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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(Mark One)

☑ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2008

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number 1-8787

American International Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**13-2592361**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
70 Pine Street, New York, New York	**10270**
(Address of principal executive offices)	*(Zip Code)*

Registrant's telephone number, including area code (212) 770-7000

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, Par Value $2.50 Per Share	New York Stock Exchange
5.75% Series A-2 Junior Subordinated Debentures	New York Stock Exchange
4.875% Series A-3 Junior Subordinated Debentures	New York Stock Exchange
6.45% Series A-4 Junior Subordinated Debentures	New York Stock Exchange
7.70% Series A-5 Junior Subordinated Debentures	New York Stock Exchange
Corporate Units (composed of stock purchase contracts and junior subordinated debentures)	New York Stock Exchange
NIKKEI 225 ® Index Market Index Target-Term Securities ® due January 5, 2011	NYSE Arca

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☑ No ☐

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☑

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Act.

Large accelerated filer ☑ Accelerated filer ☐ Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes

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☐ No ☑

The aggregate market value of the voting and nonvoting common equity held by nonaffiliates of the registrant computed by reference to the price at which the common equity was last sold of $26.46 as of June 30, 2008 (the last business day of the registrant's most recently completed second fiscal quarter), was approximately $61,753,000,000.

As of January 30, 2009, there were outstanding 2,690,747,320 shares of Common Stock, $2.50 par value per share, of the registrant.

DOCUMENTS INCORPORATED BY REFERENCE

Document of the Registrant	Form 10-K Reference Locations
Portions of the registrant's definitive proxy statement for the 2009 Annual Meeting of Shareholders	Part III, Items 10, 11, 12, 13 and 14

American International Group, Inc., and Subsidiaries

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American International Group, Inc., and Subsidiaries

Part I

Item 1. *Business*

American International Group, Inc. (AIG), a Delaware corporation, is a holding company which, through its subsidiaries, is engaged in a broad range of insurance and insurance-related activities in the United States and abroad. AIG's primary activities include both General Insurance and Life Insurance & Retirement Services operations. Other significant activities include Financial Services and Asset Management.

Liquidity Events and Transactions with the NY Fed and the United States Department of the Treasury

Liquidity Entering the Third Quarter of 2008

AIG parent entered the third quarter of 2008 with $17.6 billion of cash and cash equivalents, including the remaining proceeds from the issuance of $20 billion of common stock, equity units, and junior subordinated debt securities in May 2008. In addition, AIG's securities lending collateral pool held $10.4 billion of cash and other short-term investments. On August 18, 2008, AIG raised $3.25 billion through the issuance of 8.25% Notes Due 2018.

Strategic Review and Proposed Liquidity Measures

From mid-July and throughout August 2008, AIG's then Chief Executive Officer, Robert Willumstad, was engaged in a strategic review of AIG's businesses.

During this time period, AIG was engaged in a review of measures to address the liquidity concerns in AIG's securities lending portfolio and to address the ongoing collateral calls with respect to the AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries (collectively, AIGFP) super senior multi-sector credit default swap portfolio, which at July 31, 2008 totaled $16.1 billion. To facilitate this process, AIG asked a number of investment banking firms to discuss possible solutions to these issues. In late August, AIG engaged J.P. Morgan Securities, Inc. (J.P. Morgan) to assist in developing alternatives, including a potential additional capital raise.

Continuing Liquidity Pressures

Historically, under AIG's securities lending program, cash collateral was received from borrowers and invested by AIG primarily in fixed maturity securities to earn a spread. AIG had received cash collateral from borrowers of 100 to 102 percent of the value of the loaned securities. In light of more favorable terms offered by other lenders of securities, AIG accepted cash advanced by borrowers of less than the 102 percent historically required by insurance regulators. Under an agreement with its insurance company subsidiaries participating in the securities lending program, AIG parent deposited collateral in an amount sufficient to address the deficit. AIG parent also deposited amounts into the collateral pool to offset losses realized by the pool in connection with sales of impaired securities. Aggregate deposits by AIG parent to or for the benefit of the securities lending collateral pool through August 31, 2008 totaled $3.3 billion.

In addition, from July 1, 2008 to August 31, 2008, the continuing decline in value of the super senior collateralized debt obligation (CDO) securities protected by AIGFP's super senior credit default swap portfolio, together with ratings downgrades of such CDO securities, resulted in AIGFP posting additional collateral in an aggregate net amount of $5.9 billion.

By the beginning of September 2008, these collateral postings and securities lending requirements were placing increasing stress on AIG parent's liquidity.

Rating Agencies

In early September 2008, AIG met with the representatives of the principal rating agencies to discuss Mr. Willumstad's strategic review as well as the liquidity issues arising from AIG's securities lending program and AIGFP's super senior multi-sector CDO credit default swap portfolio. On Friday, September 12, 2008, Standard & Poor's, a division of The McGraw-Hill Companies, Inc. (S&P), placed AIG on CreditWatch with negative

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implications and noted that upon completion of its review, the agency could affirm AIG parent's current rating of AA- or lower the rating by one to three notches. AIG understood that both S&P and Moody's Investors Service (Moody's) would re-evaluate AIG's ratings early in the week of September 15, 2008. Also on Friday, September 12, 2008, AIG's subsidiaries, International Lease Finance Corporation (ILFC) and American General Finance, Inc. (AGF), were unable to replace all of their maturing commercial paper with new issuances of commercial paper. As a result, AIG advanced loans to these subsidiaries to meet their commercial paper obligations.

The Accelerated Capital Raise Attempt

As a result of S&P's action, AIG accelerated the process of attempting to raise additional capital and over the weekend of September 13 and 14, 2008 discussed potential capital injections and other liquidity measures with private equity firms, sovereign wealth funds and other potential investors. AIG kept the United States Department of the Treasury and the NY Fed informed of these efforts. AIG also engaged Blackstone Advisory Services LP to assist in developing alternatives, including a potential additional capital raise. Despite offering a number of different structures through this process, AIG did not receive a proposal it could act upon in a timely fashion. AIG's difficulty in this regard resulted in part from the dramatic decline in its common stock price from $22.76 on September 8, 2008 to $12.14 on September 12, 2008. This decrease in stock price made it unlikely that AIG would be able to raise the large amounts of capital that would be necessary if AIG's long-term debt ratings were downgraded.

AIG Attempts to Enter into a Syndicated Secured Lending Facility

On Monday, September 15, 2008, AIG was again unable to access the commercial paper market for its primary commercial paper programs, AIG Funding, ILFC and AGF. Payments under the programs totaled $2.2 billion for the day, and AIG advanced loans to ILFC and AGF to meet their funding obligations. In addition, AIG experienced returns under its securities lending programs which led to cash payments of $5.2 billion to securities lending counterparts on that day.

On Monday morning, September 15, 2008, AIG met with representatives of Goldman, Sachs & Co., J.P. Morgan and the NY Fed to discuss the creation of a $75 billion secured lending facility to be syndicated among a number of large financial institutions. The facility was intended to act as a bridge loan to meet AIG parent's liquidity needs until AIG could sell sufficient assets to stabilize and enhance its liquidity position. Goldman, Sachs & Co. and J.P. Morgan immediately commenced syndication efforts.

The Rating Agencies Downgrade AIG's Long-Term Debt Rating

In the late afternoon of September 15, 2008, S&P downgraded AIG's long-term debt rating by three notches, Moody's downgraded AIG's long-term debt rating by two notches and Fitch Ratings (Fitch) downgraded AIG's long-term debt rating by two notches. As a consequence of the rating actions, AIGFP estimated that it would need in excess of $20 billion in order to fund additional collateral demands and transaction termination payments in a short period of time. Subsequently, in a period of approximately 15 days following the rating actions, AIGFP was required to fund approximately $32 billion, reflecting not only the effect of the rating actions but also changes in market values and other factors.

The Private Sector Solution Fails

By Tuesday morning, September 16, 2008, it had become apparent that Goldman, Sachs & Co. and J.P. Morgan were unable to syndicate a lending facility. Moreover, the downgrades, combined with a steep drop in AIG's common stock price to $4.76 on September 15, 2008, had resulted in counterparties withholding payments from AIG and refusing to transact with AIG even on a secured short-term basis. As a result, AIG was unable to borrow in the short-term lending markets. To provide liquidity, on Tuesday, September 16, 2008 both ILFC and AGF drew down on their existing revolving credit facilities, resulting in borrowings of approximately $6.5 billion and $4.6 billion, respectively.

Also, on September 16, 2008, AIG was notified by its insurance regulators that it would no longer be permitted to borrow funds from its insurance company subsidiaries under a revolving credit facility that AIG maintained with certain of its insurance subsidiaries acting as lenders. Subsequently, the insurance regulators required AIG to repay

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any outstanding loans under that facility and to terminate it. The intercompany facility was terminated effective September 22, 2008.

Fed Credit Agreement

By early Tuesday afternoon on September 16, 2008, it was clear that AIG had no viable private sector solution to its liquidity issues. At this point, AIG received the terms of a secured lending agreement that the NY Fed was prepared to provide. AIG estimated that it had an immediate need for cash in excess of its available liquid resources. That night, AIG's Board of Directors approved borrowing from the NY Fed based on a term sheet that set forth the terms of the secured credit agreement and related equity participation. Over the next six days, AIG elected Edward M. Liddy Director, Chairman and CEO, replacing Robert Willumstad in those positions, and negotiated a definitive credit agreement with the NY Fed and borrowed, on a secured basis, approximately $37 billion from the NY Fed before formally entering into the Credit Agreement, dated as of September 22, 2008 (as amended, the Fed Credit Agreement) between AIG and the NY Fed, which established the credit facility (Fed Facility).

On September 22, 2008, AIG entered into the Fed Credit Agreement in the form of a two-year secured loan and a Guarantee and Pledge Agreement (the Pledge Agreement) with the NY Fed. See Note 13 to the Consolidated Financial Statements for more information regarding the terms of and borrowings under the Fed Credit Agreement and subsequent amendments thereto.

AIG's Strategy for Stabilization and Repayment of the Fed Facility

In October 2008, AIG announced a restructuring of its operations, which contemplated retaining its U.S. property and casualty and foreign general insurance businesses and a continuing ownership interest in certain of its foreign life insurance operations while exploring disposition opportunities for its remaining businesses. Proceeds from sales of these assets are contractually required to be applied as mandatory prepayments pursuant to the terms of the Fed Credit Agreement. Also in October 2008, AIGFP began unwinding its businesses and portfolios. AIGFP is now entering into new derivative transactions only to maintain its current portfolio, reduce risk and hedge the currency and interest rate risks associated with its affiliated businesses. As part of its orderly wind-down, AIGFP is also opportunistically terminating contracts. Due to the long-term duration of AIGFP's derivative contracts and the complexity of AIGFP's portfolio, AIG expects that an orderly wind-down of AIGFP will take a substantial period of time.

On November 9, 2008, AIG, the NY Fed and the United States Department of the Treasury announced a set of transactions that were implemented during the fourth quarter of 2008 pursuant to which, among other actions, AIG issued $40 billion of fixed-rate cumulative perpetual serial preferred stock (Series D Preferred Stock) to the United States Department of the Treasury, terminated $62 billion of credit default swaps written by AIGFP and resolved and terminated its U.S. securities lending program.

On March 2, 2009, AIG, the NY Fed and the United States Department of the Treasury announced agreements in principle to modify the terms of the Fed Credit Agreement and the Series D Preferred Stock and to provide a $30 billion equity capital commitment facility. The parties also announced their intention to take a number of other actions intended to strengthen AIG's capital position, enhance its liquidity, reduce its borrowing costs and facilitate AIG's asset disposition program.

See Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Note 23 to the Consolidated Financial Statements for a further discussion of this strategy.

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Principal Business Units

The principal business units in each of AIG's operating segments during 2008 are shown below. For information on AIG's business segments, see Note 3 to the Consolidated Financial Statements.

General Insurance

American Home Assurance Company (American Home)
National Union Fire Insurance Company of Pittsburgh, Pa. (National Union)
New Hampshire Insurance Company (New Hampshire)
Lexington Insurance Company (Lexington)
The Hartford Steam Boiler Inspection and Insurance Company (HSB) [1]
Transatlantic Reinsurance Company
United Guaranty Residential Insurance Company
American International Underwriters Overseas, Ltd. (AIUO)
AIU Insurance Company (AIUI)

Life Insurance & Retirement Services

Domestic:	Foreign:
American General Life Insurance Company (AIG American General)	American Life Insurance Company (ALICO)
American General Life and Accident Insurance Company (AGLA)	AIG Star Life Insurance Co., Ltd. (AIG Star Life)
The United States Life Insurance Company in the City of New York (USLIFE)	AIG Edison Life Insurance Company (AIG Edison Life)
The Variable Annuity Life Insurance Company (VALIC)	American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA)
AIG Annuity Insurance Company (AIG Annuity)	American International Reinsurance Company Limited (AIRCO)
AIG SunAmerica Life Assurance Company (AIG SunAmerica)	Nan Shan Life Insurance Company, Ltd. (Nan Shan)
	The Philippine American Life and General Insurance Company (Philamlife)

Financial Services

International Lease Finance Corporation (ILFC)
AIG Financial Products Corp. and AIG Trading Group Inc. and their respective subsidiaries
American General Finance, Inc. (AGF)
AIG Consumer Finance Group, Inc. (AIGCFG)
Imperial A.I. Credit Companies (A.I. Credit)

Asset Management

AIG SunAmerica Asset Management Corp. (SAAMCo)
AIG Global Asset Management Holdings Corp. and its subsidiaries and affiliated companies (collectively, AIG Investments)
AIG Private Bank Ltd. (AIG Private Bank) [2]
AIG Global Real Estate Investment Corp. (AIG Global Real Estate)

[1] On December 22, 2008, AIG entered into a contract to sell HSB Group, Inc., the parent company of HSB, to Munich Re Group for $742 million. Subject to satisfaction of certain closing conditions, including regulatory approvals, AIG expects the sale to close by the end of the first quarter of 2009.

[2] On December 1, 2008, AIG entered into a contract to sell AIG Private Bank to Aabar Investments PJSC for $328 million. Subject to satisfaction of certain closing conditions, including regulatory approvals, AIG expects the sale to close by the end of the first quarter of 2009.

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At December 31, 2008, AIG and its subsidiaries had approximately 116,000 employees.

AIG's Internet address for its corporate website is *www.aigcorporate.com.* AIG makes available free of charge, through the Investor Information section of AIG's corporate website, Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and Proxy Statements on Schedule 14A and amendments to those reports or statements filed or furnished pursuant to Section 13(a), 14(a) or 15(d) of the Securities Exchange Act of 1934 (the Exchange Act) as soon as reasonably practicable after such materials are electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). AIG also makes available on its corporate website copies of the charters for its Audit, Nominating and Corporate Governance and Compensation and Management Resources Committees, as well as its Corporate Governance Guidelines (which include Director Independence Standards), Director, Executive Officer and Senior Financial Officer Code of Business Conduct and Ethics, Employee Code of Conduct and Related-Party Transactions Approval Policy. Except for the documents specifically incorporated by reference into this Annual Report on Form 10-K, information contained on AIG's website or that can be accessed through its website is not incorporated by reference into this Annual Report on Form 10-K.

Throughout this Annual Report on Form 10-K, AIG presents its operations in the way it believes will be most meaningful, as well as most transparent. Certain of the measurements used by AIG management are "non-GAAP financial measures" under SEC rules and regulations. Statutory underwriting profit (loss) is determined in accordance with accounting principles prescribed by insurance regulatory authorities. For an explanation of why AIG management considers this "non-GAAP measure" useful to investors, see Management's Discussion and Analysis of Financial Condition and Results of Operations.

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance and various personal lines both domestically and abroad and constitute the AIG Property Casualty Group (formerly known as Domestic General Insurance) and the Foreign General Insurance Group.

AIG Property Casualty Group is comprised of Commercial Insurance, Transatlantic, Personal Lines and Mortgage Guaranty businesses.

AIG is diversified both in terms of classes of business and geographic locations. In General Insurance, workers' compensation business is the largest class of business written and represented approximately 11 percent of net premiums written for the year ended December 31, 2008. During 2008, 9 percent, 5 percent and 5 percent of the direct General Insurance premiums written (gross premiums less return premiums and cancellations, excluding reinsurance assumed and before deducting reinsurance ceded) were written in California, New York and Texas, respectively. No other state or foreign country accounted for more than five percent of such premiums.

The majority of AIG's General Insurance business is in the casualty classes, which tend to involve longer periods of time for the reporting and settling of claims. This may increase the risk and uncertainty with respect to AIG's loss reserve development.

Commercial Insurance

AIG's primary property casualty division is Commercial Insurance. Commercial Insurance's business in the United States and Canada is conducted through American Home, National Union, Lexington, HSB and certain other General Insurance company subsidiaries of AIG. During 2008, Commercial Insurance accounted for 47 percent of AIG's General Insurance net premiums written.

Commercial Insurance writes substantially all classes of business insurance, accepting such business mainly from insurance brokers. This provides Commercial Insurance the opportunity to select specialized markets and retain underwriting control. Any licensed broker is able to submit business to Commercial Insurance without the traditional agent-company contractual relationship, but such broker usually has no authority to commit Commercial Insurance to accept a risk.

In addition to writing substantially all classes of business insurance, including large commercial or industrial property insurance, excess liability, inland marine, environmental, workers' compensation and excess and umbrella coverages, Commercial Insurance offers many specialized forms of insurance such as aviation, accident and health,

equipment breakdown, directors and officers liability (D&O), difference-in-conditions, kidnap-ransom, export credit and political risk, and various types of professional errors and omissions coverages. Also included in Commercial Insurance are the operations of AIG Risk Management, which provides insurance and risk management programs for large corporate customers and is a leading provider of customized structured insurance products, and AIG Environmental, which focuses specifically on providing specialty products to clients with environmental exposures. Lexington writes surplus lines for risks on which conventional insurance companies do not readily provide insurance coverage, either because of complexity or because the coverage does not lend itself to conventional contracts. The AIG Worldsource Division introduces and coordinates AIG's products and services to U.S.-based multinational clients and foreign corporations doing business in the U.S.

Transatlantic

Transatlantic Holdings, Inc. (Transatlantic) subsidiaries offer reinsurance capacity on both a treaty and facultative basis both in the United States and abroad. Transatlantic structures programs for a full range of property and casualty products with an emphasis on specialty risk. Transatlantic is a public company owned 58.9 percent by AIG and therefore is included in AIG's consolidated financial statements.

Personal Lines

AIG's Personal Lines operations provide automobile insurance through 21st Century Insurance, its direct marketing distribution channel, and the Agency Auto Division, its independent agent/broker distribution channel. It also provides a broad range of coverages for high net worth individuals through the AIG Private Client Group (Private Client Group). Coverages for the Personal Lines operations are written predominantly in the United States.

Mortgage Guaranty

The main business of the subsidiaries of United Guaranty Corporation (UGC) is the issuance of residential mortgage guaranty insurance, both domestically and internationally, that covers the first loss for credit defaults on high loan-to-value conventional first-lien mortgages for the purchase or refinance of one to four family residences.

On October 13, 2008, United Guaranty Residential Insurance Company (UGRIC) and United Guaranty Mortgage Indemnity Company (UGMIC) were downgraded from A+ to A- and placed on CreditWatch negative by S&P, and on February 13, 2009, UGRIC was downgraded from Aa3 to A3 and placed under review for possible downgrade by Moody's. All U.S-based mortgage insurers are currently subject to a Government Sponsored Enterprise (GSE) remediation plan as a result of industry-wide rating agency downgrades. UGRIC and UGMIC continue to write new domestic first-lien mortgage insurance and remain eligible mortgage insurers with Fannie Mae and Freddie Mac.

Foreign General Insurance

AIG's Foreign General Insurance group writes both commercial and consumer lines of insurance which is primarily underwritten through American International Underwriters (AIU), a marketing unit consisting of wholly owned agencies and insurance companies. The Foreign General Insurance group also includes business written by AIG's foreign-based insurance subsidiaries. The Foreign General Insurance group uses various marketing methods and multiple distribution channels to write both commercial and consumer lines insurance with certain refinements for local laws, customs and needs. AIU operates in Asia, the Pacific Rim, Europe, the U.K., Africa, the Middle East and Latin America. During 2008, the Foreign General Insurance group accounted for 32 percent of AIG's General Insurance net premiums written.

Discussion and Analysis of Consolidated Net Losses and Loss Expense Reserve Development

The reserve for net losses and loss expenses represents the accumulation of estimates for reported losses (case basis reserves) and provisions for losses incurred but not reported (IBNR), both reduced by applicable reinsurance recoverable and the discount for future investment income, where permitted. Net losses and loss expenses are charged to income as incurred.

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The liability for unpaid claims and claims adjustment expense (loss reserves) established with respect to foreign business are set and monitored in terms of the currency in which payment is expected to be made. Therefore, no assumption is included for changes in currency rates. See also Note 1(dd) to the Consolidated Financial Statements.

Management reviews the adequacy of established loss reserves utilizing a number of analytical reserve development techniques. Through the use of these techniques, management is able to monitor the adequacy of AIG's established reserves and determine appropriate assumptions for inflation. Also, analysis of emerging specific development patterns, such as case reserve redundancies or deficiencies and IBNR emergence, allows management to determine any required adjustments.

The "Analysis of Consolidated Losses and Loss Expense Reserve Development" table presents the development of net losses and loss expense reserves for calendar years 1998 through 2008. Immediately following this table is a second table that presents all data on a basis that excludes asbestos and environmental net losses and loss expense reserve development. The opening reserves held are shown at the top of the table for each year-end date. The amount of loss reserve discount included in the opening reserve at each date is shown immediately below the reserves held for each year. The undiscounted reserve at each date is thus the sum of the discount and the reserve held.

The upper half of the table presents the cumulative amounts paid during successive years related to the undiscounted opening loss reserves. For example, in the table that excludes asbestos and environmental losses, with respect to the net losses and loss expense reserve of $25.29 billion at December 31, 2001, by the end of 2008 (seven years later) $36.35 billion had actually been paid in settlement of these net loss reserves. In addition, as reflected in the lower section of the table, the original undiscounted reserve of $26.71 billion was reestimated to be $46.69 billion at December 31, 2008. This increase from the original estimate generally results from a combination of a number of factors, including reserves being settled for larger amounts than originally estimated. The original estimates will also be increased or decreased as more information becomes known about the individual claims and overall claim frequency and severity patterns. The redundancy (deficiency) depicted in the table, for any particular calendar year, presents the aggregate change in estimates over the period of years subsequent to the calendar year reflected at the top of the respective column heading. For example, the deficiency of $107 million at December 31, 2008 related to December 31, 2007 net losses and loss expense reserves of $70.03 billion represents the cumulative amount by which reserves in 2007 and prior years have developed unfavorably during 2008.

The bottom of each table below presents the remaining undiscounted and discounted net loss reserve for each year. For example, in the table that excludes asbestos and environmental losses, for the 2003 year-end, the remaining undiscounted reserves held at December 31, 2008 are $15.40 billion, with a corresponding discounted net reserve of $14.36 billion.

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Analysis of Consolidated Losses and Loss Expense Reserve Development

The following table presents for each calendar year the losses and loss expense reserves and the development thereof including those with respect to asbestos and environmental claims. See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Operating Review — General Insurance Operations — Liability for unpaid claims and claims adjustment expense.

(In millions)	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Net Reserves Held	$25,418	$25,636	$25,684	$26,005	$29,347	$36,228	$47,254	$57,476	$62,630	$69,288	$72,455
Discount (in Reserves Held)	897	1,075	1,287	1,423	1,499	1,516	1,553	2,110	2,264	2,429	2,574
Net Reserves Held (Undiscounted)	26,315	26,711	26,971	27,428	30,846	37,744	48,807	59,586	64,894	71,717	75,029
Paid (Cumulative) as of:											
One year later	7,205	8,266	9,709	11,007	10,775	12,163	14,910	15,326	14,862	16,531	
Two years later	12,382	14,640	17,149	18,091	18,589	21,773	24,377	25,152	24,388		
Three years later	16,599	19,901	21,930	23,881	25,513	28,763	31,296	32,295			
Four years later	20,263	23,074	26,090	28,717	30,757	33,825	36,804				
Five years later	22,303	25,829	29,473	32,685	34,627	38,087					
Six years later	24,114	28,165	32,421	35,656	37,778						
Seven years later	25,770	30,336	34,660	38,116							
Eight years later	27,309	31,956	36,497								
Nine years later	28,626	33,489									
Ten years later	29,799										

(In millions)	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Net Reserves Held (Undiscounted)	$26,315	$ 26,711	$ 26,971	$ 27,428	$ 30,846	$ 37,744	$48,807	$59,586	$64,894	$71,717	$75,029
Undiscounted Liability as of:											
One year later	25,897	26,358	26,979	31,112	32,913	40,931	53,486	59,533	64,238	71,873	
Two years later	25,638	27,023	30,696	33,363	37,583	49,463	55,009	60,126	64,764		
Three years later	26,169	29,994	32,732	37,964	46,179	51,497	56,047	61,242			
Four years later	28,021	31,192	36,210	45,203	48,427	52,964	57,618				
Five years later	28,607	33,910	41,699	47,078	49,855	54,870					
Six years later	30,632	38,087	43,543	48,273	51,560						
Seven years later	33,861	39,597	44,475	49,803							
Eight years later	34,986	40,217	45,767								
Nine years later	35,556	41,168									
Ten years later	36,161										
Net Redundancy / (Deficiency)	(9,846)	(14,457)	(18,796)	(22,375)	(20,714)	(17,126)	(8,811)	(1,656)	130	(156)	
Remaining Reserves (Undiscounted)	6,362	7,679	9,270	11,687	13,782	16,783	20,814	28,947	40,376	55,342	
Remaining Discount	453	537	644	768	903	1,040	1,190	1,398	1,691	2,113	
Remaining Reserves	5,909	7,142	8,626	10,919	12,879	15,743	19,624	27,549	38,685	53,229	

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The following table presents the gross liability (before discount), reinsurance recoverable and net liability recorded at each year-end and the reestimation of these amounts as of December 31, 2008:

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
						(In millions)					
Gross Liability, End of Year	$ 36,973	$ 37,278	$ 39,222	$ 42,629	$ 48,173	$ 53,387	$ 63,431	$79,279	$82,263	$87,929	$91,832
Reinsurance Recoverable, End of Year	10,658	10,567	12,251	15,201	17,327	15,643	14,624	19,693	17,369	16,212	16,803
Net Liability, End of Year	26,315	26,711	26,971	27,428	30,846	37,744	48,807	59,586	64,894	71,717	75,029
Reestimated Gross Liability	55,592	61,885	68,507	73,240	74,920	75,807	76,619	82,943	82,923	88,264	
Reestimated Reinsurance Recoverable	19,431	20,717	22,740	23,437	23,360	20,937	19,001	21,701	18,159	16,391	
Reestimated Net Liability	36,161	41,168	45,767	49,803	51,560	54,870	57,618	61,242	64,764	71,873	
Cumulative Gross Redundancy/(Deficiency)	(18,619)	(24,607)	(29,285)	(30,611)	(26,747)	(22,420)	(13,188)	(3,664)	(660)	(335)	

Analysis of Consolidated Losses and Loss Expense Reserve Development Excluding Asbestos and Environmental Losses and Loss Expense Reserve Development

The following table presents for each calendar year the losses and loss expense reserves and the development thereof excluding those with respect to asbestos and environmental claims. See also Management's Discussion and Analysis of Financial Condition and Results of Operations — Operating Review — General Insurance Operations — Liability for unpaid claims and claims adjustment expense.

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
						(In millions)					
Net Reserves Held	$24,554	$24,745	$24,829	$25,286	$28,650	$35,559	$45,742	$55,227	$60,451	$67,597	$71,062
Discount (in Reserves Held)	897	1,075	1,287	1,423	1,499	1,516	1,553	2,110	2,264	2,429	2,574
Net Reserves Held (Undiscounted)	25,451	25,820	26,116	26,709	30,149	37,075	47,295	57,337	62,715	70,026	73,636
Paid (Cumulative) as of:											
One year later	7,084	8,195	9,515	10,861	10,632	11,999	14,718	15,047	14,356	16,183	
Two years later	12,190	14,376	16,808	17,801	18,283	21,419	23,906	24,367	23,535		
Three years later	16,214	19,490	21,447	23,430	25,021	28,129	30,320	31,163			
Four years later	19,732	22,521	25,445	28,080	29,987	32,686	35,481				
Five years later	21,630	25,116	28,643	31,771	33,353	36,601					
Six years later	23,282	27,266	31,315	34,238	36,159						
Seven years later	24,753	29,162	33,051	36,353							
Eight years later	26,017	30,279	34,543								
Nine years later	26,832	31,469									
Ten years later	27,661										

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American International Group, Inc., and Subsidiaries

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
						(In millions)					
Net Reserves Held (Undiscounted)	$25,451	$ 25,820	$ 26,116	$ 26,709	$ 30,149	$ 37,075	$47,295	$57,337	$62,715	$70,026	$73,636
Undiscounted Liability as of:											
One year later	24,890	25,437	26,071	30,274	32,129	39,261	51,048	57,077	62,043	70,133	
Two years later	24,602	26,053	29,670	32,438	35,803	46,865	52,364	57,653	62,521		
Three years later	25,084	28,902	31,619	36,043	43,467	48,691	53,385	58,721			
Four years later	26,813	30,014	34,102	42,348	45,510	50,140	54,908				
Five years later	27,314	31,738	38,655	44,018	46,925	51,997					
Six years later	28,345	34,978	40,294	45,201	48,584						
Seven years later	30,636	36,283	41,213	46,685							
Eight years later	31,556	36,889	42,459								
Nine years later	32,113	37,795									
Ten years later	32,672										
Net Redundancy/(Deficiency)	(7,221)	(11,975)	(16,343)	(19,976)	(18,435)	(14,922)	(7,613)	(1,384)	194	(107)	
Remaining Reserves (Undiscounted)	5,011	6,326	7,916	10,332	12,425	15,396	19,427	27,558	38,986	53,950	
Remaining Discount	453	537	644	768	903	1,040	1,190	1,398	1,691	2,113	
Remaining Reserves	4,558	5,789	7,272	9,564	11,522	14,356	18,237	26,160	37,295	51,837	

The following table presents the gross liability (before discount), reinsurance recoverable and net liability recorded at each year-end and the reestimation of these amounts as of December 31, 2008:

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
						(In millions)					
Gross Liability, End of Year	$ 34,474	$ 34,666	$ 36,777	$ 40,400	$ 46,036	$ 51,363	$ 59,790	$73,808	$77,111	$83,551	$87,973
Reinsurance Recoverable, End of Year	9,023	8,846	10,661	13,691	15,887	14,288	12,495	16,472	14,396	13,525	14,337
Net Liability, End of Year	25,451	25,820	26,116	26,709	30,149	37,075	47,295	57,336	62,715	70,026	73,636
Reestimated Gross Liability	46,549	53,249	60,393	65,655	67,678	68,955	70,056	76,802	77,439	83,658	
Reestimated Reinsurance Recoverable	13,877	15,454	17,934	18,970	19,094	16,958	15,148	18,081	14,918	13,525	
Reestimated Net Liability	32,672	37,795	42,459	46,685	48,584	51,997	54,908	58,721	62,521	70,133	
Cumulative Gross Redundancy/(Deficiency)	(12,075)	(18,583)	(23,616)	(25,255)	(21,642)	(17,592)	(10,266)	(2,994)	(328)	(107)	

The liability for unpaid claims and claims adjustment expense as reported in AIG's consolidated balance sheet at December 31, 2008 differs from the total reserve reported in the Annual Statements filed with state insurance departments and, where appropriate, with foreign regulatory authorities. The differences at December 31, 2008 relate primarily to reserves for certain foreign operations not required to be reported in the United States for statutory reporting purposes. Further, statutory practices in the United States require reserves to be shown net of applicable reinsurance recoverable.

The reserve for gross losses and loss expenses is prior to reinsurance and represents the accumulation for reported losses and IBNR. Management reviews the adequacy of established gross loss reserves in the manner previously described for net loss reserves.

For further discussion regarding net reserves for losses and loss expenses, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Results of Operations — Segment Results — General Insurance Operations — Liability for unpaid claims and claims adjustment expense.

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services operations provide insurance, financial and investment-oriented products throughout the world. Insurance-oriented products consist of individual and group life, payout annuities (including structured settlements), endowment and accident and health policies. Retirement savings products consist generally of fixed and variable annuities.

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Foreign Life Insurance & Retirement Services

In its Foreign Life Insurance & Retirement Services businesses, AIG operates principally through ALICO, AIG Star Life, AIG Edison Life, AIA, Nan Shan and Philamlife. ALICO is incorporated in Delaware and all of its business is written outside the United States. ALICO has operations either directly or through subsidiaries in Europe, including the U.K., Latin America, the Caribbean, the Middle East, South Asia and the Far East, with Japan being the largest territory. AIA operates primarily in China (including Hong Kong), Singapore, Malaysia, Thailand, Korea, Australia, New Zealand, Vietnam, Indonesia and India. The operations in India are conducted through a joint venture, Tata AIG Life Insurance Company Limited. Nan Shan operates in Taiwan. Philamlife is the largest life insurer in the Philippines. AIG Star Life and AIG Edison Life operate in Japan. Operations in foreign countries comprised 80 percent of Life Insurance & Retirement Services premiums and other considerations in 2008.

The Foreign Life Insurance & Retirement Services companies have over 350,000 full and part-time agents, as well as independent producers, and sell their products largely to indigenous persons in local and foreign currencies. In addition to the agency outlets, these companies also distribute their products through direct marketing channels, such as mass marketing, and through brokers and other distribution outlets, such as financial institutions in 2008.

Domestic Life Insurance and Domestic Retirement Services

AIG's principal Domestic Life Insurance and Domestic Retirement Services operations include AGLA, AIG American General, AIG Annuity, USLIFE, VALIC and AIG SunAmerica. These companies utilize multiple distribution channels including independent producers, brokerage, career agents and financial institutions to offer life insurance, annuity and accident and health products and services, as well as financial and other investment products. The Domestic Life Insurance and Domestic Retirement Services operations comprised 20 percent of total Life Insurance & Retirement Services premiums and other considerations.

Reinsurance

AIG's General Insurance subsidiaries worldwide operate primarily by underwriting and accepting risks for their direct account and securing reinsurance on that portion of the risk in excess of the limit which they wish to retain. This operating policy differs from that of many insurance companies that will underwrite only up to their net retention limit, thereby requiring the broker or agent to secure commitments from other underwriters for the remainder of the gross risk amount.

Various AIG profit centers, including Commercial Insurance, AIU and AIG Risk Finance, as well as certain Life Insurance subsidiaries, use AIRCO as a reinsurer for certain of their businesses. In Bermuda, AIRCO discounts reserves attributable to certain classes of business assumed from other AIG subsidiaries.

For a further discussion of reinsurance, see Item 1A. Risk Factors — Reinsurance; Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Insurance Risk Management — Reinsurance; and Note 1 to the Consolidated Financial Statements.

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Insurance Investment Operations

A significant portion of AIG's General Insurance and Life Insurance & Retirement Services revenues are derived from AIG's insurance investment operations. The following table summarizes the investment results of the insurance operations:

Years Ended December 31,	Annual Average Cash and Invested Assets			Return on Average Cash and Invested Assets(b)	Return on Average Invested Assets(c)
	Cash (including short-term investments)(a)	Invested Assets(a)	Total		
			(In millions)		
General Insurance:					
2008	**$ 9,766**	**$111,435**	**$121,201**	**2.9%**	**3.1%**
2007	5,874	117,050	122,924	5.0	5.2
2006	3,201	102,231	105,432	5.4	5.6
2005	2,450	86,211	88,661	4.5	4.7
2004	2,012	73,338	75,350	4.2	4.4
Life Insurance & Retirement Services:					
2008	**$ 29,278**	**$385,980**	**$415,258**	**2.4%**	**2.6%**
2007	25,926	423,743	449,669	5.0	5.3
2006	13,698	392,348	406,046	4.9	5.1
2005	11,137	356,839	367,976	5.1	5.2
2004	7,737	309,627	317,364	4.9	5.1

(a) *Including investment income due and accrued and real estate. Also, includes collateral assets invested under the securities lending program.*

(b) *Net investment income divided by the annual average sum of cash and invested assets.*

(c) *Net investment income divided by the annual average invested assets.*

AIG's worldwide insurance investment policy places primary emphasis on investments in government and fixed income securities in all of its portfolios and, to a lesser extent, investments in high-yield bonds, common stocks, real estate, hedge funds and other alternative investments, in order to enhance returns on policyholders' funds and generate net investment income. The ability to implement this policy is somewhat limited in certain territories as there may be a lack of attractive long-term investment opportunities or investment restrictions may be imposed by the local regulatory authorities.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft leasing, capital markets, consumer finance and insurance premium finance. Together, the Aircraft Leasing, Capital Markets and Consumer Finance operations generate the majority of the revenues produced by the Financial Services operations. A.I. Credit also contributes to Financial Services results principally by providing insurance premium financing for both AIG's policyholders and those of other insurers.

Aircraft Leasing

AIG's Aircraft Leasing operations are the operations of ILFC, which generates its revenues primarily from leasing new and used commercial jet aircraft to foreign and domestic airlines. Revenues also result from the remarketing of commercial jet aircraft for ILFC's own account, and remarketing and fleet management services for airlines and financial institutions. See also Note 3 to Consolidated Financial Statements.

Capital Markets

Capital Markets is comprised of the operations of AIGFP, which engaged as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit,

currencies, energy, equities and interest rates. AIGFP also invests in a diversified portfolio of securities and principal investments and engages in borrowing activities that involve issuing standard and structured notes and other securities and entering into guaranteed investment agreements (GIAs). Due to the extreme market conditions experienced in 2008, the downgrades of AIG's credit ratings by the rating agencies, as well as AIG's intent to refocus on its core businesses, AIGFP has begun to unwind its businesses and portfolios including those associated with credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities. See Management's Discussion and Analysis of Financial Condition and Results of Operations — Outlook — Financial Services.

Consumer Finance

AIG's Consumer Finance operations in North America are principally conducted through AGF. AGF derives most of its revenues from finance charges assessed on real estate loans, secured and unsecured non-real estate loans and retail sales finance receivables. In the second quarter of 2008, AGF ceased its wholesale originations (originations through mortgage brokers). In light of severe stress in the U.S. housing sector, AGF also closed 179 branch offices and reduced new loan originations in the fourth quarter of 2008.

AIG's foreign consumer finance operations are principally conducted through AIGCFG. AIGCFG operates primarily in emerging and developing markets. AIGCFG has operations in Argentina, China, Brazil, Hong Kong, Mexico, the Philippines, Poland, Taiwan, Thailand, India and Colombia. Through February 18, 2009, AIGCFG had entered into contracts to sell certain of its operations in Taiwan, Thailand and the Philippines.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. These services and products are offered to individuals, pension funds and institutions (including AIG subsidiaries) globally through AIG's Spread-Based Investment business, Institutional Asset Management, and Brokerage Services and Mutual Funds business. Also included in Asset Management operations are the results of certain SunAmerica sponsored partnership investments.

Revenues and operating income (loss) for Asset Management are affected by the general conditions in the equity and credit markets. In addition, net realized gains (losses) and performance fee (carried interest) revenues are contingent upon various fund closings, maturity levels, investment management performance and market conditions.

Spread-Based Investment Business

AIG's Spread-Based Investment business includes the results of AIG's proprietary spread-based investment operations, the Matched Investment Program (MIP) and the Guaranteed Investment Contracts (GIC), which the MIP replaced. Due to the extreme market conditions experienced in 2008 and the downgrades of AIG's credit ratings, the MIP is currently in run-off. As previously disclosed, the GIC has been in run-off since the inception of the MIP in 2006. No additional debt issuances are expected for either the MIP or GIC for the foreseeable future.

Institutional Asset Management

AIG's Institutional Asset Management business, conducted through AIG Investments, provides an array of investment products and services globally to institutional investors, pension funds, AIG subsidiaries, AIG affiliates and high net worth investors. These products include traditional equity and fixed maturity securities, and a wide range of real estate, private banking and alternative asset classes. Services include investment advisory and sub-advisory services, investment monitoring and transaction structuring. Within the equity and fixed maturity asset classes, AIG Investments offers various forms of structured investments. Within the alternative asset class, AIG Investments offers hedge and private equity funds and fund-of-funds, direct investments and distressed debt investments. AIG Global Real Estate provides a wide range of real estate investment, development and management services for AIG subsidiaries, as well as for third-party institutional investors, pension funds and high net worth investors. AIG Global Real Estate also maintains a proprietary real estate investment portfolio through various joint venture platforms.

AIG expects to divest its Institutional Asset Management businesses consisting of investment services that are offered to third-party clients. The businesses offered for sale exclude those investment services providing traditional fixed income and shorter duration asset and liability management for AIG's insurance company subsidiaries. AIG expects to continue relationships with the divested businesses for other investment management services used by those subsidiaries.

AIG Investments previously acquired alternative investments, primarily consisting of direct private equity and private equity fund investments, with the intention of "warehousing" such investments until the investment or economic benefit thereof could be transferred to a fund or other AIG-managed investment product. However, AIG Investments' intended launch of such new products and funds has been indefinitely postponed. As a result of this decision, AIG will retain these investments with a net asset value of $1.1 billion at December 31, 2008 as proprietary investments until they can be divested. Unaffiliated investment commitments associated with these investments were approximately $720 million at December 31, 2008 and are expected to be funded over the next five years. AIG accounts for these investments based on the attributes of the investment using consolidation, equity or cost accounting methods, as appropriate.

Other Operations

AIG's Other operations include interest expense, restructuring costs, expenses of corporate staff not attributable to specific business segments, expenses related to efforts to improve internal controls, corporate initiatives, certain compensation plan expenses and the settlement costs more fully described in Note 14(a) to the Consolidated Financial Statements.

Certain AIG subsidiaries provide insurance-related services such as adjusting claims and marketing specialized products. Several wholly owned foreign subsidiaries of AIG operating in countries or jurisdictions such as Ireland, Bermuda, Barbados and Gibraltar provide insurance and related administrative and back office services to affiliated and unaffiliated insurance and reinsurance companies, including captive insurance companies unaffiliated with AIG.

For additional information regarding the business of AIG on a consolidated basis, the contributions made to AIG's consolidated revenues and operating income and the assets held by its General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management operations and Other operations, see Selected Financial Data, Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes 1 and 3 to the Consolidated Financial Statements.

Locations of Certain Assets

As of December 31, 2008, approximately 39 percent of the consolidated assets of AIG were located in foreign countries (other than Canada), including $7.7 billion of cash and securities on deposit with foreign regulatory authorities. Foreign operations and assets held abroad may be adversely affected by political developments in foreign countries, including tax changes, nationalization and changes in regulatory policy, as well as by consequence of hostilities and unrest. The risks of such occurrences and their overall effect upon AIG vary from country to country and cannot easily be predicted. If expropriation or nationalization does occur, AIG's policy is to take all appropriate measures to seek recovery of such assets. Certain of the countries in which AIG's business is conducted have currency restrictions which generally cause a delay in a company's ability to repatriate assets and profits. See also Item 1A. Risk Factors — Foreign Operations and Notes 1 and 3 to the Consolidated Financial Statements.

Regulation

AIG's operations around the world are subject to regulation by many different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In light of AIG's liquidity problems in the third and fourth quarters of 2008, AIG and its regulated subsidiaries have been subject to intense review and supervision around the world. Regulators have taken significant steps to protect the businesses of the entities they regulate. These steps have included:

- restricting or prohibiting the payment of dividends to AIG;

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- restricting or prohibiting other payments to AIG;
- requesting additional capital contributions by AIG;
- requesting that intercompany reinsurance reserves be covered by assets locally;
- restricting the business in which the subsidiaries may engage;
- requiring pre-approval of all proposed transactions between the regulated subsidiaries and AIG or any with affiliates; and
- requiring more frequent reporting, including with respect to capital and liquidity positions.

These and other actions have made it challenging for AIG to continue to engage in business in the ordinary course. AIG does not expect these conditions to change until its financial situation stabilizes.

In 1999, AIG became a unitary thrift holding company within the meaning of the Home Owners' Loan Act (HOLA) when the Office of Thrift Supervision (OTS) granted AIG approval to organize AIG Federal Savings Bank. AIG is subject to OTS regulation, examination, supervision and reporting requirements. In addition, the OTS has enforcement authority over AIG and its subsidiaries. Among other things, this permits the OTS to restrict or prohibit activities that are determined to be a serious risk to the financial safety, soundness or stability of AIG's subsidiary savings association, AIG Federal Savings Bank.

Under prior law, a unitary savings and loan holding company, such as AIG, was not restricted as to the types of business in which it could engage, provided that its savings association subsidiary continued to be a qualified thrift lender. The Gramm-Leach-Bliley Act of 1999 (GLBA) provides that no company may acquire control of an OTS regulated institution after May 4, 1999 unless it engages only in the financial activities permitted for financial holding companies under the law or for multiple savings and loan holding companies. The GLBA, however, grandfathered the unrestricted authority for activities with respect to a unitary savings and loan holding company existing prior to May 4, 1999, so long as its savings association subsidiary continues to be a qualified thrift lender under the HOLA. As a unitary savings and loan holding company whose application was pending as of May 4, 1999, AIG is grandfathered under the GLBA and generally is not restricted under existing laws as to the types of business activities in which it may engage, provided that AIG Federal Savings Bank continues to be a qualified thrift lender under the HOLA.

Certain states require registration and periodic reporting by insurance companies that are licensed in such states and are controlled by other corporations. Applicable legislation typically requires periodic disclosure concerning the corporation that controls the registered insurer and the other companies in the holding company system and prior approval of intercorporate services and transfers of assets (including in some instances payment of dividends by the insurance subsidiary) within the holding company system. AIG's subsidiaries are registered under such legislation in those states that have such requirements.

AIG's insurance subsidiaries, in common with other insurers, are subject to regulation and supervision by the states and by other jurisdictions in which they do business. Within the United States, the method of such regulation varies but generally has its source in statutes that delegate regulatory and supervisory powers to an insurance official. The regulation and supervision relate primarily to approval of policy forms and rates, the standards of solvency that must be met and maintained, including risk-based capital, the licensing of insurers and their agents, the nature of and limitations on investments, restrictions on the size of risks that may be insured under a single policy, deposits of securities for the benefit of policyholders, requirements for acceptability of reinsurers, periodic examinations of the affairs of insurance companies, the form and content of reports of financial condition required to be filed, and reserves for unearned premiums, losses and other purposes. In general, such regulation is for the protection of policyholders rather than the equity owners of these companies.

AIG has taken various steps to enhance the capital positions of the AIG Property Casualty Group companies. AIG entered into capital maintenance agreements with these companies that set forth procedures through which AIG will provide ongoing capital support. Also, in order to allow the AIG Property Casualty Group companies to record as an admitted asset at December 31, 2008 certain reinsurance ceded to non-U.S. reinsurers (which has the effect of maintaining the level of the statutory surplus of such companies), AIG obtained and entered into reimbursement agreements for approximately $1.6 billion of letters of credit issued

by several commercial banks in favor of certain AIG Property Casualty Group companies and funded trusts totalling $2.9 billion. Finally, AIG has agreed to contribute capital to the AIG Property Casualty Group companies that hold shares of Transatlantic if, upon selling their Transatlantic shares they receive less than the shares' statutory book value. The amount of the capital contribution would equal the difference between the aggregate statutory book value of the shares they sold and the aggregate cash proceeds they received in respect to those shares.

In the U.S., the Risk-Based Capital (RBC) formula is designed to measure the adequacy of an insurer's statutory surplus in relation to the risks inherent in its business. Thus, inadequately capitalized general and life insurance companies may be identified. The U.S. RBC formula develops a risk-adjusted target level of statutory surplus by applying certain factors to various asset, premium and reserve items. Higher factors are applied to more risky items and lower factors are applied to less risky items. Thus, the target level of statutory surplus varies not only as a result of the insurer's size, but also based on the risk profile of the insurer's operations.

The RBC Model Law provides for four incremental levels of regulatory attention for insurers whose surplus is below the calculated RBC target. These levels of attention range in severity from requiring the insurer to submit a plan for corrective action to placing the insurer under regulatory control.

The statutory surplus of each of AIG's AIG Property Casualty Group and U.S.-based Life Insurance subsidiaries exceeded their RBC minimum required levels as of December 31, 2008.

To the extent that any of AIG's insurance entities would fall below prescribed levels of statutory surplus, it would be AIG's intention to provide appropriate capital or other types of support to that entity.

A substantial portion of AIG's General Insurance business and a majority of its Life Insurance business is conducted in foreign countries. The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as the underwriting companies operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification or revocation by such authorities, and these subsidiaries could be prevented from conducting business in certain of the jurisdictions where they currently operate. A change in control of AIG, such as that resulting from the issuance of the Series C Preferred Stock (described in Note 15 to the Consolidated Financial Statements), or changes in the ownership of a regulated subsidiary that may result from a disposition of the subsidiary or the repayment of outstanding amounts under the Fed Facility with subsidiary preferred equity, may also trigger change of control requirements in jurisdictions around the world and result in other regulatory actions.

In addition to licensing requirements, AIG's foreign operations are also regulated in various jurisdictions with respect to currency, policy language and terms, advertising, amount and type of security deposits, amount and type of reserves, amount and type of capital to be held, amount and type of local investment and the share of profits to be returned to policyholders on participating policies. Some foreign countries regulate rates on various types of policies. Certain countries have established reinsurance institutions, wholly or partially owned by the local government, to which admitted insurers are obligated to cede a portion of their business on terms that may not always allow foreign insurers, including AIG subsidiaries, full compensation. In some countries, regulations governing constitution of technical reserves and remittance balances may hinder remittance of profits and repatriation of assets.

See Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Regulation and Supervision and Note 16 to Consolidated Financial Statements.

Competition

AIG's businesses operate in highly competitive environments, both domestically and overseas. Principal sources of competition are insurance companies, banks, investment banks and other non-bank financial institutions.

The insurance industry in particular is highly competitive. Within the United States, AIG's General Insurance subsidiaries compete with approximately 3,400 other stock companies, specialty insurance organizations, mutual companies and other underwriting organizations. AIG's Life Insurance & Retirement Services subsidiaries compete in the United States with approximately 2,100 life insurance companies and other participants in related financial services fields. Overseas, AIG's subsidiaries compete for business with the foreign insurance operations of large U.S. insurers and with global insurance groups and local companies in particular areas in which they are active.

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As a result of the reduction of the credit ratings of AIG and its subsidiaries, uncertainty relating to AIG's financial condition and AIG's asset disposition plan, AIG's businesses have faced and continue to face intense competition to retain existing customers and to maintain business with existing customers and counterparties at historical levels. Further, AIG has been and continues to be at a significant disadvantage in soliciting new customers. AIG expects these difficult conditions to continue for the foreseeable future.

Competition is also intense for key employees. The announced asset dispositions, decline in AIG's common stock price and uncertainty surrounding AIG's financial condition have adversely affected AIG's ability to retain key employees and to attract new employees. While AIG has granted retention awards and taken other steps to retain its key employees, no assurance can be given that these actions will be successful.

For a further discussion of the risks of AIG's disadvantage in soliciting new customers and losing key employees, see item 1A. Risk Factors — Employees.

Directors and Executive Officers of AIG

All directors of AIG are elected for one-year terms at the annual meeting of shareholders. All executive officers are elected to one-year terms, but serve at the pleasure of the Board of Directors.

Except as hereinafter noted, each of the executive officers has, for more than five years, occupied an executive position with AIG or companies that are now its subsidiaries. There are no arrangements or understandings between any executive officer and any other person pursuant to which the executive officer was elected to such position. Prior to joining AIG in September 2008, Mr. Liddy served at the private equity investment firm of Clayton, Dubilier & Rice, Inc. during 2008. From January 1999 until his retirement in April 2008, Mr. Liddy served as Chairman of the Board of The Allstate Corporation (Allstate), the parent of Allstate Insurance Company. He also served as Chief Executive Officer of Allstate from January 1999 to December 2006 and President from January 1995 to May 2005. Ms. Reynolds was President and Chief Executive Officer of Safeco Corporation from January 2006 to September 2008 and Chairman from May 2008 to September 2008. Previously, Ms. Reynolds served as President and Chief Executive Officer of AGL Resources, an Atlanta-based energy holding company, from 2000 to 2005 and Chairman from 2002 to 2005. From January 2000 until joining AIG in May 2004, Dr. Frenkel served as Chairman of Merrill Lynch International, Inc. Prior to joining AIG in September 2006, Ms. Kelly served as Executive Vice President and General Counsel of MCI/WorldCom. Previously, she was Senior Vice President and General Counsel of Sears, Roebuck and Co. from 1999 to 2003. From June 2004 until joining AIG in May 2007, Mr. Kaslow was a managing partner of QuanStar Group, LLC (an advisory services firm), and, from January 2002 until May 2004, Mr. Kaslow was Senior Executive Vice President of Human Resources for Vivendi Universal (an entertainment and telecommunications company).

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Set forth below is information concerning the directors and executive officers of AIG as of February 18, 2009.

Name	Title	Age	Served as Director or Officer Since
Stephen F. Bollenbach	Director	66	2008
Dennis D. Dammerman	Director	63	2008
Martin S. Feldstein	Director	69	1987
Edward M. Liddy	Director and Chief Executive Officer	63	2008
George L. Miles, Jr.	Director	67	2005
Suzanne Nora Johnson	Director	51	2008
Morris W. Offit	Director	72	2005
James F. Orr III	Director	65	2006
Virginia M. Rometty	Director	50	2006
Michael H. Sutton	Director	67	2005
Edmund S. W. Tse	Director, Senior Vice Chairman — Life Insurance	70	1996
Richard H. Booth	Vice Chairman — Transition Planning and Chief Administrative Officer	61	2008
Jacob A. Frenkel	Vice Chairman — Global Economic Strategies	64	2004
Anastasia D. Kelly	Vice Chairman — Legal, Human Resources, Corporate Communications and Corporate Affairs	59	2006
Paula R. Reynolds	Vice Chairman — Chief Restructuring Officer	52	2008
Frank G. Wisner	Vice Chairman — External Affairs	70	1997
David L. Herzog	Executive Vice President and Chief Financial Officer	49	2005
Rodney O. Martin, Jr.	Executive Vice President — Life Insurance	56	2002
Kristian P. Moor	Executive Vice President — AIG Property Casualty Group	49	1998
Win J. Neuger	Executive Vice President	59	1995
Nicholas C. Walsh	Executive Vice President — Foreign General Insurance	58	2005
Jay S. Wintrob	Executive Vice President — Retirement Services	51	1999
William N. Dooley	Senior Vice President — Financial Services	56	1992
Andrew J. Kaslow	Senior Vice President and Chief Human Resources Officer	58	2007
Robert E. Lewis	Senior Vice President and Chief Risk Officer	57	1993
Monika M. Machon	Senior Vice President and Chief Investment Officer	48	2009
Brian T. Schreiber	Senior Vice President — Global Capital Planning and Analysis	43	2002

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American International Group, Inc., and Subsidiaries

Item 1A. ***Risk Factors***

AIG has been significantly and adversely affected by recent events in the marketplace as well as in its businesses, and is subject to significant risks, as discussed below. Many of these risks are interrelated and occur under similar business and economic conditions, and the occurrence of certain of them may in turn cause the emergence, or exacerbate the effect, of others. Such a combination could materially increase the severity of the impact on AIG. As a result, should certain of these risks emerge, AIG may need additional support from the U.S. government. Without additional support from the U.S. government, in the future there could exist substantial doubt about AIG's ability to continue as a going concern. See Management's Discussion and Analysis of Financial Condition and Results of Operations — Consideration of AIG's Ability to Continue as a Going Concern and Note 1 to the Consolidated Financial Statements for a further discussion.

Proposed Transactions with the NY Fed and the United States Department of the Treasury

No assurance can be given that the NY Fed and the United States Department of the Treasury will complete the proposed transactions with AIG. AIG has entered into certain agreements in principle and announced intentions to enter into transactions with the NY Fed and the United States Department of the Treasury described below and in Note 23 to the Consolidated Financial Statements. These proposed transactions are designed to promote AIG's restructuring. Neither agreements in principle nor the intentions are legally binding, and neither the NY Fed nor the United States Department of the Treasury is bound to proceed with the transactions or complete them on the terms currently contemplated. AIG, however, expects to be able to complete these transactions and others necessary to enable an orderly restructuring and understands that the NY Fed and the United States Department of the Treasury remain committed to providing AIG with continued support. If AIG is unable to complete one or more of the proposed transactions, AIG's credit ratings may be downgraded and AIG may not be able to complete its restructuring plan. See Credit and Financial Strength Ratings for a discussion of the impact of a downgrade in AIG's credit ratings.

The proposed repayment of outstanding amounts under the Fed Facility with subsidiary preferred equity in holding companies for AIA and ALICO is complex and may need to be restructured. The NY Fed's proposed investment in two new holding companies for AIA and ALICO is unprecedented and it is possible that the terms of the exchange may change, perhaps materially.

Business and Credit Environment

AIG's businesses, results of operations and financial condition have been materially and adversely affected by market conditions and will be materially affected by these conditions for the foreseeable future. During 2008, worldwide economic conditions significantly deteriorated and the United States economy and most other major economies entered into a recession. It is difficult to predict how long global recessionary conditions will exist or the manner in which AIG's markets, products, financial condition and businesses will be negatively affected in the future.

The global financial crisis has resulted in a lack of liquidity, highly volatile markets, a steep depreciation in asset values across all classes, an erosion of investor confidence, a widening of credit spreads, a lack of price transparency in many markets and the collapse or merger of several prominent financial institutions. Difficult economic conditions also resulted in increased unemployment and a severe decline in business activity across a wide range of industries and regions. Global regulators, governments and central banks have taken a number of unprecedented steps to address these issues but these steps have so far failed to prevent financial markets from declining by a very substantial amount, both in percentage terms and in absolute terms. It is unclear whether these measures will be effective or, if effective, when markets will stabilize.

AIG has been materially and adversely affected by these conditions and events in a number of ways, including:

- the need to enter into transactions with the NY Fed and the United States Department of the Treasury, and to participate in generally available governmental programs addressing disruptions in financial markets;
- severe and continued declines in the valuation and performance of its investment portfolio across all asset classes, leading to decreased investment income, material unrealized and realized losses,

including other-

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than-temporary impairments, both of which decreased AIG's shareholders' equity and, to a lesser extent, the regulatory capital of its subsidiaries;

- significant credit losses due to the failure of, or governmental intervention with respect to, several prominent institutions;
- impairment of goodwill in its insurance and financial services businesses; and
- a general decline in business activity leading to reduced premium volume, increases in surrenders or cancellations of policies and increased competition from other insurers.

The consequences of these conditions have been more severe for AIG than for other insurers. Since the third quarter of 2008, AIG's principal sources of liquidity have been the Fed Facility and issuances of commercial paper under the Commercial Paper Funding Facility established by the NY Fed (CPFF). Authorization for the CPFF to accept new issuances of commercial paper is set to expire on October 30, 2009, with all outstanding issuances under the program maturing by January 2010. Since mid-September 2008, AIG has had no access to funding in public markets.

Certain of AIG's in-force and new business products in its life insurance businesses provide minimum benefit guarantees and crediting rates. Low interest rates driven by recessionary or deflationary environments could result in a negative spread between the yield produced by AIG's investment portfolios and the underlying costs of these products. While potentially providing short-term benefits, long-term profitability of the business could be negatively affected by this negative spread and the volume and value of new business could be adversely affected by low interest rate environments.

Credit and Financial Strength Ratings

Adverse ratings actions regarding AIG's long-term debt ratings by the major rating agencies would require AIG to post a substantial amount of additional collateral payments pursuant to, and/or permit the termination of, derivative transactions to which AIGFP is a party, which could further adversely affect AIG's business and its consolidated results of operations, financial condition and liquidity. Additional obligations to post collateral or the costs of assignment, termination or obtaining alternative credit could exceed the amounts then available under the Fed Facility. In the third quarter of 2008, S&P, Moody's, Fitch and A.M. Best Company (A.M. Best) each downgraded the credit ratings of AIG Inc. and most of the Insurer Financial Strength Ratings of AIG's insurance operating subsidiaries. In particular, S&P downgraded AIG's long-term debt rating by three notches, Moody's downgraded AIG's long-term debt rating by two notches, Fitch downgraded AIG's long-term debt rating by two notches and A.M. Best downgraded AIG's issuer credit rating from a+ to bbb and most of AIG's Insurer Financial Strength Ratings from A+ to A.

Subsequent to the rating actions referred to above, the following rating actions were taken:

- Moody's lowered AIG's Senior Unsecured Debt rating to A3 from A2 and ILFC's and American General Finance Corporation's (AGF Corp.) Senior Unsecured Debt ratings to Baa1 from A3. Most ratings remain under review for possible downgrade with ILFC revised to under review with direction uncertain.
- S&P revised the CreditWatch status on AIG's and AGF Corp.'s ratings from CreditWatch Developing to CreditWatch Negative in October 2008. Subsequently, S&P lowered its long-term debt rating on ILFC from A– to BBB+, and its short-term debt rating from A−1 to A−2. The ratings remain on Credit Watch Developing. S&P lowered its long-term debt rating on AGF Corp. from BBB to BB+, and its short-term debt rating from A−3 to B. The long-term debt ratings were assigned a Negative Outlook. S&P also revised the credit watch status of AIG's property and casualty subsidiaries from Credit Watch Developing to Credit Watch Negative.
- Fitch lowered its long-term debt ratings on AGF Corp. from A to BBB. The ratings remain on Rating Watch Evolving. Fitch also removed the ratings of AIG, Inc. and its property and casualty subsidiaries from Rating Watch Evolving and assigned them a Stable Outlook.

- A.M. Best affirmed the Insurer Financial Strength Ratings and Issuer Credit Ratings of the insurance subsidiaries of AIG, Inc. In addition A.M. Best affirmed the Issuer Credit Rating of AIG, Inc. These ratings were removed from Under Review with Negative Implications and assigned a Negative Outlook.

Credit ratings estimate a company's ability to meet its obligations and may directly affect the cost and availability to that company of unsecured financing and its eligibility for certain government sponsored funding programs such as the CPFF, as discussed below. In the event of a further downgrade of AIG's long-term senior debt ratings, AIGFP would be required to post additional collateral and AIG or certain of AIGFP's counterparties would be permitted to elect early termination of contracts.

It is estimated that as of the close of business on February 18, 2009, based on AIGFP's outstanding municipal GIAs, secured funding arrangements and financial derivative transactions (including AIGFP's super senior credit default swap portfolio) at that date, a one-notch downgrade of AIG's long-term senior debt ratings to Baa1 by Moody's and BBB+ by S&P would permit counterparties to make additional collateral calls and permit either AIGFP or the counterparties to elect early termination of contracts, resulting in up to approximately $8 billion of corresponding collateral postings and termination payments, a two-notch downgrade to Baa2 by Moody's and BBB by S&P would result in approximately $2 billion in additional collateral postings and termination payments, and a three-notch downgrade to Baa3 by Moody's and BBB- by S&P would result in approximately $1 billion in additional collateral and termination payments.

The actual amount of collateral that AIGFP would be required to post to counterparties in the event of such downgrades, or the aggregate amount of payments that AIG could be required to make, would depend on market conditions, the fair value of outstanding affected transactions and other factors prevailing at the time of the downgrade. If AIG is unable to secure sufficient additional funding through the Fed Facility or otherwise, AIG could become insolvent.

ILFC is a party to two Export Credit Agency (ECA) facilities that require ILFC to segregate security deposits and maintenance reserves related to aircraft financed under these facilities into separate accounts in the event of a downgrade in ILFC's credit ratings. In October 2008, Moody's downgraded ILFC's debt ratings, and ILFC was subsequently notified by the trustees under its ECA facilities that it would be required to segregate security deposits and maintenance reserves totaling approximately $260 million in separate accounts. Further downgrades would impose additional restrictions under these facilities, including the requirement to segregate rental payments and would require prior consent to withdraw funds from the segregated account.

For a further discussion of AIG's liquidity, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Capital Resources and Liquidity — Liquidity.

A downgrade in the short-term credit ratings of the commercial paper programs of certain AIG affiliates could make these issuers ineligible for participation in the CPFF. AIG Funding and affiliates Curzon Funding LLC and Nightingale Finance LLC currently obtain financing through participation in the CPFF. As of February 18, 2009, AIG Funding, Curzon Funding LLC and Nightingale Finance LLC had $6.1 billion, $6.8 billion and $1.1 billion, respectively, outstanding under the CPFF. However, in the event of a downgrade of the short-term credit ratings applicable to the commercial paper programs of these issuers, they may no longer qualify for participation in the CPFF and would likely have significant difficulty obtaining access to alternative sources of liquidity. AIG's subsidiary, ILFC, participated in the CPFF at December 31, 2008, but on January 21, 2009, S&P downgraded ILFC's short-term debt rating and, as a result, ILFC lost access to the CPFF. The CPFF purchases only U.S. dollar-denominated commercial paper (including asset-backed commercial paper) that is rated at least A-1/P-1/F1 by a major nationally recognized statistical rating organization (NRSRO) or, if rated by multiple major NRSROs, is rated at least A-1/P-1/F1 by two or more major NRSROs. Accordingly, these AIG entities will lose access to the CPFF if:

- AIG Funding's short-term rating is downgraded by any two of S&P, Moody's or Fitch;
- Curzon Funding LLC's short-term rating is downgraded by either S&P or Moody's; or
- Nightingale Finance LLC's short-term rating is downgraded by either S&P or Moody's.

Adverse rating actions could result in further reductions in credit limits extended to AIG and in a decline in the number of counterparties willing to transact with AIG or its affiliates. To appropriately manage risk, AIG needs trading counterparties willing to extend sufficient credit limits to purchase and sell securities, commodities and

other assets, as well as to conduct hedging activities. To the extent that counterparties are unwilling to trade with or to extend adequate credit limits to AIG or its subsidiaries, AIG could be exposed to open positions or other unhedged risks, resulting in increased volatility of results and increased losses.

A downgrade in the Insurer Financial Strength ratings of AIG's insurance companies could prevent the companies from writing new business and retaining customers and business. Insurer Financial Strength ratings are an important factor in establishing the competitive position of insurance companies. Insurer Financial Strength ratings measure an insurance company's ability to meet its obligations to contract holders and policyholders, help maintain public confidence in a company's products, facilitate marketing of products and enhance a company's competitive position.

Further downgrades of the Insurer Financial Strength ratings of AIG's insurance companies may prevent these companies from offering products and services or result in increased policy cancellations or termination of assumed reinsurance contracts. Moreover, a downgrade in AIG's credit ratings may, under credit rating agency policies concerning the relationship between parent and subsidiary ratings, result in a downgrade of the Insurer Financial Strength ratings of AIG's insurance subsidiaries.

Liquidity

AIG parent's ability to access funds from its subsidiaries is severely limited. As a holding company, AIG parent depends significantly on dividends, distributions and other payments from its subsidiaries to fund payments due on AIG's obligations, including its debt securities. Further, the majority of AIG's investments are held by its regulated subsidiaries. In light of AIG's current financial situation, many of AIG's regulated subsidiaries have been significantly restricted from making dividend payments, or advancing funds, to AIG, and AIG expects these restrictions to continue. AIG's subsidiaries also are limited in their ability to make dividend payments or advance funds to AIG because of the need to retain funds to conduct their own operations. These factors may hinder AIG's ability to access funds that AIG may need to make payments on its obligations, including those arising from day-to-day business activities.

AIG parent's ability to support its subsidiaries is limited. Historically, AIG has provided capital and liquidity to its subsidiaries to maintain regulatory capital ratios, comply with rating agency requirements and meet unexpected cash flow obligations. AIG's current limited access to liquidity may reduce or prevent AIG from providing support to its subsidiaries. If AIG is unable to provide support to a subsidiary having an immediate capital need, the subsidiary could become insolvent or, in the case of an insurance subsidiary or other regulated entity, could be seized by its regulator.

A significant portion of AIG's investments are illiquid and are difficult to sell, or to sell in significant amounts at acceptable prices, to generate cash to meet AIG's needs. AIG's investments in certain securities, including certain fixed income securities and certain structured securities, direct private equities, limited partnerships, hedge funds, mortgage loans, flight equipment, finance receivables and real estate are illiquid. These asset classes represented approximately 31 percent of the carrying value of AIG's total cash and invested assets at December 31, 2008. In addition, the steep decline in the U.S. real estate market and the current disruption in the credit markets have materially adversely affected the liquidity of other AIG securities portfolios, including its residential and commercial mortgage-backed securities portfolios. If AIG requires significant amounts of cash on short notice in excess of anticipated cash requirements or is required to post or return collateral in connection with AIGFP's derivative transactions, then AIG may have difficulty selling these investments or terminating these transactions in a timely manner or may be forced to sell or terminate them at unfavorable values.

If AIG fails to maintain compliance with the continued listing standards of the New York Stock Exchange (NYSE), the NYSE may initiate suspension and de-listing procedures, which will have a material adverse effect on the liquidity of AIG's common stock. AIG's common stock and other securities are listed on the NYSE. AIG is subject to the NYSE's continued listing requirements, including, among other things, the requirement that AIG maintain an average closing price equal to at least $1.00 over each consecutive 30-day trading period. The share price of AIG's common stock has declined significantly since the third quarter of 2008, and recently has begun to close below $1.00. AIG has not been informed of any non-compliance by the NYSE, but there is no assurance that AIG will be able to maintain compliance with the NYSE's continued listing standards or that, in the event of non-compliance, the NYSE will not take action to suspend and de-list AIG's securities from trading. A de-listing would

have a significant adverse effect on the liquidity of AIG's common stock, making it more difficult and expensive for AIG to raise additional capital.

Fed Facility and Series D Preferred Stock

The Fed Credit Agreement and the Series D Preferred Stock require AIG to devote significant resources to debt repayment and preferred stock dividends for the foreseeable future, thereby significantly reducing capital available for other purposes. AIG is required to repay the five-year Fed Facility primarily from the proceeds of sales of assets, including businesses. The amount available under the Fed Facility is permanently reduced by the amount of such repayments as they are made. In addition, the $40 billion liquidation preference of the Series D Fixed Rate Cumulative Perpetual Preferred Stock (Series D Preferred Stock) issued to the United States Department of the Treasury accumulates dividends at 10 percent per year. These dividends, and the dividends on any other series of preferred stock issued by AIG, are not deductible for tax purposes.

AIG's significant obligations require it to dedicate all of its proceeds from asset dispositions and a considerable portion of its cash flows from operations to the repayment of the Fed Facility, thereby reducing the funds available for investment in its businesses. Moreover, because AIG's debt service and preferred stock dividend obligations are very high, AIG may be more vulnerable to competitive pressures and have less flexibility to plan for or respond to changing business and economic conditions.

A further inability to effect asset sales in accordance with its asset disposition plan or to do so at acceptable prices could result in AIG not being able to repay its borrowings under the Fed Facility. See Capital Resources and Liquidity Requirements — Asset Disposition Plan for a discussion of AIG's asset disposition plan.

Borrowings available to AIG under the Fed Facility may not be sufficient to meet AIG's funding needs and additional financing may not be available or could be prohibitively expensive. Additional collateral calls, continued high surrenders of annuity and other policies, further downgrades in AIG's credit ratings or a further deterioration in AIGFP's remaining super senior credit default swap portfolio could cause AIG to require additional funding in excess of the borrowings available under the Fed Facility. In that event, AIG would be required to find additional financing and new financing sources. In the current business environment such financing could be difficult, if not impossible, to obtain and, if available, very expensive, and additional funding from the NY Fed, United States Department of the Treasury or other government sources may not be available. If AIG is unable to obtain sufficient financing to meet its capital needs, AIG could become insolvent.

Borrowings under the Fed Facility are subject to the NY Fed being satisfied with the collateral pledged by AIG. A condition to borrowing under the Fed Facility is that the NY Fed be satisfied with the collateral pledged by AIG (including its value). It is possible that the NY Fed may determine that AIG's collateral is insufficient to permit a borrowing for many reasons including:

- a decline in the value of AIG's businesses;
- poor performance in one or more of AIG's businesses; and
- low prices received by AIG in its asset disposition plan.

Such a determination could limit AIG's ability to borrow under the Fed Facility.

AIG must sell or otherwise dispose of significant assets to service the debt under the Fed Facility. AIG must make asset dispositions to repay the borrowings under the Fed Facility. A continued delay or inability to effect these dispositions at acceptable prices and on acceptable terms could result in AIG being unable to repay the Fed Facility by its maturity date.

While AIG has adopted an asset disposition plan, as discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity — Asset Disposition Plan, this plan may not be successfully executed due to, among other things:

- an inability of purchasers to obtain funding due to the deterioration in the credit markets;
- a general unwillingness of potential buyers to commit capital in the difficult current market environment;
- an adverse change in interest rates and borrowing costs; and

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- continued declines in AIG asset values and deterioration in its businesses.

Further, AIG may be unable to negotiate favorable terms in connection with asset sales, including with respect to price. As a result, AIG may need to modify its asset disposition plan to sell additional or different assets.

If AIG is not able to repay the Fed Facility from the proceeds of asset dispositions and cannot otherwise repay the Fed Facility in accordance with its terms, an event of default would result. In such an event, the NY Fed could enforce its security interest in AIG's pledged collateral. In addition, an event of default or declaration of acceleration under the Fed Credit Agreement could also result in an event of default under other agreements. In such an event, AIG would likely not have sufficient liquid assets to meet its obligations under such agreements.

The Fed Credit Agreement includes financial and other covenants that impose restrictions on AIG's financial and business operations. The Fed Credit Agreement requires AIG to maintain a minimum aggregate liquidity level and restricts AIG's ability to make certain capital expenditures. The Fed Credit Agreement also restricts AIG's and its restricted subsidiaries' ability to incur additional indebtedness, incur liens, merge, consolidate, sell assets, enter into hedging transactions outside the normal course of business, or pay dividends. These covenants could restrict AIG's business and thereby adversely affect AIG's results of operations.

Moreover, if AIG fails to comply with the covenants in the Fed Credit Agreement and is unable to obtain a waiver or amendment, an event of default would result. If an event of default were to occur, the NY Fed could, among other things, declare outstanding borrowings under the Fed Credit Agreement immediately due and payable and enforce its security interest in AIG's pledged collateral. In addition, an event of default or declaration of acceleration under the Fed Credit Agreement could also result in an event of default under AIG's other agreements.

AIG's results of operations and cash flows will be materially and adversely affected by a significant increase in interest expense and preferred stock dividends paid. AIG expects its results of operations in 2009 and in future periods to be significantly adversely affected by the recognition of interest expense on borrowings under the Fed Facility and by the payment of significant preferred stock dividends. In addition, the prepaid commitment fee asset of $23 billion associated with the Series C Preferred Stock (described below) was capitalized and is being amortized through interest expense over the term of the Fed Facility, which is five years.

The Series D Preferred Stock accrues dividends, payable if, as and when declared, at a rate of 10 percent per annum, or $4 billion, on the $40 billion of liquidation preference, which are not tax deductible.

Controlling Shareholder

Following the issuance of the Series C Preferred Stock to the AIG Credit Facility Trust, a trust for the sole benefit of the United States Treasury, the Trust, which is overseen by three independent trustees, will hold a controlling interest in AIG. AIG's interests and those of AIG's minority shareholders may not be the same as those of the Trust or the United States Treasury. In accordance with the Fed Credit Agreement, in early March 2009, AIG expects to issue 100,000 shares of Series C Perpetual, Convertible, Participating Preferred Stock, par value $5.00 per share and at an initial liquidation preference of $5.00 per share (the Series C Preferred Stock), to the AIG Credit Facility Trust, a trust for the sole benefit of the United States Treasury (together with its trustees, the Trust) established under the AIG Credit Facility Trust Agreement dated as of January 16, 2009 (as it may be amended from time to time, the Trust Agreement). The Trust will hold the Series C Preferred Stock for the sole benefit of the United States Treasury. The Series C Preferred Stock is entitled to:

- participate in any dividends paid on the common stock, with the payments attributable to the Series C Preferred Stock being approximately 77.9 percent of the aggregate dividends paid on common stock, treating the Series C Preferred Stock as converted; and
- to the extent permitted by law, vote with AIG's common stock on all matters submitted to AIG's shareholders and hold approximately 77.9 percent of the aggregate voting power of common stock, treating the Series C Preferred Stock as converted.

The dividends payable on and the total voting power of (i) the shares of common stock underlying the

Series C Preferred Stock, (ii) the 53,798,766 shares of common stock underlying the warrants issued to the United States Department of the Treasury on November 25, 2008 and (iii) the shares of common stock underlying the warrants to be issued to the United States Department of the Treasury in connection with the capital commitment facility will

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not exceed 79.9 percent of the aggregate dividends payable on and the voting power of the outstanding shares of common stock, treating the Series C Preferred Stock as converted.

The Series C Preferred Stock will remain outstanding even if the Fed Facility is repaid in full or otherwise terminates. In addition, upon shareholder approval and the filing with the Delaware Secretary of State of certain amendments to AIG's Restated Certificate of Incorporation, the Trust can convert at its option all or a portion of the Series C Preferred Stock into common stock.

As a result of its ownership of the Series C Preferred Stock, the Trust will be able, subject to the terms of the Trust Agreement and the Series C Preferred Stock, to elect all of AIG's directors and will be able, to the extent permitted by law, to control the vote on substantially all matters, including:

- approval of mergers or other business combinations;
- a sale of all or substantially all of AIG's assets;
- issuance of any additional common stock or other equity securities;
- the selection and tenure of AIG's Chief Executive Officer and other executive officers; and
- other matters that might be favorable to the United States Treasury.

Moreover, the Trust's ability to prevent any change in control of AIG could also have an adverse effect on the market price of the common stock.

The Trust may also, subject to the terms of the Trust Agreement and applicable securities laws, transfer all, or a portion of, the Series C Preferred Stock to another person or entity and, in the event of such a transfer, that person or entity could become the controlling shareholder.

Possible future sales of Series C Preferred Stock or common stock by the Trust could adversely affect the market for AIG common stock. Pursuant to the Series C Preferred Stock Purchase Agreement, dated as of March 1, 2009, between the Trust and AIG (the Series C Preferred Stock Purchase Agreement), AIG has agreed to file a shelf registration statement that will allow the Trust to publicly sell Series C Preferred Stock or any shares of common stock it receives upon conversion of the Series C Preferred Stock. In addition, the Trust could sell Series C Preferred Stock or shares of common stock without registration under certain circumstances, such as in a private transaction. Although AIG can make no prediction as to the effect, if any, that such sales would have on the market price of common stock, sales of substantial amounts of Series C Preferred Stock or common stock, or the perception that such sales could occur, could adversely affect the market price of common stock. If the Trust sells or transfers shares of Series C Preferred Stock or common stock as a block, another person or entity could become AIG's controlling shareholder.

Change of Control

The issuance of the Series C Preferred Stock may have adverse consequences for AIG and its subsidiaries with regulators and contract counterparties. The issuance of the Series C Preferred Stock will result in a change of control of AIG. A change of control of AIG triggers notice, approval and/or other regulatory requirements in many of the more than 130 countries and jurisdictions in which AIG and its subsidiaries operate. AIG has undertaken a worldwide review of the regulatory requirements arising in connection with the issuance of the Series C Preferred Stock, and has worked to achieve material compliance with applicable regulatory requirements. In this connection, AIG has submitted notices to regulators in the jurisdictions where its principal businesses are located, and currently has no knowledge that any regulator intends to impose any penalties or take any other actions as a result of the change in control of AIG in a manner that would be adverse in any material respect to AIG. However, in light of the large number of jurisdictions in which AIG and its subsidiaries operate and the complexity of assessing and addressing the regulatory requirements in each of the relevant jurisdictions, AIG has not been able to obtain all regulatory consents or approvals that may be required in connection with the issuance of the Series C Preferred Stock. Accordingly, no assurances can be provided that the failure to obtain all required consents or approvals will not have a material adverse effect on AIG's consolidated financial condition, results of operations or cash flows.

AIG and its subsidiaries are also parties to various contracts and other agreements that may be affected by a change of control of AIG. Although AIG believes the change of control arising from the issuance of the Series C

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Preferred Stock will not result in a breach of any material contract or agreement, no assurances can be given that AIG's counterparties to such contracts and agreements will not claim that breaches have occurred. If AIG were to be found to have breached any material contract or agreement, its consolidated financial condition, results of operations or cash flows could be materially adversely affected.

Concentration of Investments and Exposures

Concentration of AIG's investment portfolios in any particular segment of the economy may have adverse effects. AIG results of operations have been adversely affected and may continue to be adversely affected by a concentration in residential mortgage-backed, commercial mortgage-backed and other asset-backed securities. AIG also has significant exposures to financial institutions and, in particular, to money center and global banks. These types of concentrations in AIG's investment portfolios could have an adverse effect on the investment portfolios and consequently on AIG's consolidated results of operations or financial condition. While AIG seeks to mitigate this risk by having a broadly diversified portfolio, events or developments that have a negative effect on any particular industry, asset class, group of related industries or geographic region may have a greater adverse effect on the investment portfolios to the extent that the portfolios are concentrated. Furthermore, AIG's ability to sell assets relating to such particular groups of related assets may be limited if other market participants are seeking to sell at the same time.

Concentration of AIG's insurance and other risk exposures may have adverse effects. AIG seeks to manage the risks to which it is exposed as a result of the insurance policies, derivatives and other obligations that it undertakes to customers and counterparties by monitoring the diversification of its exposures by exposure type, industry, geographic region, counterparty and otherwise and by using reinsurance, hedging and other arrangements to limit or offset exposures that exceed the limits it wishes to retain. In certain circumstances, or with respect to certain exposures, such risk management arrangements may not be available on acceptable terms, or AIG's exposure in absolute terms may be so large that even slightly adverse experience compared to AIG's expectations may cause a material adverse effect on AIG's consolidated financial condition or results of operations.

Casualty Insurance Underwriting and Reserves

Casualty insurance liabilities are difficult to predict and may exceed the related reserves for losses and loss expenses. AIG has announced that it intends to focus its resources on its core property and casualty insurance businesses while selling other businesses to repay the borrowing under the Fed Credit Agreement. As a result, AIG expects to become more reliant on these businesses.

Although AIG annually reviews the adequacy of the established liability for unpaid claims and claims adjustment expense, there can be no assurance that AIG's loss reserves will not develop adversely and have a material adverse effect on AIG's results of operations. Estimation of ultimate net losses, loss expenses and loss reserves is a complex process for long-tail casualty lines of business, which include excess and umbrella liability, D&O, professional liability, medical malpractice, workers' compensation, general liability, products liability and related classes, as well as for asbestos and environmental exposures. Generally, actual historical loss development factors are used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past. Moreover, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for reserves with respect to a number of years to be significantly affected by changes in loss cost trends or loss development factors that were relied upon in setting the reserves. These changes in loss cost trends or loss development factors could be attributable to changes in inflation or in the judicial environment, or in other social or economic phenomena affecting claims, such as the effects that the recent disruption in the credit markets could have on reported claims under D&O or professional liability coverages. For a further discussion of AIG's loss reserves see also Management's Discussion and Analysis of Financial Condition and Results of Operations — Segment Results — General Insurance Operations — Liability for unpaid claims and claims adjustment expense.

Catastrophe Exposures

The occurrence of catastrophic events could adversely affect AIG's consolidated financial condition or results of operations. The occurrence of events such as hurricanes, earthquakes, pandemic disease, acts of terrorism and other catastrophes could adversely affect AIG's consolidated financial condition or results of operations, including by exposing AIG's businesses to the following:

- widespread claim costs associated with property, workers' compensation, mortality and morbidity claims;
- loss resulting from the value of invested assets declining to below the amount required to meet policy and contract liabilities; and
- loss resulting from actual policy experience emerging adversely in comparison to the assumptions made in the product pricing related to mortality, morbidity, termination and expenses.

Reinsurance

Reinsurance may not be available or affordable. AIG subsidiaries are major purchasers of reinsurance and utilize reinsurance as part of AIG's overall risk management strategy. Reinsurance is an important risk management tool to manage transaction and insurance line risk retention and to mitigate losses that may arise from catastrophes. Market conditions beyond AIG's control determine the availability and cost of the reinsurance purchased by AIG subsidiaries. For example, reinsurance may be more difficult to obtain after a year with a large number of major catastrophes. Accordingly, AIG may be forced to incur additional expenses for reinsurance or may be unable to obtain sufficient reinsurance on acceptable terms, in which case AIG would have to accept an increase in exposure risk, reduce the amount of business written by its subsidiaries or seek alternatives.

Reinsurance subjects AIG to the credit risk of its reinsurers and may not be adequate to protect AIG against losses. Although reinsurance makes the reinsurer liable to the AIG subsidiary to the extent the risk is ceded, it does not relieve the AIG subsidiary of the primary liability to its policyholders. Accordingly, AIG bears credit risk with respect to its subsidiaries' reinsurers to the extent not mitigated by collateral or other credit enhancements. A reinsurer's insolvency or inability or refusal to make timely payments under the terms of its agreements with the AIG subsidiaries could have a material adverse effect on AIG's results of operations and liquidity. For additional information on AIG's reinsurance, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management — Reinsurance.

Policyholder Behavior

AIG's policyholders, agents and other distributors of AIG's insurance products have expressed significant concerns in the wake of announcements by AIG of adverse financial results. AIG expects that these concerns will be exacerbated by the announcement of AIG's 2008 results. Many of AIG's businesses depend upon the financial stability (both actual and perceived) of AIG's parent company. Concerns that AIG or its subsidiaries may not be able to meet their obligations have negatively affected AIG's businesses in many ways, including:

- requests by customers to withdraw funds from AIG under annuity and certain life insurance contracts;
- a refusal by independent agents, brokers and banks to continue to offer AIG products and services;
- a refusal of counterparties, customers or vendors to continue to do business with AIG; and
- requests by customers and other parties to terminate existing contractual relationships.

Continued economic uncertainty, additional adverse results or a lack of confidence in AIG and AIG's businesses may cause AIG customers, agents and other distributors to cease or reduce their dealings with AIG, turn to competitors or shift to products that generate less income for AIG. Although AIG has announced its intent to refocus its business and certain AIG subsidiaries are rebranding themselves in an attempt to overcome a perception of instability, AIG cannot be sure that such efforts will be successful in attracting or maintaining clients.

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Foreign Operations

Foreign operations expose AIG to risks that may affect its operations, liquidity and financial condition. AIG provides insurance, investment and other financial products and services to both businesses and individuals in more than 130 countries and jurisdictions. A substantial portion of AIG's General Insurance business and a majority of its Life Insurance & Retirement Services business is conducted outside the United States. Operations outside the United States, particularly those in developing nations, may be affected by regional economic downturns, changes in foreign currency exchange rates, political upheaval, nationalization and other restrictive government actions, which could also affect other AIG operations.

The degree of regulation and supervision in foreign jurisdictions varies. Generally, AIG, as well as its subsidiaries operating in such jurisdictions, must satisfy local regulatory requirements. Licenses issued by foreign authorities to AIG subsidiaries are subject to modification and revocation. Thus, AIG's insurance subsidiaries could be prevented from conducting future business in certain of the jurisdictions where they currently operate. Adverse actions from any single country could adversely affect AIG's results of operations, liquidity and financial condition depending on the magnitude of the event and AIG's net financial exposure at that time in that country.

Employees

Because of the decline in the value of equity awards previously granted to employees and the uncertainty surrounding AIG's asset disposition program, AIG may be unable to retain key employees, including individuals critical to the execution of its disposition plan. AIG relies upon the knowledge and talent of its employees to successfully conduct business. The decline in AIG's common stock price has dramatically reduced the value of equity awards previously granted to its key employees. Also, the announcement of proposed asset dispositions has resulted in competitors seeking to hire AIG's key employees. AIG has implemented retention programs to seek to keep its key employees, but there can be no assurance that the programs will be effective. A loss of key employees could reduce the value of AIG's businesses and impair its ability to effect a successful asset disposition plan.

A loss of key employees in AIG's financial reporting process could prevent AIG from making required filings, preparing financial statements and otherwise adversely affect its internal controls. AIG relies upon the knowledge and experience of the employees involved in these functions for the effective and timely preparation of required filings and financial statements and operation of internal controls. If these employees depart, AIG may not be able to replace them with individuals having comparable knowledge and experience.

The limitations on incentive compensation contained in the American Recovery and Reinvestment Act of 2009 may adversely affect AIG's ability to retain its highest performing employees. On February 17, 2009, the American Recovery and Reinvestment Act of 2009 (Recovery Act) was signed into law. The Recovery Act contains restrictions on bonus and other incentive compensation payable to the five executives named in a company's proxy statement and the next twenty highest paid employees of companies receiving TARP funds. Historically, AIG has embraced a pay-for-performance philosophy. Depending upon the limitations placed on incentive compensation by the final regulations issued under the Recovery Act, it is possible that AIG may be unable to create a compensation structure that permits AIG to retain its highest performing employees. If this were to occur, AIG's asset disposition plan, businesses and results of operations would be adversely affected, perhaps materially.

Conflicts of interest may arise as AIG implements its asset disposition plan. AIG relies on certain key employees to operate its businesses during the asset disposition period, to provide information to prospective buyers and to maximize the value of businesses to be divested. The successful completion of the asset disposition plan could be adversely affected by any conflict of interests between AIG and its employees arising as a result of the asset disposition process.

Employee error and misconduct may be difficult to detect and prevent and may result in significant losses. Losses may result from, among other things, fraud, errors, failure to document transactions properly or to obtain proper internal authorization or failure to comply with regulatory requirements, both generally, and during the asset disposition process. There have been a number of highly publicized cases involving fraud or other misconduct by employees in the financial services industry in recent years, and AIG runs the risk that employee misconduct could occur. It is not always possible to deter or prevent employee misconduct and the controls that AIG has in place to prevent and detect this activity may not be effective in all cases.

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Regulation

AIG is subject to extensive regulation in the jurisdictions in which it conducts its businesses, and recent regulatory actions have made it challenging for AIG to continue to engage in business in the ordinary course. AIG's operations around the world are subject to regulation by different types of regulatory authorities, including insurance, securities, investment advisory, banking and thrift regulators in the United States and abroad. AIG's operations have become more diverse and consumer-oriented, increasing the scope of regulatory supervision and the possibility of intervention. In light of AIG's liquidity issues beginning in the third quarter of 2008, AIG and its regulated subsidiaries have been subject to intense review and supervision around the world. Regulators have taken significant steps to protect the businesses of the entities they regulate. These steps have included:

- Restricting or prohibiting the payment of dividends to AIG;
- Restricting or prohibiting other payments to AIG;
- Requesting additional capital contributions by AIG;
- Requesting that intercompany reinsurance reserves be covered by assets locally;
- Restricting the business in which the subsidiaries may engage; and
- Requiring pre-approval of all proposed transactions between the regulated subsidiaries and AIG or any affiliate.

AIG does not expect these conditions to change unless its financial situation stabilizes.

Adjustments to Life Insurance & Retirement Services Deferred Policy Acquisition Costs

Interest rate fluctuations, increased surrenders and other events may require AIG subsidiaries to accelerate the amortization of deferred policy acquisition costs (DAC) which could adversely affect AIG's consolidated financial condition or results of operations. DAC represents the costs that vary with and are related primarily to the acquisition of new and renewal insurance and annuity contracts. When interest rates rise or customers lose confidence in a company, policy loans and policy surrenders and withdrawals of life insurance policies and annuity contracts may increase as policyholders seek to buy products with perceived higher returns or more stability, requiring AIG subsidiaries to accelerate the amortization of DAC. To the extent such amortization exceeds surrender or other charges earned upon surrender and withdrawals of certain life insurance policies and annuity contracts, AIG's results of operations could be negatively affected.

DAC for both insurance-oriented and investment-oriented products, as well as retirement services products is reviewed for recoverability, which involves estimating the future profitability of current business. This review involves significant management judgment. If the actual emergence of future profitability were to be substantially lower than estimated, AIG could be required to accelerate its DAC amortization and such acceleration could adversely affect AIG's results of operations. For a further discussion of DAC, see also Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Estimates and Notes 1 and 8 to the Consolidated Financial Statements.

Risk Management

AIG is exposed to a number of significant risks, and AIG's risk management policies, processes and controls may not be effective in mitigating AIG's risk exposures in all market conditions and to all types of risk. The major risks to which AIG is exposed include credit risk, market risk, including credit spread risk, operational risk, liquidity risk and insurance risk. Given continued capital markets volatility, persistent risk aversion, inadequate liquidity in the markets of many asset classes, combined with AIG's weakened financial condition, AIG may not have adequate risk management policies, tools and processes and AIG may not have sufficient access to the markets and trading counterparties to effectively implement risk mitigating strategies and techniques. This environment could materially and adversely affect AIG's consolidated results of operations, liquidity or financial condition, result in regulatory action or litigation or further damage AIG's reputation. For a further discussion of AIG's risk management process and controls, see Management's Discussion and Analysis of Financial Condition and Results of Operations — Risk Management.

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Operational risks of asset dispositions. AIG is exposed to various operational risks associated with the dispositions of subsidiaries and the resulting restructuring of AIG at the business and corporate levels. These risks include the ability to deconsolidate systems and processes of divested operations without adversely affecting AIG, the ability of AIG to fulfill its obligations under any transition separation agreements agreed upon with buyers, the ability of AIG to downsize the corporation as dispositions are accomplished and the ability of AIG to continue to provide services previously performed by divested entities.

AIGFP wind-down risks. An orderly and successful wind-down of AIGFP's businesses and portfolios is subject to numerous risks, including market conditions, counterparty willingness to transact, or terminate transactions, with AIGFP and the retention of key personnel. An orderly and successful wind-down will also depend on the stability of AIG's credit ratings. Further downgrades of AIG's credit ratings likely would have an adverse effect on the wind-down of AIGFP's businesses and portfolios.

Use of Estimates

If actual experience differs from management's estimates used in the preparation of financial statements, AIG's consolidated results of operations or financial condition could be adversely affected. The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, are those described in Management's Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Estimates. These accounting estimates require the use of assumptions, some of which are highly uncertain at the time of estimation. For example, recent market volatility and declines in liquidity have made it more difficult to value certain of AIG's invested assets and the obligations and collateral relating to certain financial instruments issued or held by AIG, such as AIGFP's super senior credit default swap portfolio. Additionally, the recoverability of deferred tax assets depends in large part on assumptions about future profitability. These estimates, by their nature, are based on judgment and current facts and circumstances. Therefore, actual results could differ from these estimates, possibly in the near term, and could have a material effect on the consolidated financial statements.

Legal Proceedings

Significant legal proceedings may adversely affect AIG's results of operations. AIG is party to numerous legal proceedings, including securities class actions and regulatory or governmental investigations. Due to the nature of the litigation, the lack of precise damage claims and the type of claims made against AIG, AIG cannot currently quantify its ultimate liability for these actions. It is possible that developments in these unresolved matters could have a material adverse effect on AIG's consolidated financial condition or consolidated results of operations for an individual reporting period. For a discussion of these unresolved matters, see Note 14 to the Consolidated Financial Statements.

Aircraft Suppliers

There are limited suppliers of aircraft and engines. The supply of jet transport aircraft, which ILFC purchases and leases, is dominated by two airframe manufacturers, Boeing and Airbus, and a limited number of engine manufacturers. As a result, ILFC is dependent on the manufacturers' success in remaining financially stable, producing aircraft and related components which meet the airlines' demands, both in type and quantity, and fulfilling their contractual obligations to ILFC. Competition between the manufacturers for market share is intense and may lead to instances of deep discounting for certain aircraft types that could negatively affect ILFC's competitive pricing.

Item 1B. ***Unresolved Staff Comments***

There are no material unresolved written comments that were received from the SEC staff 180 days or more before the end of AIG's fiscal year relating to AIG's periodic or current reports under the Exchange Act.

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Item 2. ***Properties***

AIG and its subsidiaries operate from approximately 2,000 offices in the United States, 41 in Puerto Rico, 8 in Canada and numerous offices in over 100 foreign countries. The offices in Greensboro and Winston-Salem, North Carolina; Springfield, Illinois; Amarillo, Ft. Worth, Houston and Lewisville, Texas; Wilmington, Delaware; San Juan, Puerto Rico; Tampa, Florida; Livingston, New Jersey; Evansville, Indiana; Nashville, Tennessee; 70 Pine Street, 72 Wall Street and 175 Water Street in New York, New York; and offices in more than 30 foreign countries and jurisdictions including Bermuda, Chile, Hong Kong, the Philippines, Japan, the U.K., Singapore, Malaysia, Switzerland, Taiwan and Thailand are located in buildings owned by AIG and its subsidiaries. The remainder of the office space utilized by AIG subsidiaries is leased.

Item 3. ***Legal Proceedings***

For a discussion of legal proceedings, see Note 14(a) to the Consolidated Financial Statements, which is incorporated herein by reference.

Item 4. ***Submission of Matters to a Vote of Security Holders***

There were no matters submitted to a vote of security holders during the fourth quarter of 2008.

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American International Group, Inc., and Subsidiaries

Part II

Item 5. ***Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities***

AIG's common stock is listed on the New York Stock Exchange, as well as on the stock exchanges in Ireland and Tokyo.

The following table presents the high and low closing sales prices on the New York Stock Exchange Composite Tape and the dividends paid per share of AIG's common stock for each quarter of 2008 and 2007:

	2008			2007		
	High	**Low**	**Dividends Paid**	High	Low	Dividends Paid
First quarter	**$59.32**	**$39.80**	**$ 0.200**	$72.15	$66.77	$ 0.165
Second quarter	**49.04**	**26.46**	**0.200**	72.65	66.49	0.165
Third quarter	**30.10**	**2.05**	**0.220**	70.44	61.64	0.200
Fourth quarter	**4.00**	**1.35**	**—**	70.11	51.33	0.200

The approximate number of record holders of common stock as of January 30, 2009 was 58,182.

Under the Fed Credit Agreement, AIG is restricted from paying dividends on its common stock.

For a discussion of certain restrictions on the payment of dividends to AIG by some of its insurance subsidiaries, see Item 1A. Risk Factors — Liquidity — AIG parent's ability to access funds from its subsidiaries is severely limited, and Note 15 to the Consolidated Financial Statements.

AIG's table of equity compensation plans previously approved by security holders and equity compensation plans not previously approved by security holders will be included in the definitive proxy statement for AIG's 2009 Annual Meeting of Shareholders, which will be filed with the SEC no later than 120 days after the close of AIG's fiscal year pursuant to Regulation 14A.

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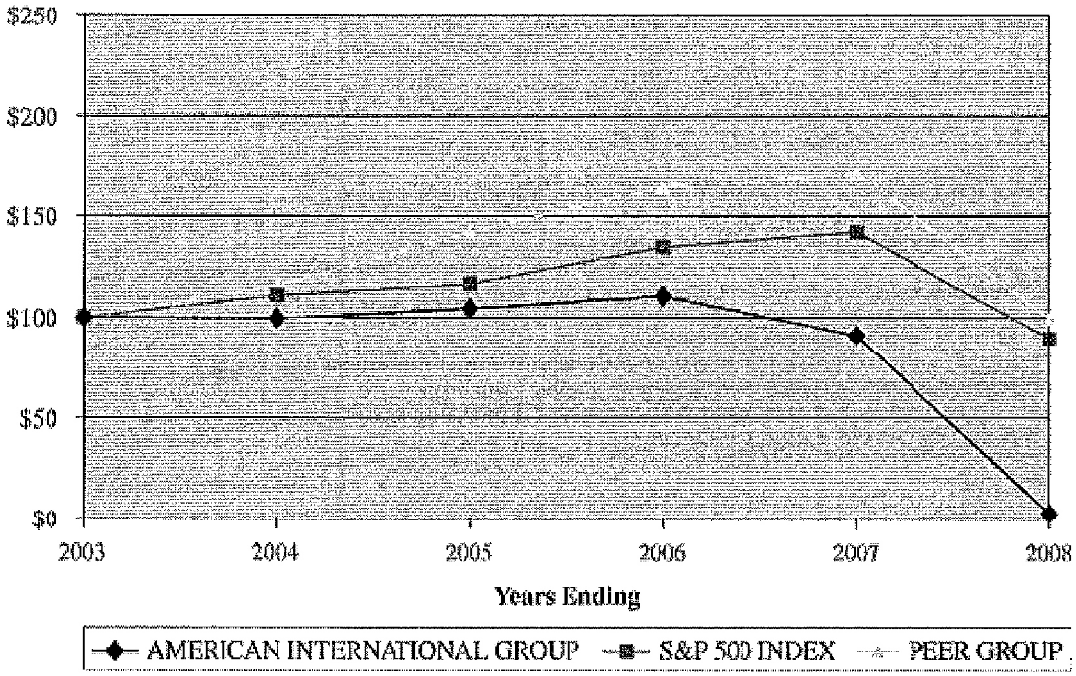
Performance Graph

The following Performance Graph compares the cumulative total shareholder return on AIG common stock for a five-year period (December 31, 2003 to December 31, 2008) with the cumulative total return of the S&P's 500 stock index (which includes AIG) and a peer group of companies consisting of nine insurance companies to which AIG compares its business and operations: ACE Limited, Aflac Incorporated, The Chubb Corporation, The Hartford Financial Services Group, Inc., Lincoln National Corporation, MetLife, Inc., Prudential Financial, Inc., The Travelers Companies, Inc. (formerly The St. Paul Travelers Companies, Inc.) and XL Capital Ltd.

FIVE-YEAR CUMULATIVE TOTAL SHAREHOLDER RETURNS
Value of $100 Invested on December 31, 2003



	As of December 31,					
	2003	2004	2005	2006	2007	2008
AIG	$100.00	$ 99.48	$104.31	$110.62	$ 91.00	**$ 2.64**
S&P 500	100.00	110.88	116.33	134.70	142.10	**89.53**
Peer Group	100.00	115.57	142.12	164.44	171.76	**99.39**

Item 6. *Selected Financial Data*

American International Group, Inc. and Subsidiaries
Selected Consolidated Financial Data

The Selected Consolidated Financial Data should be read in conjunction with Management's Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and accompanying notes included elsewhere herein.

	Years Ended December 31,				
	2008	2007	2006(a)	2005(a)	2004(a)
	(In millions, except per share data)				
Revenues *(b)(c)* :					
Premiums and other considerations	$ 83,505	$ 79,302	$ 74,213	$ 70,310	$ 66,704
Net investment income	12,222	28,619	26,070	22,584	19,007
Net realized capital gains (losses)	(55,484)	(3,592)	106	341	44
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	(28,602)	(11,472)	—	—	—
Other income	(537)	17,207	12,998	15,546	12,068
Total revenues	11,104	110,064	113,387	108,781	97,823
Benefits, claims and expenses:					
Policyholder benefits and claims incurred	63,299	66,115	60,287	64,100	58,600
Policy acquisition and other insurance expenses *(f)*	27,565	20,396	19,413	17,773	16,049
Interest expense *(g)*	17,007	4,751	3,657	2,572	2,013
Restructuring expenses and related asset impairment and other expenses	758	—	—	—	—
Other expenses	11,236	9,859	8,343	9,123	6,316
Total benefits, claims and expenses	119,865	101,121	91,700	93,568	82,978
Income (loss) before income tax expense (benefit), minority interest and cumulative effect of change in accounting principles *(b)(c)(d)(e)*	(108,761)	8,943	21,687	15,213	14,845
Income tax expense (benefit) *(h)*	(8,374)	1,455	6,537	4,258	4,407
Income (loss) before minority interest and cumulative effect of change in accounting principles	(100,387)	7,488	15,150	10,955	10,438
Minority interest	1,098	(1,288)	(1,136)	(478)	(455)
Income (loss) before cumulative effect of change in accounting principles	(99,289)	6,200	14,014	10,477	9,983
Cumulative effect of change in accounting principles, net of tax	—	—	34	—	(144)
Net income (loss)	(99,289)	6,200	14,048	10,477	9,839
Earnings (loss) per common share:					
Basic					
Income (loss) before cumulative effect of change in accounting principles	(37.84)	2.40	5.38	4.03	3.83
Cumulative effect of change in accounting principles, net of tax	—	—	0.01	—	(0.06)
Net income (loss)	(37.84)	2.40	5.39	4.03	3.77
Diluted					
Income (loss) before cumulative effect of change in accounting principles	(37.84)	2.39	5.35	3.99	3.79
Cumulative effect of change in accounting principles, net of tax	—	—	0.01	—	(0.06)
Net income (loss)	(37.84)	2.39	5.36	3.99	3.73
Dividends declared per common share	0.42	0.77	0.65	0.63	0.29
Year-end balance sheet data:					
Total assets	860,418	1,048,361	979,410	853,048	801,007
Long-term debt *(i)*	177,485	162,935	135,316	100,314	86,653
Commercial paper and extendible commercial notes *(j)*	15,718	13,114	13,363	9,535	10,246
Total liabilities	807,708	952,560	877,542	766,545	721,135
Shareholders' equity	$ 52,710	$ 95,801	$101,677	$ 86,317	$ 79,673

EXHIBIT
Exhibit 505
PENGAD 800-631-6989

(a) *Certain reclassifications have been made to prior period amounts to conform to the current period presentation.*

(b) *In 2008, 2007, 2006, 2005 and 2004, includes other-than-temporary impairment charges of $50.8 billion, $4.7 billion, $944 million, $598 million and $684 million, respectively. Also includes gains (losses) from hedging activities that did not qualify for hedge accounting treatment under FAS 133, including the related foreign exchange gains and losses. In 2008, 2007, 2006, 2005 and 2004, respectively, the effect was $(4.0) billion, $(1.44) billion, $(1.87) billion, $2.02 billion, and $385 million in revenues and $(4.0) billion, $(1.44) billion, $(1.87) billion, $2.02 billion and $671 million in operating income. These amounts result primarily from interest rate and foreign currency derivatives that are effective economic hedges of investments and borrowings.*

(c) *Includes an other-than-temporary impairment charge of $643 million on AIGFP's available for sale investment securities reported in other income in 2007.*

(d) *Includes current year catastrophe-related losses of $1.8 billion in 2008, $276 million in 2007, $3.28 billion in 2005 and $1.16 billion in 2004. There were no significant catastrophe-related losses in 2006.*

(e) *Reduced by fourth quarter charges of $1.8 billion and $850 million in 2005 and 2004, respectively, related to the annual review of General Insurance loss and loss adjustment reserves. In 2006, 2005 and 2004, changes in estimates for asbestos and environmental reserves were $198 million, $873 million and $850 million, respectively.*

(f) *In 2008, includes goodwill impairment charges of $3.2 billion.*

(g) *In 2008, includes $11.4 billion of interest expense on the Fed Facility, which was comprised of $9.3 billion of amortization on the prepaid commitment fee asset associated with the Fed Facility and $2.1 billion of accrued compounding interest.*

(h) *In 2008, includes a $20.6 billion valuation allowance to reduce AIG's deferred tax asset to an amount AIG believes is more likely than not to be realized, and a $5.5 billion deferred tax expense attributable to the potential sale of foreign businesses.*

(i) *Includes that portion of long-term debt maturing in less than one year. See Note 13 to the Consolidated Financial Statements.*

(j) *Includes borrowings of $6.8 billion, $6.6 billion and $1.7 billion for AIGFP, AIG Funding and ILFC, respectively, under the CPFF at December 31, 2008.*

See Note 1(ff) to the Consolidated Financial Statements for effects of adopting new accounting standards.

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American International Group, Inc., and Subsidiaries

Item 7. ***Management's Discussion and Analysis of Financial Condition and Results of Operations***

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations, AIG presents its operations in the way it believes will be most meaningful. Statutory underwriting profit (loss) is presented in accordance with accounting principles prescribed by insurance regulatory authorities because these are standard measures of performance used in the insurance industry and thus allow more meaningful comparisons with AIG's insurance competitors. AIG has also incorporated into this discussion a number of cross-references to additional information included throughout this Annual Report on Form 10-K to assist readers seeking additional information related to a particular subject.

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Cautionary Statement Regarding Forward-Looking Information

This Annual Report on Form 10-K and other publicly available documents may include, and AIG's officers and representatives may from time to time make, projections and statements which may constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These projections and statements are not historical facts but instead represent only AIG's belief regarding future events, many of which, by their nature, are inherently uncertain and outside AIG's control. These projections and statements may address, among other things, the outcome of proposed transactions with the NY Fed and the United States Department of the Treasury, the number, size, terms, cost and timing of dispositions and their potential effect on AIG's businesses, financial condition, results of operations, cash flows and liquidity (and AIG at any time and from time to time may change its plans with respect to the sale of one or more businesses), AIG's exposures to subprime mortgages, monoline insurers and the residential and commercial real estate markets and AIG's strategy for growth, product development, market position, financial results and reserves. It is possible that AIG's actual results and financial condition will differ, possibly materially, from the anticipated results and financial condition indicated in these projections and statements. Factors that could cause AIG's actual results to differ, possibly materially, from those in the specific projections and statements include a failure to complete the proposed transactions with the NY Fed and the United States Department of the Treasury, developments in global credit markets and such other factors as discussed throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations and in Item 1A. Risk Factors of this Annual Report on Form 10-K. AIG is not under any obligation (and expressly disclaims any obligation) to update or alter any projection or other statement, whether written or oral, that may be made from time to time, whether as a result of new information, future events or otherwise.

Overview

Operations

AIG identifies its operating segments by product line, consistent with its management structure. These segments are General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management. Through these operating segments, AIG provides insurance, financial and investment products and services to both businesses and individuals in more than 130 countries and jurisdictions.

AIG's subsidiaries serve commercial, institutional and individual customers through an extensive property-casualty and life insurance and retirement services network. AIG's Financial Services businesses include commercial aircraft and equipment leasing, capital markets operations and consumer finance, both in the United States and abroad. AIG also provides asset management services to institutions and individuals.

General Business Environment

The 2008 business environment was one of the most difficult in recent decades. In the U.S., real GDP shrank at annual rates of more than 4 percent in the second half of the year and almost 4 percent in the fourth quarter alone. At the beginning of 2008, the unemployment rate was 4.9 percent and by year-end was 7.2 percent.

The strong declines in the overall U.S. economy during the second half of 2008 occurred despite repeated reductions of interest rates by the Federal Reserve, the creation of numerous credit facilities for the banking system and the passage of a stimulus package.

Consideration of AIG's Ability to Continue as a Going Concern

In connection with the preparation of this Annual Report on Form 10-K, management has assessed whether AIG has the ability to continue as a going concern (See Note 1 to the Consolidated Financial Statements). In making this assessment, AIG has considered:

- The commitment of the NY Fed and the United States Department of the Treasury to the orderly restructuring of AIG and their commitment to continuing to work with AIG to maintain its ability to meet its obligations as they come due;
- The liquidity events in the second half of 2008, including transactions with the NY Fed and the United States Department of the Treasury;

- AIG's liquidity-related actions and plans to stabilize its businesses and repay the Fed Facility;
- The level of AIG's realized and unrealized losses and the negative impact of these losses in shareholders' equity and on the capital levels of AIG's insurance subsidiaries;
- The substantial resolution of the liquidity issues surrounding AIGFP's multi-sector super senior credit default swap portfolio and the U.S. securities lending program;
- The additional capital provided to AIG by the United States Department of the Treasury;
- Anticipated transactions with the NY Fed and the United States Department of the Treasury;
- The continuing liquidity issues in AIG's businesses and AIG's actions to address such issues; and
- The substantial risks to which AIG is subject.

Each of these items is discussed in more detail below.

In considering these items, management has made significant judgments and estimates with respect to the potentially adverse financial and liquidity effects of AIG's risks and uncertainties. Management has also assessed other items and risks arising in AIG's businesses and made reasonable judgments and estimates with respect thereto. After consideration, management believes that it will have adequate liquidity to finance and operate AIG's businesses and continue as a going concern for at least the next twelve months.

It is possible that the actual outcome of one or more of management's plans could be materially different or that one or more of management's significant judgments or estimates about the potential effects of the risks and uncertainties could prove to be materially incorrect or that the principal transactions disclosed in Note 23 to the Consolidated Financial Statements (and as discussed below) are not consummated. If one or more of these possible outcomes is realized, AIG may need additional U.S. government support to meet its obligations as they come due.

Liquidity

Liquidity Events in the Second Half of 2008

In the second half of 2008, AIG experienced an unprecedented strain on liquidity. This strain led to a series of transactions with the NY Fed and the United States Department of the Treasury. The two principal causes of the liquidity strain were demands for the return of cash collateral under the U.S. securities lending program and collateral calls on AIGFP's super senior multi-sector CDO credit default swap portfolio.

Under AIG's securities lending program, cash collateral was received from borrowers in exchange for loans of securities owned by AIG's insurance company subsidiaries. The cash was invested by AIG in fixed income securities, primarily residential mortgage-backed securities (RMBS), to earn a spread. During September 2008, borrowers began in increasing numbers to request a return of their cash collateral. Because of the illiquidity in the market for RMBS, AIG was unable to sell RMBS at acceptable prices and was forced to find alternative sources of cash to meet these requests. As of the end of August, AIG's U.S. securities lending program had approximately $69 billion of borrowings outstanding. See Investments — Securities Lending Activities for additional information about the securities lending program.

Additionally, throughout the second half of 2008, declines in the fair values of the super senior multi-sector CDO securities protected by AIGFP's credit default swap portfolio, together with ratings downgrades of the CDO securities, resulted in AIGFP being required to post significant additional collateral. As of the end of August 2008, AIG had posted approximately $19.7 billion of collateral under its super senior credit default swap portfolio. See Critical Accounting Estimates — Fair Value Measurements of Certain Financial Assets and Liabilities for additional information about AIGFP's super senior multi-sector CDO credit default swap portfolio.

Both of these liquidity strains were significantly exacerbated by the downgrades of AIG's long-term debt ratings by S&P, Moody's and Fitch on September 15, 2008.

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Arrangements with the Federal Reserve Bank of New York and the United States Department of the Treasury

Fed Credit Agreement

Because of these immediate liquidity requirements, AIG's Board of Directors determined that the only viable alternative was to accept an arrangement offered by the NY Fed, and on September 16, 2008, approved borrowing from the NY Fed based on a term sheet that set forth the terms of the secured credit agreement and related equity participation. Over the next six days, AIG elected Edward M. Liddy Director, Chairman and CEO, replacing Robert Willumstad in those positions, negotiated a definitive credit agreement with the NY Fed and borrowed, on a secured basis, approximately $37 billion from the NY Fed, enabling AIG to meet its liquidity requirements before formally entering into a credit agreement with the NY Fed.

On September 22, 2008, AIG entered into the Fed Credit Agreement in the form of a two-year secured loan and the Pledge Agreement with the NY Fed. On November 9, 2008, AIG and the NY Fed agreed to amend the Fed Credit Agreement to reduce the total commitment under the Fed Facility to $60 billion following the issuance of the Series D Preferred Stock (described below), extend the term of the Fed Facility to 5 years and reduce the related interest and fees payable under the Fed Facility. See Note 13 to the Consolidated Financial Statements for information regarding the terms of and borrowings under the Fed Credit Agreement.

Series D Preferred Stock Issuance

On November 25, 2008, AIG entered into a Securities Purchase Agreement (the Series D Preferred Stock Purchase Agreement) with the United States Department of the Treasury pursuant to which, among other things, AIG issued and sold to the United States Department of the Treasury, as part of the Troubled Asset Relief Program (TARP) and the Systemically Significant Failing Institutions Program, $40 billion of Series D Preferred Stock, and a warrant to purchase 53,798,766 shares of common stock (the Warrant). The proceeds from the sale of the Series D Preferred Stock and the Warrant were used to repay borrowings under the Fed Facility. See Note 15 to the Consolidated Financial Statements for further information on the Series D Preferred Stock and the Warrant.

Termination of $62 billion of CDS

On November 25, 2008, AIG entered into a Master Investment and Credit Agreement (the ML III Agreement) with the NY Fed, Maiden Lane III LLC (ML III), and The Bank of New York Mellon, which established arrangements, through ML III, to fund the purchase of the multi-sector CDOs underlying or related to certain credit default swaps and other similar derivative instruments (CDS) written by AIG Financial Products Corp. in connection with the termination of such CDS transactions. Concurrently, AIG Financial Products Corp.'s counterparties to such CDS transactions agreed to terminate those CDS transactions relating to the multi-sector CDOs purchased from them by ML III. Through December 31, 2008, ML III had purchased from counterparties a total of $62.1 billion in par amount of CDO securities, and the associated credit default swaps had been terminated. Approximately $12.2 billion notional amount of AIG Financial Products Corp.'s CDS transactions referencing super senior multi-sector CDOs remained outstanding as of February 18, 2009. See Note 5 to the Consolidated Financial Statements for further information on the transactions with ML III.

Resolution of U.S. Securities Lending Program

On December 12, 2008, AIG, certain of AIG's wholly owned U.S. life insurance subsidiaries, and AIG Securities Lending Corp. (the AIG Agent), another AIG subsidiary, entered into an Asset Purchase Agreement (the ML II Agreement) with Maiden Lane II LLC (ML II), a Delaware limited liability company whose sole member is the NY Fed.

Pursuant to the ML II Agreement, the life insurance subsidiaries sold to ML II all of their undivided interests in a pool of $39.3 billion face amount of RMBS held by the AIG Agent as agent of the life insurance subsidiaries in connection with AIG's U.S. securities lending program. In exchange for the RMBS, the life insurance subsidiaries received an initial purchase price of approximately $19.8 billion plus the right to receive deferred contingent portions of the total purchase price of $1 billion plus participation in the residual, each of which is subordinated to the repayment of the NY Fed loan to ML II. These life insurance subsidiaries applied the net cash proceeds of sale of

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the RMBS toward the amounts due by such life insurance subsidiaries in terminating both the U.S. securities lending program and the interim agreement entered into with the NY Fed whereby the NY Fed borrowed securities from AIG subsidiaries in exchange for cash collateral. See Investments — Securities Lending Activities and Note 5 to the Consolidated Financial Statements for further information on the transaction with ML II.

AIG Affiliates Participate in the NY Fed's Commercial Paper Funding Facility

On October 27, 2008, four affiliates of AIG (including ILFC) applied for participation in the CPFF. Currently, AIG Funding, Inc., an AIG subsidiary, and two of AIGFP's sponsored vehicles, Curzon Funding LLC and Nightingale Finance LLC may issue up to approximately $6.9 billion, $7.2 billion and $1.1 billion, respectively, of commercial paper under the CPFF. AIG Funding uses the proceeds to refinance AIG's outstanding commercial paper as it matures, meet other working capital needs and make prepayments under the Fed Facility while the two other programs use the proceeds to refinance maturing commercial paper. On January 21, 2009, S&P downgraded ILFC's short-term credit rating and, as a result, ILFC can no longer participate in the CPFF.

Series C Preferred Stock Issuance

On March 1, 2009, AIG entered into the Series C Preferred Stock Purchase Agreement with the Trust, pursuant to which AIG agreed to issue and sell 100,000 shares of Series C Preferred Stock to the Trust. AIG expects to issue the Series C Preferred Stock to the Trust in early March, 2009. The aggregate purchase price for the Series C Preferred Stock was $500,000, with an understanding that additional and independently sufficient consideration was also furnished in September 2008 by the NY Fed in the form of its $85 billion lending commitment under the Fed Credit Agreement.

The Series C Preferred Stock Purchase Agreement, among other things:

- provides the Trust with rights to require registration of the Series C Preferred Stock under the Securities Act of 1933 and for AIG to facilitate other dispositions;
- prohibits AIG from issuing capital stock without the approval of the Trust so long as the Trust owns 50 percent of the Series C Preferred Stock, subject to certain exceptions relating to existing obligations and employee benefit plans;
- requires AIG and its Board of Directors to work in good faith with the Trust to ensure satisfactory corporate governance arrangements;
- requires the following proposals to be presented to AIG's shareholders at AIG's 2009 Annual Meeting of Shareholders:
  - to amend AIG's Restated Certificate of Incorporation to permit AIG's Board of Directors to issue classes of preferred stock that are not of equal rank and cause the Series D Preferred Stock and any other series of preferred stock subsequently issued to the United States Department of the Treasury to rank senior to the Series C Preferred Stock and any other subsequently issued series of preferred stock that is not issued to the United States Department of the Treasury; and
  - to eliminate any restriction on the pledging of all or substantially all of AIG's properties or assets; and
- requires the following proposals to be presented to AIG's shareholders at a special shareholders' meeting or at a future annual shareholders' meeting following notice from the Trust:
  - to amend AIG's Restated Certificate of Incorporation to decrease the par value of AIG's common stock, increase the authorized number of shares of common stock and, if these amendments are not approved;
  - to amend the terms of AIG's Restated Certificate of Incorporation to decrease the par value of AIG's serial preferred stock and increase the number of authorized shares of AIG's serial preferred stock, and amend the terms of the Series C Preferred Stock to increase the number of shares of Series C Preferred Stock so that each share of Series C Preferred Stock would be convertible into common stock on approximately a one-to-one basis.

EXHIBIT
PENGAD 800-631-6989
Exhibit 505

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The Series C Preferred Stock is not redeemable by AIG and, upon the effectiveness of the required amendments to AIG's Restated Certificate of Incorporation, will be convertible into common stock. From issuance, the Series C Preferred Stock will, to the extent permitted by law, vote with the common stock as a single class and represent approximately 77.9 percent of the voting power of the common stock, treating the Series C Preferred Stock as converted. The Series C Preferred Stock will also participate in any dividends paid on the common stock, with approximately 77.9 percent of all dividends paid allocated to the Series C Preferred Stock, treating the Series C Preferred Stock as converted. Upon the liquidation, dissolution or winding up of AIG, the Series C Preferred Stock is entitled to a liquidation preference per share equal to the greater of (i) $5.00 and (ii) the amount that would be payable with respect to the shares of common stock issuable upon conversion of such share of Series C Preferred Stock. For additional information about the Series C Preferred Stock, see Note 15 to the Consolidated Financial Statements.

March 2009 Agreements in Principle

On March 2, 2009, AIG, the NY Fed and the United States Department of the Treasury announced agreements in principle to modify the terms of the Fed Credit Agreement and the Series D Preferred Stock and to provide a $30 billion equity capital commitment facility. The United States Government has issued the following statement referring to the agreements in principle and other transactions they expect to undertake with AIG intended to strengthen AIG's capital position, enhance its liquidity, reduce its borrowing costs and facilitate AIG's asset disposition program.

> "The steps announced today provide tangible evidence of the U.S. government's commitment to the orderly restructuring of AIG over time in the face of continuing market dislocations and economic deterioration. Orderly restructuring is essential to AIG's repayment of the support it has received from U.S. taxpayers and to preserving financial stability. The U.S. government is committed to continuing to work with AIG to maintain its ability to meet its obligations as they come due."

See Note 23 to the Consolidated Financial Statements.

Modification to Series D Preferred Stock

On March 2, 2009, AIG and the United States Department of the Treasury announced their agreement in principle to enter into a transaction pursuant to which the United States Department of the Treasury would modify the terms of the Series D Preferred Stock. The modification will be effected by an exchange of 100 percent of the outstanding shares of Series D Preferred Stock for newly issued perpetual serial preferred stock (Series E Preferred Stock), with a liquidation preference equal to the issuance-date liquidation preference of the Series D Preferred Stock surrendered plus accumulated but unpaid dividends thereon. The terms of the Series E Preferred Stock will be the same as for the Series D Preferred Stock except that the dividends will not be cumulative. The Series D Preferred Stock bore cumulative dividends.

The dividend rate on both the cumulative Series D Preferred Stock and the non-cumulative Series E Preferred Stock is 10 percent per annum. Concurrent with the exchange of the shares of Series D Preferred Stock for the Series E Preferred Stock, AIG will enter into a replacement capital covenant in favor of the holders of a series of AIG debt, pursuant to which AIG will agree that prior to the third anniversary of the issuance of the Series E Preferred Stock AIG will not repay, redeem or purchase, and no subsidiary of AIG will purchase, all or any part of the Series E Preferred Stock except with the proceeds obtained from the issuance by AIG or any subsidiary of AIG of certain capital securities. AIG will make a statement of intent substantially similar to the replacement capital covenant with respect to subsequent years. The Series D Preferred Stock was not subject to a replacement capital covenant.

Equity Capital Commitment Facility

On March 2, 2009, AIG and the United States Department of the Treasury announced its agreement in principle to provide AIG with a 5-year equity capital commitment facility of $30 billion. AIG may use the facility to sell to the United States Department of the Treasury fixed-rate, non-cumulative perpetual serial preferred stock

(Series F Preferred Stock). The facility will be available to AIG so long as AIG is not the debtor in a pending case under Title 11, United States Code, and the Trust (or any successor entity established for the benefit of the United States Treasury) "beneficially owns" more than 50 percent of the aggregate voting power of AIG's voting securities at the time of such drawdown.

The terms of the Series F Preferred Stock will be substantially similar to the Series E Preferred Stock, except that the Series F Preferred Stock will not be subject to a replacement capital covenant or the statement of intent.

In connection with the equity capital commitment facility, the United States Department of the Treasury will also receive warrants exercisable for a number of shares of common stock of AIG equal to 1 percent of AIG's then outstanding common stock and, upon issuance of the warrants, the dividends payable on, and the voting power of, the Series C Preferred Stock will be reduced by the number of shares subject to the warrant.

Repayment of Fed Facility with Subsidiary Preferred Equity

On March 2, 2009, AIG and the NY Fed announced their intent to enter into a transaction pursuant to which AIG will transfer to the NY Fed preferred equity interests in newly-formed special purpose vehicles (SPVs). Each SPV will have (directly or indirectly) as its only asset 100 percent of the common stock of an AIG operating subsidiary (AIA in one case and ALICO in the other). AIG expects to own the common interests of each SPV and will initially have the right to appoint the entire board of directors of each SPV. In exchange for the preferred equity interests received by the NY Fed, there would be a concurrent substantial reduction in the outstanding balance and maximum available amount to be borrowed on the Fed Facility.

Securitizations

On March 2, 2009, AIG and the NY Fed announced their intent to enter into a transaction pursuant to which AIG will issue to the NY Fed senior certificates in one or more newly-formed SPVs backed by inforce blocks of life insurance policies in settlement of a portion of the outstanding balance of the Fed Facility. The amount of the Fed Facility reduction will be based on the proceeds received. The SPVs are expected to be consolidated by AIG.

Modification to Fed Facility

On March 2, 2009, AIG and the NY Fed announced their agreement in principle to amend the Fed Credit Agreement to remove the interest rate floor. Under the current terms, interest accrues on the outstanding borrowings under the Fed Facility at three-month LIBOR (no less than 3.5 percent) plus 3.0 percent per annum. The 3.5 percent LIBOR floor will be eliminated following the amendment. In addition, the Fed Facility will be amended to ensure that the total commitment will be at least $25 billion, even after giving effect to the repayment of the Fed Facility with subsidiary preferred equity and securitization transactions described above. These proceeds are expected to substantially reduce the outstanding borrowings under the Fed Facility from the amount outstanding as of December 31, 2008.

Liquidity Position

At December 31, 2008, AIG had outstanding borrowings under the Fed Facility of $36.8 billion, with a remaining borrowing capacity of $23.2 billion, and accrued compounding interest and fees totaled $3.6 billion.

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Borrowings outstanding and remaining available amount that can be borrowed under the Fed Facility were as follows:

	Inception through December 31, 2008	Inception through February 18, 2009(c)
	(In millions)	
Borrowings:		
Loans to AIGFP for collateral postings, GIA and other debt maturities	$ 46,997	$ 47,547
Capital contributions to insurance companies *(a)*	20,850	20,850
Repayment of obligations to securities lending program	3,160	3,160
Repayment of intercompany loans	1,528	1,528
Contributions to AIGCFG subsidiaries	1,672	1,686
Debt repayments	2,109	2,319
Funding of equity interest in ML III	5,000	5,000
Repayment from the proceeds of the issuance of Series D Preferred Stock and common stock warrant	(40,000)	(40,000)
Other *(a)(b)*	(4,516)	(6,890)
Net borrowings	36,800	35,200
Total Fed Facility	60,000	60,000
Remaining available amount	$ 23,200	$ 24,800
Net borrowings	$ 36,800	$ 35,200
Accrued compounding interest and fees	3,631	3,631
Total balance outstanding	$ 40,431	$ 38,831

(a) Includes securities lending activities.

(b) Includes repayments from funds received from the Fed Securities Lending Agreement and the CPFF.

(c) At February 25, 2009, $36 billion was outstanding under the Fed Facility.

AIG's Strategy for Stabilization and Repayment of AIG's Obligations as They Come Due

Future Cash Requirements

The following table shows the maturing debt of AIG and its subsidiaries for each quarter of 2009:

	First Quarter 2009	Second Quarter 2009	Third Quarter 2009	Fourth Quarter 2009	Total
			(In millions)		
AIG	$ 418	$ —	$ —	$1,000	$ 1,418
AIG MIP	—	1,156	—	—	1,156
AIGFP	1,421	765	2,132	1,125	5,443
ILFC	917	1,097	1,151	2,986	6,151
AGF	835	931	3,209	1,661	6,636
Other subsidiaries	312	227	114	124	777
Total	$3,903	$4,176	$6,606	$6,896	$21,581

In addition, at February 18, 2009, AIG affiliates had issued $14 billion in commercial paper to the CPFF with the majority of maturities in April of 2009. If AIG's short-term ratings are downgraded, AIG Funding may lose access to the CPFF and would be required to find other sources to fund the maturing commercial paper.

AIG expects to meet these obligations primarily through borrowings from the Fed Facility and the cash flows, including from dispositions, of assets supporting these obligations. Approximately $3.1 billion of AIGFP's debt maturities through December 31, 2009 are fully collateralized with assets backing the corresponding liabilities. It is expected that AGF and ILFC will require support from AIG, in addition to their cash flows from operations and proceeds from asset sales and securitizations, to meet their 2009 obligations. See Note 13 to the Consolidated Financial Statements for additional information regarding the terms of the Fed Credit Agreement and the related Pledge Agreement.

In 2009, AIG made capital contributions of $1.25 billion to certain of its Domestic Life Insurance & Retirement Services companies. If a substantial portion of the Domestic Life Insurance & Retirement Services bond portfolio diminishes significantly in value or suffers credit events, AIG may need to provide additional capital support for these operations.

AIG has developed certain plans (described below), some of which have already been implemented, to provide stability to its businesses and to provide for the timely repayment of the Fed Facility; other plans are still being formulated.

Asset Disposition Plan

On October 3, 2008, AIG announced a restructuring plan under which AIG's Life Insurance & Retirement Services operations and certain other businesses would be divested in whole or in part. Since that time, AIG has sold certain businesses and assets and has entered into contracts to sell others. However, global market conditions have continued to deteriorate, posing risks to AIG's ability to divest assets at acceptable values. As announced on March 2, 2009 and as described in Note 23 to the Consolidated Financial Statements, AIG's restructuring plan has evolved in response to these market conditions. Specifically, AIG's current plans involve transactions between AIG and the NY Fed with respect to AIA and ALICO, as well as plans to retain the majority of AIG's U.S. property and casualty and foreign general insurance businesses.

AIG believes that these current plans are necessary to maximize the value of its businesses over a longer time frame. Therefore, some businesses that have previously been prepared for sale will be divested, some will be held for later divestiture, and some businesses will be prepared for potential subsequent offerings to the public. Dispositions of certain businesses will be subject to regulatory approval. Proceeds from these dispositions, to the extent they do not represent required capital of AIG's insurance company subsidiaries, are contractually required to be applied toward the repayment of the Fed Facility as mandatory repayments.

In connection with AIG's asset disposition plan, through February 18, 2009, AIG had sold, or entered into contracts to sell the following operations:

- On November 26, 2008, AIG sold its 50 percent stake in the Brazilian joint venture Unibanco AIG Seguros S.A. to AIG's JV partner Unibanco-União de Bancos Brasileiros S.A.
- On December 1, 2008, AIG entered into a contract to sell AIG Private Bank Ltd. to Aabar Investments PJSC.
- On December 18, 2008, AIG sold the assets of its Taiwan Finance business to Taiwan Acceptance Corporation.
- On December 19, 2008, AIG entered into a contract to sell Deutsche Versicherungs-und Rückversicherungs-Aktiengesellschaft (Darag), a German general insurance subsidiary of AIG affiliate Württembergische und Badische Versicherungs-AG(WüBa) in Germany, to Augur.
- On December 22, 2008, AIG entered into a contract to sell HSB Group, Inc., the parent company of HSB, to Munich Re Group.
- On January 13, 2009, AIG entered into a contract to sell AIG Life Insurance Company of Canada to BMO Financial Group.

- On January 23, 2009, AIG entered into a contract to sell AIG PhilAm Savings Bank, PhilAm Auto Financing and Leasing, and PFL Holdings to EastWest Banking Corporation.
- On February 5, 2009, AIG entered into a contract to sell AIG Retail Bank Public Company Limited and AIG Card (Thailand) to Bank of Ayudhya.

Subject to satisfaction of certain closing conditions, including regulatory approvals, AIG expects those sales that are under contract to close during the first half of 2009. These operations had total assets and liabilities with carrying values of approximately $14.1 billion and $12.6 billion, respectively, at December 31, 2008. Aggregate proceeds from the sale of these businesses, including repayment of intercompany loan facilities, are expected to be $2.8 billion. These eight transactions are expected to generate $2.1 billion of net cash proceeds to repay outstanding borrowings on the Fed Facility, after taking insurance affiliate capital requirements into account.

AIG expects to divest its Institutional Asset Management businesses that manage third-party assets. These businesses offered for sale exclude those providing traditional fixed income and shorter duration asset and liability management for AIG's insurance company subsidiaries. The extraction of these asset management businesses will require the establishment of shared service arrangements between the remaining asset management businesses and those that are sold as well as the establishment of new asset management contracts, which will be determined in conjunction with the buyers of these businesses.

AIGFP is engaged in a multi-step process of unwinding its businesses and portfolios. In connection with that process, certain assets have been sold, or are under contract to be sold. The proceeds from these sales will be used for AIGFP's liquidity and are not included in the amounts above. The NY Fed has waived the requirement under the Fed Credit Agreement that the proceeds of these sales be applied as a mandatory repayment under the Fed Facility, which would result in a permanent reduction of the NY Fed's commitment to lend to AIG. Instead, the NY Fed has given AIGFP permission to retain the proceeds of the completed sales, and has required that the proceeds of pending sales be used to voluntarily repay the Fed Facility, with the amounts repaid available for future reborrowing subject to the terms of the Fed Facility. AIGFP is also opportunistically terminating contracts. AIGFP is entering into new derivative transactions only to hedge its current portfolio, reduce risk and hedge the currency, interest rate and other market risks associated with its affiliated businesses. Due to the long-term duration of AIGFP's derivative contracts and the complexity of AIGFP's portfolio, AIG expects that an orderly wind-down will take a substantial period of time. The cost of executing the wind-down will depend on many factors, many of which are not within AIGFP's control, including market conditions, AIGFP's access to markets via market counterparties, the availability of liquidity and the potential implications of further rating downgrades.

AIG continually evaluates overall market conditions, performance of businesses that are for sale, and market and business performance of competitors and likely bidders for the assets. This evaluation informs decision-making about the timing and process of putting businesses up for sale. Depending on market and business conditions, as noted above, AIG can modify its sales approach to maximize value for AIG and the U.S. taxpayers in the disposition process. Such a modification could result in the sale of additional or other assets.

Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (FAS 144) requires that certain criteria be met in order for AIG to classify a business as held for sale. At December 31, 2008, the held for sale criteria in FAS 144 was not met for AIG's significant businesses included in its asset disposition plan.

Expense Reductions and Preservation of Cash and Capital

AIG developed a plan to review significant projects and eliminated, delayed, or curtailed those that are discretionary or non-essential to make available internal resources and to improve liquidity by reducing cash outflows to outside service providers. AIG also suspended the dividend on its common stock to preserve capital.

Liquidity of Parent and Subsidiaries

AIG (Parent Company)

At February 18, 2009, AIG parent had the following sources of liquidity:

- $24.8 billion of available borrowings under the Fed Facility;
- $753 million of available commercial paper borrowings under the CPFF; and
- $1.1 billion of cash and short-term investments.

These sources of liquidity will be supplemented when the liquidity arrangements expected to be entered into among AIG, the NY Fed and the United States Department of the Treasury are implemented. As a result, AIG believes that it has sufficient liquidity at the parent level to meet its obligations through at least the next twelve months. However, no assurance can be given that AIG's cash needs will not exceed projected amounts. Additional collateral calls at AIGFP, a further downgrade of AIG's credit ratings or unexpected capital or liquidity needs of AIG's subsidiaries may result in significant additional cash needs. For a further discussion of this risk, see Item 1A. Risk Factors.

Since the fourth quarter of 2008, AIG has not had access to its traditional sources of long-term or short-term financing through the public debt markets. Further, in light of AIG's current common stock price, AIG does not expect to be able to issue equity securities in the public markets in the foreseeable future.

Traditionally AIG depended on dividends, distributions, and other payments from subsidiaries to fund payments on its obligations. In light of AIG's current financial situation, many of its regulated subsidiaries are restricted from making dividend payments, or advancing funds, to AIG (see Item 1A. Risk Factors). Primary uses of cash flow are for debt service and subsidiary funding. In 2008, AIG parent collected $2.7 billion in dividends and other payments from subsidiaries (primarily from insurance company subsidiaries), issued $12.8 billion of debt and retired $3.2 billion of debt, excluding MIP and Series AIGFP debt. Excluding MIP and Series AIGFP debt, AIG parent made interest payments totaling $1.5 billion, and made $27.2 billion in net capital contributions to subsidiaries. AIG paid $1.7 billion in dividends to shareholders in 2008, prior to the suspension of dividends in September 2008.

AIG parent funds a portion of its short-term working capital needs through commercial paper issued by AIG Funding. Since October 2008, all commercial paper issuance for AIG Funding has been through the CPFF program. As of December 31, 2008, AIG Funding had $6.9 billion of commercial paper outstanding with an average maturity of 32 days, of which $6.6 billion was issued through the CPFF.

AIG's liquidity could also be further impaired by unforeseen significant outflows of cash. This situation may arise due to circumstances that AIG may be unable to control, such as more extensive general market disruption or an operational problem that affects third parties or AIG. Regulatory and other legal restrictions would likely limit AIG's ability to transfer funds freely, either to or from its subsidiaries. For a further discussion of the regulatory environment in which AIG subsidiaries operate and other issues affecting AIG's liquidity, see Item 1A. Risk Factors.

General Insurance

AIG currently expects that its general insurance subsidiaries will be able to continue to meet their obligations as they come due through cash from operations and, to the extent necessary, asset dispositions. One or more large catastrophes, however, may require AIG to provide additional support to the affected general insurance operations. In addition, further downgrades in AIG's credit ratings could put pressure on the insurer financial strength ratings of these subsidiaries. A downgrade in the insurer financial strength ratings of an insurance company subsidiary could result in non-renewals or cancellations by policyholders and adversely affect these companies' ability to meet their own obligations and require that AIG provide capital or liquidity support to them. For a discussion of AIG's potential inability to support its subsidiaries, see Item 1A. Risk Factors — Liquidity.

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General Insurance operating cash flow is derived from underwriting and investment activities. Cash flow from underwriting operations includes collections of periodic premiums and paid loss recoveries, less reinsurance premiums, losses, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and losses and benefits are paid. Investment cash flow is primarily derived from interest and dividends received, and includes investment maturities and repayments.

With respect to General Insurance operations, if paid losses accelerated beyond AIG's ability to fund such losses from current operating cash flows, AIG might need to liquidate a portion of its General Insurance investment portfolio and/or attempt to arrange for financing. A liquidity strain could result from the occurrence of one or several significant catastrophic events in a relatively short period of time. Additional strain on liquidity could occur if the investments liquidated to fund such paid losses were sold in a depressed market place. Further liquidity strains could also arise if reinsurance recoverable on such paid losses became uncollectible or collateral supporting such reinsurance recoverable significantly decreased in value.

At December 31, 2008, General Insurance had liquidity in the form of cash and short-term investments of $11.7 billion. In the event additional liquidity is required, management believes it can provide such liquidity through sale of a portion of its substantial holdings in government and corporate bonds as well as equity securities. Government and corporate bonds represented 97.6 percent of total fixed income investments at December 31, 2008. Given the size and liquidity profile of AIG's General Insurance investment portfolios, AIG believes that deviations from its projected claim experience do not constitute a significant liquidity risk. AIG's asset/liability management process takes into account the expected maturity of investments and the specific nature and risk profile of liabilities. Historically, there has been no significant variation between the expected maturities of AIG's General Insurance investments and the payment of claims.

AIG has arranged for letters of credit that totaled $1.6 billion and funded trusts totaling $2.9 billion at December 31, 2008, to allow certain AIG Property and Casualty Group subsidiaries to obtain admitted surplus credit for reinsurance provided by non-admitted carriers. Substantially all the letters of credit may be cancelled on December 31, 2010. The inability of AIG to renew or replace these letters of credit or otherwise obtain equivalent financial support would result in a reduction of the statutory surplus of these property and casualty companies. AIG Property Casualty Group maintains liquidity in its investment portfolio through holdings of $6.2 billion of municipal securities which have been refunded and are escrowed to the call or to maturity. The maturities of these holdings are all less than ten years, and the bonds are secured by the United States Department of the Treasury or Government Agency securities held in escrow by trustees. These municipal holdings have substantial unrealized gains and demonstrated liquidity even during the market dislocations experienced during the fourth quarter of 2008.

Life Insurance & Retirement Services

Life Insurance & Retirement Services operating cash flow is derived from underwriting and investment activities. Cash flow from underwriting operations includes collections of periodic premiums and policyholders' contract deposits, and paid loss recoveries, less reinsurance premiums, losses, benefits, surrenders, and acquisition and operating expenses. Generally, there is a time lag from when premiums are collected and losses and benefits are paid. Investment cash flow is primarily derived from interest and dividends received, and includes investment maturities and repayments. Contributions from AIG parent also represent a liquidity source.

If a substantial portion of the Life Insurance & Retirement Services operations bond portfolio diminished significantly in value and/or defaulted, AIG might need to provide capital or liquidity support to these operations. For a discussion of AIG's potential inability to support its subsidiaries, see Item 1A. Risk Factors — Liquidity. A significant increase in policy surrenders and withdrawals, which could be triggered by a variety of factors, including AIG-specific concerns, could result in a substantial liquidity strain. Other potential events causing a liquidity strain could include economic collapse of a nation or region in which Life Insurance & Retirement Services operations exist, nationalization, catastrophic terrorist acts, or other economic or political upheaval.

At December 31, 2008, Life Insurance & Retirement Services had liquidity in the form of cash and short-term investments of $32.3 billion. In the event additional liquidity is required, management believes it can provide such liquidity through sale of a portion of its substantial holdings in government and corporate bonds as well as equity

securities. Government and corporate bonds represented 84.8 percent of total fixed income investments at December 31, 2008. Given the size and liquidity profile of AIG's Life Insurance & Retirement Services investment portfolios, AIG believes that deviations from its projected claim experience do not constitute a significant liquidity risk. AIG's asset/liability management process takes into account the expected maturity of investments and expected benefit payments and policy surrenders as well as the specific nature and risk profile of these liabilities. The Life Insurance & Retirement Services subsidiaries have been able to meet liquidity needs, even during the period of higher surrenders which was experienced from mid-September through year-end 2008, and expect to be able to do so in the foreseeable future.

Foreign Life Insurance Companies

AIG's Foreign Life Insurance companies (including ALICO) have had significant capital needs following publicity of AIG parent's liquidity issues and related credit ratings downgrades and reflecting the decline in the equity markets. AIG contributed $4.4 billion to the Foreign Life Insurance companies during 2008 ($4.0 billion of which was contributed using borrowings under the Fed Facility). In Taiwan, AIG contributed approximately $1.8 billion to Nan Shan in 2008 as a result of the continued declines in the Taiwan equity market and foreign currency movements. AIG made capital contributions of $2.6 billion to support foreign life operations in Hong Kong and Japan, principally due to the steep decline in AIG's common stock price.

AIG believes that its Foreign Life Insurance subsidiaries have adequate capital to support their business plans through 2009; however, to the extent the investment portfolios of the Foreign Life Insurance companies continue to be adversely affected by market conditions, AIG may need to make additional capital contributions to these companies. For a discussion of AIG's potential inability to support its subsidiaries, see Item 1A. Risk Factors — Liquidity.

Domestic Life Insurance and Domestic Retirement Services Companies

AIG's Domestic Life Insurance and Domestic Retirement Services companies have two primary liquidity needs: the funding of surrenders, and obtaining capital to offset statutory other-than-temporary impairment charges. At the current rate of surrenders, AIG believes that its Domestic Life Insurance and Domestic Retirement Services companies will have sufficient resources to meet these obligations. A substantial increase in surrender activity could, however, place stress on the liquidity of these companies and require asset sales or contributions from AIG.

During the year ended December 31, 2008 and through February 27, 2009, AIG contributed capital totaling $22.7 billion ($18.0 billion of which was contributed using borrowings under the Fed Facility) to certain of its Domestic Life Insurance and Domestic Retirement Services subsidiaries to replace a portion of the capital lost as a result of net realized capital losses (primarily resulting from other-than-temporary impairment charges). Further capital contributions may be required to the extent additional statutory net realized capital losses are incurred. For a discussion of AIG's potential inability to support its subsidiaries, see Item 1A. Risk Factors — Liquidity.

Financial Services

AIG's major Financial Services operating subsidiaries consist of ILFC, AIGFP, AGF and AIGCFG. Traditional sources of funds considered in meeting the liquidity needs of these operations are generally no longer available. These sources included GIAs' issuance of long- and short-term debt, issuance of commercial paper, bank loans and bank credit facilities. However, AIGCFG has been able to retain a significant portion of customer deposits, providing a measure of liquidity.

ILFC

ILFC's traditional source of liquidity had been collections of lease payments and borrowing in the public debt markets to fund aircraft purchases and to satisfy maturing debt. Additional liquidity is provided by the proceeds of aircraft sales.

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In September 2008, ILFC was unable to borrow in the public debt markets, and therefore, ILFC borrowed the full $6.5 billion amount available under its credit facilities. ILFC was also accepted into the CPFF and had borrowed approximately $1.7 billion under the CPFF as of December 31, 2008. On January 21, 2009, however, S&P downgraded ILFC's short-term credit rating and, as a result, ILFC lost access to the CPFF. The $1.7 billion ILFC had borrowed under the CPFF was due and paid on January 28, 2009. ILFC is currently seeking secured financing. ILFC has the capacity under its present facilities and indentures, to enter into secured financings in excess of $5.0 billion. If ILFC continues to be limited in its ability to use this capacity, AIG expects that these borrowings and cash flows from operations, which may include aircraft sales, will be inadequate to permit ILFC to meet its obligations for 2009. Therefore, AIG will need to provide support through additional asset sales or funding for the remaining amounts.

As a result of Moody's downgrade of ILFC's long-term debt rating, ILFC received notice under the provisions of the Export Credit Facilities to segregate security deposits and maintenance reserves related to aircraft funded under the facilities into separate accounts. ILFC had 90 days from the date of the notice to comply and, subsequent to December 31, 2008, ILFC segregated approximately $260 million of deposits and maintenance reserves. The amount of funds required to be segregated under the facility agreements fluctuates with the changes in the related deposits, maintenance reserves, and debt maturities. Further rating downgrades would impose additional restrictions under these facilities including the requirement to segregate rental payments and would require prior consent to withdraw funds from the segregated account.

AIGFP

AIGFP had historically funded its operations through the issuance of notes and bonds, GIA borrowings and other structured financing transactions. AIGFP also obtained funding through repurchase agreements.

In the last half of 2008, AIGFP's access to its traditional sources of liquidity were significantly reduced and it relied on AIG Parent to meet most of its liquidity needs. AIGFP's asset backed commercial paper conduit, Curzon Funding LLC, was accepted into the CPFF with a total borrowing limit of $7.2 billion, and had approximately $6.8 billion outstanding at February 18, 2009. Separately, a structured investment vehicle sponsored, but not consolidated, by AIGFP, Nightingale Finance LLC, was also accepted into the CPFF with a borrowing limit of $1.1 billion. As of February 18, 2009, this vehicle had approximately $1.1 billion outstanding under the CPFF.

AGF

AGF's traditional source of liquidity has been collections of customer receivables and borrowing in the public markets.

In September 2008, AGF was unable to borrow in the public debt markets and drew down $4.6 billion, the full amount available, under its primary credit facilities. AGF anticipates that its primary source of funds to support its operations and repay its obligations will be customer receivable collections. In order to improve cash flow, AGF will limit its lending activities and manage its expenses. In addition, AGF is pursuing sales of certain of its finance receivables and seeking securitization financing. AIG expects that AGF's existing sources of funds will be inadequate to meet its debt and other obligations for 2009. Therefore, AIG will need to provide support through additional asset sales or funding for the remaining amounts.

AIGCFG

AIGCFG experienced significant deposit withdrawals in Hong Kong during September 2008. AIGCFG subsidiaries borrowed $1.6 billion from AIG in September and October of 2008 to meet these withdrawals and other cash needs. No further material funding was required during the remainder of the fourth quarter of 2008.

Since November of 2008, AIGCFG subsidiaries have been able to retain significant deposit balances as a result of the lowered perceived risk, as well as depository insurance support provided by various regulatory authorities in countries in which AIGCFG units operate.

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AIG believes that the funding needs of AIGCFG have stabilized, but it is possible that renewed customer and counterparty concerns could substantially increase AIGCFG's liquidity needs in 2009. Through February 18, 2009, AIGCFG had entered into contracts to sell certain of its operations in Taiwan, Thailand and the Philippines.

Asset Management

Asset Management's principal cash requirements are to fund general working capital needs, investment commitments related to proprietary investments originally acquired for warehouse purposes, contractual capital commitments, proprietary investments of AIG Global Real Estate and any liquidity mismatches in the Spread-Based Investment business. Requirements related to Institutional Asset Management are funded through general operating cash flows from management and performance fees, proceeds from events in underlying funds (capital calls to third parties, sale of portfolio companies, etc.) as well as intercompany funding provided by AIG. Accordingly, Institutional Asset Management's ability to fund certain of its needs may depend on advances from AIG under various intercompany borrowing facilities. Restrictions on these facilities would have adverse consequences on the ability of the business to satisfy its respective obligations. With respect to the Global Real Estate business, investing activities are also funded through third-party financing arrangements which are secured by the relevant properties.

The GIC and MIP programs are in run-off. AIG expects to fund its obligations under these programs through cash flows generated from invested assets (principal and interest) as well as sales of investments, primarily fixed maturity securities. However, illiquidity and diminished values within the investment portfolios may impair AIG's ability to sell the related program assets or sell such assets for a price adequate to settle the corresponding liabilities when they come due. In such a case, AIG parent would need to fund the payments.

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American International Group, Inc., and Subsidiaries

Debt

Total debt was as follows:

	At December 31, 2008	2007
	(In millions)	
Debt issued by AIG:		
Fed Facility (secured)	**$ 40,431**	$ —
Notes and bonds payable	**11,756**	14,588
Junior subordinated debt	**11,685**	5,809
Junior subordinated debt attributable to equity units	**5,880**	—
Loans and mortgages payable	**416**	729
MIP matched notes and bonds payable	**14,446**	14,267
AIGFP matched notes and bonds payable	**4,660**	874
Total AIG debt	**89,274**	36,267
Debt guaranteed by AIG:		
AIGFP *(a)*		
Commercial paper *(b)*	**6,802**	—
GIAs	**13,860**	19,908
Notes and bonds payable	**5,250**	36,676
Loans and mortgages payable	**2,175**	1,384
Hybrid financial instrument liabilities *(c)*	**2,113**	7,479
Total AIGFP debt	**30,200**	65,447
AIG Funding commercial paper *(b)*	**6,856**	4,222
AIGLH notes and bonds payable	**798**	797
Liabilities connected to trust preferred stock	**1,415**	1,435
Total debt issued or guaranteed by AIG	**128,543**	108,168
Debt not guaranteed by AIG:		
ILFC		
Commercial paper *(b)*	**1,748**	4,483
Junior subordinated debt	**999**	999
Notes and bonds payable *(d)*	**30,047**	25,737
Total ILFC debt	**32,794**	31,219
AGF		
Commercial paper and extendible commercial notes	**188**	3,801
Junior subordinated debt	**349**	349
Notes and bonds payable	**23,089**	22,369
Total AGF debt	**23,626**	26,519
AIGCFG		
Commercial paper	**124**	287
Loans and mortgages payable	**1,596**	1,839
Total AIGCFG debt	**1,720**	2,126
Other subsidiaries	**670**	775
Debt of consolidated investments held through:		

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American International Group, Inc., and Subsidiaries

	At December 31,	
	2008	2007
	(In millions)	
A.I. Credit *(e)*	—	321
AIG Investments	**1,300**	1,636
AIG Global Real Estate	**4,545**	5,096
AIG SunAmerica	**5**	186
ALICO	—	3
Total debt of consolidated investments	**5,850**	7,242
Total debt not guaranteed by AIG	**64,660**	67,881
Consolidated:		
Total commercial paper and extendible commercial notes	**613**	13,114
Federal Reserve Bank of New York commercial paper funding facility	**15,105**	—
Total long-term debt	**177,485**	162,935
Total debt	**$193,203**	$176,049

(a) *In 2008, AIGFP borrowings are carried at fair value.*

(b) *Includes borrowings of $6.8 billion, $6.6 billion and $1.7 billion for AIGFP (through Curzon Funding LLC, AIGFP's asset-backed commercial paper conduit), AIG Funding and ILFC, respectively, under the CPFF at December 31, 2008.*

(c) *Represents structured notes issued by AIGFP that are accounted at fair value.*

(d) *Includes borrowings under Export Credit Facility of $2.4 billion and $2.5 billion at December 31, 2008 and 2007, respectively.*

(e) *Represents commercial paper issued by a variable interest entity secured by receivables of A.I. Credit.*

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Long-Term Debt

A roll forward of long-term debt, excluding debt of consolidated investments is as follows:

for the year ended December 31, 2008 (In millions)	Balance at December 31, 2007	Issuances	Maturities and Repayments	Effect of Foreign Exchange	Other Non-Cash Changes(b)	Balance at December 31, 2008
AIG						
Fed Facility	$ —	$ 96,650	$ (59,850)	$ —	$ 3,631	**$ 40,431**
Notes and bonds payable	14,588	—	(2,700)	(1)	(131)	**11,756**
Junior subordinated debt	5,809	6,953	—	(1,078)	1	**11,685**
Junior subordinated debt attributable to equity units	—	5,880	—	—	—	**5,880**
Loans and mortgages payable	729	457	(762)	8	(16)	**416**
MIP matched notes and bonds payable	14,267	—	(194)	(38)	411	**14,446**
AIGFP matched notes and bonds payable	874	3,464	(198)	—	520	**4,660**
AIGFP *(a)*						
GIAs	19,908	5,070	(16,576)	—	5,458	**13,860**
Notes and bonds payable and hybrid financial instrument liabilities	44,155	63,803	(99,531)	—	(1,064)	**7,363**
Loans and mortgages payable	1,384	9,254	(8,512)	—	49	**2,175**
AIGLH notes and bonds payable	797	—	—	—	1	**798**
Liabilities connected to trust preferred stock	1,435	—	(19)	—	(1)	**1,415**
ILFC notes and bonds payable	25,737	9,389	(4,575)	(507)	3	**30,047**
ILFC junior subordinated debt	999	—	—	—	—	**999**
AGF notes and bonds payable	22,369	5,844	(4,659)	(427)	(38)	**23,089**
AGF junior subordinated debt	349	—	—	—	—	**349**
AIGCFG loans and mortgages payable	1,839	2,278	(2,431)	(214)	124	**1,596**
Other subsidiaries	775	23	(165)	26	11	**670**
Total	$ 156,014	$209,065	$(200,172)	$ (2,231)	$ 8,959	**$ 171,635**

(a) *In 2008, AIGFP borrowings are carried at fair value.*

(b) *Includes the change in fair value and cumulative effect of the adoption of FAS 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (FAS 159). Also includes commitment fee and accrued compounding interest of $3.63 billion on the Fed Facility.*

AIG (Parent Company)

AIG traditionally issued debt securities from time to time to meet its financing needs and those of certain of its subsidiaries, as well as to opportunistically fund the MIP. The maturities of the debt securities issued by AIG to fund the MIP are generally expected to be paid using the cash flows of assets held by AIG as part of the MIP portfolio. However, mismatches in the timing of cash inflows and outflows of the MIP, as well as shortfalls due to impairments of MIP assets, would need to be funded by AIG parent.

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On August 18, 2008, AIG sold $3.25 billion principal amount of senior unsecured notes in a Rule 144A/Regulation S offering which bear interest at a per annum rate of 8.25 percent and mature in 2018. The proceeds from the sale of these notes were used by AIGFP for its general corporate purposes, and the notes are included within "AIGFP matched notes and bonds payable" in the preceding tables. AIG has agreed to use commercially reasonable efforts to consummate an exchange offer for the notes pursuant to an effective registration statement within 360 days of the date on which the notes were issued.

As of December 31, 2008, approximately $7.5 billion principal amount of senior notes were outstanding under AIG's medium-term note program, of which $3.2 billion was used for AIG's general corporate purposes, $893 million was used by AIGFP (included within "AIGFP matched notes bonds and payable" in the preceding tables) and $3.4 billion was used to fund the MIP. The maturity dates of these notes range from 2009 to 2052. To the extent considered appropriate, AIG may enter into swap transactions to manage its effective borrowing rates with respect to these notes.

As of December 31, 2008, the equivalent of $12.0 billion of notes were outstanding under AIG's Euro medium-term note program, of which $9.7 billion were used to fund the MIP and the remainder was used for AIG's general corporate purposes. The aggregate amount outstanding includes a $588 million loss resulting from foreign exchange translation into U.S. dollars, of which $0.1 million gain relates to notes issued by AIG for general corporate purposes and $588 million loss relates to notes issued to fund the MIP. AIG has economically hedged the currency exposure arising from its foreign currency denominated notes.

In May 2008, AIG raised a total of approximately $20 billion through the sale of (i) 196,710,525 shares of AIG common stock in a public offering at a price per share of $38; (ii) 78.4 million Equity Units in a public offering at a price per unit of $75; and (iii) $6.9 billion in unregistered offerings of junior subordinated debentures in three series. The Equity Units and junior subordinated debentures receive hybrid equity treatment from the major rating agencies under their current policies but are recorded as long-term debt on the consolidated balance sheet. The Equity Units consist of an ownership interest in AIG junior subordinated debentures and a stock purchase contract obligating the holder of an equity unit to purchase, and obligating AIG to sell, a variable number of shares of AIG common stock on three dates in 2011 (a minimum of 128,944,480 shares and a maximum of 154,738,080 shares, subject to anti-dilution adjustments).

During 2007 and 2008, AIG issued an aggregate of $12.5 billion of junior subordinated debentures in U.S. dollars, British Pounds and Euros in eight series. In connection with each series of junior subordinated debentures, AIG entered into a Replacement Capital Covenant (RCC) for the benefit of the holders of AIG's 6.25 percent senior notes due 2036. The RCCs provide that AIG will not repay, redeem, or purchase the applicable series of junior subordinated debentures on or before a specified date, unless AIG has received qualifying proceeds from the sale of the replacement capital securities.

In October 2007, AIG borrowed a total of $500 million on an unsecured basis pursuant to a loan agreement with a third-party bank. The entire amount of the loan was repaid on September 30, 2008.

AIGFP

Approximately $3.1 billion of AIGFP's debt maturities through December 31, 2009 are fully collateralized with assets backing the corresponding liabilities. However, mismatches in the timing of cash inflows on the assets and outflows with respect to the liabilities may require assets to be sold to satisfy maturing liabilities. Depending on market conditions and AIGFP's ability to sell assets at that time, proceeds from sales may not be sufficient to satisfy the full amount due on maturing liabilities. Any shortfalls would need to be funded by AIG parent.

ILFC

ILFC has a $4.3 billion Export Credit Facility for use in connection with the purchase of approximately 75 aircraft delivered through 2001. This facility was guaranteed by various European Export Credit Agencies. The interest rate varies from 5.75 percent to 5.86 percent on these amortizing ten-year borrowings depending on the delivery date of the aircraft. At December 31, 2008, ILFC had $365 million outstanding under this facility. The debt is collateralized by a pledge of the shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility.

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ILFC has a similarly structured Export Credit Facility for up to a maximum of $3.6 billion for Airbus aircraft to be delivered through May 31, 2009. The facility becomes available as the various European Export Credit Agencies provide their guarantees for aircraft based on a forward-looking calendar, and the interest rate is determined through a bid process. The interest rates are either LIBOR based with spreads ranging from (0.04) percent to 0.90 percent or at fixed rates ranging from 4.2 percent to 4.7 percent. At December 31, 2008, ILFC had $2.1 billion outstanding under this facility. At December 31, 2008, the interest rate of the loans outstanding ranged from 2.51 percent to 4.71 percent. The debt is collateralized by a pledge of shares of a subsidiary of ILFC, which holds title to the aircraft financed under the facility. Borrowings with respect to these facilities are included in ILFC's notes and bonds payable in the preceding table of borrowings.

At December 31, 2008, the total funded amount of ILFC's bank financings was $7.6 billion. The fundings mature through February 2012. The interest rates are LIBOR-based, with spreads ranging from 0.30 percent to 1.625 percent. At December 31, 2008, the interest rates ranged from 2.15 percent to 4.36 percent. AIG does not guarantee any of the debt obligations of ILFC.

AGF

As of December 31, 2008, notes and bonds aggregating $23.1 billion were outstanding with maturity dates ranging from 2009 to 2031 at interest rates ranging from 0.23 percent to 9 percent. To the extent considered appropriate, AGF may enter into swap transactions to manage its effective borrowing rates with respect to these notes and bonds.

AIG does not guarantee any of the debt obligations of AGF but has provided a capital support agreement for the benefit of AGF's lenders under the AGF 364-Day Syndicated Facility. Under this support agreement, AIG has agreed to cause AGF to maintain (1) consolidated net worth of $2.2 billion and (2) an adjusted tangible leverage ratio of less than or equal to 8 to 1 at the end of each fiscal quarter.

Revolving Credit Facilities

AIG, ILFC and AGF maintain committed, unsecured revolving credit facilities listed on the table below in order to support their respective commercial paper programs and for general corporate purposes. Some of the facilities, as noted below, contain a "term-out option" allowing for the conversion by the borrower of any outstanding loans at expiration into one-year term loans.

Both ILFC and AGF have drawn the full amount available under their revolving credit facilities. AIG's syndicated facilities contain a covenant requiring AIG to maintain total shareholders' equity (calculated on a consolidated basis consistent with GAAP) of at least $50 billion at all times. If AIG fails to maintain this level of total shareholders' equity at any time, it will lose access to those facilities. Additionally, if an event of default occurs under those facilities, including AIG failing to maintain $50 billion of total shareholders' equity at any time, which causes the banks to terminate either of those facilities, then AIG may be required to collateralize approximately

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$2.7 billion of letters of credit that AIG has obtained for the benefit of its insurance subsidiaries so that these subsidiaries may obtain statutory recognition of their intercompany reinsurance transactions.

At December 31, 2008 (in millions) Facility	Size	Borrower(s)	Available Amount (In millions)	Expiration	One-Year Term-Out Option
AIG:					
364-Day Syndicated Facility *(a)*	$2,125	AIG/AIG Funding *(b)*	$ 2,125	July 2009	Yes
5-Year Syndicated Facility *(a)*	1,625	AIG/AIG Funding *(b)*	1,625	July 2011	No
Total AIG	$3,750		$ 3,750		
ILFC:					
5-Year Syndicated Facility	$2,500	ILFC	$ —	October 2011	No
5-Year Syndicated Facility	2,000	ILFC	—	October 2010	No
5-Year Syndicated Facility	2,000	ILFC	—	October 2009	No
Total ILFC	$6,500		$ —		
AGF:					
364-Day Syndicated Facility	$2,450	American General Finance Corporation	$ —	July 2009	Yes
		American General Finance, Inc. *(c)*	—		
5-Year Syndicated Facility	2,125	American General Finance Corporation	—	July 2010	No
Total AGF	$4,575		$ —		

(a) On October 5, 2008, Lehman Brothers Holdings Inc. (LBHI), the parent company of Lehman Brothers Bank, FSB (LBB), filed for bankruptcy protection. LBB is a lender under AIG's 364-Day Syndicated Facility and 5-Year Syndicated Facility and had committed to provide $100 million and $42.5 million, respectively, under these facilities. While LBB is not included in the LBHI bankruptcy filing, AIG cannot be certain whether LBB would fulfill it commitments under these facilities.

(b) Guaranteed by AIG. In September 2008, AIG Capital Corporation was removed as a borrower on the syndicated facilities.

(c) AGF is an eligible borrower for up to $400 million only.

Credit Ratings

The cost and availability of unsecured financing for AIG and its subsidiaries are generally dependent on their short-and long-term debt ratings. The following table presents the credit ratings of AIG and certain of its subsidiaries as of February 18, 2009. In parentheses, following the initial occurrence in the table of each rating, is an indication of that rating's relative rank within the agency's rating categories. That ranking refers only to the

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generic or major rating category and not to the modifiers appended to the rating by the rating agencies to denote relative position within such generic or major category.

	Short-term Debt			Senior Long-term Debt		
	Moody's	S&P	Fitch	Moody's(a)	S&P(b)	Fitch(c)
AIG	P-1 (1st of 3) *(g)*	A-1 (1st of 8) *(e)*	F1 (1st of 5)	A3 (3rd of 9) *(g)*	A- (3rd of 8) *(e)*	A (3rd of 9)
AIG Financial Products Corp. *(d)*	P-1 *(g)*	A-1 *(e)*	—	A3 *(g)*	A- *(e)*	—
AIG Funding *(d)*	P-1 *(g)*	A-1 *(e)*	F1	—	—	—
ILFC	P-2 (2nd of 3) *(h)*	A-2 (2nd of 8) *(f)*	F1 *(j)*	Baa1 (4th of 9) *(h)*	BBB+ (4th of 8) *(f)*	A *(j)*
American General Finance Corporation	P-2 *(i)*	B (4th of 8)	F1 *(j)*	Baa1 *(g)*	BB+ (5th of 8) *(i)*	BBB (4th of 9) *(j)*
American General Finance, Inc.	P-2 *(g)*	A-3 (3rd of 8)	F1 *(j)*	—	—	BBB *(j)*

(a) *Moody's appends numerical modifiers 1, 2 and 3 to the generic rating categories to show relative position within the rating categories.*

(b) *S&P ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.*

(c) *Fitch ratings may be modified by the addition of a plus or minus sign to show relative standing within the major rating categories.*

(d) *AIG guarantees all obligations of AIG Financial Products Corp. and AIG Funding.*

(e) *Credit Watch Negative.*

(f) *Credit Watch Developing.*

(g) *Under Review for Possible Downgrade.*

(h) *Under Review with Direction Uncertain.*

(i) *Negative Outlook.*

(j) *Rating Watch Evolving.*

These credit ratings are current opinions of the rating agencies. As such, they may be changed, suspended or withdrawn at any time by the rating agencies as a result of changes in, or unavailability of, information or based on other circumstances. Ratings may also be withdrawn at AIG management's request. This discussion of ratings is not a complete list of ratings of AIG and its subsidiaries.

"Ratings triggers" have been defined by one independent rating agency to include clauses or agreements the outcome of which depends upon the level of ratings maintained by one or more rating agencies. "Ratings triggers" generally relate to events that (i) could result in the termination or limitation of credit availability, or require accelerated repayment, (ii) could result in the termination of business contracts or (iii) could require a company to post collateral for the benefit of counterparties.

A significant portion of AIGFP's GIAs, structured financing arrangements and financial derivative transactions include provisions that require AIGFP, upon a downgrade of AIG's long-term debt ratings, to post collateral or, with the consent of the counterparties, assign or repay its positions or arrange a substitute guarantee of its obligations by an obligor with higher debt ratings. Furthermore, certain downgrades of AIG's long-term senior debt ratings would permit either AIG or the counterparties to elect early termination of contracts.

The actual amount of collateral that AIGFP would be required to post to counterparties in the event of such downgrades, or the aggregate amount of payments that AIG could be required to make, depends on market conditions, the fair value of outstanding affected transactions and other factors prevailing at the time of the downgrade. For the impact of a downgrade in AIG's credit ratings, see Item 1A. Risk Factors — Credit Ratings.

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Contractual Obligations

Contractual obligations in total, and by remaining maturity were as follows:

		Payments due by Period			
At December 31, 2008	Total Payments	Less Than One Year	1-3 Years	3+-5 Years	More Than Five Years
			(In millions)		
Borrowings *(a)*	$ 131,204	$ 20,417	$ 33,574	$ 18,607	$ 58,606
Fed Facility	40,431	—	—	40,431	—
Interest payments on borrowings	81,860	5,361	9,281	22,832	44,386
Loss reserves *(b)*	89,258	24,546	27,224	12,942	24,546
Insurance and investment contract liabilities *(c)*	620,440	32,059	41,703	38,103	508,575
GIC liabilities *(d)*	18,020	6,175	2,472	3,406	5,967
Aircraft purchase commitments	16,677	3,028	448	2,917	10,284
Operating leases	4,258	800	1,094	699	1,665
Other long-term obligations	562	228	308	12	14
Total *(e)(f)*	$1,002,710	$ 92,614	$116,104	$139,949	$654,043

(a) Excludes commercial paper and borrowings incurred by consolidated investments and includes hybrid financial instrument liabilities recorded at fair value.

(b) Represents future loss and loss adjustment expense payments estimated based on historical loss development payment patterns. Due to the significance of the assumptions used, the periodic amounts presented could be materially different from actual required payments.

(c) Insurance and investment contract liabilities include various investment-type products with contractually scheduled maturities, including periodic payments of a term certain nature. Insurance and investment contract liabilities also include benefit and claim liabilities, of which a significant portion represents policies and contracts that do not have stated contractual maturity dates and may not result in any future payment obligations. For these policies and contracts (i) AIG is currently not making payments until the occurrence of an insurable event, such as death or disability, (ii) payments are conditional on survivorship, or (iii) payment may occur due to a surrender or other non-scheduled event out of AIG's control. AIG has made significant assumptions to determine the estimated undiscounted cash flows of these contractual policy benefits, which assumptions include mortality, morbidity, future lapse rates, expenses, investment returns and interest crediting rates, offset by expected future deposits and premiums on inforce policies. Due to the significance of the assumptions used, the periodic amounts presented could be materially different from actual required payments. The amounts presented in this table are undiscounted and therefore exceed the future policy benefits and policyholder contract deposits included in the balance sheet.

(d) Represents guaranteed maturities under GICs.

(e) Does not reflect unrecognized tax benefits of $3.4 billion, the timing of which is uncertain.

(f) The majority of AIGFP's credit default swaps require AIGFP to provide credit protection on a designated portfolio of loans or debt securities. At December 31, 2008, the fair value derivative liability was $5.9 billion relating to AIGFP's super senior multi-sector CDO credit default swap portfolio, net of amounts realized in extinguishing derivative obligations. Due to the long-term maturities of these credit default swaps, AIG is unable to make reasonable estimates of the periods during which any payments would be made.

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Off Balance Sheet Arrangements and Commercial Commitments

Off Balance Sheet Arrangements and Commercial Commitments in total, and by remaining maturity were as follows:

at December 31, 2008	Total Amounts Committed	Amount of Commitment Expiration: Less Than One Year	1-3 Years	3+-5 Years	Over Five Years
		(In millions)			
Guarantees:					
Liquidity facilities *(a)*	$ 912	$ —	$ —	$ 799	$ 113
Standby letters of credit	1,541	1,340	41	25	135
Construction guarantees *(b)*	155	—	—	—	155
Guarantees of indebtedness	776	77	134	307	258
All other guarantees	1,857	69	48	28	1,712
Commitments:					
Investment commitments *(c)*	9,185	2,575	3,742	1,951	917
Commitments to extend credit	629	132	437	54	6
Letters of credit	316	306	10	—	—
Other commercial commitments *(d)*	1,034	3	—	160	871
Total	$ 16,405	$ 4,502	$4,412	$3,324	$ 4,167

(a) Primarily liquidity facilities provided in connection with certain municipal swap transactions and collateralized bond obligations.

(b) Primarily AIG SunAmerica construction guarantees connected to affordable housing investments.

(c) Includes commitments to invest in limited partnerships, private equity, hedge funds and mutual funds and commitments to purchase and develop real estate in the United States and abroad.

(d) Includes options to acquire aircraft. Excludes commitments with respect to pension plans. The annual pension contribution for 2009 is expected to be approximately $600 million for U.S. and non-U.S. plans.

Arrangements with Variable Interest Entities

AIG enters into various arrangements with variable interest entities (VIEs) in the normal course of business. AIG's insurance companies are involved with VIEs primarily as passive investors in debt securities (rated and unrated) and equity interests issued by VIEs. Through its Financial Services and Asset Management operations, AIG has participated in arrangements that included designing and structuring entities, warehousing and managing the collateral of the entities, entering into insurance transactions with VIEs. Interest holders in the VIEs generally have recourse only to the assets and cash flows of the VIEs and do not have recourse to AIG, except, in limited circumstances, when AIG has provided a guarantee to the VIEs' interest holders.

Under FIN 46(R), AIG consolidates a VIE when it is the primary beneficiary of the entity. The primary beneficiary is the party that either (i) absorbs a majority of the VIE's expected losses; (ii) receives a majority of the VIE's expected residual returns; or (iii) both. For a further discussion of AIG's involvement with VIEs, see Note 9 of Notes to the Consolidated Financial Statements.

Outlook

General disruptions in the global equity and credit markets and the liquidity issues at AIG have negatively affected the results of each of AIG's operating segments as discussed below.

General Insurance

Commercial Insurance has been generally successful in retaining clients, although some have reduced the number of lines or limits of coverage due in part to concerns over AIG's financial strength. In addition, the number

of new business opportunities has declined since September of 2008. Senior management has spent considerable time since September 2008 meeting with policyholders and brokers explaining the financial strength of Commercial Insurance and the protections afforded policyholders by insurance regulations. However, net premiums written declined 22 percent in the fourth quarter of 2008 compared to the same period of 2007. The retention of existing business continues to be moderately lower than in the comparable prior year period, however retention levels have improved in the early part of 2009 compared to the fourth quarter of 2008.

Overall, rates in Commercial Insurance are essentially flat in early 2009 compared to the first quarter of 2008. The stabilization of rates is an improvement from the fourth quarter of 2008 and reflects the offsetting effects of downward pressure on premiums from the current recessionary environment and the recent introduction of new competitors in the marketplace and the upward pressure on premiums from the combination of investment and underwriting losses suffered by the commercial insurance industry.

AIG expects that the current recessionary environment will continue to affect UGC's operating results for the foreseeable future and will result in a significant operating loss for UGC in 2009.

Foreign General Insurance has been successful in retaining business in its property, casualty and consumer lines. During the critical first quarter 2009 renewal period with more than 30 percent of the annual production expected, business retention was strong in Foreign General Insurance's top three regions, U.K./Ireland, Europe and the Far East, with the significant majority of clients maintaining their relationship with AIG. However, there was some expected "de-risking" among customers to further diversify their portfolios as well as a slight reduction in new business production. Because the three regions represent the majority of business, recent business activity is comparable to 2008. Overall, gross premiums to date for 2009 were essentially flat from the comparable period of 2008 as measured in original currency.

Life Insurance & Retirement Services

AIG expects that the aforementioned events and AIG's previously announced asset disposition plan will continue to adversely affect Life Insurance & Retirement Services operating results in 2009, specifically net investment income, deferred policy acquisition costs and sales inducement asset (SIA) amortization and net realized capital gains (losses). In addition, AIG's liquidity issues have affected certain operations through higher surrender activity, primarily in the U.S. domestic retirement fixed annuity business and foreign investment-oriented and retirement products in Japan and Asia. While surrender levels have declined from their peaks in mid-September of 2008, they continue to be higher than historic levels in certain products and countries and AIG expects them to continue to be volatile.

These uncertainties, together with rating agency downgrades, have resulted in significantly reduced levels of new sales activity, particularly among products and markets where ratings are critical. Sales of investment-oriented and retirement services products have also declined due to the general decline in the equity markets. New sales activity is expected to remain at lower levels until the uncertainties relating to AIG are resolved.

Financial Services

AIGFP began unwinding its businesses and portfolios during the fourth quarter of 2008, and these activities are expected to continue at least through 2009. In connection with these activities, AIGFP has disaggregated its portfolio of existing transactions into a number of separate "books", and has developed a plan for addressing each book, including each book's risks, risk mitigation options, monitoring metrics and certain implications of various potential outcomes. Each plan has been reviewed by a steering committee whose membership includes senior executives of AIG. The plans are subject to change as efforts progress and as conditions in the financial markets evolve, and they contemplate, depending on the book in question, alternative strategies, including sales, assignments or other transfers of positions, terminations of positions, and/or run-offs of positions in accordance with existing terms. Execution of the plans is overseen by a transaction approval process involving increasingly senior members of AIGFP's and AIG's respective management groups as specific actions entail greater liquidity and revenue consequences. Successful execution of the plans is subject, to varying degrees depending on the transactions of a given book, to market conditions and, in many circumstances, counterparty negotiation and agreement.

As a consequence of its wind-down strategy, AIGFP is entering into new derivative transactions only to hedge its current portfolio, reduce risk and hedge the currency, interest rate and other market risks associated with its affiliated businesses. AIGFP has already reduced the size of certain portions of its portfolio, including effecting a substantial reduction in credit derivative transactions in respect of multi-sector CDOs (see Termination of $62 billion of CDS below), a sale of its commodity index business, termination of its activities as a foreign exchange prime broker, sale and other disposition of the large majority of its energy/infrastructure investment portfolio. Due to the long-term duration of many of AIGFP's derivative contracts and to the complexity of AIGFP's portfolio, AIG expects that an orderly wind-down will take a substantial period of time. The cost of executing the wind-down will depend on many factors, many of which are not within AIGFP's control, including market conditions, AIGFP's access to markets via market counterparties, the availability of liquidity and the potential implications of further rating downgrades.

AIGCFG experienced significant deposit withdrawals in Hong Kong during September 2008. The inability of AIGCFG to access its traditional sources of funding resulted in AIG lending $1.6 billion to subsidiaries of AIGCFG in September and October of 2008. Additional funding during the remainder of the fourth quarter of 2008 was not material. AIG has entered into contracts to sell certain finance operations in Taiwan, Thailand and the Philippines.

Asset Management

Distressed global markets have reduced the value of assets under management, translating to lower base management fees and reduced carried interest revenues. Tight credit markets have put pressure on the commercial and residential real estate markets, which has caused values in certain geographic locations to fall, resulting in impairment charges on real estate held for investment purposes.

Liquidity issues at AIG parent and lower asset performance as a result of challenging market conditions have contributed to the loss of institutional and retail clients, as well as higher redemptions from some of AIG subsidiaries' managed hedge and mutual funds, have prevented AIG subsidiaries from launching new funds and will continue to adversely affect Asset Management results.

Within the Spread-Based Investment business, distressed markets have resulted in significant loss of invested asset value, and AIG expects such losses to continue through mid 2009. In addition, AIG does not expect to issue any additional debt to fund the Matched Investment Program for the foreseeable future.

As AIG implements the proposed transactions with the NY Fed and United States Department of the Treasury described above and in Note 23 to the Consolidated Financial Statements, AIG expects to incur significant additional restructuring related charges, such as accelerated amortization of the pre-paid commitment asset and, potentially, the write-off of intangible assets. Further, if AIG continues to incur losses in its businesses, AIG may need to write off material amounts of goodwill.

Results of Operations

Consolidated Results

Fourth quarter 2008 net loss

Due to continued severe market deterioration and charges related to ongoing restructuring activities, AIG incurred a substantial net loss of $61.7 billion in the fourth quarter of 2008. This loss resulted primarily from the following:

- net realized capital losses arising from other-than-temporary impairment charges of $18.6 billion ($13.0 billion after tax) reflecting severity losses primarily related to CMBS, other structured securities and securities of financial institutions due to rapid and severe market valuation declines where the impairment period was not deemed temporary; losses related to the change in AIG's intent and ability to hold to recovery certain securities; and issuer-specific credit events, including charges associated with investments in financial institutions;
- net realized capital losses of $2.4 billion ($1.7 billion after tax) related to certain securities lending activities which were deemed to be sales due to reduced levels of collateral provided by counterparties;

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- net realized capital losses of $2.3 billion ($1.6 billion after tax) related to declines in fair values of RMBS for the month of October prior to the sale of these securities to ML II;
- net realized capital losses of $1.7 billion ($1.2 billion after tax) primarily related to foreign exchange transactions and derivatives activity;
- unrealized market valuation losses on AIGFP's super senior credit default swap portfolio totaling $6.9 billion ($4.5 billion after tax); a credit valuation loss of $7.8 billion ($5.1 billion after tax) representing the effect of changes in credit spreads on the valuation of AIGFP's assets and liabilities; and losses primarily from winding down of AIGFP's businesses and portfolios of $1.5 billion ($1.0 billion after tax);
- losses on hedges not qualifying for hedge accounting treatment under FAS 133 of $3.3 billion ($2.2 billion after tax) largely due to the significant decline in U.S. interest rates, resulting in a decrease in the fair value of the derivatives, which primarily economically hedge AIG's debt. To a lesser extent, the strengthening of the U.S. dollar, mainly against the British Pound and Euro decreased the fair value of the foreign currency derivatives economically hedging AIG's non-U.S. dollar denominated debt and foreign exchange transactions;
- interest expense associated with the Fed Facility of $10.6 billion ($6.9 billion after tax), including accelerated amortization of the prepaid commitment fee of $6.6 billion ($4.3 billion after tax);
- goodwill impairment charges of $3.6 billion, principally related to the General Insurance and Domestic Life Insurance and Domestic Retirement Services businesses; and
- the inability to obtain a tax benefit for a significant amount of the losses incurred during the quarter as reflected in the addition to the valuation allowance of $17.6 billion, and other discrete items of $3.4 billion.

AIG's consolidated statements of income (loss) for the years ended December 31, 2008, 2007 and 2006 were as follows:

	Years Ended December 31,			Percentage Increase/ (Decrease)	
	2008	2007	2006	2008 vs. 2007	2007 vs. 2006
	(In millions, except per share data)				
Revenues:					
Premiums and other considerations	**$ 83,505**	$ 79,302	$ 74,213	5%	7%
Net investment income	**12,222**	28,619	26,070	(57)	10
Net realized capital gains (losses)	**(55,484)**	(3,592)	106	—	—
Unrealized market valuation losses on AIGFP super senior credit default swap portfolio	**(28,602)**	(11,472)	—	—	—
Other income (loss)	**(537)**	17,207	12,998	—	32
Total revenues	**11,104**	110,064	113,387	(90)	(3)
Benefits, claims and expenses:					
Policyholder benefits and claims incurred	**63,299**	66,115	60,287	(4)	10
Policy acquisition and other insurance expenses	**27,565**	20,396	19,413	35	5
Interest expense	**17,007**	4,751	3,657	258	30
Restructuring expenses and related asset impairment and other expenses	**758**	—	—	—	—
Other expenses	**11,236**	9,859	8,343	14	18
Total benefits, claims and expenses	**119,865**	101,121	91,700	19	10
Income (loss) before income tax expense (benefit), minority interest and cumulative effect of change in accounting principles	**(108,761)**	8,943	21,687	—	(59)
Income tax expense (benefit):					

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	Years Ended December 31,			Percentage Increase/(Decrease)	
	2008	2007	2006	2008 vs. 2007	2007 vs. 2006
	(In millions, except per share data)				
Current	1,706	3,219	5,489	(47)	(41)
Deferred	(10,080)	(1,764)	1,048	—	—
Total income tax expense (benefit)	(8,374)	1,455	6,537	—	(78)
Income (loss) before minority interest and cumulative effect of change in accounting principles	(100,387)	7,488	15,150	—	(51)
Minority interest	1,098	(1,288)	(1,136)	—	13
Income (loss) before cumulative effect of change in accounting principles	(99,289)	6,200	14,014	—	(56)
Cumulative effect of change in accounting principles, net of tax	—	—	34	—	—
Net income (loss)	$ (99,289)	$ 6,200	$14,048	—%	(56)%

Premiums and Other Considerations

2008 and 2007 Comparison

Premiums and other considerations increased in 2008 compared to 2007 primarily due to:

- growth in Foreign Life Insurance & Retirement Services of $3.3 billion resulting from increased production and favorable foreign exchange rates;
- an increase of $1.7 billion in Foreign General Insurance due to growth in commercial and consumer lines driven by new business from both established and new distribution channels, a decrease in the use of reinsurance and favorable foreign exchange rates; and
- growth in Domestic Life Insurance due to an increase in sales of payout annuities sales and growth in life insurance business in force.

These increases were partially offset by a decline in Commercial Insurance premiums of $1.5 billion primarily from lower U.S. workers' compensation premiums attributable to declining rates, lower employment levels and increased competition, as well as a decline in other casualty lines of business.

2007 and 2006 Comparison

Premiums and other considerations increased in 2007 compared to 2006 primarily due to:

- growth in Foreign Life Insurance & Retirement Services of $2.4 billion as a result of increased life insurance production, growing group products business in Europe, improved sales in Thailand and the favorable effect of foreign exchange rates;
- an increase of $1.8 billion in Foreign General Insurance primarily due to growth in new business from both established and new distribution channels, including Central Insurance Co. Ltd. Taiwan acquired in late 2006; and
- growth in Domestic Life Insurance primarily due an increase in life insurance business in force and payout annuity premiums.

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Net Investment Income

The components of consolidated net investment income were as follows:

	Years Ended December 31, 2008	2007	2006	Percentage Increase/(Decrease) 2008 vs. 2007	2007 vs. 2006
	(In millions)				
Fixed maturities, including short-term investments	**$20,839**	$21,445	$19,773	(3)%	8%
Equity securities	**592**	575	277	3	108
Interest on mortgage and other loans	**1,516**	1,423	1,253	7	14
Partnerships	**(2,022)**	1,986	1,596	—	24
Mutual funds	**(989)**	535	948	—	(44)
Trading account losses	**(725)**	(150)	—	—	—
Other investments*	**1,002**	959	1,241	4	(23)
Total investment income before policyholder income and trading gains (losses)	**20,213**	26,773	25,088	(25)	7
Policyholder investment income and trading gains (losses)	**(6,984)**	2,903	2,016	—	44
Total investment income	**13,229**	29,676	27,104	(55)	9
Investment expenses	**1,007**	1,057	1,034	(5)	2
Net investment income	**$12,222**	$28,619	$26,070	(57)%	10%

* *Includes net investment income from securities lending activities, representing interest earned on securities lending invested collateral offset by interest expense on securities lending payable.*

2008 and 2007 Comparison

Net investment income decreased in 2008 compared to 2007 due to:

- losses from partnership and mutual fund investments reflecting significantly weaker market conditions in 2008 than in 2007;
- significant policyholder investment income and trading losses for Life Insurance & Retirement Services (together, policyholder trading losses), which were $7.0 billion in 2008 compared to policyholder trading gains of $2.9 billion for 2007, reflecting equity market declines. Policyholder trading gains (losses) are offset by a change in incurred policy losses and benefits expense. Policyholder trading gains (losses) generally reflect the trends in equity markets, principally in Japan and Asia;
- losses related to AIG's economic interest in ML II and investment in ML III of approximately $1.1 billion in 2008; and
- the effect of increased levels of short-term investments, for liquidity purposes.

2007 and 2006 Comparison

Net investment income increased in 2007 compared to 2006 due to higher levels of interest income on fixed maturity securities, an increase in income from partnerships as well as higher policyholder trading gains. Partially offsetting these increases were trading account losses related to certain investment-oriented products in the U.K. for Life Insurance & Retirement Services. The policyholder trading gains for 2007 generally reflected the trends in equity markets, principally in Japan and Asia.

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Net Realized Capital Gains (Losses)	Years Ended December 31, 2008	2007	2006
	(In millions)		
Sales of fixed maturity securities	$ (5,266)	$ (468)	$(382)
Sales of equity securities	(119)	1,087	813
Sales of real estate and other assets	1,239	619	303
Other-than-temporary impairments:			
Severity*	(29,146)	(1,557)	—
Lack of intent to hold to recovery	(12,110)	(1,054)	(636)
Trading at 25 percent or more discount for nine consecutive months	—	—	—
Foreign currency declines	(1,903)	(500)	—
Issuer-specific credit events	(5,985)	(515)	(262)
Adverse projected cash flows on structured securities	(1,661)	(446)	(46)
Foreign exchange transactions	3,123	(643)	(382)
Derivative instruments	(3,656)	(115)	698
Total	$(55,484)	$(3,592)	$ 106

* *In 2007, includes $643 million related to AIGFP reported in other income.*

2008 and 2007 Comparison

Net realized capital losses increased $51.9 billion in 2008 compared to 2007 primarily due to an increase in other-than-temporary impairment charges of $46.7 billion. The increase in other-than-temporary impairment charges included the following significant items:

- an increase in severity losses primarily related to certain RMBS, other structured securities and securities of financial institutions due to rapid and severe market valuation declines where the impairment period was not deemed temporary;
- losses related to the change in AIG's intent and ability to hold to recovery certain securities, primarily those held as collateral in the securities lending program;
- issuer-specific credit events, including charges associated with investments in financial institutions; and
- adverse projected cash flows on certain structured securities impaired under Emerging Issues Task Force Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transferor in Securitized Financial Assets" (EITF 99 -20) and related interpretive guidance.

These other-than-temporary impairment charges were partially offset by the favorable effect of foreign exchange transactions due to strengthening of the U.S. dollar. See Investments — Portfolio Review — Other-Than-Temporary Impairments.

During the fourth quarter of 2008, in connection with certain securities lending transactions, AIG met the requirements of sale accounting under FAS 140 because collateral received was insufficient to fund substantially all of the cost of purchasing replacement assets for the securities lent to various counterparties. Accordingly, AIG recognized a loss of $2.4 billion on deemed sales of these securities. Also, net realized capital losses in 2008 included a loss of $2.3 billion, incurred in the fourth quarter of 2008, on RMBS prior to their purchase by ML II. See Investments — Securities Lending Activities and Note 5 to the Consolidated Financial Statements.

2007 and 2006 Comparison

AIG recorded net realized capital losses in 2007 compared to net realized capital gains in 2006 primarily due to an increase in other-than-temporary impairment charges. Other-than-temporary impairment charges included an

increase in severity losses primarily related to certain RMBS and other structured securities, resulting from the disruption in the U.S. residential mortgage and credit markets.

Unrealized Market Valuation Losses on AIGFP Super Senior Credit Default Swap Portfolio

The unrealized market valuation losses on AIGFP's super senior credit default swap portfolio increased in 2008 compared to 2007 due to significant widening in credit spreads and the downgrades of RMBS and CDO securities by rating agencies in 2008 driven by the credit concerns resulting from U.S. residential mortgages and the severe liquidity crisis affecting the markets. In connection with the termination of $62.1 billion net notional amount of CDS transactions related to multi-sector CDOs purchased in the ML III transaction, AIG Financial Products Corp. paid $32.5 billion through the surrender of collateral previously posted (net of $2.5 billion received pursuant to the shortfall agreement), of which $2.5 billion (included in Other income (loss)) is related to certain 2a-7 Put transactions written on multi-sector CDOs purchased by ML III. These losses did not affect income, as unrealized market valuation losses were already recorded in income. See Capital Markets Results and Critical Accounting Estimates — Valuation of Level 3 Assets and Liabilities and Note 5 to the Consolidated Financial Statements.

Other Income (loss)

2008 and 2007 Comparison

Other Income (loss) decreased in 2008 compared to 2007 primarily due to increased losses in Capital Markets of $13.7 billion, which includes a credit valuation adjustment of $9.1 billion on AIGFP's assets and liabilities which are measured at fair value. Asset Management other income decreased by $2.4 billion primarily as a result of lower partnership income related to the Spread-Based Investment Business reflecting weaker market conditions in 2008 and a decline in Institutional Asset Management revenues reflecting lower carried interest and losses on sales of real estate investments. These decreases were partially offset by increased rental revenues for ILFC, driven by a larger aircraft fleet and higher lease rates.

2007 and 2006 Comparison

Other Income increased in 2007 compared to 2006 primarily due to a $2 billion positive effect for AIGFP related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, increased Asset Management revenues primarily resulting from higher partnership income and carried interest as well as increased rental revenues for ILFC, driven by a larger aircraft fleet and higher lease rates.

Policyholder Benefits and Claims Incurred

2008 and 2007 Comparison

Policyholder benefits and claims incurred decreased in 2008 compared to 2007 due to a reduction in incurred policy losses and benefits expense for Life Insurance & Retirement Services of $7.0 billion in 2008 compared to an increase of $2.9 billion in 2007 related to policyholder trading gains (losses) as discussed above in net investment income. These losses more than offset increased claims and claims adjustment expenses of $5.6 billion in AIG's General Insurance operations, which reflected increased catastrophe losses of $1.5 billion principally from hurricanes Ike and Gustav and a $1.8 billion increase in Mortgage Guaranty claims incurred, reflecting the continued deterioration of the U.S. housing market.

2007 and 2006 Comparison

Policyholder benefits and claims incurred increased in 2007 compared to 2006 primarily due to increases in policyholder benefits and claims incurred of $3.2 billion in Life Insurance & Retirement Services due to losses and benefits arising from policyholder trading losses of $886 million discussed above in Net Investment Income, a $1.1 billion increase in Foreign General Insurance resulting from the June 2007 U.K. floods, an increase in severe but non-catastrophic losses and higher frequency of non-severe losses, and a $1.1 billion increase in Mortgage Guaranty claims incurred resulting from the deterioration of the U.S. housing market.

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Policy Acquisition and Other Insurance Expenses

2008 and 2007 Comparison

Policy acquisition and other insurance expenses increased in 2008 compared to 2007 primarily due to a $3.6 billion increase in General Insurance expenses and a $3.7 billion increase in Life Insurance & Retirement Services expenses. General Insurance expenses increased primarily due to goodwill impairment charges of $2.0 billion, including $1.2 billion from Commercial Insurance and $696 million from Personal Lines, respectively, primarily related to goodwill arising from acquisitions. Life Insurance & Retirement Services expenses increased primarily due to $1.2 billion of goodwill impairment charges related to Domestic Life Insurance and Domestic Retirement Services of $402 million and $817 million, respectively. Life Insurance & Retirement Services expenses also increased as a result of the effect of foreign exchange, growth in the business and the effect of FAS 159 implementation.

2007 and 2006 Comparison

Policy acquisition and other insurance expenses increased in 2007 compared to 2006 primarily due costs associated with realigning certain legal entities through which Foreign General Insurance operates and the increased significance of Foreign General consumer lines business, which have higher acquisition costs. Life Insurance & Retirement Services expenses increased principally as a result of the effect of growth in the Foreign Life Insurance & Retirement Services business, increased DAC amortization related to the adoption of SOP 05-1, higher operating expenses related to remediation activities and the effect of foreign exchange.

Interest Expense

2008 and 2007 Comparison

Interest expense increased in 2008 compared to 2007 on higher levels of borrowings. Interest expense in 2008 included $11.4 billion of interest expense on the Fed Facility which was comprised of $9.3 billion of amortization of the prepaid commitment fee asset associated with the Fed Facility, including accelerated amortization of the prepaid commitment asset of $6.6 billion in connection with the restructuring of the Fed Facility and $1.9 billion of accrued compounding interest. Interest expense in 2008 also included interest on the debt and Equity Units from the dates of issuance in May 2008. The above amounts are reflected in the Other category in AIG's segment results.

2007 and 2006 Comparison

Interest expense increased in 2007 compared to 2006 reflecting higher levels of borrowings, including interest on the junior subordinated debt issued in March and June 2007, borrowings used to fund the MIP and borrowings used for general corporate purposes.

Restructuring expenses and related asset impairment and other expenses

As described in Note 1 to the Consolidated Financial Statements, AIG commenced an organization-wide restructuring plan under which some of its businesses will be divested, some will be held for later divestiture, and some businesses will be prepared for potential subsequent offerings to the public. In connection with activities under this plan, AIG recorded restructuring and separation expenses of $758 million in 2008, consisting of severance expenses of $89 million, contract termination expenses of $27 million, asset write-downs of $51 million, other exit expenses of $140 million and separation expenses of $451 million.

Other exit expenses primarily include consulting and other professional fees related to (i) asset disposition activities, (ii) AIG's debt and capital restructuring program with the NY Fed and the United States Department of the Treasury and (iii) unwinding of AIGFP's businesses and portfolios.

Severance and separation expenses described above include retention awards of $492 million to key employees to maintain ongoing business operations and facilitate the successful execution of the restructuring and asset disposition plan. This amount also includes retention awards to AIGFP's employees under its retention program, which was established in the first quarter of 2008 due to the declining market environment, to manage and

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unwind its complex businesses. The total amount expected to be incurred related to these retention programs is approximately $1.0 billion.

For the year ended December 31, 2008, $139 million, $68 million, $287 million and $69 million of the restructuring and separation expenses have been recorded within the General Insurance, Life Insurance & Retirement Services, Financial Services and Asset Management segments, respectively, while $195 million has been recorded in Other operations.

Total restructuring and separation expenses could have a material affect on future results of operations and cash flows.

Other Expenses

2008 and 2007 Comparison

Other Expenses increased in 2008 compared to 2007 primarily due to goodwill impairment charges of $791 million in 2008 in the Financial Services segment related to the Consumer Finance and Capital Markets businesses, which resulted from the downturn in the housing markets, the credit crisis and the intent to unwind AIGFP's businesses and portfolios. In addition, other expenses in 2008 increased compared to 2007 due to higher AGF provisions for finance receivable losses of $674 million in response to the higher levels of delinquencies in AGF's finance receivable portfolio.

2007 and 2006 Comparison

Other Expenses increased in 2007 compared to 2006 primarily due to increases in MIP and compensation related expenses in Asset Management, increases in depreciation expense on flight equipment in line with the increase in the size of the aircraft fleet and an increase in AGF's provision for finance receivable losses of $206 million.

Income tax expense (benefit)

2008 and 2007 Comparison

The effective tax rate on the pre-tax loss for 2008 was 7.7 percent. The effective tax rate was lower than the statutory rate of 35 percent due primarily to $26.1 billion of deferred tax expense recorded during 2008, comprising $5.5 billion of deferred tax expense attributable to the potential sale of foreign businesses and a $20.6 billion valuation allowance to reduce its deferred tax asset to an amount that AIG believes is more likely than not to be realized.

Realization of the deferred tax asset depends on AIG's ability to generate sufficient taxable income of the appropriate character within the carryforward periods of the jurisdictions in which the net operating losses and deductible temporary differences were incurred. AIG assessed its ability to realize its deferred tax asset of $31.9 billion and concluded a $20.6 billion valuation allowance was required to reduce the deferred tax asset to an amount AIG believes is more likely than not that to be realized. See Note 20 to Consolidated Financial Statements for additional discussion regarding deferred tax asset realization.

2007 and 2006 Comparison

The effective tax rate declined from 30.1 percent in 2006 to 16.3 percent in 2007, primarily due to the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio and other-than-temporary impairment charges. These losses, which are taxed at a U.S. tax rate of 35 percent and are included in the calculation of income tax expense, reduced AIG's overall effective tax rate. In addition, other tax benefits, including tax exempt interest and effects of foreign operations were proportionately larger in 2007 than in 2006 due to the decline in pre-tax income in 2007. Furthermore, tax deductions taken in 2007 for SICO compensation plans for which the expense had been recognized in prior years also reduced the effective tax rate in 2007.

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Segment Results

The following table summarizes the operations of each operating segment. See also Note 3 to the Consolidated Financial Statements.

	Years Ended December 31,			Percentage Increase/(Decrease)	
	2008	2007	2006	2008 vs. 2007	2007 vs. 2006
		(In millions)			
Total Revenues:					
General Insurance	$ 44,676	$ 51,708	$ 49,206	(14)%	5%
Life Insurance & Retirement Services	3,054	53,570	50,878	(94)	5
Financial Services	(31,095)	(1,309)	7,777	—	—
Asset Management	(4,526)	5,625	4,543	—	24
Other	(81)	457	483	—	(5)
Consolidation and eliminations	(924)	13	500	—	(97)
Total	$ 11,104	$110,064	$113,387	(90)	(3)
Net realized capital gains (losses):					
General Insurance	$ (5,023)	$ (106)	$ 59	—	—
Life Insurance & Retirement Services	(44,347)	(2,398)	88	—	—
Financial Services	(498)	(100)	(133)	—	—
Asset Management	(8,758)	(1,000)	(125)	—	—
Other	3,142	12	217	—	(95)
Total	$ (55,484)	$ (3,592)	$ 106	—	—
Operating Income (loss):					
General Insurance	$ (5,746)	$ 10,526	$ 10,412	—	1
Life Insurance & Retirement Services	(37,446)	8,186	10,121	—	(19)
Financial Services	(40,821)	(9,515)	383	—	—
Asset Management	(9,187)	1,164	1,538	—	(24)
Other	(15,055)	(2,140)	(1,435)	—	—
Consolidation and eliminations	(506)	722	668	—	8
Total	$(108,761)	$ 8,943	$ 21,687	—%	(59)%

General Insurance Operations

AIG's General Insurance subsidiaries are multiple line companies writing substantially all lines of property and casualty insurance and various personal lines both domestically and abroad and constitute the AIG Property Casualty Group (formerly known as Domestic General Insurance) and the Foreign General Insurance Group.

As previously noted, AIG believes it should present and discuss its financial information in a manner most meaningful to its financial statement users. Accordingly, in its General Insurance business, AIG uses certain regulatory measures, where AIG has determined these measurements to be useful and meaningful.

A critical discipline of a successful general insurance business is the objective to produce profit from underwriting activities taking into account costs of capital. AIG views underwriting results to be critical in the overall evaluation of performance.

Statutory underwriting profit is derived by reducing net premiums earned by net losses and loss expenses incurred and net expenses incurred. Statutory accounting generally requires immediate expense recognition and ignores the matching of revenues and expenses as required by GAAP. That is, for statutory purposes, expenses (including acquisition costs) are recognized immediately, not over the same period that the revenues are earned. Thus, statutory expenses exclude changes in DAC.

GAAP provides for the recognition of certain acquisition expenses at the same time revenues are earned, the accounting principle of matching. Therefore, acquisition expenses are deferred and amortized over the period the related net premiums written are earned. DAC is reviewed for recoverability, and such review requires management judgment. The most comparable GAAP measure to statutory underwriting profit is income before income taxes, minority interest and cumulative effect of change in accounting principles. A table reconciling statutory underwriting profit to income before income taxes, minority interest and cumulative effect of change in accounting principles is contained in footnote (b) to the following table. See also Critical Accounting Estimates herein and Notes 1 and 8 to the Consolidated Financial Statements.

AIG, along with most property and casualty insurance companies, uses the loss ratio, the expense ratio and the combined ratio as measures of underwriting performance. The loss ratio is the sum of claims and claims adjustment expenses divided by net premiums earned. The expense ratio is underwriting expenses divided by net premiums earned. These ratios are relative measurements that describe, for every $100 of net premiums earned, the cost of losses and expenses, respectively. A combined ratio of less than 100 percent indicates an underwriting profit and over 100 percent indicates an underwriting loss.

Net premiums written are initially deferred and earned based upon the terms of the underlying policies. The net unearned premium reserve constitutes deferred revenues which are generally earned ratably over the policy period. Thus, the net unearned premium reserve is not fully recognized in income as net premiums earned until the end of the policy period.

The underwriting environment varies from country to country, as does the degree of litigation activity. Regulation, product type and competition have a direct effect on pricing and consequently on profitability as reflected in underwriting profit and general insurance ratios.

General Insurance Results

General Insurance operating income is comprised of statutory underwriting profit (loss), changes in DAC, net investment income and net realized capital gains and losses. Operating income (loss), as well as net premiums written, net premiums earned, net investment income and net realized capital gains (losses) and statutory ratios were as follows:

	Years Ended December 31,			Percentage Increase/(Decrease)	
	2008	2007	2006	2008 vs. 2007	2007 vs. 2006
	(In millions, except ratios)				
Net premiums written:					
AIG Property Casualty Group					
Commercial Insurance	**$21,099**	$24,112	$24,312	(12)%	(1)%
Transatlantic	**4,108**	3,953	3,633	4	9
Personal Lines	**4,514**	4,808	4,654	(6)	3
Mortgage Guaranty	**1,123**	1,143	866	(2)	32
Foreign General Insurance	**14,390**	13,051	11,401	10	14
Total	**$45,234**	$47,067	$44,866	(4)%	5%

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	Years Ended December 31, 2008	2007	2006	Percentage Increase/(Decrease) 2008 vs. 2007	2007 vs. 2006
	(In millions, except ratios)				
Net premiums earned:					
AIG Property Casualty Group					
Commercial Insurance	**$22,351**	$23,849	$23,910	(6)%	—%
Transatlantic	**4,067**	3,903	3,604	4	8
Personal Lines	**4,679**	4,695	4,645	—	1
Mortgage Guaranty	**1,038**	886	740	17	20
Foreign General Insurance	**14,087**	12,349	10,552	14	17
Total	**$46,222**	$45,682	$43,451	1%	5%
Net investment income:					
AIG Property Casualty Group					
Commercial Insurance	**$ 1,969**	$ 3,879	$ 3,411	(49)%	14%
Transatlantic	**440**	470	435	(6)	8
Personal Lines	**223**	231	225	(3)	3
Mortgage Guaranty	**183**	158	140	16	13
Foreign General Insurance	**651**	1,388	1,484	(53)	(6)
Reclassifications and eliminations	**11**	6	1	—	—
Total	**$ 3,477**	$ 6,132	$ 5,696	(43)%	8%
Net realized capital gains (losses)	**$ (5,023)**	$ (106)	$ 59	—%	—%
Operating income (loss) *(a)* :					
AIG Property Casualty Group Commercial Insurance	**$ (3,065)**	$ 7,305	$ 5,845	—%	25%
Transatlantic	**(61)**	661	589	—	12
Personal Lines	**(785)**	67	432	—	(84)
Mortgage Guaranty	**(2,475)**	(637)	328	—	—
Foreign General Insurance	**618**	3,137	3,228	(80)	(3)
Reclassifications and eliminations	**22**	(7)	(10)	—	—
Total	**$ (5,746)**	$10,526	$10,412	—%	1%
Statutory underwriting profit (loss) *(a)(b)* :					
AIG Property Casualty Group Commercial Insurance	**$ (1,465)**	$ 3,404	$ 2,322	—%	47%
Transatlantic	**(80)**	165	129	—	28
Personal Lines	**(944)**	(191)	204	—	—
Mortgage Guaranty	**(2,666)**	(849)	188	—	—
Foreign General Insurance	**1,014**	1,544	1,565	(34)	(1)
Total	**$ (4,141)**	$ 4,073	$ 4,408	—%	(8)%
AIG Property Casualty Group *(a)* :					
Loss ratio	**86.3**	71.2	69.6		
Expense ratio	**30.1**	20.6	21.7		
Combined ratio	**116.4**	91.8	91.3		

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	Years Ended December 31, 2008	2007	2006	Percentage Increase/(Decrease) 2008 vs. 2007	2007 vs. 2006
	(In millions, except ratios)				
Foreign General Insurance *(a)* :					
Loss ratio	**55.6**	50.6	48.9		
Expense ratio	**36.9**	35.1	34.3		
Combined ratio	**92.5**	85.7	83.2		
Consolidated *(a)* :					
Loss ratio	**76.9**	65.6	64.6		
Expense ratio	**32.2**	24.5	24.7		
Combined ratio	**109.1**	90.1	89.3		

(a) Catastrophe-related losses in 2008 and 2007 by reporting unit were as follows. There were no significant catastrophe-related losses in 2006.

	2008 Insurance Related Losses	2008 Net Reinstatement Premium Cost	2007 Insurance Related Losses	2007 Net Reinstatement Premium Cost
	(In millions)			
Reporting Unit:				
Commercial Insurance	**$ 1,408**	**$ 5**	$ 113	$ (13)
Transatlantic	**191**	**(14)**	11	(1)
Personal Lines	**105**	**2**	61	14
Foreign General Insurance	**128**	**15**	90	1
Total	**$ 1,832**	**$ 8**	$ 275	$ 1

(b) Statutory underwriting profit (loss) is a measure that U.S. domiciled insurance companies are required to report to their regulatory authorities. The following table reconciles statutory underwriting profit (loss) to operating income (loss) for General Insurance for the years ended December 31, 2008, 2007 and 2006:

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Years Ended December 31,	Commercial Insurance	Transatlantic	Personal Lines	Mortgage Guaranty	Foreign General Insurance	Reclassifications and Eliminations	Total
				(In millions)			
2008							
Statutory underwriting profit (loss)	$ (1,465)	$ (80)	$ (944)	$ (2,666)	$ 1,014	$ —	$(4,141)
Increase (decrease) in DAC	(90)	7	(10)	1	33	—	(59)
Net investment income	1,969	440	223	183	651	11	3,477
Net realized capital gains (losses)	(3,479)	(428)	(54)	7	(1,080)	11	(5,023)
Operating income (loss)	$ (3,065)	$ (61)	$ (785)	$ (2,475)	$ 618	$ 22	$(5,746)
2007							
Statutory underwriting profit (loss)	$ 3,404	$ 165	$ (191)	$ (849)	$ 1,544	$ —	$ 4,073
Increase in DAC	97	17	29	57	227	—	427
Net investment income	3,879	470	231	158	1,388	6	6,132
Net realized capital gains (losses)	(75)	9	(2)	(3)	(22)	(13)	(106)
Operating income (loss)	$ 7,305	$ 661	$ 67	$ (637)	$ 3,137	$ (7)	$10,526
2006							
Statutory underwriting profit (loss)	$ 2,322	$ 129	$ 204	$ 188	$ 1,565	$ —	$ 4,408
Increase in DAC	14	14	2	3	216	—	249
Net investment income	3,411	435	225	140	1,484	1	5,696
Net realized capital gains (losses)	98	11	1	(3)	(37)	(11)	59
Operating income (loss)	$ 5,845	$ 589	$ 432	$ 328	$ 3,228	$ (10)	$10,412

AIG transacts business in most major foreign currencies. The following table summarizes the effect of changes in foreign currency exchange rates on the growth of General Insurance net premiums written:

	Years Ended December 31, 2008	2007
Growth in original currency*	(5.5)%	3.5%
Foreign exchange effect	1.6	1.4
Growth as reported in U.S. dollars	(3.9)%	4.9%

* *Computed using a constant exchange rate for each period.*

2008 and 2007 Comparison

General Insurance reported an operating loss in 2008 compared to operating income in 2007 due to declines in underwriting results and net investment income as well as increased net realized capital losses. The combined ratio for 2008 increased to 109.1, an increase of 19.0 points compared to the same period in 2007, primarily due to an increase in the loss ratio of 11.3 points. The loss ratio for accident year 2008 recorded in 2008 was 6.8 points higher than the loss ratio for accident year 2007 recorded in 2007. Catastrophe-related losses were $1.8 billion and $276 million in 2008 and 2007, accounting for 3.4 points of the increase in the accident year loss ratio. Increases in Mortgage Guaranty losses accounted for 2.8 points of the increase in the 2008 accident year loss ratio. The loss ratio also increased for other property and casualty lines due to premium rate decreases and changes in loss trends. Development from prior years increased incurred losses by $155 million in 2008 and decreased incurred losses by $606 million in 2007. The expense ratio increased primarily due to goodwill impairment charges of $2.0 billion in

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2008, principally attributable to goodwill arising from the acquisitions of HSB, 21st Century, and Transatlantic as well as the recognition of a premium deficiency reserve of $222 million in 2008 related to UGC's second-lien business. Also contributing to the operating loss was Personal Lines, primarily resulting from the goodwill impairment charge noted above.

General Insurance net premiums written declined $1.8 billion in 2008 compared to 2007, including a decline in U.S. workers' compensation net premiums of $1.7 billion due to declining rates, lower employment levels and increased competition. Declining rates in other casualty lines within Commercial Insurance and a reduction in Personal Lines net premiums earned were largely offset by growth in Foreign General Insurance from both established and new distribution channels and the positive effect of changes in foreign currency exchange rates.

See Results of Operations — Consolidated Results for further discussion on Net investment income and Realized capital gains (losses).

<u>*2007 and 2006 Comparison*</u>

General Insurance operating income increased in 2007 compared to 2006 due to growth in net investment income, partially offset by a decline in underwriting profit and net realized capital losses. The 2007 combined ratio increased to 90.1, an increase of 0.9 points compared to 2006, primarily due to an increase in the loss ratio of 1.0 points. The loss ratio for accident year 2007 recorded in 2007 was 2.3 points higher than the loss ratio for accident year 2006 recorded in 2006. Increases in Mortgage Guaranty losses accounted for a 2.1 point increase in the 2007 accident year loss ratio. The higher 2007 accident year loss ratio was partially offset by favorable development on prior years, which reduced incurred losses by $606 million and $53 million in 2007 and 2006, respectively. Additional favorable loss development of $50 million (recognized in consolidation and related to certain asbestos settlements) reduced overall incurred losses.

Commercial Insurance Results

<u>*2008 and 2007 Comparison*</u>

Commercial Insurance operating income decreased in 2008 compared to 2007, primarily due to significant declines in underwriting results and net investment income, as well as significantly greater net realized capital losses in 2008. The decline in underwriting results is also reflected in the combined ratio, which increased 21.6 points in 2008 compared to 2007. The loss ratio for accident year 2008 recorded in 2008 included a 6.0 point effect related to catastrophe losses, and was 13.3 points higher than the loss ratio for accident year 2007 recorded in 2007. Prior year development and increases in the loss reserve discount reduced incurred losses by $169 million and $555 million in 2008 and 2007, respectively, accounting for an additional 1.6 point increase in the combined ratio.

Commercial Insurance net premiums written declined in 2008 compared to 2007 primarily due to declines in premiums from workers' compensation and other casualty lines. Declines in other casualty lines were due to declining rates and reduced activity in the construction and transportation industries. Management and Professional liability lines declined due to increased competition, particularly in the fourth quarter of 2008.

Commercial Insurance expense ratio increased to 26.8 in 2008 compared to 18.4 in 2007. The most significant driver of the increase was goodwill impairment charges principally attributable to goodwill arising from the acquisition of HSB, representing 5.4 points of the increase in the expense ratio. Additionally, the provision for uncollectible premiums and other provisions increased approximately $178 million due to economic conditions, compared to a reduction of $18 million of expenses in 2007 as provisions established in 2006 were released, accounting for 0.9 points of the increase in the expense ratio. The remaining increase is due to the decline in net premiums earned and mix of business. While AIG is aggressively pursuing expense reductions, the impact of expense savings will lag the decline in net written premiums.

<u>*2007 and 2006 Comparison*</u>

Commercial Insurance operating income increased in 2007 compared to 2006 primarily due to growth in both net investment income and underwriting profit. The improvement is also reflected in the combined ratio, which declined 4.9 points in 2007 compared to 2006, primarily due to an improvement in the loss ratio of 3.3 points. Catastrophe-related losses increased the 2007 loss ratio by 0.4 points. The loss ratio for accident year 2007 recorded

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in 2007 was 0.9 points lower than the loss ratio recorded in 2006 for accident year 2006. The loss ratio for accident year 2006 has improved in each quarter since September 30, 2006. As a result, the 2007 accident year loss ratio is 2.8 points higher than the 2006 accident year loss ratio, reflecting reductions in 2006 accident year losses recorded through December 31, 2007. Prior year development reduced incurred losses by $390 million in 2007 and increased incurred losses by $175 million in 2006, accounting for 2.4 points of the improvement in the loss ratio.

Commercial Insurance expense ratio decreased to 18.4 in 2007 compared to 20.1 in 2006, primarily due to the 2006 charge related to the remediation of the material weakness in internal control over certain balance sheet reconciliations that accounted for 2.1 points of the decline. The decline was partially offset by increases in operating expenses for marketing initiatives and operations.

Mortgage Guaranty Results

2008 and 2007 Comparison

Mortgage Guaranty operating loss increased in 2008 compared to 2007 due to declining housing values, increasing mortgage foreclosures and the recognition of a premium deficiency reserve on the second-lien business. The domestic first-lien operating loss increased by $1.0 billion in 2008 to $1.1 billion compared to 2007 while the second-lien operating loss of $1.2 billion in 2008, which includes the recognition of a $222 million premium deficiency reserve, increased $656 million compared to 2007.

During 2008, UGC tightened underwriting standards and increased premium rates for its first-lien business and ceased insuring second-lien business as of September 30, 2008. During the fourth quarter of 2008, UGC ceased insuring new private student loan business and suspended insuring new business throughout its European operations. All of these actions were in response to the deteriorating market conditions and resulted in a significant decline in new business written during the second half of 2008.

Net premiums written declined in 2008 compared to 2007. First- and second-lien business net premiums written grew moderately, primarily due to increased persistency year over year. However, new insurance written, which is a measure of the amount of new insurance added to the portfolio, decreased 45 percent, 82 percent and 42 percent for first- and second-lien business and international business, respectively, during 2008 compared to 2007. These declines are primarily due to UGC's tightening of underwriting guidelines and rate increases during the year and the actions described above.

Claims and claims adjustment expenses increased $1.8 billion compared to 2007 primarily due to the continuing decline in the domestic housing market. Domestic first-lien losses incurred of $1.8 billion increased 159 percent compared to the same period in 2007 resulting in a 2008 first-lien loss ratio of 276 compared to a 2007 loss ratio of 122. Second-lien losses incurred of $1.2 billion increased 61 percent compared to the same period in 2007. UGC strengthened international loss reserves by $96 million during the fourth quarter of 2008. Increases in both domestic and international losses incurred resulted in an overall loss ratio for Mortgage Guaranty (excluding the second-lien business in run-off) of 257 in 2008 compared to 111 in 2007. UGC's ability to cede losses to captive insurers will be reduced in future periods primarily due to captive reinsurers exceeding the limits of the reinsurance agreements.

Historically, Mortgage Guaranty included all mortgage insurance risks in a single premium deficiency test because the manner of acquiring, servicing and measuring the profitability of all Mortgage Guaranty contracts was consistent. Due to the run-off in the second-lien business, management no longer measures the profitability for the second-lien business in the same manner as that for Mortgage Guaranty's ongoing businesses, and will no longer report loss ratio or expense ratio information for the second-lien business. As a result, UGC performs a separate premium deficiency calculation for the second-lien business.

At December 31, 2008, the present value of expected second-lien future losses and expenses (net of expected future recoveries) was $1.4 billion, and was offset by the present value of expected second-lien future premiums of $499 million and the already established liability for unpaid claims and claims adjustment expense of $701 million, resulting in a premium deficiency reserve of $222 million. The second-lien risk in force at December 31, 2008 totaled $2.9 billion with 530 thousand second-lien policies in force compared to $3.8 billion of risk in force and 644 thousand policies in force at December 31, 2007. The second-lien business is expected to run-off over the next 10 to 12 years. Risk in force represents the full amount of second-lien loans insured reduced for contractual

aggregate loss limits on certain pools of loans, usually 10 percent of the full amount of loans insured in each pool. Mortgage Guaranty may record net losses on this business in future periods because the timing of future delinquencies may precede recognition of future premiums in an amount in excess of the premium deficiency reserve.

UGC's domestic mortgage risk in force totaled $30.1 billion as of December 31, 2008 and the 60-day delinquency ratio was 7.5 percent (based on number of policies, consistent with mortgage industry practice) compared to domestic mortgage risk in force of $29.8 billion and a delinquency ratio of 3.7 percent at December 31, 2007. Approximately 84 percent of the domestic mortgage risk is secured by first-lien, owner-occupied properties.

2007 and 2006 Comparison

Mortgage Guaranty incurred an operating loss in 2007 compared to operating income in 2006 as the deteriorating U.S. residential housing market adversely affected losses incurred for both the domestic first- and second-lien businesses. Domestic first- and second-lien losses incurred increased 362 percent and 346 percent respectively, compared to 2006, resulting in loss ratios of 122.0 and 357.0, respectively, in 2007. Increases in domestic losses incurred resulted in an overall loss ratio of 168.6 in 2007 compared to 47.2 in 2006. Prior year development reduced incurred losses in 2007 by $25 million compared to a reduction of $115 million in 2006, which accounted for 10.2 points of the increase in the loss ratio.

Net premiums written increased in 2007 compared to 2006 primarily due to growth in the international markets, accounting for 58 percent of the increase in net premiums written. In addition, the increased use of mortgage insurance for credit enhancement as well as better persistency resulted in an increase in domestic first-lien premiums.

The expense ratio in 2007 was 21.2, down from 23.4 in 2006 as premium growth offset the effect of increased expenses related to UGC's international expansion and the employment of additional operational resources in the second-lien business.

Foreign General Insurance Results

2008 and 2007 Comparison

Foreign General Insurance operating income decreased in 2008 compared to 2007 due to a decrease in statutory underwriting profit and change in DAC of $724 million, an increase in net realized capital losses reflecting other-than-temporary-impairment charges related to the deterioration in the fixed income markets (see — Results of Operations — Consolidated Results-Net Realized Gains (losses) for further discussion), and a decrease in net investment income reflecting lower mutual fund and partnership income related to poor performance in the equity markets (see Results of Operations — Consolidated Results — Net Investment Income for further discussion).

Net premiums written increased 10 percent (5 percent in original currency) in 2008 compared to 2007 due to growth in commercial and consumer lines driven by new business from established and new distribution channels, including the late 2007 acquisition of Württembergische und Badische Versicherungs — AG (WüBa) in Germany. New business in the commercial lines in the U.K. and Europe and decreases in the use of reinsurance increased net premiums earned, but were partially offset by declines in premium rates. Growth in personal accident business in Latin America, South East Asia and Europe also contributed to the increase, however, premiums from the Lloyd's Syndicate Ascot continued to decline.

The loss ratio in 2008 increased 5.1 points compared to 2007 due to:

- The loss ratio for accident year 2008 recorded in 2008 was 3.2 points higher than the loss ratio recorded in 2007 for accident year 2007 primarily due to continued rate erosion and increased lower level claims frequency.
- Loss development on prior accident years increased the loss ratio by 1.9 points.

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2007 and 2006 Comparison

Foreign General Insurance operating income decreased in 2007 compared to 2006, due primarily to decreases in net investment income and statutory underwriting profit. Net investment income in 2006 included income of $424 million from unit investment trusts (UCITS) adjustments. Underwriting profit decreased due to losses from the June 2007 U.K. floods, an increase in severe but non-catastrophic losses and higher frequency of non-severe losses compared to 2006, partially offset by higher favorable loss development on prior accident years.

Net premiums written increased 14 percent (10 percent in original currency) in 2007 compared to 2006, reflecting growth in commercial and consumer lines driven by new business from both established and new distribution channels, including Central Insurance Co. Ltd. in Taiwan acquired in late 2006. Net premiums written for commercial lines increased due to new business in the U.K. and Europe and decreases in the use of reinsurance, partially offset by declines in premium rates. Growth in consumer lines in Latin America, Asia and Europe also contributed to the increase. Net premiums written for the Lloyd's syndicate Ascot (Ascot) and Aviation declined due to rate decreases and increased market competition.

The 2007 loss ratio increased a total of 1.7 points compared to 2006. Losses of $90 million from the June 2007 U.K. floods added 0.7 points to the loss ratio and higher severe but non-catastrophic losses and higher loss frequency for personal accident business in Japan and personal lines business in Asia and Latin America added 1.6 points to the loss ratio. Partially offsetting these increases was favorable loss development on prior accident years of $286 million in 2007 compared to $183 million in 2006, which decreased the loss ratio by 0.6 points.

The 2007 expense ratio increased 1.3 points compared to 2006. This increase reflected the cost of realigning certain legal entities through which Foreign General Insurance operates and the increased significance of consumer lines of business, which have higher acquisition costs. These factors contributed 0.7 points to the 2007 expense ratio.

Liability for unpaid claims and claims adjustment expense

The following table presents the components of the General Insurance gross liability for unpaid claims and claims adjustment expense (loss reserves) by major lines of business on a statutory annual statement basis:*

	At December 31,	
	2008	2007
	(In millions)	
Other liability occurrence	**$19,773**	$20,580
Workers' compensation	**15,170**	15,568
Other liability claims made	**13,189**	13,878
International	**11,786**	7,036
Auto liability	**5,593**	6,068
Property	**5,201**	4,274
Mortgage guaranty/credit	**3,137**	1,426
Reinsurance	**3,102**	3,127
Products liability	**2,400**	2,416
Medical malpractice	**2,210**	2,361
Aircraft	**1,693**	1,623
Accident and health	**1,451**	1,818
Commercial multiple peril	**1,163**	1,900
Fidelity/surety	**1,028**	1,222
Other	**2,362**	2,203
Total	**$89,258**	$85,500

* *Presented by lines of business pursuant to statutory reporting requirements as prescribed by the National Association of Insurance Commissioners.*

Reserves for non-U.S. domiciled companies are carried in the International line of business. As a result of restructuring of certain foreign operations in 2008, reserves for the International line of business included amounts formerly reported in other lines of business.

AIG's gross liability for unpaid claims and claims adjustment expense represents the accumulation of estimates of ultimate losses, including estimates for incurred but not yet reported reserves (IBNR) and loss expenses. The methods used to determine loss reserve estimates and to establish the resulting reserves are continually reviewed and updated. Any adjustments resulting therefrom are currently reflected in operating income. Because loss reserve estimates are subject to the outcome of future events, changes in estimates are unavoidable given that loss trends vary and time is often required for changes in trends to be recognized and confirmed. Reserve changes that increase previous estimates of ultimate cost are referred to as unfavorable or adverse development or reserve strengthening. Reserve changes that decrease previous estimates of ultimate cost are referred to as favorable development.

Estimates for mortgage guaranty insurance losses and loss adjustment expense reserves are based on notices of mortgage loan delinquencies and estimates of delinquencies that have been incurred but have not been reported by loan servicers, based upon historical reporting trends. Mortgage Guaranty establishes reserves using a percentage of the contractual liability (for each delinquent loan reported) that is based upon past experience regarding certain loan factors such as age of the delinquency, cure rates, dollar amount of the loan and type of mortgage loan. Because mortgage delinquencies and claims payments are affected primarily by macroeconomic events, such as changes in home price appreciation or depreciation, interest rates and unemployment, the determination of the ultimate loss cost requires a high degree of judgment. AIG believes it has provided appropriate reserves for currently delinquent loans. Consistent with industry practice, AIG does not establish a reserve for insured loans that are not currently delinquent, but that may become delinquent in future periods.

At December 31, 2008, General Insurance net loss reserves increased $3.17 billion from 2007 to $72.46 billion. The net loss reserves represent loss reserves reduced by reinsurance recoverable, net of an allowance for unrecoverable reinsurance and applicable discount for future investment income.

The following table classifies the components of the General Insurance net liability for unpaid claims and claims adjustment expense by business unit:

	At December 31,	
	2008	2007
	(In millions)	
Commercial Insurance	**$48,789**	$47,392
Transatlantic	**7,349**	6,900
Personal Lines	**2,460**	2,417
Mortgage Guaranty	**3,004**	1,339
Foreign General Insurance	**10,853**	11,240
Total net loss reserves	**$72,455**	$69,288

Discounting of Reserves

At December 31, 2008, AIG's overall General Insurance net loss reserves reflect a loss reserve discount of $2.57 billion, including tabular and non-tabular calculations. The tabular workers' compensation discount is calculated using a 3.5 percent interest rate and the 1979-81 Decennial Mortality Table. The non-tabular workers' compensation discount is calculated separately for companies domiciled in New York and Pennsylvania, and follows the statutory regulations for each state. For New York companies, the discount is based on a five percent interest rate and the companies' own payout patterns. For Pennsylvania companies, the statute has specified discount factors for accident years 2001 and prior, which are based on a six percent interest rate and an industry payout pattern. For accident years 2002 and subsequent, the discount is based on the payout patterns and investment yields of the companies. Certain other liability occurrence and products liability occurrence business in AIRCO that was written by Commercial Insurance is discounted based on the yield of United States Department of the Treasury securities ranging from one to twenty years and the Commercial Insurance payout pattern for this business. The discount is comprised of the following: $733 million — tabular discount for workers' compensation in Commercial

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Insurance; $1.67 billion — non-tabular discount for workers' compensation in Commercial Insurance; and, $170 million — non-tabular discount for other liability occurrence and products liability occurrence in AIRCO for Commercial Insurance business. Since 1998 AIRCO has assumed on a quota share basis certain general liability and products liability business written by Commercial Insurance, and the reserves for this business are carried on a discounted basis by AIRCO.

Results of the Reserving Process

AIG believes that the General Insurance net loss reserves are adequate to cover General Insurance net losses and loss expenses as of December 31, 2008. While AIG regularly reviews the adequacy of established loss reserves, there can be no assurance that AIG's ultimate loss reserves will not develop adversely and materially exceed AIG's loss reserves as of December 31, 2008. In the opinion of management, such adverse development and resulting increase in reserves is not likely to have a material adverse effect on AIG's consolidated financial condition, although it could have a material adverse effect on AIG's consolidated results of operations for an individual reporting period. See Item 1A. Risk Factors — Casualty Insurance and Underwriting Reserves.

The following table presents the reconciliation of net loss reserves:

	At December 31,		
	2008	2007	2006
		(In millions)	
Net liability for unpaid claims and claims adjustment expense at beginning of year	**$69,288**	$62,630	$57,476
Foreign exchange effect	**(2,113)**	955	741
Acquisitions and dispositions *(a)*	**(269)**	317	55
Losses and loss expenses incurred:			
Current year	**35,085**	30,261	27,805
Prior years, other than accretion of discount *(b)*	**118**	(656)	(53)
Prior years, accretion of discount	**317**	327	300
Losses and loss expenses incurred	**35,520**	29,932	28,052
Losses and loss expenses paid:			
Current year	**13,440**	9,684	8,368
Prior years	**16,531**	14,862	15,326
Losses and loss expenses paid	**29,971**	24,546	23,694
Net liability for unpaid claims and claims adjustment expense at end of year	**$72,455**	$69,288	$62,630

(a) *Reflects the closing balance with respect to Unibanco divested in the fourth quarter of 2008 and the opening balance with respect to the acquisitions of WüBa and the Central Insurance Co., Ltd. in 2007 and 2006, respectively.*

(b) *Includes $88 million and $181 million in 2007 and 2006, respectively, for the general reinsurance operations of Transatlantic and, $7 million, $64 million and $103 million of losses incurred in 2008, 2007 and 2006, respectively, resulting from 2005 and 2004 catastrophes.*

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American International Group, Inc., and Subsidiaries

The following tables summarize development, (favorable) or unfavorable, of incurred losses and loss expenses for prior years (other than accretion of discount):

	Years Ended December 31,		
	2008	2007 (In millions)	2006
Prior Accident Year Development by Reporting Unit:			
Commercial Insurance	**$ (24)**	$(390)	$ 175
Personal Lines	**65**	7	(111)
Mortgage Guaranty	**177**	(25)	(115)
Foreign General Insurance	**(62)**	(286)	(183)
Subtotal	**156**	(694)	(234)
Transatlantic	**(1)**	88	181
Asbestos settlements*	**(37)**	(50)	—
Prior years, other than accretion of discount	**$118**	$(656)	$ (53)

* *Represents the effect of settlements of certain asbestos liabilities.*

	Years Ended December 31,		
	2008	2007 (In millions)	2006
Prior Accident Year Development by Major Class of Business:			
Excess casualty (Commercial Insurance)	**$1,105**	$ 73	$ 102
D&O and related management liability (Commercial Insurance)	**(430)**	(305)	(20)
Excess workers' compensation (Commercial Insurance)	**(12)**	(14)	74
Healthcare (Commercial insurance)	**(310)**	(194)	(130)
Reinsurance (Transatlantic)	**(1)**	88	181
Asbestos and environmental (primarily Commercial Insurance)	**51**	18	208
All other, net	**(285)**	(322)	(468)
Prior years, other than accretion of discount	**$ 118**	$(656)	$ (53)

	Years Ended December 31, Calendar Year		
	2008	2007 (In millions)	2006
Prior Accident Year Development by Accident Year:			
Accident Year			
2007	**$(370)**		
2006	**(590)**	$(1,248)	
2005	**(455)**	(446)	$(1,576)
2004	**(335)**	(428)	(511)
2003	**200**	37	(212)
2002	**176**	234	373
2001	**238**	263	29
2000	**341**	321	338
1999	**346**	47	382
1998 and prior	**567**	564	1,124
Prior years, other than accretion of discount	**$ 118**	$ (656)	$ (53)

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American International Group, Inc., and Subsidiaries

In determining the loss development from prior accident years, AIG conducts analyses to determine the change in estimated ultimate loss for each accident year for each profit center. For example, if loss emergence for a profit center is different than expected for certain accident years, the actuaries examine the indicated effect such emergence would have on the reserves of that profit center. In some cases, the higher or lower than expected emergence may result in no clear change in the ultimate loss estimate for the accident years in question, and no adjustment would be made to the profit center's reserves for prior accident years. In other cases, the higher or lower than expected emergence may result in a larger change, either favorable or unfavorable, than the difference between the actual and expected loss emergence. Such additional analyses were conducted for each profit center, as appropriate, in 2008 to determine the loss development from prior accident years for 2008. As part of its reserving process, AIG also considers notices of claims received with respect to emerging issues, such as those related to the U.S. mortgage and housing market.

2008 Net Loss Development

In 2008, net loss development from prior accident years was adverse by approximately $118 million, including approximately $339 million of favorable development relating to loss sensitive business in the first three months of 2008 (which was offset by an equal amount of negative earned premium development), and excluding approximately $317 million from accretion of loss reserve discount. Excluding both the favorable development relating to loss sensitive business and accretion of loss reserve discount, net loss development from prior accident years in 2008 was adverse by approximately $457 million. The overall adverse development of $118 million consisted of approximately $1.75 billion of favorable development from accident years 2004 through 2007 offset by approximately $1.87 billion of adverse loss development from accident years 2003 and prior. The adverse development from accident years 2003 and prior was primarily related to excess casualty business within Commercial Insurance; this business accounted for approximately $1.25 billion of the adverse development from accident years 2003 and prior. The favorable development from accident years 2004 through 2007 included approximately $590 million in favorable development from business written by Lexington Insurance Company, including healthcare, catastrophic casualty, casualty and program businesses. Financial Services divisions within Commercial Insurance, including D&O and related management liability business, contributed approximately $430 million to the favorable development from accident years 2004 through 2007, relating primarily to D&O, and related management liability business from accident years 2004 and 2005. The adverse development from accident years 2003 and prior included approximately $200 million related to claims involving MTBE, a gasoline additive, primarily on excess casualty business within Commercial Insurance from accident years 2000 and prior. In addition, the excess casualty adverse development reflect continued emergence of latent claims such as construction defect, product aggregate, and pharmaceutical related exposures, as well as higher than expected large loss activity from these accident years. AIG's exposure to these latent exposures was reduced after 2002 due to significant changes in policy terms and conditions as well as underwriting guidelines. (See Net Loss Development by Class of Business below). Other segments throughout AIG also contributed to the adverse development from accident year 2003 and prior, including approximately $215 million relating to Transatlantic. Mortgage Guaranty contributed approximately $177 million of overall adverse development in 2008, with $159 million relating to accident year 2007. See Year-to-Date Mortgage Guaranty Results — 2008 and 2007 Comparison above.

2007 Net Loss Development

In 2007, net loss development from prior accident years was favorable by approximately $656 million, including approximately $88 million of adverse development from Transatlantic; and excluding approximately $327 million from accretion of loss reserve discount. Excluding Transatlantic, as well as accretion of discount, net loss development in 2007 from prior accident years was favorable by approximately $744 million. The overall favorable development of $656 million consisted of approximately $2.12 billion of favorable development from accident years 2004 through 2006, partially offset by approximately $1.43 billion of adverse development from accident years 2002 and prior and $37 million of adverse development from accident year 2003. In 2007, most classes of AIG's business continued to experience favorable development for accident years 2004 through 2006. The majority of the adverse development from accident years 2002 and prior was related to development from excess casualty and primary workers' compensation business within Commercial Insurance and from Transatlantic. The development from accident year 2003 was primarily related to adverse development from excess casualty and primary workers' compensation business within Commercial Insurance offset by favorable development from most

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other classes of business. The overall favorable development of $656 million included approximately $305 million pertaining to the D&O and related management liability classes of business within Commercial Insurance, consisting of approximately $335 million of favorable development from accident years 2003 through 2006, partially offset by approximately $30 million of adverse development from accident years 2002 and prior. The overall favorable development of $656 million also included approximately $300 million of adverse development from primary workers' compensation business within Commercial Insurance.

2006 Net Loss Development

In 2006, net loss development from prior accident years was favorable by approximately $53 million, including approximately $198 million in net adverse development from asbestos and environmental reserves resulting from the updated ground-up analysis of these exposures in the fourth quarter of 2006; approximately $103 million of adverse development pertaining to the major hurricanes in 2004 and 2005; and $181 million of adverse development from Transatlantic; and excluding approximately $300 million from accretion of loss reserve discount. Excluding the fourth quarter asbestos and environmental reserve increase, catastrophes and Transatlantic, as well as accretion of discount, net loss development in 2006 from prior accident years was favorable by approximately $535 million. The overall favorable development of $53 million consisted of approximately $2.30 billion of favorable development from accident years 2003 through 2005, partially offset by approximately $2.25 billion of adverse development from accident years 2002 and prior. In 2006, most classes of AIG's business continued to experience favorable development for accident years 2003 through 2005. The adverse development from accident years 2002 and prior reflected development from excess casualty, workers' compensation, excess workers' compensation, and post-1986 environmental liability classes of business, all within Commercial Insurance, from asbestos reserves within Commercial Insurance and Foreign General Insurance, and from Transatlantic.

Net Loss Development by Class of Business

The following is a discussion of the primary reasons for the development in 2008, 2007 and 2006 for those classes of business that experienced significant prior accident year developments during the three-year period. See Asbestos and Environmental Reserves below for a further discussion of asbestos and environmental reserves and development.

Excess Casualty: Excess Casualty reserves experienced significant adverse loss development in 2008, following relatively minor adverse development in 2006 and 2007. However, all three years exhibited significant adverse development from accident years 2002 and prior. The increase in loss costs resulted primarily from medical inflation, which increased the economic loss component of tort claims, advances in medical care, which extended the life span of severely injured claimants, and larger jury verdicts, which increased the value of severe tort claims. An additional factor affecting AIG's excess casualty experience in recent years has been the exhaustion of underlying primary policies for products liability coverage and for homebuilders. This has led to increased loss emergence relating to claims involving exhaustion of underlying product aggregates and increased construction defect-related claims activity on AIG's excess and umbrella policies. Many excess casualty policies were written on a multi-year basis in the late 1990s, which limited AIG's ability to respond to emerging market trends as rapidly as would otherwise be the case. In subsequent years, AIG responded to these emerging trends by increasing rates and implementing numerous policy form and coverage changes. This led to a significant improvement in experience beginning with accident year 2001. In 2007 and 2008, a significant portion of the adverse development from accident years 2002 and prior also related to latent exposures, including pharmaceutical exposures as well as the construction defect and product aggregate related exposures noted above. AIG's exposure to these latent exposures was sharply reduced after 2002 due to significant changes in policy terms and conditions as well as underwriting guidelines. Another contributor to the adverse development during 2006 through 2008 is that actual loss development for other large losses for accident years 1998 and subsequent have emerged at higher than expected levels as compared to the loss emergence pattern exhibited from earlier accident years. This has caused significant additional development for accident years 1998 to 2002, and to a lesser extent 2003. In 2008, this phenomenon also caused some adverse development for accident year 2004; however the accident year results for accident years 2003 and 2004 both remain very favorable.

For the year-end 2007 loss reserve review, AIG claims staff updated its review of accounts with significant exposure to construction defect-related claims. AIG's actuaries determined that no significant changes in the

assumptions were required. Prior accident year loss development in 2007 was adverse by approximately $75 million, a minor amount for this class of business. However, AIG continued to experience adverse development in this class for accident years 2002 and prior, amounting to approximately $450 million in 2007. In addition, loss reserves developed adversely for accident year 2003 by approximately $100 million in 2007 for this class. The loss ratio for accident year 2003 remained very favorable for this class and had been relatively stable over the past several years. Favorable development in 2007 for accident years 2004 through 2006 largely offset the adverse development from accident years 2003 and prior. A significant portion of the adverse development from accident years 2002 and prior related to the latent exposures described above.

For the year-end 2006 loss reserve review, AIG claims staff updated the separate review for accounts with significant exposure to construction defect-related claims in order to assist the actuaries in determining the proper reserve for this exposure. AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year loss development in 2006 was adverse by approximately $100 million, a relatively minor amount for this class of business. However, AIG continued to experience adverse development for this class for accident years prior to 2003.

For the year-end 2008 loss reserve review, AIG claims staff again updated its review of accounts with significant exposure to construction defect-related claims. In response to the continued upward developments on these claims, and based on an updated analysis of this development, AIG increased the reserves by an additional $75 million beyond the increases identified in the claims review. In response to the continued adverse development of product aggregate related claims during 2007 and 2008, AIG's actuaries conducted a special analysis of product aggregate-related claims development, resulting in an increase in the IBNR reserve for this exposure of $175 million. In response to the high level of pharmaceutical related claim emergence during 2007 and 2008, AIG claims staff reviewed the remaining exposure, and based on this review an additional reserve of $10 million was established. In response to the much greater than expected actual loss emergence for other large losses for accident years 1998 and subsequent during 2007 and 2008, AIG's actuaries increased the loss development factor assumptions for this business, resulting in a further increase of approximately $200 million in loss reserves for this class. In total, the specific increases in reserves related to these items increased the excess casualty reserves by approximately $460 million during 2008, of which $370 million was recognized in AIG's fourth quarter 2008 results. In the first three months of 2008, AIG also recognized approximately $200 million of losses relating to MTBE, a gasoline additive, which primarily related to excess casualty business from accident years 2000 and prior. While the various adjustments described above were intended to respond appropriately to the recent adverse trends in loss experience, excess casualty remains a highly volatile class of business and there cannot be any assurance that further adjustments to assumptions in the loss reserve process for this class of business will not be necessary.

Loss reserves pertaining to the excess casualty class of business are generally included in the other liability occurrence line of business, with a small portion of the excess casualty reserves included in the other liability claims made line of business, as presented in the table above.

D&O and Related Management Liability Classes of Business: AIG experienced an insignificant amount of favorable development in 2006 for the D&O and related management liability class of business, followed by significant favorable development during 2007 and 2008. The favorable development throughout the three-year period related primarily to accident years 2004 and 2005, and to a lesser extent accident years 2003 and 2006. Loss cost trends for D&O and related management liability classes of business were adverse in accident years 2002 and prior due to a variety of factors, including an increase in frequency and severity of corporate bankruptcies; the increase in the frequency of financial restatements; the sharp rise in market capitalization of publicly traded companies; and the increase in the number of initial public offerings. The 2003 through 2006 period was marked by a significant reduction in claims related to these factors; thus the expected loss ratios initially established for these accident years have developed favorably, particularly for 2004 and 2005. Beginning in accident year 2007, claims relating to the credit crisis have resulted in increased overall claim activity, and accident year 2007 reserves developed adversely by a relatively insignificant amount during 2008. AIG utilizes ground up claims projections by AIG claims staff as a benchmark to select the loss reserves for this business; these projections are updated annually.

For the year-end 2008 loss reserve review, AIG's actuaries took into account the continued favorable loss emergence for accident years 2006 and prior. They determined that, in order to respond to the significant favorable loss emergence during 2007 and 2008, greater weight should be applied to the improving loss experience for

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accident years 2006 and prior. Loss reserve selections therefore gave increased weight to the improved experience and less weight to the ground-up claim projections for these accident years, as the experience has continued to improve relative to the claim benchmark that was originally established for these accident years. For accident year 2007, the claim projections include claims relating to the credit crisis. The recognition of these projections resulted in a significant increase in loss reserves for some D&O subclasses. However this was partially offset by favorable loss development for other subclasses that were significantly less affected by the credit crisis. The overall development for accident year 2007 was thus only a modest increase in loss reserves. The reserves established for accident year 2008 reflect AIG's expectation of increased claim activity relating to the credit crisis. Given the uncertainty of the ultimate development from claims relating to the credit crisis in accident years 2007 and 2008, there is a greater than normal potential variation in the loss ratios for these accident years. The increased responsiveness to the improving loss trends for accident years 2006 and prior resulted in approximately $225 million of favorable loss development in the fourth quarter of 2008 for this business, primarily in accident years 2004 and 2005.

For the year-end 2007 loss reserve review, AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year reserve development in 2007 was favorable by approximately $305 million, due primarily to favorable development from accident years 2004 and 2005, and to a lesser extent 2003 and 2006. AIG's actuaries continued to benchmark the loss reserve indications to the ground-up claim projections provided by AIG claims staff for this class of business. For the year-end 2007 loss reserve review, the ground-up claim projections included all accident years through 2006, and included stock options backdating-related exposures from accident year 2006.

For the year-end 2006 loss reserve review, AIG's actuaries determined that no significant changes in the assumptions were required. Prior accident year loss development in 2006 was favorable by approximately $20 million, an insignificant amount for these classes. AIG's actuaries continued to benchmark the loss reserve indications to the ground-up claim projections provided by AIG claims staff for this class of business. For the year-end 2006 loss reserve review, the ground-up claim projections included all accident years through 2005.

Loss reserves pertaining to D&O and related management liability classes of business are included in the other liability claims made line of business, as presented in the table above.

Healthcare: Healthcare business written by Commercial Insurance produced moderate favorable development in 2006 and 2007 and significant favorable development in 2008. Healthcare loss reserves have benefited from favorable market conditions and an improved legal environment in accident years 2002 and subsequent, following a period of adverse loss trends and market conditions that began in the mid 1990's. For the year-end 2008 loss reserve review, AIG's actuaries responded to the consistently favorable experience observed during the latest three years by utilizing more responsive assumptions relating to loss development factors, loss trend factors, and expected loss ratios for this business. These modified assumptions resulted in approximately $140 million of additional favorable development that was recognized in the fourth quarter of 2008 for this business.

Overview of Loss Reserving Process

The General Insurance loss reserves can generally be categorized into two distinct groups. One group is short-tail classes of business consisting principally of property, personal lines and certain casualty classes. The other group is long-tail casualty classes of business which includes excess and umbrella liability, D&O, professional liability, medical malpractice, workers' compensation, general liability, products liability and related classes.

Short-Tail Reserves

For operations writing short-tail coverages, such as property coverages, the process of recording quarterly loss reserves is generally geared toward maintaining an appropriate reserve for the outstanding exposure, rather than determining an expected loss ratio for current business. For example, the IBNR reserve required for a class of property business might be expected to approximate 20 percent of the latest year's earned premiums, and this level of reserve would generally be maintained regardless of the loss ratio emerging in the current quarter. The 20 percent factor would be adjusted to reflect changes in rate levels, loss reporting patterns, known exposure to unreported losses, or other factors affecting the particular class of business.

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Long-Tail Reserves

Estimation of ultimate net losses and loss expenses (net losses) for long-tail casualty classes of business is a complex process and depends on a number of factors, including the class and volume of business involved. Experience in the more recent accident years of long-tail casualty classes of business shows limited statistical credibility in reported net losses because a relatively low proportion of net losses would be reported claims and expenses and an even smaller percentage would be net losses paid. Therefore, IBNR would constitute a relatively high proportion of net losses.

AIG's carried net long-tail loss reserves are tested using loss trend factors that AIG considers appropriate for each class of business. A variety of actuarial methods and assumptions is normally employed to estimate net losses for long-tail casualty classes of businesses. These methods ordinarily involve the use of loss trend factors intended to reflect the annual growth in loss costs from one accident year to the next. For the majority of long-tail casualty classes of business, net loss trend factors approximated five percent. Loss trend factors reflect many items including changes in claims handling, exposure and policy forms, current and future estimates of monetary inflation and social inflation and increases in litigation and awards. These factors are periodically reviewed and adjusted, as appropriate, to reflect emerging trends which are based upon past loss experience. Thus, many factors are implicitly considered in estimating the year to year growth in loss costs.

A number of actuarial assumptions are generally made in the review of reserves for each class of business. For longer-tail classes of business, actuarial assumptions generally are made with respect to the following:

- Loss trend factors which are used to establish expected loss ratios for subsequent accident years based on the projected loss ratio for prior accident years.
- Expected loss ratios for the latest accident year (i.e., accident year 2008 for the year-end 2008 loss reserve analysis) and, in some cases for accident years prior to the latest accident year. The expected loss ratio generally reflects the projected loss ratio from prior accident years, adjusted for the loss trend (see above) and the effect of rate changes and other quantifiable factors on the loss ratio. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are used for at least the three most recent accident years.
- Loss development factors which are used to project the reported losses for each accident year to an ultimate basis. Generally, the actual loss development factors observed from prior accident years would be used as a basis to determine the loss development factors for the subsequent accident years.

AIG records quarterly changes in loss reserves for each of its many General Insurance classes of business. The overall change in AIG's loss reserves is based on the sum of these classes of business changes. For most long-tail classes of business, the process of recording quarterly loss reserve changes involves determining the estimated current loss ratio for each class of coverage. This loss ratio is multiplied by the current quarter's net earned premium for that class of coverage to determine the current accident quarter's total estimated net incurred loss and loss expense. The change in loss reserves for the quarter for each class is thus the difference between the net incurred loss and loss expense, estimated as described above, and the net paid losses and loss expenses in the quarter. Also any change in estimated ultimate losses from prior accident years, either positive or negative, is reflected in the loss reserve for the current quarter.

Details of the Loss Reserving Process

The process of determining the current loss ratio for each class of business is based on a variety of factors. These include, but are not limited to, the following considerations: prior accident year and policy year loss ratios; rate changes; changes in coverage, reinsurance, or mix of business; and actual and anticipated changes in external factors affecting results, such as trends in loss costs or in the legal and claims environment. The current loss ratio for each class of business reflects input from actuarial, underwriting and claims staff and is intended to represent management's best estimate of the current loss ratio after reflecting all of the factors described above. At the close of each quarter, the assumptions underlying the loss ratios are reviewed to determine if the loss ratios remain appropriate. This process includes a review of the actual claims experience in the quarter, actual rate changes achieved, actual changes in coverage, reinsurance or mix of business, and changes in certain other factors that may

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affect the loss ratio. When this review suggests that the initially determined loss ratio is no longer appropriate, the loss ratio for current business is changed to reflect the revised assumptions.

A comprehensive annual loss reserve review is completed in the fourth quarter of each year for each AIG general insurance subsidiary. These reviews are conducted in full detail for each class of business for each subsidiary, and thus consist of hundreds of individual analyses. The purpose of these reviews is to confirm the appropriateness of the reserves carried by each of the individual subsidiaries, and therefore of AIG's overall carried reserves. The reserve analysis for each class of business is performed by the actuarial personnel who are most familiar with that class of business. In completing these detailed actuarial reserve analyses, the actuaries are required to make numerous assumptions, including the selection of loss development factors and loss cost trend factors. They are also required to determine and select the most appropriate actuarial methods to employ for each business class. Additionally, they must determine the appropriate segmentation of data from which the adequacy of the reserves can be most accurately tested. In the course of these detailed reserve reviews a point estimate of the loss reserve is determined. The sum of these point estimates for each class of business for each subsidiary provides an overall actuarial point estimate of the loss reserve for that subsidiary. The ultimate process by which the actual carried reserves are determined considers both the actuarial point estimate and numerous other internal and external factors including a qualitative assessment of inflation and other economic conditions in the United States and abroad, changes in the legal, regulatory, judicial and social environment, underlying policy pricing, terms and conditions, and claims handling. Loss reserve development can also be affected by commutations of assumed and ceded reinsurance agreements.

Actuarial Methods for Major Classes of Business

In testing the reserves for each class of business, a determination is made by AIG's actuaries as to the most appropriate actuarial methods. This determination is based on a variety of factors including the nature of the claims associated with the class of business, such as frequency or severity. Other factors considered include the loss development characteristics associated with the claims, the volume of claim data available for the applicable class, and the applicability of various actuarial methods to the class. In addition to determining the actuarial methods, the actuaries determine the appropriate loss reserve groupings of data. For example, AIG writes a great number of unique subclasses of professional liability. For pricing or other purposes, it is appropriate to evaluate the profitability of each subclass individually. However, for purposes of estimating the loss reserves for professional liability, it is appropriate to combine the subclasses into larger groups. The greater degree of credibility in the claims experience of the larger groups may outweigh the greater degree of homogeneity of the individual subclasses. This determination of data segmentation and actuarial methods is carefully considered for each class of business. The segmentation and actuarial methods chosen are those which together are expected to produce the most accurate estimate of the loss reserves.

Actuarial methods used by AIG for most long-tail casualty classes of business include loss development methods and expected loss ratio methods, including "Bornhuetter Ferguson" methods described below. Other methods considered include frequency/severity methods, although these are generally used by AIG more for pricing analysis than for loss reserve analysis. Loss development methods utilize the actual loss development patterns from prior accident years to project the reported losses to an ultimate basis for subsequent accident years. Loss development methods generally are most appropriate for classes of business which exhibit a stable pattern of loss development from one accident year to the next, and for which the components of the classes have similar development characteristics. For example, property exposures would generally not be combined into the same class as casualty exposures, and primary casualty exposures would generally not be combined into the same class as excess casualty exposures. Expected loss ratio methods are generally utilized by AIG where the reported loss data lacks sufficient credibility to utilize loss development methods, such as for new classes of business or for long-tail classes at early stages of loss development.

Expected loss ratio methods rely on the application of an expected loss ratio to the earned premium for the class of business to determine the loss reserves. For example, an expected loss ratio of 70 percent applied to an earned premium base of $10 million for a class of business would generate an ultimate loss estimate of $7 million. Subtracting any reported paid losses and loss expense would result in the indicated loss reserve for this class. "Bornhuetter Ferguson" methods are expected loss ratio methods for which the expected loss ratio is applied only to the expected unreported portion of the losses. For example, for a long-tail class of business for which only

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10 percent of the losses are expected to be reported at the end of the accident year, the expected loss ratio would be applied to the 90 percent of the losses still unreported. The actual reported losses at the end of the accident year would be added to determine the total ultimate loss estimate for the accident year. Subtracting the reported paid losses and loss expenses would result in the indicated loss reserve. In the example above, the expected loss ratio of 70 percent would be multiplied by 90 percent. The result of 63 percent would be applied to the earned premium of $10 million resulting in an estimated unreported loss of $6.3 million. Actual reported losses would be added to arrive at the total ultimate losses. If the reported losses were $1 million, the ultimate loss estimate under the "Bornhuetter Ferguson" method would be $7.3 million versus the $7 million amount under the expected loss ratio method described above. Thus, the "Bornhuetter Ferguson" method gives partial credibility to the actual loss experience to date for the class of business. Loss development methods generally give full credibility to the reported loss experience to date. In the example above, loss development methods would typically indicate an ultimate loss estimate of $10 million, as the reported losses of $1 million would be estimated to reflect only 10 percent of the ultimate losses.

A key advantage of loss development methods is that they respond quickly to any actual changes in loss costs for the class of business. Therefore, if loss experience is unexpectedly deteriorating or improving, the loss development method gives full credibility to the changing experience. Expected loss ratio methods would be slower to respond to the change, as they would continue to give more weight to the expected loss ratio, until enough evidence emerged for the expected loss ratio to be modified to reflect the changing loss experience. On the other hand, loss development methods have the disadvantage of overreacting to changes in reported losses if in fact the loss experience is not credible. For example, the presence or absence of large losses at the early stages of loss development could cause the loss development method to overreact to the favorable or unfavorable experience by assuming it will continue at later stages of development. In these instances, expected loss ratio methods such as "Bornhuetter Ferguson" have the advantage of properly recognizing large losses without extrapolating unusual large loss activity onto the unreported portion of the losses for the accident year. AIG's loss reserve reviews for long-tail classes typically utilize a combination of both loss development and expected loss ratio methods. Loss development methods are generally given more weight for accident years and classes of business where the loss experience is highly credible. Expected loss ratio methods are given more weight where the reported loss experience is less credible, or is driven more by large losses. Expected loss ratio methods require sufficient information to determine the appropriate expected loss ratio. This information generally includes the actual loss ratios for prior accident years, and rate changes as well as underwriting or other changes which would affect the loss ratio. Further, an estimate of the loss cost trend or loss ratio trend is required in order to allow for the effect of inflation and other factors which may increase or otherwise change the loss costs from one accident year to the next.

Frequency/severity methods generally rely on the determination of an ultimate number of claims and an average severity for each claim for each accident year. Multiplying the estimated ultimate number of claims for each accident year by the expected average severity of each claim produces the estimated ultimate loss for the accident year. Frequency/severity methods generally require a sufficient volume of claims in order for the average severity to be predictable. Average severity for subsequent accident years is generally determined by applying an estimated annual loss cost trend to the estimated average claim severity from prior accident years. Frequency/severity methods have the advantage that ultimate claim counts can generally be estimated more quickly and accurately than can ultimate losses. Thus, if the average claim severity can be accurately estimated, these methods can more quickly respond to changes in loss experience than other methods. However, for average severity to be predictable, the class of business must consist of homogeneous types of claims for which loss severity trends from one year to the next are reasonably consistent. Generally these methods work best for high frequency, low severity classes of business such as personal auto. AIG also utilizes these methods in pricing subclasses of professional liability. However, AIG does not generally utilize frequency/severity methods to test loss reserves, due to the general nature of AIG's reserves being applicable to lower frequency, higher severity commercial classes of business where average claim severity is volatile.

Excess Casualty: AIG generally uses a combination of loss development methods and expected loss ratio methods for excess casualty classes. Expected loss ratio methods are generally utilized for at least the three latest accident years, due to the relatively low credibility of the reported losses. The loss experience is generally reviewed separately for lead umbrella classes and for other excess classes, due to the relatively shorter tail for lead umbrella business. Automobile-related claims are generally reviewed separately from non-auto claims, due to the shorter-tail

nature of the automobile related claims. Claims relating to certain latent exposures such as construction defects or exhaustion of underlying product aggregate limits are reviewed separately due to the unique emergence patterns of losses relating to these claims. The expected loss ratios utilized for recent accident years are based on the projected ultimate loss ratios of prior years, adjusted for rate changes, estimated loss cost trends and all other changes that can be quantified. The estimated loss cost trend utilized in the year-end 2008 reviews averaged approximately five percent for excess casualty classes. Frequency/severity methods are generally not utilized as the vast majority of reported claims do not result in a claim payment. In addition, the average severity varies significantly from accident year to accident year due to large losses which characterize this class of business, as well as changing proportions of claims which do not result in a claim payment.

D&O: AIG generally utilizes a combination of loss development methods and expected loss ratio methods for D&O and related management liability classes of business. Expected loss ratio methods are given more weight in the two most recent accident years, whereas loss development methods are given more weight in more mature accident years. In addition to these traditional actuarial methods, AIG's actuaries utilize ground-up claim projections provided by AIG claims staff as a benchmark for determining the indicated ultimate losses for all accident years other than the most recent accident year. For the year-end 2008 loss reserve review, claims projections for accident years 2007 and prior were utilized. These classes of business reflect claims made coverage, and losses are characterized by low frequency and high severity. Thus, the claim projections can produce an overall indicator of the ultimate loss exposure for these classes by identifying and estimating all large losses. Frequency/severity methods are generally not utilized for these classes as the overall losses are driven by large losses more than by claim frequency. Severity trends have varied significantly from accident year to accident year.

Workers' Compensation: AIG generally utilizes loss development methods for all but the most recent accident year. Expected loss ratio methods generally are given significant weight only in the most recent accident year. Workers' compensation claims are generally characterized by high frequency, low severity, and relatively consistent loss development from one accident year to the next. AIG is a leading writer of workers' compensation, and thus has sufficient volume of claims experience to utilize development methods. AIG does not believe frequency/severity methods are as appropriate, due to significant growth and changes in AIG's workers' compensation business over the years. AIG generally segregates California business from other business in evaluating workers' compensation reserves. Certain classes of workers' compensation, such as construction, are also evaluated separately. Additionally, AIG writes a number of very large accounts which include workers' compensation coverage. These accounts are generally priced by AIG actuaries, and to the extent appropriate, the indicated losses based on the pricing analysis may be utilized to record the initial estimated loss reserves for these accounts.

Excess Workers' Compensation: AIG generally utilizes a combination of loss development methods and expected loss ratio methods. Loss development methods are given the greater weight for mature accident years such as 2002 and prior. Expected loss ratio methods are given the greater weight for the more recent accident years. Excess workers' compensation is an extremely long-tail class of business, with loss emergence extending for decades. Therefore there is limited credibility in the reported losses for many of the more recent accident years. For the mature accident years, AIG's actuaries utilize claims projections provided by AIG claims staff to help determine the loss development factors for this class of business.

General Liability: AIG generally uses a combination of loss development methods and expected loss ratio methods for primary general liability or products liability classes. For certain classes of business with sufficient loss volume, loss development methods may be given significant weight for all but the most recent one or two accident years, whereas for smaller or more volatile classes of business, loss development methods may be given limited weight for the five or more most recent accident years. Expected loss ratio methods would be utilized for the more recent accident years for these classes. The loss experience for primary general liability business is generally reviewed at a level that is believed to provide the most appropriate data for reserve analysis. For example, primary claims made business is generally segregated from business written on an occurrence policy form. Additionally, certain subclasses, such as construction, are generally reviewed separately from business in other subclasses. Due to the fairly long-tail nature of general liability business, and the many subclasses that are reviewed individually, there is less credibility in the reported losses and increased reliance on expected loss ratio methods. AIG's actuaries generally do not utilize frequency/severity methods to test reserves for this business, due to significant changes and growth in AIG's general liability and products liability business over the years.

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Commercial Automobile Liability: AIG generally utilizes loss development methods for all but the most recent accident year for commercial automobile classes of business. Expected loss ratio methods are generally given significant weight only in the most recent accident year. Frequency/severity methods are generally not utilized due to significant changes and growth in this business over the years.

Healthcare: AIG generally uses a combination of loss development methods and expected loss ratio methods for healthcare classes of business. The largest component of the healthcare business consists of coverage written for hospitals and other healthcare facilities. Reserves for excess coverage are tested separately from those for primary coverage. For primary coverages, loss development methods are generally given the majority of the weight for all but the latest three accident years, and are given some weight for all years other than the latest accident year. For excess coverages, expected loss methods are generally given all the weight for the latest three accident years, and are also given considerable weight for accident years prior to the latest three years. For other classes of healthcare coverage, an analogous weighting between loss development and expected loss ratio methods is utilized. The weights assigned to each method are those which are believed to result in the best combination of responsiveness and stability. Frequency/severity methods are sometimes utilized for pricing certain healthcare accounts or business. However, in testing loss reserves the business is generally combined into larger groupings to enhance the credibility of the loss experience. The frequency/severity methods that are applicable in pricing may not be appropriate for reserve testing and thus frequency/severity methods are not generally employed in AIG's healthcare reserve analyses.

Professional Liability: AIG generally uses a combination of loss development methods and expected loss ratio methods for professional liability classes of business. Loss development methods are used for the more mature accident years. Greater weight is given to expected loss ratio methods in the more recent accident years. Reserves are tested separately for claims made classes and classes written on occurrence policy forms. Further segmentations are made in a manner believed to provide an appropriate balance between credibility and homogeneity of the data. Frequency/severity methods are used in pricing and profitability analyses for some classes of professional liability; however, for loss reserve testing, the need to enhance credibility generally results in classes that are not sufficiently homogenous to utilize frequency/severity methods.

Catastrophic Casualty: AIG utilizes expected loss ratio methods for all accident years for catastrophic casualty business. This class of business consists of casualty or financial lines coverage which attaches in excess of very high attachment points; thus the claims experience is marked by very low frequency and high severity. Because of the limited number of claims, loss development methods are not utilized. The expected loss ratios and loss development assumptions utilized are based upon the results of prior accident years for this business as well as for similar classes of business written above lower attachment points. The business is generally written on a claims made basis. AIG utilizes ground-up claim projections provided by AIG claims staff to assist in developing the appropriate reserve.

Aviation: AIG generally uses a combination of loss development methods and expected loss ratio methods for aviation exposures. Aviation claims are not very long-tail in nature; however, they are driven by claim severity. Thus a combination of both development and expected loss ratio methods are used for all but the latest accident year to determine the loss reserves. Expected loss ratio methods are used to determine the loss reserves for the latest accident year. Frequency/severity methods are not employed due to the high severity nature of the claims and different mix of claims from year to year.

Personal Auto (Domestic): AIG generally utilizes frequency/severity methods and loss development methods for domestic personal auto classes. For many classes of business, greater reliance is placed on frequency/severity methods as claim counts emerge quickly for personal auto and allow for more immediate analysis of resulting loss trends and comparisons to industry and other diagnostic metrics.

Fidelity/Surety: AIG generally uses loss development methods for fidelity exposures for all but the latest accident year. Expected loss ratio methods are also given weight for the more recent accident years, and for the latest accident year they may be given 100 percent weight. For surety exposures, AIG generally uses the same method as for short-tail classes.

Mortgage Guaranty: AIG tests mortgage guaranty reserves using loss development methods, supplemented by an internal claim analysis by actuaries and staff who specialize in the mortgage guaranty business. The claim

analysis projects ultimate losses for claims within each of several categories of delinquency based on actual historical experience and is essentially a frequency/severity analysis for each category of delinquency. Additional reserve tests using "Bornhuetter Ferguson" methods are also employed, as well as tests measuring losses as a percent of risk in force. Reserves are reviewed separately for each class of business to consider the loss development characteristics associated with the claims, the volume of claim data available for the applicable class and the applicability of various actuarial methods to the class.

Short-Tail Classes: AIG generally uses either loss development methods or IBNR factor methods to set reserves for short-tail classes such as property coverages. Where a factor is used, it generally represents a percent of earned premium or other exposure measure. The factor is determined based on prior accident year experience. For example, the IBNR for a class of property coverage might be expected to approximate 20 percent of the latest year's earned premium. The factor is continually reevaluated in light of emerging claim experience as well as rate changes or other factors that could affect the adequacy of the IBNR factor being employed.

International: Business written by AIG's Foreign General Insurance sub-segment includes both long-tail and short-tail classes of business. For long-tail classes of business, the actuarial methods utilized would be analogous to those described above. However, the majority of business written by Foreign General Insurance is short-tail, high frequency and low severity in nature. For this business, loss development methods are generally employed to test the loss reserves. AIG maintains a data base of detailed historical premium and loss transactions in original currency for business written by Foreign General Insurance, thereby allowing AIG actuaries to determine the current reserves without any distortion from changes in exchange rates over time. In testing the Foreign General Insurance reserves, AIG's actuaries segment the data by region, country or class of business as appropriate to determine an optimal balance between homogeneity and credibility.

Loss Adjustment Expenses: AIG determines reserves for legal defense and cost containment loss adjustment expenses for each class of business by one or more actuarial methods. The methods generally include development methods analogous to those described for loss development methods. The developments could be based on either the paid loss adjustment expenses or the ratio of paid loss adjustment expenses to paid losses, or both. Other methods include the utilization of expected ultimate ratios of paid loss expense to paid losses, based on actual experience from prior accident years or from similar classes of business. AIG generally determines reserves for adjuster loss adjustment expenses based on calendar year ratios of adjuster expenses paid to losses paid for the particular class of business. AIG generally determines reserves for other unallocated loss adjustment expenses based on the ratio of the calendar year expenses paid to overall losses paid. This determination is generally done for all classes of business combined, and reflects costs of home office claim overhead as a percent of losses paid.

Catastrophes: Special analyses are conducted by AIG in response to major catastrophes in order to estimate AIG's gross and net loss and loss expense liability from the events. These analyses may include a combination of approaches, including modeling estimates, ground-up claim analysis, loss evaluation reports from on-site field adjusters, and market share estimates.

AIG's loss reserve analyses do not calculate a range of loss reserve estimates. Because a large portion of the loss reserves from AIG's General Insurance business relates to longer-tail casualty classes of business driven by severity rather than frequency of claims, such as excess casualty and D&O, developing a range around loss reserve estimates would not be meaningful. Using the reserving methodologies described above, AIG's actuaries determine their best estimate of the required reserve and advise management of that amount. AIG then adjusts its aggregate carried reserves as necessary so that the actual carried reserves as of December 31 reflect this best estimate.

Volatility of Reserve Estimates and Sensitivity Analyses

As described above, AIG uses numerous assumptions in determining its best estimate of reserves for each class of business. The importance of any specific assumption can vary by both class of business and accident year. If actual experience differs from key assumptions used in establishing reserves, there is potential for significant variation in the development of loss reserves, particularly for long-tail casualty classes of business such as excess casualty, D&O or workers' compensation. Set forth below is a sensitivity analysis that estimates the effect on the loss reserve position of using alternative loss trend or loss development factor assumptions rather than those actually used in determining AIG's best estimates in the year-end loss reserve analyses in 2008. The analysis addresses each major class of business for which a material deviation to AIG's overall reserve position is believed reasonably

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possible, and uses what AIG believes is a reasonably likely range of potential deviation for each class. There can be no assurance, however, that actual reserve development will be consistent with either the original or the adjusted loss trend or loss development factor assumptions, or that other assumptions made in the reserving process will not materially affect reserve development for a particular class of business.

Excess Casualty: For the excess casualty class of business, the assumed loss cost trend was approximately five percent. After evaluating the historical loss cost trends from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2008 loss reserve review for excess casualty will range from negative five percent to positive 15 percent, or approximately ten percent lower or higher than the assumption actually utilized in the year-end 2008 reserve review. A ten percent change in the assumed loss cost trend for excess casualty would cause approximately a $2.4 billion increase or a $1.6 billion decrease in the net loss and loss expense reserve for this class of business. It should be emphasized that the ten percent deviations are not considered the highest possible deviations that might be expected, but rather what is considered by AIG to reflect a reasonably likely range of potential deviation. Actual loss cost trends in the early 1990s were negative for several years, including amounts below the negative five percent cited above, whereas actual loss cost trends in the late 1990s ran well into the double digits for several years, including amounts greater than the 15 percent cited above. Thus, there can be no assurance that loss trends will not deviate by more than ten percent. The loss cost trend assumption is critical for the excess casualty class of business due the long-tail nature of the claims and therefore is applied across many accident years.

For the excess casualty class of business, the assumed loss development factors are also a key assumption. After evaluating the historical loss development factors from prior accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss development factors will range from approximately 4.4 percent below those actually utilized in the year-end 2008 reserve review to approximately 6.4 percent above those factors actually utilized. If the loss development factor assumptions were changed by 4.4 percent and 6.4 percent, respectively, the net loss reserves for the excess casualty class would decrease by approximately $900 million under the lower assumptions or increase by approximately $1.5 billion under the higher assumptions. Generally, actual historical loss development factors are used to project future loss development. However there can be no assurance that future loss development patterns will be the same as in the past, or that they will not deviate by more than the amounts illustrated above. Moreover, as excess casualty is a long-tail class of business, any deviation in loss cost trends or in loss development factors might not be discernible for an extended period of time subsequent to the recording of the initial loss reserve estimates for any accident year. Thus, there is the potential for the reserves with respect to a number of accident years to be significantly affected by changes in the loss cost trends or loss development factors that were initially relied upon in setting the reserves. These changes in loss trends or loss development factors could be attributable to changes in inflation or in the judicial environment, or in other social or economic conditions affecting claims. Thus, there is the potential for variations greater than the amounts cited above, either positively or negatively.

D&O and Related Management Liability Classes of Business: For D&O and related management liability classes of business, the assumed loss cost trend was approximately four percent. After evaluating the historical loss cost trends from prior accident years since the early 1990s, including the potential effect of recent claims relating to the credit crisis, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2008 loss reserve review for these classes will range from negative 11 percent to positive 24 percent, or approximately 15 percent lower or 20 percent higher than the assumption actually utilized in the year-end 2008 reserve review. A 20 or 15 percent change in the assumed loss cost trend for these classes would cause approximately a $950 million increase or a $600 million decrease, respectively, in the net loss and loss expense reserves for these classes of business. It should be emphasized that the 20 and 15 percent deviations are not considered the highest possible deviations that might be expected, but rather what is considered by AIG to reflect a reasonably likely range of potential deviation. Actual loss cost trends for these classes since the early 1990s were negative for several years, including amounts below the negative 11 percent cited above, whereas actual loss cost trends exceeded the 24 percent figure cited above for several other years. Because the D&O class of business has exhibited highly volatile loss trends from one accident year to the next, there is the possibility of an exceptionally high deviation.

For D&O and related management liability classes of business, the assumed loss development factors are also an important assumption but less critical than for excess casualty. Because these classes are written on a claims

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made basis, the loss reporting and development tail is much shorter than for excess casualty. However, the high severity nature of the claims does create the potential for significant deviations in loss development patterns from one year to the next. After evaluating the historical loss development factors for these classes of business for accident years since the early 1990s, in AIG's judgment, it is reasonably likely that actual loss development factors will range from approximately 8.5 percent lower to 3.5 percent higher than those factors actually utilized in the year-end 2008 loss reserve review for these classes. If the loss development factor assumptions were changed by 8.5 percent and 3.5 percent, respectively, the net loss reserves for these classes would be estimated to decrease or increase by approximately $300 million and $150 million, respectively. As noted above for excess casualty, actual historical loss development factors are generally used to project future loss development. However, there can be no assurance that future loss development patterns will be the same as in the past, or that they will not deviate by more than the 8.5 percent or 3.5 percent amounts.

Excess Workers' Compensation: For excess workers' compensation business, loss costs were trended at six percent per annum. After reviewing actual industry loss trends for the past ten years, in AIG's judgment, it is reasonably likely that actual loss cost trends applicable to the year-end 2008 loss reserve review for excess workers' compensation will range five percent lower or higher than this estimated loss trend. A five percent change in the assumed loss cost trend would cause approximately a $425 million increase or a $275 million decrease in the net loss reserves for this business. It should be emphasized that the actual loss cost trend could vary significantly from this assumption, and there can be no assurance that actual loss costs will not deviate, perhaps materially, by greater than five percent.

For excess workers' compensation business, the assumed loss development factors are a critical assumption. Excess workers' compensation is an extremely long-tail class of business, with a much greater than normal uncertainty as to the appropriate loss development factors for the tail of the loss development. After evaluating the historical loss development factors for prior accident years since the 1980s, in AIG's judgment, it is reasonably likely that actual loss development factors will range from approximately 12 percent lower to 20 percent higher than those factors actually utilized in the year-end 2008 loss reserve review for excess workers' compensation. If the loss development factor assumptions were increased by 20 percent or decreased by 12 percent, the net loss reserves for excess workers' compensation would increase or decrease by approximately $950 million and $550 million, respectively. Given the exceptionally long-tail for this class of business, there is the potential for actual deviations in the loss development tail to exceed the deviations assumed, perhaps materially.

Primary Workers' Compensation: For primary workers' compensation, the loss cost trend assumption is not believed to be material with respect to AIG's loss reserves. This is primarily because AIG's actuaries are generally able to use loss development projections for all but the most recent accident year's reserves, so there is limited need to rely on loss cost trend assumptions for primary workers' compensation business.

However, for primary workers' compensation business the loss development factor assumptions are important. Generally, AIG's actual historical workers' compensation loss development factors would be expected to provide a reasonably accurate predictor of future loss development. However, workers' compensation is a long-tail class of business, and AIG's business reflects a very significant volume of losses particularly in recent accident years due to growth of the business. After evaluating the actual historical loss developments since the 1980s for this business, in AIG's judgment, it is reasonably likely that actual loss development factors will fall within the range of approximately 3.6 percent below to 9.4 percent above those actually utilized in the year-end 2008 loss reserve review. If the loss development factor assumptions were changed by 3.6 percent and 9.4 percent, respectively, the net loss reserves for workers' compensation would decrease or increase by approximately $900 million and $2.4 billion, respectively. For this class of business, there can be no assurance that actual deviations from the expected loss development factors will not exceed the deviations assumed, perhaps materially.

Other Casualty Classes of Business: For casualty business other than the classes discussed above, there is generally some potential for deviation in both the loss cost trend and loss development factor assumptions. However, the effect of such deviations is expected to be less material when compared to the effect on the classes cited above.

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Asbestos and Environmental Reserves

The estimation of loss reserves relating to asbestos and environmental claims on insurance policies written many years ago is subject to greater uncertainty than other types of claims due to inconsistent court decisions as well as judicial interpretations and legislative actions that in some cases have tended to broaden coverage beyond the original intent of such policies and in others have expanded theories of liability. The insurance industry as a whole is engaged in extensive litigation over these coverage and liability issues and is thus confronted with a continuing uncertainty in its efforts to quantify these exposures.

AIG continues to receive claims asserting injuries and damages from toxic waste, hazardous substances, and other environmental pollutants and alleged claims to cover the cleanup costs of hazardous waste dump sites, referred to collectively as environmental claims, and indemnity claims asserting injuries from asbestos.

The vast majority of these asbestos and environmental claims emanate from policies written in 1984 and prior years. Commencing in 1985, standard policies contained an absolute exclusion for pollution-related damage and an absolute asbestos exclusion was also implemented. The current environmental policies that AIG underwrites on a claims-made basis have been excluded from the analysis herein.

The majority of AIG's exposures for asbestos and environmental claims are excess casualty coverages, not primary coverages. Thus, the litigation costs are treated in the same manner as indemnity amounts. That is, litigation expenses are included within the limits of the liability AIG incurs. Individual significant claim liabilities, where future litigation costs are reasonably determinable, are established on a case-by-case basis.

Estimation of asbestos and environmental claims loss reserves is a subjective process and reserves for asbestos and environmental claims cannot be estimated using conventional reserving techniques such as those that rely on historical accident year loss development factors. The methods used to determine asbestos and environmental loss estimates and to establish the resulting reserves are continually reviewed and updated by management.

Significant factors which affect the trends that influence the asbestos and environmental claims estimation process are the court resolutions and judicial interpretations which broaden the intent of the policies and scope of coverage. The current case law can be characterized as still evolving, and there is little likelihood that any firm direction will develop in the near future. Additionally, the exposures for cleanup costs of hazardous waste dump sites involve issues such as allocation of responsibility among potentially responsible parties and the government's refusal to release parties from liability.

Due to this uncertainty, it is not possible to determine the future development of asbestos and environmental claims with the same degree of reliability as with other types of claims. Such future development will be affected by the extent to which courts continue to expand the intent of the policies and the scope of the coverage, as they have in the past, as well as by the changes in Superfund and waste dump site coverage and liability issues. If the asbestos and environmental reserves develop deficiently, such deficiency would have an adverse effect on AIG's future results of operations.

With respect to known asbestos and environmental claims, AIG established over two decades ago specialized toxic tort and environmental claims units, which investigate and adjust all such asbestos and environmental claims. These units evaluate these asbestos and environmental claims utilizing a claim-by-claim approach that involves a detailed review of individual policy terms and exposures. Because each policyholder presents different liability and coverage issues, AIG generally evaluates exposure on a policy-by-policy basis, considering a variety of factors such as known facts, current law, jurisdiction, policy language and other factors that are unique to each policy. Quantitative techniques have to be supplemented by subjective considerations, including management judgment. Each claim is reviewed at least semi-annually utilizing the aforementioned approach and adjusted as necessary to reflect the current information.

In both the specialized and dedicated asbestos and environmental claims units, AIG actively manages and pursues early resolution with respect to these claims in an attempt to mitigate its exposure to the unpredictable development of these claims. AIG attempts to mitigate its known long-tail environmental exposures by utilizing a combination of proactive claim-resolution techniques, including policy buybacks, complete environmental releases, compromise settlements, and, where indicated, litigation.

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With respect to asbestos claims handling, AIG's specialized claims staff operates to mitigate losses through proactive handling, supervision and resolution of asbestos cases. Thus, while AIG has resolved all claims with respect to miners and major manufacturers (Tier One), its claims staff continues to operate under the same proactive philosophy to resolve claims involving accounts with products containing asbestos (Tier Two), products containing small amounts of asbestos, companies in the distribution process, and parties with remote, ill-defined involvement in asbestos (Tiers Three and Four). Through its commitment to appropriate staffing, training, and management oversight of asbestos cases, AIG seeks to mitigate its exposure to these claims.

To determine the appropriate loss reserve as of December 31, 2008 for its asbestos and environmental exposures, AIG performed a series of top-down and ground-up reserve analyses. In order to ensure it had the most comprehensive analysis possible, AIG engaged a third-party actuary to assist in a review of these exposures, including ground-up estimates for asbestos reserves consistent with the 2005 through 2007 reviews as well as a top-down report year projection for environmental reserves. Prior to 2005, AIG's reserve analyses for asbestos and environmental exposures were focused around a report year projection of aggregate losses for both asbestos and environmental reserves. Additional tests such as market share analyses were also performed. Ground-up analyses take into account policyholder-specific and claim-specific information that has been gathered over many years from a variety of sources. Ground-up studies can thus more accurately assess the exposure to AIG's layers of coverage for each policyholder, and hence for all policyholders in the aggregate, provided a sufficient sample of the policyholders can be modeled in this manner.

In order to ensure its ground-up analysis was comprehensive, AIG staff produced the information required at policy and claim level detail for over 800 asbestos defendants. This represented over 95 percent of all accounts for which AIG had received any claim notice of any amount pertaining to asbestos exposure. AIG did not set any minimum thresholds, such as amount of case reserve outstanding, or paid losses to date, that would have served to reduce the sample size and hence the comprehensiveness of the ground-up analysis. The results of the ground-up analysis for each significant account were examined by AIG's claims staff for reasonableness, for consistency with policy coverage terms, and any claim settlement terms applicable. Adjustments were incorporated accordingly. The results from the universe of modeled accounts, which as noted above reflects the vast majority of AIG's known exposures, were then utilized to estimate the ultimate losses from accounts or exposures that could not be modeled and to determine an appropriate provision for unreported claims.

AIG conducted a comprehensive analysis of reinsurance recoverability to establish the appropriate asbestos and environmental reserve net of reinsurance. AIG determined the amount of reinsurance that would be ceded to insolvent reinsurers or to commuted reinsurance contracts for both reported claims and for IBNR. These amounts were then deducted from the indicated amount of reinsurance recoverable. The year-end 2008 analysis reflected an update to the comprehensive analysis of reinsurance recoverability that was first completed in 2005 and updated in 2006 and 2007. All asbestos accounts for which there was a significant change in estimated losses in the 2008 review were analyzed to determine the appropriate reserve net of reinsurance.

AIG also completed a top-down report year projection of its indicated asbestos and environmental loss reserves. These projections consist of a series of tests performed separately for asbestos and for environmental exposures.

For asbestos, these tests project the losses expected to be reported over the next 18 years, i.e., from 2009 through 2026, based on the actual losses reported through 2008 and the expected future loss emergence for these claims. Three scenarios were tested, with a series of assumptions ranging from more optimistic to more conservative.

For environmental claims, an analogous series of frequency/severity tests are produced. Environmental claims from future report years, (i.e., IBNR) are projected out eight years, i.e., through the year 2016.

At year-end 2008, AIG considered a number of factors and recent experience in addition to the results of the respective top-down and ground-up analyses performed for asbestos and environmental reserves. AIG considered the significant uncertainty that remains as to AIG's ultimate liability relating to asbestos and environmental claims. This uncertainty is due to several factors including:

- The long latency period between asbestos exposure and disease manifestation and the resulting potential for involvement of multiple policy periods for individual claims;

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- The increase in the volume of claims by currently unimpaired plaintiffs;
- Claims filed under the non-aggregate premises or operations section of general liability policies;
- The number of insureds seeking bankruptcy protection and the effect of prepackaged bankruptcies;
- Diverging legal interpretations; and
- With respect to environmental claims, the difficulty in estimating the allocation of remediation cost among various parties.

After carefully considering the results of the ground-up analysis, which AIG updates on an annual basis, as well as all of the above factors, including the recent report year experience, AIG increased its gross asbestos reserves by $200 million and increased its net asbestos reserves by $30 million. Additionally, during 2008 an amount of adverse incurred loss development pertaining to asbestos was reflected which was primarily attributed to several large defendants, the effect of which was largely offset by one large favorable settlement.

Upon completion of the environmental top-down report year analysis performed in the fourth quarter of 2008, no adjustment to gross and net reserves was recognized. Additionally, during 2008 a moderate amount of favorable gross incurred loss development pertaining to environmental was reflected which was primarily attributable to recent favorable experience which was fully insured, resulting in no favorable net development on environmental net reserves.

A summary of reserve activity, including estimates for applicable IBNR, relating to asbestos and environmental claims separately and combined appears in the table below. The vast majority of such claims arise from policies written in 1984 and prior years. The current environmental policies that AIG underwrites on a claims-made basis have been excluded from the table below.

	As of or for the Years Ended December 31,					
	2008		2007		2006	
	Gross	Net	Gross	Net	Gross	Net
	(In millions)					
Asbestos:						
Liability for unpaid claims and claims adjustment expense at beginning of year	**$3,864**	**$1,454**	$4,523	$1,889	$4,501	$1,840
Losses and loss expenses incurred *	**273**	**53**	96	5	572	267
Losses and loss expenses paid *	**(694)**	**(307)**	(755)	(440)	(550)	(218)
Liability for unpaid claims and claims adjustment expense at end of year	**$3,443**	**$1,200**	$3,864	$1,454	$4,523	$1,889
Environmental:						
Liability for unpaid claims and claims adjustment expense at beginning of year	**$ 515**	**$ 237**	$ 629	$ 290	$ 969	$ 410
Losses and loss expenses incurred *	**(44)**	**(2)**	10	13	(231)	(59)
Losses and loss expenses paid *	**(54)**	**(41)**	(124)	(66)	(109)	(61)
Liability for unpaid claims and claims adjustment expense at end of year	**$ 417**	**$ 194**	$ 515	$ 237	$ 629	$ 290
Combined:						
Liability for unpaid claims and claims adjustment expense at beginning of year	**$4,379**	**$1,691**	$5,152	$2,179	$5,470	$2,250
Losses and loss expenses incurred *	**229**	**51**	106	18	341	208
Losses and loss expenses paid *	**(748)**	**(348)**	(879)	(506)	(659)	(279)
Liability for unpaid claims and claims adjustment expense at end of year	**$3,860**	**$1,394**	$4,379	$1,691	$5,152	$2,179

* *All amounts pertain to policies underwritten in prior years, primarily to policies issued in 1984 and prior.*

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American International Group, Inc., and Subsidiaries

The gross and net IBNR included in the liability for unpaid claims and claims adjustment expense, relating to asbestos and environmental claims separately and combined were estimated as follows:

	At December 31, 2008 Gross	2008 Net	2007 Gross	2007 Net	2006 Gross	2006 Net
	(In millions)					
Asbestos	**$2,301**	**$ 939**	$2,701	$1,145	$3,270	$1,469
Environmental	**249**	**99**	325	131	378	173
Combined	**$2,550**	**$1,038**	$3,026	$1,276	$3,648	$1,642

A summary of asbestos and environmental claims count activity was as follows:

As of or for the Years Ended December 31,	2008 Asbestos	2008 Environmental	2008 Combined	2007 Asbestos	2007 Environmental	2007 Combined	2006 Asbestos	2006 Environmental	2006 Combined
Claims at beginning of year	**6,563**	**7,652**	**14,215**	6,878	9,442	16,320	7,293	9,873	17,166
Claims during year:									
Opened	**639**	**1,065**	**1,704**	656	937	1,593	643	1,383	2,026
Settled	**(219)**	**(207)**	**(426)**	(150)	(179)	(329)	(150)	(155)	(305)
Dismissed or otherwise resolved	**(1,203)**	**(1,836)**	**(3,039)**	(821)	(2,548)	(3,369)	(908)	(1,659)	(2,567)
Claims at end of year	**5,780**	**6,674**	**12,454**	6,563	7,652	14,215	6,878	9,442	16,320

Survival Ratios — Asbestos and Environmental

The following table presents AIG's survival ratios for asbestos and environmental claims at December 31, 2008, 2007 and 2006. The survival ratio is derived by dividing the current carried loss reserve by the average payments for the three most recent calendar years for these claims. Therefore, the survival ratio is a simplistic measure estimating the number of years it would be before the current ending loss reserves for these claims would be paid off using recent year average payments. The December 31, 2008 survival ratio is lower than the ratio at December 31, 2007 because the more recent periods included in the rolling average reflect higher claims payments. In addition, AIG's survival ratio for asbestos claims was negatively affected by the favorable settlement described above, as well as several similar settlements during 2007. These settlements reduced gross and net asbestos survival ratios at December 31, 2008 by approximately 1.1 years and 2.4 years, respectively, and reduced gross and net asbestos survival ratios at December 31, 2007 by approximately 1.3 years and 2.6 years, respectively. Many factors, such as aggressive settlement procedures, mix of business and level of coverage provided, have a significant effect on the amount of asbestos and environmental reserves and payments and the resultant survival ratio. Moreover, as discussed above, the primary basis for AIG's determination of its reserves is not survival ratios, but instead the ground-up and top-down analysis. Thus, caution should be exercised in attempting to determine reserve adequacy for these claims based simply on this survival ratio.

AIG's survival ratios for asbestos and environmental claims, separately and combined, were based upon a three-year average payment and were as follows:

Years Ended December 31,	Gross	Net
2008		
Survival ratios:		
Asbestos	**5.2**	**3.7**
Environmental	**4.4**	**3.5**
Combined	**5.1**	**3.7**

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American International Group, Inc., and Subsidiaries

Years Ended December 31,	Gross	Net
2007		
Survival ratios:		
Asbestos	7.1	5.6
Environmental	4.7	3.7
Combined	6.7	5.2
2006		
Survival ratios:		
Asbestos	11.8	12.9
Environmental	5.6	4.5
Combined	10.4	10.3

Life Insurance & Retirement Services Operations

AIG's Life Insurance & Retirement Services operations offer a wide range of insurance and retirement savings products both domestically and abroad.

AIG's Foreign Life Insurance & Retirement Services operations include insurance and investment-oriented products such as whole and term life, investment linked, universal life and endowments, personal accident and health products, group products including pension, life and health, and fixed and variable annuities. The Foreign Life Insurance & Retirement Services products are sold through independent producers, career agents, financial institutions and direct marketing channels.

AIG's Domestic Life Insurance operations offer a broad range of protection products, such as individual life insurance and group life and health products, including disability income products and payout annuities, which include single premium immediate annuities, structured settlements and terminal funding annuities. The Domestic Life Insurance products are sold through independent producers, career agents, financial institutions and direct marketing channels. Home service operations include an array of life insurance, accident and health and annuity products sold primarily through career agents.

AIG's Domestic Retirement Services operations include group retirement products, individual fixed and variable annuities sold through banks, broker-dealers and exclusive sales representatives, and annuity runoff operations, which include previously acquired "closed blocks" and other fixed and variable annuities largely sold through distribution relationships that have been discontinued.

AIG's Life Insurance & Retirement Services reports its operations through the following major internal reporting units and legal entities:

Foreign Life Insurance & Retirement Services

Japan and Other

- American Life Insurance Company (ALICO)
- AIG Star Life Insurance Co., Ltd. (AIG Star Life)
- AIG Edison Life Insurance Company (AIG Edison Life)

Asia

- American International Assurance Company, Limited, together with American International Assurance Company (Bermuda) Limited (AIA)
- Nan Shan Life Insurance Company, Ltd. (Nan Shan)
- American International Reinsurance Company Limited (AIRCO)
- The Philippine American Life and General Insurance Company (Philamlife)

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Domestic Life Insurance

- American General Life Insurance Company (AIG American General)
- The United States Life Insurance Company in the City of New York (USLIFE)
- American General Life and Accident Insurance Company (AGLA)

Domestic Retirement Services

- The Variable Annuity Life Insurance Company (VALIC)
- AIG Annuity Insurance Company (AIG Annuity)
- AIG SunAmerica Life Assurance Company (AIG SunAmerica)

Life Insurance & Retirement Services Results

Life Insurance & Retirement Services results were as follows:

Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses) (In millions)	Total Revenues	Operating Income (Loss)*
2008					
Japan and Other	**$ 14,513**	**$ 980**	**$ (5,693)**	**$ 9,800**	**$ (2,687)**
Asia	**15,406**	**981**	**(6,092)**	**10,295**	**(3,650)**
Total Foreign Life & Retirement Services	**29,919**	**1,961**	**(11,785)**	**20,095**	**(6,337)**
Domestic Life Insurance	**6,248**	**3,799**	**(11,568)**	**(1,521)**	**(10,238)**
Domestic Retirement Services	**1,128**	**4,346**	**(20,994)**	**(15,520)**	**(20,871)**
Total	**$ 37,295**	**$ 10,106**	**$ (44,347)**	**$ 3,054**	**$ (37,446)**
2007					
Japan and Other	$ 12,387	$ 6,083	$ (294)	$ 18,176	$ 3,044
Asia	14,214	5,766	107	20,087	3,153
Total Foreign Life & Retirement Services	26,601	11,849	(187)	38,263	6,197
Domestic Life Insurance	5,836	3,995	(803)	9,028	642
Domestic Retirement Services	1,190	6,497	(1,408)	6,279	1,347
Total	$ 33,627	$ 22,341	$ (2,398)	$ 53,570	$ 8,186
2006					
Japan and Other	$ 11,106	$ 5,239	$ 406	$ 16,751	$ 3,821
Asia	13,060	4,519	301	17,880	3,060
Total Foreign Life & Retirement Services	24,166	9,758	707	34,631	6,881
Domestic Life Insurance	5,543	3,778	(215)	9,106	917
Domestic Retirement Services	1,057	6,488	(404)	7,141	2,323
Total	$ 30,766	$ 20,024	$ 88	$ 50,878	$ 10,121
Percentage Increase/(Decrease) 2008 vs. 2007:					
Japan and Other	17%	(84)%	—%	(46)%	—%
Asia	8	(83)	—	(49)	—
Total Foreign Life & Retirement Services	12	(83)	—	(47)	—
Domestic Life Insurance	7	(5)	—	—	—
Domestic Retirement Services	(5)	(33)	—	—	—
Total	11%	(55)%	—%	(94)%	—%

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American International Group, Inc., and Subsidiaries

Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses) (In millions)	Total Revenues	Operating Income (Loss)*
Percentage Increase/(Decrease) 2007 vs. 2006:					
Japan and Other	12%	16%	—%	9%	(20)%
Asia	9	28	(64)	12	3
Total Foreign Life & Retirement Services	10	21	—	10	(10)
Domestic Life Insurance	5	6	—	(1)	(30)
Domestic Retirement Services	13	—	—	(12)	(42)
Total	9%	12%	—%	5%	(19)%

* *2008 operating income (loss) includes goodwill impairment charges of $402 million and $817 million for Domestic Life Insurance and Domestic Retirement Services , respectively.*

The following table presents the gross insurance in force for Life Insurance & Retirement Services:

	At December 31, 2008	2007 (In billions)	2006
Foreign*	**$1,352**	$1,327	$1,163
Domestic	**1,026**	985	908
Total	**$2,378**	$2,312	$2,071

* *Includes increases of $57.8 billion, $55.1 billion and $41.5 billion related to changes in foreign exchange rates at December 31, 2008, 2007 and 2006, respectively.*

2008 and 2007 Comparison

Total revenues decreased in 2008 compared to 2007, primarily due to significantly higher levels of net realized capital losses and lower net investment income. See Consolidated Results and Investments — Portfolio Review for further discussion.

Premiums and other considerations increased in 2008 compared to 2007 primarily due to increased production and favorable foreign exchange rates in the Foreign Life Insurance & Retirement Services operations and sales of payout annuities in Domestic Life Insurance.

In addition to the higher net realized capital losses and lower net investment income noted above, the operating loss for 2008 increased as a result of DAC and sales inducement asset (SIA) unlocking and related reserve strengthening of $1.5 billion in the Domestic Retirement Services operations resulting from the continued weakness in the equity markets, the significantly higher surrender activity resulting from AIG parent's liquidity issues beginning in mid-September and goodwill impairment charges of $1.2 billion in the Domestic Life Insurance and Domestic Retirement Services companies. The impairment charges were attributable to declines in the estimated fair values of reporting units in the Property and Casualty Group, Domestic Life Insurance and Domestic Retirement Services, Consumer Finance and Capital Markets businesses attributable to the uncertain economic environment that developed in late 2008 coupled with other indications of fair value developed through the restructuring and asset disposition activities. The operating loss also included higher benefit costs in the Japan variable life product resulting from declines in the Japanese equity market. These decreases were partially offset by the favorable effect of foreign exchange rates and growth in the underlying business in force. The operating loss in 2008 included a DAC and SIA benefit of $3.2 billion related to net realized capital losses compared to a benefit of $333 million in 2007.

AIG adopted FAS 157 on January 1, 2008. The adoption of FAS 157 resulted in an increase in pre-tax net realized capital losses of $155 million as of January 1, 2008, partially offset by a $47 million DAC benefit related to

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these losses. These results were primarily due to an increase in the embedded policy derivative liability valuations resulting from the inclusion of explicit risk margins.

AIG adopted FAS 159 on January 1, 2008 and elected to apply the fair value option to a closed block of single premium variable life business in Japan and to an investment-linked product sold principally in Asia. The adoption of FAS 159 with respect to these fair value elections resulted in a decrease to 2008 opening retained earnings of $559 million, net of tax. The fair value of the liabilities for these policies totaled $2.6 billion at December 31, 2008 and is reported in policyholder contract deposits.

2007 and 2006 Comparison

The severe credit market disruption was a key driver of operating results in 2007 principally due to significant net realized capital losses resulting from other-than-temporary impairment charges and losses on derivative instruments not qualifying for hedge accounting treatment. See Results of Operations Consolidated Results — Net Realized Gains (Losses) for further discussion.

Life Insurance & Retirement Services total revenues increased in 2007 compared to 2006 despite the higher net realized capital losses primarily due to higher premiums and other considerations and higher net investment income.

Operating income in 2007 decreased compared to 2006 primarily due to net realized capital losses and the following:

- mark-to-market trading losses of $150 million related to investment-linked products in the U.K.;
- DAC amortization charges of $108 million related to the adoption in 2007 of SOP 05-1;
- remediation activity charges of $118 million; and
- out-of-period adjustments related to UCITS and participating policyholder dividends, which increased 2006 operating income by $332 million.

These decreases were partially offset as operating income in 2006 was negatively affected by charges of $125 million for the Superior National arbitration ruling, $66 million related to exiting the domestic financial institutions credit life business and $55 million related to other litigation charges.

Foreign Life Insurance & Retirement Services Results

Foreign Life Insurance & Retirement Services results on a sub-product basis were as follows:

Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income / (Loss)
			(In millions)		
2008					
Life insurance	$ 17,839	$ 1,734	$ (8,837)	$10,736	$ (5,669)
Personal accident	7,055	371	(385)	7,041	1,040
Group products	3,777	510	73	4,360	564
Individual fixed annuities	761	2,320	(2,660)	421	(2,125)
Individual variable annuities	487	(2,974)	24	(2,463)	(147)
Total	$ 29,919	$ 1,961	$ (11,785)	$20,095	$ (6,337)

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American International Group, Inc., and Subsidiaries

Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income / (Loss)
			(In millions)		
2007					
Life insurance	$ 16,630	$ 7,473	$ 85	$24,188	$ 3,898
Personal accident	6,094	354	(3)	6,445	1,457
Group products	2,979	753	(76)	3,656	263
Individual fixed annuities	438	2,283	(171)	2,550	548
Individual variable annuities	460	986	(22)	1,424	31
Total	$ 26,601	$ 11,849	$ (187)	$38,263	$ 6,197
2006					
Life insurance	$ 15,732	$ 5,937	$ 574	$22,243	$ 4,247
Personal accident	5,518	285	55	5,858	1,459
Group products	2,226	648	47	2,921	450
Individual fixed annuities	400	2,027	31	2,458	580
Individual variable annuities	290	861	—	1,151	145
Total	$ 24,166	$ 9,758	$ 707	$34,631	$ 6,881
Percentage Increase/(Decrease) 2008 vs. 2007:					
Life insurance	7%	(77)%	—%	(56)%	—%
Personal accident	16	5	—	9	(29)
Group products	27	(32)	—	19	114
Individual fixed annuities	74	2	—	(83)	—
Individual variable annuities	6	—	—	—	—
Total	12%	(83)%	—%	(47)%	—%
Percentage Increase/(Decrease) 2007 vs. 2006:					
Life insurance	6%	26%	(85)%	9%	(8)%
Personal accident	10	24	—	10	—
Group products	34	16	—	25	(42)
Individual fixed annuities	10	13	—	4	(6)
Individual variable annuities	59	15	—	24	(79)
Total	10%	21%	—%	10%	(10)%

AIG transacts business in most major foreign currencies and therefore premiums and other considerations reported in U.S. dollars vary by volume and from changes in foreign currency translation rates.

The following table summarizes the effect of changes in foreign currency exchange rates on the growth of the Foreign Life Insurance & Retirement Services premiums and other considerations:

	Years Ended December 31, 2008	2007
Growth in original currency*	6.7%	7.6%
Foreign exchange effect	5.8	2.5
Growth as reported in U.S. dollars	12.5%	10.1%

* *Computed using a constant exchange rate each period.*

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2008 and 2007 Comparison

Total revenues for Foreign Life Insurance & Retirement Services in 2008 decreased compared to 2007 primarily due to substantial net realized capital losses and significantly lower net investment income. See Consolidated Results — Net Investment Income and — Net Realized Capital Gains (Losses).

Despite the continued growth in the underlying business in force and the positive effect of foreign exchange, operating income in 2008 also decreased compared to 2007 due to:

- higher losses of $262 million on certain investment linked-products in the U.K. due to mark-to-market trading losses partially offset by a positive change in benefit reserves resulting from changes to the Premier Access Bond product following significant surrender activity as a result of the AIG liquidity issues in mid-September. As allowed under the contract terms, surrenders were suspended to allow sufficient time to develop an appropriate course of action with the respective distribution network and to protect the interest of the fund's policyholders. Policyholders received a cash distribution equal to approximately half of their account value and were given the option to receive the remainder in cash at a discounted amount based on the value of the underlying investments or transfer their account value into a newly created fund. The newly created fund is valued at the net asset value of the underlying investments but provides for a guarantee of a minimum amount should the policyholder remain in the fund until July 2012. Any surrenders prior to July 2012 will be at the net asset value;
- higher benefit costs, net of related DAC unlocking, of $106 million principally related to volatility in the Japanese equity market and declines in interest rates and,
- Foreign Life Insurance & Retirement Services continued its ongoing project to increase standardization of AIG's actuarial systems and processes throughout the world which resulted in a favorable effect on operating income of $151 million for 2008 compared to a $183 million positive effect in 2007.

Partially offsetting these items were higher DAC and SIA benefits of $132 million related to the net realized capital losses and higher surrender charge income related to the temporary spike in policy surrenders during the fourth quarter. Generally, surrenders have returned to normal levels in the foreign operations. In addition, operating income for 2007 included $118 million of remediation activity charges and $67 million of additional claim expense related to an industry-wide regulatory claims review in Japan.

2007 and 2006 Comparison

Total revenues for Foreign Life Insurance & Retirement Services in 2007 increased compared to 2006, primarily due to higher premiums and other considerations and net investment income partially offset by net realized capital losses. Net investment income increased in 2007 compared to 2006 due to higher levels of assets under management, higher policyholder trading gains and higher partnership and mutual fund income.

Operating income decreased in 2007 compared to 2006 principally due to:

- net realized capital losses;
- mark-to-market trading losses of $150 million related to investment-linked products in the U.K.;
- remediation activity charge of $118 million;
- additional claim expense of $67 million relating to an industry-wide regulatory review of claims in Japan;
- additional policyholder benefits expense of $36 million related to a closed block of Japanese business with guaranteed benefits; and
- out-of-period adjustments benefiting 2006 earnings for $332 million related to UCITS and participating policyholder dividend reserves.

These decreases were partially offset by higher net investment income, a $183 million positive effect of changes in actuarial estimates and the positive effect of changes in foreign exchange rates.

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*Foreign Life Insurance & Retirement Services Sales and Deposits**

First year premium, single premium and annuity deposits for Foreign Life Insurance & Retirement Services were as follows:

	Years Ended December 31,			Percentage Increase (Decrease)			
				2008 vs 2007		2007 vs 2006	
(In millions)	2008	2007	2006	U.S. $	Original Currency	U.S. $	Original Currency
First year premium	**$ 4,815**	$ 5,032	$ 4,542	(4)%	**(7)%**	11%	9%
Single premium	**10,738**	15,905	5,283	(32)	**(33)**	201	183
Annuity deposits	**17,665**	19,150	21,916	(8)	**(9)**	(13)	(18)

* *Excludes operations in Brazil.*

2008 and 2007 Comparison

First year premium sales in 2008 declined compared to 2007 primarily due to decreases in life insurance and personal accident sales. In Japan, life insurance sales were lower due to reduced levels of increasing term sales and lower sales in the fourth quarter of 2008 related to AIG's liquidity issues. Also in Japan, personal accident sales declined in the direct marketing distribution channel due to lower response rates resulting from market saturation. In Taiwan, regular premium life insurance sales declined due to a shift in sales to investment-linked and variable annuity products. These declines were partially offset by increases in group products sales, particularly in Japan, Australia and the Middle East.

Single premium sales in 2008 declined compared to 2007 primarily due to lower guaranteed income bond deposits in the U.K. which fell as customers shifted to variable annuity products during the first three quarters of the year and which were significantly negatively affected in the fourth quarter by AIG's liquidity issues. Single premium sales in Asia also dropped as customers became concerned about declining equity markets, particularly in Taiwan, Hong Kong, Singapore and China. A new single premium personal accident and health product launched in Japan during the first quarter of 2008 continues to perform well and sales, which started through banks, are being expanded to the agency channels.

Annuity deposits decreased in 2008 compared to 2007 as the decline in individual variable annuity deposits more than offset the increase in individual fixed annuity deposits. Investment-linked deposits in the U.K. decreased significantly in the fourth quarter of 2008 due to the AIG liquidity issues. Individual variable annuity deposits in Taiwan increased in 2008 compared to 2007 due to the launch of a new variable annuity product. In Japan, individual fixed annuity deposits increased in 2008 compared to 2007 due primarily to a favorable exchange rate environment for non-yen denominated products. However, AIG's liquidity issues and the planned disposition of AIG's Japan life operations negatively affected deposits in the fourth quarter of 2008 as banks suspended the distribution of AIG products. While some banks in Japan have resumed sales of annuity products, most have not. AIG has, therefore, increased sales of annuity deposits through agents.

2007 and 2006 Comparison

First year premium sales in 2007 increased compared to 2006 in both U.S. dollar terms and original currency primarily due to strong investment-oriented product sales in Southeast Asia. This increase was partially offset by declines in Japan resulting from the suspension of increasing term sales and lower personal accident production resulting from changes in local tax regulations.

Single premium sales in 2007 increased dramatically compared to 2006, driven primarily by guaranteed income bond sales in the U.K. and investment-oriented product sales in Hong Kong and Singapore.

Annuity deposits declined in 2007 compared to 2006. Individual fixed annuity deposits were negatively affected by an unfavorable exchange rate environment and a shift to variable annuity products. Individual variable annuity deposits declined in 2007 compared to 2006 in both Europe and Japan. In Europe, lower deposits reflected the effect of tax law changes that reduced tax benefits to policyholders. In Japan, lower sales resulted from increased

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American International Group, Inc., and Subsidiaries

competition and the introduction of a new law that increased sales compliance and customer suitability requirements.

Domestic Life Insurance Results

Domestic Life Insurance results, presented on a sub-product basis were as follows:

Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses) (In millions)	Total Revenues	Operating Income (Loss)(a)
2008					
Life insurance	**$ 2,478**	**$ 1,324**	**$ (8,182)**	**$ (4,380)**	**$ (7,360)**
Home service	**743**	**613**	**(1,422)**	**(66)**	**(1,314)**
Group life/health	**847**	**192**	**(336)**	**703**	**(332)**
Payout annuities *(b)*	**2,131**	**1,242**	**(1,209)**	**2,164**	**(1,026)**
Individual fixed and runoff annuities	**49**	**428**	**(419)**	**58**	**(206)**
Total	**$ 6,248**	**$ 3,799**	**$ (11,568)**	**$ (1,521)**	**$(10,238)**
2007					
Life insurance	$ 2,352	$ 1,528	$ (584)	$ 3,296	$ 226
Home service	767	640	(100)	1,307	216
Group life/health	842	200	(16)	1,026	67
Payout annuities *(b)*	1,820	1,153	(67)	2,906	74
Individual fixed and runoff annuities	55	474	(36)	493	59
Total	$ 5,836	$ 3,995	$ (803)	$ 9,028	$ 642
2006					
Life insurance	$ 2,127	$ 1,377	$ (83)	$ 3,421	$ 654
Home service	790	630	(38)	1,382	282
Group life/health	995	213	(8)	1,200	(159)
Payout annuities *(b)*	1,582	1,004	(51)	2,535	76
Individual fixed and runoff annuities	49	554	(35)	568	64
Total	$ 5,543	$ 3,778	$ (215)	$ 9,106	$ 917
Percentage Increase/(Decrease) 2008 vs. 2007:					
Life insurance	5%	(13)%	—%	—%	—%
Home service	(3)	(4)	—	—	—
Group life/health	1	(4)	—	(31)	—
Payout annuities	17	8	—	(26)	—
Individual fixed and runoff annuities	(11)	(10)	—	—	—
Total	7%	(5)%	—%	—%	—%

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Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses)	Total Revenues	Operating Income (Loss)(a)
			(In millions)		
Percentage Increase/(Decrease) 2007 vs. 2006:					
Life insurance	11%	11%	—%	(4)%	(65)%
Home service	(3)	2	—	(5)	(23)
Group life/health	(15)	(6)	—	(15)	—
Payout annuities	15	15	—	15	(3)
Individual fixed and runoff annuities	12	(14)	—	(13)	(8)
Total	5%	6%	—%	(1)%	(30)%

(a) *2008 operating income (loss) includes goodwill impairment charges of $80 million for life insurance, $280 million for home service and $42 million for group life/health.*

(b) *Premiums and other considerations include structured settlements, single premium immediate annuities and terminal funding annuities.*

2008 and 2007 Comparison

Total revenues for Domestic Life Insurance decreased in 2008 compared to 2007 primarily due to significantly higher net realized capital losses and lower net investment income, partially offset by higher premiums and other considerations. Domestic Life Insurance premiums and other considerations increased due to strong payout annuities sales and growth in life insurance business in force. The growth in payout annuities deposits was driven by structured settlement and terminal funding annuities in both the U.S. and Canada. Net investment income declined due to higher policyholder trading losses offset in policyholder benefits, reduced overall investment yields from increased levels of short-term investments and lower partnership and call and tender income. Partially offsetting these items were growth in underlying businesses and reduced losses due to the phaseout of synthetic fuel production investments. The increase in net realized capital losses was primarily driven by other-than-temporary impairment charges. See Results of Operations — Consolidated Results — Net Investment Income and Net Realized Capital Losses and Investments — Securities Lending Activities.

Domestic Life Insurance reported a significant operating loss in 2008 compared to operating income in 2007 due principally to significantly lower revenues (as described above), goodwill impairment charges and restructuring expenses in 2008. Partially offsetting these items was the continued growth in the underlying business in force and favorable mortality experience in life insurance and payout annuities. Life insurance results were also affected by higher DAC amortization of $30 million related to the change in the unearned revenue liability described above, resulting in a net benefit of $22 million. In addition, 2007 payout annuities operating income was adversely affected by a $30 million adjustment to increase group annuity reserves. Policyholder benefit reserves in 2008 included an increase of $12 million related to the workers' compensation reinsurance program compared to a reduction in expense of $52 million in 2007. Operating income (loss) includes a DAC benefit related to realized capital losses of $364 million in 2008 compared to a benefit of $13 million in 2007.

2007 and 2006 Comparison

Total revenues for Domestic Life Insurance decreased in 2007 compared to 2006 primarily due to net realized capital losses partially offset by higher net investment income and premiums and other considerations. The Domestic Life Insurance premiums and other considerations increased as a result of higher payout annuity deposits and growth in life insurance business in force, partially offset by decreased group life/health premiums from exiting the financial institutions credit life business at the end of 2006.

Operating income decreased in 2007 compared with 2006 due principally to net realized capital losses. In addition, operating income in 2007 was negatively affected by a $52 million charge due to changes in actuarial estimates which included DAC unlocking and refinements in estimates resulting from actuarial valuation system enhancements and a $67 million increase in DAC amortization related to SOP 05-1. These items were partially

offset by a $52 million decrease in policy benefits due to additional reinsurance recoveries associated with Superior National. Operating income in 2006 included a $125 million charge related to the Superior National workers' compensation arbitration, a $66 million loss related to exiting the financial institutions credit life business and a $55 million charge related to litigation reserves.

Domestic Life Insurance Sales and Deposits

Domestic Life Insurance sales and deposits by product* were as follows:

	Years Ended December 31,			Percentage Increase/ (Decrease)	
	2008	2007	2006	2008 vs. 2007	2007 vs. 2006
	(In millions)				
Life insurance					
Periodic premium by product:					
Universal life	**$ 167**	$ 230	$ 334	(27)%	(31)%
Variable universal life	**63**	55	56	15	(2)
Term life	**210**	219	240	(4)	(9)
Whole life/other	**11**	9	13	22	(31)
Total periodic premiums by product	**451**	513	643	(12)	(20)
Unscheduled and single deposits	**267**	426	269	(37)	58
Total life insurance	**718**	939	912	(24)	3
Home service					
Life insurance and accident and health	**87**	96	95	(9)	1
Fixed annuities	**199**	116	107	72	8
Unscheduled and single deposits	**21**	18	19	17	(5)
Total home service	**307**	230	221	33	4
Group life/health	**121**	118	148	3	(20)
Payout annuities	**2,893**	2,612	2,465	11	6
Individual fixed and runoff annuities	**930**	420	641	121	(34)
Total sales and deposits	**$4,969**	$4,319	$4,387	15%	(2)%

* *Life insurance sales include periodic premium from new business expected to be collected over a one-year period and unscheduled and single premiums from new and existing policyholders. Sales of group accident and health insurance represent annualized first year premium from new policies. Annuity sales represent deposits from new and existing policyholders.*

2008 and 2007 Comparison

Total Domestic Life Insurance sales and deposits increased in 2008 compared to 2007 primarily due to strong payout and individual fixed annuities sales, partially offset by a decline in total life insurance premiums. Payout annuities sales increased due to strong terminal funding and structured settlement sales in both the U.S. and Canada. Individual fixed annuities sales increased as a result of the interest rate environment as credited rates offered were more competitive with the rates offered by banks on certificates of deposit. The ratings downgrades and negative publicity related to AIG resulted in lower sales and deposits for the fourth quarter of 2008.

The U.S. life insurance market remains highly competitive and Domestic Life's emphasis on maintaining new business margins has affected sales of term and universal life products, although recent enhancements to term products resulted in an increase in sales prior to AIG's liquidity issues in September 2008.

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Domestic Retirement Services Results

Domestic Retirement Services results, presented on a sub-product basis were as follows:

Years Ended December 31,	Premiums and Other Considerations	Net Investment Income	Net Realized Capital Gains (Losses) (In millions)	Total Revenues	Operating Income (Loss)(a)
2008					
Group retirement products	$ 401	$ 1,461	$ (6,700)	$ (4,838)	$ (6,283)
Individual fixed annuities	128	2,487	(11,928)	(9,313)	(11,646)
Individual variable annuities	584	85	(1,281)	(612)	(1,884)
Individual annuities — runoff *(b)*	15	313	(1,085)	(757)	(1,058)
Total	$ 1,128	$ 4,346	$ (20,994)	$(15,520)	$ (20,871)
2007					
Group retirement products	$ 446	$ 2,280	$ (451)	$ 2,275	$ 696
Individual fixed annuities	96	3,664	(829)	2,931	530
Individual variable annuities	627	166	(45)	748	122
Individual annuities — runoff *(b)*	21	387	(83)	325	(1)
Total	$ 1,190	$ 6,497	$ (1,408)	$ 6,279	$ 1,347
2006					
Group retirement products	$ 386	$ 2,279	$ (144)	$ 2,521	$ 1,017
Individual fixed annuities	122	3,581	(257)	3,446	1,036
Individual variable annuities	531	202	5	738	193
Individual annuities — runoff *(b)*	18	426	(8)	436	77
Total	$ 1,057	$ 6,488	$ (404)	$ 7,141	$ 2,323
Percentage Increase/(Decrease) 2008 vs. 2007:					
Group retirement products	(10)%	(34)%	—%	(315)%	—%
Individual fixed annuities	33	(30)	—	(417)	—
Individual variable annuities	(7)	(48)	—	(182)	—
Individual annuities — runoff	(29)	(19)	—	(331)	—
Total	(5)%	(31)%	—%	(348)%	—%
Percentage Increase/(Decrease) 2007 vs. 2006:					
Group retirement products	16%	—%	—%	(10)%	(32)%
Individual fixed annuities	(21)	2	—	(15)	(49)
Individual variable annuities	18	(18)	—	1	(37)
Individual annuities — runoff	17	(9)	—	(25)	—
Total	13%	—%	—%	(12)%	(42)%

(a) *2008 operating income (loss) includes goodwill impairment charges of $817 million for individual fixed annuities.*

(b) *Primarily represents runoff annuity business sold through discontinued distribution relationships.*

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American International Group, Inc., and Subsidiaries

2008 and 2007 Comparison

Domestic Retirement Services incurred an operating loss in 2008 compared to operating income in 2007, primarily due to significantly increased net realized capital losses, losses on partnership investments as well as DAC unlocking and related reserve strengthening resulting from increased surrenders and deteriorating equity markets and goodwill impairment charges. See Results of Operations — Consolidated Results — Net Investment Income and Net Realized Capital Losses for further information. AIG discontinued its U.S. securities lending program in December 2008. See Investments — Securities Lending Activities.

Both group retirement products and individual fixed annuities reported operating losses in 2008 compared to operating income in 2007 primarily as a result of increased net realized capital losses due to higher other-than-temporary impairment charges and goodwill impairment charges, lower net investment income due to partnership losses, lower yield enhancement income and reduced overall investment yield from increased levels of short-term investments. In addition, DAC and SIA unlocking for group retirement products and individual fixed annuities totaled $210 million and $171 million, respectively, driven by projected increases in surrenders and deteriorating equity markets. These negative effects were partially offset by DAC and SIA benefits of $1.7 billion related to the net realized capital losses compared to $182 million in 2007.

Individual variable annuities reported an operating loss in 2008 compared to operating income in 2007 primarily as a result of significantly increased net realized capital losses, principally due to $822 million of increased embedded policy derivative liability valuations, net of related economic hedges and other-than-temporary impairment charges. In addition, the operating loss included $1.1 billion of DAC unlocking and related reserve strengthening resulting primarily from the deteriorating equity markets. Operating losses also included DAC and SIA benefits of $454 million related to the net realized capital losses compared to $16 million in 2007.

2007 and 2006 Comparison

Total revenues and operating income for Domestic Retirement Services declined in 2007 compared to 2006 primarily due to increased net realized capital losses. Net realized capital losses for Domestic Retirement Services increased due to higher other-than-temporary impairment charges and sales to reposition assets in certain investment portfolios for both group retirement products and individual fixed annuities, as well as from changes in the value of certain individual variable annuity product guarantees and related hedges associated with living benefit features. Changes in actuarial estimates, including DAC unlockings and refinements to estimates resulting from actuarial valuation system enhancements, resulted in a net decrease to operating income of $112 million in 2007.

Domestic Retirement Services Sales and Deposits

The following table presents the account value roll forward for Domestic Retirement Services by product:

	Years Ended December 31,	
	2008	2007
	(In millions)	
Group retirement products		
Balance at beginning of year	$ 68,109	$64,357
Deposits — annuities	5,661	5,898
Deposits — mutual funds	1,520	1,633
Total Deposits	7,181	7,531
Surrenders and other withdrawals	(6,693)	(6,551)
Death benefits	(246)	(262)
Net inflows (outflows)	242	718
Change in fair value of underlying investments, interest credited, net of fees	(11,490)	3,034
Balance at end of year	$ 56,861	$68,109

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American International Group, Inc., and Subsidiaries

	Years Ended December 31,	
	2008	2007
	(In millions)	
Individual fixed annuities		
Balance at beginning of year	$ 50,508	$ 52,685
Deposits	7,276	5,085
Surrenders and other withdrawals	(9,571)	(7,565)
Death benefits	(1,721)	(1,667)
Net inflows (outflows)	(4,016)	(4,147)
Change in fair value of underlying investments, interest credited, net of fees	1,902	1,970
Balance at end of year	$ 48,394	$ 50,508
Individual variable annuities		
Balance at beginning of year	$ 33,108	$ 31,093
Deposits	3,455	4,472
Surrenders and other withdrawals	(4,240)	(4,158)
Death benefits	(480)	(497)
Net inflows (outflows)	(1,265)	(183)
Change in fair value of underlying investments, interest credited, net of fees	(8,250)	2,198
Balance at end of year	$ 23,593	$ 33,108
Total Domestic Retirement Services		
Balance at beginning of year	$151,725	$148,135
Deposits	17,912	17,088
Surrenders and other withdrawals	(20,504)	(18,274)
Death benefits	(2,447)	(2,426)
Net inflows (outflows)	(5,039)	(3,612)
Change in fair value of underlying investments, interest credited, net of fees	(17,838)	7,202
Balance at end of year, excluding runoff	128,848	151,725
Individual annuities runoff	5,079	5,690
Balance at end of year	$133,927	$157,415
General and separate account reserves and mutual funds		
General account reserve	$ 89,140	$ 88,801
Separate account reserve	38,499	60,461
Total general and separate account reserves	127,639	149,262
Group retirement mutual funds	6,288	8,153
Total reserves and mutual funds	$133,927	$157,415

2008 and 2007 Comparison

Deposits in all three product lines were negatively affected by the AIG ratings downgrades and AIG's liquidity issues commencing in September 2008. The decrease in group retirement products deposits was due to a decline in both group annuity deposits and group mutual fund deposits. The improvement in individual fixed annuity deposits was due to a steepened yield curve, providing the opportunity to offer higher interest crediting rates than certificates of deposits and mutual fund money market rates available at the time. Both group retirement products and individual fixed annuities deposits decreased after the AIG ratings downgrades. Individual variable annuity product sales declined due to the AIG ratings downgrades and continued weakness in the equity markets.

Domestic Retirement Services surrenders and other withdrawals increased in all three product lines in 2008 compared to 2007 primarily due to the AIG ratings downgrades and AIG's liquidity issues.

2007 and 2006 Comparison

Domestic Retirement Services deposits increased in 2007 compared to 2006 primarily reflecting higher deposits in group retirement products and individual variable annuities, partially offset by a decrease in individual fixed annuities. Group retirement deposits increased 10 percent in 2007 compared to 2006 as a result of an increased focus on sales management and acquiring outside deposits. Mutual funds deposits increased 20 percent while group annuity deposits increased 8 percent. Individual fixed annuity sales continued to face increased competition from bank deposit products and money market funds offering very competitive short-term rates in the 2007 yield curve environment, and as a result deposits decreased 5 percent in 2007 compared to 2006. Individual variable annuity deposits increased 5 percent in 2007 compared to 2006 despite the discontinuation of a major bank proprietary product.

Domestic Retirement Services surrenders and other withdrawals increased in 2007 compared to 2006 reflecting higher surrenders in both group retirement products and individual fixed annuities. Group retirement surrenders increased as a result of both normal maturing of the business and higher large group surrenders in 2007 compared to 2006. Individual fixed annuity surrenders and withdrawals increased in 2007 due to both an increasing number of policies coming out of their surrender charge period and increased competition from bank deposit products.

The following table presents Domestic Retirement Services reserves by surrender charge category and surrender rates:

At December 31,	Group Retirement Products*	Individual Fixed Annuities	Individual Variable Annuities
		(In millions)	
2008			
No surrender charge	$ 43,797	$ 10,287	$ 8,594
0% – 2%	1,320	3,043	3,097
Greater than 2% – 4%	1,714	6,711	2,187
Greater than 4%	2,710	25,110	7,663
Non-Surrenderable	1,032	3,243	2,052
Total Reserves	$ 50,573	$ 48,394	$ 23,593
Surrender rates	10.5%	18.8%	14.9%
2007			
No surrender charge	$ 49,770	$ 11,316	$ 13,014
0% – 2%	3,284	3,534	5,381
Greater than 2% – 4%	3,757	7,310	5,133
Greater than 4%	2,280	24,956	9,492
Non-Surrenderable	865	3,392	88
Total Reserves	$ 59,956	$ 50,508	$ 33,108
Surrender rates	9.8%	14.6%	12.8%

* *Excludes mutual funds of $6.3 billion and $8.2 billion in 2008 and 2007, respectively.*

Surrender rates increased for group retirement products and individual variable and fixed annuities in 2008 compared to 2007 primarily due to the AIG ratings downgrades and AIG's liquidity issues.

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Deferred Policy Acquisition Costs and Sales Inducement Assets

DAC for Life Insurance & Retirement Services products arises from the deferral of costs that vary with, and are directly related to, the acquisition of new or renewal business. Policy acquisition costs for life insurance products are generally deferred and amortized over the premium paying period in accordance with FAS 60, "Accounting and Reporting by Insurance Enterprises" (FAS 60). Policy acquisition costs that relate to universal life and investment-type products are generally deferred and amortized, with interest in relation to the incidence of estimated gross profits to be realized over the estimated lives of the contracts in accordance with FAS 97. Value of Business Acquired (VOBA) is determined at the time of acquisition and is reported on the consolidated balance sheet with DAC and amortized over the life of the business, similar to DAC. AIG offers sales inducements to contract holders (bonus interest) on certain annuity and investment contracts. Sales inducements are recognized as an asset (SIA) with a corresponding increase to the liability for policyholder contract deposits on the consolidated balance sheet and are amortized over the life of the contract similar to DAC. The deferral of acquisition and sales inducement costs decreased $164 million in 2008 compared to 2007 primarily due to declines in new business production resulting from AIG's liquidity issues. Total amortization expense increased by $1.5 billion in 2008 compared to 2007. The current year amortization includes a $3.2 billion increase to operating income related to net realized capital losses in 2008 compared to $333 million in 2007 reflecting significantly higher other-than-temporary impairment charges. Current year amortization for Domestic Retirement Services also includes adjustments for DAC and SIA unlocking of $961 million related to the continued weakness in the equity markets and DAC and SIA unlocking of $267 million due to higher surrender activity. There was no effect from higher surrender activity in Domestic Life and the Foreign Life operations as the write-off of the DAC was offset by related policy charges. In 2007, amortization expense included changes in actuarial estimates of $732 million, mostly offset in policyholder benefits and claims incurred, which decreased the reported expense. Annualized amortization expense levels in 2008 and 2007 were approximately 13 percent and 10 percent, respectively, of the opening DAC balance.

AIG adopted FAS 159 on January 1, 2008 and elected to apply fair value accounting for an investment-linked product sold principally in Asia. Upon fair value election, all DAC and SIA are written off and there is no further deferral or amortization of DAC and SIA for that product. The amounts of DAC and SIA written off as of January 1, 2008 were $1.1 billion and $299 million, respectively.

The following table summarizes the major components of the changes in DAC/VOBA and SIA:

	Years Ended December 31,					
	2008			2007		
	DAC/VOBA	SIA	Total	DAC/VOBA	SIA	Total
	(In millions)					
Foreign Life Insurance & Retirement Services						
Balance at beginning of year	$ 26,175	$ 681	$26,856	$ 21,153	$404	$21,557
Acquisition costs deferred	5,622	66	5,688	5,640	241	5,881
Amortization (charged) or credited to operating income *(a)*	(4,449)	(90)	(4,539)	(1,879)	10	(1,869)
Change in unrealized gains (losses) on securities	261	(8)	253	301	16	317
Increase (decrease) due to foreign exchange	(352)	(33)	(385)	831	10	841
Other *(b)*	(1,091)	(299)	(1,390)	129	—	129
Balance at end of year	$ 26,166	$ 317	$26,483	$ 26,175	$681	$26,856

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American International Group, Inc., and Subsidiaries

	Years Ended December 31,					
	2008			2007		
	DAC/VOBA	SIA	Total	DAC/VOBA	SIA	Total
	(In millions)					
Domestic Life Insurance						
Balance at beginning of year	$ 6,432	$ 53	$ 6,485	$ 6,006	$ 46	$ 6,052
Acquisition costs deferred	865	16	881	895	15	910
Amortization (charged) or credited to operating income	(324)	(4)	(328)	(652)	(8)	(660)
Change in unrealized gains (losses) on securities	379	—	379	162	—	162
Increase (decrease) due to foreign exchange	(116)	—	(116)	85	—	85
Other *(b)*	—	1	1	(64)	—	(64)
Balance at end of year	$ 7,236	$ 66	$ 7,302	$ 6,432	$ 53	$ 6,485
Domestic Retirement Services						
Balance at beginning of year	$ 5,838	$ 991	$ 6,829	$ 5,651	$ 887	$ 6,538
Acquisition costs deferred	790	210	1,000	741	201	942
Amortization (charged) or credited to operating income *(a)*	(198)	39	(159)	(836)	(151)	(987)
Change in unrealized gains (losses) on securities	779	175	954	282	54	336
Increase (decrease) due to foreign exchange	2	—	2	—	—	—
Balance at end of year	$ 7,211	$1,415	$ 8,626	$ 5,838	$ 991	$ 6,829
Total Life Insurance & Retirement Services						
Balance at beginning of year	$ 38,445	$1,725	$40,170	$ 32,810	$1,337	$34,147
Acquisition costs deferred	7,277	292	7,569	7,276	457	7,733
Amortization (charged) or credited to operating income *(a)*	(4,971)	(55)	(5,026)	(3,367)	(149)	(3,516)
Change in unrealized gains (losses) on securities	1,419	167	1,586	745	70	815
Increase due to foreign exchange	(466)	(33)	(499)	916	10	926
Other *(b)*	(1,091)	(298)	(1,389)	65	—	65
Balance at end of year	$ 40,613	$1,798	$42,411	$ 38,445	$1,725	$40,170

(a) In 2007, Foreign Life Insurance & Retirement Services includes lower amortization of $836 million related to changes in actuarial estimates, mostly offset in Policyholder benefits and claims incurred. Domestic Retirement Services includes higher amortization of $104 million related to changes in actuarial estimates.

(b) In 2008, primarily represents the cumulative effect of adoption of FAS 159. In 2007, includes the cumulative effect of adoption of SOP 05-1.

As AIG operates in various global markets, the estimated gross profits used to amortize DAC, VOBA and SIA are subject to differing market returns and interest rate environments in any single period. The combination of market returns and interest rates may lead to acceleration of amortization in some products and regions and simultaneous deceleration of amortization in other products and regions.

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DAC, VOBA and SIA for insurance-oriented, investment-oriented and retirement services products are reviewed for recoverability, which involves estimating the future profitability of current business. This review involves significant management judgment. If actual future profitability is substantially lower than estimated, AIG's DAC, VOBA and SIA may be subject to an impairment charge and AIG's results of operations could be significantly affected in future periods.

Taiwan

Beginning in 2000, the yield available on Taiwanese 10-year government bonds dropped from approximately 6 percent to 1.5 percent at December 31, 2008. Yields on most other invested assets have correspondingly dropped over the same period. Current sales are focused on products such as:

- variable separate account products which do not contain interest rate guarantees,
- participating products which contain very low implied interest rate guarantees, and
- accident and health policies and riders.

In developing the reserve adequacy analysis for Nan Shan, several key best estimate assumptions have been made:

- Observed historical mortality improvement trends have been projected to 2014;
- Morbidity, expense and termination rates have been updated to reflect recent experience;
- Taiwan government bond rates are expected to remain at current levels for 10 years and gradually increase to best estimate assumptions of a market consensus view of long-term interest rate expectations;
- Foreign assets are assumed to comprise 35 percent of invested assets, resulting in a composite long-term investment assumption of approximately 4.9 percent; and
- The current practice permitted in Taiwan of offsetting positive mortality experience with negative interest margins, thus eliminating the need for mortality dividends, will continue.

Future results of the reserve adequacy tests will involve significant management judgment as to mortality, morbidity, expense and termination rates and investment yields. Adverse changes in these assumptions could accelerate DAC amortization and necessitate reserve strengthening. Future results of the reserve adequacy tests will be affected by the nature, timing and duration of any potential change in investment strategy implemented for Nan Shan.

Financial Services Operations

AIG's Financial Services subsidiaries engage in diversified activities including aircraft leasing, capital markets, and consumer finance and insurance premium finance. Together, the Aircraft Leasing, Capital Markets and Consumer Finance operations generate the majority of the revenues produced by the Financial Services operations. A.I. Credit also contributes to Financial Services income principally by providing insurance premium financing for both AIG's policyholders and those of other insurers.

Capital Markets represents the operations of AIGFP, which engaged as principal in a wide variety of financial transactions, including standard and customized financial products involving commodities, credit, currencies, energy, equities and interest rates. AIGFP also invests in a diversified portfolio of securities and engages in borrowing activities that involve issuing standard and structured notes and other securities and entering into GIAs. Given the extreme market conditions experienced in 2008, downgrades of AIG's credit ratings by the rating agencies, as well as AIG's intent to refocus on its core businesses, AIGFP has begun to unwind its businesses and portfolios including those associated with credit protection written through credit default swaps on super senior risk tranches of diversified pools of loans and debt securities.

Historically, AIG's Capital Markets operations derived a significant portion of their revenues from hedged financial positions entered into in connection with counterparty transactions. AIGFP has also participated as a dealer in a wide variety of financial derivatives transactions. Revenues and operating income of the Capital Markets operations and the percentage change in these amounts for any given period are significantly affected by changes in

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the fair value of AIGFP's assets and liabilities and by the number, size and profitability of transactions entered into during that period relative to those entered into during the comparative period.

Financial Services Results

Financial Services results were as follows:

	Years Ended December 31, 2008	2007	2006	Percentage Increase/(Decrease) 2008 vs. 2007	2007 vs. 2006
	(In millions)				
Revenues:					
Aircraft Leasing	$ **5,075**	$ 4,694	$4,082	8%	15%
Capital Markets	**(40,333)**	(9,979)	(186)	—	—
Consumer Finance	**3,849**	3,655	3,587	5	2
Other, including intercompany adjustments	**314**	321	294	(2)	9
Total	**$(31,095)**	$ (1,309)	$7,777	—%	—%
Operating income (loss):					
Aircraft Leasing	$ **1,116**	$ 873	$ 578	28%	51%
Capital Markets	**(40,471)**	(10,557)	(873)	—	—
Consumer Finance	**(1,261)**	171	668	—	(74)
Other, including intercompany adjustments	**(205)**	(2)	10	—	—
Total	**$(40,821)**	$ (9,515)	$ 383	—%	—%

2008 and 2007 Comparison

Financial Services reported operating losses in 2008 and 2007, primarily due to unrealized market valuation losses related to AIGFP's super senior credit default swap portfolios of $28.6 billion and $11.5 billion in 2008 and 2007, respectively. AIGFP also recorded operating losses of $9.3 billion in 2008 representing the effect of changes in credit spreads on the valuation of AIGFP's assets and liabilities, including $185 million of gains reflected in the unrealized market valuation loss on the super senior credit default swaps. AGF's operating income declined in 2008 compared to 2007 primarily due to increases in the provision for finance receivable losses of $674 million resulting from increases to the allowance for finance receivable losses in response to the higher levels of delinquencies on AGF's finance receivable portfolio, higher net charge-offs, and a goodwill impairment charge of $341 million. As of December 31, 2008, AGF reclassified $1.0 billion of real estate loans to be held for sale due to management's change in intent to hold these receivables. Based on negotiations with prospective purchasers, AGF determined that a write-down of $27 million was necessary to reduce the carrying value of these loans to net realizable value. The sales of these loans were completed in February 2009. As of December 31, 2008, AGF's intent to hold for investment the remainder of the finance receivable portfolio had not changed. AIGCFG also recorded a goodwill impairment charge of $343 million in 2008. The net loss in the Other reporting unit resulted primarily from the change in fair value of interest rate swaps on economically hedged exposures.

ILFC generated strong operating income growth in 2008 compared to 2007, driven to a large extent by a larger aircraft fleet, higher lease rates and lower composite borrowing rates.

2007 and 2006 Comparison

Financial Services reported an operating loss in 2007 compared to operating income in 2006 primarily due to an unrealized market valuation loss of $11.5 billion on AIGFP's super senior credit default swap portfolio, an other-than-temporary impairment charge on AIGFP's available for sale investment securities of $643 million recorded in other income, and a decline in operating income for AGF. AGF's operating income declined in 2007 compared to 2006, due to reduced residential mortgage origination volumes, lower revenues from its mortgage banking activities and increases in the provision for finance receivable losses. In 2007, AGF's mortgage banking operations also recorded a pre-tax charge of $178 million, representing the estimated cost of implementing the Supervisory Agreement entered into with the OTS.

ILFC generated strong operating income growth in 2007 compared to 2006, driven to a large extent by a larger aircraft fleet, higher lease rates and higher utilization.

In 2007, AIGFP began applying hedge accounting under FAS 133 to certain of its interest rate swaps and foreign currency forward contracts that hedge its investments and borrowings and AGF and ILFC began applying hedge accounting to most of their derivatives that hedge floating rate and foreign currency denominated borrowings. Prior to 2007, hedge accounting was not applied to any of AIG's derivatives and related assets and liabilities. Accordingly, revenues and operating income were exposed to volatility resulting from differences in the timing of revenue recognition between the derivatives and the hedged assets and liabilities.

Capital Markets Results

<u>2008 and 2007 Comparison</u>

AIGFP's operating loss increased in 2008 compared to 2007 primarily related to its super senior multi-sector CDO credit default swap portfolio and the effect of credit spreads on the valuation of its assets and liabilities. The 2008 net operating loss was driven by the extreme market conditions experienced during the year and the effects of downgrades of AIG's credit ratings by the rating agencies. The net operating results were also affected by internal efforts during the first half of 2008 intended to preserve liquidity. As a result of AIG's intention to refocus on its core business, AIGFP began unwinding its businesses and portfolios. For a further discussion, see Overview — Outlook — Financial Services.

AIG recognized an unrealized market valuation loss of $28.6 billion in 2008 compared to $11.5 billion in 2007, representing the change in fair value of its super senior credit default swap portfolio. The principal components of the loss recognized in 2008 were as follows:

- Approximately $25.7 billion relates to derivatives written on the super senior tranches of multi-sector CDOs. The material decline in the fair value of these derivatives was caused by significant deterioration in the pricing and credit quality of RMBS, CMBS and CDO securities. Included in this amount is a loss of $4.3 billion with respect to the change in fair value of transactions outstanding at December 31, 2008 having a net notional amount of $12.6 billion. Also included in the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio are losses of approximately $995 million that were subsequently realized through payments to counterparties to acquire at par value the underlying CDO securities with fair values that were less than par. Specifically, during the second quarter of 2008, AIGFP issued new maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts), with a net notional amount of $5.4 billion on the super senior security issued by a CDO of AAA-rated commercial mortgage-backed securities (CMBS) pursuant to a facility that was entered into in 2005. All of these 2a-7 Puts and other 2a-7 Puts in AIGFP's multi-sector CDO super senior credit default swap portfolio with a combined net notional amount of $9.4 billion were exercised by the counterparties during 2008. In addition, AIGFP extinguished its obligations with respect to one other credit default swap by purchasing the protected CDO security at its principal amount outstanding of $162 million. These transactions represent all of the payments that have been made to counterparties through December 31, 2008 on the super senior credit default swap portfolio of AIGFP under the settlement provisions of these contracts. AIGFP has not committed to enter into any new 2a-7 Puts.

  Further, included in the unrealized market valuation losses on AIGFP's super senior credit default swap portfolio are losses of approximately $21.1 billion that were subsequently realized through the termination of contracts through the ML III transaction. See Note 5 to the Consolidated Financial Statements.

- Approximately $2.3 billion relates to derivatives written as part of the corporate arbitrage portfolio. The decline in the fair value of these derivatives was caused by the continued significant widening in corporate credit spreads.

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- Approximately $379 million relates to the decline in fair value of a transaction in the regulatory capital portfolio where AIGFP no longer believes the credit default swap is used by the counterparty to obtain regulatory capital relief.

See Critical Accounting Estimates — Valuation of Level 3 Assets and Liabilities and Note 5 to the Consolidated Financial Statements for a discussion of AIGFP's super senior credit default swap portfolio.

During 2008, AIGFP recognized a loss of $888 million on credit derivatives which are not included in the super senior credit default swap portfolio, compared to a net gain of $370 million in 2007.

The following table presents AIGFP's credit valuation adjustment gains (losses) for the year ended December 31, 2008 (excluding intercompany transactions):

Counterparty Credit Valuation Adjustment on Assets	(In millions)	AIG's Own Credit Valuation Adjustment on Liabilities	
Trading securities	$ (8,928)	Term notes	$ 248
Loans and other assets	(61)	Hybrid term notes	646
Derivative assets	(1,667)	GIAs	(415)
		Other liabilities	55
		Derivative liabilities*	860
Decrease in assets	$(10,656)	Decrease in liabilities	$1,394
Net pre-tax decrease to other income	$ (9,262)		

* *Includes super senior credit default swap portfolio*

Capital Markets' operating loss for 2008 includes a loss of $9.3 billion representing the effect of changes in credit spreads on the valuation of AIGFP's assets and liabilities, including $185 million of gains reflected in the unrealized market valuation loss on super senior credit default swaps. Historically, AIG's credit spreads and those on AIGFP's assets moved in a similar fashion. This relationship began to diverge during second quarter of 2008 and continued to diverge through the end of the year. While AIG's credit spreads widened significantly during 2008, the credit spreads on the ABS and CDO products, which represent a significant portion of AIGFP's investment portfolio, widened even more. The losses on AIGFP's assets more than offset the net gain on its liabilities that was driven by the significant widening in AIG's credit spreads. The net gain on AIGFP's liabilities was reduced by the effect of posting collateral and the early terminations of GIAs, term notes and hybrid term notes. Included in the 2008 operating loss is the transition amount of $291 million related to the adoption of FAS 157 and FAS 159.

The most significant component of Capital Markets operating expenses is compensation. Due to the significant losses recognized by AIGFP during 2008, the entire amount of $563 million accrued under AIGFP's various deferred compensation plans and special incentive plan was reversed in 2008. Total compensation expense in 2008 was $426 million including retention awards.

2007 and 2006 Comparison

Capital Markets reported an operating loss in 2007 compared to operating income in 2006, primarily due to fourth quarter 2007 unrealized market valuation losses related to AIGFP's super senior credit default swap portfolio principally written on multi-sector CDOs and an other-than-temporary impairment charge on AIGFP's investment portfolio of CDOs of ABS. These losses were partially offset by the effect of applying hedge accounting to certain hedging activities beginning in 2007, as described below, and net unrealized market gains related to certain credit default swaps purchased against the AAA to BBB-rated risk layers on portfolios of reference obligations. AIGFP experienced higher transaction flow in 2007 in its rate and currency products which contributed to its revenues.

Included in AIGFP's net operating loss was a net unrealized market valuation gain of $401 million on certain credit default swaps and embedded credit derivatives in credit-linked notes in 2007. In these transactions, AIGFP purchased protection at the AAA - to BBB-rated risk layers on portfolios of reference obligations that include multi-sector CDO obligations.

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During the fourth quarter of 2007, certain of AIGFP's available for sale investments in super senior and AAA-rated bonds issued by multi-sector CDOs experienced severe declines in their fair value. As a result, AIGFP recorded an other-than-temporary impairment charge in other income of $643 million. Notwithstanding AIG's intent and ability to hold such securities at such time until they recover in value, and despite structures which indicated that a substantial amount of the securities should continue to perform in accordance with their original terms, AIG concluded that it could not reasonably assert that the recovery period would be temporary. See also Investments — Financial Services Invested Assets and Note 5 to the Consolidated Financial Statements.

The change in fair value of AIGFP's credit default swaps that reference CDOs and the decline in fair value of its investments in CDOs were caused by the significant widening in spreads in the fourth quarter on asset-backed securities, principally those related to U.S. residential mortgages, the severe liquidity crisis affecting the structured finance markets and the effects of rating agency downgrades on those securities.

In addition, in 2007 AIGFP recognized a net gain of $211 million related to hedging activities that did not qualify for hedge accounting treatment under FAS 133, compared to a net loss of $1.82 billion in 2006.

The year ended December 31, 2007 included an out-of-period charge of $380 million to reverse net gains recognized in previous periods on transfers of available for sale securities among legal entities consolidated within AIGFP, and a $166 million reduction in fair value at March 31, 2007 of certain derivatives that were an integral part of, and economically hedge, the structured transactions that were affected by the proposed regulations issued by the United States Department of the Treasury. The net loss on AIGFP's derivatives recognized in 2006 included an out-of-period charge of $223 million related to the remediation of the material weakness in internal control over accounting for certain derivative transactions under FAS 133. The net loss also reflects the effect of increases in U.S. interest rates and a weakening of the U.S. dollar on derivatives hedging AIGFP's assets and liabilities.

Financial market conditions in 2007 were characterized by increases in global interest rates, widening of credit spreads, higher equity valuations and a slightly weaker U.S. dollar.

The most significant component of Capital Markets operating expenses is compensation, which was approximately $423 million and $544 million in 2007 and 2006, respectively. The amount of compensation was not affected by gains and losses arising from derivatives not qualifying for hedge accounting treatment under FAS 133.

Asset Management Operations

AIG's Asset Management operations comprise a wide variety of investment-related services and investment products. These services and products are offered to individuals, pension funds and institutions (including AIG subsidiaries) globally through AIG's Spread-Based Investment business, Institutional Asset Management, and Brokerage Services and Mutual Funds businesses. Also included in Asset Management operations are the results of certain SunAmerica sponsored partnership investments.

The revenues and operating income (loss) for this segment are affected by the general conditions in the equity and credit markets. In addition, net realized gains and carried interest are contingent upon various fund closings, maturity levels and market conditions. In the Institutional Asset Management business, carried interest, computed in accordance with each fund's governing agreement, is based on the investment's performance over the life of each fund. Unrealized carried interest is recognized based on each fund's performance as of the balance sheet date. Future fund performance may negatively affect previously recognized carried interest.

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Asset Management Results

Asset Management results were as follows:

	Years Ended December 31,			Percentage Increase/(Decrease)	
	2008	2007	2006	2008 vs. 2007	2007 vs. 2006
	(In millions)				
Revenues:					
Spread-Based Investment business	**$(6,918)**	$2,023	$2,713	—%	(25)%
Institutional Asset Management	**1,938**	2,900	1,240	(33)	134
Brokerage Services and Mutual Funds	**273**	322	293	(15)	10
Other Asset Management	**181**	380	297	(52)	28
Total	**$(4,526)**	$5,625	$4,543	—%	24%
Operating income (loss):					
Spread-Based Investment business	**$(8,543)**	$ (89)	$ 732	—%	—%
Institutional Asset Management	**(848)**	784	438	—	79
Brokerage Services and Mutual Funds	**28**	100	87	(72)	15
Other Asset Management	**176**	369	281	(52)	31
Total	**$(9,187)**	$1,164	$1,538	—%	(24)%

2008 and 2007 Comparison

Asset Management recognized an operating loss in 2008 compared to operating income in 2007, primarily due to higher other-than-temporary impairment charges on fixed maturity securities, higher mark-to-market losses on unhedged derivatives, significantly lower partnership income, higher equity losses and realized losses on real estate investments, and lower net carried interest revenues. Partially offsetting these declines were increases in net foreign exchange gains on foreign currency denominated GIC and MIP liabilities. Included in the Institutional Asset Management operating income during 2007 was a gain on the sale of a portion of AIG's investment in The Blackstone Group L.P. (Blackstone) in connection with its initial public offering.

As noted in the Asset Disposition section of Management's Discussion and Analysis of Financial Condition and Results of Operations, certain businesses within the Asset Management segment are being divested. The $9.2 billion operating loss for 2008 includes approximately $4.5 billion in net operating losses related to businesses which are expected to be retained by AIG, including the MIP. AIG will retain the businesses that manage the short duration asset and liability management and traditional fixed income investment services for the insurance companies.

2007 and 2006 Comparison

Asset Management revenues increased in 2007 compared to 2006 primarily due to increased partnership income, management fees, and carried interest.

Asset Management operating income decreased in 2007 compared to 2006, due to foreign exchange, interest rate and credit-related mark-to-market losses and other-than-temporary impairment charges on fixed income investments. These other-than-temporary impairment charges were due primarily to changes in market liquidity and spreads. Partially offsetting these decreases were higher partnership income, increased gains on real estate investments and a gain of $398 million on the sale of a portion of AIG's investment in Blackstone in connection with its initial public offering. Revenues increased in 2007 compared to 2006 periods as a result of consolidating several warehoused investments. AIG consolidates the operating results of warehoused investments until such time as they are sold or otherwise divested. A portion of these amounts is offset in minority interest expense, which is not a component of operating income (loss).

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American International Group, Inc., and Subsidiaries

Spread-Based Investment Business Results

2008 and 2007 Comparison

The Spread-Based Investment business reported increased operating losses in 2008 compared to 2007 due to significantly higher net realized capital losses and lower partnership income. Net realized capital losses were $8.6 billion in 2008 compared to $1.3 billion in 2007. The increase in net realized capital losses for 2008 primarily consists of an increase of $6.4 billion in other-than-temporary impairment charges on fixed maturity securities for both the GIC and MIP, higher net mark-to-market losses of $1.2 billion on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment for both the GIC and MIP and higher net mark-to-market losses of $374 million on credit default swap investments held by the MIP due to the widening of corporate credit spreads. The MIP credit default swaps are comprised of single-name investment grade corporate exposures. AIG enters into derivative arrangements to hedge the effect of changes in currency and interest rates associated with the fixed and floating rate and foreign currency denominated obligations issued under these programs. Some of these hedging relationships qualify for hedge accounting treatment, while others do not, and although being effective economic hedges, creates volatility in operating results. Partially offsetting these declines were increased net foreign exchange gains on foreign denominated GIC reserves and MIP liabilities of $1.3 billion.

The increase in other-than-temporary impairment charges on fixed maturity securities held in the GIC and MIP portfolios were $3.2 billion for the GIC and $3.2 billion for the MIP in 2008, primarily resulting from severity and credit losses and the change in AIG's intent to hold securities to recovery related to both the U.S. securities lending portfolio and its general portfolios. See Investments — Portfolio Review — Other-Than-Temporary Impairments.

In the GIC program, income from partnership investments decreased $1.4 billion for 2008 compared to 2007 due to significantly higher returns in the 2007 period and weaker market conditions in 2008. GIC income was also affected by higher net mark-to-market losses of $676 million on interest rate and foreign exchange hedges not qualifying for hedge accounting treatment. Offsetting these declines were net foreign exchange gains on foreign-denominated GIC reserves which increased by $1.2 billion in 2008 compared to 2007 as a result of the strengthening of the U.S. dollar. As noted below, a significant portion of these GIC reserves mature in the next twelve months. The derivative losses included net mark-to-market losses on interest rate and foreign exchange derivatives used to economically hedge the effect of interest rate and foreign exchange rate movements on GIC reserves. Although these economic hedges are partially effective in hedging the interest rate and foreign exchange risk, AIG has not applied hedge accounting treatment.

The MIP recognized an operating loss, due to net realized capital losses, of $4.8 billion in 2008, and an operating loss of $794 million in 2007.

AIG did not issue any additional debt to fund the MIP in 2008 and does not intend to issue any additional debt for the foreseeable future. Through December 31, 2008, the MIP had cumulative debt issuances of $13.4 billion. During 2007, AIG issued the equivalent of $8.1 billion of securities to fund the MIP in the Euromarkets and the U.S. public and private markets. See Note 13 to the Consolidated Financial Statements for a schedule of maturities of the MIP debt.

The GIC program is in runoff with no new GICs issued subsequent to 2005. The anticipated runoff of the domestic GIC portfolio was as follows:

At December 31,	Less Than One Year	1-3 Years	3+-5 Years	Over Five Years	Total
			(In billions)		
Domestic GICs	$ 6.0	$ 2.0	$ 3.0	$ 3.8	$14.8

2007 and 2006 Comparison

The Spread-Based Investment business reported an operating loss in 2007 compared to operating income in 2006 due to foreign exchange, interest rate and credit-related mark-to-market losses and other-than-temporary impairment charges on fixed income investments, partially offset by increased partnership income. In 2007, the GIC program incurred foreign exchange losses of $526 million on foreign-denominated GIC reserves. Partially offsetting these losses were $269 million of net mark-to-market gains on derivative positions. These net gains included mark-to-market gains on foreign exchange derivatives used to economically hedge the effect of foreign

exchange rate movements on foreign-denominated GIC reserves and mark-to-market losses on interest rate hedges that did not qualify for hedge accounting treatment.

The MIP experienced mark-to-market losses of $193 million due to interest rate and foreign exchange derivative positions that, while partially effective in hedging interest rate and foreign exchange risk, did not qualify for hedge accounting treatment and an additional $98 million due to credit default swap losses. The mark-to-market losses for 2007 were driven primarily by a decline in short-term interest rates, the decline in the value of the U.S. dollar and widening credit spreads.

Also contributing to the operating loss were other-than-temporary impairment charges on various fixed maturity investments held in the GIC and MIP portfolios of approximately $836 million as a result of movements in credit spreads and decreased market liquidity. See Investments — Portfolio Review — Other-Than-Temporary Impairments. These losses were partially offset by an increase in partnership income associated with the GIC.

Institutional Asset Management Results

<u>2008 and 2007 Comparison</u>

Institutional Asset Management recognized an operating loss in 2008 compared to operating income in 2007, primarily resulting from the difficult market conditions in 2008 in the private equity, hedge fund and real estate environments. The operating loss reflects higher net equity losses and impairment charges of $330 million and lower net realized capital gains of $211 million on real estate investments, and lower carried interest of $209 million. Due to the current global real estate market conditions, several of AIG Global Real Estate's investments were deemed to be impaired, and several equity investments were written off during 2008. These impairments and write-offs totaled $269 million. The reduction in carried interest revenues was driven by lower net unrealized carry due to higher fund performance in 2007 and significantly lower fund performance in 2008.

Increased losses from warehoused investments of $92 million were incurred as such investments were not able to be sold or otherwise divested as originally contemplated. Such assets are now considered proprietary investments of the Institutional Asset Management business. Total operating losses including funding costs from these investments for 2008 and 2007 were $257 million and $165 million, respectively, with 2008 reflecting a full-year of such losses compared to a partial year in 2007. Of these operating losses, $142 million and $35 million for 2008 and 2007, respectively, are offset in minority interest expense, which is not a component of operating income (loss).

Additional losses resulted from a decrease in securities lending fees of $60 million as the U.S. securities lending program was terminated and restructuring-related expenses of $43 million primarily related to employee-related costs associated with the intended divestment of various asset management businesses, including AIG Private Bank. Included in the 2007 results was a $398 million gain related to the sale of a portion of AIG's investment in Blackstone.

AIG's unaffiliated client assets under management, including retail mutual funds and institutional accounts, were $68.9 billion and $97.6 billion at December 31, 2008 and December 31, 2007, respectively. The decline from December 31, 2007 reflects lower asset values due to the significant deterioration in the credit and equity markets during 2008 as well as the effect of net client outflows. Although there was a significant decline in end of period unaffiliated client assets under management, average assets under management decreased nominally in 2008 compared to 2007 and resulted in slightly lower base management fees.

<u>2007 and 2006 Comparison</u>

Operating income for Institutional Asset Management increased in 2007 compared to 2006 reflecting increased carried interest revenues driven by higher valuations of portfolio investments that are generally associated with improved performance in the equity markets. The increase also reflects the $398 million gain from the sale of a portion of AIG's investment in Blackstone in connection with its initial public offering. Also contributing to this increase were higher base management fees driven by higher levels of third-party assets under management. Partially offsetting these increases were the operating losses from warehousing activities. The consolidated warehoused private equity investments are not wholly owned by AIG and thus, a significant portion of the effect of consolidating these operating losses is offset in minority interest, which is not a component of operating income.

Brokerage Services and Mutual Funds

Revenues and operating income related to Brokerage Services and Mutual Fund activities decreased in 2008 from 2007 due to lower fee income as a result of a lower asset base and a decline in commission income resulting from difficult market conditions. In addition, restructuring expenses of $24 million were recorded in 2008 primarily related to employee costs.

Other Asset Management Results

Revenues and operating income related to Other Asset Management activities declined in 2008 from 2007 and increased in 2007 from 2006, due to changes in partnership income driven by weaker market conditions in 2008 and 2006 compared to strong market conditions in 2007.

Critical Accounting Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires the application of accounting policies that often involve a significant degree of judgment. AIG considers that its accounting policies that are most dependent on the application of estimates and assumptions, and therefore viewed as critical accounting estimates, to be those relating to items considered by management in the determination of AIG's ability to continue as a going concern, liability for general insurance unpaid claims and claims adjustment expenses, future policy benefits for life and accident and health contracts, recoverability of DAC, estimated gross profits for investment-oriented products, the allowance for finance receivable losses, flight equipment recoverability, other-than-temporary impairments, goodwill impairment, estimates with respect to income taxes and fair value measurements of certain financial assets and liabilities, including credit default swaps. These accounting estimates require the use of assumptions about matters, some of which are highly uncertain at the time of estimation. To the extent actual experience differs from the assumptions used, AIG's results of operations would be directly affected.

The major categories for which assumptions are developed and used to establish each critical accounting estimate are highlighted below.

AIG's Ability to Continue as a Going Concern

When assessing AIG's ability to continue as a going concern, management must make judgments and estimates about the following:

- the marketability of assets to be disposed of and the timing and amount of related cash proceeds to be used to repay indebtedness;
- plans to raise new funds or restructure debt;
- projections of future profitability and the timing and amount of cash flows from operating activities;
- the funding needs of regulated subsidiaries;
- AIG's ability to comply with debt covenants;
- plans to reduce expenditures;
- the effects of ratings agency actions on collateral requirements and other contractual conditions; and
- the future regulatory, business, credit, and competitive environments in which AIG operates around the world.

These factors individually and collectively will have a significant effect on AIG's ability to generate sufficient cash to repay indebtedness as it becomes due and profitably operate its businesses as it executes its restructuring initiatives.

Liability for Unpaid Claims and Claims Adjustment Expenses (General Insurance):

- *Loss trend factors:* used to establish expected loss ratios for subsequent accident years based on premium rate adequacy and the projected loss ratio with respect to prior accident years.
- *Expected loss ratios for the latest accident year:* in this case, accident year 2008 for the year-end 2008 loss reserve analysis. For low-frequency, high-severity classes such as excess casualty, expected loss ratios generally are utilized for at least the three most recent accident years.
- *Loss development factors:* used to project the reported losses for each accident year to an ultimate amount.
- *Reinsurance recoverable on unpaid losses:* the expected recoveries from reinsurers on losses that have not yet been reported and/or settled.

For discussion of sensitivity analysis on the reserve for unpaid claims and claims adjustment expenses, see Results of Operations — Segment Results — General Insurance Operations — Liability for Unpaid Claims and Claims Adjustment Expense.

Future Policy Benefits for Life and Accident and Health Contracts (Life Insurance & Retirement Services):

- *Interest rates:* which vary by geographical region, year of issuance and products.
- *Mortality, morbidity and surrender rates:* based upon actual experience by geographical region modified to allow for variation in policy form, risk classification and distribution channel.

Periodically, the net benefit reserves (policy benefit reserves less DAC) established for Life Insurance & Retirement Services companies are tested to ensure that, including consideration of future expected premium payments, they are adequate to provide for future policyholder benefit obligations. The assumptions used to perform the tests are current best-estimate assumptions as to policyholder mortality, morbidity, terminations, company maintenance expenses and invested asset returns. For long duration traditional business, a "lock-in" principle applies, whereby the assumptions used to calculate the benefit reserves and DAC are set when a policy is issued and do not change with changes in actual experience. These assumptions include margins for adverse deviation in the event that actual experience might deviate from these assumptions. For business in-force outside of North America, 52 percent of total policyholder benefit liabilities at December 31, 2008 resulted from traditional business where the lock-in principle applies. In most foreign locations, various guarantees are embedded in policies in force that may remain applicable for many decades into the future.

As experience changes over time, the best-estimate assumptions are updated to reflect observed changes. Because of the long-term nature of many of AIG's liabilities subject to the lock-in principle, small changes in certain of the assumptions may cause large changes in the degree of reserve adequacy. In particular, changes in estimates of future invested asset return assumptions have a large effect on the degree of reserve adequacy.

Deferred Policy Acquisition Costs (Life Insurance & Retirement Services):

- *Recoverability:* based on current and future expected profitability, which is affected by interest rates, foreign exchange rates, mortality/morbidity experience, expenses, investment returns and policy persistency.

Deferred Policy Acquisition Costs (General Insurance):

- *Recoverability:* based upon the current terms and profitability of the underlying insurance contracts.

Estimated Gross Profits for Investment-Oriented Products (Life Insurance & Retirement Services):

- *Estimated gross profits:* to be realized over the estimated duration of the contracts (investment-oriented products) affect the carrying value of DAC, unearned revenue liability, SIAs and associated amortization patterns. Estimated gross profits include investment income and gains and losses on investments less required interest, actual mortality and other expenses.

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Allowance for Finance Receivable Losses (Financial Services):

- *Historical defaults and delinquency experience:* utilizing factors, such as delinquency ratio, allowance ratio, charge-off ratio and charge-off coverage.
- *Portfolio characteristics:* portfolio composition and consideration of the recent changes to underwriting criteria and portfolio seasoning.
- *External factors:* consideration of current economic conditions, including levels of unemployment and personal bankruptcies.
- *Migration analysis:* empirical technique measuring historical movement of similar finance receivables through various levels of repayment, delinquency, and loss categories to existing finance receivable pools.

Flight Equipment Recoverability (Financial Services):

- *Expected undiscounted future net cash flows:* based upon current lease rates, projected future lease rates and estimated terminal values of each aircraft based on expectations of market participants.

Other-Than-Temporary Impairments:

AIG evaluates its available for sale, equity method and cost method investments for impairment such that a security is considered a *candidate* for other-than-temporary impairment if it meets any of the following criteria:

- Trading at a significant (25 percent or more) discount to par, amortized cost (if lower) or cost for an extended period of time (nine consecutive months or longer);
- The occurrence of a discrete credit event resulting in (i) the issuer defaulting on a material outstanding obligation; (ii) the issuer seeking protection from creditors under the bankruptcy laws or any similar laws intended for court supervised reorganization of insolvent enterprises; or (iii) the issuer proposing a voluntary reorganization pursuant to which creditors are asked to exchange their claims for cash or securities having a fair value substantially lower than par value of their claims; or
- AIG may not realize a full recovery on its investment, regardless of the occurrence of one of the foregoing events.

The determination that a security has incurred an other-than-temporary decline in value requires the judgment of management and consideration of the fundamental condition of the issuer, its near-term prospects and all the relevant facts and circumstances. The above criteria also consider circumstances of a rapid and severe market valuation decline, such as that experienced in current credit markets, in which AIG could not reasonably assert that the impairment period would be temporary (severity losses). For further discussion, see Investments — Portfolio Review — Other-Than-Temporary Impairments.

At each balance sheet date, AIG evaluates its available for sale securities holdings with unrealized losses. When AIG does not intend to hold or lacks the ability to hold such securities until they have recovered their cost basis, AIG records the unrealized loss in income. If a loss is recognized from a sale subsequent to a balance sheet date pursuant to changes in circumstances, the loss is recognized in the period in which the intent to hold the securities to recovery no longer existed.

In periods subsequent to the recognition of an other-than-temporary impairment charge for fixed maturity securities, which is not credit or foreign exchange related, AIG generally accretes into income the discount or amortizes the reduced premium resulting from the reduction in cost basis over the remaining life of the security.

Goodwill Impairment

Goodwill is the excess of the cost of an acquired business over the fair value of the identifiable net assets of the acquired business. Goodwill is tested for impairment annually, or more frequently if circumstances indicate an impairment may have occurred. During 2008, AIG performed goodwill impairment tests at June 30, September 30, and December 31.

The impairment assessment involves a two-step process in which an initial assessment for potential impairment is performed and, if potential impairment is present, the amount of impairment is measured and recorded. Impairment is tested at the reporting unit level or, when all reporting units that comprise an operating segment have similar economic characteristics, impairment is tested at the operating segment level.

Management initially assesses the potential for impairment by estimating the fair value of each of AIG's reporting units or operating segments and comparing the estimated fair values with the carrying amounts of those reporting units, including allocated goodwill. The estimate of a reporting unit's fair value may be based on one or a combination of approaches including market-based earning multiples of the unit's peer companies, discounted expected future cash flows, external appraisals or, in the case of reporting units being considered for sale, third-party indications of fair value, if available. Management considers one or more of these estimates when determining the fair value of a reporting unit to be used in the impairment test. As part of the impairment test, management compares the sum of the estimated fair values of AIG's reporting units with AIG's fully diluted common stock market capitalization as a basis for concluding on the reasonableness of the estimated reporting unit fair values.

If the estimated fair value of a reporting unit exceeds its carrying value, goodwill is not impaired. If the carrying value of a reporting unit exceeds its estimated fair value, goodwill associated with that reporting unit potentially is impaired. The amount of impairment, if any, is measured as the excess of the carrying value of goodwill over the estimated fair value of the goodwill. The estimated fair value of the goodwill is measured as the excess of the fair value of the reporting unit over the amounts that would be assigned to the reporting unit's assets and liabilities in a hypothetical business combination. An impairment charge is recognized in income to the extent of the excess. During 2008, AIG recorded an aggregate goodwill impairment charge of $4.1 billion. This impairment charge was primarily attributable to declines in estimated fair values of reporting units in the Property and Casualty Group, Domestic Life Insurance and Domestic Retirement Services, Consumer Finance and Capital Markets businesses attributable to the uncertain economic environment during the 2008 fourth quarter.

Management observed a narrowing of the fair values over the carrying values of the Foreign General Insurance and Institutional Asset Management reporting units during the fourth quarter of 2008. Fair value exceeded book value in the Foreign General Insurance, Foreign Life Insurance & Retirements Services — Japan & Other, and Institutional Asset Management reporting units as of December 31, 2008; therefore, the goodwill of these reporting units was considered not impaired. AIG's stock price, along with the stock prices of other companies in the financial services industry, including insurers, has continued to decline in 2009. AIG will continue to monitor overall competitive, business and economic conditions, and other events or circumstances that might result in an impairment of goodwill in the future.

Valuation Allowance on Deferred Tax Assets:

At December 31, 2008, AIG recorded a net deferred tax asset after valuation allowance of $11 billion compared to a net deferred tax liability of $5.3 billion at December 31, 2007. SFAS 109 permits this asset to be recorded if the asset meets a more likely than not standard (i.e. more than 50 percent likely) that the asset will be realized. Realization of AIG's net deferred tax asset depends on AIG's ability to generate sufficient future taxable income of the appropriate character within carryforward periods of the jurisdictions in which the net operating and capital losses, tax credits and deductible temporary differences were incurred. Because the realization of the deferred tax asset relies on a projection of future income, AIG views this as a critical accounting estimate.

In making this estimate, AIG considered its ability to execute its divestiture plan at the values anticipated and within the timeframe expected. The realization of the deferred tax asset is highly dependent on the ability of AIG to generate significant gains from these transactions.

AIG is also relying upon producing taxable operating profits from the businesses to be retained, principally Commercial Insurance and Foreign General Insurance. AIG has evaluated its forecasts of future operating income and determined that there would be sufficient operating income, inclusive of gains on the divestiture of businesses. There are many risk factors that could affect the attainment of AIG's budgeted results. See Item 1A. Risk Factors.

When making its assessment about the realization of its deferred tax assets at December 31, 2008, AIG considered all available evidence, including (i) the nature, frequency, and severity of current and cumulative financial reporting losses, (ii) actions completed during 2008 and expected to be completed during 2009 that are

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designed to eliminate or limit a recurrence of the factors that contributed to the recent cumulative losses, giving greater weight to actions completed through December 31, 2008 and to the expectation that strategies will be executed in 2009 to mitigate credit losses in the future on certain classes of invested assets, (iii) the carryforward periods for the net operating and capital loss and foreign tax credit carryforwards, (iv) the sources and timing of future taxable income, giving greater weight to discrete sources and to earlier future years in the forecast period, and (v) tax planning strategies that would be implemented, if necessary, to accelerate taxable amounts.

In assessing future GAAP taxable income, AIG considered its strong earnings history exclusive of the recent losses on the AIGFP super senior credit default swap portfolio and from the securities lending program. AIG also considered the completed transactions with the NY Fed and the United States Department of the Treasury, including (i) amendment to the Fed Credit Agreement designed to reduce the interest rate payable on outstanding borrowing and undrawn amounts; (ii) the transfer of RMBS related to AIG's U.S. securities lending program to ML II; and (iii) the termination of multi-sector credit default swap transactions and sale of underlying CDOs to ML III.

In addition, AIG also considered the proposed transactions with the NY Fed and the United States Department of the Treasury announced on March 2, 2009, including (i) the modification of the terms of the Series D Preferred Stock; (ii) establishment of a equity capital commitment facility for the sales of Series F Preferred Stock to the United States Department of the Treasury, along with warrants to purchase shares of common stock; and (iii) amendment to the Fed Credit Agreement designed to reduce the interest rate payable on outstanding borrowing by revising the LIBOR floor. These transactions are designed to enhance AIG's ability to generate taxable income from the sales of businesses under its asset disposition plan, continue the earnings strength of the insurance businesses it intends to sell, and underscore the United States Government's commitment to the orderly restructuring of AIG over time in the face of continuing market dislocations and economic deterioration.

The forecast of taxable income was prepared using budgets submitted by each of AIG's significant operating units for management planning purposes and is consistent with the forecast used in AIG's going concern analysis. AIG's profitability in any given period can be materially affected by conditions in global financial markets, economic conditions, catastrophes and other events around the world and, currently, AIG-specific events. Further, the results of operations in the first quarter of 2009 may not be indicative of the results expected for the full year because the transactions being discussed with the United States Department of the Treasury and the NY Fed are not expected to be in place. However, AIG believes its forecasts are achievable.

Income Taxes on Earnings of Certain Foreign Subsidiaries:

In connection with AIG's asset disposition plan, AIG determined it can no longer assert that earnings of its foreign subsidiaries will be indefinitely reinvested. Due to the complexity of the U.S. federal income tax laws involved in determining the amount of income taxes incurred on these potential dispositions, as well as AIG's reliance on reasonable assumptions and estimates in calculating this liability, AIG considers the U.S. federal income taxes accrued on the earnings of certain foreign subsidiaries to be a critical accounting estimate.

Fair Value Measurements of Certain Financial Assets and Liabilities:

Overview

AIG measures at fair value on a recurring basis financial instruments in its trading and available for sale securities portfolios, certain mortgage and other loans receivable, certain spot commodities, derivative assets and liabilities, securities purchased (sold) under agreements to resell (repurchase), securities lending invested collateral, non-marketable equity investments included in other invested assets, certain policyholder contract deposits, securities and spot commodities sold but not yet purchased, certain trust deposits and deposits due to banks and other depositors, certain long-term debt, and certain hybrid financial instruments included in other liabilities. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between willing, able and knowledgeable market participants at the measurement date.

The degree of judgment used in measuring the fair value of financial instruments generally correlates with the level of pricing observability. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Conversely, financial instruments traded in

other-than-active markets or that do not have quoted prices have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment. An active market is one in which transactions for the asset or liability being valued occur with sufficient frequency and volume to provide pricing information on an ongoing basis. An other-than-active market is one in which there are few transactions, the prices are not current, price quotations vary substantially either over time or among market makers, or in which little information is released publicly for the asset or liability being valued. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established, the characteristics specific to the transaction and general market conditions.

AIG management is responsible for the determination of the value of the financial assets and financial liabilities carried at fair value and the supporting methodologies and assumptions. With respect to securities, AIG employs independent third-party valuation service providers to gather, analyze, and interpret market information and derive fair values based upon relevant methodologies and assumptions for individual instruments. When AIG's valuation service providers are unable to obtain sufficient market observable information upon which to estimate the fair value for a particular security, fair value is determined either by requesting brokers who are knowledgeable about these securities to provide a quote, which is generally non-binding, or by employing widely accepted internal valuation models.

Valuation service providers typically obtain data about market transactions and other key valuation model inputs from multiple sources and, through the use of widely accepted internal valuation models, provide a single fair value measurement for individual securities for which a fair value has been requested under the terms of service agreements. The inputs used by the valuation service providers include, but are not limited to, market prices from recently completed transactions and transactions of comparable securities, interest rate yield curves, credit spreads, currency rates, and other market-observable information, as applicable. The valuation models take into account, among other things, market observable information as of the measurement date as well as the specific attributes of the security being valued including its term, interest rate, credit rating, industry sector, and when applicable, collateral quality and other issue or issuer-specific information. When market transactions or other market observable data is limited, the extent to which judgment is applied in determining fair value is greatly increased.

AIG employs specific control processes to determine the reasonableness of the fair values of AIG's financial assets and financial liabilities. AIG's processes are designed to ensure that the values received or internally estimated are accurately recorded and that the data inputs and the valuation techniques utilized are appropriate, consistently applied, and that the assumptions are reasonable and consistent with the objective of determining fair value. AIG assesses the reasonableness of individual security values received from valuation service providers through various analytical techniques. In addition, AIG may validate the reasonableness of fair values by comparing information obtained from AIG's valuation service providers to other third-party valuation sources for selected securities. AIG also validates prices for selected securities obtained from brokers through reviews by members of management who have relevant expertise and who are independent of those charged with executing investing transactions.

The fair value of fixed income and equity securities by source of value determination was as follows:

At December 31, 2008	Fair Value (In billions)	Percent of Total
Fair value based on external sources *(a)*	$ 387	91%
Fair value based on internal sources	38	9
Total fixed income and equity securities *(b)*	$ 425	100%

(a) Includes $45.8 billion whose primary source is broker quotes.

(b) Includes available for sale, trading and securities lending invested collateral securities.

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See Note 4 to the Consolidated Financial Statements for more detailed information about AIG's accounting policy for the incorporation of credit risk in fair value measurements and the measurement of fair value of the following financial assets and financial liabilities:

- Fixed maturity securities;
- Equity securities traded in active markets — trading and available for sale;
- Non-traded equity investments — other invested assets;
- Private limited partnership and hedge fund investments — other invested assets;
- Separate account assets;
- Freestanding derivatives;
- Embedded policy derivatives;
- AIGFP's super senior credit default swap portfolio; and
- Policyholder contract deposits.

Level 3 Assets and Liabilities

Under FAS 157, assets and liabilities recorded at fair value in the consolidated balance sheet are classified in a hierarchy for disclosure purposes consisting of three "levels" based on the observability of inputs available in the marketplace used to measure the fair value. See Note 4 to the Consolidated Financial Statements for additional information about fair value measurements.

At December 31, 2008, AIG classified $42.1 billion and $21.1 billion of assets and liabilities, respectively, measured at fair value on a recurring basis as Level 3. This represented 4.9 percent and 2.6 percent of the total assets and liabilities, respectively, measured at fair value on a recurring basis. Level 3 fair value measurements are based on valuation techniques that use at least one significant input that is unobservable. These measurements are made under circumstances in which there is little, if any, market activity for the asset or liability. AIG's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment.

In making the assessment, AIG considers factors specific to the asset or liability. In certain cases, the inputs used to measure fair value of an asset or a liability may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety is classified is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Valuation of Level 3 Assets and Liabilities

AIG values its assets and liabilities classified as Level 3 using judgment and valuation models or other pricing techniques that require a variety of inputs including contractual terms, market prices and rates, yield curves, credit curves, measures of volatility, prepayment rates and correlations of such inputs, some of which may be unobservable. The following paragraphs describe the methods AIG uses to measure on a recurring basis the fair value of the major classes of assets and liabilities classified in Level 3.

Private equity and real estate fund investments: These assets initially are valued at the transaction price, i.e., the price paid to acquire the asset. Subsequently, they are measured based on net asset value using information provided by the general partner or manager of these investments, the accounts of which generally are audited on an annual basis. AIG considers observable market data and performs diligence procedures in validating the appropriateness of using the net asset value as a fair value measurement.

Corporate bonds and private placement debt: These assets initially are valued at the transaction price. Subsequently, they are valued using market data for similar instruments (e.g., recent transactions, bond spreads or credit default swap spreads), comparisons to benchmark derivative indices or movements in underlying credit spreads. When observable price quotations are not available, fair value is determined based on cash flow models with yield curves, bond or single-name credit default swap spreads and estimated recovery rates.

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American International Group, Inc., and Subsidiaries

Certain Residential Mortgage-Backed Securities (RMBS) and Commercial Mortgage-Backed Securities (CMBS): These assets initially are valued at the transaction price. Subsequently, they may be valued by comparison to transactions in instruments with similar collateral and risk profiles, remittances received and updated cumulative loss data on underlying obligations, discounted cash flow techniques, and/or for RMBS option adjusted spread analyses.

Certain Asset-Backed Securities — non-mortgage: These assets initially are valued at the transaction price. Subsequently, they may be valued based on external price/spread data. When position-specific external price data are not observable, the valuation is based on prices of comparable securities.

CDOs: These assets initially are valued at the transaction price. Subsequently, they are valued based on external price/spread data from independent third parties, dealer quotations, matrix pricing, the BET model or a combination thereof.

Interests in ML II and ML III: At their inception, AIG's economic interest in ML II and membership interest in ML III (Maiden Lane Interests) were valued at the transaction prices of $1 billion and $5 billion, respectively. Subsequently, Maiden Lane Interests are valued using a discounted cash flow methodology that uses the estimated future cash flows of the assets to which the Maiden Lane Interests are entitled and the discount rates applicable to such interests as derived from the fair value of the entire asset pool. The implicit discount rates are calibrated to the changes in the estimated asset values for the underlying assets commensurate with AIG's interests in the capital structure of the respective entities. Estimated cash flows and discount rates used in the valuations are validated, to the extent possible, using market observable information for securities with similar asset pools, structure and terms.

See Note 4 to the Consolidated Financial Statements for further discussion.

AIGFP's Super Senior Credit Default Swap Portfolio: AIGFP wrote credit protection on the super senior risk layer of collateralized loan obligations (CLOs), multi-sector CDOs and diversified portfolios of corporate debt, and prime residential mortgages. In these transactions, AIGFP is at risk of credit performance on the super senior risk layer related to such assets. These transactions placed a significant demand on AIGFP's liquidity during 2008, primarily as a result of their collateral posting provisions (see General Contractual Terms below). To a lesser extent, AIGFP also wrote protection on tranches below the super senior risk layer, primarily in respect of regulatory capital relief transactions.

As discussed under Arbitrage Portfolio and ML III Transaction below, during the fourth quarter of 2008, AIG Financial Products Corp. terminated the vast majority of the credit default swaps it had written on multi-sector CDOs. See Note 5 to the Consolidated Financial Statements for further discussion.

The net notional amount, fair value of derivative liability and unrealized market valuation loss of the AIGFP super senior credit default swap portfolio, including credit default swaps written on mezzanine tranches of certain regulatory capital relief transactions, by asset class were as follows:

	Net Notional Amount December 31,		Fair Value Of Derivative Liability at December 31,		Unrealized Market Valuation Loss Year Ended December 31(a),	
	2008(b)	2007(b)	2008(c)	2007(c)	2008(d)	2007(d)
	(In millions)					
Regulatory Capital:						
Corporate loans	**$125,628**	$229,313	**$ —**	$ —	**$ —**	$ —
Prime residential mortgages	**107,246**	149,430	**—**	—	**—**	—
Other *(e)*	**1,575**	—	**379**	—	**379**	—
Total	**234,449**	378,743	**379**	—	**379**	—

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	Net Notional Amount December 31,		Fair Value Of Derivative Liability at December 31,		Unrealized Market Valuation Loss Year Ended December 31(a),	
	2008(b)	2007(b)	2008(c)	2007(c)	2008(d)	2007(d)
	(In millions)					
Arbitrage:						
Multi-sector CDOs *(f)*	**12,556**	78,205	**5,906**	11,246	**25,700**	11,246
Corporate debt/CLOs *(g)*	**50,495**	70,425	**2,554**	226	**2,328**	226
Total	**63,051**	148,630	**8,460**	11,472	**28,028**	11,472
Mezzanine tranches *(h)*	**4,701**	5,770	**195**	—	**195**	—
Total	**$302,201**	$533,143	**$9,034**	$11,472	**$28,602**	$11,472

(a) *There were no unrealized market valuation losses in 2006.*

(b) *Net notional amounts presented are net of all structural subordination below the covered tranches.*

(c) *Fair value amounts are shown before the effects of counterparty netting adjustments and offsetting cash collateral in accordance with FIN 39.*

(d) *Includes credit valuation adjustment gains of $185 million in 2008 representing the positive effect of AIG's widening credit spreads on the valuation of the derivatives liabilities. AIGFP began reflecting this valuation adjustment as a result of the adoption of SFAS 157 on January 1, 2008. Prior to January 1, 2008, a credit valuation adjustment was not reflected in the valuation of AIGFP's liabilities.*

(e) *During 2008, a European RMBS regulatory capital relief transaction was not terminated as expected when it no longer provided regulatory capital relief to the counterparty as a result of arbitrage opportunities arising from its unique attributes and the counterparty's access to a particular funding source.*

(f) *Includes $9.7 billion in net notional amount of credit default swaps written with cash settlement provisions at December 31, 2008. In connection with the terminations of CDS transactions in respect of the ML III transaction, AIG Financial Products Corp. paid $32.5 billion through the surrender of collateral previously posted (net of the $2.5 billion received pursuant to the shortfall agreement), of which $2.5 billion (included in Other income (loss)) is related to certain 2a-7 Put transactions written on multi-sector CDOs purchased by ML III.*

(g) *Includes $1.5 billion of credit default swaps written on the super senior tranches of CLOs as of December 31, 2008.*

(h) *Includes offsetting purchased CDS of $2.0 billion and $2.7 billion in net notional amount at December 31, 2008 and 2007, respectively.*

The changes in the net notional amount of the AIGFP super senior credit default swap portfolio, including credit default swaps written on mezzanine tranches of certain regulatory capital relief transactions were as follows:

For The Year Ended December 31, 2008

	Net Notional Amount December 31, 2007	Terminations and Maturities	ML III Transaction(a)	Effect of Foreign Exchange Rates(b)	Amortization/ Reclassification	Net Notional Amount December 31, 2008
	(In millions)					
Regulatory Capital:						
Corporate loans	$ 229,313	$ (75,480)	$ —	$ (3,554)	$ (24,651)	$ 125,628
Prime residential mortgages	149,430	(24,222)	—	(6,539)	(11,423)	107,246
Other *(c)*	—	—	—	(207)	1,782	1,575
Total	378,743	(99,702)	—	(10,300)	(34,292)	234,449

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	Net Notional Amount December 31, 2007	Terminations and Maturities	ML III Transaction(a)	Effect of Foreign Exchange Rates(b)	Amortization/ Reclassification	Net Notional Amount December 31, 2008
			(In millions)			
Arbitrage:						
Multi-sector CDOs	78,205	(2,146)	(62,130)	(227)	(1,146)	12,556
Corporate debt/CLOs	70,425	(17,147)	—	(943)	(1,840)	50,495
Total	148,630	(19,293)	(62,130)	(1,170)	(2,986)	63,051
Mezzanine tranches	5,770	(358)	—	(529)	(182)	4,701
Total	$ 533,143	$ (119,353)	$ (62,130)	$(11,999)	$ (37,460)	$ 302,201

(a) *Includes $8.5 billion of multi-sector CDOs underlying 2a-7 Puts written by AIG Financial Products Corp.*

(b) *Relates to the strengthening of the U.S. dollar, primarily against the Euro and the British Pound.*

(c) *During 2008, a European RMBS regulatory capital relief transaction was not terminated as expected when it no longer provided regulatory capital relief to the counterparty as a result of arbitrage opportunities arising from its unique attributes and the counterparty's access to a particular funding source.*

General Contractual Terms

AIGFP entered into CDS transactions in the ordinary course of its business. In the majority of AIGFP's credit derivative transactions, AIGFP sold credit protection on a designated portfolio of loans or debt securities. Generally, AIGFP provides such credit protection on a "second loss" basis, meaning that AIGFP will incur credit losses only after a shortfall of principal and/or interest, or other credit events, in respect of the protected loans and debt securities, exceeds a specified threshold amount or level of "first loss."

Typically, the credit risk associated with a designated portfolio of loans or debt securities has been tranched into different layers of risk, which are then analyzed and rated by the credit rating agencies. At origination, there is usually an equity layer covering the first credit losses in respect of the portfolio up to a specified percentage of the total portfolio, and then successive layers ranging generally from a BBB-rated layer to one or more AAA-rated layers. A significant majority of transactions that are rated by rating agencies have risk layers or tranches that were rated AAA at origination and are immediately junior to the threshold level above which AIGFP's payment obligation would generally arise. In transactions that were not rated, AIGFP applied equivalent risk criteria for setting the threshold level for its payment obligations. Therefore, the risk layer assumed by AIGFP with respect to the designated portfolio of loans or debt securities in these transactions is often called the "super senior" risk layer, defined as a layer of credit risk senior to one or more risk layers that have been rated AAA by the credit rating agencies, or if the transaction is not rated, structured to the equivalent thereto.

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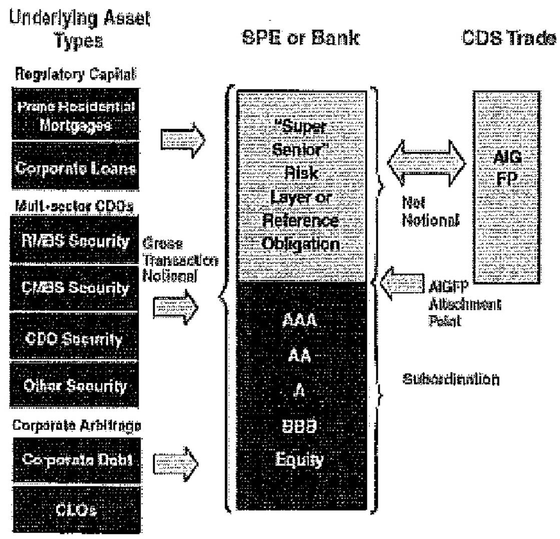
The following graphic represents a typical structure of a transaction including the super senior risk layer:



Regulatory Capital Portfolio

A total of $234.4 billion (consisting of corporate loans and prime residential mortgages) in net notional exposure of AIGFP's super senior credit default swap portfolio as of December 31, 2008 represented derivatives written for financial institutions, principally in Europe, for the purpose of providing regulatory capital relief rather than for arbitrage purposes. These transactions were entered into by Banque AIG, AIGFP's French regulated bank subsidiary, and written on diversified pools of residential mortgages and corporate loans (made to both large corporations and small to medium sized enterprises). In exchange for a periodic fee, the counterparties receive credit protection with respect to diversified loan portfolios they own, thus reducing their minimum capital requirements.

The regulatory benefit of these transactions for AIGFP's financial institution counterparties is generally derived from the terms of the Capital Accord of the Basel Committee on Banking Supervision (Basel I) that existed through the end of 2007 and which is in the process of being replaced by the Revised Framework for the International Convergence of Capital Measurement and Capital Standards issued by the Basel Committee on Banking Supervision (Basel II). Prior to the adoption of Basel II, a financial institution was required to hold capital against its assets, based on the categorization of the issuer or guarantor of the assets. One of the means for a financial institution to reduce its required regulatory capital was to purchase credit protection on a group of its assets from a regulated financial institution, such as Banque AIG, in order to benefit from such regulated financial institution's lower risk weighting (e.g., 20 percent vs. 100 percent) that is assigned to those assets under Basel I. A lower risk weighting reduces the amount of capital a financial institution is required to hold against such assets.

Unlike Basel I, Basel II gives credit to the relative risk of loss associated with the assets, meaning that less capital is required for such assets. After a financial institution has implemented a capital model that is compliant with Basel II and has obtained approval from its local regulator, the CDS transactions provide no additional regulatory benefit in most cases, except during a transition period. The Basel II implementation includes a transition period during which the financial institutions must calculate their capital requirements under both Basel I and Basel II (until December 31, 2009). During this period, the capital required is "floored" at a percentage of the Basel I capital calculation; therefore, until early 2010, these CDS transactions may still provide regulatory capital benefit for AIGFP's counterparties, depending on each counterparty's particular circumstances. In addition, in a limited number of instances, counterparties may decide to hold these CDSs for a longer period of time because they provide a regulatory capital benefit, while smaller, under Basel II.

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Given the prospect of Basel II, the CDS transactions were structured with early termination rights for counterparties following a regulatory event such as the implementation of Basel II. The pace at which the CDS transactions were and will be terminated early varies among the counterparties based on a number of factors including their progress in having the internal capital models approved by their national regulator, the effect of the transitional floor on overall total capital charges, the counterparties' capital needs and their sensitivity to Basel I capital measures. AIG expects that the counterparties in the remaining CDS transactions will terminate the vast majority of transactions with AIGFP during this transition period within the next 15 months.

When a counterparty elects to terminate a transaction early pursuant to the terms of the contracts, the early termination is at no cost to AIGFP. The counterparty may be required to pay the remaining balance of an agreed-upon minimum fee to AIGFP. Typically, the minimum guaranteed fee on recent transactions is equal to the fees due to AIGFP through the first call date (which is the first date on which a counterparty can terminate the transaction at no cost). During 2008, $99.7 billion in net notional amount was terminated or matured. Through February 18, 2009, AIGFP has also received formal termination notices for an additional $26.5 billion in net notional amount with effective termination dates in 2009.

The regulatory capital relief CDS transactions require cash settlement and, other than collateral posting, AIGFP is required to make a payment in connection with a regulatory capital relief transaction only if realized credit losses in respect of the underlying portfolio exceed AIGFP's attachment point (see Triggers and Settlement Alternatives below).

The super senior tranches of these CDS transactions continue to be supported by high levels of subordination, which, in most instances, have increased since origination. The weighted average subordination supporting the European residential mortgage and corporate loan referenced portfolios at December 31, 2008 was 12.7 percent and 18.3 percent, respectively. Delinquencies, defaults and realized losses for both types of referenced portfolios have been modest to date. Substantially all of the underlying assets are not rated by one of the principal rating agencies. The highest level of realized losses to date in any single residential mortgage and corporate loan pool was 2.1 percent and 0.42 percent, respectively. The European residential mortgage portfolios are each comprised of thousands of seasoned, prime, full documentation, mostly first lien, owner-occupied mortgages originated largely at bank retail branches at modest loan-to-value (LTV) ratios, except for one $1.6 billion high LTV CDS transaction, which benefits from both subordination and a significant percentage of pool mortgage insurance. The corporate loan transactions are each comprised of several hundred secured and unsecured loans diversified by industry and, in some instances, by country, and have tight per-issuer concentration limits. Both types of transactions generally allow some substitution and replenishment of loans, subject to tightly defined constraints, as older loans mature or are prepaid. These replenishment rights usually mature within the first few years of the trade, after which the proceeds of any prepaid or maturing loans are applied first to the super senior tranche (sequentially), thereby increasing the relative level of subordination supporting the balance of AIGFP's super senior CDS exposure.

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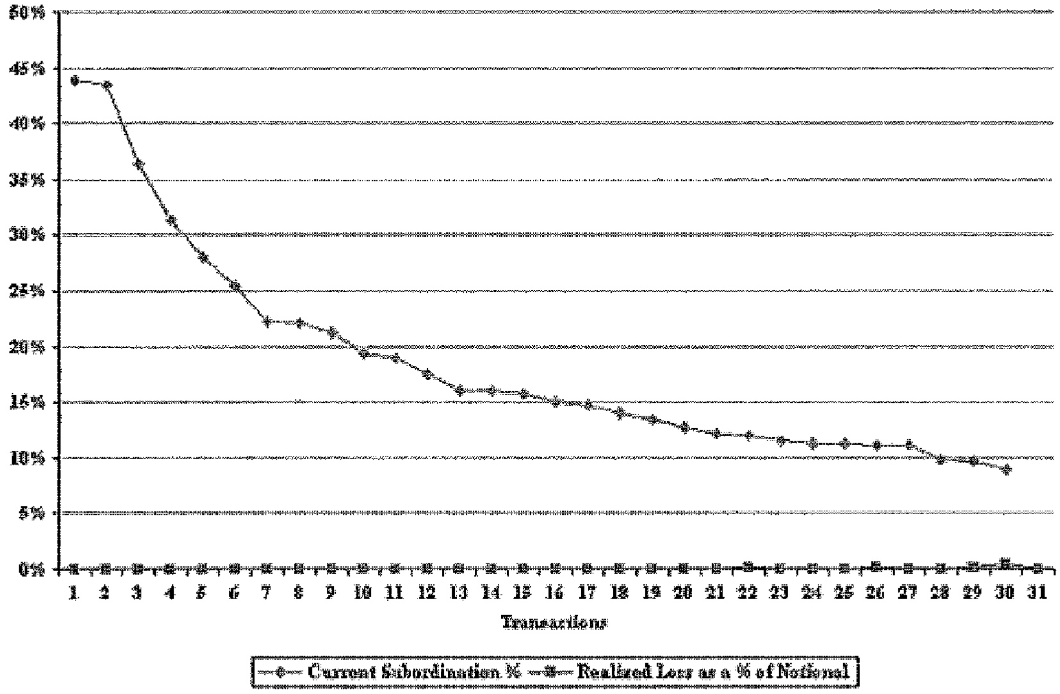
American International Group, Inc., and Subsidiaries

The following graph presents subordination level from highest to lowest and realized losses as a percent of gross notional amount for each regulatory capital relief super senior CDS transaction written on a diversified portfolio of corporate loans as of December 31, 2008:



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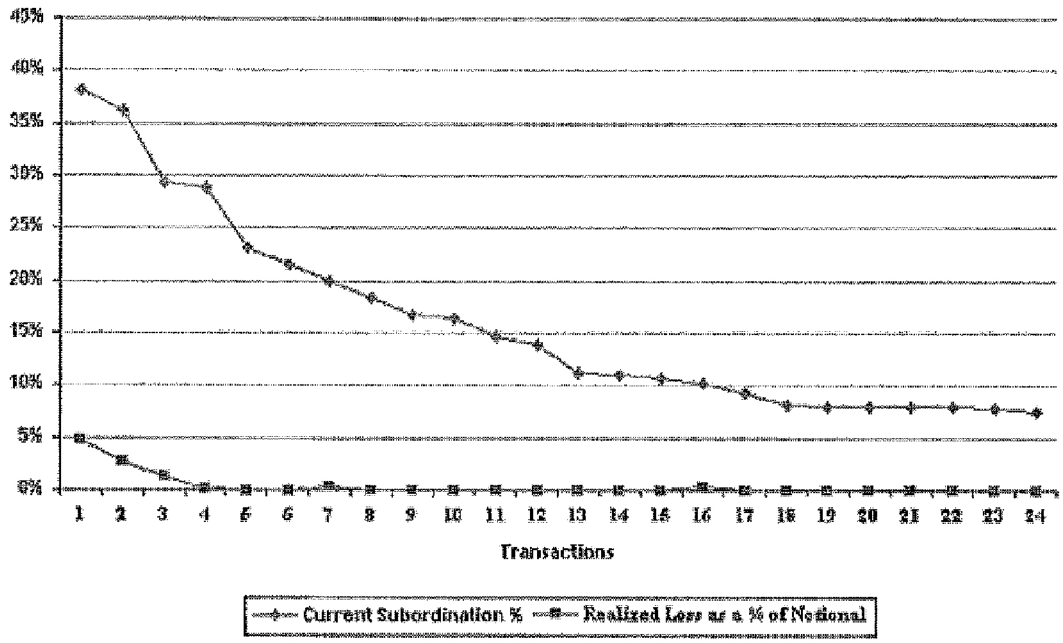
American International Group, Inc., and Subsidiaries

The following graph presents subordination level from highest to lowest and realized losses as a percent of notional amount for each regulatory capital relief super senior CDS transaction written on a diversified portfolio of residential mortgages as of December 31, 2008:



Given the current performance of the underlying portfolios, the level of subordination and the expectation that counterparties will terminate these transactions prior to their maturity; AIG Financial Products Corp. does not expect that it will be required to make payments pursuant to the contractual terms of these transactions.

Arbitrage Portfolio

A total of $63.1 billion in net notional exposure on AIG Financial Products Corp.'s super senior credit default swaps as of December 31, 2008 are arbitrage-motivated transactions written on multi-sector CDOs or designated pools of investment grade senior unsecured corporate debt or CLOs. While certain credit default swaps written on corporate debt and multi-sector CDOs provide for cash settlement, $2.8 billion in net notional amount of CDS transactions written on multi-sector CDOs and all the CDS transactions written on CLOs ($1.5 billion net notional) require physical settlement (see Triggers and Settlement Alternatives below). The ML III transaction eliminated the vast majority of the super senior multi-sector CDO credit default swap exposure.

ML III Transaction

On November 25, 2008, AIG entered into a Master Investment and Credit Agreement with the NY Fed, ML III, and The Bank of New York Mellon which established arrangements for the purchase by ML III of the multi-sector CDOs referenced in certain CDS transactions between AIG Financial Products Corp. and its counterparties. Concurrently, AIG Financial Products Corp.'s counterparties to such CDS transactions agreed to terminate the CDS transactions relating to the multi-sector CDOs purchased by ML III.

During 2008, AIG Financial Products Corp. terminated multi-sector CDO transactions with a net notional amount of $62.1 billion with its counterparties, and concurrently, ML III purchased the underlying multi-sector CDOs including $8.5 billion of multi-sector CDOs underlying 2a-7 Puts written by AIG Financial Products Corp. The CDS transactions terminated in connection with ML III contained physical settlement provisions and were denominated in U.S. dollars. The net payment made by ML III to the counterparties for the purchase of the multi-sector CDOs was $26.8 billion, which was funded by AIG's equity interest in ML III in the amount of $5 billion and

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$24.3 billion of borrowings under a senior loan from the NY Fed to ML III. A portion of the net payment made by ML III to the counterparties for the purchase of the multi-sector CDOs facilitated the resolution of $8.0 billion of liquidity arrangements, which had funded certain of the multi-sector CDOs in connection with the 2a-7 Puts.

In connection with the ML III transaction, AIG Financial Products Corp. entered into a Shortfall Agreement, dated November 25, 2008 and amended on December 18, 2008 (the Shortfall Agreement), with ML III under which ML III made a payment of $2.5 billion to AIG Financial Products Corp. representing the amount by which collateral surrendered as part of the termination of the CDS exceeded the fair value of the CDS as of October 31, 2008.

Among the multi-sector CDOs purchased by ML III are certain CDO securities with a net notional amount of $1.7 billion for which the related 2a-7 Puts to AIG Financial Products Corp. remained outstanding as of December 31, 2008. For the $252 million notional amount of multi-sector CDOs held by ML III with 2a-7 Puts that may be exercised in 2009, ML III has agreed to not sell the multi-sector CDOs in 2009 and to either not exercise its put option on such multi-sector CDOs or to simultaneously exercise their par put option with a par purchase of the multi-sector CDO securities. In exchange, AIG Financial Products Corp. has agreed to pay to ML III the consideration that it receives for providing the put protection. AIG Financial Products Corp. and ML III are currently negotiating an agreement that will outline procedures to be taken by ML III and AIG Financial Products Corp. for multi-sector CDOs with put options that may be exercised after December 31, 2009, with the objective of mitigating or eliminating the impact on AIG Financial Products Corp. of such 2a-7 Puts and capturing the associated economics for ML III.

In connection with the termination of $62.1 billion net notional amount of CDS transactions in respect of the ML III transaction, AIG Financial Products Corp. paid $32.5 billion, net of $2.5 billion received in connection with the shortfall agreement, through the surrender of collateral previously posted. Included in this amount is $2.5 billion related to multi-sector CDOs underlying 2a-7 Puts previously written by AIG Financial Products Corp. and sold to ML III. As a result of the termination of such CDS, AIG Financial Products Corp. is no longer subject to any further collateral calls related to such CDS transactions nor subject to the risk of having to make a payment to a counterparty to physically settle the CDS transactions following the occurrence of a credit event, thereby alleviating the demand on AIGFP's liquidity.

Multi-Sector CDOs

The gross transaction notional amount of the multi-sector CDOs on which AIGFP wrote protection on the super senior tranche, subordination below the super senior risk layer, net notional amount and fair value of derivative liability by underlying collateral type were as follows (excluding 2a-7 Puts):

At December 31, 2008	Gross Transaction Notional Amount(a)	Subordination Below the Super Senior Risk Layer	Net Notional Amount(b)	Fair Value of Derivative Liability
	(In millions)			
High grade with sub-prime collateral	$ 6,776	$ 2,808	$ 3,968	$ 1,797
High grade with no sub-prime collateral	10,156	5,816	4,340	1,428
Total high grade *(c)*	16,932	8,624	8,308	3,225
Mezzanine with sub-prime	6,407	2,955	3,452	2,156
Mezzanine with no sub-prime	1,697	901	796	525
Total mezzanine *(d)*	8,104	3,856	4,248	2,681
Total	$ 25,036	$ 12,480	$ 12,556	$ 5,906

(a) Total outstanding principal amount of securities held by a CDO.

(b) Net notional size on which AIGFP wrote credit protection.

(c) "High grade" refers to transactions in which the underlying collateral credit ratings on a stand-alone basis were predominantly AA or higher at origination.

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(d) *"Mezzanine" refers to transactions in which the underlying collateral credit ratings on a stand-alone basis were predominantly A or lower at origination.*

The net notional amounts of the multi-sector CDOs on which AIGFP wrote protection on the super senior tranche, by settlement alternative, were as follows:

	December 31, 2008	December 31, 2007
	(In millions)	
CDS transactions with cash settlement provisions		
US dollar denominated	$ 7,947	$ 10,544
Euro denominated	1,780	2,075
Total CDS transactions with cash settlement provisions	9,727	12,619
CDS transactions with physical settlement provisions		
US dollar denominated	766	63,040
Euro denominated	2,063	2,546
Total CDS transactions with physical settlement provisions	2,829	65,586
Total	$ 12,556	$ 78,205

The following table presents, for each multi-sector CDO that is a reference obligation in a CDS written by AIGFP, the gross and net notional amounts at December 31, 2008, attachment points at inception and at December 31, 2008 and percentage of gross notional amount rated less than B-/B3 at December 31, 2008:

CDO	Gross Notional Amount at December 31, 2008	Net Notional Amount at December 31, 2008	Attachment Point at Inception*	Attachment Point at December 31, 2008*	Percentage of Gross Notional Amount Rated Less than B-/B3 at December 31, 2008
1	$ 1,680	$ 1,440	12.00%	14.28%	15.88%
2	665	396	27.00%	40.45%	20.20%
3	1,064	814	20.00%	23.49%	18.96%
4	1,328	531	40.00%	60.02%	42.68%
5	463	238	36.00%	48.55%	42.37%
6	698	327	53.00%	53.19%	2.86%
7	1,000	470	53.00%	53.00%	0.00%
8	1,412	360	76.00%	74.50%	39.33%
9	1,130	4	10.83%	11.29%	6.89%
10	403	221	39.33%	45.30%	65.11%
11	1,268	1,103	12.27%	10.24%	5.04%
12	1,348	960	25.24%	27.86%	6.54%
13	1,490	1,350	10.00%	9.42%	8.76%
14	575	302	33.00%	47.48%	54.63%
15	623	265	33.25%	37.36%	60.94%
16	2,570	1,780	16.50%	17.84%	0.00%
17	495	277	32.00%	44.08%	43.08%
18	682	529	24.49%	22.46%	68.89%
19	779	469	32.90%	39.75%	81.03%
20	393	224	34.51%	43.09%	78.07%
21	4,970	496	9.72%	10.31%	0.00%
Total	$ 25,036	$ 12,556			

* *Expressed as a percentage of gross notional amount.*

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In a number of instances, the level of subordination with respect to individual CDOs has increased since inception relative to the overall size of the CDO. While the super senior tranches are amortizing, subordinate layers have not been reduced by realized losses to date. Such losses are expected to emerge in the future. At inception, substantially all of the underlying assets were rated B-/B3 or higher and in most cases at least BBB. Thus, the percentage of gross notional amount rated less than B-/B3 represents deterioration in the credit quality of the underlying assets.

The gross transaction notional amount, percentage of the total CDO collateral pools, and ratings and vintage breakdown of collateral securities in the multi-sector CDOs at December 31, 2008, by ABS category, were as follows (excluding 2a-7 Puts):

	Gross Transaction Notional Amount (Dollars in millions)	Percent of Total	Ratings AAA	AA	A	BBB	BB	<BB	NR	Vintage 2008	2007	2006	2005	2004+P
RMBS PRIME	$ 3,013	12.79%	10.50%	0.95%	0.57%	0.26%	0.00%	0.51%	0.00%	0.31%	7.39%	3.72%	0.59%	0.78%
RMBS ALT-A	3,526	14.96%	8.91%	0.99%	0.78%	1.68%	0.55%	2.05%	0.00%	0.68%	3.91%	5.33%	4.29%	0.75%
RMBS SUBPRIME	6,865	29.12%	0.93%	3.74%	2.29%	2.55%	2.38%	17.23%	0.00%	0.00%	1.33%	1.94%	17.30%	8.55%
CMBS	4,457	17.47%	2.93%	2.33%	2.74%	6.72%	2.24%	0.42%	0.09%	0.07%	0.96%	5.26%	4.85%	6.33%
CDO	3,151	12.42%	1.54%	1.74%	1.58%	1.24%	0.83%	5.35%	0.14%	0.00%	0.61%	1.45%	3.31%	7.05%
OTHER	4,024	13.24%	3.70%	3.01%	4.18%	1.75%	0.04%	0.36%	0.20%	0.32%	0.58%	2.85%	4.43%	5.06%
Total	$ 25,036	100.00%	28.51%	12.76%	12.14%	14.20%	6.04%	25.92%	0.43%	1.38%	14.78%	20.55%	34.77%	28.52%

The corporate arbitrage portfolio consists principally of CDS written on portfolios of senior unsecured corporate obligations that were generally rated investment grade at the inception of the CDS. These CDS transactions require cash settlement (see Triggers and Settlement Alternatives below). This portfolio also includes CDS with a net notional amount of $1.5 billion written on the senior part of the capital structure of CLOs, which require physical settlement.

The gross transaction notional amount of CDS transactions written on portfolios of senior unsecured corporate obligations (excluding CLOs), percentage of the total referenced portfolios, and ratings by industry sector, in addition to the subordinations below the super senior risk layer and AIGFP's net notional exposure at December 31, 2008, by industry sector, were as follows:

	Gross Transaction Notional Amount (Dollars in millions)	Percent of Total	Ratings AAA	Aa	A	Baa	Ba	<Ba	NR
United States Industrial	$ 23,363	37.5%	0.0%	0.4%	7.5%	19.2%	4.7%	5.4%	0.3%
Financial	9,776	15.7%	0.4%	0.6%	7.6%	4.6%	1.5%	0.3%	0.7%
Utilities	2,218	3.6%	0.0%	0.0%	0.5%	2.7%	0.1%	0.1%	0.2%
Other	1,364	2.2%	0.0%	0.0%	0.0%	0.1%	0.0%	0.0%	2.1%
Total United States	36,721	59.0%	0.4%	1.0%	15.6%	26.6%	6.3%	5.8%	3.3%
Non-United States Industrial	18,616	29.9%	0.1%	0.9%	9.0%	14.4%	2.2%	1.0%	2.3%
Financial	3,088	5.0%	0.1%	0.7%	3.0%	0.8%	0.1%	0.0%	0.3%
Government	1,853	3.0%	0.0%	0.4%	1.4%	1.0%	0.2%	0.0%	0.0%
Utilities	1,680	2.7%	0.0%	0.0%	1.5%	0.8%	0.0%	0.0%	0.4%
Other	268	0.4%	0.0%	0.0%	0.2%	0.1%	0.0%	0.0%	0.1%

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American International Group, Inc., and Subsidiaries

	Gross Transaction Notional Amount	Percent of Total	Ratings AAA	Aa	A	Baa	Ba	<Ba	NR
	(Dollars in millions)								
Total Non-United States	25,505	41.0%	0.2%	2.0%	15.1%	17.1%	2.5%	1.0%	3.1%
Total	$ 62,226	100.0%	0.6%	3.0%	30.7%	43.7%	8.8%	6.8%	6.4%
Subordination	$ 13,242								
Net Notional Amount	$ 48,984								
Fair Value of Derivative Liability	$ 2,147								

Triggers and Settlement Alternatives

At December 31, 2008, all outstanding CDS transactions for regulatory capital purposes and the majority of the arbitrage portfolio (comprising $56.7 billion or 90 percent of the net notional amount for the arbitrage portfolio at December 31, 2008) have cash-settled structures in respect of a basket of reference obligations, where AIGFP's payment obligations may be triggered by payment shortfalls, bankruptcy and certain other events such as write-downs of the value of underlying assets (see Cash Settlement below). For the remainder of the CDS transactions in respect of the arbitrage portfolio (comprising $6.4 billion or 10 percent of the net notional amount for the arbitrage portfolio at December 31, 2008), AIGFP's payment obligations are triggered by the occurrence of a credit event under a single reference security, and performance is limited to a single payment by AIGFP in return for physical delivery by the counterparty of the reference security (see Physical Settlement below). By contrast, at December 31, 2007, under the large majority of CDS transactions in respect of multi-sector CDOs (comprising $65.6 billion or 44.1 percent of the net notional amount for the arbitrage portfolio at December 31, 2007) AIGFP's payment obligations were triggered by the occurrence of a non-payment event under a single reference CDO security, and performance was limited to a single payment by AIGFP in return for physical delivery by the counterparty of the reference security.

Cash Settlement. Transactions requiring cash settlement (principally on a "pay as you go" basis) are generally in respect of baskets of reference credits (which may also include single-name CDS in addition to securities and loans) rather than a single reference obligation as in the case of the physically settled transactions described below. Under these credit default swap transactions:

- Each time a "triggering event" occurs a "loss amount" is calculated. A triggering event is generally a failure by the relevant obligor to pay principal of or, in some cases, interest on one of the reference credits in the underlying basket. Triggering events may also include bankruptcy of the obligors of the reference credits, write-downs or payment postponements with respect to interest or to the principal amount of a reference credit payable at maturity. The determination of the loss amount is specific to each triggering event. It can represent the amount of a shortfall in ordinary course interest payments on the reference credit, a write-down in the interest on or principal of such reference credit or payment postponed. It can also represent the difference between the notional or par amount of such reference credit and its market value, as determined by reference to market quotations. A "write-down" with respect to a referenced credit may arise as a result of a reduction in the outstanding principal amount of such referenced credit (other than as a result of a scheduled or unscheduled payment of principal), whether caused by a principal deficiency, realized loss or forgiveness of principal. An implied write-down may also result from the existence of a shortfall between the referenced credit's pool principal balance and the aggregate balance of all *pari passu* obligations and senior securities backed by the same pool.
- Triggering events can occur multiple times, either as a result of continuing shortfalls in interest or write-downs or payment postponements on a single reference credit, or as a result of triggering events in respect of different reference credits included in a protected basket. In connection with each triggering event, AIGFP is required to make a cash payment to the buyer of protection under the related CDS only if the aggregate loss amounts calculated in respect of such triggering event and all prior triggering events exceed a specified threshold amount (reflecting AIGFP's attachment point).

- If there are reimbursements received (actual or deemed) by the CDS buyer in respect of prior triggering events, AIGFP will be entitled to receive equivalent amounts from the counterparty to the extent AIGFP has previously made a related payment.

Physical Settlement. For CDS transactions requiring physical settlement, AIGFP is generally required to pay unpaid principal and accrued interest for the relevant reference obligation in return for physical delivery of such reference obligation by the CDS buyer upon the occurrence of a credit event. After purchasing the reference obligation, AIGFP may sell the security and recover all or a portion of the purchase price paid under the CDS, or hold such security and be entitled to receive subsequent collections of principal and interest. AIGFP generally is required to settle such a transaction only if the following conditions are satisfied:

- A "Credit Event" (as defined in the relevant CDS transaction confirmation) must have occurred. In all CDS transactions subject to physical settlement, "Failure to Pay" is specified as a Credit Event and is generally triggered if there is a failure by the issuer under the related CDO to make a payment under the reference obligation (after the expiration of any applicable grace period and, in certain transactions, subject to a nominal non-payment threshold having been met).

  - In addition, certain of the AIGFP CDS (with an aggregate net notional amount totaling $265 million and $8.3 billion at December 31, 2008 and 2007, respectively) provide credit protection in respect of CDOs that require minimum amounts of collateral to be maintained to support the CDO debt, where the notional amount of such collateral, subject to certain adjustments, is affected by among other things the ratings of the securities and other obligations comprising such collateral. In the event that the issuer of such a CDO fails to maintain the minimum levels of collateral, an event of default would occur, triggering a right by a specified controlling class of CDO note holders to accelerate the payment of principal and interest on the protected reference obligations. Under certain of the CDSs, upon acceleration of the reference obligations underlying a CDS, AIGFP may be required to purchase such reference obligations for a purchase price equal to unpaid principal of and accrued interest on the CDO in settlement of the CDS. As a result of this over-collateralization feature of these CDOs, AIGFP potentially may be required to purchase such CDO securities in settlement of the related CDS sooner than would be required if such CDOs did not have an over-collateralization feature. One of these CDOs was accelerated in 2008, and AIGFP extinguished its CDS obligations by purchasing the protected CDO security for $162 million, which equaled the principal amount outstanding related to this CDS, of which $103 million was recorded in the trading securities portfolio and $59 million was recorded in the available for sale portfolio. AIGFP had no CDS net notional exposure with respect to CDOs that have experienced over-collateralization events of default at February 18, 2009.

  - In addition to subordination, cash flow diversion mechanics may provide further protection from losses for holders of the super senior CDO securities. Following the acceleration of a CDO security, all, or a portion of, available cash flows in a CDO could be diverted from the junior tranches to the most senior tranches. In a CDO with such a feature, the junior tranches may not receive any cash flows until all interest on, and principal of, the super senior tranches are paid in full. Thus, potential losses borne by the holders of the super senior CDO securities may be mitigated as cash flows that would otherwise be payable to junior tranches throughout the entire CDO capital structure are instead diverted directly to the most senior tranches. Cash flow diversion mechanics also may arise in the context of over-collateralization tests. Upon a failure by the CDO issuer to comply with certain over-collateralization tests (other than those that trigger an indenture event of default), cash flows that would otherwise be payable to certain junior tranches throughout the CDO capital structure may instead be diverted to more senior tranches. Consequently, the super senior risk layer is paid down at a faster rate, effectively increasing the relative level of subordination.

  - The existence of a tranche of securities ranking *pari passu* with the super senior CDO securities does not provide additional subordination that protects holders of the super senior CDO securities, as holders of such *pari passu* securities are entitled to receive payments from available cash flows at the same level of priority as holders of the super senior securities. Thus, a *pari passu* tranche of securities does not affect the amount of losses that have to be absorbed by classes of CDO securities other than the super senior CDO

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securities before the super senior securities incur a loss, although the *pari passu* tranche will absorb losses on a pro rata basis after subordinate classes of securities are exhausted.

- The CDS buyer must deliver the reference obligation within a specified period, generally within 30 days. There is no payment obligation if delivery is not made within this period.
- Upon completion of the physical delivery and payment by AIGFP, AIGFP would be the holder of the relevant reference obligation and have all rights associated with a holder of such securities.

2a-7 Puts : Included in the multi-sector CDO portfolio are maturity-shortening puts that allow the holders of the securities issued by certain CDOs to treat the securities as short-term eligible 2a-7 investments under the Investment Company Act of 1940 (2a-7 Puts). Holders of securities are required, in certain circumstances, to tender their securities to the issuer at par. If an issuer's remarketing agent is unable to resell the securities so tendered, AIGFP must purchase the securities at par as long as the security has not experienced a payment default or certain bankruptcy events with respect to the issuer of such security have not occurred.

At December 31, 2007, 2a-7 Puts with a net notional amount of $6.5 billion were outstanding and included as part of the multi-sector CDO portfolio. During 2008, AIGFP issued new 2a-7 Puts with a net notional amount of $5.4 billion on the super senior security issued by a CDO of AAA-rated CMBS pursuant to a facility that was entered into in 2005. AIGFP is not a party to any commitments to issue any additional 2a-7 Puts. During 2008, AIGFP repurchased multi-sector CDO securities with a principal amount of $9.4 billion in connection with these obligations, of which $8.0 billion was funded using existing liquidity arrangements. In connection with the ML III transaction, ML III purchased $8.5 billion of multi-sector CDOs underlying 2a-7 Puts written by AIGFP. A portion of the net payment made by ML III to the counterparties for the purchase of the multi-sector CDOs facilitated the resolution of liquidity arrangements, which had funded certain of the multi-sector CDOs in connection with the 2a-7 Puts. Among the multi-sector CDOs purchased by ML III are certain CDO securities with a net notional amount of $1.7 billion for which the related 2a-7 Puts to AIGFP remained outstanding as of December 31, 2008. For the $252 million net notional amount of multi-sector CDOs held by ML III with 2a-7 Puts that may be exercised in 2009, ML III has agreed to not sell the multi-sector CDOs in 2009 and to either not exercise its put option on such multi-sector CDOs or to simultaneously exercise their par put option with a par purchase of the multi-sector CDO securities. In exchange, AIG Financial Products Corp. has agreed to pay to ML III the consideration that it received for providing the put protection. AIG Financial Products Corp. and ML III are currently negotiating an agreement that will outline procedures to be taken by ML III and AIG Financial Products Corp. for multi-sector CDOs with put options that may be exercised after December 31, 2009, with the objective of mitigating or eliminating the impact on AIG Financial Products Corp. of such 2a-7 Puts and capturing the associated economics for ML III. At December 31, 2008, 2a-7 Puts with a net notional amount of $1.7 billion were outstanding.

Termination Events. Certain of the super senior credit default swaps provide the counterparties with an additional termination right if AIG's rating level falls to BBB or Baa2. At that level, counterparties to the CDS transactions with the following net notional amounts at December 31, 2008, by portfolio, have the right to terminate the transactions early:

	Net Notional Amount At December 31, 2008 (In millions)
Multi-sector CDO	$ 5,501
Corporate arbitrage	27,908
Regulatory capital	5,205
Total	$ 38,614

If counterparties exercise this right, the contracts provide for the counterparties to be compensated for the cost to replace the transactions, or an amount reasonably determined in good faith to estimate the losses the counterparties would incur as a result of the termination of the transactions.

Given the level of uncertainty in estimating both the number of counterparties who may elect to exercise their right to terminate and the payment that may be triggered in connection with any such exercise, AIG is unable to

reasonably estimate the aggregate amount that it would be required to pay under the super senior credit default swaps in the event of any further downgrade.

Certain super senior credit default swaps written for regulatory capital relief, with a net notional amount of $161.5 billion at December 31, 2008, include triggers that require certain actions to be taken by AIG once AIG's rating level falls to certain levels, which, if not taken, give rise to a right of the counterparties to terminate the CDS. Such actions include posting collateral, transferring the swap or providing a guarantee from a more highly rated entity. In light of the rating actions taken in respect of AIG on September 15, 2008, AIGFP has implemented collateral arrangements in a large majority of these transactions. In the event of a termination of the contract that is caused by AIG's rating downgrade, AIGFP is obligated to compensate the counterparty based on its "loss." As a result of AIGFP posting collateral, AIG eliminated the counterparties' right to terminate under this downgrade provision, thereby avoiding the uncertainty of determining the "loss" from an early termination of a regulatory capital CDS.

Collateral

Most of AIGFP's credit default swaps are subject to collateral posting provisions. These provisions differ among counterparties and asset classes. Although AIGFP has collateral posting obligations associated with both regulatory capital relief transactions and arbitrage transactions, the large majority of these obligations to date have been associated with arbitrage transactions in respect of multi-sector CDOs.

The collateral arrangements in respect of the multi-sector CDO, regulatory capital and corporate arbitrage transactions are nearly all documented under a Credit Support Annex (CSA) to an ISDA Master Agreement (Master Agreement). The Master Agreement and CSA forms are standardized form agreements published by the ISDA, which market participants have adopted as the primary contractual framework for various kinds of derivatives transactions, including CDS. The Master Agreement and CSA forms are designed to be customized by counterparties to accommodate their particular requirements for the anticipated types of swap transactions to be entered into. Elective provisions and modifications of the standard terms are negotiated in connection with the execution of these documents. The Master Agreement and CSA permit any provision contained in these documents to be further varied or overridden by the individual transaction confirmations, providing flexibility to tailor provisions to accommodate the requirements of any particular transaction. A CSA, if agreed by the parties to a Master Agreement, supplements and forms part of the Master Agreement and contains provisions (among others) for the valuation of the covered transactions, the delivery and release of collateral, the types of acceptable collateral, the grant of a security interest (in the case of a CSA governed by New York law) or the outright transfer of title (in the case of a CSA governed by English law) in the collateral that is posted, the calculation of the amount of collateral required, the valuation of the collateral provided, the timing of any collateral demand or return, dispute mechanisms, and various other rights, remedies and duties of the parties with respect to the collateral provided.

In general, each party has the right under a CSA to act as the "Valuation Agent" and initiate the calculation of the exposure of one party to the other (Exposure) in respect of transactions covered by the CSA. The valuation calculation may be performed daily, weekly or at some other interval, and the frequency is one of the terms negotiated at the time the CSA is signed. The definition of Exposure under a standard CSA is the amount that would be payable to one party by the other party upon a hypothetical termination of that transaction. This amount is determined, in most cases, by the Valuation Agent using its estimate of mid-market quotations (i.e., the average of hypothetical bid and ask quotations) of the amounts that would be paid for a replacement transaction. AIGFP determines Exposure typically by reference to the mark-to-market valuation of the relevant transaction produced by its systems and specialized models. Exposure amounts are typically determined for all transactions under a Master Agreement (unless the parties have specifically agreed to exclude certain transactions, not to apply the CSA or to set a specific transaction Exposure to zero). The aggregate Exposure less the value of collateral already held by the relevant party (and following application of certain thresholds) results in a net exposure amount (Delivery Amount). If this amount is a positive number, then the other party must deliver collateral with a value equal to the Delivery Amount. Under the standard CSA, the party not acting as Valuation Agent for any particular Exposure calculation may dispute the Valuation Agent's calculation of the Delivery Amount. If the parties are unable to resolve this dispute, the terms of the standard CSA provide that the Valuation Agent is required to recalculate Exposure using, in substitution for the disputed Exposure amounts, the average of actual quotations at mid-market from four leading dealers in the relevant market.

EXHIBIT
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Exhibit 505

CSOC.CBR.00030717

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After an Exposure amount is determined for a transaction subject to a CSA, it is combined with the Exposure amounts for all other transactions under the relevant Master Agreement, which may be netted against one another where the counterparties to a Master Agreement are each exposed to one another in respect of different transactions. Actual collateral postings with respect to a Master Agreement may be affected by other agreed CSA terms, including threshold and independent amounts, that may increase or decrease the amount of collateral posted.

Regulatory Capital Relief Transactions

As of December 31, 2008, 68.0 percent of AIGFP's regulatory capital relief transactions (measured by net notional amount) were subject to a CSA. In other transactions, which represent 1.0 percent of the total net notional amount of the outstanding regulatory capital relief transactions, AIGFP is obligated to put a CSA or alternative collateral arrangement in place if AIG's ratings fall below certain levels (typically, A-/A3). At December 31, 2008, 31.0 percent of the regulatory capital relief portfolio is not subject to collateral posting provisions. In general, each regulatory capital relief transaction is subject to a stand-alone Master Agreement or similar agreement, under which the aggregate Exposure is calculated with reference to only a single transaction.

The underlying mechanism that determines the amount of collateral to be posted varies from one counterparty to another, and there is no standard formula. The varied mechanisms resulted from varied negotiations with different counterparties. The following is a brief description of the primary mechanisms that are currently being employed to determine the amount of collateral posting for this portfolio.

Reference to Market Indices — Under this mechanism, the amount of collateral to be posted is determined based on a formula that references certain tranches of a market index, such as either Itraxx or CDX. This mechanism is used for CDS transactions that reference either corporate loans, or residential mortgages. While the market index is not a direct proxy, it has the advantage of being readily obtainable.

Market Value of Reference Obligation — Under this mechanism the amount of collateral to be posted is determined based on the difference between the net notional amount of a referenced RMBS security and the security's market value.

Expected Loss Models — Under this mechanism, the amount of collateral to be posted is determined based on the amount of expected credit losses, generally determined using a rating-agency model.

Negotiated Amount — Under this mechanism, the amount of collateral to be posted is determined based on bespoke terms negotiated between AIGFP and the counterparty, which could be a fixed percentage of the notional amount or present value of premiums to be earned by AIGFP.

The amount of collateral postings by underlying mechanism as described above with respect to the regulatory capital relief portfolio (prior to consideration of transactions other than AIGFP's super senior credit default swap portfolio subject to the same Master Agreements) were as follows (there were no collateral postings on this portfolio prior to March 31, 2008):

	March 31, 2008	June 30, 2008	September 30, 2008	December 31, 2008	February 18, 2009
			(In millions)		
Reference to market indices	$ 212	$ 177	$ 157	$ 667	$ 417
Market value of reference obligation	—	142	286	380	299
Expected loss models	—	—	—	5	5
Negotiated amount	—	—	—	235	213
Other	—	—	—	—	18
Total	$ 212	$ 319	$ 443	$ 1,287	$ 952

Arbitrage Portfolio — Multi-Sector CDOs

In the large majority of the CDS transactions in respect of multi-sector CDOs, the standard CSA provisions for the calculation of Exposure have been modified, with the Exposure amount determined pursuant to an agreed

formula that is based on the difference between the net notional amount of such transaction and the market value of the relevant underlying CDO security, rather than the replacement value of the transaction. As of any date, the "market value" of the relevant CDO security is the price at which a marketplace participant would be willing to purchase such CDO security in a market transaction on such date, while the "replacement value of the transaction" is the cost on such date of entering into a credit default swap transaction with substantially the same terms on the same referenced obligation (e.g., the CDO security). In cases where a formula is utilized, a transaction-specific threshold is generally factored into the calculation of Exposure, which reduces the amount of collateral required to be posted. These thresholds typically vary based on the credit ratings of AIG and/or the reference obligations, with greater posting obligations arising in the context of lower ratings. For the large majority of counterparties to these transactions, the Master Agreement and CSA cover non-CDS transactions (e.g., interest rate and cross currency swap transactions) as well as CDS transactions. As a result, the amount of collateral to be posted by AIGFP in relation to the CDS transactions will be added to or offset by the amount, if any, of the Exposure AIG has to the counterparty on the non-CDS transactions.

Arbitrage Portfolio — Corporate Debt/CLOs

Almost all of AIGFP's corporate arbitrage transactions are subject to CSAs. 97.6 percent (measured by net notional amount) of these transactions contain no special collateral posting provisions, but are subject to a Master Agreement that includes a CSA. These transactions are treated the same as other transactions subject to the same Master Agreement and CSA, with the calculation of collateral in accordance with the standard CSA procedures outlined above. 17.5 percent (measured by net notional amount) of these transactions, although subject to a Master Agreement and CSA, have specific valuation and threshold provisions. These thresholds are typically based on a combination of the credit rating of AIG and a ratings model of the transaction developed by Moody's model rating of the transaction (and not based on the value of any underlying reference obligations). Thus, as long as AIG maintains a rating above a specified threshold and the Moody's model of the underlying transaction exceeds a specified rating, the collateral provisions do not apply.

Collateral Calls

AIGFP has received collateral calls from counterparties in respect of certain super senior credit default swaps, of which a large majority relate to multi-sector CDOs. To a lesser extent, AIGFP has also received collateral calls in respect of certain super senior credit default swaps entered into by counterparties for regulatory capital relief purposes and in respect of corporate arbitrage.

Frequently, valuation estimates made by counterparties with respect to certain super senior credit default swaps or the underlying reference CDO securities, for purposes of determining the amount of collateral required to be posted by AIGFP in connection with such instruments, have differed, at times significantly, from AIGFP's estimates. In almost all cases, AIGFP has been able to successfully resolve the differences or otherwise reach an accommodation with respect to collateral posting levels, including in certain cases by entering into compromise collateral arrangements. Due to the ongoing nature of these collateral calls, AIGFP may engage in discussions with one or more counterparties in respect of these differences at any time. Valuation estimates made by counterparties for collateral purposes are, like any other third-party valuation, considered in the determination of the fair value estimates of AIGFP's super senior credit default swap portfolio.

Through June 30, 2007, AIGFP had not received any collateral calls related to this super senior credit default swap portfolio. Since that date and through February 18, 2009, counterparties have made large collateral calls against AIGFP, in particular related to the multi-sector CDO portfolio. This was largely driven by deterioration in the market value of the reference obligations and the effects of the downgrade of AIG's ratings.

The amount of collateral postings with respect to AIGFP's super senior credit default swap portfolio (prior to offsets for other transactions) were as follows:

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	December 31, 2007	March 31, 2008	June 30, 2008	September 30, 2008	December 31, 2008
			(In millions)		
Regulatory capital	$ —	$ 212	$ 319	$ 443	$ 1,287
Arbitrage — multi-sector CDO	2,718	7,590	13,241	31,469	5,129
Arbitrage — corporate	161	368	259	902	2,349
Total	$ 2,879	$ 8,170	$13,819	$ 32,814	$ 8,765

The amount of future collateral posting requirements is a function of AIG's credit ratings, the rating of the reference obligations and any further decline in the market value of the relevant reference obligations, with the latter being the most significant factor. While a high level of correlation exists between the amount of collateral posted and the valuation of these contracts in respect of the arbitrage portfolio, a similar relationship does not exist with respect to the regulatory capital portfolio given the nature of how the amount of collateral for these transactions is determined. Given the severe market disruption, lack of observable data and the uncertainty regarding the potential effects on market prices of measures recently undertaken by the federal government to address the credit market disruption, AIGFP is unable to reasonably estimate the amounts of collateral that it would be required to post.

Models and Modeling

AIGFP values its credit default swaps written on the super senior risk layers of designated pools of debt securities or loans using internal valuation models, third-party price estimates and market indices. The principal market was determined to be the market in which super senior credit default swaps of this type and size would be transacted, or have been transacted, with the greatest volume or level of activity. AIG has determined that the principal market participants, therefore, would consist of other large financial institutions who participate in sophisticated over-the-counter derivatives markets. The specific valuation methodologies vary based on the nature of the referenced obligations and availability of market prices.

The valuation of the super senior credit derivatives continues to be challenging given the limitation on the availability of market observable information due to the lack of trading and price transparency in the structured finance market, particularly during and since the second half of 2007. These market conditions have increased the reliance on management estimates and judgments in arriving at an estimate of fair value for financial reporting purposes. Further, disparities in the valuation methodologies employed by market participants and the varying judgments reached by such participants when assessing volatile markets have increased the likelihood that the various parties to these instruments may arrive at significantly different estimates as to their fair values.

AIGFP's valuation methodologies for the super senior credit default swap portfolio have evolved in response to the deteriorating market conditions and the lack of sufficient market observable information. AIG has sought to calibrate the model to available market information and to review the assumptions of the model on a regular basis.

Arbitrage Portfolio — Multi-Sector CDOs

The underlying assumption of the valuation methodology for AIGFP's credit default swap portfolio wrapping multi-sector CDOs is that, to be willing to assume the obligations under a credit default swap, a market participant would require payment of the full difference between the cash price of the underlying tranches of the referenced securities portfolio and the net notional amount specified in the credit default swap.

AIGFP uses a modified version of the Binomial Expansion Technique (BET) model to value its credit default swap portfolio written on super senior tranches of CDOs of ABS, including the 2a-7 Puts. The BET model was developed in 1996 by a major rating agency to generate expected loss estimates for CDO tranches and derive a credit rating for those tranches, and has been widely used ever since.

AIG selected the BET model for the following reasons:

- it is known and utilized by other institutions;
- it has been studied extensively, documented and enhanced over many years;

- it is transparent and relatively simple to apply;
- the parameters required to run the BET model are generally observable; and
- it can easily be modified to use probabilities of default and expected losses derived from the underlying collateral securities market prices instead of using rating-based historical probabilities of default.

The BET model has certain limitations. A well known limitation of the BET model is that it can understate the expected losses for super senior tranches when default correlations are high. The model uses correlations implied from diversity scores which do not capture the tendency for correlations to increase as defaults increase. Recognizing this concern, AIG tested the sensitivity of the valuations to the diversity scores. The results of the testing demonstrated that the valuations are not very sensitive to the diversity scores because the expected losses generated from the prices of the collateral pool securities are currently high, breaching the attachment point in most transactions. Once the attachment point is breached by a sufficient amount, the diversity scores, and their implied correlations, are no longer a significant driver of the valuation of a super senior tranche.

AIGFP has adapted the BET model to estimate the price of the super senior risk layer or tranche of the CDO. AIG modified the BET model to imply default probabilities from market prices for the underlying securities and not from rating agency assumptions. To generate the estimate, the model uses the price estimates for the securities comprising the portfolio of a CDO as an input and converts those price estimates to credit spreads over current LIBOR-based interest rates. These credit spreads are used to determine implied probabilities of default and expected losses on the underlying securities. These data are then aggregated and used to estimate the expected cash flows of the super senior tranche of the CDO.

The application of the modified BET model involves the following steps for each individual super senior tranche of a CDO in the portfolio:

1) Calculation of the cash flow pattern that matches the weighted average life for each underlying security of the CDO;
2) Calculation of an implied credit spread for each security from the price and cash flow pattern determined in step 1. This is an arithmetic process which converts prices to yields (similar to the conversion of United States Department of the Treasury security prices to yields), and then subtracts LIBOR-based interest rates to determine the credit spreads;
3) Conversion of the credit spread into its implied probability of default. This also is an arithmetic process that determines the assumed level of default on the security that would equate the present value of the expected cash flows discounted at a risk-free rate with the present value of the contractual cash flows discounted using LIBOR-based interest rates plus the credit spreads;
4) Generation of expected losses for each underlying security using the probability of default and recovery rate;
5) Aggregation of the cash flows for all securities to create a cash flow profile of the entire collateral pool within the CDO;
6) Division of the collateral pool into a number of hypothetical independent identical securities based on the CDO's diversity score so that the cash flow effects of the portfolio can be mathematically aggregated properly. The purpose of dividing the collateral pool into hypothetical securities is a simplifying assumption used in all BET models as part of a statistical technique that aggregates large amounts of homogeneous data;
7) Simulation of the default behavior of the hypothetical securities using a Monte Carlo simulation and aggregation of the results to derive the effect of the expected losses on the cash flow pattern of the super senior tranche taking into account the cash flow diversion mechanism of the CDO;
8) Discounting of the expected cash flows determined in step 7 using LIBOR-based interest rates to estimate the value of the super senior tranche of the CDO; and