

July 31, 2009

Dear Colleague:

In case you missed it, please find the article below that ran in today's New York Times highlighting the inability of the state insurance regulators to properly oversee AIG. This article further advocates our position that the uneven state based system of insurance regulation with state insurance commissioners with different legal authorities, different funding levels, and varied levels of expertise and priorities, has not provided a comprehensive look at the insurance market.

We introduced H.R. 1880, *The National Insurance Consumer Protection Act*, to create a national insurance regulator with the resources and authority to regulate insurance companies whose breadth and scope far exceed the capabilities of the state-based system. Leaving the business of insurance regulation solely to the various state insurance commissioners fails to keep pace with what, today, is a national and international business. Uniformity of insurance standards and oversight through the creation of a national insurance regulator, with the authority to charter and exclusively regulate national insurers and reinsurers, is the only realistic option.

If you are interested in cosponsoring H.R. 1880 or have any questions, please have your staff contact J.D. Grom w/ Rep. Bean (5-3711) or Mike Ahern w/ Rep. Royce (5-4111).

Sincerely,

Melissa Bean & Ed Royce

Excerpts

“In the months since A.I.G. received its \$182 billion rescue from the Treasury and the Federal Reserve, state insurance regulators have said repeatedly that its core insurance operations were sound — that the financial disaster was caused primarily by a small unit that dealt in exotic derivatives.”

“But state regulatory filings offer a different picture... The companies' weaknesses emerge in their filings with state insurance regulators — particularly when several are reviewed together. But that appears not to happen often, because there are so many. A.I.G. has more than 4,000 units in more than 100 countries....”

“Normally, when an insurance company weakens, regulators in its home state will first measure its capital. They may demand a weak company rebuild its capital, and if it fails, eventually bar it from selling new policies... But policyholder advocates said they feared state regulators were deferring to the wishes of the Fed and Treasury, to use the insurance operations to pay back the taxpayers. ‘The insurance commissioners, for whatever reason, are letting them do this,’ Mr. Myrick said. ‘I’d be jumping out of my shoes.’”

July 31, 2009

After Rescue, New Weakness Seen at A.I.G.

By [MARY WILLIAMS WALSH](#)

http://www.nytimes.com/2009/07/31/business/31aig.html?_r=1&hp

The dozens of insurance companies that make up the [American International Group](#) show signs of considerable weakness even after their corporate parent got the biggest bailout in history, a review of state regulatory filings shows.

Over time, the weaknesses could mean trouble for A.I.G.'s policyholders, and they raise difficult questions for regulators, who normally step in when an insurer gets into trouble. State commissioners are supposed to keep insurers from writing new policies if there is any doubt that they can cover their claims. But in A.I.G.'s case, regulators are eager for the insurers to keep writing new business, because they see it as the best hope of paying back taxpayers.

In the months since A.I.G. received its \$182 billion rescue from the [Treasury](#) and the [Federal Reserve](#), state insurance regulators have said repeatedly that its core insurance operations were sound — that the financial disaster was caused primarily by a small unit that dealt in exotic [derivatives](#).

But state regulatory filings offer a different picture. They show that A.I.G.'s individual insurance companies have been doing an unusual volume of business with each other for many years — investing in each other's [stocks](#); borrowing from each other's investment portfolios; and guaranteeing each other's insurance policies, even when they have lacked the means to make good. Insurance examiners working for the states have occasionally flagged these activities, to little effect.

More ominously, many of A.I.G.'s insurance companies have reduced their own exposure by sending their risks to other companies, often under the same A.I.G. umbrella.

Echoing state regulators' statements, the company said the interdependency of its businesses posed no problem and strongly disputed that any units had obligations they could not pay.

"There is absolutely no concern about the capital in these companies," said Rob Schimek, the chief financial officer of A.I.G.'s property and casualty insurance business. The company authorized him to speak about these issues.

Nothing is wrong with spreading risks to other companies, a practice known as reinsurance, when it is carried out with unrelated, solvent companies. It can also be acceptable in small amounts between related companies. But A.I.G.'s companies have reinsured each other to such a large extent, experts say, that now billions of dollars worth of risks may have ended up at related companies that lack the means to cover them.

"An organization like this one relies on constant, ever-growing premium volume, so it can cover and pay for the deficits," said W. O. Myrick, a retired chief insurance examiner for Louisiana.

If A.I.G.'s incoming premiums shrink, he warned, "the whole thing's going to collapse in on itself."

Mr. Myrick has not fully examined all the A.I.G. subsidiaries but said his own recent review of many state filings raised serious concerns, particularly about the use of reinsurance to "bounce things around inside the holding company group."

"That is a method used by holding companies to falsify the liabilities," he said.

A.I.G.'s premiums have, in fact, been declining in important lines. Its ratings have fallen, and customers tend to steer clear of lower-rated insurers. To woo them back, A.I.G. has in some cases lowered its prices, competitors say. A.I.G.

executives insist they would rather lose a customer than drive down prices dangerously.

A.I.G. has also pledged a share of its life insurance premiums to the Fed, to pay back about \$8 billion. Details have not been provided, but consumer advocates say it is not clear how the life companies will pay future claims if their premiums are diverted.

“Eventually, there’s going to be a battle between the policyholders and the feds,” said Thomas D. Gober, a former insurance examiner who now has his own [forensic](#) accounting firm that specializes in insurance fraud. “The Fed is going to say, ‘We want our money back,’ but the law says, ‘Policyholders come first.’ It’s going to be ugly.”

Mr. Gober is a consultant for a lawsuit on behalf of A.I.G. policyholders, filed in California Superior Court in Los Angeles. The lawsuit seeks a court order requiring all A.I.G. subsidiaries doing business in California to put enough money to cover their obligations into a secure account controlled by the state treasurer.

The goal is to keep money from being moved out of California or used to finance A.I.G.’s other activities, said Maria C. Severson, a lawyer for the plaintiffs.

The lawsuit also seeks to bar A.I.G. companies from soliciting new business without full disclosure of their financial condition.

The condition of A.I.G.’s individual companies is hard to see in the parent company’s filings with the Securities and Exchange Commission. Those filings simply tally all the individual subsidiaries’ financial information.

The companies’ weaknesses emerge in their filings with state insurance regulators — particularly when several are reviewed together. But that appears not to happen often, because there are so many. A.I.G. has more than 4,000 units in more than 100 countries.

Responsibility for A.I.G.'s 71 American insurance companies is spread among 19 state insurance commissions, which do not conduct examinations simultaneously.

As a result, Mr. Myrick said, a conglomerate like A.I.G. "can keep moving assets around to clean up one company" at a time, when examiners were looking. He said that it would take a coordinated, multistate examination of all the insurance companies to catch this.

Mr. Schimek, speaking for the insurance companies, said that in 2005, a team of examiners had at least considered A.I.G.'s property and casualty businesses as a group.

"It was a thorough examination," he said. "I have absolutely no concern about the integrity of the financial information that's been filed under my watch." State regulators confirmed that they believed the A.I.G. subsidiaries under their authority were solvent. Mike Moriarty, deputy insurance superintendent for New York State, said that while A.I.G. subsidiaries did not report all their reinsured obligations on their balances sheets, state regulators could "follow the trail of liabilities" and make sure they did not get lost in the holding company.

Obligations "can't be hidden from state insurance regulators," Mr. Moriarty said.

One A.I.G. subsidiary, the National Union Fire Insurance Company of Pittsburgh, shows what can happen by heavily relying on affiliates. Its most recent regulatory filing in Pennsylvania said it had more than enough money to pay its obligations.

But at the end of 2008, more than a third of National Union's portfolio was invested in the stock of other A.I.G. companies, which are not publicly traded. National Union might not be able to sell all of these shares, and it is not clear what it could get for them. Many states bar insurers from investing that heavily in related companies.

Meanwhile, National Union has \$42.1 billion in obligations looming off its balance sheet. These have been transferred to 56 other A.I.G. companies, through reinsurance. National Union will have to pay any of these claims and then collect from its relatives.

But it is not clear that the affiliates could pay promptly. National Union's biggest reinsurance partner is American Home Assurance, an A.I.G. subsidiary that has taken \$23.1 billion of obligations off National Union's hands. In a New York filing, American Home reports total assets of \$26.3 billion, but part of that consists of assets that cannot be used to pay claims, like furniture. It too includes a number of investments in other A.I.G. companies.

In addition, American Home has "unconditionally" guaranteed the obligations of 16 other A.I.G. subsidiaries, bringing the total it might have to pay to \$140.6 billion.

Normally, when an insurance company weakens, regulators in its home state will first measure its capital. They may demand a weak company rebuild its capital, and if it fails, eventually bar it from selling new policies.

Like New York regulators, Pennsylvania regulators say they do not see a problem. "The insurance companies remain strong and are probably the most valuable assets within the A.I.G. structure," said Joel Ario, Pennsylvania's insurance commissioner. "To the best we know it, we think the companies are sound."

But policyholder advocates said they feared state regulators were deferring to the wishes of the Fed and Treasury, to use the insurance operations to pay back the taxpayers.

"The insurance commissioners, for whatever reason, are letting them do this," Mr. Myrick said. "I'd be jumping out of my shoes."