The Rescue of American International Group Module C: AIG Investment Program

Alec Buchholtz  
Yale School of Management

Aidan Lawson  
Yale School of Management

Follow this and additional works at: https://elischolar.library.yale.edu/journal-of-financial-crisis

Part of the Corporate Finance Commons, Economic History Commons, Economic Policy Commons, Finance Commons, Finance and Financial Management Commons, Insurance Commons, Other Public Affairs, Public Policy and Public Administration Commons, and the Public Economics Commons

Recommended Citation
Available at: https://elischolar.library.yale.edu/journal-of-financial-crisis/vol3/iss1/4

This Case Study is brought to you for free and open access by the Journal of Financial Crises and EliScholar – A Digital Platform for Scholarly Publishing at Yale. For more information, please contact journalfinancialcrises@yale.edu.
READERS TAKE NOTICE:
As of April 2024, the YPFS Resource Library’s site domain has changed to https://elischolar.library.yale.edu/ypfs-financial-crisis-resource-library/.

Please be aware that upon clicking any of the URL references to the former Resource Library domains, either https://ypfs.som.yale.edu or https://ypfsresourcelibrary.blob.core.windows.net/, in the "References/Key Program Documents" section of a case study, readers will encounter a "page not found" error.

Readers can still retrieve a given resource cited within this case study on the new site by searching here for the title cited.

This case study is available in Journal of Financial Crises: https://elischolar.library.yale.edu/journal-of-financial-crisis/vol3/iss1/4
The Rescue of American International Group
Module C: AIG Investment Program

Alec Buchholtz and Aidan Lawson

February 19, 2020, Revised: April 15, 2021

Abstract

In September 2008, the Federal Reserve Bank of New York (FRBNY) extended an $85 billion credit line to AIG to address its liquidity stresses, but AIG’s balance sheet remained under pressure. The insurance giant was projected to report large third-quarter losses and was at risk of being downgraded by major credit rating agencies. For these reasons, in early November 2008, the US Treasury invested $40 billion of Troubled Assets Relief Program (TARP) funds into AIG in exchange for 4 million shares of AIG Series D preferred stock and a warrant to purchase AIG common stock. The investment helped repay a portion of AIG’s debt to the FRBNY, restructured the terms of the credit line, and deleveraged AIG’s balance sheet. With similar concerns arising at the end of the first quarter of 2009, Treasury made a second TARP investment of $30 billion in exchange for 300,000 shares of Series F preferred stock and another common stock warrant. Treasury converted all the preferred stock from its TARP investments into AIG common stock in January 2011 and sold it over the following two years.

Keywords: AIG, Troubled Assets Relief Program (TARP), Emergency Economic Stabilization Act (EESA), preferred stock, warrant, capital injections

1 This case study is one of seven 2021 Yale Program on Financial Stability (YPFS) case modules considering the various elements of the government’s rescue of American International Group:
   • “The Rescue of American International Group, Module D: Maiden Lane II” by Lily S. Engbith and Devyn Jeffereis.
   • “The Rescue of American International Group, Module E: Maiden Lane III” by Lily S. Engbith and Devyn Jeffereis.
   • “The Rescue of American International Group, Module F: The AIG Credit Facility Trust” by Alec Buchholtz and Aidan Lawson.

2 Alec Buchholtz - Research Associate, YPFS, Yale School of Management.

3 Aidan Lawson - Research Associate, YPFS, Yale School of Management.
American International Group, Inc.: AIG Investment Program

At a Glance

Congress passed the Emergency Economic Stabilization Act of 2008 on October 3, 2008, authorizing the creation of the $700 billion Troubled Assets Relief Program (TARP), which the US Treasury used to provide financial assistance to bank, non-bank, and non-financial institutions and markets (EESA 2008). Under TARP, the Systemically Significant Failing Institutions (SSFI) program aimed to “to provide capital on a case-by-case basis to systemically significant institutions that are at substantial risk of failure (Treasury 2008e, 3).”

The Federal Reserve Bank of New York (FRBNY) had extended to AIG, the nation’s largest insurance company, an $85 billion loan in September, but the company’s financial woes continued. In November, Treasury invested $40 billion in AIG under the SSFI program (Webel 2017, 14). AIG used the funds to partially repay some of its debt to the FRBNY under the credit facility (AIG 2010). In exchange, Treasury received 4 million shares of Series D preferred stock and a warrant to purchase 53 million shares of common stock (AIG 2009, 193; Treasury 2008b, pdf 228).

As AIG’s financial condition continued to worsen, the Fed and Treasury announced a restructuring plan in March 2009 in which it modified some of the terms of the November 2008 investment (FRB 2008b). Treasury exchanged the Series D preferred stock it had received for 400,000 shares of Series E preferred stock that better resembled AIG common equity and would thus improve AIG’s financial leverage (FRB 2008b). Further, Treasury committed an additional $30 billion of TARP funds to AIG under an equity capital facility, with $165 million set aside to pay retention bonuses for employees of AIG’s Financial Products unit (GAO 2009, 35). In exchange, Treasury received 300,000 shares of Series F preferred stock and a warrant to purchase 3,000 shares of AIG common stock (GAO 2009, 35). Treasury later retitled the two SSFI investments in AIG the “AIG Investment Program.”

In January 2011, Treasury executed a recapitalization plan for AIG, converting the preferred stock accumulated through the two TARP investments into more than 1 million shares of AIG common stock. By December 2012, Treasury had sold off all its AIG common stock to recoup its investment (Treasury 2012a). In March 2013, Treasury sold its warrants back to AIG, officially ending all government interest and assistance in AIG (Webel 2017, 4).
Summary Evaluation

Financial analysts and regulators believe that the TARP investments in AIG did improve the company’s leverage and restore AIG’s outlook in the eyes of credit rating agencies (Moody’s Investor Service 2008; Moody’s Investor Service 2009). However, the added commitment of $70 billion in taxpayer money, on top of the $85 billion RCF, drew stark criticism from Congress and the public. Disapproval focused in part on the $165 million in retention bonuses for executives in the AIG unit that caused a large portion of its financial losses (SIGTARP 2009a, 15–18).
### American International Group 2008: United States Context

<table>
<thead>
<tr>
<th></th>
<th>2007</th>
<th>2008</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GDP</strong> (SAAR, Nominal GDP in LCU converted to USD)</td>
<td>$14,681.5 billion</td>
<td>$14,559.5 billion</td>
</tr>
<tr>
<td><strong>GDP per capita</strong> (SAAR, Nominal GDP in LCU converted to USD)</td>
<td>$47,976</td>
<td>$48,383</td>
</tr>
<tr>
<td><strong>Sovereign credit rating (five-year senior debt)</strong></td>
<td>As of Q4, 2007:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Fitch: AAA</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Moody’s: Aaa</td>
<td></td>
</tr>
<tr>
<td></td>
<td>S&amp;P: AAA</td>
<td></td>
</tr>
<tr>
<td></td>
<td>As of Q4, 2008:</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Fitch: AAA</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Moody’s: Aaa</td>
<td></td>
</tr>
<tr>
<td></td>
<td>S&amp;P: AAA</td>
<td></td>
</tr>
<tr>
<td><strong>Size of banking system</strong></td>
<td>$9,231.7 billion</td>
<td>$9,938.3 billion</td>
</tr>
<tr>
<td><strong>Size of banking system as a percentage of GDP</strong></td>
<td>62.9%</td>
<td>68.3%</td>
</tr>
<tr>
<td><strong>Size of banking system as a percentage of financial system</strong></td>
<td>Banking system assets equal to 29.0% of financial system in 2007</td>
<td>Banking system assets equal to 30.5% of financial system in 2008</td>
</tr>
<tr>
<td><strong>Five-bank concentration of banking system</strong></td>
<td>43.9%</td>
<td>44.9%</td>
</tr>
<tr>
<td><strong>Foreign involvement in banking system</strong></td>
<td>22%</td>
<td>18%</td>
</tr>
<tr>
<td><strong>Government ownership of banking system</strong></td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td><strong>Existence of deposit insurance</strong></td>
<td>100% insurance on deposits up to $100,000 for 2007</td>
<td>100% insurance on deposits up to $250,000 for 2008</td>
</tr>
</tbody>
</table>

Sources: Bloomberg; World Bank Global Financial Development Database; World Bank, Bank Regulation and Supervision Survey; Federal Deposit Insurance Corporation
I. Overview

Background

By September 2008, wholesale credit markets in the US, which has been under stress most of the year as a result of effects from the subprime mortgage crisis were showing significant signs of strain, which would only worsen when on September 15, the investment bank Lehman brothers filed for bankruptcy. (FCIC 2010, 349). The effects of the bankruptcy were felt throughout the financial system and created additional severe lending stresses as companies hoarded their cash.

For months, American International Group (AIG), a trillion dollar insurance and financial products company had been experiencing liquidity strains. Although its balance sheet was huge, most of its liquid assets and cash were held in its regulated insurance subsidiaries whose regulators would not permit the cash to flow to the holding company or other non-insurance subsidiaries. (FCIC 2010, 344). In the days prior to the Lehman bankruptcy AIG sought a loan from the Federal Reserve Bank of New York (FRBNY). (FCIC 2010, 345).

On September 16, 2008, the Board of Governors of the Federal Reserve, utilizing its emergency lending powers under Section 13(3) of the Federal Reserve Act, announced, with the full support of the Treasury Department, that it had authorized the FRBNY to lend up to $85 billion to AIG (FRBd 2008b; FRBd 2016). The FRBNY would enter into the Revolving Credit Facility (RCF) with AIG, which offered AIG an immediate liquidity cushion to address funding strains some due to collateral calls from trading partners and counterparties of the AIG Financial Products (AIGFP) division (GAO 2011, 25). (See Buchholtz and Lawson 2021a for more details on the terms of the RCF.)

The RCF was the first federal assistance provided to AIG. However, it quickly seemed insufficient to alleviate AIG’s worsening capital and liquidity woes. The company drew $72 billion on the RCF by early November (FRBd 2016). Credit rating agencies continued to express concerns about AIG’s poor capital position and the size and stringency of the company’s debt to the FRBNY (GAO 2011, 8). The US government was also worried that investors would react badly to the upcoming announcement of major third-quarter losses. Negative news could adversely affect investor confidence and damage the value of subsidiaries that the company was trying to offload (GAO 2011, 52–53). The FRBNY even considered asking the rating agencies to take a “ratings holiday,” that is, to refrain temporarily from downgrading the company (GAO 2011, 53). To satisfy rating agencies and stabilize AIG’s financial condition, the government decided to restructure the terms of the RCF and provide further financial assistance to AIG (GAO 2011, 52–53).

The funding to assist AIG was available through the $700 billion Troubled Assets Relief Program (TARP), authorized by Congress under the Emergency Economic Stabilization Act of 2008 (EESA) on October 3, 2008 (EESA 2008). Administered by the Treasury, TARP made available a variety of asset purchase and capital injection facilities “aimed at stabilizing the financial system and restoring liquidity, enabling the flow of credit consumers and businesses, and restoring economic growth” (Treasury 2009b, Summary).
Among them, the Systemically Significant Failing Institutions (SSFI) program aimed “to provide stability and prevent disruption to financial markets in order to limit the impact on the economy and protect American jobs, savings and retirement security from the failure of a systemically significant institution” (Treasury 2008c, 3). The SSFI was later renamed the AIG Investment Program, as AIG was the only company to benefit from the program (See Appendix A more information on the SSFI program.)

**Program Description**

The AIG Investment Program, as the SSFI investments ultimately came to be known, was comprised of two components: the initial Nov 2008 TARP investment and, when that proved insufficient to alleviate AIG’s woes, the March 2009 investment.

**November 2008 TARP Investment**

On November 10, 2008, the Fed and Treasury announced that Treasury would invest $40 billion into AIG via the SSFI program, in part to facilitate repayment of a portion of the debt owed by AIG under the FRBNY’s RCF and in part to provide a cash buffer on AIG’s balance sheet (FRBd 2008b; Webel 2017,14). Since FRBNY’s RCF was extended prior to the passage of TARP, the preferred stock obtained in connection with the RCF loan was issued to an independent Trust established by the FRBNY, and managed by three independent trustees, appointed by the FRBNY, for the benefit of the US Treasury (Webel 2017, 9,11). The original $40 billion, as well as any subsequent capital investments, were made possible through EESA, which gave Treasury, through TARP, the ability to invest in the equity of banks and other institutions, a power it did not have before.

AIG and Treasury signed a Securities Purchase Agreement on November 25, 2008, pursuant to which, in exchange for its investment, Treasury received 4 million shares of AIG Series D fixed-rate cumulative perpetual preferred stock (Series D preferred stock) and a warrant to purchase 2% of AIG’s outstanding common stock (Series D warrant) (Treasury 2008f, 6). Treasury transferred the investment directly to the FRBNY on November 25 on AIG’s behalf (Treasury 2008e, 8). The Series D preferred stock came with an aggregate $40 billion liquidation preference, adjusted to $10,000 per share, with a par value of $5.00 per share and a perpetual life span (Treasury 2008a, pdf 223). Treasury was to receive cumulative dividends on the preferred stock at a rate of 10% per annum paid quarterly when AIG’s board of directors declared dividends (Treasury 2008a, pdf 223). Any unpaid dividends were to compound quarterly. In addition, the Series D preferred stock ranked senior to all other series of preferred stock and AIG common stock (Treasury 2008a, pdf 223).

**Dividends and Directors**

If AIG did not pay dividends to Treasury for four quarters, consecutive or not, Treasury could nominate and elect the greater of two new directors to AIG’s board of directors or the number of directors equal to 20% of AIG’s board of directors (Treasury 2008a, pdf 111). Treasury would be able to elect its choice of directors as a separate class from all other AIG share classes (Treasury 2008a, pdf 111). Following four consecutive quarters of dividend
payments, thereafter, any Treasury-elected director would have to resign. (Treasury 2008a, pdf 111).

Beyond the election of directors associated with unpaid dividends, the Series D preferred stock was non-voting except in the following cases (Treasury 2008a, pdf 111–112):

1. Any authorization or issuance of shares other than convertible preferred stock ranking senior or pari passu to the Series D preferred stock;
2. Any amendment that adversely affects the rights of the Series D preferred stock;
3. Any merger, exchange, or similar transaction unless the Series D preferred stock remains outstanding or is converted into or exchanged for preference securities of the surviving or resulting entity.

Warrant

The Series D warrant allowed Treasury, upon exercise, to purchase 53,798,766 shares of AIG common stock—then 2% of outstanding AIG common stock—at an initial strike, or exercise, price of $2.50 per share (Treasury 2008b, pdf 228). The strike price could be amended based on the market price of the common stock on the day of exercise (Treasury 2008a, pdf 136). The warrant had a duration of 10 years and could be “exercisable upon issuance, in whole or in part” (Treasury 2008b, pdf 136). However, Treasury agreed not to exercise any voting power of the common stock received from the exercise of this warrant at any point (Treasury 2008b, Sec. 4.6, pdf 39).

Executive Compensation

Since the November 2008 investment was made through TARP, AIG was required to change its compensation structure, bonuses, incentives, benefit plans, and other arrangements with senior executive officers to conform to Section 111 of EESA (Treasury 2008g). Section 111 included an “anti-abuse rule” aimed at preventing executives and top officers at institutions receiving TARP aid from reaping the benefits of federal assistance (EESA 2008). EESA provided Treasury the ability to change AIG’s executive compensation and corporate governance standards, including the compensation for senior executive officers; rules on bonuses, retention awards, or other incentive compensation provided to officers and other highly compensated employees; and the prohibition of “golden parachute payments” to the most senior executive officers, among other regulations (GAO 2009, 60).

Table 1, compiled by the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP), summarizes the executive compensation and bonus pool terms included in the government’s November 2008 investment in AIG.
Corporate Governance

In terms of lobbying restrictions, AIG had to adhere to a new “comprehensive written policy on lobbying, governmental ethics, and political activity,” wherein any changes to the existing terms required approval by Treasury (Treasury 2008f, 4). EESA rules also mandated that AIG create a new plan for corporate spending to be approved by Treasury. (Treasury 2008g).

The initial term sheet required AIG to create a risk management committee that would “oversee the major risks involved in [AIG’s] business operations and review [AIG’s] actions to mitigate and manage those risks” (Treasury 2008f, 5). The term sheet required AIG to create such a committee within 30 days of the investment, and it would have to be active, at the minimum, until Treasury no longer owned any shares of Series D preferred stock or common shares purchased through the Series D warrant (Treasury 2008a, pdf 45; Treasury 2008f, 5). Last, the term sheet stipulated that AIG was subject to the same reporting requirements that it had to follow under the FRBNY’s Revolving Credit Facility (Treasury 2008f, 4).

March 2009 TARP Investment

Despite the earlier government assistance, AIG’s woes continued and it worried about another ratings downgrade; the ratings agencies were concerned about a number of factors, including the impact of the RCL on AIG’s leverage ratio. (FRBd 2008c) In March 2009, Treasury announced a second investment under the AIG Investment Program in the form of a $30 billion funding commitment, sometimes referred to as the Equity Capital Facility (ECF), which had a duration of five years, until April 17, 2014 (AIG n.d., 11). In return for the new funding commitment, Treasury received the right to purchase 300,000 shares of Series F

---

Table 1:

Executive and Bonus Compensation Terms for Nov. 2008 TARP Investment in AIG

<table>
<thead>
<tr>
<th>Restriction</th>
<th>Definition</th>
<th>Employees Applicable to</th>
<th>Requirements for Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Golden Parachutes</td>
<td>Any payment in the nature of compensation to (or for the benefit of) the applicable employee(a)</td>
<td>SEOs (the CEO, CFO, and the next 3 highest paid)(b)</td>
<td>Prohibits all severance payments to the aforementioned employee(a)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Senior Partners (the partners who participate in the senior partners plan)(c)</td>
<td>Prohibits severance beyond 3x the aforementioned employees’ base salary(c)</td>
</tr>
<tr>
<td>Bonus Compensation(a)</td>
<td>All payments (cash and assets) made in excess of the executive’s base salary paid with respect to a fiscal year. This does not include:</td>
<td>SEOs (the CEO, CFO, and the next 3 highest paid) and senior partners (the partners who participate in the senior partners plan)</td>
<td>Bonus compensation for FY 2009, retention payments, and termination payments shall not exceed 3.5 times the sum of the senior executives’ base salary and target annual bonus for FY 2008.</td>
</tr>
</tbody>
</table>
fixed-rate non-cumulative perpetual preferred stock (Series F preferred stock) in AIG, as well as another warrant (Series F warrant), this time to purchase 1% of AIG common stock as of the date of the warrant ((Treasury/FRBd 2009; Treasury 2009 2–3). The ECF went into effect on April 17, 2009 (GAO 2009, 35).

The Series F preferred stock had a par value of $5.00 per share, with its liquidation preference beginning at $0 upon issue to Treasury (Treasury 2009d, 8) The stock’s liquidation preference increased by the amount drawn on the new commitment (Treasury 2009d, 5–6). According to SIGTARP, “the shares had no value until cash was disbursed from Treasury,” or drawn upon by AIG (SIGTARP 2009c, 62). For example, if AIG drew $1 billion from the March 2009 investment, the overall value of the Series F preferred stock would increase to $1 billion, reducing the available amount of the Treasury’s investment by an equal amount.

As part of the restructuring, the Treasury also exchanged its Series D cumulative preferred stock for 400,000 shares of Series E non-cumulative preferred stock. The new shares had characteristics closer to common stock are were intended to boost AIG’s balance sheet.

Commitment to make retention payments

Treasury provided AIG $165 million of the total $30 billion commitment to make retention payments to AIG Financial Product employees (Treasury 2009d, 1). The ECF agreement required AIG to repay Treasury for its commitment via three installments of $55 million each from its operating cash flow: on December 17, 2010, August 17, 2012, and April 17, 2014 (Treasury 2009d, 2).

Dividends

Under the Series F purchase agreement, AIG could not make dividend payments on any basic common stock or redeem any shares of common or other capital stock, without the consent of Treasury, prior to the termination of the March 2009 investment. The Series F preferred stock became the most senior of all AIG preferred stock (Treasury 2009a, 2). Treasury would receive non-cumulative dividends “at a rate per annum equal to the applicable dividend rate [10% per annum] on the applicable liquidation amount per share of the Series F preferred stock,” payable quarterly, in arrears on February 1, May 1, August 1, and November 1 every year, and payable when declared by AIG’s board of directors (Treasury 2009a, A-2).

As shareholders of the Series F preferred stock, Treasury had the right to nominate and elect the greater of two new directors to AIG’s board of directors or the amount of directors equal to 20% of AIG’s board (Treasury 2009a, A-7). However, unlike the Series D preferred stock, this right would become exercisable if dividends were not paid for any four quarters, whether consecutive or not (Treasury 2009a, A-7).

Warrant

Treasury’s purchase of the Series F warrant on April 17 enabled the government to purchase 1%, or 3,000 outstanding, unissued shares of AIG common stock (Treasury 2009e, 2). The warrant had an initial strike, or exercise, price of $2.50 per share and a 10-year limit
“exercisable upon issuance, in whole or in part” (Treasury 2009f, 5). Moreover, Treasury agreed not to exercise any voting rights of AIG common stock acquired upon exercising the Series F Warrant (Treasury 2009f, 7).

Executive Compensation

Executive compensation restrictions were broadened with the passage of the American Recovery and Reinvestment Act of 2009 (ARRA) in February of 2009. Bonus restrictions from EESA that applied exclusively to senior executive officers (SEOs) extended to SEOs and the 20 next highest paid employees (ARRA 2009, 518). AIG was allowed to issue “long-term, restricted stock” to those same employees in lieu of now-prohibited bonuses, retention awards, and incentive payments, so long as the stock did not vest while AIG had TARP funds outstanding and the grant would not be more than one-third of total compensation to the employee receiving it (ARRA 2009, 518). Prohibitions on golden parachute payments, likewise, were extended to SEOs and the five next highest paid employees.

Corporate Governance

There were no significant changes with respect to corporate governance in the March 2009 restructuring. After the March 2009 investment, Treasury issued additional guidance on these issues, summarized in their Interim Final Rule on TARP Standards for Compensation and Corporate Governance, released on June 10, 2009 (Treasury 2009c).

This rule was designed to implement the ARRA provisions and consolidate all of the executive-compensation-related provisions directed at TARP recipients into a single rule. The rule (1) limited executive compensation for certain executives and highly compensated employees at companies receiving TARP funds, (2) appointed a special master to review compensation plans at such firms, (3) implemented and expanded earlier Treasury proposals regarding the need for shareholders and directors to work together on compensation issues, (4) set additional compensation and governance standards for firm to improve accountability and disclosure. (Treasury 2009c).

For an overview of the two TARP investments in AIG in November 2008 and March 2009, see Table 2.
Table 2: November 2008 and March 2009 TARP Investments in AIG

<table>
<thead>
<tr>
<th></th>
<th>November 2008 Investment</th>
<th>March 2009 Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Program</strong></td>
<td>Systemically Significant Financial Institutions (SSFI) via TARP</td>
<td>Systemically Significant Financial Institutions (SSFI) via TARP</td>
</tr>
<tr>
<td><strong>Date Announced</strong></td>
<td>November 25, 2008</td>
<td>April 17, 2009</td>
</tr>
<tr>
<td><strong>Amount</strong></td>
<td>$40 billion capital injection</td>
<td>$30 billion commitment</td>
</tr>
<tr>
<td><strong>Preferred Stock</strong></td>
<td>4 million shares of Series D fixed-rate cumulative perpetual preferred stock (Exchanged for 400,000 shares of Series E non-cumulative preferred stock in March 2009)</td>
<td>300,000 shares of Series F fixed-rate non-cumulative perpetual preferred stock ($2 billion was exchanged for 20,000 shares of Series G cumulative preferred stock at Recapitalization in January 2011)</td>
</tr>
<tr>
<td><strong>Warrant</strong></td>
<td>2% of AIG’s outstanding common stock</td>
<td>1% of AIG’s outstanding common stock</td>
</tr>
</tbody>
</table>

Outcomes

**November 2008 Investment**

On November 10, 2008, the Board of Governors, Treasury, and AIG announced a restructuring plan for AIG (which closed on November 25, 2008) (COP 2010b; Treasury 2008f). The November 2008 investment enabled AIG to repay some of the amount that it had drawn on the FRBNY’s RCF; the amount of available credit under the RCF was also reduced from $85 billion to $60 billion (FRBd 2016, 6).

The November 2008 investment helped to restructure AIG’s balance sheet, thereby avoiding any downgrades from the major credit rating agencies. It also contributed to a restructuring of the terms of the RCF under the Credit Agreement (YPFS 2018a). The AIG common stock into which the Series C preferred stock issued pursuant to the RCF could be converted was adjusted to 77.9% of AIG outstanding common stock to accommodate the 2% conversion under the Series D warrant, keeping the total conversion amount at less than 80% for accounting reasons (Treasury 2008f, 6). Generally Accepted Accounting Principles (GAAP) standards, if the government’s ownership was 80% or greater, it would be deemed to control the company and would be required to consolidate AIG’s balance sheet with the government balance sheet, something the government sought to avoid, although ultimately, it would have to consolidate the company. (See Buchholtz and Lawson 2021a for more information on the changes implemented to the terms of the RCF and the preferred stock.)
With the expectation that 2008 fourth-quarter losses would be greater than $40 billion and that credit agencies would further likely downgrade AIG, the US government sought to provide additional aid to the insurance firm (COP 2010b, Sec. 1[D][1]). In March 2009, the US government announced a second restructuring plan for AIG, which included exchanging the 4 million shares of Series D preferred stock worth $40 billion for 400,000 shares of Series E preferred stock worth $41.6 billion⁴ (SIGTARP 2009c, 62). The Series E preferred stock provided for non-cumulative dividends, unlike the cumulative dividends of Series D, and limited AIG’s ability to redeem the preferred stock except with the proceeds from the issuance of equity capital” (SIGTARP 2009c, 62). The Series E preferred stock also permitted Treasury to elect new directors to AIG’s board of directors if dividends were not paid for four quarters, consecutive or not (SIGTARP 2009, 61).

The Series E preferred stock was also subject to a Replacement Capital Covenant, which stated that AIG could not repurchase the Series E preferred stock from Treasury prior to April 17, 2012, unless AIG replaced the Series E preferred stock with “qualifying equity replacement capital securities” (Treasury 2009d, 1). Eligible qualifying securities included common stock, qualifying warrants, qualifying non-cumulative preferred stock, or mandatorily convertible preferred stock (Treasury 2009d, 1).

In their initial report to Congress, Treasury and the Federal Reserve Board stated that the new Series E preferred stock would “more closely resemble common equity and thus improve the quality of AIG’s equity and financial leverage” (Treasury 2009b, 8–9). The Series E shares were seen as more like common shares because their dividends were non-cumulative, meaning the company was under no obligation to pay past dividends; the Series D preferred shares had been cumulative (GAO 2011, 10–11). This idea proved successful as credit rating agencies viewed the new Series E preferred stock more favorably than the Series D preferred stock when assessing AIG’s financial situation at the time (GAO 2011, 10–11).

During AIG’s 2009 Annual Meeting of Shareholders, AIG stockholders voted to conduct a 20-to-1 reverse stock split, which affected the total amount of stock available for purchase under the Series D warrant, but nonetheless allowed Treasury to purchase 2% of the outstanding AIG common stock upon exercise (SIGTARP 2011, 61). Another vote during the meeting increased the exercise price of AIG common stock from $2.50 to $50.00 per share (SIGTARP 2011, 61). (See Buchholtz and Lawson 2021a for more information on the events of the 2009 shareholder meeting.)

In September 2010, Treasury, the FRBNY, and AIG, designed a Recapitalization Plan (Recapitalization) for all of the federal assistance provided to AIG (AIG et al 2010a). As part of the Recapitalization, Treasury converted the 400,000 shares of Series E preferred stock to...

---

⁴ The 400,000 shares of Series E preferred stock were valued at $104,011.44 per share, up from the $10,000 per share of the Series D preferred stock. The higher proportional value per share for Series E shares also includes about $1.6 billion in cumulative unpaid dividends that was due to Treasury on the Series D preferred stock (GAO 2011).
924,546,133 shares of AIG common stock, on January 14, 2011, representing 51.4% of all outstanding AIG common stock (AIG et al 2010a, 2).

**Executive Compensation Controversy**

In March 2009 it became public knowledge that AIG planned to pay $218 million in retention bonuses to more than 400 employees of its AIG Financial Product Division, which had contributed to AIG’s near-failure. While the payments provoked public outcry, legal opinions from private parties and government counsels all concluded that the retention plans for those employees were contractually binding (SIGTARP 2009a, Summary). More specifically, because AIG agreed to the payments prior to the passage by Congress of the American Recovery and Reinvestment Act of 2009 (ARRA) on February 11, 2009, the payments were not subject to executive compensation restrictions enacted by EESA, ARRA, or related Treasury guidelines. (SIGTARP 2009a, 400). In late March 2009, Treasury Secretary Timothy Geithner requested that the Department of Justice (DOJ) conduct an investigation into the retention payments and determine if there was a “legal basis to recoup the retention awards” (SIGTARP 2009a, 17). However, the DOJ concluded there were no alternatives to paying the bonuses that had legal merit (SIGTARP 2009a, 17).

**March 2009 Investment**

At the 2009 Annual Meeting, shareholders passed a resolution to reduce the par value of AIG common stock, which reduced the Series F warrant’s exercise price from $2.50 to $0.00002 per share (SIGTARP 2011, 63).

Prior to recapitalization, AIG had drawn about $7.5 billion of the $30 billion March 2009 investment (GAO 2011, 33). However, the March 2009 investment played a large role during the January 2011 recapitalization of AIG. Of the $7.5 billion drawn on the commitment, Treasury exchanged $2 billion of the Series F preferred stock for 20,000 shares of Series G preferred stock (AIG et al 2010; AIG 2011, 11). Treasury exchanged the remaining $5.5 billion of Series F preferred stock for approximately 167.6 million shares of AIG common stock at $2.50 per share (AIG et al 2010a, 1). Last, AIG drew down the remaining amount of $20.3 billion under the March 2009 investment to purchase from the FRBNY preferred interests in two special purpose vehicles established by AIG (AIA Preferred Interests and ALICO Preferred Interests). AIG had transferred such preferred interests to the FRBNY in partial payment for amount outstanding under the RCF. (AIG et al 2010, 1-2; AIG 2011, 10).

**Treasury’s Stake in AIG after Recapitalization**

The Office of Financial Stability (OFS), which was created with the passage of TARP to manage the program, was used to manage the shares that Treasury held directly. Treasury gradually sold the AIG common stock converted from the Series E and the Series F preferred

---

5 Further, Treasury’s interim final rules on ARRA compensation guidelines for financial institutions receiving federal assistance, published on June 15, 2009, also reiterated that restrictions did not apply to payment agreements agreed upon prior to the guidelines (SIGTARP 2009a, 30).
stock during recapitalization to the public, with the final sale of the remaining stock coming on December 10, 2012. Treasury received $38.2 billion in net proceeds from the sales (Treasury 2013, 14). Treasury never exercised the Series D and Series F warrants, and in March 2013 sold both warrants back to AIG for approximately $25 million, in aggregate (Treasury 2013, 14).

2010 Shareholder Meeting

By the beginning of February 2010, AIG had not reinstated dividend payments to shareholders, which AIG’s board of directors had originally suspended to all share classes on September 23, 2008 (AIG 2008, 137). Therefore, on February 1, 2010, following more than four quarters without dividend payments, Treasury exercised its right to elect new directors to AIG’s board of directors granted by the Series E and Series F preferred stock (GAO 2011; Treasury/FRBd 2009). At the time of the 2010 Annual Meeting, since 11 directors held seats on AIG’s board, Treasury was able to nominate and elect the number of members equal to 20% of the board, or in this case, two new directors, increasing the total numbers to thirteen. (AIG 2010, 19).

According to the terms of the Series E and Series F preferred stock, any directors elected by Treasury would step down from AIG’s board of directors when dividends had been paid for four consecutive quarters following their election (Treasury/FRBd 2009). However, following the execution of the recapitalization, AIG’s Nominating and Corporate Governance Committee decided that it would be in the best interest of AIG and its shareholders to keep the two Treasury elected directors on AIG’s board of directors.

II. Key Design Decisions

1. The AIG Investment Program was part of a multi-faceted intervention by the US government.

The Treasury’s initial investment in AIG, was announced on November 10, 2008, as part of a restructuring plan put forth by FRBNY and Treasury. The plan restructured the original aid that AIG had obtained from FRBNY under the Revolving Credit Facility (RCF) to make the terms less aggressive, contingent on the disbursement of a capital injection via the Treasury’s purchase of $40 billion in cumulative perpetual preferred Series D stock ((FRBd 2008c, 4-6). Additionally, the $37.8 billion Securities Borrowing Facility, which had been established in early October by the FRBNY, would be terminated in favor of Maiden Lane II and III, two new facilities that were designed to purchase (1) residential mortgage-backed securities (RMBS) in the company’s securities lending and (2) underlying Collateralized Debt Obligations (CDOs) from credit default swap counterparties, respectively (FRBd 2008c, 4-9). The combined funds provided by the Treasury and Fed for AIG totaled $182.3 billion (Treasury 2012b).

2. The Treasury used Troubled Assets Relief Program (TARP) funds to finance the AIG Investment Program.
Congress passed the Emergency Economic Stabilization Act of 2008 (EESA) on October 3, 2008. Section 101 of the Act established TARP as the principal vehicle through which Treasury would fight the crisis (EESA 2008, Sec. 101). The Systemically Significant Failing Institutions (SSFI program), later AIG Investment Program, was one of the many programs that came out of the first wave of TARP funding and AIG was its only beneficiary (EESA 2008, Title).

3. Treasury, through the Office of Financial Stability, was the manager and administrator of the program.

Treasury created the Office of Financial Stability (OFS) as directed by Section 101 of EESA to act as a general administrator for all TARP programs, which included monitoring the equity obtained through the AIG Investment Program.

4. AIG was required to comply with restrictions on executive compensation and corporate governance that were outlined in Section 111 of EESA.

Any institutions that took TARP capital were subject to certain restrictions on executive compensation. Treasury, per Section 111 of EESA, required that AIG, “comply with the most stringent limitations on executive compensation for its top five senior executive officers” (Treasury 2008f). Additionally, the legislation included limitations on bonus and “golden parachute” payments, as well as lobbying restrictions (EESA 2008, Sec. 111).

These restrictions would become more stringent with the passage of ARRA in February of 2009. The bonus and golden parachute restrictions would be broadened and retention and incentive rewards prohibited (except in the case of long-term, restricted stock). Treasury published additional guidance on executive compensation in an Interim Final Rule, dated June 10, 2009. The rule included a clawback provision on executive compensation, the creation of a special master for TARP executive compensation, and further accountability for the boards of directors of institutions receiving TARP funds (Treasury 2009c).

In addition to the conditions for accepting the TARP investment, AIG was required to create a risk management committee within 30 days that would “oversee the major risks involved in [AIG’s] business operations and review [AIG’s] actions to mitigate and manage those risks” (Treasury 2008f, 5). The committee was required to be active at least until Treasury no longer owned any shares of Series D preferred stock or the Series D warrant (Treasury 2008f, 5). As part of the terms of the Series D stock, the firm also was required to “continue

---

6 ARRA specified that prohibitions on “accruing any bonus, retention award, or incentive compensation” during the period in which an institution had TARP funding outstanding would not apply if payments in lieu of these were made in the form of “long-term, restricted stock.” These restrictions applied to AIG’s SEOs as well as its 20 next-highest compensated employees. For further discussion of the characteristics of this stock see ARRA, Sec. 7001.

7 While the term sheet said AIG had to create such a committee within 30 days of the investment, Treasury’s guidelines to EESA released in early October 2008 dictated that a committee must be created within 90 days (Treasury 2008d).
to maintain and implement its comprehensive written policy on lobbying, governmental ethics, and political activity . . . .” (Treasury 2008f, 4). Any changes to this plan were required to be approved by Treasury (Treasury 2008f, 3).

5. **FRBNY and Treasury released the details of the AIG Investment Program and Restructuring Plan on November 10, 2008, the same day that AIG released its third-quarter results.**

The decision to release details of the Restructuring Plan on the same day that AIG released its earnings was made because officials had anticipated that AIG would face the possibility of a ratings downgrade or other negative market reaction based on newly reported losses (GAO 2011, 52 - 53). Treasury stated that, “Together with the steps taken by the Federal Reserve, this restructuring will improve the ability of the firm to execute its asset disposition plan in an orderly manner” (Treasury 2008f). Treasury further stated that the $40 billion investment “was necessary to preserve stability in the financial system and to give AIG time to sell assets in an orderly manner to pay back taxpayers” (Treasury 2008e, 8).

6. **Treasury invested $40 billion into AIG in November 2008 as part of a joint Treasury–Federal Reserve restructuring effort of AIG assistance to improve its capital position.**

Despite the $85 billion RCF that the government extended to AIG on September 22, 2008, the company’s liquidity issues persisted, and AIG remained at risk of a ratings downgrade (GAO 2011, 129). The loan alleviated AIG’s immediate problems, but it actually “increased the company’s leverage and lowered [its] interest coverage ratio, two key metrics used by credit rating agencies in assessing the financial strength of an issuer” (FRBd 2008c, 4).

As a result, on November 10, 2008, the Board of Governors and Treasury announced a restructuring plan pursuant to which Treasury would invest $40 billion in funds in AIG, which the company would use to pay down amounts borrowed under the RCF. (Treasury 2008f). According to Treasury, the investment aimed to “restructure federal assistance” to AIG and help it to “execute its asset disposition plan in an orderly manner” (Treasury 2008f) by “establish[ing] a ‘durable capital structure’ for AIG and facilities designed to resolve the liquidity issues AIG had experienced in its CDS [credit default swap] portfolio and its US securities lending program” (AIG 2008, 1). Treasury also would exchange the preferred shares that it held for a new preferred share that had more properties in common with common stock. And the credit agreement was amended to reduce the interest rate, the commitment fee, and the maturity date associated with the RCF which was extended from two years to five years. (FRBNY 2008). (GAO 2011, 45).

7. **Treasury received shares of Series D cumulative preferred stock and a warrant to purchase 2% of outstanding AIG common stock to increase the return to taxpayers in the event that AIG ultimately recovered.**

According to the Federal Reserve Board general counsel Scott Alvarez, Treasury’s receipt of Series D preferred stock was based on a review of the equity classes that were already authorized by the company. Alvarez stated that in order to come to agreements with AIG
quickly, the government needed to use every resource available and avoid having to seek a shareholder vote in order to issue new classes of preferred stock (YPFS 2018b).

Lastly, Treasury also received a 10-year Series D warrant that allowed it to purchase 53,798,766 shares of AIG common stock, which represented 2% of outstanding AIG common stock at the time (Treasury 2008b, pdf 127). The strike price, which was $2.50 at the time, could be amended based on the market price of the common stock on the day of exercise (Treasury 2008a, pdf 136). The warrant, if exercised, allowed the sale of AIG common stock, which would contribute to Treasury's ability to recoup the funds invested in AIG (Treasury 2008a, pdf 131–144).

8. The Series D cumulative preferred stock was exchanged for Series E non-cumulative preferred stock that better resembled common equity in March 2009.

The exchange from Series D to E preferred stock occurred on March 4, 2009, after a restructuring agreement, dated March 2, was finalized. One of the major changes that came with this exchange was that the dividends on the Series E preferred equity were non-cumulative, whereas they were cumulative for the Series D preferred equity (GAO 2011, 10). The Series E preferred stock (and Series F preferred stock after it) more closely resembled common equity, as AIG was not obligated to pay out missed dividends, and thus, rating agencies evaluated the stock more positively (GAO 2011, 10–11).

9. The Series E Preferred Stock was subject to a Replacement Capital Covenant, which clarified Treasury’s senior rights to repayment and served as notice that the government would continue to support AIG.

A Replacement Capital Covenant (the Covenant) was placed on the Series E preferred stock to ensure that AIG could not repurchase the Series E preferred stock prior to repaying Treasury for the November 2008 investment, unless AIG replaced the Series E preferred stock with “qualifying equity replacement capital securities” (Treasury 2009d, 1). The Covenant also provided that Treasury would have senior rights to receive repayments before any new AIG debtholders.

Treasury’s Chief Restructuring Officer, Jim Millstein, stated that the credit rating agencies and AIG’s auditor, PricewaterhouseCoopers, were concerned in early 2009 that AIG would announce losses of more than $40 billion in its upcoming 2008 annual report; in fact, AIG reported losses of more than $60 billion (COP 2010b, Oversight Report – Section 1[D][5]). The rating agencies and AIG’s auditor wanted assurance that the government would continue to stand behind AIG after the 2008 losses were reported (YPFS 2018a). More specifically, the auditor wished to issue AIG’s financial statements without a going concern qualification, which likely would have led to a credit downgrade, and consequently to further liquidity runs on AIG by counterparties (YPFS 2018a). The Covenant served as a notice that the government stood behind its investments to AIG and allowed the auditor to feel comfortable in issuing AIG’s 2008 statements (YPFS 2018a).
10. In March 2009, Treasury committed an additional $30 billion to AIG via the AIG Investment Program to signal that the government would continue to stand behind AIG.

In a joint press release with the Federal Reserve Board, on March 2, 2009, Treasury announced its intent to commit the $30 billion investment, sometimes referred to as the Equity Capital Facility (ECF). (Treasury/FRBd 2009). AIG assets continued to be in low demand and the possibility of further credit downgrades again was a major factor in the US government’s decision (Treasury/FRBd 2009). According to Treasury’s Chief Restructuring Officer, Jim Millstein, fourth-quarter 2008 losses “prompted AIG’s auditors and credit rating agencies to require incremental equity in order to ensure that [AIG] had sufficient liquidity” (COP 2010a, 8). The new commitment signaled to AIG’s auditors and credit rating agencies that the US government stood behind AIG even with its losses, providing an additional $30 billion of credit if need be, thereby allowing the auditor to issue AIG’s 2008 financial statements without a going concern qualification and allow AIG to maintain its credit ratings (COP 2010a, 8).

At the time, according to FRBNY records, the government considered a variety of new financial packages for AIG. One possibility was to establish “a derivatives products company with a government backstop to engage in transactions with AIG Financial Products’ derivative counterparties . . . .” Another was to fully nationalize AIG. This was seen as a potentially attractive option because, “...although nationalization posed a number of risks and issues, it simplified certain aspects of the AIG situation. For instance, it would have provided a solution for AIGFP, prevented credit ratings downgrades, and addressed complex restructuring issues that would no longer have been relevant” (GAO 2011, 50). Ultimately, what became the March 2009 investment was intended to “strengthen AIG’s capital levels and improve its leverage” (GAO 2011, 11).

As part of the March 2009 investment agreement, AIG was to submit an outline on its use of the capital received from Treasury’s purchase of Series F preferred stock (Treasury 2009d, 5). According to a July 2010 SIGTARP report, AIG used funds from the March 2009 investment to (SIGTARP 2010, 87–88):

“meet capital solvency requirements resulting from declines in the value of AIG’s investments, purchase shares of United Guaranty Corporation (“UGC”), an AIG subsidiary; provide capital support to UGC; settle payments for UGC; redeem all of its preferred shares held by National Union Fire Insurance Company of Pittsburgh; purchase its shares from American International Assurance Co., Ltd. (“AIA”) subsidiaries AIA(B) and Philam Life AIG; and purchase its shares held by the American Life Insurance Company (“ALICO”) unit (Japan).”

11. Treasury received shares of Series F non-cumulative preferred stock and a warrant to purchase 1% of outstanding AIG common stock to provide further potential upside to taxpayers.
As in the case of the Series D shares, the Treasury chose to receive preferred shares. Like the Series E shares, dividend payment under the Series F preferred stock were non-cumulative.

The Series F preferred stock also came with warrants. Similar to the Series D warrant included in the November 2008 investment, the Series F warrant served as an additional consideration to the corresponding preferred stock. If exercised, the sale of the received common stock could contribute to Treasury’s ability to recoup the funds invested in AIG (Treasury/FRBd 2009; Treasury 2008f).

12. Using its authorities under Section 111(b) of EESA, Treasury imposed executive compensation, bonus payment, and corporate governance restrictions on AIG.

Based on its powers under Section 111(b) of EESA, Treasury placed strict compensation restrictions and corporate governance guidelines on TARP recipients (EESA 2008). Prior to the announcement of the first restructuring plan, however, Treasury determined that because AIG was already receiving federal assistance from the FRBNY, via the RCF and Maiden Lane facilities, it would impose “greater compensation restrictions than those imposed on [other] financial institutions” receiving TARP assistance (SIGTARP 2009a 4).

According to the Treasury’s Notice 2008-PSSFI, to comply with EESA Section 111(b)(2)(A), a committee had to be established “to review the relationship between risk management policies and executive compensation arrangements” (Treasury 2008d, 3). The committee also had to review compensation plans for senior executive officers and ensure that those employees were not incentivized via bonuses to take “unnecessary and excessive risks that threaten the value of the financial institution” (Treasury 2008d, 3).

13. Of the total March 2009 investment, $165 million was allocated to retention payments to AIG Financial Products employees. These payments were seen as contractually committed and necessary to maximize value as AIG unwound its derivatives portfolio.

Although $30 billion was committed, in aggregate, to AIG under the March 2009 investment, the maximum commitment decreased to slightly more than $29.8 billion after Treasury designated $165 million of the commitment to retention payments for employees of AIG Financial Products (AIGFP), AIG Trading Group, Inc., and the respective subsidiaries of both8 (GAO 2009, 35). These retention payments were intended to maintain operations and contribute to the wind down of CDS portfolios within the Financial Products division. However, to ensure that Treasury recouped the $165 million, a commitment fee was included in the terms of the March 2009 investment, which AIG would pay in three installments of $55 million each, due on December 17, 2010; August 17, 2012; and April 17, 2014 (Treasury 2009d, 2).

---

8 Shortly after the creation of the March 2009 investment, the House of Representatives passed a bill that placed a 90% tax on all bonuses paid to employees of companies receiving TARP funds. The Senate version of the bill decreased the bonus tax to 70% (35% to the corporation and 35% to the employee), however it did not pass when brought to a vote (Dye 2010).
At the time of both TARP investments, the FRBNY was closely monitoring AIG’s financial situation and was aware of the payments extended to employees to retain their services as they wound down the complex trades and general operations of AIGFP (SIGTARP 2009a, 11–13). It was not until late February 2009 that Treasury was included in discussions about the retention plans for AIGFP employees, as the retention payments had "garnered press and Congressional attention" (SIGTARP 2009a, 13).

According to then–Secretary of the Treasury Timothy Geithner, former AIG Chief Executive Officer Ed Liddy communicated to him that $165 million of retention bonuses were “contractually committed and payable by March 15 [2009]” to AIGFP employees and that the “contracts were legally binding” (Geithner 2009, 1). Following the advice of Treasury’s counsel, Geithner indicated that any contracts signed prior to the passage of the ARRA were still effective, notwithstanding any executive compensation limits under ARRA (Geithner 2009, 1). Thus, Treasury and AIG devoted $165 million of the March 2009 investment to the retention payments, including commitment fees “to recover funds on behalf of taxpayers” (Geithner 2009, 2).

14. In 2011, the Treasury and Federal Reserve engaged in a proactive restructuring and recapitalization to reduce AIG’s reliance on government funding and allow the government to exit its investment in AIG.

While the preferred stock had a perpetual term length, the original SSFI agreement provided that Treasury’s consent would be needed if any equity were repurchased prior to (1) the fifth anniversary of the agreement being signed, or (2) the entirety of Treasury's stake in AIG being sold off to third parties. Subsequent to one of these conditions being met, AIG could purchase the warrant for the Series D preferred stock (Treasury 2008f, 2). The Equity Capital Facility (ECF) also had a five-year lifespan, but neither the ECF nor the original SSFI investment was held for that long.

Following the signing of the Recapitalization Agreement on January 14, 2011, the Treasury exchanged its remaining preferred stock for common stock. After completion of the plan, Treasury held about 1.65 billion shares of AIG common stock that it would offer to the public (GAO 2012, 10–12). The $30 billion ECF from the March 2009 agreement would, in conjunction with the January 2011 agreement, be converted into (1) approximately 167 million shares of common stock, (2) 20,000 shares of Series G cumulative preferred stock, and (3) preferred Interests in the AIA and ALICO SPVs (AIG 2011, 11).

Treasury began to sell its holdings of AIG common stock in early 2011 through six public offerings (Treasury 2012a, 1). These sales garnered an average price of $31.18 per share and netted the government approximately $4.1 billion in profits (Treasury 2012a, 1). The final sale occurred on December 10, 2012 (Treasury 2013, 14). The Treasury also earned $0.9 billion from its preferred stock holdings, for a combined profit of $5 billion. (Treasury 2012a, 1).
III. Evaluation

Treasury authorized a total of $69.8 billion for investment into AIG and ultimately disbursed $67.8 billion (Treasury 2013, 14). Treasury exchanged AIG’s right to draw down the final $2 billion for 20,000 shares of Series G preferred stock (AIG 2011, 11). Treasury completed the public sale of all TARP-related AIG common stock that it held in December 2012 (Webel 2013, 2). AIG would repurchase the Series D and Series F warrants on March 1, 2013, for $25 million (Treasury 2013, 14). According to the Congressional Research Service, the final net loss for Treasury on its TARP investments in AIG approximated $13.5 billion; however, the overall profit from sales of AIG stock held by the government, including the stock held by the AIG Trust, were approximately $5 million (Webel 2013, 9).

Although proceeds from the TARP reimbursements were less than Treasury’s investments, the Office of the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) argued, “this was offset by the proceeds from the additional Treasury shares of AIG, resulting in overall proceeds exceeding disbursements for Treasury” (Treasury 2013, 14).

Credit rating agencies viewed both TARP investments in AIG favorably, maintaining AIG’s credit rating following each of the two investment announcements in November 2008 and March 2009 (Moody’s Investor Service 2008; Moody’s Investor Service 2009). Commenting on the November 2008 investment, Moody’s said, the “recapitalization and de-risking transactions provide AIG with additional time and flexibility to facilitate asset sales and bolster AIG’s operating performance” (Moody’s Investor Service 2008). Moody’s also said the new capital structure would promote market confidence, especially from AIG counterparties, and “[provide] significant incremental protection for senior creditors” at the time (Moody’s Investor Service 2008). In March 2009, despite AIG’s $61.7 billion loss for the fourth quarter of 2008, Treasury’s $30 billion investment gave credit rating agencies renewed confidence in AIG’s viability (Moody’s Investor Service 2009). S&P said the new $30 billion commitment and the continuance of federal financial assistance to AIG “improves [AIG’s] capital adequacy and reduces pressure on debt holders” (Scroggins 2009).

The $165 million AIGFP retention payments and exclusion of 57 employees from executive compensation restrictions drew considerable public and congressional outrage in March 2009 (SIGTARP 2009a, 16–18). SIGTARP released an audit examining the compensation plans at AIG. It noted that the public and Congress mainly questioned why AIG was rewarding the employees of the division whose losses were largely blamed for the losses and near bankruptcy of the company, meaning the Financial Products Division (AIGFP). (SIGTARP 2009a, 2). The SIGTARP audit found that AIGFP employees had lost “$790 million in future compensation” based on AIG’s performance as of March 2009 (SIGTARP 2009a, 7). It further found that the compensation plans and rewards encouraged employees, who were unsure of their job stability because of the market conditions and AIG’s circumstances, to stay with AIG (SIGTARP 2009a, 7).

Through a series of debates over amending the US tax code, Democrats and Republicans both agreed that employee bonuses should be subject to a high corporate tax for companies that received more than $5 billion from TARP (H.R. 1586, H3656). The bonus tax rate was
disputed, ranging from 90% to even 100% of the amount paid out (H.R. 1586, H3656). Members of Congress also argued that because Treasury and the FRBNY were so involved with AIG, they could have forced AIG to not have paid out any bonuses, have employees repay their bonuses, or have negotiated new bonus contracts, similar to how employees of the autoworkers were doing as a condition of receiving TARP funds (H.R. 1586, H3657–3658). House members described the bonuses as “outrageous” and “an egregious waste of taxpayer dollars” (H.R. 1586, H3664). Further, an AIG shareholder filed a civil suit in the Los Angeles Superior Court asserting, “there was no rational business purpose or justification for these lucrative additional payments, particularly given AIG’s deteriorating financial condition” (Eseen 2009). Representatives suggested during a House meeting amending the law so that any bonus payments made by TARP recipients to their employees, as well as any future contractual obligations, be approved by Treasury prior to any payout (H.R. 1586, H3661). Following the public response, New York governor Andrew Cuomo announced that 15 of the top 20 bonus recipients at AIG voluntarily returned their bonuses, equal to about an estimated $50 million, to AIG (Clifford 2009).

Because AIG was the only institution to utilize the SSFI program, one scholar, Fabio Leonardi, has argued that that the SSFI program, along with other programs like the Targeted Investment Program and the Asset Guarantee Program (used by Citigroup and Bank of America), were discriminatory and that the US government had violated World Trade Organization (WTO) agreements (Leonardi 2011, Abstract). Given its narrow investment in a single institution, Leonardi argued that the SSFI program “discriminated, de facto, against foreign-like financial service suppliers commercially present in the US” (Leonardi 2011, 310).

IV. References


https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/AIG_Form_10-K_20090302.pdf.


Moody’s Investor Service. 2008. "Moody’s maintains present ratings on AIG (senior debt at A3, review down); comments on 3Q08 results and restructuring plan.” Press release,
November 10, 2008.
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Moody's_Moody's_maintains_present_ratings_on_Comments_on_3Q08_results_and_restructuring_plan_20081110.pdf.


https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/FRBNY_Securities_Purchase

———. 2008c. “Initial Section 105(a) Troubled Asset Relief Program Report to Congress for

https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Exec%20Comp%20PSSFI%20Notice%20Revised.pdf.

———. 2008e. “Responses to Questions of the First Report of the Congressional Oversight

Stabilization Act.” (Includes AIG Term Sheet: TARP AIG SSFI Investment Senior Preferred

International Group, Inc.” April 17, 2009.

———. 2009b. “Initial Section 105(a) Troubled Asset Relief Program Report to Congress for

———. 2009c. “Interim Final Rule on TARP Standards for Compensation and Corporate

17, 2009.

———. 2009e. “Securities Purchase Agreement: Series F Preferred Stock.” United States
Department of the Treasury. April 17, 2009.

April 17, 2009.


V. Key Program Documents

Summary of Program

Actions Related to AIG – Page on Federal Reserve Bank of New York’s website covering highlights, timelines, and documents surrounding FRBNY’s actions on AIG.  
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Actions%20Related%20to%20AIG%20-%20FEDERAL%20RESERVE%20BANK%20of%20NEW%20YORK.pdf

Investment in American International Group (AIG) – Page on the US Department of the Treasury’s website covering all TARP-related assistance to AIG, which includes press releases, program documents, and a timeline of Treasury’s investments.  
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/US%20Department%20Investment%20In%20American%20International%20Group%20AIG%202012.pdf

https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Congressional_Oversight_Panel_June_2010_Report_20100610_2.pdf

Implementation Documents

Agreement to Amend Warrants (01/14/2011) – Agreement among AIG, the AIA SPV, the ALICO SPV, FRBNY, Treasury, and AIG Credit Facility Trust to issue warrants to purchase common stock from November 25, 2008 (Securities Purchase Agreement) and April 17, 2009 (Securities Exchange Agreement).  
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/AIG_Agreement_to_Amend_Warrants_20110114.pdf

Certificate of Designations of Series E Fixed Rate Non-Cumulative Perpetual Preferred Stock of American International Group, Inc. (03/04/2009) – Certificate of Designations by AIG creating 400,000 shares of Series E fixed-rate, non-cumulative, perpetual preferred stock.  

Certificate of Designations of Series F Fixed Rate Non-Cumulative Perpetual Preferred Stock of American International Group, Inc. (04/17/2009) – Certificate of Designations by AIG creating 300,000 shares of Series F fixed-rate, non-cumulative, perpetual preferred stock.  

Master Transaction Agreement (12/08/2010) – Agreement among AIG, the ALICO SPV, the AIA SPV, FRBNY, Treasury, and AIG Credit Facility Trust over the closing of the Recapitalization


Registration Rights Agreement (01/14/2011) – Agreement between AIG and Treasury wherein AIG issued 1.6 billion shares of common stock to Treasury as part of the Recapitalization Plan announced in September 2010, converted from all other preferred shares Treasury received through government aid packages to AIG. https://ypfresource.blob.core.windows.net/fcic/YPFS/AIG_Registration_Rights_Agreement_20110114_2.pdf


Securities Purchase Agreement: Series D Preferred Stock (11/25/2008) – Purchase agreement entered into by AIG and US Treasury to sell 4 million shares of Series D fixed-rate, cumulative, perpetual preferred stock and a warrant to purchase 53.8 million shares of common stock to Treasury for $40 billion under TARP’s Systemically Significant Failing Institutions (SSFI) program. https://ypfresource.blob.core.windows.net/fcic/YPFS/FRBNY_Securities_Purchase_Agreement_Series_D_Preferred_Stock_200811125.pdf


TARP AIG SSFI Investment: Summary of Senior Preferred Terms (11/10/2008) – Term sheet for Treasury’s $40 billion TARP investment in AIG under the Systemically Significant Financial Institutions (SSFI) program. https://ypfresource.blob.core.windows.net/fcic/YPFS/US_Treasury_TARP_AIG_SSFI_Investment_Summary_of_Senior_Preferred_Terms_20081110_0.pdf

Term Sheet: March 2, 2009 (03/02/2009) – Term sheet for Treasury’s exchange of Series D preferred stock for Series E preferred stock. The document also describes the terms of a new $30 billion TARP capital commitment the Equity Capital Facility, to AIG, in exchange for Series F preferred stock and a warrant to purchase common stock.
Warrant to Purchase Common Stock (04/17/2009) – Document that authorized the purchase of a warrant for Treasury to purchase 3,000 shares of AIG common stock in exchange for a $30 billion commitment through the TARP SSFI’s Equity Capital Facility (ECF).
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Warrant%20(1).pdf

Legal/Regulatory Guidance


Emergency Economic Stabilization Act of 2008 (EESA) (10/03/2008) – Law passed by Congress to stabilize the American financial system and restore liquidity in struggling financial, bank, and non-bank institutions by creating the $700 billion TARP.
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/EESA_2008_10_03.pdf

Federal Reserve Act, Section 13: Powers of Federal Reserve Banks – Section of the Federal Reserve Act that grants emergency authority to the Federal Reserve “in unusual and exigent circumstances” to lend to persons, individuals, and companies and spells out the terms of that authority, used by the Fed to provide funding to AIG.
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/FRA_Section_13_Sept_19_2008_0.pdf

Press Releases/Announcements

Treasury Department and Federal Reserve Board and announce restructuring of financial support to AIG (11/10/2008) – Press release announcing a $40 billion TARP investment in AIG and changes to the AIG Credit Facility, including reduction of the RCF to $60 billion, the reduction of the interest rate, reduction of the commitment fee, and extension of the term to five years.
https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/FRB_FRB_and_Treasury_Department_announce_restructuring_of_financial_support_to_AIG_20081110.pdf

Treasury Announces the Completion of AIG’s Recapitalization (01/14/2011) – Treasury’s announcement that the recapitalization of AIG is complete, the Credit Facility has been terminated, and Treasury now owns 92% of the company after conversion of preferred shares to common stock.

Treasury to Invest in AIG Restructuring Under the Emergency Economic Stabilization Act (03/02/2009) – Treasury announces investment in restructuring plan for AIG, which includes investing $40 billion of TARP-related money under the Systemically Significant Financial Institutions (SSFI) program in exchange for preferred stock from AIG.
Media Stories

AIG ratings affirmed on new bailout plan (Business Insurance – 03/02/2009) – News article reflecting the changes in AIG’s credit ratings following the additional $30 billion in TARP funds extended to AIG and latest restructuring plan. https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Business_Insurance_AIG_ratings_affirmed_on_new_bailout_plan_20090302.pdf

AIG to get $22 billion in TARP funds for Fed exit (Reuters – November 1, 2010) – News article describing the final steps to be taken by FRBNY, Treasury, and AIG in the Recapitalization Plan, which includes AIG’s drawing an additional $22 billion from the TARP Equity Capital Facility. https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Reuters_AIG_to_get_$22_billion_in_TARP_funds_for_Fed_exit_20101101_0.pdf


Moody’s maintains present ratings on AIG (senior debt at A3, review down); comments on 3Q08 results and restructuring plan (Moody’s Investor Service – 11/10/2008) – Moody’s views the federal restructuring of AIG assistance positively and maintains AIG’s ratings, citing that the new infusion of TARP funds provides AIG “with additional time and flexibility to facilitate asset sales and bolster AIG’s operating performance.” https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Moody’s_Moody’s_maintains_present_ratings_on_Comments_on_3Q08_results_and_restructuring_plan_20081110.pdf


Treasury will give AIG another $40 billion, restructure loans (ABC News – 11/10/2008) – News article on Treasury’s extension of $40 billion to AIG as part of TARP and changes under a restructuring plan to the FRBNY’s Revolving Credit Facility. https://ypfs.som.yale.edu/node/4157

Key Academic Papers


Afterword to The AIG Bailout (Sjostrom 2015) – Addendum to the author’s 2009 article. https://ypfsresourcelibrary.blob.core.windows.net/fcic/YPFS/Sjostrom_University_of_Arizona_Afterword_to_the_AIG_Bailout_20150404_0.pdf
Reports/Assessments


Troubled Asset Relief Program: Government’s Exposure to AIG Lessens as Equity Investments are Sold (Government Accountability Office, 05/2012) – Research report that discusses government lending to and investments in AIG.


Troubled Asset Relief Program (TARP): Implementation and Status (Congressional Research Service, 06/27/2013) – Research report that discusses government investments in AIG.

Appendix A

TARP’s Systemically Significant Failing Institutions Program (SSFI)

On October 3, 2008, Congress passed the Emergency Economic Stabilization Act of 2008, which authorized Treasury to establish a $700 Troubled Assets Relief Program (TARP) and a new Office of Financial Stability (OFS) within Treasury (EESA 2008). EESA allowed Treasury to purchase and insure assets from financial institutions, which included residential mortgages and other financial instruments, such as equities, to “promote financial market stability” (GAO 2009, 10). Under TARP, Treasury created the Systemically Significant Financial Institutions (SSFI) program “to provide stability and prevent disruption to financial markets in order to limit the impact on the economy and protect American jobs, savings and retirement security from the failure of a systemically significant institution” (Treasury 2008c, 3). The program provided Treasury with the authority to determine:

1. The extent to which the failure of an institution could threaten the viability of its creditors and counterparties;
2. The number and size of financial institutions that are seen by investors or counterparties as similarly situated to the failing institution, or that would otherwise be likely to experience indirect contagion effects from the failure of the institution;
3. Whether the institution is sufficiently important to the nation’s financial and economic system; or,
4. The extent and probability of the institution’s ability to access alternative sources of capital and liquidity.

More specifically, the SSFI program aimed to “provide capital on a case-by-case basis to systemically significant institutions that are at substantial risk of failure” (Treasury 2008c, 3). Treasury intended to inject capital through the purchase of debt, equity, or warrants, following a consultation with the chairman of the Board of Governors of the Federal Reserve and notifying Congress (Treasury 2008c, 4). Treasury maintained that warrants would be required of any institution participating in the SSFI program “to minimize the long-term costs and maximize the benefits to the taxpayers in accordance with EESA” (Treasury 2008c, 4).

Although the SSFI program was capable of assisting a variety of companies and institutions, AIG was the only institution to utilize it throughout the program’s existence. This contributed to its being renamed the AIG Investment Program (AIGIP), according to the US Department of the Treasury website.
Appendix B

Timeline of Significant Events in AIG Assistance

September 16, 2008: The Board of Governors of the Federal Reserve, with the support of the Treasury, authorizes the Federal Reserve Bank of New York to extend a $85 billion emergency credit line to AIG to provide the firm with liquidity assistance and prevent its failure.

November 10, 2008: AIG and Treasury agree in principle, under the Systemically Significant Financial Institutions (SSFI) program of the Troubled Assets Relief Program (TARP), for Treasury to purchase $40 billion in newly issued Series D preferred stock with limited-class voting rights, with the cash being used to pay down AIG’s debt under the FRBNY’s Revolving Credit Facility.

November 25, 2008: The purchase agreements for the Series D preferred stock and Series D warrant are executed, giving Treasury 4 million shares of Series D preferred stock in AIG. The second amendment to the Credit Agreement is agreed upon, reducing the amount available from the Revolving Credit Facility from $85 billion to $60 billion, reducing the interest rate on the Facility, extending the duration of the facility to five years, and reducing the FRBNY’s controlling equity interest from Series C preferred stock to 77.9%.

March 2, 2009: The Board of Governors, Treasury, and AIG announce the second restructuring of federal assistance to AIG, involving a new Equity Capital Facility under TARP, modifications to the Revolving Credit Facility, and changes to the preferred stock under the SSFI program.

April 17, 2009: The exchange agreement for Treasury’s shares of Series D and Series E AIG preferred stock is executed. The purchase agreement for the Series F preferred stock, which Treasury received in connection with the Equity Capital Facility, is executed. The third Amendment to the Credit Agreement is agreed upon.

April 1, 2010: Treasury nominates and elects two new members to AIG’s board of directors at the 2010 Annual Meeting of Shareholders, after AIG fails to pay dividends out for four quarters.
September 30, 2010: Treasury, the Federal Reserve Bank of New York, AIG and the AIG Credit Facility Trust release a Recapitalization Plan for the Revolving Credit Facility, which involves the use of funds and the equity provided by the two TARP investments.

December 8, 2010: A Master Transaction Agreement is agreed upon that provides all the transactions and terms of the Recapitalization Plan and effectively ends the FRBNY’s involvement in AIG. The terms include converting all preferred stock held by the AIG Credit Facility Trust and Treasury into AIG common stock, with the intent to gradually sell such stock to recoup Treasury’s TARP investments.


December 10, 2012: Treasury sells off the remaining AIG common stock in its sixth and final public offering, netting Treasury a $36 billion gain and ending any remaining active equity stake in AIG.

March 2013: Treasury sells its Series D warrant and Series F warrants back to AIG for approximately $25 million, ending all government interest and assistance in AIG.

Development of this case has been supported by a generous grant from the Alfred P. Sloan Foundation to the Yale Program on Financial Stability.

Copyright 2018, 2019, 2020, 2021 © Yale University. All rights reserved. To order copies of this material or to receive permission to reprint any or all of this document, please contact the Yale Program for Financial Stability at ypfs@yale.edu.