analysis (continued)

Cash Analysis	Period Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
Cash Flows from Investing Activities:			
Sales and maturities of fixed maturity securities AFS	$30,145	$112,899	$140,076
Sales of equity securities AFS	2,112	12,475	11,661
Proceeds from fixed maturity securities HTM	18	205	46
Sales of flight equipment	27	697	573
Sales or distributions of other invested assets	2,698	14,087	14,899
Payments received on mortgage, policy, collateral, and guaranteed loans	658	5,165	3,679
Principal payments received on finance receivables HFI	3,349	12,586	12,461
Purchases of fixed maturity securities AFS	(34,273)	(146,465)	(175,657)
Purchases of equity securities AFS	(2,436)	(14,482)	(13,273)
Purchases of fixed maturity security HTM	(9)	(197)	(3,333)
Purchases of flight equipment	(1,917)	(6,009)	(6,193)
Purchases of other invested assets	(4,586)	(16,040)	(15,059)
Acquisitions of new businesses, net of cash acquired	(584)		
Mortgage, policy, collateral, and guaranteed loans issued	(2,326)	(7,438)	(5,310)
Finance receivables held for investment - originations and purchases	(3,409)	(13,830)	(17,276)
Change in securities lending collateral	(5,521)	(9,835)	(10,301)
Net additions to real estate, fixed assets, and other assets	(259)	(1,097)	(941)
Net change in short-term investments	(588)	(9,716)	760
Net change in non-AIGFP derivative assets and liabilities	38	(45)	688
Net cash used in investing activities	$(16,863)	$(67,040)	$(62,500)
Cash Flows from Financing Activities:			
Policyholders' contract deposits	$14,080	$54,195	$50,229
Policyholders' contract withdrawals	(14,682)	(41,866)	(35,797)
Change in other deposits	(1,340)	1,269	(957)
Change in commercial paper	279	2,952	(476)
Notes, bonds, loans and mortgages payable issued	19,186	58,763	53,624
Repayments on notes, bonds, loans and mortgages payable	(14,549)	(24,047)	(40,767)
Issuance of guaranteed investment agreements	3,740	12,265	13,437
Maturities of guaranteed investment agreements	979	(12,433)	(10,861)
Change in securities lending payable	(1,775)	9,789	10,437
Redemption of subsidiary company preferred stock	5,716	-	(100)
Issuance of treasury stock	52	163	82
Payments advanced to purchase shares	(3,000)	-	-
Acquisition of Treasury Stock	(16)	(20)	(176)
Cash dividends paid to shareholders	(430)	(1,638)	(1,421)
Other, net	112	398	(85)
Net cash provided by financing activities	$8,352	$59,790	$37,169

Cash Analysis (continued)

Cash Analysis	Period Ended 03/31/2007	Fiscal Year Ended 12/31/2006	Fiscal Year Ended 12/31/2005
SUMMARY:			
Net cash provided by operating activities	$8,633	$6,829	$25,382
Net cash used in investing activities	(16,863)	(67,040)	(62,500)
Net cash provided by financing activities	8,352	59,790	37,169
Effect on exchange rate changes on cash	(10)	114	(163)
Change in cash	112	(307)	(112)
Cash at beginning of year	1,590	1,897	2009
Cash at end of Period	$1,702	$1,590	$1,897

Risk Concentrations

AIG has a system for identifying, aggregating, and reporting risk concentrations. The following table lists AIG's top ten risk concentrations as of March 31, 2007. The company is refining its risk aggregation program and, through this refinement, may identify new risk concentrations or better define existing risk concentrations. Of these reported exposures, all are either cross-border or industry sector thus composed of various sub obligations. AIG's largest single obligor exposure as of the reporting date was to Citigroup at $7.5 billion.

AIG does not capture and aggregate operational risk and full-spectrum catastrophic risk; however, OTS expects to receive these results with 2008 reporting:

Concentration 03/31/2007	Amount ($ billions)	Concentration Type
Global Financial Institutions	$73.1	Industry
United Kingdom	$57.1	Cross-border Country
US Residential Mortgage	$55.8	US Real Estate
US Commercial Mortgage	$43.0	US Real Estate
Hong Kong	$24.7	Cross-border Country
Telecommunications	$19.6	Industry
Canada	$17.1	Cross-border Country
France	$16.9	Cross-border Country
Germany	$16.7	Cross-border Country
Japan	$16.1	Cross-border Country

Significant Intra-Group Transactions

The following table lists AIG's significant intra-group transactions (IGT) as of March 31, 2007. AIG subsidiaries report IGT on a quarterly basis to OTS via AIG's Comptrollers Group to capture significant transactions among AIG legal entities. AIG requires the subsidiaries to report any transactions over the threshold amount of $1.4 billion, which represents 5.0 percent of the Supplementary Capital Adequacy Requirement (SCAR). While the report is manual and labor intensive to develop, management considers it comprehensive. OTS suggests that IAD add the IGT process to the 2008 AIG internal audit program.

Transaction Description	Affiliate Paying Funds, Ceding Risk or Receiving Guarantees of Performance	Affiliate Receiving Funds, Assuming Risk, or Providing Guarantees of Performance
$6.1 billion in Loans	American General Life Insurance Co	AIG Financial Products Corp
$1.8 billion in Loans	American General Finance Inc	American General Finance Service
$4.8 billion in Loans	American General Finance Inc	American General Finance Service
$9.1 billion in Loans	American General Finance Inc	MorEquity, Inc.
$40.3 billion in Term Notes	AIG, Inc.	AIG Financial Products Corp
$8.5 billion in Hybrid Term Notes	AIG, Inc.	AIG Financial Products Corp
$19.8 billion in Guaranteed Investment Agreements	AIG, Inc.	AIG Financial Products Corp
$1.8 billion Lease Transaction	International Lease Finance Co	Whitney Leasing, Limited
$2.1 billion* in Ceded Insurance	National Union Fire Insurance Co	American Home Insurance Co
$3.3 billion in Assumed Insurance	Illinois National Insurance Co	National Union Fire Insurance Co
$591 million* in Ceded Insurance	National Union Fire Insurance Co	Commerce and Industry Insurance Co
$296 million* in Ceded Insurance	National Union Fire Insurance Co	New Hampshire Insurance Co
$296 million*in Ceded Insurance	National Union Fire Insurance Co	Insurance State of PA
$296 million* in Ceded Insurance	National Union Fire Insurance Co	Birmingham Insurance Company
$3.3 billion in Assumed Reinsurance	National Union Fire Insurance Co	American International Reinsurance Co
$2.4 billion in Assumed Reinsurance	AIA Insurance Co	American International Reinsurance Co
$3.5 billion in Ceded Insurance	American General Insurance Co	AIG Bermuda Insurance Co

Significant Intra-Group Transactions (continued)

Transaction Description	Affiliate Paying Funds, Ceding Risk or Receiving Guarantees of Performance	Affiliate Receiving Funds, Assuming Risk, or Providing Guarantees of Performance
$2.0 billion Investment in Affiliate	National Union Fire Insurance Co	AIG Cap Co
$2.5 billion Investment in Affiliate	National Union Fire Insurance Co	Lexington Insurance Co
$2.2 billion Investment in Affiliate	National Union Fire Insurance Co	International Lease Finance Co
$4.0 billion Investment in Affiliate	American Life Insurance Co	AIG, Inc.
$3.2 billion Investment in Affiliate	American General Finance Inc	American General Finance Corp
$17.9 billion Investment in Affiliate	AIG Inc.	American International Reinsurance Co
$4.0 billion Investment in Affiliate	AIG Inc.	American International Underwriters Overseas
$9.5 billion Investment in Affiliate	AIG Inc.	American Life Insurance Co
$17.3 billion Investment in Affiliates	AIG Inc.	AIG Property Casualty Insurance Group
$26.7 billion Investment in Affiliate	AIG Inc.	American General Corporation
$1.8 billion Tax Payment	AIG Inc.	Financial Services Division

* These transactions reflect net amounts between companies. Individual gross balances, representing ceded or assumed risk, exceed $1.4 billion. These transactions reflect risk transfer between AIG companies as part of general insurance pooling arrangements.

Miscellaneous

Targeted Reviews

OTS completed the following targeted reviews during the review period. OTS presented the review findings and discussed recommendations at quarterly senior management meetings and target review exit meetings. Management has been responsive in initiating corrective actions.

Subject: Consumer Finance Group **Start Date: 02/05/2007** **Exit Meeting Date: 03/21/2007 and 04/16/2007**
Recommendations: • OTS noted similar operating weaknesses and inefficiencies that AIG and CFG management identified as part of the CFG reorganization. OTS concurs with the need to continue the initiatives AIG and CFG management is undertaking to improve credit and risk management processes, including integrating macroeconomic metrics into the local level credit process and programs; developing compliance plans at the local level consistent with global corporate compliance plans and standards; refining compliance issues tracking and resolution between business lines and corporate groups; building the operational risk group risk assessment and monitoring; transitioning the IAD from process based to risk based; completing the 2007 audit plan under new standards, methodology, and allocation of resources; and, participating in conglomerate-wide projects to modernize financial reporting and CFG projects to upgrade underwriting platforms and budgeting systems.

Miscellaneous (continued)

Subject: International Lease Finance Corporation (ILFC)
Start Date: 02/20/2007
Exit Meeting Dates: 03/21/2007 & 04/16/07

Recommendations:

- Broaden the information ILFC gathers and reports in the Airline Rating List, or create a similar report, to categorize and stratify the risk profile of the lessee portfolio. ILFC should also consider reporting information on the number, type, average age, geographical location, and net book value of aircraft; lease maturities and lease payment status; and any other information that characterizes the portfolio.
- Implement a process for conducting a quarterly lessee portfolio delinquency summary analysis for quantitative trending and analyses of portfolio quality. The process should also report information on leading and lagging indicators relating to repossession, redeployment, delinquency, and lease defaults activities.
- Implement a process for conducting a quarterly summary analysis of aircraft lease rate factors by aircraft type, aggregate aircraft portfolio, and any other segmentation for trending and analyses of portfolio quality. The process should report information on lease terminations; number and net book value of leases; weighted average lease rate factors; recent (i.e. marginal) lease rate factors; and any other information that characterizes the portfolio.
- Provide AIG (either through the ILFC Board or appropriate AIG corporate control group) summary reports of analyses of lessee portfolio risk, lessee portfolio delinquency, and aircraft portfolio lease rate factors (for comparison with the cost of funds).
- Continue to upgrade ILFC technology and systems in consultation and coordination with the AIG Controller's Group (Project FIRE) and PwC.

Subject: AIG Financial Products Corp. (AIG-FP)
Start Date: 04/23/2007
Exit Meeting Dates: 07/30/2007

Recommendations:

- Fast track the May 22, 2007 Proposal on Potential Future Exposure and, as addressed within the Proposal, incorporate credit risk into stress testing. If AIG-FP and AIG management does not place higher priority on the proposal than other ongoing projects, provide a written statement outlining the rationale.
- Design and implement an exception based reporting system for credit exceptions (similar to the exception based reporting system for market risk sensitivities).

Subject: AIG Global Reinsurance Division (GRD) – Catastrophic Risk Management
Start Date: 04/25/2007
Exit Meeting Date: 07/30/2007

Recommendations:

- Periodically review (by the Board or a designated Board committee) AIG's risk appetite (acceptable levels of

Miscellaneous (continued)

exposure to catastrophic events).

- Continue to develop and refine procedures to improve the formal risk communication process, with specific emphasis on regular Board or Board committee reporting of AIG's integrated risk profile.
- Coordinate catastrophic insurance risk management procedures with emerging efforts to address simultaneous catastrophic credit, market, and operational risk events.

Subject: American General Finance, Inc. (AGF)
Start Date: 05/29/2007
Exit Meeting Date: 07/30/2007

Recommendations:

- Implement enhanced fraud prevention procedures based on industry best practices and consider the filing of Suspicious Activity Reports (SAR) for the Wilmington Finance and MorEquity origination channels.
- Revise internal audit policy and procedures to ensure that all auditable entities receive at least a limited review within a specific period.
- Perform an independent audit review of the branch network and MorEquity, Inc. during 2007 to review anti-predatory lending practices.

Holding Company Definitions

Holding Company Rating Definitions

The composite rating is the overall assessment of the holding company enterprise as reflected by its organizational structure, risk management, capital, and earnings. The composite rating encompasses both a forward-looking and current assessment of the consolidated enterprise, as well as an assessment of the relationship between the companies in the enterprise. The composite rating is not a simple numeric average of the CORE components; rather, the composite rating reflects OTS's judgment of the relative importance of each component to the operation of the holding company enterprise. Some components may receive more weight than others depending on the SLHC's activities and risk profile. Assignment of a composite rating may incorporate any factor that significantly affects the overall condition of the holding company enterprise, although generally the composite rating is closely related to the component ratings assigned.

Composite 1. A holding company enterprise in this group is sound in almost every respect and generally has components rated 1 or 2. Any weaknesses are minor, and the Board of directors and management can correct them in the normal course of business. The enterprise is able to withstand economic, financial, and risk exposure changes because of an effective organizational structure, solid risk management practices, more than sufficient capital and strong earnings. Cash flow is more than sufficient and adequately services debt and other obligations. This holding company enterprise exhibits strong performance and risk management practices relative to its size, complexity, and risk profile.

Composite 2. A holding company enterprise in this group is fundamentally sound but may have modest weaknesses. The Board of directors and management are capable and willing to correct any weaknesses. Generally, no component rating should be more severe than 3 for this holding company enterprise. The organizational structure, risk management practices, capital and earnings create stability, and this holding company enterprise is capable of withstanding business fluctuations. Cash flow is adequate to service obligations. Overall, risk management practices are satisfactory relative to the enterprise's size, complexity, and risk profile.

Composite 3. A holding company enterprise in this group raises some degree of supervisory concern in one or more of the component areas, with weaknesses that range from moderate to severe. The magnitude of the deficiencies is generally not severe enough to rate a component more severely than 4. Management may lack the ability or willingness to effectively address weaknesses within appropriate time frames. The holding company enterprise's capital structure and earnings leave it less resistant to adverse business conditions. The effectiveness of the organizational structure and risk management practices may be less than satisfactory relative to the enterprise's size, complexity, and risk profile. However, there is only a remote threat to the holding company enterprise's continued viability.

Composite 4. A holding company enterprise in this group has serious financial or managerial deficiencies that result in unsatisfactory performance. The supervisory concerns, which management and the Board are not satisfactorily addressing, range from severe to critically deficient. A holding company enterprise in this group generally does not have sufficient capital and earnings to withstand adverse business fluctuations. The effectiveness of the organizational structure and risk management practices are generally unacceptable relative to the enterprise's size, complexity, and risk profile. The enterprise may place undue pressure on subsidiaries to meet its cash flow by up streaming imprudent dividends or fees. Unless there is prompt action to correct these conditions, future viability could be impaired.

Composite 5. The magnitude and character of the risk management or financial weaknesses of a holding company enterprise in this category could lead to insolvency without immediate aid from shareholders or supervisory action. The volume and severity of problems are beyond the Board and management's ability or willingness to control or correct. The effectiveness of the organizational structure and risk management practices are inadequate relative to the enterprise's size, complexity, and risk profile. The inability to prevent liquidity or capital depletion places the holding company enterprise's continued viability in serious doubt.

Holding Company Risk/Complexity Category Definitions

The three holding company risk/complexity categories are defined as follows:

Category I

This category holding company is viewed as noncomplex and having relatively low risk.

Category II

Holding Company Definitions (continued)

This category holding company is considered to have a complex structure and/or a higher risk.

Category III

This category holding company is one of the most complex or highest risk holding companies. It is made up of a number of different companies or legal enterprises that offer products from more than one financial sector.